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Welcome to Business Law

What you will learn
This course introduces you to fundamental legal principles affecting business in the United States, including the sources and classifications of laws in the U.S. You will learn to recognize and apply basic legal concepts relating to contracts, torts, and product liability; explore various forms of business organizations common in the United States; and gain a fundamental understanding of select legal topics critical to operating a business, including real property, personal property, credit and secured transactions, agency and employment, and bankruptcy.

How you will learn
You will learn by doing. Rather than simply reading generic material in a textbook, you will access specific information available at online legal resources to supplement the information presented in the instructional material. Not only will you study actual laws from your particular state, you will also develop practical Internet search skills that are essential to succeed in today's competitive employment market.

Internet activities are designed to be completed at home or in the university's learning resource centers and computer labs. Although it is necessary to read the information available at the various websites, it is not necessary to print them. It is also not necessary to have an Internet connection or projector in the classroom. Class time will generally be devoted to discussing the concepts addressed in each learning plan.

⚠️ Caution … A little knowledge is dangerous.
As you progress through this course, please keep in mind the old adage that "a little knowledge is dangerous." This advice is particularly important in legal matters. If you or someone you know has a particular legal problem or question, seek professional assistance from an attorney.

Although effort has been made to assure the accuracy of the materials in this course, laws and procedures change frequently and are subject to differing interpretations. The course materials and comments made by the instructor in this class do not constitute, and should not be treated as legal advice regarding any particular situation. Neither National American University, Dlorah, Inc., nor their instructors, officers, agents and employees shall be responsible or liable for any individual's reliance on information presented in this course.

You should consult an attorney if you have any questions regarding the applicability of any legal doctrines or concepts discussed in this class to any particular factual situation. You should also refrain from advising other persons regarding legal matters, which may constitute the unauthorized practice of law.
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Learning Plan 1

The U.S. Legal System

"A government of laws and not of men (and women)..."¹

Mt Rushmore, The Shrine of Democracy²

PURPOSE OF LAW

From the dawn of the earliest civilizations, people have created laws to give order and structure to their societies. Of course, the first laws were not written and were often imposed by a single ruler or small group of rulers – often by force.

As civilizations developed, so did their laws. One of the earliest known written laws is the Code of Hammurabi proclaimed by the king of ancient Babylon approximately 1780 B.C. The 282 separate laws of the Code, carved on an eight-foot black stone pillar, address such topics as slavery, divorce, crimes, and commerce. The Code also includes the familiar maxims, "An eye for an eye," and "A tooth for a tooth."

"If a man put out the eye of another man, his eye shall be put out."
"If a man knock out the teeth of his equal, his teeth shall be knocked out."

View image iv of the Code of Hammurabi. iii

There have been discussions since then about whether the law is a form of civil management or a way to dictate individual behavior. There have also been discussions throughout the ages as to whether laws should change or stay the same. In addition there have been battles about whether laws should be created by a national government so they are uniform for everyone or by individual states or regions.

Laws and legal systems continued to evolve as civilizations expanded and became more complex, leading to the development of the Anglo-American common law system, the Romano-Germanic civil law system, the Islamic law system (Shari'a), and other sophisticated legal systems. Despite their differences, the laws adopted and enforced in these legal systems provide many of the same functions, including:

- Creating the government
- Establishing rights
- Defining obligations
- Regulating public & private conduct
- Protecting individuals & businesses
- Regulating commerce
Although there are various definitions of law throughout the world, they are all based upon the principle that they consist of enforceable rules governing relationships among individuals and society. All law consists of rules of conduct established by the government of a society to maintain harmony, stability, and justice. It does this by defining the rights and duties of its people. It also provides a way to protect people by enforcing these rights and duties through the courts. Obviously, the law cannot stop a person from violating the law, but it can punish an individual who chooses to do so.

As legal systems continue to evolve laws are constantly amended and new laws enacted to address the increasingly complex relationships in our societies.

To understand the law in the United States, it is important to have a basic understanding of its origins.

**COMMON LAW**

The term *common law* comes from the attempts of early English kings to establish a body of law that all the courts in the kingdom would hold in common. Judges maintained consistency by relying on previous legal decisions whenever they faced a similar set of circumstances. In this way, they established a body of common law. As the process continued, judges began to record their decisions and shared with other judges. This body of recorded decisions became known as *common law*. Later, cases that involved similar legal principles or facts could be decided with reference to that precedent. The practice of deciding new cases with reference to former decisions or precedents eventually became a cornerstone of our judicial system and formed a doctrine called *stare decisis* which means “to stand alone.” Under this legal theory, judges are obligated to follow the precedents established within their jurisdictions.

Although *common law* and *stare decisis* provide a solid basis for our judicial system because it makes the law more stable and predictable, often times a court will depart from the rule of precedent if it decides that the precedent should no longer be followed. Oftentimes courts decide that due to technological or social change, the precedent is now inapplicable, and therefore the courts rule contrary to the precedent.

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**THE U.S. LEGAL SYSTEM**

In addition to common law, the legal system of the United States is founded upon the U.S. Constitution, which divides governmental powers among Federal, state, and local authorities. Those powers are further divided among different branches of government (Executive, Legislative, and Judicial). Because of the size and complexity of U.S. society, many lower level governmental powers are delegated to government agencies. As a result, laws in the United States are created by many different sources, including:

- The Constitution of the United States
- State Constitutions
- Federal/State Statutes
- Federal/State Court Cases
- County/City Ordinances
- Government Agency Regulation
The Constitution of the United States

The Constitution of the United States establishes the foundation and framework for the democratic legal system in the U.S. The writers of the Constitution stated their intent in the opening paragraph of the Constitution, called the preamble:

>We the People of the United States, in Order to form a more perfect Union, establish Justice, insure domestic Tranquility, provide for the common defence, promote the general Welfare, and secure the Blessings of Liberty to ourselves and our Posterity, do ordain and establish this Constitution for the United States of America.

To accomplish these purposes, the Constitution creates a democracy under a federal system of government in which governmental power is shared between the national government (often called the Federal government) in Washington D.C. and the state governments.

To prevent the concentration of power in any one person or group, the Constitution separates the powers of the Federal government into three branches, each with a different function. The Legislative Branch (Congress) makes the laws; the Executive Branch (the President) executes and enforces the laws; and the Judicial Branch, (the Federal Courts) interprets the laws. This system of "checks and balances" prevents any one branch from gaining too much power.
The Bill of Rights, adopted shortly after the Constitution, provides the first ten amendments to the Constitution. These amendments protect the rights of individual citizens and specify that powers not delegated to the Federal government under the Constitution are reserved in the states or their citizens.

Since the adoption of the Bill of Rights, seventeen additional amendments to the U.S. Constitution have been adopted to address various issues, including:

- Abolishing slavery
- Granting equal protection of the laws
- Authorizing income taxes
- Granting women the right to vote
- Lowering the Federal voting age to eighteen

Read the U.S. Constitution, the Bill of Rights, and subsequent Constitutional Amendments at the National Constitution Center website.

STATE CONSTITUTIONS

Each of the fifty states of the United States has adopted its own separate state constitution. Like the Federal government, the governments of each of the fifty states are also divided into three branches: an Executive Branch (Governor), Legislative Branch (State Legislature), and Judicial Branch (State Courts).

Briefly review a state constitution of your choice available at the Cornell University Law School Legal Information Institute.
**LOCAL GOVERNMENTS**

In addition to the Federal government and fifty state governments, the thousands of counties, cities, and towns across the United States have established their own local governmental units, such as county commissioners, city councils, mayors, local school boards, etc.

**GOVERNMENT AGENCIES**

Sometimes called the "fourth branch of government," government agencies perform much of the work of the Federal, state, and local governments.* Although not specifically mentioned in the U.S. Constitution, such agencies are necessary to attend to the volume and complexity of the issues encountered by the different levels of government. Examples of Federal and state agencies include:

<table>
<thead>
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<tr>
<td>Federal Communications Commission</td>
<td>Motor Vehicles</td>
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<tr>
<td>Environmental Protection Agency</td>
<td>Public Utility Commission</td>
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*Most agencies are part of the Executive Branch.

Agencies can be classified as **regulatory** or **social welfare**. The Federal Environmental Protection Agency is an example of a regulatory agency that implements regulations to protect the environment. The Federal Social Security Administration is an example of a social welfare agency that provides benefits to retired and disabled persons and their families.

Rules and regulations implemented by government agencies have the force of law.

**SOURCES AND HIERARCHY OF U.S. LAW**

The U.S. Constitution provides the original and supreme law for the United States. Since the adoption of the Constitution, thousands of other laws have been made, and continue to be made and modified, by Federal, state, and local governments. These laws can be classified as **codified laws** and **case law**.

**Codified laws** are written laws made by the Legislative Branch, including

- **Ordinances** passed by local county and city boards and councils
- **Administrative rules and regulations** implemented by Federal, state, and local agencies
**Case law** is made by Federal, state, and local courts.

- Judges make case law when they decide a case in situations in which there is no statute or administrative rule or regulation. As we have discussed, such decisions form a *precedent* that must be followed by lower courts within that jurisdiction.
- Judges also make case law by *interpreting and applying statutes* passed by Congress and state legislatures, and ordinances passed by local county and city boards and councils.

The U.S. Constitution (including its Amendments) and Federal laws made in accordance with the Constitution are the supreme laws of the land and therefore *superior* to all other laws in the United States. No state or local law may violate the Constitution or Federal law. The *Supremacy Clause* in Article VI of the U.S. Constitution provides:

*This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.*

Generally, Federal law is superior to state law and local laws, while state law is superior to local, county, and city laws.

Review the University System of Georgia’s chart showing the [Hierarchy of Law in Georgia](https://example.com), which is a good example of the relationship between Federal law, state law, and local law.viii

**CLASSIFICATION OF LAW**

Laws can be classified in several ways. Many different classifications apply to the same law. Initially, it must be determined whether a law is a Federal law, state law, or local law. Then, the law can be classified as either civil or criminal, and either substantive or procedural.

**Civil Law and Criminal Law**

The most important difference between laws is the distinction between civil law and criminal law.

- **Civil law** addresses matters between private individuals and businesses, such as contracts, property transfers, inheritance, business organizations, and personal injury. In a civil case, one party tries to make the other party comply with a duty or pay for the damage caused by a failure to do so.
- **Criminal law** involves the protection of society and has to do with a wrong committed against the public as a whole. Criminal statutes and ordinances define certain conduct as crimes. The government prosecutes a person accused of a crime and seeks punishment for violation of the criminal statute.

Watch the YouTube video [Criminal Law Vs Civil Law](https://example.com) posted by LearnByLyrics to further understand the differences between civil and criminal law.

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Read the article [Differences between Civil and Criminal Law in the USA](#) by Dr. Ronald B. Standler.

The same conduct can be both a civil wrong and a crime. For example, a person who kills a pedestrian while driving a vehicle while impaired by drugs or alcohol may be guilty of the crime of vehicular homicide and also liable to the pedestrian's surviving family in a civil wrongful death action.

**Substantive and Procedural Law**

Laws can also be classified as substantive law and procedural law.

- **Substantive law** addresses the rights and duties of individuals and businesses. A person's right to own property is substantive law. Similarly, a person's duty to keep his property safe for visitors is also substantive law.

- **Procedural law** provides the rules used in enforcing substantive law during trials and administrative hearings. Procedural law determines where, when, and how a lawsuit may be filed, as well as the rules to be followed during trial and appeal.

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**ACCESSING LAWS AND LAWMAKERS**

Access to laws and lawmakers is much easier today than it was in 1780 B.C., when the Code of Hammurabi was inscribed on an eight-foot stone pillar. The Internet provides an easy method of obtaining information and contacting government officials. The fact that anyone who wants to know what the laws are only need to get on their computer, tablet or phone and access a website to research ensures that virtually everyone in society has equal access to the law.

Visit each of the following Websites for a glimpse of the functions of the Federal and state governments.

**Federal Government**

- Executive Branch
  - [The White House](#)
  - [The Library of Congress Official US Executive Branch Websites](#)

- Legislative Branch
  - [U.S. Senate](#)
  - [U.S. House of Representatives](#)

**State Governments**

- [USA State Government](#)
  - [USA Government Departments and Agencies](#)

**Statutes**

- [Cornell University Law School’s Legal Information Institute U.S. Code](#)
- [Cornell University Law School’s Legal Information Institute Listing by Jurisdiction](#)
Federal and State Resources
  o USA Government Departments and Agencies

ADVERSARY PROCESS
Determined societies resolve disputes in different ways. In the United States, the U.S. Constitution and other laws provide individuals and businesses with the right to have disputes resolved through the court system. You may have heard the phrase that a person is entitled to his "day in court."

The laws of our government are interpreted and enforced by a system of courts authorized by either the federal or a state constitution and established by legislative authority.

Federal Courts
The federal court system is authorized by Article III of the U.S. Constitution. The federal court system includes the Supreme Court, the courts of appeals and the federal district courts. Visit each of the following websites for a glimpse of the functions of the Federal courts.
  o Federal Court System (United States Courts)
  o U.S. Supreme Court (Supreme Court of the United States)
  o U.S. Court of Appeals (United States Courts)
  o U.S. District Courts (United States Courts)
  o U.S. Bankruptcy Court (United States Courts)

Also visit the Federal Judicial Center website and read the section How Cases Move Through Federal Courts to view a flowchart and learn how criminal and civil cases move through the Federal Court System.

State Courts
The courts of each state are organized according to the provisions of the state constitutions. Review a chart of court system in your state, or the state of your choice, at the State Court Structure Charts prepared by the National Center for State Courts.

Courts are called upon to determine both criminal cases and civil cases. The trials in both cases have many similarities, but also distinct differences. Trials in both cases in use of the adversary process in which opposing parties present their arguments to the court. However, the burden of proof in a civil case is much less than the burden of proof in a criminal case.

In a civil case, the plaintiff (complaining party) must prove his or her case by a preponderance of the evidence. Under this standard, the plaintiff must convince the judge or jury that it is more likely than not that the plaintiff’s allegation is true. By contrast, in a criminal case, the state must prove its case beyond a reasonable doubt. In addition, in a criminal case the jury must have a unanimous verdict, where as in a civil case typically only three-fourths of the jurors need to agree.
Review *A Guide to Legal Literacy, Understanding the U.S. Legal System* published by the State Bar of California to learn:

- How Cases Come to Court
- Types of Courts
- Stages of a Criminal Case Before Trial
- The Stages of a Civil Suit Before Trial
- The Trial
- The Role of Attorneys
- Who Decides
- The Verdict
- The Appeal
- Changing the System

For a more detailed look at the stages in a criminal case, review this interactive flowchart prepared by the Bureau of Justice Statistics entitled *What is the sequence of events in the criminal justice system?*

For future reference during this course, please download and print for your personal use the *Glossary of Terms* provided by the American Bar Association.
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Learning Plan 2

Torts

Definition of a Tort

Tort is not a word that people use often in everyday conversation. Yet, it is something with which most people in the United States are familiar. A more commonly used term is personal injury. A person only needs to look at the yellow pages in the local telephone book, watch the television commercials, and see the numerous billboard signs to realize how prevalent claims for personal injury have become in U.S. society. Some people argue that the proliferation of personal injury claims has reached epidemic proportions, while others assert that the vast majority of claims seek legitimate compensation for people who have been injured, or whose property has been damaged, by the negligent or intentional conduct of others.

Personal injury is only one kind of tort. Black's Law Dictionary, 5th Edition, defines a tort as follows:

Tort . . . A private or civil wrong or injury, other than breach of contract, for which the court will provide a remedy in the form of an action for damages. . . Three elements of every tort action are: Existence of legal duty from defendant to plaintiff, breach of duty, and damage as proximate result . . .

By definition, a tort is any "civil (private) wrong or injury, other than a breach of contract." By contrast, a crime is a public wrong. Note that the same act may be both a tort and a crime. For example, a person who operates a motor vehicle while under the influence of alcohol or drugs and causes an accident that injures a pedestrian, may be guilty of a crime, as well as liable for a tort.

The person who commits the offensive conduct in a civil proceeding is called a “tortfeasor” or “defendant”. The party who was injured is generally referred to as the “injured party” or “plaintiff.” In a criminal proceeding the person who commits the offensive conduct is the “defendant” and the person who was injured is generally the “victim.”

In order for a tort to have been committed a 3-part test must be applied, the defendant must have a legal duty to the plaintiff, there must be a breach of that duty, and there must be damages that resulted from the actions or inactions of the defendant.

Some theories of tort apply a 4-part test that would break out duty, breach, injury and cause. In other words, the defendant had a duty to observe or protect the plaintiff; the defendant breached
that duty; the plaintiff was injured; the injury was caused by the defendant’s actions or inactions.

**RESPONDEAT SUPERIOR**

Tort actions can occur in a business setting because of the doctrine of respondeat superior (Latin for “let the master respond”). The legal theory may impose legal liability on employers and make them pay for the torts committed by their employees who are acting with the scope of their employment. The doctrine ensures that injuries to persons and property caused by a business are paid for by the business whether occurring at the hands of the owner or employee.

Review the YouTube video *Episode 1.2: An Overview of Tort Law – Intentional Torts, Negligence, and Strict Liability* posted by Aaron Dewald to see a more detailed explanation of torts and examples of types of torts.

---

**CLASSIFICATION OF TORTS**

Torts can be classified into three main categories:

- Intentional Torts
- Negligence
- Strict Liability

Read the following articles:

- [Tort](https://www.law.cornell.edu) (Cornell University Law School Legal Information Institute)
- [Personal Injury Law: The Basics](https://www.findlaw.com) (FindLaw)
- [A Brief Overview of Tort Law](https://www.laws.com) (Laws.com)

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**INTENTIONAL TORTS**

The case law and statutes of many states define numerous types of intentional tort in which a person who was injured, or whose property was damaged, by the intentional act of another may be compensated for such injury or damage. An intentional tort requires that the tortfeasor (the one committing the tort) must *intend* to commit an act. In other words, the actor must intend the normal consequences of his or her actions or know with substantial certainty that a particular consequence will result from the act. In addition, that act must cause harm to a person or damage to property.

Examples of different types of intentional torts include:

- Assault
- Battery
- False Imprisonment
- Defamation
- Invasion of Privacy
- Trespass
- Liable

Each tort has distinct elements, all of which must be present before an injured party may be
compensated. Although the elements of particular torts vary from state to state, the following elements are generally recognized by the different states.

Many people think of assault and battery as the same thing or interchangeable terms. However, although they often take place together, they each have distinct elements.

**Elements of Assault**

1. Intentional act
2. Causes a reasonable apprehension
3. Of immediate harmful or offensive contact

An intentional, unexcused act that creates in another person a reasonable apprehension or fear of immediate harmful or offensive contact is an assault. Apprehension is not the same as fear. If a contact is such that a reasonable person would want to avoid it, there is a reasonable basis for believing that the contact will occur, the plaintiff suffers apprehension whether or not he or she is afraid.

**Generally, threatening words, without some kind of act, are not enough to constitute an assault.**

**Elements of Battery**

1. Intentional act
2. Causes harmful or offensive contact

The completion of the act that caused the apprehension is a battery if it results in harm to the plaintiff. Battery is an unexcused and harmful or offensive physical contact that is intentionally performed. The contact can be harmful or it can be simply offensive, such as an unwanted touch. The contact can involve any part of the body or anything attached to it. For example an item of clothing that the individual touched, is wearing, or a chair in which the individual is sitting.

Whether the contact is offensive is determined by the reasonable person standard. The contact can either be made by the defendant or by something the defendant has done, such as a thrown object.

**Example**

Josephine goes to her local Stop-and-Go, a gas station and convenience store near her home. When she goes to check out, she realizes that the store clerk, Fred, is her ex-husband and she points a gun at him and then shoots him.

The pointing of the gun at Fred is an assault. The firing of the gun is battery.

Read the FindLaw article **Assault, Battery and Intentional Torts**, including all subtopics, presented by FindLaw.

**Elements of False Imprisonment**

1. Intentional act
2. Confines or restrains a person, without lawful privilege, for an appreciable length of time
Example
While you are sitting in a third floor classroom, actively participating in a class discussion about business law, another instructor enters the room and screams that you and your classmates are enjoying business law too much. He then runs from the room, slamming and locking the door behind him. You hear muffled footsteps and the instructor's voice yelling in the distance, "You can stay in there until you learn to enjoy my class as much as you enjoy business law." With no means of escape or communication, you, your classmates, and your business law instructor are confined in the classroom for several hours, until the night cleaning staff arrives and unlocks the door to clean the room.

Read the FindLaw article Defamation, Libel and Slander, including all subtopics, presented by FindLaw.

Intentional Infliction of Emotional Distress
1. Intentional act
2. Extreme and outrageous conduct
3. Causes severe emotional distress

Example
Bob falsely tells Fred that Bob had seen a news report that Fred’s wife had just been killed in an automobile accident. Bob’s statement causes Fred severe emotional distress.

Trespass to Land
1. Intentional act
2. Causes physical invasion of land

Example
Rather than drive five miles around Sarah's land, Dan intentionally drives his sports utility vehicle across Sarah's land without her permission to go fishing at a nearby lake.

DEFENSES TO INTENTIONAL TORTS
Although the elements may be present for an intentional tort, a person may not be liable (responsible) for a tort if a valid defense exists. Examples of valid defenses include:

Consent
Self-defense
Defense of Others
Defense of Property
Necessity

Unlike assault, threatening words can constitute false imprisonment, if a person is restrained by direct or indirect threats of force against the person, the person’s immediate family, or the person’s property.
UNINTENTIONAL TORT

NEGLIGENCE

Negligence is a tort that happens when someone suffers injury because of another’s failure to exercise the proper duty of care. Unlike in an intentional tort, the tortfeasor does not have to intend to bring about the consequences of the act. The generally recognized elements of negligence are:

Elements of Negligence

1. Duty
2. Breach of duty
3. Actual and proximate cause
4. Damage to person or property

In order to analyze a situation to determine if negligence occurred, four questions must be asked, the answers to which all must be yes:

1. Did the defendant owe a duty of care to the plaintiff?
2. Did the defendant breach that duty?
3. Did the plaintiff suffer an injury as a result of the defendant’s breach of duty?
4. Did the defendant’s breach of duty cause the plaintiff’s injury?

Read the following article presented by FindLaw:
Negligence, including all subtopics.

Defenses to Negligence

A person may not be liable for negligence if the person has a valid defense. Defenses to negligence include:

1. Contributory negligence – The defense of contributory negligence involves failure of the injured party to be careful enough to ensure personal safety. Contributory negligence completely prevents the injured party from recovering any damages.

2. Comparative negligence – To soften the harsh effects of contributory negligence, many states have adopted comparative negligence statutes that require courts to assign damages according to the degree of fault of each party. Rather than deny any recovery, the court weighs the degree of wrongdoing to determine the amount of damages owed. If the tortfeasor was 80 percent negligent and the injured party only 20 percent negligent then the injured party may recover 80 percent of the losses suffered for example.

3. Assumption of risk – If the injured party was aware of the danger involved in a certain situation and willingly agreed to be exposed to that danger, he or she has assumed any risk associated with that activity. The only thing a court would look at would be the awareness to the extent of the danger in considering whether to award or deny damages.

Review the article Defenses to Negligence by USLegal.com before reading further.
CAUSATION
Another necessary element of a tort is causation. In other words, the bad or wrongful activity must have caused the harm for a tort to have been committed.

There are two types of cause:
1. Causation in fact – The injury occurred because of the defendant’s act and in fact the injury would not have occurred without the defendant’s actions. This is determined by using the “but for” test. But for the wrongful act, the injury would not have occurred.
2. Proximate cause – Exists when the connection between and act and an injury is strong enough to justify imposing liability. The test for proximate cause is: Was the harm foreseeable? Foreseeability is determined by the courts and is determined in part by the extent to which the courts are willing to stretch the defendant’s duty of care.

REASONABLE PERSON
The reasonable person standard is the test that the court will apply in determining the duty of care. The question applied is: How would a reasonable person have acted in the same circumstances? It is not how an individual person would act, rather it is society’s judgment on how people should act. Review the Standards of Care and the “Reasonable Person” article presented by FindLaw.

STRICT LIABILITY
The last category of tort is strict liability, sometimes called liability without fault. Strict liability is available in only a limited number of situations and generally only where the activity itself is an extreme risk. The elements of strict liability are:

Elements of Strict Liability
1. Absolute duty
2. Breach of duty
3. Actual and proximate cause
4. Damage to person or property

Unlike negligence, strict liability imposes an absolute duty in certain situations, including:
- Ultra hazardous or abnormally dangerous activities
- Keeping wild animals

DAMAGES

A person who is injured or whose property is damaged by the wrongful act of another, whether it be an intentional tort, negligence, or strict liability, is entitled to monetary compensation, referred to as damages. Damages may be classified as compensatory damages and punitive damages.

Compensatory Damages
The purpose of compensatory damages is to monetarily compensate the injured person for the loss suffered as a result of the tort. Compensatory damages can include medical expenses, loss of income, and pain and suffering.

Punitive Damages
Punitive damages, sometimes called exemplary damages, may be awarded in addition to compensatory damages. Punitive damages are intended to punish the wrongdoer for outrageous or reckless conduct, such as fraud.

Punitive damages differ from a criminal fine in that the injured person receives the punitive damages, while criminal fines are received by the government prosecuting the crime.

Read Damages, including the imbedded links addressing specific torts, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

Read the following three cases that address the tort concepts of false imprisonment, battery, and trespass.

ANGELOPOULOS v. LAZARUS PA INC., et al.
2005 PA Super 304, 884 A.2d 255
(2005)

MUSMANNO, J.:

Lazarus PA Incorporated, Rich's Department Stores Incorporated, and Federated Department Stores Incorporated (collectively, "Lazarus") appeal from the Order granting the Motion for a new trial filed by Rosario Angelopoulos ("Angelopoulos"). We affirm.

While shopping at a Lazarus Department Store, Angelopoulos approached an irresistible display of Godiva chocolate. According to Angelopoulos, one box of chocolates did not have a lid, and the interior cellophane wrapper covering the chocolate was slashed on both sides of the box. N.T., 9/2-5/03, at 17. At trial, Angelopoulos described the display as follows:

It was just a treat to look at it, so I go to look at it and I touch it and I move my eyes to the side and I see the small box with the plastic--like something had a slide--slashed it, kind of
curled up, like it was saying, Please help yourself. *Id.* at 16. Thinking that the open box was a free sample, Angelopoulos thought, I said, Oh, my God. If anything, it was my cholesterol that came to me. Should [I] have one? And I said, Well, one won't hurt me. That was my feeling.

And I took the box and I took one. *Id.* Unable to resist temptation, Angelopoulos succumbed to the call of the chocolate, ate a piece, and then returned to the display several minutes later and consumed a second piece. Thinking that the chocolates were a free sample, Angelopoulos did not pay for either morsel of chocolate. *Id.* at 67, 72.

The trial court's Opinion described what next transpired: Several minutes later, Michael Demicco ["Demicco"], a loss prevention associate for Lazarus, followed by Janet Lesure, a trainee for loss prevention, approached [Angelopoulos]. [Demicco] requested that [Angelopoulos] follow him to the loss prevention office located in the Lazarus store. [Angelopoulos] complied. [Demicco] and Ms. Lesure searched [Angelopoulos's] purse and bags and Ms. Lesure performed a search of her body. [Angelopoulos] was then handcuffed to a table affixed to the floor. Her identification documentation and her Lazarus credit card were taken from her purse. [Demicco] presented [Angelopoulos] with a statement of admission. He completed her name and address and the dollar amount of the merchandise allegedly taken by [Angelopoulos]. Only the signature line was blank. [Angelopoulos] objected to the admission form and asked to see the store manager. [Llewellyn], [Demicco's] supervisor, entered the room and agreed to find the store manager. He returned, accompanied by Patty Connelly, a store manager. [Angelopoulos] asked to have the handcuffs removed and Ms. Connelly indicated that she did not have the power to have the handcuffs removed and that it was the policy of the loss prevention group to handcuff everyone suspected of shoplifting. After repeated refusals to sign the admission form, [Angelopoulos] ultimately did agree to sign the form provided that [Demicco] wrote on the form, "Took 2 pieces of chocolate out of box and ate it without purchase. Foil was cracked." She was then released from the handcuffs. [Demicco] then told [Angelopoulos] that Lazarus must take her photograph, to which she objected. She then scratched out her signature from the admission form. Throughout the detention process, [Angelopoulos] was kept handcuffed continuously for a period of approximately 50 to 55 minutes. Trial Court Opinion, 8/31/04, at 1-4. Lazarus filed no charges against Angelopoulos as a result of the incident.

Angelopoulos subsequently filed a Complaint against Lazarus asserting claims of false imprisonment and battery. At the close of the trial, the jury received the following written interrogatories:

**False Imprisonment**

Question 1: Do you find that [Lazarus] intentionally caused the confinement of [Angelopoulos] against her will? (Jury's answer: Yes.)

Question 2: Do you find that [Lazarus] had probable cause to believe that [Angelopoulos] had committed or was committing a theft of merchandise from the store? (Jury's answer: Yes.)

Question 3: Do you find that [Lazarus's] detention of [Angelopoulos] was done in a reasonable manner, for a reasonable time, and for a proper purpose? (Jury's answer: Yes.)
Battery
Question 4: Do you find that [Lazarus] committed a battery against [Angelopoulos]? (Judge's
Answer: No.)

See Trial Court Opinion, 8/31/04, at 4. The jury found Lazarus not liable on both counts,
after which Angelopoulos filed post-trial Motions.

The trial court granted Angelopoulos's Motion for a new trial, concluding that the jury's
answer to Question 3 of the written interrogatories was against the weight of the evidence.
Specifically, the trial court determined that "Lazarus's policies and practices with regard to
retail theft, as applied to [Angelopoulos] on October 29, 2001, were in violation of the
Retail Theft Act." Id. at 12. In support of its conclusion, the trial court set forth the
following explanation in its Opinion: The [trial court] reaches this conclusion based upon a
confluence of factors, all of which were in play on the day in question: the handcuffing of
Angelopoulos; the refusal to release [Angelopoulos] from the handcuffs once she
objected; the use of the handcuffs and detention to accomplish a purpose beyond one of the
six reasons enumerated in the Retail Theft Act; the duration of the detention; the
presentation of the admission form; and the refusal of Lazarus to release [Angelopoulos]
when she stated that she would not sign the admission form, even though there was no
longer any reason to continue to detain her for one of the enumerated purposes under the
Act. Id. at 12. Thereafter, Lazarus filed the instant timely appeal.

Lazarus presents the following claims for our review:

I. Whether the trial court abused its discretion and invaded the province of the jury by
granting a new trial on the grounds that the verdict was against the weight of the evidence
where the evidence was, at best, conflicting and the trial judge merely would have reached a
different decision on the same facts?

II. Whether the trial court erred in submitting punitive damages to the jury? Brief for the
Appellants at 4. We will address these claims in order.

Lazarus first claims that the trial court abused its discretion and invaded the province of the
jury by granting a new trial on the basis that the verdict was against the weight of the
evidence. According to Lazarus, "the evidence regarding whether [Angelopoulos's]
detention was reasonable in duration and purpose was conflicting and the trial court merely
would have answered jury interrogatory number three differently on the same set of facts." 
Brief for the Appellants at 24. Lazarus asserts that the jury could reasonably have found that
Lazarus had probable cause to detain Angelopoulos, and that the detention was for a
reasonable time and conducted in a reasonable manner. Id.

When reviewing an attack on the trial court's grant of a new trial, we will not disturb its
decision absent an abuse of discretion or clear error of law. Mammoccio v. 1818 Mkt. P'shp,
734 A.2d 23, 28 (Pa.Super.1999). An abuse of discretion exists when the trial court has
rendered a judgment that is manifestly unreasonable, arbitrary, or capricious, has failed to
apply the law, or was motivated by partiality, prejudice, bias, or ill will. Harman ex rel.
"One of the least assailable grounds for the exercise of such power [i.e., granting a new trial.] is the trial court's conclusion that the verdict was against the weight of the evidence and that the interests of justice therefore require that a new trial be awarded; especially in such a case is an appellate court reluctant to interfere." Hershey v. Pittsburgh & W.V.R. Co., 366 Pa. 158, 76 A.2d 379, 381 (1950) (citations omitted); accord Armbruster v. Horowitz, 572 Pa. 1, 813 A.2d 698, 703 (2002). [The Pennsylvania Supreme Court] has repeatedly emphasized that it is not only a trial court's inherent fundamental and salutary power, but its duty to grant a new trial when it believes the verdict was against the weight of the evidence and resulted in a miscarriage of justice. Although a new trial should not be granted because of a mere conflict in testimony or because the trial judge on the same facts would have arrived at a different conclusion, a new trial should be awarded when the jury's verdict is so contrary to the evidence as to shock one's sense of justice and the award of a new trial is imperative so that right may be given another opportunity to prevail. Armbruster, 813 A.2d at 703 (quoting Thompson v. City of Philadelphia, 507 Pa. 592, 493 A.2d 669, 672 (1985) (citations omitted)).

The Retail Theft Act ("the Act") provides, in relevant part, as follows:
A peace officer, merchant or merchant's employee or an agent under contract with a merchant, who has probable cause to believe that retail theft has occurred or is occurring on or about a store or other retail mercantile establishment and who has probable cause to believe that a specific person has committed or is committing the retail theft may detain the suspect in a reasonable manner for a reasonable time on or off the premises for all or any of the following purposes: to require the suspect to identify himself, to verify such identification, to determine whether such suspect has in his possession unpurchased merchandise taken from the mercantile establishment and, if so, to recover such merchandise, to inform a peace officer, or to institute criminal proceedings against the suspect. Such detention shall not impose civil or criminal liability upon the peace officer, merchant, employee, or agent so detaining. 18 Pa.C.S.A. § 3929. Thus, the Act authorized Lazarus to detain Angelopoulos, without civil liability, for the purpose of (a) identifying Angelopoulos, (b) verifying her identity, (c) determining whether she had unpurchased merchandise in her possession, (d) recovering unpurchased merchandise from Angelopoulos's possession, (e) informing a peace officer, and (f) instituting criminal proceedings.

In this case, the trial court determined that Lazarus's detention of Angelopoulos violated the Act, as Lazarus held Angelopoulos beyond the time necessary to conduct the purposes authorized by the Act. The trial court explained its determination as follows: [T]he use of handcuffs is not a per se violation of the Retail Theft Act so long as the handcuffs are used to accomplish one or more of the enumerated justifications of a detention. It is apparent that Lazarus handcuffed [Angelopoulos] initially for legitimate purposes. However, once they were able to identify [Angelopoulos] (they had her identification documentation and her Lazarus charge card), and confirm by searching her that she did not possess any unpurchased merchandise (she was only observed eating two pieces of chocolate), there was no longer any reason to detain her, and unquestionably no reason to keep her handcuffed. Fifty to fifty-five minutes appears to be an unusually long period of time under the circumstances for a few ministerial acts. Lazarus had no intention of informing a peace officer at that time nor did they intend to detain her for the purpose of
instituting criminal proceedings at that time. There no longer existed any statutorily permitted reasons to continue her detention. At that point, [Angelopoulos] should have been released from her handcuffs as she had repeatedly requested. Once they refused to release her, as testified to by [Demicco], the handcuffing went beyond the bounds of the principal reasons behind the Act, and beyond the bounds of decency. To continue to keep her handcuffed, while presenting to her for her signature what is essentially a confession form, is clearly unjustified. Trial Court Opinion, 8/31/04, at 13. The trial court's determination is supported by the overwhelming evidence of record. At trial, Demicco, Lazarus's loss prevention specialist, testified that he observed Angelopoulos on a video security monitor. N.T., 9/2-5/03, at 4. Over a span of about four minutes, Demicco saw Angelopoulos eat two pieces of Godiva chocolate from an opened box on a store display. Id. As a result, Demicco approached Angelopoulos and asked her to follow him to an "apprehension room." Id. at 5.

The testimony at trial reveals that Demicco escorted Angelopoulos to the apprehension room at 3:45 p.m. Id. at 79. Once Demicco and Angelopoulos arrived in the apprehension room, a female security guard performed a pat-down search of Angelopoulos, after which she was handcuffed to a table in the room. Id. at 5-6. Also upon entering the room, someone from the loss prevention department searched Angelopoulos's bags to make certain no other unpurchased goods were present in the bags. Id. at 65. Demicco asked for and received Angelopoulos's identification. Id. at 66. At that point in time, Angelopoulos asked to be released from the handcuffs. Id. at 67-68.

Rather than releasing Angelopoulos from the handcuffs, Demicco showed Angelopoulos an "admission form," and explained to her that once he wrote down her general information, "it was up to her if she wanted to admit to it, then she would sign it. If not, then she would be released." Id. at 68. Demicco further testified that he would not release Angelopoulos from the handcuffs "until I got down her general information and explained [the form] to her." Id. at 69 (emphasis added).

Demicco acknowledged that Angelopoulos, at first, did not want to sign the form. Id. at 69, 71. When Demicco refused to release Angelopoulos from the handcuffs, Angelopoulos asked to see a store manager. Id. at 71-72. Demicco first brought [Llewellyn], the manager of loss prevention for Lazarus's South Hills Village store, to speak with Angelopoulos. Id. at 72. When Llewellyn refused to release Angelopoulos from the handcuffs, she again asked to speak with a store manager. At that time, Patty Connelly ("Connelly"), the executive vice-president of the store, arrived to speak with Angelopoulos. Id. Connelly declined to interfere. Id. at 73.

At trial, Llewellyn admitted that Angelopoulos asked to be released from the handcuffs as soon as he entered the room. Id. at 143. Llewellyn further admitted that prior to his encounter with Angelopoulos, he had checked out Angelopoulos's credit history at the store. Id. at 148. Thus, the record is clear that at the very latest, Lazarus possessed the information necessary to identify Angelopoulos, and to verify her identity, at the beginning of the encounter between Llewellyn and Angelopoulos.

Demicco testified that if a person refused to sign the "admission form," they would be released from the handcuffs and be "free to go." Id. at 39. Thus, the record is also clear that
Lazarus did not intend to detain Angelopoulos for the purpose of calling a peace officer or initiating criminal proceedings, but for the purpose of presenting an admission form and gaining the suspected shoplifter's signature on that form.

Based upon the foregoing, we discern no abuse of discretion by the trial court in concluding that the jury's answer to Question Number 3 on the written interrogatories was against the weight of the evidence. At the very latest, Lazarus's authority to detain Angelopoulos ended prior to the time Llewellyn entered the apprehension room. The only purpose for further detaining Angelopoulos was to secure her signature on an admission form. We agree with the trial court's conclusion that Lazarus's continued detention of Angelopoulos, in handcuffs, exceeded all bounds of decency and we express our outrage at such a procedure. Such coercive tactics are not authorized by the Retail Theft Act. Accordingly, we affirm the trial court's grant of a new trial based upon Angelopoulos's challenge to the weight of the evidence.

Lazarus next claims that the trial court erred in submitting the issue of punitive damages to the jury. According to Lazarus, there was no evidence that Lazarus "acted with malice, ill-will, or in reckless disregard of [Angelopoulos's] rights." Brief for Appellants at 32. We disagree.

"Punitive damages are awarded to punish a defendant for certain outrageous acts and to deter [it] or others from engaging in similar conduct." G.J.D. v. Johnson, 552 Pa. 169, 713 A.2d 1127, 1131 (1998) (citation omitted) (emphasis deleted). In general, the assessment of punitive damages is proper whenever a party's actions are of such an outrageous nature as to demonstrate intentional, willful, wanton or reckless conduct resulting from either an evil motive or because of a reckless indifference to the rights of others. Ruffing v. 84 Lumber Co., 410 Pa.Super. 459, 600 A.2d 545, 551 (1991). It is the role of the trial court to determine, in its discretion, whether the plaintiff has presented sufficient evidence from which a jury could reasonably conclude that the defendant acted outrageously. Slappo v. J's Development Assoc., Inc., 791 A.2d 409, 417 (Pa.Super.2002). We review the trial court's decision for an error of law. Id.

As set forth above, the evidence of record supported the trial court's conclusion that Lazarus detained Angelopoulos in violation of the Retail Theft Act for an unreasonable period of time, in an unreasonable manner, and for a nefarious purpose. At the very least, Lazarus's conduct exhibited a reckless indifference to the rights of Angelopoulos. Accordingly, we discern no error by the trial court in submitting the issue of punitive damages to the jury. Thus, Lazarus is not entitled to relief on this claim.

For the foregoing reasons, we affirm the Order of the trial court awarding a new trial to Angelopoulos.

Order affirmed.
GARNER v. KOVALAK
817 N.E.2d 311 (Ind. App. 2004)

MAY, Judge

Terry Garner appeals the small claims court’s judgment in favor of Eric Kovalak. Garner raises one issue, which we restate as whether the court erred when it determined Kovalak was not liable to Garner for the damage Kovalak caused to Garner’s trees when Kovalak swerved into Garner’s yard to avoid a car crash. We affirm.

FACTS AND PROCEDURAL HISTORY

Garner and his wife, Elizabeth, own a property in St. Joseph County that measures just over four acres. Along the north and east sides of the property, next to the roadway, are trees that measure twenty to twenty-five feet tall. At about noon on September 29, 2003, Kovalak was driving on the road adjacent to the Garners’ property when a brown Cadillac driven by an unidentified driver swerved over the centerline and into Kovalak’s lane. To avoid the Cadillac, Kovalak drove onto the Garners’ property. Kovalak avoided the Cadillac, but he knocked down two of the Garners’ trees. Garner obtained an estimate that removal and replacement of the damaged trees would cost $1,500.00.

On November 25, 2003, Garner filed a small claims action against Kovalak for the damaged trees. After a bench trial, the court entered judgment for Kovalak in an order that stated simply:

–After due consideration, the Court finds that judgment should be and is entered in favor of [Kovalak] and against [Garner].‖ (App. at 17.)

DISCUSSION AND DECISION

As an initial matter, we note Kovalak did not file an appellee’s brief. When an appellee fails to file a brief, we may reverse the trial court’s decision if the appellant demonstrates a prima facie case of reversible error. Wright v. Wright, 782 N.E.2d 363, 366 (Ind. Ct. App. 2002). Prima facie means –at first sight, on first appearance, or on the face of it.‖ Thurman v. Thurman, 777 N.E.2d 41, 42 (Ind. Ct. App. 2002). This rule relieves us of the burden of controverting appellant’s arguments for reversal, which is a burden that properly rests with the appellee. Wright, 782 N.E.2d at 366. It does not, however, relieve us of –our obligation to decide the law as applied to the facts in the record in order to determine whether reversal is required.‖ Vukovich v. Coleman, 789 N.E.2d 520, 525 n.4 (Ind. Ct. App. 2003).

Because the rules of small claims court make trials therein informal, –with the sole objective of dispensing speedy justice between the parties according to the rules of substantive law,‖ Ind. Small Claims Rule 8(a), we review the court’s procedural and evidentiary decisions with deference. Lae v. Householder, 789 N.E.2d 481, 483 (Ind. 2003). However, we review de novo a small claims court’s decisions regarding substantive law. Id. Judgments of small claims courts are –subject to review as prescribed by relevant Indiana rules and statutes.‖ Id. (quoting S.C.R. 11(A)).

Garner claims the court should have found Kovalak responsible for the damage to his trees under the theory of trespass quare clausum fregit. See footnote Under that theory:
[II]t is necessary for the plaintiff to prove only that he was in possession of the land and that the defendant entered thereon without right, such proof entitling the plaintiff to nominal damages without proof of injury, and upon additional proof of injury to products of the soil, the plaintiff is entitled to compensatory damages. *Hawke v. Maus*, 141 Ind. App. 126, 131, 226 N.E.2d 713, 717 (1967).

Garner testified that he and his wife own the land on which Kovalak drove and the trees Kovalak damaged. Garner also testified he did not give Kovalak permission to enter his property on the day of the accident, and he presented an estimate indicating the damage was $1,500.00. Kovalak acknowledged his vehicle hit two of Garner’s trees. Based on that testimony it appears uncontested that Garner possessed the land, Kovalak entered without right, and $1500 worth of damage was caused to Garner’s products of the soil. Id. Accordingly, Garner demonstrated all the elements required for recovery under the theory of trespass *quare clausum fregit*. However, a trespasser cannot be held liable unless a voluntary act caused his entry onto the plaintiff’s property. As we explained in *Hawke*: In order to be liable for a trespass on land . . . , it is necessary only that the actor intentionally be upon any part of the land in question. It is not necessary that he intend to invade the possessor’s interest in the exclusive possession of his land and, therefore, that he know his entry to be an intrusion. The intention which is required to make the actor liable under the rule stated in this Section is an intention to enter upon the particular piece of land in question, irrespective of whether the actor knows or should know that he is not entitled to enter.

Although it is not necessary that the trespasser intend to commit a trespass or even that he know that his act will constitute a trespass, it is required for trespass that there be an intentional act and an intent to do the very act which results in the trespass. The driver of an automobile who suddenly loses control of his car because he is seized with a heart attack, a stroke, a fainting spell, is not liable unless he knew that he was likely to become ill, in which case he is to be found negligent in driving the car at all. The same conclusions are reached when the defendant’s car is struck by another vehicle and thrown out of control. *Id.* at 129-30, 226 N.E.2d at 715-16 (internal citations and quotations omitted).

Thus, the question before us is whether Kovalak’s act, swerving his vehicle onto Garner’s property to miss an on-coming car that had crossed the centerline and entered Kovalak’s lane, was —intentional or —unintentional. Id Kovalak testified he used both hands to turn his truck right to avoid the Cadillac and he left the road such that the closest his truck came to the Cadillac was 15 to 25 feet. App. at 14.) Garner cites that testimony as proof Kovalak intentionally drove onto Garner’s property. We disagree.

Kovalak’s testimony indicated he was driving on the highway at fifty-five miles per hour when an on-coming car crossed over his lane into the grass on his side of the road and then back into his lane. He claimed he swerved to prevent a head-on collision. The police report indicates the officer —photographed the tire marks left by the unidentified vehicle. (Defendant’s Exhibit A at

4.) Kovalak’s insurer found he was not responsible for the accident because an unidentified
driver ran him off the road. Given those facts, we cannot say the trial court erred in implicitly finding the act of another caused Kovalak to leave the road and enter the Garners’ property, and that Kovalak’s act was therefore unintentional. See, e.g., State v. Magnuson, 488 N.E.2d 743, 750 (Ind. Ct. App. 1986) (The record contained evidence from which the trier of fact could determine the driver had no time for deliberation, and therefore an instruction on sudden emergency was not unwarranted.), reh’g denied, trans. denied.

Nor can we say as a matter of law that Kovalak’s decision to steer his truck to the right to avoid a head-on collision was an –intentional act. An intentional act is one –resulting for the actor’s will directed to that end.‖ Black’s Law Dictionary 25 (7th ed. 1999). –An act is intentional when foreseen and desired by the doer, and this foresight and desire resulted in the act through the operation of the will.‖ Id. An act done intentionally is also done voluntarily. ‖Id.‖ at 1569. An act is voluntary if it is not constrained, impelled or influenced by another.‖ Webster’s 3rd New International Dictionary Unabridged 2564 (G. & C. Merriam Co. 1976). As a trier of fact could reasonably find Kovalak’s action was impelled by the brown Cadillac, we decline to hold as a matter of law his act was intentional.

Affirmed.

SHARPNACK, J., and BAILEY, J., concur.

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Learning Plan 3

Creating a Contract

**Development of Contract Law**
People have entered into agreements for thousands of years. Before the development of a monetary system, people would barter for goods and services. As societies progressed, so did commerce. Agreements became more sophisticated and money became the medium of exchange. Such were the beginnings of contract law.

Commerce around the world today could not function without contracts. Contracts range from buying lunch at your favorite fast food restaurant to developing an upscale high-rise condominium complex in an urban setting. As contracts became more complex, so did the laws governing contracts, including the development of the *Uniform Commercial Code*.

But, what exactly is a contract? Black's Law Dictionary, 5th Ed., defines a contract as follows:

**Contract.** An agreement between two or more persons which creates an obligation to do or not to do a particular thing.

Read the following articles:

**Contracts**, including the imbedded links, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

**Contract Basics** presented by FindLaw.

Contract law is generally state law. Each state has its own particular definition of a contract.

**Bilateral Contract**
A bilateral contract is a contract in which each contracting party makes a promise to the other contracting party.

**Unilateral Contract**
A unilateral contract is a contract in which one contracting party makes a promise to the other contracting party in return for an act by the other party.

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Executory Contract
An executory contract is a contract in which one or both contracting parties are required to perform some act in the future. The contract is not yet completed.

Executed Contract
An executed contract is a contract that has been fully performed by both contracting parties and nothing remains to be done by either party. The transaction is complete.

Valid Contract
A valid contract is a contract that fulfills all the requirements of a contract and is enforceable.

Unenforceable Contract
An unenforceable contract is a contract that is otherwise valid, but cannot be enforced, because fails to meet a certain requirement for that type of contract. For example, certain contracts, such as contracts for the sale of land, must be in writing to be enforceable.

Void Contract
A void contract is a contract that is void and without legal effect from its attempted creation. An example of a void contract is a contract to commit a crime.

Voidable Contract
A voidable contract is a contract that is enforceable, but can be avoided by one or both of the contracting parties. An example of a voidable contract is a contact entered into by a mentally incompetent person.

Review the article, Contracts and the Law presented by FindLaw.

Offer + Acceptance + Consideration = Contract
Under the common law, three elements are necessary to create a contract:
1. Offer
2. Acceptance
3. Consideration

Please review the YouTube video Contracts – Offer and Acceptance generally regarding offer and acceptance before continuing with the reading.

Offer
The term offer has been defined in slightly different ways by courts and state legislatures. Black's Law Dictionary, 5th Ed., provides several definitions of an offer, including the following:
Offer, n…. A promise, a commitment to do or refrain from doing some specified thing in the future. The offer creates a power of acceptance permitting the offeree by accepting the offer to transform the offer's promise into a contractual obligation.

More simply stated, an offer is a promise made by the offeror (the person making the offer) to do something, or not to do something.

Elements of an Offer
To be effective, the offeror must have present intent to make an offer. In addition, the terms of the offer must be:
1. Definite and certain
2. Communicated to the offeree (the person receiving the offer)

Present Intent. The offeror must have present intent to make an offer that can be accepted to create a contract. At times a person may make a statement that appears to be an offer, but does not intend it to be an offer. An example is a person who is merely joking. If Otto Mobile, who is frustrated with car exclaims, "I'll sell this car to the first person that gives me $5!" such a statement is not a real offer.

In cases where it is difficult to determine whether a person intended to make an offer, the court will apply the "objective standard" test. The court will hold that statement is an offer, if a "reasonable person," who objectively reviews the statement and the surrounding circumstances, would believe that the offeror intended to make an offer.

Definite and Certain. The offer must be definite and certain. It must sufficiently identify the subject of the offer and the terms of the offer. The offer must be so certain that the offeree need only say "I accept!" to create a contract. "I offer to sell you one of my boats," is not an offer. It is neither definite nor certain, because it does not identify which boat is to be sold, nor state the purchase price that the offeror would accept to create a contract.

Communicated to the Offeree. The offer must also be communicated to the offeree. If the offeror merely thinks about making an offer, then it is not an offer. Likewise, if the offeror tells someone that he intends to make an offer, but does not communicate it to the offeree, then no offer has been made.

Termination of an Offer
No contract is created if an offer is terminated prior to its acceptance. An offer may terminate by the action (or inaction) of the parties, or by operation of law.

Termination by the parties action/inaction
An offer is terminated if:
1. The offeree rejects the offer.
2. The offeror revokes the offer before it is accepted by the offeree.
3. The offer expires according to its terms.
4. The offeree fails to accept the offer within a reasonable time.
An offeree may terminate an offer by **rejecting** it. An offeror may terminate an offer, in many cases, by **revoking** it before it is accepted by the offeree. Generally, the offeror's revocation is not effective until it is received by the offeree.

**Exceptions:**

**Option Contract.** An offeror may not revoke an offer if the offer has entered into an **option contract.** An option contract is an agreement in which the offeror has agreed to "hold the offer open" for a certain period of time in exchange for some payment by the offeree. For example, Mary Millionaire, who owns an office building, offers to sell the building to Bob Buyer. Bob does not currently have funds to purchase the building, but would like time to obtain financing. The parties agree to enter into a real estate option contract, in which Mary and Bob agree that in exchange for Bob's payment of $5,000 to Mary, Mary gives Bob an option to buy her building for $500,000, if Bob tenders (delivers) the money to Mary within 90 days. Under the terms of this option contract, Mary may not revoke her offer for 90 days. If Bob tenders the agreed purchase price to Mary within that time period, she must sell him the building. If Bob fails to tender the purchase price to Mary within the 90 days, Mary's offer terminates.

**Unilateral Contract.** Generally, an offeror may not revoke an offer for a unilateral contract (a contract requiring offeree's act as acceptance), if the offeree has started performance. If a court allows an offeror to revoke an offer for a unilateral contract prior to the offeree's full performance, the court may order the offeror to compensate the offeree for any benefit that the offeror received from offeree's partial performance.

For example, if Howard Homeowner offers to pay Pat Painter $500 to paint Howard's house and then Howard revokes the offer when Pat is only half finished painting the house, the court in one state may prohibit Howard from revoking the offer, while a court in another state may allow Howard to revoke the offer, but order that Howard pay Pat for the reasonable value of painting half of Howard's house.

**Firm Offers.** Under the Uniform Commercial Code (UCC) a **firm offer** by a **merchant** (a person in the business of selling the contract item) to sell **goods** (personal property governed by the UCC) may not be revoked, if the offer is written and contains assurances by the merchant that the offer will remain open. Section 2-205 of the UCC provides:

**§ 2-205. Firm Offers.** An offer by a merchant to buy or sell goods in a signed writing which by its terms gives assurance that it will be held open is not revocable, for lack of consideration, during the time stated or if no time is stated for a reasonable time, but in no event may such period of irrevocability exceed three months; but any such term of assurance on a form supplied by the offeree must be separately signed by the offeror.

*Note:* The UCC is a model code that states have adopted with modifications. As a result, the foregoing section may be different in different states.

An offer may also terminate if it is not accepted by the deadline for acceptance stated in the offer. If an offer does not have a deadline for acceptance, it may terminate if it is not accepted by the offeree within a **reasonable time.** What is considered a reasonable time depends upon the
circumstances? For example, a reasonable time to accept an offer to buy bananas is much shorter than a reasonable time to accept an offer to purchase office furniture.

Termination by operation of law

An offer may also terminate before acceptance by *operation of law*, including:

1. Either the offeror or offeree die or become mentally incompetent.
2. The subject matter of the offer (the contract item) is destroyed.
3. A law is passed after the offer, but before acceptance, that would make the contract illegal.

An offer terminates if either the offeror or offeree dies or becomes mentally incompetent before the offer is accepted by the offeree. (Neither person has the capacity to enter into a contract.) Destruction of the subject matter of the contract before the offer is accepted also terminates the offer. For example, if Mary Millionaire offers to sell her office building to Bob Buyer, but the building burns down before Bob accepts, the offer is terminated. Finally, an offer is terminated if a law is passed before acceptance that would make the contract illegal. If Joe Gambler offered to sell gambling machines to Big Bucks Casino, but the state legislature then passed a statute prohibiting gambling prior to Big Bucks' acceptance, the offer would be terminated.

Acceptance

An offer must be accepted by the offeree to create a contract. If an offer is not accepted, then no contract is formed. Once an offeree accepts an offer, the offeree cannot change or withdraw the acceptance.

Elements of an Acceptance

To be effective, an acceptance must be:

1. An unequivocal and unconditional acceptance, without material changes to the offer
2. Communicated to the offeror (unless the offer requires the performance of an act)

Unequivocal and Unconditional. The acceptance must accept the offer unconditionally, without changes. The offeree may not put conditions on the acceptance. For example, the offeree may not say, "I accept your offer, if you lower the price by $100." The requirement that the acceptance match the offer is called the "mirror image rule." The acceptance must "mirror" the offer. If an offeree attempts to accept the offer with changes, the offer terminates and the offeree attempted acceptance is deemed to be a counteroffer. If an counter offer, the parties switch sides. The original offeree is the offeror and the original offeror is offeree.
Communicated to the Offeror. The offeree must communicate the acceptance to the offeror. If the offer does not require a particular manner of communication, then the offeree may communicate the acceptance using any reasonable method.

Generally, if an offer requires that the acceptance be communicated by a certain method (such as a requirement that the acceptance be written and sent by certified mail), then the acceptance must comply with such terms to be effective. In such case, the acceptance is effective when it is mailed. If an offeree attempts to communicate acceptance through an unauthorized method, then the acceptance is not effective until it is received by the offeror, prior to revocation of the offer.

\textit{Exception:} An acceptance of a unilateral contract need not be communicated to the offeror. An offer for a unilateral contracts requires the performance of an act by the offeree to accept the offer. For example, an offerer may offer to pay a reward for the return of a lost item. In a unilateral contract, the offeree must perform the act, rather than merely communicate his acceptance.

\textbf{CONSIDERATION}

Consideration is the final necessary element of a contract. An offer and acceptance does not create a contract without consideration.

\textbf{Elements of Consideration}

Consideration must be:

1. A bargained for exchange
2. Have legal value

\textbf{Bargained for Exchange.} The parties to a contract must exchange something as consideration for the contract. A promise that is not supported by consideration is not a contract. It is simply a promise. The parties to a bilateral contract exchange a promise for a promise. The parties to a unilateral contract exchange a promise for an act. A pure gift is not consideration, because it was not given in exchange for something.

\textbf{Legal Value.} The consideration for a contract must have legal value. Legal value is not the same as economic value. Legal value can be:

1. Promising to do something that a person is not required to do.
2. Promising \textbf{not} to do something that a person is entitled to do.

Alan Account can enter into a contract by promising to provide accounting service to a business. Because Alan is not required to provide such service, his promise has legal value. However, if Alan's daughter, Suzy, promised Alan that she would not exceed the speed limit when driving to and from school, such a promise would not have legal value, because Suzy has a pre-existing legal duty to drive safely and not to exceed the speed limit.

Promising \textbf{not} to do something also has legal value. If Alan Account made a mistake in his accounting service, his client could bring a lawsuit against him to recover the amount of money lost by Alan's mistake. However, Alan and his client could enter into a contract in which the client agreed not to exercise his legal right to sue Alan, in exchange for Alan's payment of an agreed amount of money to compensate the client for Alan' mistake.
Read the article *What is "Consideration" and How Much is Required?* presented by FindLaw.

**EQUITABLE THEORIES**

Contract law requires that certain requirements be fulfilled before a contract is created. Unfortunately, transactions are not always simple. A situation may occur where a person entered into a transaction in good faith and conferred a benefit upon another person, only to find that a valid, enforceable contract had not been formed. Rather than allow the other person to profit from the lack of a contract, a court may use equitable theories of *quasi-contract* and *promissory estoppel* to prevent injustice.

**Quasi-Contract**

If an injustice would result, a court may impose a *quasi-contract* ("like a contract"), to provide the "innocent" party with the reasonable value of the thing sold, or services conferred, upon the other party. *Quasi-contracts* are completely different than an actual contract in which two parties have bargained for their positions. They do not arise from any agreement, express or implied, between the parties themselves, rather they are fictional contracts imposed by courts and imposed on parties in the interest of fairness and justice.

**Promissory Estoppel**

*Promissory estoppel* occurs when a person makes a promise to another person that he should reasonably expect would cause the other person to act or forbear from acting, and which does in fact cause such action or forbearance, and injustice would occur unless the promise was enforced.

Read the article addressing equitable remedies, entitled *When Will a Promise or Statement Be Considered a Binding Contract?* presented by FindLaw.

**CONTRACT LAWS**

As previously mentioned, contract law is generally state law. Each state has its own particular definition of a contract.

Review the *statutes* of your state, or a state of your choice, that define:

- Offer
- Acceptance
- Consideration

Statutes are available online at the Cornell University Law School Legal Information Institute. Ask your instructor for assistance, if you have difficulty locating the statutes.
Read the following cases and any other cases assigned by your instructor.

Supreme Court of South Dakota.


No. 26776.

Decided: August 6, 2014


¶ 1.] East Side Lutheran Church (East Side) appeals from a summary judgment ruling that barred its claim for failing to timely file suit within the applicable six–year statute of limitations. We affirm in part and reverse in part.

Background

¶ 2.] In April 2002, East Side contracted with NEXT, Inc. (NEXT) for construction of a new addition to East Side's church and renovation to its existing structure. NEXT worked as East Side's representative for the project and contracted with third–party defendants Brown Architecture & Design Company (Brown) and Fiegen Construction Company (Fiegen). Brown provided design and architectural work on the project and Fiegen served as the general contractor. Fiegen subcontracted with fourth–party defendant M.J. Dalsin Company (Dalsin) to complete the roof construction associated with the project.1 The project was substantially completed in August 2003.
[¶ 3.] In the months immediately following the project’s completion, East Side experienced a variety of problems throughout the structure. The problems included ice dams, bats in the church, chipping concrete, hail penetration, and drainage issues, but the overriding problem was water infiltration. The water infiltration persisted and resulted in this litigation.

[¶ 4.] East Side and NEXT communicated about, and NEXT attempted to eradicate, the water infiltration from the date of the project’s completion until May 2009. On January 23, 2009, NEXT’s attorney sent a letter to East Side explaining that Fiegen and Dalsin were “unwilling to perform any additional work[.]” and that NEXT had, without admitting liability, “notified its insurance carrier of a potential claim.” Later that spring, on May 28, 2009, NEXT’s attorney informed East Side’s attorney that NEXT “will be undertaking no additional repairs to” the church. The letter further stated that East Side “will need to either undertake its own repairs and proceed with litigation or contact Fiegen and Dalsin regarding any such repairs.”

[¶ 5.] In March 2010, East Side hired Michael Ollerich of American Technical Services. Ollerich’s reports confirmed that the church was experiencing water infiltration. Ollerich’s reports further indicated the project’s design contained structural errors; the work completed contained construction errors; and the structure was experiencing ventilation and insulation problems. East Side filed suit against NEXT in July 2010.3

[¶ 6.] NEXT, Brown, Fiegen, and Dalsin (Defendants) moved for summary judgment on the basis that East Side filed its suit outside of the six-year statute of limitations. See SDCL 15–2–13. The Defendants argued that because East Side knew of the water infiltration immediately after construction was completed, the six-year statute of limitations began to run as early as August 2003. As a result, the statute of limitations lapsed in 2009 and East Side’s July 2010 lawsuit was not timely filed.

[¶ 7.] East Side opposed summary judgment and argued that its lawsuit is based in part on the project’s structural design errors and construction errors. Because it did not know of the structural design errors and construction errors until Ollerich’s 2010 reports, it argued its claims did not accrue until 2010, making its suit timely. East Side also argued that equitable estoppel tolled the statute of limitations.

[¶ 8.] The circuit court granted summary judgment to Defendants on the statute of limitations issue because East Side “had actual or constructive notice of a cause of action immediately after the substantial completion [of the project] in August of 2003.” The circuit court also granted summary judgment to Defendants on the issue of equitable estoppel because there was no “genuine issue of material fact regarding whether or not any of the [D]efendants misrepresented or concealed material facts from [East Side] in order to induce [East Side] to change its position in reliance upon either those misrepresentations or that concealment.” East Side now appeals to this Court arguing the circuit court’s rulings on the statute of limitations and equitable estoppel were error.4

Decision

Statute of limitations

[¶ 9.] The parties agree that the six-year statute of limitations prescribed by SDCL 15–2–13 controls East Side’s claims. East Side commenced this action in July 2010. Thus, any claims that accrued before July 2004 are barred. As a result, we must resolve if there are any genuine issues of material fact as to whether any or all of East Side’s claims accrued before July 2004.

¶ 11. “Because the point at which a period of limitations begins to run must be decided from the facts of each case, statute of limitations questions are normally left for a jury.” Strassburg, 1998 S.D. 72, ¶ 7, 581 N.W.2d at 513 (citation omitted); see also Wissink v. Van De Stroet, 1999 S.D. 92, ¶ 11, 598 N.W.2d 213, 215 (citations omitted) (“This Court has recognized that, generally, statute of limitations questions are left for the jury.”); Huron Ctr., Inc. v. Henry Carlson Co., 2002 S.D. 103, ¶ 11, 650 N.W.2d 544, 548 (citation omitted) (“[T]he question of when accrual occurred is one of fact generally reserved for trial.”). “Here, we must ascertain whether there is any genuine issue of material fact concerning the date the cause of action accrued; if not, and if the applicable limitations period has expired as a matter of law, then the [Defendants are] entitled to summary judgment.” Strassburg, 1998 S.D. 72, ¶ 7, 581 N.W.2d at 513 (citation omitted).

¶ 12. There is no genuine issue of material fact concerning East Side’s actual notice of the water infiltration prior to July 2004. It is undisputed East Side knew water infiltration existed throughout the building almost immediately after construction was completed in August 2003. Because East Side’s actual notice of the water infiltration gave rise to a situation where East Side could have filed suit and sought relief, any claim with a sufficient relationship to the water infiltration so as to put East Side on constructive notice of that claim (water infiltration claim) accrued and statutorily lapsed prior to East Side’s July 2010 lawsuit. See Spencer v. Estate of Spencer, 2008 S.D. 129, ¶ 16, 759 N.W.2d 539, 544 (citation omitted) (“A cause of action accrues when the right to sue arises.”).

¶ 13. We must next determine whether accrual of the water infiltration claims encompasses all of East Side’s alleged design and construction error claims, and whether that is a factual or legal question.5 East Side contends this case presents “different acts constituting breaches of contract,” which result “in separate or different damages” that “give rise to separately accrued claims.” East Side argues that “[m]any of the structural deficiencies and defects [discovered in 2010] had nothing to do with water infiltration[,]” and as a result, there is a factual dispute as to when the different claims accrued. Defendants argue that the water infiltration places East Side, as a matter of law, on constructive notice of any other defect in the building. Defendants contend there have not been different acts constituting separate breaches of contract, but only East Side learning the full extent of its damages.6

¶ 14. A claim can accrue “even when one may not yet know all the underlying facts or the full extent of damages.” Strassburg, 1998 S.D. 72, ¶ 13, 581 N.W.2d at 515 (citations omitted). But different causes of action can accrue under the same contract. See Dakota, Minn. & E. R.R. Corp. v. Acuity, 2006 S.D. 72, ¶ 23, 720 N.W.2d 655, 662 (providing that different causes of action existed under the same insurance contract). “Statutes of limitations begin to run when plaintiffs first become aware of facts prompting a reasonably prudent person to seek information about the problem and its cause.” Strassburg, 1998 S.D. 72, ¶ 13, 581 N.W.2d at 515 (citations omitted).

¶ 15. East Side had actual notice of the water infiltration throughout its building prior to July 2004. Whether that actual notice is enough to put East Side on constructive notice of its structural design error
and construction error claims (making the structural design error and construction error claims accrue prior to July 2004), and whether that determination is a question of fact or law, is the heart of this case. Because what a reasonably prudent person should inquire into when learning of water infiltration can differ depending on the circumstances, we conclude there is a genuine issue of material fact as to when East Side’s structural design error and construction error claims accrued. Huron Ctr., 2002 S.D. 103, ¶ 11, 650 N.W.2d at 548 (providing when accrual occurs is a question of fact reserved for trial). As a result, it is up to the trier of fact to determine whether East Side’s actual notice of the water infiltration constitutes a sufficient circumstance to put a prudent person on inquiry of each of the construction error and design error claims East Side complains of, i.e., which of East Side’s claims are barred by the statute of limitations because of the relationship to the water infiltration. See Strassburg, 1998 S.D. 72, ¶ 10, 581 N.W.2d at 514; see also SDCL 17–1–4. On remand, the trier of fact must parse out which alleged deficiencies have a sufficient relationship to the water infiltration to put East Side on actual or constructive notice of the alleged deficiency. See Johnston v. Centennial Log Homes & Furnishing, Inc., 305 P.3d 781, 789 (Mont.2013) (providing “that factual questions arise in determining the extent to which the problems discovered by 2005 are related to the issues discovered between 2008 and 2010”). If East Side was put on actual or constructive notice of the alleged deficiency because of the actual notice of the water infiltration, then a claim based on that alleged deficiency is not a separate cause of action but accrued at the time of the water infiltration and is therefore barred by the statute of limitations. If East Side was not put on actual or constructive notice of the alleged deficiency because of the actual notice of the water infiltration, then a claim based on that alleged deficiency is a separate cause of action with a separate accrual date.

[¶ 16.] Defendants ask us to rule as a matter of law that East Side possessed constructive notice of its design error and construction error claims. In doing so, Defendants state Ollerich’s reports did not outline separate and distinct causes of action, but rather outlined the full extent of East Side’s damages. Defendants argue that the water infiltration was such an obvious manifestation of a defect that all reasonably prudent persons would be put on inquiry about underlying problems with the design and construction of the building. See Huron Ctr., 2002 S.D. 103, ¶ 16, 650 N.W .2d at 549 (“There is, however, no evidence of the initial severity of the problems, whether it was possible that they could have been dismissed as simple maintenance, or at what point the problems became such that Huron Center should have known they were beyond routine repairs.”); see also Performing Arts Ctr. Auth. v. Clark Constr. Grp., Inc., 789 So.2d 392, 394 (Fla.Ct.App.2001) (citations omitted) (“In sum, we conclude that where there is an obvious manifestation of a defect, notice will be inferred at the time of manifestation regardless of whether the plaintiff has knowledge of the exact nature of the defect. However, as in this case, where the manifestation is not obvious but could be due to causes other than an actionable defect, notice as a matter of law may not be inferred.”). However, whether a defect is so obvious as to encompass all potential claims raises the question: How obvious does a defect need to be to make all claims accrue? That determination will be properly addressed by a trier of fact when it decides which claims East Side was put on notice of when it learned of the water infiltration. We decline to make that determination as a matter of law. Therefore, we reverse the circuit court, holding that a trier of fact must determine whether any or all of East Side’s design error and construction error claims accrued at the time of actual notice of the water infiltration.
Equitable Estoppel

¶ 17. Equitable estoppel will only be applied when all four elements are proven by clear and convincing evidence: (1) Defendants made false representations to or concealed material facts from East Side; (2) East Side did not have knowledge of the real facts; (3) the misrepresentations or concealment was made with the intention that it should be acted upon; and (4) East Side relied upon those misrepresentations or concealment to its prejudice or injury. See Wilcox v. Vermeulen, 2010 S.D. 29, ¶ 19 n.7, 781 N.W.2d 464, 471 n.7 (citations omitted); see also Cooper v. James, 2001 S.D. 59, ¶ 16, 627 N.W.2d 784, 789 (citations omitted).

¶ 18. East Side contends that NEXT lulled East Side “into a false sense of security” when NEXT continually reassured East Side that the water infiltration would be fixed. East Side contends this creates a question of fact preventing summary judgment. See Cooper, 2001 S.D. 59, ¶¶ 17–18, 627 N.W.2d at 789. We disagree. Even if East Side was lulled into a false sense of security that its problems would be fixed, it fails to identify a single fact demonstrating that Defendants misrepresented or concealed material facts. Indeed, NEXT, on numerous occasions, attempted to fix the water infiltration and even stated that it did not know why the infiltration continued. In addition, East Side had knowledge of the real facts of the case—that there was leaking throughout the building.

¶ 19. Even if Defendants’ actions to fix the water infiltration were misrepresentations intended to be relied upon, East Side could not have reasonably relied on those representations. In January 2009, NEXT informed East Side it had submitted a claim to its insurer. In May 2009, NEXT informed East Side that NEXT would not be undertaking any additional repairs to the church. The May 2009 letter further stated that East Side “will need to either undertake its own repairs and proceed with litigation or contact Fiegen and Dalsin regarding any such repairs.” These communications were given within the statute of limitations for any water infiltration claim. Therefore, equitable estoppel was properly denied by the circuit court.

¶ 20. In conclusion, we reverse the circuit court’s ruling that barred East Side’s claims of design error and construction error, concluding that a genuine issue of material fact exists to determine when those claims accrued. We remand for further proceedings in line with this opinion. Furthermore, we affirm the circuit court’s grant of summary judgment on the equitable estoppel claim.

FOOTNOTES
1. Dalsin in turn sub-subcontracted with fifth-party defendant AJ Contracting to provide work on the roof construction. Dalsin obtained a default judgment against AJ Contracting prior to the circuit court’s summary judgment ruling.

2. Water was found in the west entrance, east vestibule, Pastor’s office, quilting room, prison ministry office, furnace room, north-side basement, kitchen, pre-kindergarten room, kindergarten room, storage room, second-floor altar-guide room, and second-floor south furnace room. In addition, hail was found in the narthex. Gigi Rieder, East Side’s office manager, testified that the water infiltration was “throughout the structure.”

3. In addition to defending the lawsuit, NEXT sued third-party defendants Brown and Fiegen, Fiegen sued fourth-party defendant Dalsin, and Dalsin sued fifth-party defendant AJ Contracting.

4. Our review of a summary judgment ruling is clear: We must determine whether the moving party demonstrated the absence of any genuine issue of material fact and showed entitlement to judgment on the merits as a matter of law. The evidence must be viewed most favorably to the nonmoving party and
reasonable doubts should be resolved against the moving party. The nonmoving party, however, must present specific facts showing that a genuine, material issue for trial exists. Our task on appeal is to determine only whether a genuine issue of material fact exists and whether the law was correctly applied. If there exists any basis which supports the ruling of the trial court, affirma

5. East Side’s complaint alleges breach of contract and negligence causes of action. Defendants argue East Side cannot maintain an action for negligence because all of East Side’s causes of action arise from under the contract. See Fisher Sand & Gravel Co. v. S.D. Dep’t of Transp., 1997 S.D. 8, ¶¶ 14–15, 558 N.W.2d 864, 867–68 (providing that in order for a plaintiff to maintain a tort claim against a party it contracted with, a duty independent of the contract must exist). This issue, although briefly addressed to the circuit court and in the briefs by Defendants, was not addressed by the circuit court and is not an issue raised on appeal by either party. We therefore decline to address it.

6. Defendants also point to East Side’s complaint that only pleaded two causes of action: (1) breach of contract for not “performing the construction in a good and workmanlike manner[;]” and (2) NEXT’s negligence “in its construction and supervision of its subcontractors on the work completed[,]” Defendants argue that because the complaint did not outline each separate cause of action East Side presents to this Court, it cannot raise those separate actions on appeal. We disagree. “South Dakota still adheres to the rules of notice pleading[.]” Gruhlke v. Sioux Empire Fed. Credit Union, Inc., 2008 S.D. 89, ¶ 17, 756 N.W.2d 399, 409. “[U]nder notice pleading, a case consists not in the pleadings, but the evidence, for which the pleadings furnish the basis. Cases are generally to be tried on the proofs rather than the pleadings.” St. Pierre v. State ex rel. S.D. Real Estate Comm’n, 2012 S.D. 25, ¶ 20, 813 N.W.2d 151, 157 (citation and internal quotation marks omitted). East Side adequately put Defendants on notice of its claims and presented evidence in support of its claims. Both in its response to NEXT's statement of undisputed facts and at the summary judgment hearing, East Side claimed structural design errors and construction errors as reported by Ollerich. We conclude the issue was properly raised.


SEVERSON, Justice.

[¶ 21.] GILBERTSON, Chief Justice, and KONENKAMP, ZINTER, and WILBUR, Justices, concur.

GERAETS v.
HALTER
1999 SD 11, 588 N.W.2d 231
(1999)

AMUNDSON, Justice

Patrick and Michael Geraets appeal from a trial court judgment finding no enforceable contract on the sale of real property. We affirm.

FACTS
Patrick (Pat) and Michael (Mike) Geraets operated as a partnership known as "Geraets Brothers." Ernest and Ethel Halter owned land that the Geraets rented. Prior to the transaction in question, Ernest had always dealt with the partnership, Geraets Brothers, and not with either Pat or Mike individually.

On September 2, 1997, Mike Geraets and Ernest discussed the sale of Halters' land. A price of $750 per acre was agreed upon and the two decided to go to Ernest's attorney, Glen Eng, to draw up the necessary papers. On the way to Eng's office, Mike phoned Pat regarding the purchase of the land. Ernest was advised the brothers would be purchasing the land together.

When Ernest and Mike arrived at Eng's office, it was determined Mike and Pat were undecided as to the division of the land to be purchased. Attorney Eng advised the parties he would wait to draw up two offer and purchase agreements until the Geraets had decided how they wanted to split the land. A contract for deed would be drafted after the purchase agreements were received back, along with a $500 down payment.

On September 19, 1997, Mike and Pat contacted Eng with the information on how they wanted to split the land. Eng drew up the purchase agreements and the Halters signed them. Eng subsequently sent out two separate offer and purchase agreements signed by the Halters to Mike Geraets.

Neither Eng nor the Halters received any word back until October 22, 1997. In the interim, Ernest frequently stopped by Eng's office to inquire whether he had received any response. On October 22, Ernest stopped at Pat's home to ask about the status of the agreements. Pat was not available, but Ernest spoke with Pat's wife. Pat's wife informed Ernest that Mike had injured his back and he was contemplating quitting farming. Furthermore, Pat and Mike were considering dissolving their partnership.

The following day, October 23, Ernest and Pat spoke on the telephone. Pat informed Ernest that Mike was no longer interested but he (Pat) would take the land himself. Pat testified Ernest replied that he would "just as soon deal with one person." Ernest testified the one person he had in mind was the Geraets Brothers. Following the phone conversation, the same day, Ernest went to visit Pat. Ernest testified he told Pat at that time he did not want to go through with the sale. Pat testified that Ernest had only mentioned he was unsure what he wanted to do with the land.

On October 28, at approximately 1:00 p.m., Ernest went to Pat's home and told him "the deal was off." Ernest also told Pat he was not going to sell the land for anything less than $1,000 per acre. Ernest then went to Eng's office to advise him he no longer wished to sell. That same day Eng sent two letters, one to Pat and one to Mike, stating that the Halters had withdrawn the offer.

At some point near the end of October, Mike decided to allow Pat to purchase all of the property and gave him a copy of his purchase agreement. Pat crossed out Mike's name and signed both agreements. On the morning of October 28, Pat placed both agreements in his mailbox at the end of the driveway.
On October 29, Eng received the signed purchase agreements and earnest money check from Pat. The Halters refused to sell.

Pat and Mike, brought an action seeking specific performance to compel the Halters to sell the land according to the agreements notwithstanding Mike's assignment to Pat. The trial court denied specific performance, finding no contract. Geraets appeal, raising the following issues:

1. Did the trial court err in holding that the "Offer and Purchase Agreement" documents that had been signed by the Halters were not contracts to sell, but only offers to sell?

2. Did the trial court err in holding that Michael Geraets could not assign to Patrick Geraets his interest in the "Offer and Purchase Agreement" for which Michael Geraets was the designated purchaser?

3. If the signed "Offer and Purchase Agreement" documents were merely offers to sell, did the trial court err in holding that the Halters effectively revoked their offer prior to acceptance by the Geraets?

4. Did the trial court err in holding that the Halters were the "prevailing parties" entitled to an award of disbursements under SDCL 15-17-37 even though a money judgment was entered in favor of the Geraets on an alternative count for unjust enrichment?

**STANDARD OF REVIEW**

A trial court's findings of fact will not be disturbed unless they are shown to be clearly erroneous. Talley v. Talley, 1997 SD 88, ¶19, 566 NW2d 846, 851; Jasper v. Smith, 540 NW2d 399, 401 (SD 1995); Knudsen v. Jensen, 521 NW2d 415, 418 (SD 1994). Under this standard, findings will not be disturbed unless, after a review of all the evidence, we are firmly and definitely convinced a mistake has been made. Talley, 1997 SD 88, ¶19, 566 NW2d at 851; Cordell v. Codington County, 526 NW2d 115, 116 (SD 1994). Conclusions of law are reviewed de novo, giving no deference to the trial court's determinations. Id.

**DECISION**

1. **Whether there was an enforceable contract.**

Under SDCL 53-1-2, the elements necessary for formation of a contract are: (1) parties capable of contracting; (2) their consent; (3) a lawful object; and (4) sufficient cause or consideration.
Parties must be identifiable. SDCL 53-2-3. The trial court found the parties' initial negotiations did not constitute a contract because the critical element of who the buyer was had not been resolved. This information was later provided to attorney Eng and the purchase agreements were prepared for the parties to sign. The Halsters signed the purchase agreements. The issue whether or not this was a final and complete agreement was contested at trial.

At trial, Mike Geraets testified: "I didn't know if I wanted to go through with the purchase at that time.["] Pat testified, "when he [Ernest] called me I told him that Mike had hurt his back, and that we were wanting to buy the land, but we didn't know for sure who would take over that portion of Mike's[.]" The trial court reasoned: "If a contract had been reached, there's no discussion of who the buyer is, it's already bought. [If they have already reached a contract he has] already bought, so he obviously did not believe that a contract had already been reached."

"An agreement is the result of a mutual assent of two parties to certain terms, and, if it be clear that there is no consensus, what may have been written or said becomes immaterial." Watters v. Lincoln, 29 SD 98, 100, 135 NW 712, 713 (1912) (citation omitted). "Consent is not mutual unless the parties all agree upon the same thing in the same sense." SDCL 53-3-3. Ensuing negotiations evidence absence of intent that the purchase agreement constitutes a final and complete agreement. See Sabow v. Hall, 323 NW2d 861, 863 (SD 1982) (finding no final and complete agreement where negotiations between parties continued after offer and purchase agreement were signed); cf. Rusch v. Kauker, 479 NW2d 496, 500 (SD 1991) (finding a contract where the purchase agreement contained all necessary terms and conditions and any remaining negotiations involved the contract for deed).

While the Geraets contend the entire time they intended to purchase the land, their conduct showed otherwise. "Whether a contract is formed is judged objectively by the conduct of the parties, not by their subjective intent. The question is not what the party really meant, but what words and actions justified the other party to assume what was meant." Crine v. Kulzer, 498 NW2d 55, 57 (MinnApp 1993) (citations omitted). The evidence showed a delay from September 19, 1997, when the purchase agreements were received, until October 28, 1997, when the agreements were finally signed and placed in the mail. During this time, the evidence showed the Geraets themselves were uncertain as to the future of their partnership and whether the land would be purchased and, if so, who would purchase it. When Ernest finally went to visit Pat to inquire on the status of the agreements, he was told by Pat's wife that Mike was contemplating quitting farming and the partnership would be dissolved.

Based upon the Geraets own testimony, the trial court determined on-going discussions between Pat and Mike manifested no assent to be bound to a final agreement. Although there are factual disputes, the trial court is in the best position to assess the credibility of witnesses, weigh the conflicting evidence and observe the witnesses and the evidence first hand. Cowan v. Mervin Mewes, Inc., 1996 SD 40, ¶15, 546 NW2d 104, 109; In re Estate of Elliott, 537 NW2d 660, 662 (SD 1995). Upon review of the record, we find substantial evidence to support the conclusion of the trial court that no contract existed. Whenever an agreement has not passed beyond the condition of negotiation, "[a]nd, if it is left doubtful from all the evidence in the case whether a contract was concluded or not, equity will not grant specific relief." Watters, 29 SD at 104, 135NW at 713.\[^{11}\]
2. Whether the Geraets were prevailing party under statute.

Geraets contend they are the prevailing party. While the Geraets lost the issue of specific performance raised under their complaint, they obtained payment from the Halter for the following: $888 chisel plowing, $468.59 spraying costs and approximately $66 for picking rock. SDCL 15-17-37 allows the prevailing party to recover disbursements. The trial court determined the Halter to be the prevailing party. "The prevailing party is the party in whose favor the decision or verdict is or should be rendered and judgment entered." City of Aberdeen v. Lutgen, 273 NW2d 183, 185 (SD 1979) (interpreting prevailing party under SDCL 15-15-1) (citation omitted).

The Geraets' original complaint sought the remedy of specific performance to enforce a purchase agreement. Only at the conclusion of trial did the Geraets make a motion for compensatory damages for costs incurred. Halter never objected to the payment of those costs, in fact, they offered to reimburse Geraets prior to this lawsuit. The payment of Geraets' costs was not a contested issue. Therefore, Halter were properly held to be the prevailing parties.

Based on our holding on issue one, we see no need to discuss issues two and three.

We affirm.

MILLER, Chief Justice, SABERS, KONENKAMP, and GILBERTSON, Justices, concur.

Footnotes
1. Geraets argue that Halter, by signing the purchase agreements and sending them to the Geraets, did all that was necessary to create an enforceable contract. See McPherson v. Fargo, 10 SD 611, 74 NW 1057 (SD 1898). This argument presumes there was a final and complete agreement embodying the terms agreed to for the seller to sign. Id. at 1058. In the present case, there never was a final and complete agreement because the parties were of a different mind. Therefore, Fargo is inapplicable.
Learning Plan 4

Enforcing a Contract

UNENFORCEABLE CONTRACTS
Although a contract may have all the required elements (Offer + Acceptance + Consideration), it may not be enforceable. A contract may be unenforceable for several reasons:

1. A person did not have the capacity to enter into a contract.
2. A person did not voluntarily enter into the contract.
3. The contract does not comply with the statute of fraud, which requires that certain contracts be written.
4. The contract may be illegal.

Please review the brief article Who Lacks the Capacity to Contract? presented by NOLO Law for All.

Before continuing, briefly review the elements of a contract by reading the article Write a Business Contract: Key Considerations presented by FindLaw.

PERSONS LACKING CAPACITY
Contracting parties must possess the capacity (ability) to enter into a contract. During the development of contract law, it was recognized that certain groups of people may not fully understand consequences of entering into a contract and, therefore, need special protection from other persons who may take advantage of them. These group include:

1. Persons under the age of 18 years (minors)
2. Persons who are mentally incompetent
3. Persons under the influence of alcohol or drugs

Persons under the Age of 18 (Minors)
A person under the age of 18 years is not considered an adult. At age 18 a person is said to have reached the "age of majority." Prior to that age, a person is considered a "minor."

Although minors often enter into contracts, many state laws provide that such contracts are voidable. A voidable contract is enforceable, unless the minor decides to disaffirm (cancel) the contract. Generally, a minor who disaffirms a contract is entitled to the return of the consideration that the minor paid under the contract. The minor must also return the consideration that the minor received from the other party. Usually, a minor may disaffirm a contract at any time before the minor reaches the age of majority, and a reasonable time after
reaching such age. If a minor does not disaffirm a contract within a reasonable time after reaching the age of majority, the minor is held to have *ratified* the contract and is bound to its terms.

Some courts do not allow a minor to disaffirm a contract, if the minor misrepresented his/her age or was involved in some other wrongdoing when entering the contract.

**Necessaries**
An incapacitated person who later disaffirms a contract may still be liable for the *reasonable value* of any "necessaries" furnished by the other party. Necessaries include food, clothing, medical care, shelter, *etc.* **Note:** The reasonable value of such necessaries may be much less than what was actually charged by the other party.

**Persons who are mentally incompetent**
Contracts by persons who are mentally incompetent are treated in much the same way as contracts entered into by minors. A contract by a person who lacked the mental ability to understand the contract at the time he/she entered into the contract is voidable. In these cases, the contracts are voidable at the option of the mentally incompetent person but not the other party. As a voidable contract, the agreement is enforceable, unless a guardian for the incompetent person disaffirms the contract, or the incompetent person disaffirms the contract after regaining capacity.

⚠️ **Exception:**
**Persons Adjudicated Incompetent.** If a court had entered a decree declaring a person to be legally incompetent, a contract by the incompetent person after the entry of such decree is *void* and of no effect from its beginning.

**Persons under the influence of alcohol or drugs**
A contract entered into by an intoxicated person can either be valid or voidable depending upon the level of intoxication. For the contract to be voidable, it must be proved that the intoxicated person’s reason and judgment were impaired to the extent that he/she was unable to comprehend the legal consequences of entering into the contract. If the person was intoxicated but still understood the legal consequences the contract is enforceable.

**PERSONS LACKING VOLUNTARILY CONSENT**
A contract must be a voluntary agreement to be enforceable. If one party did not voluntarily consent to the contract, the contract is *voidable.* There are many situations in which consent may not have been voluntarily given:

1. **Mistake**
2. **Fraud**
3. **Duress**
4. **Undue Influence**

**Mistake**
**Mutual Mistake.** If both parties to a contract are mistaken about a *material fact* of the contract, then either party may *rescind* (cancel) the contract. In such case, each party must return the consideration that was received under the contract.

Please review the YouTube video [Contracts: Mutual Mistake](https://www.youtube.com/watch?v=example) posted by Aaron Dewald to learn
more about this type of mistake.

**Unilateral Mistake.** If only one party is mistaken about a material fact, then the contract is generally enforceable, unless the mistaken party can show some grounds for rescission, such as misrepresentation by the other party, knowledge of the mistake by the other party, an ambiguity in the terms of the contract, *etc.* As a general rule, contracting parties are under a duty to use reasonable care when entering into a contract. If the contract is written, it is presumed that the parties have read and understand the contract, and agree with its terms by signing the document.

Please review the YouTube video [Contracts: Unilateral Mistake](#) posted by Aaron Dewald to learn more about this type of mistake.

**Fraud**

Fraud occurs when one party to a contract intentionally misrepresents a fact to the other party. The innocent party's consent is not considered voluntary in such situation, because he/she did not know the true facts.

Fraud is always grounds for rescinding a contract. In the alternative, the innocent person may enforce the contract, rather than rescind it, and sue the fraudulent party for the damages resulting from the fraud. For example, a person who purchased an automobile from another person, who intentionally misrepresented the vehicle's mileage by turning back the odometer, may wish to keep the car and sue the seller for the difference in actual value of the car and the value with the lower mileage that was represented. The car buyer may also be able to recover punitive damages from the seller (additional money to punish the seller).

**Duress**

Duress occurs when one party to a contract *wrongfully* threatens the other party, so that the other party enters into the contract against his/her will. A threat may not always be wrongful. For example, a person may threaten to exercise a legal right, if such right available. However, a person may not threaten to do something that he/she knows cannot be done. For example, a landlord's threat to a tenant that "I'll have you deported, unless you sign a new lease," would be a wrongful threat. Under such a threat, a tenant may sign the lease under duress.

A contract entered into under duress is voidable and can be rescinded by the innocent party within a reasonable time after being removed from such duress. If the innocent party fails to rescind the contract within a reasonable time, then the party will have ratified the contract and will be bound to its terms.

**Undue Influence**

Undue influence occurs when one person takes advantage of another person's confidence and obtains his/her consent to a contract. Oftentimes the person being influence is an elderly person, a close friend, a person who is ill, or a person with decreased mental abilities. The influenced person may trust the other person and enter into the contract. Although the consent appears voluntary, it was actually obtained by undue influence to the detriment of the influenced person. ("Trust me.")

A contract entered into under undue influence is voidable and can by rescinded by the influenced person, or the person's guardian, within a reasonable time after discovering the undue influence.
**ILLEGAL CONTRACTS**

An illegal contract is void. Two examples of illegal contracts are:
1. A contract to commit a crime
2. A contract to commit a tort

Generally, a court will not enforce an illegal contract. As a result, the court system is not available to the parties in the event of a contract dispute.

**GAMBLING**

In general, wagers and games of chance are illegal. All states have statutes that regulate gambling (any scheme that involves distribution of property by chance among person who have paid valuable consideration for the opportunity to receive the property. Nearly all states operate lotteries, allow horse racing or permit games of chance (such as bingo) for charitable purposes. A few states allow casino gambling, but in any state a gambling-related contract may be illegal.

Read the article [Will your Contract Be Enforced Under the Law?](https://www.findlaw.com/contracts/illegal-contracts.html) presented by FindLaw.

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**STATUTE OF FRAUDS**

The *statute of frauds* is a general term given to statutes that require that certain types of contracts be written to be enforceable. Statute of Frauds has nothing to do with the commitment of a fraud, but rather it denies enforceability of certain contract that do not comply with its requirements.

Basically, the Statute of Frauds requires certain contracts to be in writing in some form. A contract that is oral when it is required to be in writing will not, as a general rule, be enforced by the courts.

Examples of such contracts include:
1. Contracts for the sale of land
2. Contracts that will take longer than one year to complete
3. Contracts for the sale of goods in which consideration is $500 or more
4. Promises made in consideration of marriage
5. Promises to answer for the debt or duty of another.

Review the YouTube video [Statute of Frauds Song](https://www.youtube.com/watch?v=Statute_of_Frauds_Song) posted by Mark DeAngelis to learn more about the Statute of Frauds.

Generally, only the party that is to be charged with a duty under the contract must sign the contract. For example, when a person borrows money from a bank or another financial institution, only the borrower signs the promissory note. Often, the written contract is not required to be in any formal format. A hand-written note be sufficient in some cases. However, it must contain enough information to identify the parties to the contract, the subject of the contract, and material terms of the contract.
A contract that fails to comply with the statute of frauds is unenforceable. However, a person who has provided consideration to the other party may be able to recover the reasonable value of the performance under the equitable theory of quasi-contract.

Read the article [What Contracts are Required to Be in Writing?](#) presented by FindLaw.

### Who May Enforce a Contract

Certainly, a contract may be enforced by the original parties to a contract. However, in many cases a contract may also be enforced by other parties, including:

1. Assignees
2. Beneficiaries of the contract

### Contracts that May be Assigned

Once a contract has been created, it is not unusual for one or both of the original parties to the contract to assign his/her rights in the contract to a third person. The person making the assignment is called the **assignor** and the person receiving the assignment is called the **assignee**.

Not all contracts may be assigned, including:

1. Certain written contracts contain a specific provision prohibiting the assignment of the contract, without the other party's prior written consent.
2. Contracts that require one party to provide a personal service, such as perform violin, are not usually assignable.
3. Statutes may prohibit the assignment of certain contracts. For example, a state may prohibit an employee to assign his/her wages under his contract of employment.
4. Contracts that increase the burden upon the non-assigning party.

Courts generally look with disfavor on limits imposed on assignments, and will carefully consider any restriction to determine if it is unduly burdensome on the party seeking the assignment.

### Effects of Assigning a Contract

After an assignment, the assignee "steps into the shoes" of the assignor. The assignee can receive the benefits and enforce the contract rights, as if he/she were the original party to the contract. Depending upon the assignment, an assignee may also become obligated to perform the duties of the assignor under the terms of the contract.

### Third Party Beneficiary Contracts

A contract need not be assigned to be enforced by a person who is not a party to the original contract. A contract may also be enforced by a beneficiary of the contract. There are two basic types of beneficiaries, intended and incidental.

**Intended Beneficiary**

An intended beneficiary can sue the promisor directly for breach of a contract made for the beneficiary’s benefit. There are two types of intended beneficiaries, creditor beneficiaries and donee beneficiaries.
Review the YouTube video [What is an intended third-party beneficiary?](https://www.uslawessentials.com/review-the-youtube-video-what-is-an-intended-third-party-beneficiary) posted by USLawEssentials to learn more about intended beneficiaries.

- **Creditor Beneficiary**
  A creditor beneficiary receives payment under the terms of the contract. If the payment is not made, the creditor beneficiary may enforce the contract, even though he/she is not one of the contracting parties. For example, if Sally Student borrows money from Last Chance National Bank to purchase a house and signs a promissory note (unilateral contract), promising to pay the bank $750 per month and Sally later enters into a contract to sell the house to George Graduate, who agrees to make the monthly payments, then the bank is a creditor beneficiary of the contract between Sally and George. Assuming the bank did not release Sally from the original promissory note, the bank can sue either Sally or George, or both, if the monthly payments are not made.

- **Donee Beneficiary**
  A donee beneficiary receives a benefit from a contract and may enforce the contract, even though he/she is not one of the contracting parties. An example is the beneficiary named on a life insurance policy. The contract is made between the insurance company and the policy holder. If the insurance company does not pay the agreed death benefit upon the death of the policy holder, the beneficiary may sue the insurance company, even though the beneficiary was not a party to the contract between the insurance company and policy holder.

**Incidental Beneficiary**
Any benefit that an incidental beneficiary receives from a contract between two parties is purely unintentional and therefore an incidental beneficiary may not enforce a contract. Although an incidental beneficiary may receive some benefit from a contract between two other persons, such benefit was not the purpose of the contract, but only an "incidental" benefit that resulted from the contract.

In determining whether a third party beneficiary is an intended or incidental beneficiary, the courts will generally use the reasonable person test. In other words, the beneficiary will be considered an intended beneficiary if a reasonable person in the position of the third party beneficiary would believe that the promise intended to confer on the beneficiary the right to bring suit to enforce the contract.

An example of an incidental beneficiary would be as follows: Howard Homeowner enters into a contract with Green Thumb Mowing Service to mow Howard's lawn. Nancy Neighbor receives a benefit from Howard's mowed lawn, which improves the appearance of the neighborhood. However, such benefit is not a material purpose of the contract. As a result, Nancy may not sue Green Thumb, if it fails to mow Howard's lawn and allows the grass to grow.
Review the statutes of your state, or a state of your choice, that define:
  o Consent to a contract
  o Mistake, duress, fraud, and undue influence
  o Oral and written contracts
  o Assignment of contracts

Statutes are available online at the Cornell University Law School Legal Information Institute. Ask your instructor for assistance, if you have difficulty locating the statutes.

**Breach of Contract**

When parties enter into a contract, they generally do not intend to breach (break) the contract. Unfortunately, for various reasons, contracts are broken. However, it is not often as simple as it may first appear to determine whether a contract has been breached. If it is determined that the contract has been breached, it is often difficult to determine the extent of damages resulting from such breach.

**Contract Conditions**

In determining whether a contract has been breached, it is necessary to review the conditions of the contract. A condition is an event that creates, limits, or terminates a party's duty to perform under the contract. Contract conditions can be classified as follows:

1. Conditions precedent
2. Conditions subsequent
3. Conditions concurrent
4. Implied conditions

**Condition Precedent**

A condition precedent is an event that must occur before a party becomes obligated to perform a duty under a contract. For example, Sam Speculator promises to buy land from Roy Rancher, if geologic tests indicate the potential for oil production on the property. (Here it is necessary for the geologic test to indicate the potential for oil production as a condition precedent.) The geologic tests are later conducted and returned, showing no chance of oil on the property. As a result, Sam's duty to buy the land did not arise.

Another example would be that John agrees to paint Eric’s house for $500 but Eric must buy the paint first. If Eric fails to buy the paint, John is not under any duty to paint the house and cannot be held in breach of the contract by failing to do so because the condition precedent has not been met.

**Condition Subsequent**

A condition subsequent is a condition that terminates an existing duty to perform. For example, Cathy Carpenter promises to build an addition to Howard Homeowner's house during the month of August, unless she is required to work on a new hotel during that month. Cathy is later informed that she is, indeed, required to work on the new hotel during the month of August. As a result, Cathy is relieved from the duty to build the addition to Howard's house.
Condition Current
Conditions current (sometimes called concurrent conditions), are conditions that occur together, so that both parties to the contract must perform their duties at the same time. For example, one party must deliver a deed to land at the time that the other parties tenders the agreed purchase price for the land.

Express Condition
An express condition is a condition that is expressly stated in the contract.

Implied Condition
An implied condition is one that is not expressly stated in the contract, but that is inferred from the circumstances surrounding the contract. For example, it may be implied that one party must deliver a deed to land at the time that the other parties tenders the agreed purchase price, even though this concurrent condition is not expressly stated in the contract.

SUBSTANTIAL PERFORMANCE
Once a party becomes obligated to perform a duty under a contract by a condition precedent, condition current, or condition subsequent, it must be determined whether the party adequately fulfilled his/her duty to perform. Generally, no breach occurs if the party substantially performed his/her duty adequately.

Read the article “Breach of Contract” and Lawsuits from FindLaw.
Read the article Breach of Contract: Material Breach from NOLO Law for All.

DAMAGES
Generally, if a party breaches a contract, the nonbreaching party is entitled to recover compensatory damages. The purpose of compensatory damages is to put the nonbreaching party in the monetary position that the party would have been had no breach occurred and the contract had been fully performed.

In certain cases, a nonbreaching party may also be entitled to consequential damages. Consequential damages may be awarded in addition to compensatory damages, if at the time the contract was made, a reasonable person could have expected that such damages would have resulted from a breach.

In some contracts the parties agree that, if a breach occurs, the nonbreaching party is entitled to liquidated damages. Liquidated damages are a set dollar amount to which the nonbreaching would be awarded in the event of breach. Such a provision is generally valid only if:

1. It would be difficult to determine actual damages at the time the parties entered into the contract.

2. The amount of the liquidated damages is reasonable and does not constitute a penalty. A nonbreaching party has a duty to mitigate (reduce) damages. For example, if an apartment
tenant breaches a one year lease after only two months, the landlord may not leave the apartment empty for the remaining ten months, but must attempt to rent it to another person. The amount of damages owed by the breaching tenant is reduced by the amount paid by the new tenant. (Of course, if the landlord cannot find a new tenant after reasonable efforts, the breaching tenant is liable for the full amount.)

**EQUITABLE REMEDIES**

In certain limited cases, monetary damages are not sufficient to adequately compensate a nonbreaching party. In such cases a party may be entitled to the equitable remedy of *specific performance* in which the court may order the breaching party to fulfill his obligations under a contract. Specific performance is available only in certain limited situations. For example, the seller of land may be ordered to convey the land to the buyer, because no two pieces of property are exactly the same. By contrast, specific performance is not available where a nonbreaching party may be adequately compensated by money.

Read the article *What is "Specific Performance" as a Legal Remedy?* presented by FindLaw.

Read the following case and any other cases assigned by your instructor.

**JACOBSON v. GULBRANSEN**

2001 SD 33, 623 N.W.2d 84 (2001)

ANDERSON, Lee D., Circuit Judge

Jeff and Carol Gulbransen (Gulbransens) appeal from a judgment in a civil action tried to the court. The trial court concluded that there was an enforceable agreement between Gulbransens and Garry Jacobson (Jacobson) for the sale of land and ordered Gulbransens to convey the land to Jacobson. On appeal, Gulbransens contend that there was no agreement between the parties or, alternatively, that the statute of frauds bars enforcement of the agreement. We affirm.

**FACTS**

Jacobson and Gulbransens are landowners in the Black Hills of South Dakota. They own land abutting on the south and north sides, respectively, of a parcel of land outside of Keystone, South Dakota that once belonged to the United States Forest Service. The Forest Service sold the property to Gulbransens in July 1997 in accordance with 16 USC § 521(c) *et seq.* These provisions permit the sale of small, difficult to manage parcels of land when the sale is in the public interest. The Forest Service conditioned the sale of any such parcel upon approval by all contiguous landowners.

Mr. Gulbransen contacted the Forest Service in 1993 after learning of the possibility of purchasing the parcel at issue in this appeal. Told that all adjoining landowners would have to
approve the sale, Gulbransen contacted his immediate neighbors while the Forest Service contacted other adjoining landowners including Jacobson and John Kinkead. Jacobson objected to the sale and reported his objections to the Forest Service. Jacobson had used two existing roads across the parcel for access to a remote portion of his own property and as an alternate egress route in case of a forest fire. To preserve these uses, Jacobson preferred that the land not be sold or developed.

The Forest Service informed Gulbransen of Jacobson's objections and directed that the objections be resolved before Gulbransen's application to purchase the land would be considered. Gulbransen were also informed that, unless the objections were resolved before March 31, 1994, the District Ranger would recommend to the Forest Supervisor that the land not be sold.

Gulbransen arranged a meeting with Jacobson and Kinkead to discuss their objections. At that meeting, he showed them a rough topographical map the Forest Service had given to him that depicted the area in question. The three men discussed the proposed sale and which piece of the parcel of land each of them would want if the sale took place. Asked to identify the piece he wanted, Jacobson pointed out a window of Gulbransen's house that faced south and indicated that was the land he wanted. Gulbransen mentioned that he and his wife wanted the five acres nearest their land and also mentioned their concerns about financing the purchase of such a large parcel of land. At the time of this discussion, the size of the parcel was thought to be around thirty acres. A later survey revealed it was only about twenty acres.

Subsequently, Gulbransen drew up and signed a document that he sent to Kinkead, Jacobson and another adjoining landowner. The document read:

This is to confirm agreement on the sale/transfer of property from the Small Tracts Act case #0207 to (name). At this date, exact surveys are not known or located, however I will convey areas sought by the McNulty's, Kinkead's and Mr. Jacobson. (McNulty's seeking areas between their property and Kinkead's, Kinkead's below their home to gate to mine, and Mr. Jacobson property located on the South end of the tract.) Property will be located and sold to requesting parties at sale price obtained from the Forest Service plus price of survey and cost of mineral claims located on said property. I am in agreement with requests and will work with adjacent landowners to satisfy their requests.

Upon receiving this document, Kinkead inserted a detailed description of the land he sought, signed it and forwarded it to the Forest Service. Jacobson signed the agreement and forwarded it to the Forest Service without any addition to the description of the land.

The Forest Service completed the sale of the land to Gulbransen in July 1997. Some months later, Gulbransen and Jacobson met to walk the land and to set the boundary, but were unable to agree on the land to be conveyed to Jacobson. This suit followed with Jacobson seeking specific performance against Gulbransen.

The trial court found Gulbransen was not a credible witness based on both the substance of his testimony and his demeanor. However, it found Jacobson was a very credible witness. With respect to the sale, the trial court determined it was in Jacobson's self-interest to maintain the status quo and that he withdrew his objections to the sale out of courtesy to Gulbransen and in reliance upon the agreement between the parties. Additionally, the court determined
Gulbransen refused to convey the land because the final size of the parcel was smaller than expected and thus, financing was less of an issue for him. In addition, land values had increased dramatically during the period between the initial negotiations and the time for conveyance.

Based upon the evidence and testimony, the trial court concluded there was an agreement between the parties to convey the south end of the parcel consisting of all but five acres retained by Gulbransens and other small parcels requested by other neighbors. The court decreed specific performance of this agreement. The original judgment also awarded attorney's fees as damages. The trial court subsequently vacated this judgment and entered an amended judgment denying the attorney's fees.

Gulbransens appeal the trial court's finding of an agreement for the conveyance of land and its decree of specific performance. By notice of review, Jacobson challenges the court's denial of attorney's fees.

**STANDARD OF REVIEW**

Our review begins with the findings of fact and a determination of whether the findings support the conclusions of law. Unless shown to be clearly erroneous, a trial court’s findings of fact will not be disturbed. Geraets v. Halter, 1999 SD 11, ¶12, 588 NW2d 231, 233. Conclusions of law are reviewed de novo. Id. at 234.

**DECISION**

**There was an enforceable agreement between the parties.**

The trial court's determination that there was an agreement between the parties was based on the evidence and testimony presented at trial. When, as here, the court's conclusions are so grounded, they will be reviewed with great deference. See e.g., Jeschke v. Wockenfuss, 534 NW2d 602, 604 (SD 1995) (credibility of witnesses and weight accorded their testimony is for the trial court and we accept that version of the evidence and any reasonable inferences favorable to the trial court's determination).

The trial court found Jacobson and the reasons given for his conduct were more credible than Gulbransen and the reasons supplied for his conduct. Because these findings are sufficiently based on the evidence and because the trial court is in the best position to judge the credibility of witnesses and to resolve disputes of fact, they will not be disturbed.

To be enforceable under South Dakota's statute of frauds, a contract for the sale of land or some memorandum of the agreement must be in writing.

The following contracts are not enforceable by action unless the contract or some memorandum thereof is in writing and subscribed by the party to be charged or his agent, as authorized in writing:

...  

(3) An agreement for sale of real estate or an interest therein, or lease of the same, for a period longer than one year. However, this does not abridge the power of any court to compel specific
performance of any agreement for sale of real estate in case of part performance thereof[.]

SDCL 53- 8-2. If the writing is a memorandum, it must describe the land, the price and the parties to the contract. Amdahl v. Lowe, 471 NW2d 770, 774-775 (SD 1991). It is not necessary that it provide a precise description of the land. Id. at 775. To be sufficient, the description must merely be clear enough for extrinsic evidence to precisely identify the land. Id. "A general description of the land which is the subject of the contract is sufficient, and parol evidence may be admitted to provide the more particular description." Id. There is no dispute that the memorandum confirming the agreement for the sale of property was signed by Gulbransen and Jacobson. This writing meets the requirement of the statute of frauds that there be written evidence that the parties reached an agreement.

Gulbransen argues that the description of land in the memorandum was indefinite or uncertain and that this resulted in an unenforceable agreement. The memorandum described the land to be conveyed to Jacobson as "the south end of the tract" and stated that, "I [Gulbransen] will convey areas sought by . . . Mr. Jacobson." The memorandum concluded with the statement that, "I am in agreement with their requests and will work with adjacent landowners to satisfy their requests." The trial court also allowed parol evidence of the parties' discussion to more precisely identify the parcel to be conveyed and all parties testified as to the land constituting that parcel. The trial court found Jacobson to be a very credible witness and found Gulbransen was not credible "based on the substance of his testimony as well as his demeanor while testifying."

This Court has stated that:

SDCL 53-8-2 requires that an agreement for the sale of real property be in writing, and subscribed by the party to be charged, before the agreement will be enforceable. The agreement itself need not be the writing relied upon, a memorandum evidencing the obligation is sufficient. SDCL 53-8-2. "The memorandum serves to furnish written evidence of the obligation to be enforced against the party who subscribes his name to the memorandum; that is, a memorandum is not required to make a contract but merely to evidence in writing that a contract has been entered into." The memorandum need not embody the exact terms of the contract; "it is sufficient that the substance of a contract for the purchase of real property is inferred from the writing[.]"

Wiggins v. Shewmake, 374 NW2d 111, 114 (SD 1985)(emphasis added) (citations omitted).

"A general description of the land which is the subject of the contract is sufficient, and parol evidence may be admitted to provide the more particular description." Amdahl, 471 NW2d at 775. Further, a property description giving the grantor or grantee the right to pick a certain acreage is not indefinite. See Holland v. Windsor, 461 P2d 47 (Wyo 1969); Delaney v. Shellabarger, 76 Nev 341, 353 P2d 903 (1960). Here, the trial court found that, based on the writing, the surrounding circumstances and the
testimony, the agreement of the parties was to allow Gulbransens to select five acres around their house and, except for small parcels sold to others, to convey the remaining acreage in the southern portion of the property to Jacobson. Moreover, the trial court found that the construction of the contract urged by Gulbransens, i.e. that the agreement was to convey only the southeast corner of the parcel to Jacobson, was inconsistent with the writing and conversation that took place when the parties reached their agreement. The language of the agreement specified that the south end would be sold to Jacobson. Gulbransen's construction of the agreement as covering only the southeast corner contradicted that language.

More to the point, the trial court concluded that construing the agreement to require the sale of the entire southern end of the parcel was the only construction that would make sense in light of Jacobson's conduct. When he originally heard of the planned sale of the parcel, Jacobson wrote to Paul Ruder, the Forest Service Ranger, objecting to the sale because he did not want the land sold or developed. It was to Jacobson's advantage to have the Forest Service own the land because, under Forest Service ownership: he had access to nearly inaccessible land that he owned; he had an alternate escape route through the land in case of fire; and, as the trial court noted, he had these advantages without the burdens of owning the land himself. Jacobson had it in his power to continue to object to and, thus, block the sale. Instead, he agreed to withdraw his objections in exchange for the southern end of the parcel excluding the five acres abutting Gulbransens' land.

Jacobson's actions enabling the Forest Service's sale of the land to Gulbransen to go forward make no sense absent the assumption that he would retain the benefits he sought to protect when he objected to the sale. The trial court found it was not credible that Jacobson would surrender these advantages for no more than the southeast corner of the parcel.

To form a contract, there must be a meeting of the minds or mutual assent on all essential terms. Read v. McKennan Hosp., 2000 SD 66, ¶ 23, 610 NW2d 782, 786. Whether the parties had such a meeting of the minds is a question of fact. See Lawrie v. Riss & Co., 248 F2d 256, 259 (8th Cir 1957)(whether or not there was a meeting of the minds was a question of fact for the trial court to determine). Whether there was mutual assent is determined by looking at the words and conduct of the parties. Read, 2000 SD 66 at ¶ 25, 610 NW2d at 786.

The trial court determined there was mutual assent to a contract between the parties for the sale of the parcel of land in this case. It made this determination based upon the memorandum, the surrounding circumstances and the parties' testimony. The contract between the parties allowed Gulbransens to select and retain five acres around their house and, except for small parcels sold to other neighbors, required them to convey the remaining acreage in the southern portion of the property to Jacobson. The trial court was correct in its finding of mutual assent to this contract and in determining that an enforceable agreement existed.

**Promissory estoppel also removes the agreement from the statute of frauds.**

The trial court further determined that the doctrine of promissory estoppel or detrimental reliance removed the parties' agreement from the statute of frauds. Jacobson, in reliance on the agreement that Gulbransen would convey the south end of the Forest Service parcel to him, allowed the sale to go through by withdrawing his objections and by so notifying the Forest Service. His conduct grew out of the agreement and was directly referable to it. The role of the statute of frauds is an evidentiary one. "[T]he purpose of the statute . . . is
to remove . . . uncertainty . . . by providing written evidence of an enforceable obligation." Sabhari v. Sapari, 1998 SD 35, n 9, 576 NW2d 886, 893. The statute of frauds will not, however, be used to work an injustice. See Matter of Estate of Gosmire, 331 NW2d 562 (SD 1983) (grantors, through partial performance of their obligation, removed oral contract to convey land from statute of frauds). Jacobson, in reliance upon his agreement with Gulbransens, withdrew his opposition to the sale of the land by the Forest Service and, thus forfeited the benefits he received from Forest Service ownership. Such detrimental reliance takes the agreement out of the statute of frauds. See Farmers Elevator Co. of Elk Point v. Lyle, 238 NW2d 290, 293 (SD 1976) (doctrine of promissory estoppel prevented party from asserting statute of frauds defense); Matter of Estate of Williams, 348 NW2d 471, 475 (SD 1984) (estoppel arises where conduct or acts induce a party to alter his position or to do what he otherwise would not have done to his prejudice). See also Scott v. Hyde, 440 NW2d 528, 531 (SD 1989) (this court has recognized the doctrine of promissory estoppel where a party has detrimentally relied on the promise of another).

The elements of promissory estoppel or detrimental reliance are, "[a] promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance[.]" Scott, 440 NW2d at 531 (quoting Valley Bank v. Dowdy, 337 NW2d 164, 165 (SD 1983)). Such a promise is binding "if injustice can be avoided only by enforcement of the promise." Id. In this case, the parties entered into an agreement that Gulbransens would retain the five acres next to their land, Kinkead and others would get the land next to their properties and Jacobson would get the remaining property in the southern end of the parcel. This agreement was reached so the land would be sold by the Forest Service to Gulbransen; i.e., the promise to convey was made to induce Jacobson to withdraw his objections to the sale.

As a direct result of the agreement, Jacobson did withdraw his objections and the sale of the parcel to Gulbransens occurred. This Court has held that, where there is such reasonable reliance upon a promise, the promisee is entitled to specific performance.

An oral promise to convey real property is enforceable by specific performance where the grantee has partially performed or has acted in reliance upon the promise of the grantor in such a manner that it would invoke a fraud or prejudice against the grantee not to grant specific performance thereon.

Gosmire, 331 NW2d at 567. The trial court correctly determined that Jacobson acted in reasonable reliance on Gulbransens's promise to convey the southern portion of the Forest Service parcel, thus taking the agreement out of the statute of frauds. The agreement was enforceable under the doctrine of promissory estoppel.

Specific performance is "[t]he presumed remedy for the breach of an agreement to transfer real property[.]" Wiggins, 374 NW2d at 115. The trial court was correct in decreeing specific performance.

An award of attorney’s fees is inappropriate in this case.

The trial court ultimately declined to award attorney's fees to Jacobson, the prevailing party. An award of attorney's fees is not the norm. The party requesting such fees has the burden to show, by a preponderance of the evidence, the basis for such an award. See State Ex Rel.
Steffen v. Peterson, 2000 SD 39, ¶ 30, 607 N.W.2d 262, 271 (party filing motion for award of attorney's fees has burden of proving entitlement to award by preponderance of evidence). Furthermore, this Court has said that, "[a]s a rule, attorney fees may only be awarded by contract or when explicitly authorized by statute." Matter of Estate of O'Keefe, 1998 SD 92, ¶¶17, 583 NW2d 138, 142 (citations omitted). Jacobson argues he is entitled to attorney's fees because the lawsuit was induced by Gulbransen's fraud. He urges this Court to carve out an exception to the rule barring such awards. We decline to create such an exception.

Affirmed.

AMUNDSON, KONENKAMP and GILBERTSON, Justices, concur. SABERS, Justice, concurs in part and dissents in part.

ANDERSON, Lee D., Circuit Judge, for MILLER, Chief Justice, disqualified. SABERS, Justice (concurring in part and dissenting in part).

I concur in all respects except for the denial of damages to Jacobson resulting from Gulbransen’s fraud in the form of attorney’s fees. These attorney’s fees were directly caused by Gulbransen’s fraud and his refusal to deed the property to Jacobson, and constitute Jacobson’s damages. The majority opinion incorrectly characterizes Jacobson’s attempt to recover these damages under these facts as an attempt to carve out a new exception to the rule barring such recovery. Therefore, I dissent as to issue 3.

As a general rule, attorney’s fees may only be awarded by contract or when explicitly authorized by statute. O’Connor v. King, 479 NW2d 162, 166 (SD 1991). Yet, —in singular circumstances we have allowed attorney[’s] fees as damages, though not expressly authorized by statute. Schuldies v. Millar, 1996 SD 120, ¶37, 555 NW2d 90, 100. In so doing, we have recognized a limited exception allowing the recovery of attorney’s fees as damages for a party attempting to recovery property wrongfully converted by another. Colton v. Decker, 540 NW2d 172, 178 (SD 1995). See generally, Dan B. Dobbs, Law of Remedies § 3.10(3) (2d Ed 1993) (outlining exceptions to the general rule); John Leusdorf, Recovering Attorney’s Fees as Damages, 38 Rutgers L Rev. 439 (1986). The facts in this case clearly support the application of this rationale.

A party is entitled to recover attorney’s fees as damages for a party’s wrongful conversion of property. These —pursuit fees include attorney’s fees, as those fees properly flow from the act of recovering property wrongfully dispossessed. See Rollins v. Leibold, 512 P2d 937, 945 (Alaska 1973); Motors Ins. Corp v. Singleton, 677 SW2d 309, 315 (Ky Ct App 1984); Fulks v. Fulks, 121 NE2d 180,182 (Ohio 1953); Schuldies, 1996 SD 120 at ¶ 48, 555 NW2d at 100 (Sabers J., concurring).

In this case, SDCL 20-10-1 provides in part that —o[ne who willfully deceives another . . . is liable for any damage which he thereby suffers. (emphasis added). The legislature did not exempt Gulbransen from any damage except attorney’s fees, and we should not either. In Colton, 540 NW2d at 178, we stated that attorney’s fees were reasonable expenses incident to recovering clear title to an impounded vehicle. The statutory authority we relied upon in Colton provided that the party should recover for their reasonable expenses resulting from the failure to provide clear title. See SDCL 57A-2-715. That statutory authority does not specifically grant attorney’s fees but utilizes language similar to SDCL 20-10-1 by providing recovery for
expenses reasonably incurred, any other reasonable expenses, and resulting from any loss or any breach. This rationale is equally applicable to granting attorney’s fees as damages under SDCL 20-10-1 on these facts.

Jacobson was forced to incur substantial legal expenses as a result of Gulbransen’s attempt to keep the property he previously agreed to convey. This is particularly egregious conduct as Gulbransen was permitted to make this purchase only because he fraudulently obtained Jacobson’s approval to the proposed sale. After Jacobson gave his approval, Gulbransen refused to sell the identified property pursuant to the agreement. Gulbransen’s fraudulent conduct forced Jacobson to bring an action for specific performance forcing Gulbransen to convey the property as agreed. The majority opinion recognizes Jacobson was legally entitled to the property. Gulbransen’s actions are tantamount to the conversion of the property identified for sale to Jacobson. Jacobson’s damages were suffered in pursuit of the property he was entitled to purchase, and attorney’s fees as damages are recoverable in this circumstance.

I would reverse and remand for a determination of the reasonable amount of attorney’s fees as damages reasonably incurred or expended to recover the property.
Learning Plan 5

Uniform Commercial Code

A. The Uniform Commercial Code
Because the United States consists of 50 states, it is possible to have fifty different sets of state laws governing contracts and other areas of law. If state contract laws were radically different, it would be difficult for individuals and companies to conduct business across state lines. To promote uniformity among state laws, the National Conference of Commissioners on Uniform State Laws drafts model laws that may be adopted by state legislatures. The Commission consists of lawyers, judges, and law professors from each state, the District of Columbia, the Commonwealth of Puerto Rico and the U.S. Virgin Islands.\textsuperscript{11}

Explore the Uniform Law Commission website.

The Uniform Commercial Code (UCC) is one of the best known laws drafted by the Uniform Law Commission. The UCC promotes consistency among state laws affecting commercial transactions through a uniform set of rules that codify several well-established contract rules, while modifying other rigid common law rules to facilitate commerce.

The UCC is divided into nine articles governing contracts related to the following commercial transactions. Please click on each article to review the provisions of each area of the UCC:

- **Article 1.** General Provisions
- **Article 2.** Sales
- **Article 2A.** Leases
- **Article 3.** Negotiable Instruments
- **Article 4.** Bank Deposit
- **Article 4A.** Funds Transfers
- **Article 5.** Letters of Credit
- **Article 6.** Bulk Transfers and [Revised] - Bulk Sales
- **Article 7.** Warehouse Receipts, Bills of Lading and Other Documents of Title
- **Article 8.** Investment Securities
- **Article 9.** Secured Transactions

The UCC has been adopted – with various modifications – in every state, as well as the District of Columbia, the Commonwealth of Puerto Rico, Guam and the U.S. Virgin Islands. Although
it is called the Uniform Commercial Code, the UCC has not been uniformly adopted and variations exist in the final versions adopted by the states.

Review the list of states that have enacted provisions of the Uniform Commercial Code (Hint: Scroll down the page).

When considering an issue related to a contract, one of the first questions should be:

*Is this contract governed by the Uniform Commercial Code as adopted by the applicable state?*

In other words, does this contract fall into one of UCC articles listed above? If so, then the state UCC provisions should be carefully reviewed, because they will be the governing law, rather than "traditional" contract theories.

### B. Article 2: Sales

2. Express & Implied Warranties
3. Defenses

Article 2 of the Uniform Commercial Code contains several provisions governing contracts involving the sale of "goods." As such it applies whenever people buy or sell goods. It applies to the sales of goods between private parties as well as to the sales of goods by businesses. As defined by Article 2, "goods" are generally tangible, moveable objects. Article 2 does not govern contracts relating to real estate and intangible items, which are not included in the definition of "goods." A "sale" is a generally defined as transfer of title to goods for a price.

To determine whether the UCC applies, you simply ask whether the contract is for the sale of goods. If the answer is "yes" then you apply the laws of the UCC. If the answer is "no" then apply the common law of contracts previously discussed.

1. **General Provisions**

Article 2 modifies a state’s general contract law and "relaxes" the rigid requirements of "traditional" contract law if the contract involves the sale of goods. Among its provisions, Article 2 sets rules regarding:

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<td>Contract formation</td>
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<td>Contracts between merchants and consumers</td>
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<td>Contracts between merchants</td>
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<td>Good faith</td>
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<td>Risk of loss</td>
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Read the article, Sales, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.
2. Express & Implied Warranties

Article 2 includes provisions regarding certain *express warranties* and *implied warranties* made by the manufacturers and sellers of goods. In the wide array of products offered on the market today, it is inevitable that some products may be defective. It is also inevitable that people may be injured and property damaged as a result of such defects.

Manufacturers and vendors of defective products that injure a person or a person's property may be liable for injuries and damage under the tort theories of negligence and strict liability, discussed in Learning Plan 2. They may also be liable to the injured person under contract and UCC theories of:

- Express Warranty
- Implied Warranty of Merchantability
- Implied Warranty of Fitness for a Particular Purpose

This combination of theories to determine liability on the basis of tort, contract, and the Uniform Commercial Code is often referred to as *product liability*.

a. Express Warranty

When a person purchases a product, the product may come with a warranty that is expressly made by the manufacturer. Often, such warranties are printed on the package or in the literature that accompanies the product. For example, many products contain express warranties such as, "Guaranteed against defects in materials or workmanship for a period of 90 days from purchase." If a product is defective, the purchaser and, in most cases, the user of a product, may recover damages if injured by the defect.

b. Implied Warranty of Merchantability (UCC 2-314)

Article 2 of the Uniform Commercial Code imposes an implied warranty of merchantability on products sold by a merchant who deals in the type of products sold. The warranty is not an express warranty, because it is not expressed either verbally or in writing. Rather, it is implied. Under the UCC, when a person purchases a product from a merchant, the person can expect that the product is "merchantable" under UCC 2-314, which provides that goods are of a quality equal to that which is generally acceptable among those who deal in such goods and are generally fit for the ordinary purpose for which such goods are used.

c. Implied Warranty of Fitness for a Particular Purpose (UCC 2-315)

Article 2 of the Uniform Commercial Code also imposes an implied warranty of fitness for a particular purpose when the seller knows, or has reason to know, that the buyer of the goods intends to use such goods for a particular purpose and the buyer relies upon the seller’s skill in select or provide such goods.

Read the following articles:

[Legal Basis for Liability in Product Cases](http://www.findlaw.com), presented by FindLaw.

[Products Liability Law](http://www.findlaw.com), presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.
3. Defenses
A manufacturer or merchant that sells a product may avoid liability if circumstances exist for a valid defense, including:

- Assumption of Risk
- Contributory Negligence
- Comparative Negligence

a. Assumption of Risk (UCC 2-715)
If a person voluntarily uses a product after becoming aware of its defect, the person is considered to have assumed the risk. In such case, the person is generally barred from recovering for an injury caused by such defect.

b. Contributory Negligence
Generally, if a person is negligent when using a product after discovering the defect in a state that allows contributory negligence as a defense, the person may not recover damages on the basis that the injury was caused by the contributory negligence of the injured person.

c. Comparative Negligence
Generally, if a person is negligent when using a product after discovering the defect in a state that allows comparative negligence as a defense, the amount of damages that a person may recover for the injury that was caused the defect will be reduced by the amount of the comparative negligence of the injured person.

Briefly review Article 2 of the Uniform Commercial Code, as drafted by National Conference of Commissioners on Uniform State Laws, available at the Cornell University Law School Legal Information Institute.

C. Article 3: Negotiable Instruments
Today, relatively few business transactions in the United States use actual cash as a method of payment. Instead, negotiable instruments and the increasing use of electronic transactions are the common method of payment for goods and services.

Article 3 of the Uniform Commercial Code, as adopted by individual states, governs the creation and negotiation of negotiable instruments. UCC Section 3-104 defines a negotiable instrument as follows:

. . . "negotiable instrument" means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it:

1. is payable to bearer or to order at the time it is issued or first comes into possession of a holder;
2. is payable on demand or at a definite time; and
3. does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money . . .
When an instrument is negotiable, its transfer from one person to another is governed by Article 3. There are four types of negotiable instruments identified by the UCC.

- Drafts
- Checks
- Notes
- Certificate of Deposit (CDs)

Negotiable instruments are generally divided into two categories: Those instruments that contain an order to pay, and those instruments that contain a promise to pay.

- Order to pay instruments include drafts and checks
- Promise to pay instruments include notes and certificates of deposit

A draft is an unconditional written order or instrument in which the drawer orders the drawee to pay money to a payee. A check is a draft drawn upon a bank. UCC Section 3-104(f) defines a check as "(i) a draft, other than a documentary draft, payable on demand and drawn on a bank or (ii) a cashier's check or teller's check. An instrument may be a check even though it is described on its face by another term, such as "money order." Take a look at your checkbook and note that each check states: "Pay to the order of"

A promissory note is a promise by the maker (the promising party) to pay a fixed amount of money to the payee named in the note, either at a specified time in the future, or upon demand by the maker. A certificate of deposit is a promissory note by a bank or other financial institution in which the institution acknowledges that it has received money from the depositor and that it will repay the money, plus interest, as a set time in the future.

In order for an instrument to be negotiable, it must be in writing; signed by the maker/drawer of the instrument, or the maker's agent; be an unconditional promise or order to pay; state a fixed amount of money; be payable on demand or at a definite time; and be payable to the order or to bearer. If it is a check itneed not meet the final requirement.

Read the article, Negotiable Instruments, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

**WRITING**

In order to meet the “in writing” requirement, the instrument must be on a material that lends itself to permanence. For example, a promise written in sand on a beach would not qualify as permanent and therefore would not be a negotiable instrument.

In addition, the writing must have portability. If the instrument is not movable it cannot be freely transferable. An example would be a promise placed on a billboard. If John place a billboard along the side of the interstate that said “I promise to pay $500 to the order of Helen” it would meet the requirements of a negotiable instrument but it would not be portable. A billboard cannot be easily transferred in the ordinary course of business therefore it would not be a negotiable instrument.
**Signed**
For an instrument to be negotiable, it must be signed by the maker if it is a note or certificate of deposit or the drawer if it is a draft or check. A signature may consist of a name, word, or mark used with the intention to authenticate a writing. It may be something such as initials or a thumbprint and may be made manually or with a stamp or computer.

**Unconditional Promise or Order to Pay**
The terms of the promise or order must be unconditional. In other words they must not be conditioned on an occurrence or nonoccurrence of some other event or agreement.

**Promise or Order**
In order for an instrument to be negotiable, it must contain an express order or promise to pay. A traditional I.O.U. that is commonly done (I.O.U. $50 signed by Fred) implies a promise to pay but is not a negotiable instrument because it does not expressly contain a promise to repay.

**Fixed Amount of Money**
Negotiable instruments must state a fixed amount of money to be paid at the time the instrument is presented for payment. This can include a specific amount of interest that included in the instrument either with a specific percentage or with indication as to how it is to be calculated. In addition, in order to be a negotiable instrument, it must be payable entirely in money. A note that contains payment in services or other goods is not negotiable.

**Payable on Demand or Definite Time**
Instruments that are payable on demand generally contain wording such as payable on presentment or payable at sight or say nothing about when payment is due. An instrument is payable at a definite time if it states a specific date or a definite period of time or a date.

**Payable to Order or Bearer**
An instrument is an order instrument if it is payable to the order of an identified person (Pay to the order of Joseph). This allows that person to transfer the instrument to whomever he/she wishes. A bearer instrument is an instrument that does not designate a specific payee. The maker or drawer of a bearer instrument agrees to pay anyone who presents the instrument for payment.

Negotiable instruments may be "negotiated" or transferred to other parties. Under UCC Section 3-302, a person who receives a check or promissory note is considered a **holder in due course** and entitled to payment of the instrument according to its terms, if the holder received the instrument for value, in good faith, and without notice that it is **overdue or has been dishonored**, or that there is an uncured default with respect to payment of another instrument issued as part of the same series, without notice that the instrument contains an unauthorized signature or has been altered, without notice of any claim to the instrument, and without notice that any party has a defense or claim in recoupment.

FALLSVIEW GLATT KOSHER CATERERS, INC. v. ROSENFIELD
7 Misc. 3d 557; 794 N.Y.S.2d 790 (2005)

Jack M. Battaglia, J.

For its complaint against Willie Rosenfeld, Fallsviw Glatt Kosher Caterers, Inc. alleges that it "operates a catering business . . . and specializes in organizing and operating programs at select hotels whereby [its] customers are provided with Glatt Kosher food service during Jewish holiday seasons"; that during the 2004 Passover holiday, it "operated a program whereby [it] provided accommodations, food and entertainment for its customers at Kutcher's Country Club"; that Mr. Rosenfeld "requested accommodations for 15 members of his family . . . and full participation in the Program"; and that he agreed to pay Fallsviw $24,050 "for the Program"; that Fallsviw "made the necessary arrangements," but Mr. Rosenfeld and his family "failed to appear at the hotel without notification" to Fallsviw; and that Mr. Rosenfeld "breached the agreement by failing to remit . . . payment in the amount of $24,050.00." (See complaint PP 1- 7.)

In lieu of an answer, Mr. Rosenfeld has moved for dismissal of the complaint pursuant to CPLR 3211 (a) (5), contending that the action is barred by section 2-201 of the Uniform Commercial Code. The motion is supported by the affidavit of Stuart A. Blander, Esq., who, in addition to serving as counsel to Mr. Rosenfeld, appears to have a direct connection to the alleged transaction that is the subject of the suit. In opposition, Fallsview relies on the affidavit of Mark Weiss, one of its officers, and on documents attached to the affidavit. The affidavits are appropriately considered on the motion (see CPLR 3211 [c]); as for the documents, Mr. Rosenfeld does not question their admissibility, although he does dispute the significance of some of them.

Section 2-201 provides that, subject to stated exceptions, "a contract for the sale of goods for the price of $500 or more is not enforceable . . . unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought." (UCC 2-201 [1].) Although Mr. Blander's affidavit states that Mr. Rosenfeld "vigorously denies the existence of any agreement--oral or written" (see affidavit in support of motion to dismiss complaint P 3), there is no affidavit from Mr. Rosenfeld to that effect or denying that there is "some writing sufficient to indicate that a contract for sale has been made" that was signed by or for him (see UCC 2-201 [1]).

Addressing General Obligations Law § 5-703, the First Department has held:
"The Statute of Frauds being an affirmative defense, it was incumbent on the movant to show that there was in fact no written contract or 'note or memorandum thereof'... This fact should have been shown by affidavits from persons having knowledge of the facts. The only supporting affidavits are those from [movant's] attorneys. We have frequently said that affidavits from attorneys without knowledge of the facts are without probative value..."

(Subgar Realty Corp. v Gothic Lbr. & Millwork, 80 A.D.2d 774, 774, 436 N.Y.S.2d 740 [1st Dept 1981]; see also Scarvalone v Kowalewicz, 26 A.D.2d 885, 886, 274 N.Y.S.2d 217 [3d Dept 1966]).

Moreover, because Willie Rosenfeld has not submitted his sworn denial of the agreement sued upon, the court would be inclined to hold the motion "in abeyance until the plaintiff has had an opportunity to depose the defendant." (See Boylan v Morrow Co., 63 N.Y.2d 616, 619, 468 N.E.2d 681, 479 N.Y.S.2d 499 [1984]; see also CPLR 3211 [d]; UCC 2-201 [3] [b]; DF Activities Corp. v Brown, 851 F.2d 920, 922 [7th Cir 1988].)

Fallsvieh, however, does not raise these points, nor does it contend that factual issues preclude a determination as to the enforceability of the alleged agreement in light of section 2-201 (1) of the Uniform Commercial Code. (See Levin v Hoffman Fuel Co., 94 A.D.2d 640, 641, 462 N.Y.S.2d 195 [1st Dept 1983], affd 60 N.Y.2d 665, 455 N.E.2d 663, 468 N.Y.S.2d 104 [1983]; Morton Bldgs. v Edson, 250 A.D.2d 657, 657-658, 671 N.Y.S.2d 690 [2d Dept 1998]; Marbelite Co., Inc. v National Sign & Signal Co., Inc., 2 Fed Appx 118, 120 [2d Cir 2001].) Fallsvieh does not contend that any of the statutory exceptions apply, or that there is any other basis to enforce the agreement if section 2-201 (1) applies. (See Country-Wide Leasing Corp. v Subaru of Am., 133 A.D.2d 735, 736, 520 N.Y.S.2d 24 [2d Dept 1987].)

Although Fallsvieh has not explicitly conceded that no qualifying writing exists, both parties have focused their legal and factual arguments on a single question—that is, whether the alleged agreement that is the basis for Fallsvieh's action is a "contract for the sale of goods for the price of $ 500 or more" within the meaning of section 2-201 (1). The parties having charted that course (see Vasinkevich v Elm Drugs, 208 A.D.2d 522, 523, 616 N.Y.S.2d 808 [2d Dept 1994]), supported by considerations of judicial economy, the court sees no compelling reason not to address the question.

Although the question to be addressed proceeds from the statutory language, "contract for the sale of goods" (see UCC 2-201 [1]), "[t]he sales-services dichotomy has been recognized and developed from the days of the law merchant." (See Milau Assoc. v North Ave. Dev. Corp., 42 N.Y.2d 482, 485, 368 N.E.2d 1247, 398 N.Y.S.2d 882 [1977].) Presented with a "hybrid sales- services contract" (see id.), that is, a contract that calls for the furnishing of both goods and services, the court must decide whether to apply the law applicable to a sale of goods, currently article 2 of the Uniform Commercial Code as adopted in this state, or to apply the law applicable to service contracts, the general law of contracts or some specialized portion thereof. The agreement alleged in the complaint (and limiting attention for the moment to the complaint alone) calls for the furnishing of "accommodations, food and entertainment" (complaint P 1) with "food" qualifying as "goods" (see UCC 2-105 [1]).

In Perlmutter v Beth David Hosp. (308 N.Y. 100, 123 N.E.2d 792 [1954]), a case decided under the pre-Code Sales Act, the Court of Appeals held that "when service predominates, and transfer
of personal property is but an incidental feature of the transaction, the transaction is not deemed a sale within the Sales Act" (id. at 104). "[I]t is the transaction, regarded in its entirety, which must determine its nature and character" (id. at 106). The Court "look[s] at the transaction for what it actually is" (id. at 107), seeking the "essence of [the] particular contract" (id. at 106), "the main object sought to be accomplished" (id.).

In Perlmutter, the Court ruled that the "transfusing of 'bad' blood, supplied by [a] hospital for a price as part of the customary services rendered by the hospital to its patients" (id. at 103) was not a "sale" of the blood for purposes of the Sales Act's implied warranties of fitness. In so doing, the Court distinguished its prior decision in Temple v Keeler (238 N.Y. 344, 144 N.E. 635 [1924]), relied upon by the plaintiff in the case before it, and relied upon by Mr. Rosenfeld here: "Not at all analogous to the case before us is our decision . . . holding that, 'where a customer enters a restaurant, receives, eats and pays for food, delivered to him on his order, the transaction is a purchase of goods.' . . . While it has been said that a restaurant owner does not sell food, but rather renders a service, the fact is that there is 'a sale of what is actually used' . . . [T]here can be no doubt that, when one goes into a restaurant, he does so in order to buy what the restaurant in truth has to sell, namely, food." (Perlmutter v Beth David Hosp., 308 N.Y. at 107, quoting Temple v Keeler, 238 N.Y. at 346, 347.)

The issue in Temple v Keeler was also the applicability of an implied warranty of fitness. In reaching the conclusion that there was "a sale of what [was] actually used" (id. at 347), the Court noted a prior "authoritative decision," construing a criminal statute, which "held that a hotel keeper who places before his guests at dinner, partridges, sells the birds, although the guests paid a total sum for [food] and lodging." (Id.)

In reaching the result it did in Perlmutter, the Court was influenced by the consequence that "if the transaction [was] deemed a sale, liability would attach irrespective of negligence or other fault." (See Perlmutter v Beth David Hosp., 308 N.Y. at 107.) In a subsequent decision, the Court of Appeals noted that its analysis in Perlmutter was "supported by policy considerations peculiar to the impure blood cases," and stated that "the court's sensitivity to . . . policy considerations . . . should suggest the need to assess all hybrid transactions along the sales-services continuum both legally and pragmatically." (Milau Assoc. v North Ave. Dev. Corp., 42 N.Y.2d at 486.)

The holding in Temple v Keller that the furnishing of food in a restaurant or hotel is accompanied by an implied warranty of fitness is now part of the Uniform Commercial Code. Section 2-314 (1) states that "a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind," unless the warranty is excluded or modified as permitted in a separate provision, and that "[u]nder this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale." (UCC 2-314 [1][emphasis added].) Thus the Uniform Commercial Code resolved the conflict among the states on the question addressed by Temple v Keeler, adopting the answer given by our Court of Appeals. (See Sofman v Denham Food Serv., Inc., 37 N.J. 304, 309-312, 181 A.2d 168, 171-173 [1962] [Schettino, J., concurring].)

The question becomes then whether the holding in Temple v Keeler necessarily constitutes a determination that every agreement that includes the furnishing of food is a "contract for the
sale of goods" as that term is used in article 2's statute of frauds, section 2-201. Decisions subsequent to Temple v Keeler that apply its holding do not answer the question, since they, too, involve the issue of warranty. (See Frier v Laube's Old Spain, 265 App Div 402, 39 N.Y.S.2d 794 [4th Dept 1943]; Conklin v Hotel Waldorf Astoria Corp., 5 Misc. 2d 496, 161 N.Y.S.2d 205 [NY City Ct, NY County 1957]; Grossman v Hotel Astor, 166 Misc. 80, 1 N.Y.S.2d 307 [Manhattan Mun Ct 1937].)

In the most recent of these decisions, England v Sanford (167 A.D.2d 147, 561 N.Y.S.2d 228 [1st Dept 1990], affd 78 N.Y.2d 928, 578 N.E.2d 437, 573 N.Y.S.2d 639 [1991]), the First Department held that a plaintiff who sustained personal injuries as a result of eating unwholesome food at a party catered by the defendant could amend her complaint to allege breach of warranty. The defendant caterer argued that the "theory was [not] viable since the service aspects of defendant's contract with the host of the party predominated over its sales aspect, i.e., that defendant was engaged mainly to organize a party and that his provision of food was merely incidental to this main purpose." (Id. at 148.) Taking a "pragmatic point of view," the Court rejected the argument, concluding that "[i]f policy considerations dictate that a restaurant owner should be liable without fault for serving unwholesome food . . . so too should a caterer." (Id.) The Court cited section 2-314 (1), but did not explain why the issue was not resolved by that provision's explicit language. It may be that the party was catered at the home of the host or some location not maintained by the caterer, so that the statutory language ("consumed either on the premises or elsewhere") was considered not strictly applicable.

A too simple answer to our question is that the statute itself explicitly limits the stated rule about serving food to "this section" (see UCC 2-314 [1]), and the rule, therefore, does not apply to any other section, such as the statute of frauds. Despite the limitation, section 2-314 and section 2-201 explicitly apply to "contracts for the sale of goods," and usually statutory language is given the same meaning throughout. (See Riley v County of Broome, 95 N.Y.2d 455, 466, 742 N.E.2d 98, 719 N.Y.S.2d 623 [2000]; Mangam v City of Brooklyn, 98 N.Y. 585, 591-592 [1885].) Moreover, "the predominant purpose test . . . presupposes that if Article 2 is to apply or not to apply, it should apply (or not apply) to the whole transaction." (1 White and Summers, Uniform Commercial Code § 1-1, at 4-5 [Practitioner's 4th ed 1995]; see also Perlmuter v Beth David Hosp., 308 N.Y. at 104.)

New York courts, nonetheless, have seemed willing to focus on the nature of the dispute between the parties, and to distinguish prior authority, when the issue is not the existence of an implied warranty, which implicates fundamental standards of liability, but more collateral matters, such as the statute of limitations (see Perlmuter v Don's Ford, 96 Misc.2d 719, 721, 409 N.Y.S.2d 628 [Utica City Ct 1978]) or the statute of frauds (see Pecker Iron Works v Sturdy Concrete Co., 96 Misc. 2d 998, 1000-1001, 410 N.Y.S.2d 251 [Civ Ct, Queens County 1978]; see also Sands v Feldman, 243 A.D.2d 294, 662 N.Y.S.2d 510 [1st Dept 1997]).

Moreover, "[t]he rules of construction of statutes are never absolute and must always be considered in the light of the surrounding circumstances; the same word may be used in varying senses depending on the intent of the Legislature." (Colon v Aetna Cas. & Sur. Co., 64 A.D.2d 498, 503, 410 N.Y.S.2d 634 [2d Dept 1978], affd 48 N.Y.2d 570, 399 N.E.2d 938, 423 N.Y.S.2d 908 [1980]; see also Becker v McCrea, 119 App Div 56, 58, 103 N.Y.S. 963,
39 Civ. Proc. R. 150 [2d Dept 1907], revd on other grounds 193 N.Y. 423, 86 N.E. 463 [1908].) A statutory warranty is a different thing than a statute of frauds--the one establishes a standard of liability against which contractual performance is to be assessed, the other determines whether the contract is provable. Each is affected by a different purpose, and operates guided by different policies. Indeed, not all statutes of frauds are alike. "New York has enacted several . . . each with its own particular language and requirements," and they "may require more or less particularity in the writings depending upon the Legislature's perception regarding the risks of false claims inherent in the contractual setting." (Fox Co. v Kaufman Org., 74 N.Y.2d 136, 140-141, 542 N.E.2d 1082, 544 N.Y.S.2d 565 [1989].)

"Predominant purpose" analysis may, and does, appropriately reflect the kinds of rules to be applied as its result and attendant policy considerations. This is not to say that the contract is "divisible" (see Perlmutt v Beth David Hosp., 308 N.Y. at 104), but that the Uniform Commercial Code may be. For present purposes, this means that the existence--or not--of an implied warranty accompanying the food served at Kutcher's Country Club during Fallsview's Passover "program" will not determine whether a contract for participation in the "program" is provable.

Mr. Rosenfeld contends that the "predominant purpose" and "main objective" of the agreement alleged by Fallsview was the "service of Kosher food," while the hotel accommodations and entertainment were merely "incidental or collateral" services. (See affidavit in support of motion to dismiss complaint P 6.) Mr. Rosenfeld points to the apparent nature of Fallsview's primary business, catering, as revealed by its corporate name "Fallsview Glatt Kosher Caterers, Inc.," and the business name "The Glatt Boys." (Id.) The programs organized and operated by Fallsview are described by reference to "Glatt Kosher food service." (Id.) These things are found on the face of Fallsview's complaint. (See complaint P 1.)

Defendant's contention that the "predominant purpose" of the alleged agreement is the sale of food is said to be "compelled by the very nature of the Passover holiday" (see affidavit in support of motion to dismiss P 7). "The essential religious obligation during this eight day period--and the principal reason why people attend events similar to the Program sponsored by plaintiff--is in order to facilitate their fulfillment of the requirement to eat only food which is prepared in strict accordance with the mandate of Jewish law for Passover, i.e., food which is 'Kosher for Passover.' It is the desire to obtain these 'goods'--and not the urge for 'entertainment' or 'accommodations'--that motivates customers to subscribe to such 'Programs.' " (Id.)

According to Mr. Rosenfeld--or rather Mr. Blander, his attorney--the "very essence of the 'experience' is the presentation and enjoyment of abundant, frequent and high quality Kosher for Passover cuisine to the guests." (Reply affidavit in further support of motion to dismiss complaint P 8.) Although, generally, an attorney's sworn or affirmed statement as to the facts is "without evidentiary value" because the attorney has no personal knowledge of them (see Zuckerman v City of New York, 49 N.Y.2d 557, 563, 404 N.E.2d 718, 427 N.Y.S.2d 595 [1980]), Mr. Blander appears to be in a position to speak to the matters alleged in his affidavit. The affidavit of Mark Weiss, Fallsview's officer, is accompanied by "confirmation" documents, two of which purport to confirm reservations of "Stu, Blander" and "Adam, Eitan, Akiva Blander." (See affidavit of Mark Weiss in opposition to defendant's motion to dismiss, exhibit B.)
Mr. Weiss does not, in any event, dispute Mr. Blander's assertions concerning the "motivation" of defendant and his guests. Much of what Mr. Blander says is reflected in statutory provisions dealing with the representation of food and other articles as "Kosher" (see Agriculture and Markets Law § 201-a et seq.; General Business Law § 349-a), and would be matters of rather common knowledge, in Brooklyn at least.

Mr. Weiss's affidavit is also accompanied by 10 sheets, designated "Kutcher's Country Club Daily Activities" for Sunday, April 4, through Tuesday, April 13, 2004. The activities possible include tennis, racquetball, swimming, Swedish massage, "make over face lift show," "trivia time," aerobics, bingo, ice skating, dancing, "showtime," "power walk," arts and crafts, day camp, ping-pong, Yiddish theater, board games, horse racing, horseback riding, wine tasting, and indoor bocci--and that is only through Wednesday. Throughout the period, there are traditional and Orthodox religious services, lectures on religious and other subjects (presumably with a religious or cultural perspective), and a series of activities that are clearly designed to be of interest to families of observant Jews during a highly significant period in their calendar. (See affidavit of Mark Weiss in opposition to defendant's motion to dismiss, exhibit A.) These activities are provided, together with accommodations and food, for an "all inclusive" price that is apparently determined by the size and location of the room(s) and the numbers and ages of the persons in each party. (See id., exhibit B.)

The court accepts Mr. Blander's characterization of Fallsview's Passover program as an "experience," and has no basis to dispute that, for him, its "very essence" is the "presentation and enjoyment of abundant, frequent and high quality Kosher for Passover cuisine." But a review of the characteristics of the "program," which is the subject matter of the alleged agreement, leads the court to conclude that the "essence" of the family and communal "experience" is defined primarily by "services" and not by "goods."

The consequences of that conclusion, i.e., that the alleged agreement is not subject to the article 2 statute of frauds, is supported by the structure, terms, purpose and context of the statutory provision. As with all statutes of fraud, the purpose of section 2-201 is "to avoid fraud by preventing the enforcement of contracts that were never in fact made." (Fox Co. v Kaufman Org., 74 N.Y.2d at 140.) Section 2-201's attempt to serve that purpose was designed in a transactional context permeated with "forms"--quotations, orders, order acknowledgments or confirmations, invoices, bills of lading, and delivery receipts among them. That context is reflected in the statute's "merchant's exception" (see UCC 2-201 [2]), as well as article 2's parol evidence rule (see UCC 2-202), its provision on firm offers (see UCC 2-205), and, perhaps most significantly, its attempt to address the "battle of the forms" (see UCC 2-207).

The intended scope of section 2-201 is also indicated by its provision that "[a] writing is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this paragraph beyond the quantity of goods shown in the writing." (See UCC 2-201 [1].) The importance of a quantity term is also evident in the "partial performance" exception, which is limited to "goods for which payment has been made and accepted or which have been received and accepted." (See UCC 2-201 [3] [c].) For the Uniform Commercial Code, quantity is even more important than price. (See UCC 2-305 [1].) A contract of the type involved here would rarely, if ever, specify the "quantity" of the "goods" to be provided. Nor would, for example, a contract for a week's stay at a weight loss spa, or a zen vegetarian
retreat, or a cruise of the islands. Even the most formal of signed contracts would be at risk of unenforceability under section 2-201 for lack of a term specifying the "quantity" of food that would be consumed.

And what of the limitation in section 2-201 to the "sale of goods for the price of $ 500 or more"? (UCC 2-201 [1].) Does the alleged agreement here specify such a price? In an all-or-nothing, nondivisible regime, such as the "predominant purpose" test suggests, how is the "price" determined? Is it the total contract price, or just the price of the "goods," and, if the latter, how is an "all inclusive" cost treated? Here, the complaint alleges a total due of $24,050 for 15 persons, and Mr. Weiss provides 10 "confirmation" documents ranging in amounts from $1,750 to $3,750. Are all or any covered, or only some?

Plaintiff argues that "[d]efendant's proposition that a hotel reservation is a sale of goods would render all reservations made via telephone or the internet unenforceable and would leave hotels in a precarious economic position." (Affirmation of Sheldon Eisenberger in opposition to defendant's motion to dismiss the complaint P 10.) That may or may not be true, but the argument does highlight the importance of ensuring that a statute of frauds structured and outfitted by the Legislature for a particular transactional context not be casually applied to a very different commercial segment and model. The structure and terms of section 2-201 tell us that it was not intended to cover the agreement alleged in this complaint. Defendant's motion to dismiss is denied.
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Learning Plan 6

Business Entities

A. Sole Proprietorship
   1. Definition
   2. Business Name
   3. Advantages/Disadvantages
   4. Summary

1. Definition

A sole proprietorship is the most basic and simplest form of business in the United States. A sole proprietorship simply consists of one person owning and operating a business. The sole proprietor is entitled to receive all profits generated by the business. The sole proprietor is also responsible for the payment of all debts incurred by the business. Although the business is owned by one person, the sole proprietor does not necessarily perform all the functions of the business. The sole proprietor may hire and employ several employees to assist in the day-to-day operation of the business.

Sole proprietorships make up about two-thirds of all business in the United States. Many types of businesses are commonly operated as sole proprietorships, including appliance repair shops, carpet cleaning services, and landscaping businesses. Many professional businesses are also operated as sole proprietorships, including dental offices with a single dentist, and law offices with a sole practicing attorney. These sole proprietors often hire support staff to assist them in their businesses.

2. Business Name

A sole proprietor may operate the business under his/her surname (last name/family name). For example, Joe Jablonksi may operate his automobile repair business as Jablonksi Auto Repair. In such a case, the business owner is not generally required to register the business name. However, if a sole proprietor wishes to operate the business under a different or assumed name, then the sole proprietor may be required to file a fictitious name statement to inform the public of the name and address of the business owner. For example, Joe Jablonski may wish to operate his automobile repair shop as Ace Auto Repair. Joe may be required by state law to file a fictitious name certificate with a county or state office similar to the following example:
The undersigned states that the undersigned will engage in and conduct business for profit in the State of South Dakota under a fictitious business name and provides the following information in accordance with SDCL 37-11-1:

1. The name of the business is Ace Auto Repair.

2. The main office of the business will be maintained at 1000 Speedway Avenue, Motor City, South Dakota 54321.

3. The following person(s) are all the person(s) who will be interested in the business:

<table>
<thead>
<tr>
<th>Name</th>
<th>Post Office Address</th>
<th>Residence Address</th>
</tr>
</thead>
<tbody>
<tr>
<td>Joseph Jablonski</td>
<td>PO Box 123</td>
<td>1000 Winner Circle</td>
</tr>
<tr>
<td></td>
<td>Motor City, SD 54399</td>
<td>Motor City, SD 54390</td>
</tr>
</tbody>
</table>

The undersigned, being first duly sworn, deposes and states that the undersigned has read the foregoing information and that the same is true to the best of the undersigned's knowledge, information, and belief.

____________________________
Joseph Jablonski

STATE OF SOUTH DAKOTA    )
COUNTY OF RAPID    ) SS.

Subscribed and sworn to before me this ___ day of ____________, 20___

(SEAL)                       Notary Public, South Dakota

My commission expires: ________________

Filing a fictitious name statement may also protect the sole proprietor by preventing other persons from using the same business name. A fictitious name statement is often effective for only a set period of time and will expire, unless it is renewed by the sole proprietor.

3. Advantages/Disadvantages

Operating a business as a sole proprietor provides many advantages to the business owner. It also has significant disadvantages. Whether the advantages outweigh the disadvantages depends upon the business and the goals of the sole proprietor. Advantages of operating a business as a sole proprietorship include
simplicity of creation and operation, owner authority, and receipt of all profits. The sole proprietor is free to make any decision he/she wishes regarding the business from whom to hire, hours of operation and what kind of business to open. The major disadvantage of a sole proprietorship is that the owner bears the burden of all liabilities incurred by the business. Additional disadvantages include, a limited ability to raise funds and limited duration of the sole proprietorship, as the business ends upon the death of the proprietor.

*Simplicity* is an obvious advantage of operating a business as a sole proprietorship. It is very easy to commence business with few legal formalities. If a person uses his/her surname in the business name and does not hire employees, the sole proprietor simply starts business operations. If a person uses a different business name, then it may be necessary to file a fictitious name statement, as discussed in the previous section. If a person hires employees, then the sole proprietor must also obtain a federal tax identification number, also known as an Employer Identification Number (EIN) from the U.S. Internal Revenue Service. Instructions for obtaining an Employer ID number are available at the [Internal Revenue Service](https://www.irs.gov) website. It may also be necessary to obtain a tax identification number from the state.

⚠ Of course, a sole proprietor must comply with any laws regulating that type of business. For example, if a person wishes to operate a restaurant that serves liquor, the sole proprietor must obtain a liquor license from the appropriate government authority.

Operating a business as a sole proprietorship also provides the sole proprietor with total *authority* over the business. The sole proprietor need not obtain the consent of other persons when making decisions regarding the business. Note, however, that a sole proprietor may delegate day-to-day management decisions to an employee, but the sole proprietor retains the ultimate authority over the business.

As owner of the business, the sole proprietor has the right to receive the *profits* generated by the business. The sole proprietor is required to file the appropriate Federal and state income tax returns and pay the required taxes on such profits.

The major disadvantage of operating a business as a sole proprietorship is the *unlimited liability* of the sole proprietor for the debts of the business. If the business does not generate sufficient income to timely pay the debts incurred from the operation of the business, the creditors of the business may seek payment from the personal assets of the sole proprietor, such as the sole proprietor's home, vehicles, investments, *etc*.

Operating a business as a sole proprietorship often results in a *limited ability to raise funds* to operate or expand the business. Funding for the business is obtained through profits, the sole proprietor's other assets, and loans. These funding sources are often limited. A sole proprietorship cannot raise capital by selling shares of stock to investors as can a corporation. Finally, a sole proprietorship has a *limited duration*. When the sole proprietor dies, the sole
proprietorship terminates. Upon the death of sole proprietor, the assets of the business are distributed according to the Last Will and Testament of the sole proprietor, or according to state law, if the sole proprietor died without a will. Another person, who inherits or purchases the assets, could continue the business, but the business operation would be conducted under another form of business - either another, separate sole proprietorship, or under another form of business organization that will be discussed in the following sections.

4. Summary
A sole proprietorship is a simple form of business that consists of one person owning and operating a business. The sole proprietor may hire employees to assist in the operation of the business. If a sole proprietor operates the business under a different or assumed name, then the sole proprietor may be required to file a fictitious name statement. Advantages of operating a business as a sole proprietorship include simplicity of creation and operation, owner authority, and receipt of profits. Disadvantages include owner liability, limited ability to raise funds, and limited duration of the sole proprietorship.

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<th>B. General Partnership</th>
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<tr>
<td>1. Definition</td>
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<tr>
<td>2. Creation</td>
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<td>3. Partners</td>
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<td>4. Dissolution</td>
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<tr>
<td>5. Summary</td>
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1. Definition
Many businesses in the United States operate as a general partnership. A general partnership is commonly defined as an "association of two or more persons to carry on a business for profit." General partners contribute their labor and resources to the partnership and, in return, share in the profits (and losses) of the business. Generally, a partnership can own property and incur debts in the partnership name.

The creation of a general partnership, the rights and duties of partners, and the dissolution of the partnership are governed by state law. Although differences exist, state laws governing partnerships are relatively uniform, because many states have adopted the Revised Uniform Partnership Act, a model law containing uniform provisions for general partnerships.

Read the article, Partnership Law, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

2. Creation
A general partnership may be created by agreement of the parties. A partnership may also be created by the conduct of the parties, even if they did not consciously consider that they were creating a partnership.
**Agreement**

Many partnerships are created by agreement of the parties. The agreement may be either written or oral. Although many states do not specifically require that partnership agreements be written, such agreements may, nonetheless, be required to be written under other state statutes. For example, if the partnership will own real property (land and fixtures), the partnership agreement must be written, because state statutes commonly require that contracts involving interests in real property must be written to be enforceable. Similarly, if the partnership business will last longer than one year must also be written, because many states require that contracts that cannot be completed within one year be written to be enforceable under the state's statute of frauds.

Even if a written partnership agreement is not required, it is often preferable to have a well-written agreement, sometimes called *Articles of Partnership*, rather than a mere oral agreement, because a written agreement can facilitate the operation of the business and avoid misunderstandings by clearly defining the rights and duties of the partners. The following is an example of a simple partnership agreement:

**PARTNERSHIP AGREEMENT**

This PARTNERSHIP AGREEMENT is made on __________, 20___ between ________ of _______________ and _______________ of _______________.

1. **Name and Business.** The parties hereby form a partnership under the name of ____________________________ to conduct a _________________.

   The principal office of the business shall be in ________________________________.

2. **Term.** The partnership shall begin on ________________, 20___, and shall continue until terminated as herein provided.

3. **Capital.** The capital of the partnership shall be contributed in cash by the partners as follows: A separate capital account shall be maintained for each partner. Neither partner shall withdraw any part of his capital account. Upon the demand of either partner, the capital accounts of the partners shall be maintained at all times in the proportions in which the partners share in the profits and losses of the partnership.

4. **Profit and Loss.** The net profits of the partnership shall be divided equally between the partners and the net losses shall be borne equally by them. A separate income account shall be maintained for each partner. Partnership profits and losses shall be charged or credited to the separate income account of each partner. If a partner has no credit balance in his income account, losses shall be charged to his capital account.

5. **Salaries and Drawings.** Neither partner shall receive any salary for services rendered to the partnership. Each partner may, from time to time, withdraw the credit balance in his income account.

6. **Interest.** No interest shall be paid on the initial contributions to the capital of the partnership or on any subsequent contributions of capital.

7. **Management Duties and Restrictions.** The partners shall have equal rights in the management of the partnership business, and each partner shall devote his entire time to the
conduct of the business. Without the consent of the other partner neither partner shall on behalf of the partnership borrow or lend money, or make, deliver, or accept any commercial paper, or execute any mortgage, security agreement, bond, or lease, or purchase or contract to purchase, or sell or contract to sell any property for or of the partnership other than the type of property bought and sold in the regular course of its business.

8. Banking. All funds of the partnership shall be deposited in its name in such checking account or accounts as shall be designated by the partners. All withdrawals therefrom are to be made upon checks signed by either partner.

9. Books. The partnership books shall be maintained at the principal office of the partnership, and each partner shall at all times have access thereto. The books shall be kept on a fiscal year basis, commencing __________ and ending __________, and shall be closed and balanced at the end of each fiscal year. An audit shall be made as of the closing date.

10. Voluntary Termination. The partnership may be dissolved at any time by agreement of the partners, in which event the partners shall proceed with reasonable promptness to liquidate the business of the partnership. The partnership name shall be sold with the other assets of the business. The assets of the partnership business shall be used and distributed in the following order: (a) to pay or provide for the payment of all partnership liabilities and liquidating expenses and obligations; (b) to equalize the income accounts of the partners; (c) to discharge the balance of the income accounts of the partners; (d) to equalize the capital accounts of the partners; and (e) to discharge the balance of the capital accounts of the partners.

11. Death. Upon the death of either partner, the surviving partner shall have the right either to purchase the interest of the decedent in the partnership or to terminate and liquidate the partnership business. If the surviving partner elects to purchase the decedent's interest, he shall serve notice in writing of such election, within three months after the death of the decedent, upon the executor or administrator of the decedent, or, if at the time of such election no legal representative has been appointed, upon any one of the known legal heirs of the decedent at the last-known address of such heir. (a) If the surviving partner elects to purchase the interest of the decedent in the partnership, the purchase price shall be equal to the decedent's capital account as at the date of his death plus the decedent's income account as at the end of the prior fiscal year, increased by his share of partnership profits or decreased by his share of partnership losses for the period from the beginning of the fiscal year in which his death occurred until the end of the calendar month in which his death occurred, and decreased by withdrawals charged to his income account during such period. No allowance shall be made for goodwill, trade name, patents, or other intangible assets, except as those assets have been reflected on the partnership books immediately prior to the decedent's death; but the survivor shall nevertheless be entitled to use the trade name of the partnership. (b) Except as herein otherwise stated, the procedure as to liquidation and distribution of the assets of the partnership business shall be the same as stated in paragraph 10 with reference to voluntary termination.

12. Arbitration. Any controversy or claim arising out of or relating to this Agreement, or the breach hereof, shall be settled by arbitration in accordance with the rules, then obtaining, of the American Arbitration Association, and judgment upon the award rendered may be entered in any court having jurisdiction thereof. In witness whereof the parties have signed this Agreement.

Executed on the date(s) stated in the acknowledgments.
STATE OF __________________________) SS.
COUNTY OF __________________________)

On this _____day of __________________, 20___, before me the undersigned notary public, personally appeared __________________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.

(SEAL)
Notary Public

My commission expires: __________________________

STATE OF __________________________) SS.
COUNTY OF __________________________)

On this _____day of __________________, 20___, before me the undersigned notary public, personally appeared __________________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.

(SEAL)
Notary Public

My commission expires: __________________________

Sometimes, parties do not plan on operating an ongoing business, but instead simply intend to associate for the purpose of completing a single venture. In such cases, the parties may enter into a joint venture agreement, such as the example below, rather than a partnership agreement.

Read the article, Joint Ventures, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.
JOINT VENTURE AGREEMENT

, of , and , of , agree to create a joint venture under the following terms and conditions.

1. Name & Address. The name of the joint venture shall be , with offices located at , or at such other location as the parties may agree.

2. Purpose. The purpose of the joint venture is to , and to engage in such other lawful business that may be necessary or incidental to the operation of such business.

3. Contributions. Each party shall make equal financial contributions and approximately equal contributions of time and skill to the operation of the joint venture business.

4. Title to Property. Legal title to real and personal property acquired by the joint venture shall be held in equal shares in the names of .

5. Division of Profits/Losses. Net profits earned by the joint venture shall be divided equally between the parties. Any losses incurred by the joint venture shall also be shared equally between the parties. Distribution of net profits and contributions to losses shall be made as the parties may agree.

6. Records and Accounting. shall maintain, or cause to be maintained, a complete set of records, statements, and accounts of the operation of the joint venture business, which shall be open at all times to .

7. Assignment/Transfer. Neither party shall assign or transfer his rights or duties in the joint venture, without the express written consent of the other party. Any transfer or assignment made without such consent shall not relieve the transferor or assignor of his duties or obligations under this agreement.

8. Arbitration. If a dispute should arise between the parties that cannot be amicably resolved by agreement, such dispute shall be submitted to binding arbitration in accordance with applicable law, with the costs and expenses of such arbitration shared equally by the parties.

9. Death/Incapacity. The death or incapacity of either party shall cause the joint venture to be dissolved at the completion of that current fiscal year. The annual net profits and proceeds from the sale of assets shall be divided equally between the surviving partner and the legal representative or guardian of the deceased or incapacitated party.

10. Term. This agreement shall continue in effect for a period of years from the date it is signed by both parties, or a different period as may be agreed in writing between the parties.

11. Termination of Agreement. On termination of this agreement for any cause, the joint venture shall be wound up and dissolved in accordance with applicable law.

Executed on the date(s) stated in the acknowledgments.
STATE OF ____________________________ ) SS.
COUNTY OF ____________________________

On this _____ day of __________________, 20___, before me the undersigned notary public, personally appeared ________________________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.

(SEAL) ________________________________
Notary Public

My commission expires: __________________________

STATE OF ____________________________ ) SS.
COUNTY OF ____________________________

On this _____ day of __________________, 20___, before me the undersigned notary public, personally appeared ________________________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.

(SEAL) ________________________________
Notary Public

My commission expires: __________________________

■ Conduct
It is possible to create a general partnership without either an oral or written partnership agreement. Under the laws of many states, persons may create a general partnership by their conduct, even if they didn't consider that they were forming a partnership. If persons own a business together, including jointly owning property used in the business, sharing management, receiving profits, and contributing to the payment of business debts, they may have unintentionally created a general partnership. In such event, the persons will be considered general partners and will have the duties and obligations of partners, without a partnership agreement.

3. Partners
In many states, a general partner may be either a natural person, with capacity under the law (i.e., a legally competent adult) or a corporation. A corporation is not considered a natural
person, but is nonetheless a "person" under the law for numerous purposes, including becoming a general partner.

- **Rights of General Partners**
  General partners have several rights in the partnership, including the following:
  - Right to participate in the management of the partnership business, unless otherwise agreed
  - Right to share in profits and surpluses of the partnership
  - Right to use partnership property for partnership purposes
  - Right to access business information and business records
  - Right to an accounting of business transactions
  - Right to the return of the partner's capital contribution, after the payment of partnership creditors

  Generally, a partner is not entitled to compensation for his/her efforts in operating the business, unless the parties agree otherwise. The partner is considered to be compensated through his/her receipt of profits from the business.

- **Duties of General Partners**
  General partners also have several duties that they owe to the partnership and other partners, including:
  - A duty to use good faith and loyalty in all dealings with the partnership and other partners
  - A duty to use care when managing the partnership business
  - A duty to pay partnership debts, if partnership assets are not sufficient

4. **Dissolution**
A general partnership does not last forever. It may be dissolved, or terminated, in various ways.

- **By the partners**
  - The partnership terminates according to the terms of the partnership agreement
  - The partners agree to terminate the partnership
  - A partner withdraws from a partnership that does not have a specific termination date in the partnership agreement (called a "partnership at will")
  - A partner is appropriately expelled from the partnership under the terms of the partnership agreement

- **By Operation of Law**
  - A partner dies
  - A partner declares bankruptcy
  - The partnership business becomes illegal
When a general partnership is dissolved, the business operated by the partnership does not necessarily end. It may continue under a new form of business, whether it be a new general partnership or another type of form of business, if the parties can come to an agreement for continuing the business.

If the partnership business is not continued, then the partnership goes through a process called *winding up*. During winding up, business transactions are completed, accounts are collected, and inventory is taken. Unless otherwise agreed, remaining assets are liquidated and distributed in the following order:

1. To creditors of the partnership, other than partners
2. To partners for the amount of any money lent to the partnership
3. To partners for the amount of their capital contributions to the partnership
4. To partners in the amount of any remaining surplus

Review the statutes of your state, or a state of your choice governing the creation, operation, and termination of a general partnership.

Statutes are available online at the Cornell University Law School Legal Information Institute.

Ask your instructor for assistance, if you have difficulty locating the statutes.

5. Summary
A general partnership is commonly defined as an "association of two or more persons to carry on a business for profit." A partnership may be created by agreement or by conduct of the parties. General partners contribute their labor and resources to the partnership and, in return, share in the profits (and losses) of the business. General partners have several rights and duties to the partnership and other partners. The creation of a general partnership, the rights and duties of partners, and the dissolution of the partnership are governed by state law.

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**C. Limited Partnership**

<table>
<thead>
<tr>
<th>1. Definition</th>
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<td>5. Dissolution</td>
<td>6. Summary</td>
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</tbody>
</table>

1. **Definition**

A *limited partnership* is a form of business organization authorized by state statutes. Such statutes generally authorize the formation of a limited partnership with one or one or more general partners and one or more limited partners.

- **General partners** manage the partnership business and are personally liable for the debts of the business.
■ *Limited partners* invest in the partnership business, but have no management authority. Limited partners are liable only for the amount that they have invested in the partnership, or the amount that they have agreed to invest in the business.

2. Creation
A limited partnership may only be created by complying with the statutes that govern the formation of such partnerships. States generally require that persons forming a limited partnership file a *certificate of limited partnership*, or a similar statement, with a designated government office, often the Secretary of State. Only the names of the general partners are listed in the certificate. The names of the limited partners do not appear of public record.

**CERTIFICATE OF LIMITED PARTNERSHIP**

The undersigned, being all the general partners of the herein named limited partnership, submit this certificate for the purpose of forming a limited partnership under the Uniform Limited Partnership Law Act of the State of ___________

1. The name of the limited partnership is (must include "L.P.", "LP", or "Limited Partnership" in the name) is: ___________

2. The name and address of the limited partnership's initial registered agent in this state is:

<table>
<thead>
<tr>
<th>Name</th>
<th>Street Address</th>
<th>City/State/Zip</th>
</tr>
</thead>
</table>

3. The name and mailing address of each general partner is:

<table>
<thead>
<tr>
<th>Name</th>
<th>Street Address</th>
<th>City/State/Zip</th>
</tr>
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4. The events, if any, on which the limited partnership is to dissolve or the number of years the limited partnership is to continue, which may be any number or perpetual: ___________

The undersigned swear and affirm, under penalty of perjury, that the foregoing statements are true and correct to the best of the undersigned's knowledge, information, and belief.

Date: ___________  

Signature

Date: ___________  

Signature

Date: ___________  

Signature
Many states make these forms available online.

If persons attempting to form a limited partnership do not substantially comply with statutes governing the formation of such partnerships, then the limited partners may become personally liable for the debts of the partnership business

3. Limited Partnership Agreement
The relationship between the general and limited partners is governed by a written limited partnership agreement, sometimes called articles of limited partnership.

LIMITED PARTNERSHIP AGREEMENT

This partnership agreement is made and entered into as of __________, 20__, by and between ____________________________

__________________________________________

ARTICLE 1
DEFINITIONS

When used in this Agreement, the following terms shall have the meanings set forth below except as otherwise specifically modified:

1.1. "Agreement" means this Agreement, as it may be amended from time to time.

1.2. "Limited Partnership" means The __________ Company (a __________ limited partnership), its successors and assigns.

1.3. "Limited Partnership Agreement" means the Limited Partnership Agreement of the Limited Partnership, as it may be amended from time to time.

1.4. "Managing Partner" means the Person so designated pursuant to Section 5.2.

1.5. "Partners" means the parties to this Agreement and their successors as partners of the Partnership. "Partner" means any one of the Partners.

1.6. "Partnership" means the partnership created by this Agreement and any successor partnership which continues the business of this partnership and which is a reformation or reconstitution of a partnership governed by this Agreement.

1.7. "Person" means an individual, partnership, joint venture, estate, association, corporation, trust company, trust or other legal entity.

1.8. "Unit" means a unit of interest in the Limited Partnership as defined in the Limited Partnership Agreement.

ARTICLE 2
GENERAL PROVISIONS

2.1. Formation of the Partnership. The Partners agree to form and by execution of this
Agreement enter into a general partnership.

2.2. Name of the Partnership. The name of the Partnership is "_________Limited Partnership." This name may be changed at any time or from time to time by the Managing Partner.

2.3. Business and Purpose of the Partnership. The business and purpose of the Partnership shall be to act as one of the general partners of the Limited Partnership, and to engage in any other related act or activity.

2.4. Principal Place of Business. The principal place of business of the Partnership shall be at ____________, ____________, ____________, but the Partners may establish any other place or places of business for the Partnership (within or without the State of ____________) as they may deem necessary or appropriate.

2.5. Term. The term of the Partnership shall commence upon the date first written above and shall continue until the Limited Partnership or any successor of the Limited Partnership which continues the business of the Limited Partnership is dissolved, liquidated and wound up and any trust or other entity formed for the purpose of liquidating or winding up the Limited Partnership is liquidated and wound up, unless sooner terminated pursuant to the provisions of this Agreement or in accordance with law.

ARTICLE 3.
POWERS AND DUTIES

3.1. General. The Partners shall devote such time and attention to the business of the Partnership as may be reasonably necessary to carry out their duties, but, subject to any policies adopted by the Limited Partnership, ___________ Management Corporation or this Partnership, neither this Agreement nor the relationship of the parties as partners shall remove or impair the right of any Partner and its partners, directors, officers and shareholders, directly or indirectly (including, without limitation, through any entity in which the Partner or any such Person holds an ownership interest) to be otherwise employed by an entity or entities other than the Partnership on a part-time or full-time basis.

3.2. Management Power. The Managing Partner shall have management and control of the ordinary course of the day-to-day business of the Partnership for the purposes stated in this Agreement and shall serve as tax matters partner for the Partnership. All matters outside the ordinary course of the day-to-day business of the Partnership shall be decided by a majority vote of the Partners.

3.3. Similar Activities of Partners. Subject to any policies adopted by the Limited Partnership, ___________ Management Corporation or this Partnership, the Partners and their partners, directors, officers and shareholders may, directly or indirectly (including, without limitation, through any entity in which the Partner or any such Person holds an ownership interest), engage in any and all aspects of any business in which the Partnership or the Limited Partnership is engaged or plans to engage, or any other businesses and activities, whether competitive with the Partnership or otherwise, for their own account and for the account of others, without having or incurring any obligation to offer any interest in such properties, businesses or activities to the Partnership, the Limited Partnership or any Partner, and nothing in this Agreement shall be deemed to prevent or any such Person from conducting other businesses and activities. Neither the Partnership, the Limited Partnership nor any of the Partners shall have any rights by virtue of this Agreement in any independent business ventures of that Person. However, all records kept and maintained by the Partners for the Partnership pursuant to this Agreement shall be maintained separately from those for other operations of those Persons.
3.4. Indemnification of Partners. The Partners and their partners, shareholders, directors and officers shall each be indemnified and held harmless to the same extent as the general partners of the Limited Partnership and their partners, shareholders, directors and officers are indemnified under the Limited Partnership Agreement.

3.5. Other Matters Concerning Partners.

(A). Each of the Partners may rely and shall be protected in acting or refraining from acting upon any resolution, certificate, statement, instrument, opinion, report, notice, request, consent, order, bond, debenture, or other paper or document believed by it to be genuine and to have been signed or presented by the proper party or parties.

(B). Each of the Partners may execute any of the powers or perform any duties listed here either directly or by or through agents, including, without limitation, partners, directors, officers, shareholders and affiliates of a Partner, the Partnership or the Limited Partnership. Each of the Partners may consult with counsel, accountants, appraisers, management consultants, investment bankers, and other consultants and advisers selected by it (who may serve as such for the Partnership or any affiliated Person) and any opinion of that Person as to matters which the Partner believes to be within its professional or expert competence shall be full and complete authorization and protection in respect to any action taken or suffered or omitted by the Partner in good faith and in accordance with that opinion. None of the Partners shall be responsible for the misconduct, negligence, acts or omissions of any such Person or of any agent or employee of the Partnership, a Partner or the Limited Partnership, nor shall any Partner assume any obligations in that connection other than the obligation to use due care in the selection of those Persons.

(C). Any and all fees, commissions, compensation and other consideration received by a Partner or a partner, director, officer or shareholder of a Partner shall be the exclusive property of the recipient, in which the Partnership shall have no right or claim, and the participation by any Person in any agreement permitted here shall not constitute a breach by that Person of any duty that it may owe the Partnership or the Partners under this Agreement or by operation of law.

ARTICLE 4. CAPITAL, ALLOCATIONS AND DISTRIBUTIONS

4.1. Capital Contributions. Each Partner shall contribute _______ Units or the right to receive _______ Units or the right to receive _______ Units to the capital of the Partnership. This contribution shall be made no later than _______ days after the record date for determining shareholders of The _______ Company, a _______ corporation, entitled to receive Units pursuant to the Plan of Reorganization and Liquidation of that corporation or the date the Person becomes a General Partner, whichever is later. No Partner shall be required to make additional contributions to the capital of this Partnership.

4.2. Compensation. The Partnership shall pay all of the costs and expenses incurred by the Partners in connection with the business and affairs of the Partnership, and the Partners shall receive any other compensation as is approved by the board of directors of _______

Management Corporation.

4.3. Allocations and Distributions. All revenue, income, expenditures, losses, credits and distributions of cash or property shall be allocated or distributed to the Partners in proportion to the number of Units contributed by them for the period or day to which the allocation or distribution pertains.

4.4. Capital Account. A capital account shall be established for each Partner. All allocations of revenue and income shall be credited, and distributions and all allocations of expenditures, losses
and credits, shall be debited to the respective capital accounts of the Partners. 4.5. No Interest or Withdrawals. No Partner shall be entitled to interest on any capital contribution, and no Partner shall have the right to withdraw or demand the return of any or all of its capital contribution, except as specifically provided in this Agreement.

4.6. Creditor’s Interest in the Partnership. No creditor who makes a loan to the Partnership shall have or acquire at any time as a result of making the loan, any direct or indirect interest in the profits, capital or property of the Partnership other than as a creditor.

4.7. Nature of Interests. All property owned by the Partnership, whether real or personal, tangible or intangible, shall be deemed to be owned by the Partnership as an entity, and none of the Partners shall have any direct ownership of that property.

ARTICLE 5.
ADMISSION AND WITHDRAWAL

5.1. Assignment or Transfer. No Partner shall sell, assign, transfer, mortgage, hypothecate, or encumber its interest in the Partnership, except with the written consent of ________ Management Corporation or its successor.

5.2. Partners; Managing Partner. The Persons serving as Partners of this Partnership shall be (1) ________ Management Corporation or any successor to ________ Management Corporation or any successor to ________ Management Corporation which serves as managing general partner of the Limited Partnership pursuant to the Limited Partnership Agreement, (2) the chief executive officer of ________ Management Corporation or its successor and (3) another officer or director of ________ Management Corporation or its successor designated by the board of directors of ________ Management Corporation or its successor. The individual who serves as a Partner by virtue of his or her position as chief executive officer or ________ Management Corporation or its successor shall be the Managing Partner. If the chief executive officer of ________ Management Corporation or its successor ceases to serve in that capacity, he or she shall cease at the same time to serve as a Partner and as Managing Partner and his or her successor as chief executive officer shall be admitted as a Partner of this Partnership and shall serve as Managing Partner of the Partnership. If the individual serving as a Partner pursuant to (3) above ceases to be an officer or director of ________ Management Corporation or its successor or the board of directors or its successor appoints another officer or director of ________ Management Corporation or its successor to serve as a Partner in his or her stead, he or she shall cease at the same time to serve as a Partner, and his or her successor shall be appointed by the board of directors of ________ Management Corporation or its successor from among its officers and directors. The successor shall be admitted as a Partner of this Partnership immediately upon his or her appointment by that board and his or her acceptance of that appointment. If ________ Management Corporation or its successor ceases to serve as a Partner, the individual Partners shall continue to serve as Partners notwithstanding anything in this Section 5.2 to the contrary until other Persons become Partners pursuant to Section 5.3.

5.3. Other Partners. If ________ Management Corporation ceases to serve as a general partner of the Limited Partnership, then it shall cease at the same time to serve as a Partner and its successor as a general partner of the Partnership and two Persons designated by the successor shall each be admitted as a Partner of this Partnership. Any other Persons serving as Partners of the Partnership when ________ Management Corporation ceases to serve as a general partner of the Limited Partnership shall cease to serve as a Partner at the time when the successor to ________ Management Corporation is admitted as a general partner of the Limited Partnership.
5.4. Other Admission of a Partner. Any Person admitted as a Partner other than pursuant to Sections 5.2 or 5.3 shall become a Partner only with the approval of all Partners.

5.5. Consent of Spouse. Within 20 days after any individual becomes a Partner or the Partner marries, the Partner shall have the Partner's spouse execute a consent substantially in the form attached as Exhibit _____________.

5.6. Return of Capital. On ceasing to serve as a Partner, a former Partner shall be entitled to a return of the same number of Units (as adjusted for any Unit split, stock dividend, recapitalization or other similar change affecting the number of Units held by the Partnership) it contributed to the Partnership plus a return of any other capital contributed to the Partnership.

5.7. Capital Contribution of a New Partner. On the admission of any Person to serve as a Partner, the Person shall contribute Units to the capital of the Partnership as provided in Article 4.

5.8. Withdrawal. ______________ Management Corporation may not withdraw as a Partner unless it no longer serves as a general partner of the Limited Partnership, this Partnership no longer serves as a general partner of the Limited Partnership or this Partnership is dissolved and its business is not continued. Any individual serving as a Partner may not withdraw except upon appointment of his or her successor by ______________ Management Corporation or its successor. Except as provided in this Article 5, no Partner may withdraw from the Partnership.

5.9. Additional Partners. The Partners agree and consent in advance that on the election or appointment of a new Partner to the Partnership, the new Partner shall, on agreeing in writing to be bound by the terms and provisions of this Agreement, and on agreeing to contribute to the capital of the Partnership of the number of Units pursuant to Section 4.1, become a party to this Agreement. If other Persons become parties to this Agreement, this Agreement will continue to be binding on every Partner without the reexecution of, or amendment to this Agreement.

ARTICLE 6.
BOOKS AND RECORDS

6.1. Fiscal Year and Method of Accounting. The fiscal year of the Partnership shall be as selected by the Managing Partner, and the books of the Partnership shall be kept on any basis determined by the Partners.

6.2. Books of Account. Complete and accurate accounts of all transactions of the Partnership shall be kept in proper books, and each Partner shall enter, or cause to be entered therein, a full and accurate account of all its transactions on behalf of the Partnership.

6.3. Inspection of Books. The books of account and other records of the Partnership shall, at all times, be kept in the principal place of business of the Partnership, and each of the Partners shall, at all times, have access to, and may inspect and copy, any of them.

6.4. Tax Returns. The Managing Partner shall arrange for the preparation and timely filing of all necessary tax returns for the Partnership.

ARTICLE 7.
TERMINATION, DISSOLUTION AND LIQUIDATION

7.1. Termination. The Partnership shall terminate on the occurrence of any event of dissolution as defined in Section 7.2.

7.2. Dissolution. The Partnership shall be dissolved by the occurrence of any event which
under applicable law causes the dissolution of a general partnership notwithstanding an agreement to the contrary, or of any of the following events:

(a) The distribution of substantially all Partnership property;

(b) The written election of all Partners to dissolve and wind up the affairs of the Partnership which specifies the date such election shall be effective;

(c) The Partnership ceases to serve as a general partner of the Limited Partnership;

(d) The expiration of the term of the Partnership; or

(e) An event which makes it unlawful to conduct the business of the Partnership.

7.3. Liquidation. On the dissolution of the Partnership, no further business shall be conducted, except for taking any action as shall be necessary for the winding up of the affairs of the Partnership and the distribution of its assets to the Partners. Partnership properties may be sold, if a price deemed reasonable by the Partners may be obtained, and the proceeds as well as all other cash and properties of the Partnership shall be distributed as follows:

First, all of the Partnership's debts and liabilities to Persons other than a Partner, but excluding secured creditors whose obligations will be assumed or otherwise transferred on the liquidation of Partnership assets, shall be paid and discharged.

Second, all of the Partnership's debts and liabilities to Partners shall be paid and discharged.

Third, subject to the maintenance of a reserve for contingent liabilities as agreed by the Partners, the Partners shall receive either in cash or in kind, the amounts allocated to their respective capital accounts in accordance with this Agreement.

7.4. Distribution to Partners. On liquidation pursuant to Section 7.3, any Units or other securities held by the Partnership shall be partitioned and the Partners shall cause appropriate certificates or evidences of ownership to be issued in the names of the Partners according to their respective interests.

7.5. No Recourse. The Partners shall look solely to the assets of the Partnership for the payment of any income allocated to the Partners and the return of any capital contributed to the Partnership and if the assets of the Partnership remaining after payment or discharge of the debts and liabilities of the Partnership are insufficient to pay all or any part of those amounts, they shall have no recourse against any Partner, or any director, officer, shareholder, employee or agent of a Partner, the Limited Partnership or a partner of the Limited Partnership for that purpose.

ARTICLE 8.
MISCELLANEOUS

8.1. Notices. All notices or other communications required or permitted to be given pursuant to this Agreement shall be in writing and shall be considered as properly given or made if personally delivered or if mailed by United States first class mail, postage prepaid and addressed to the Partner’s address for notices as it appears on the records of the Partnership. Any Partner may change the address for notices, by giving notice of the change to the Partnership. Commencing on the tenth (10th) day after giving notice, the newly designated address shall be the Partner’s address for the purpose of all notices or other communications required or permitted to be given pursuant to this Agreement. Any notice or other communication shall be deemed to have been given as of the date on which it is personally
delivered or, if mailed, the date on which it is deposited in the United States mails.

8.2. Amendment. This Agreement may be amended at any time and from time to time with the approval of Management Corporation or its successor and at least one other Partner. All amendments shall be in writing and shall be signed by the Partners approving the amendment.

8.3. Choice of Law. This Agreement and all rights and liabilities of the parties hereto with reference to the Partnership shall be subject to and governed by the laws of the State of as applied to agreements solely among residents to be entered into and performed entirely within .

8.4. Article and Section Headings. The headings in this Agreement are inserted for convenience and identification only and are in no way intended to describe, interpret, define or limit the scope, extent or intent of this Agreement or any of its provisions.

8.5. Execution of Counterparts. This Agreement may be executed in any number of counterparts with the same effect as if all parties had all signed the same document. All counterparts shall be construed together and shall constitute one agreement. Each party shall become bound by the Agreement immediately upon affixing his or her signature to it, independently of the signature of any other party.

8.6. Remedies Cumulative. The remedies of the parties under this Agreement are cumulative and shall not exclude any other remedies to which any Person may be lawfully entitled.

8.7. Waiver. No failure by any party to insist on the strict performance of any covenant, duty, agreement, or condition of this Agreement or to exercise any right or remedy consequent upon a breach shall constitute a waiver of any breach or any other covenant, duty, agreement, or condition.

8.8. Assignability. Subject to the restrictions on transferability, each of the covenants, terms, provisions and agreements contained in this Agreement shall be binding upon and inure to the benefit of the successors and assigns of the respective parties.

8.9. Gender and Number. Whenever the context requires, the gender of all words used shall include the masculine, feminine and neuter, the singular of all words shall include the singular and plural, and the plural of all words shall include the singular and plural.

8.10. Severability. If any provision of this Agreement, or its application, shall, for any reason and to any extent, be invalid or unenforceable, the remainder of this Agreement and the application of the provision to other Persons or circumstances shall not be affected but rather shall be enforced to the maximum extent permissible under applicable law.

In witness, the undersigned have executed this Agreement as of the day and year first written above
4. Duties and Obligations of Partners
General partners are responsible for managing the partnership business and must use good faith and reasonable business judgment in their management activities. General partners are personally liable for the debts of the business.

Limited partners may not participate in the management of the business. For this reason, limited partners are sometime referred to as "silent partners." Although a limited partner may not participate in the management of the partnership business, many states allow the limited partner to engage in certain activities that are not considered management, including:

1. Acting as an independent contractor, an agent, or an employee of the limited partnership
2. Consulting with a general partner and advise a general partner
3. Acting as a surety of the limited partnership
4. Agreeing or disagreeing to amend the limited partnership agreement
5. Voting on the following matters:
   a. Dissolution and winding up of the limited partnership
   b. Sale, exchange, lease, mortgage, pledge, or other transfer of all, or substantially all, of the assets of the limited partnership, other than in the ordinary course of business
   c. Incurring debt, other than in the ordinary course of business
   d. Change in the nature of business
   e. Removal of the general partner
Limited partners are only liable for the amount that they have invested in the partnership, or the amount that they have agreed to invest in the business under the limited partnership agreement. However, limited partner may become personally liable for the debts of the business if they participate in the day-to-day management of the business.

5. Dissolution
State statutes usually provide that a limited partnership is dissolved by:

- Occurrence of the expiration date or expiration event stated in the certificate of limited partnership
- Written consent of all the general and limited partners
- Death, incompetence, or withdrawal of a general partner, unless all the remaining general and limited partners agree to continue the business
- Order of a court, when the court determines that it is no longer practical to continue the partnership business according the limited partnership agreement

Generally, the death or incompetence of a limited partner does not dissolve a limited partnership.

When a partnership is dissolved, the business goes through a process of "winding up" in which the assets of the partnership are distributed in accordance with state statutes, which generally provide payment as follows:

1. Debts owed to outside creditors of the limited partnership in the order of priority established by state statutes
2. The share of profits owed to limited partners according to the limited partnership agreement
3. Capital contributions (investment in the partnership) made by limited partners
4. The share of profits owed to general partners according to the limited partnership agreement
5. Capital contributions made by general partners

Review the statutes of your state, or a state of your choice governing the creation, operation, and termination of a limited partnership. Statutes are available online at the Cornell University Law School Legal Information Institute.

Ask your instructor for assistance, if you have difficulty locating the statutes.

If available, review an online form certificate of limited partnership for your state, or a state of your choice, at state’s Secretary of State website. The South Dakota Secretary of State website is linked here as an example.

6. Summary
A limited partnership is a form of business organization authorized by state statutes. Such statutes generally authorize the formation of a limited partnership with one or one or more general partners and one or more limited partners. General partners manage the partnership business and are personally liable for the debts of the business. Limited partners invest in the partnership business, but have no management authority. Limited partners are liable only for the amount that they have invested in the partnership, or the amount that they have agreed to invest in the business.

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D. Business Corporation

1. Definition
2. Creation
3. Persons Involved in a Corporation
4. Organization Meeting
5. Bylaws
6. Shares of Stock
7. Doing Business outside the State
8. Dissolution
9. Advantages/Disadvantages
10. Summary

1. Definition
A business corporation is a legal entity created under state statutes. A business corporation exists and operates separately from its owners, the stockholders. As a legal entity (a legal person), a corporation can own property, incur debts, and can sue and be sued in court. Because a corporation exists under statutes, it is sometimes called a "creature of the state."
Read the article Corporations presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

2. Creation
A business corporation is created by filing articles of incorporation with the designated government office, often the Secretary of State. The contents of the articles of incorporation are prescribed by statute. Often, state law requires that articles of incorporation contain certain information, such as:

1. The name of the corporation
2. The number of shares the corporation is authorized to issue
3. The street address, or a statement that there is no street address, of the corporation's principal office
4. The street address, or a statement that there is no street address, of the corporation's initial registered office, and the name of its initial registered agent at that office
5. The name and address of each incorporator

State statutes often allow articles of incorporation to also include other optional information, including:

1. The names and addresses of the persons who are to serve as the initial directors
2. The purpose or purposes of the corporation
3. Provisions concerning the management of the business and regulation of the affairs of the corporation
4. Provisions that define, limit, and regulate the powers of the corporation, its board of directors, and shareholders
5. The par value for authorized shares or classes of shares
6. A provision eliminating or limiting the liability of a director to the corporation or its shareholders for money damages for any action taken, or any failure to take any action, as a director

Review corporation information for your state, or the state of your choice at the state's Secretary of State website. The South Dakota Secretary of State website is linked here as an example.
ARTICLES OF INCORPORATION

These Articles of Incorporation are executed by the undersigned for the purpose of forming a business corporation under the __________ Business Corporation Act.

ARTICLE I.

The name of the corporation is ____________________, Inc.

ARTICLE II.

The period of the corporation's duration is perpetual.

ARTICLE III.

The purpose for which the corporation is organized is to ________________________ and to engage in all other lawful business.

ARTICLE IV.

The corporation shall have authority to issue ________________ (_______) shares of common stock with a par value of ____________ and no/100 Dollars ($____.00) per share.

ARTICLE V.

The corporation will not commence business until consideration of at least One Thousand and no/100 Dollars ($1,000.00) has been received for the issuance of shares.

ARTICLE VI.

The address of the corporation's initial registered office is ________________________.
The name of its initial registered agent at such address is ________________________.

ARTICLE VII.

The number of directors constituting the corporation's initial board of directors is __________ (____). The names and addresses of the persons who are to serve as the initial directors are: ________________________

ARTICLE VIII.

The names and addresses of the corporation's incorporators are: ________________________

ARTICLE IX.

Every director and officer of the corporation shall be indemnified against all liabilities, civil and criminal, incurred in relation to their duties, including the reasonable expenses of defense, except to the extent that such director or officer shall have been finally adjudged to be liable for negligence or misconduct in the matter out of which the liability arises.

These Articles of Incorporation may be amended in the manner authorized by law at the time of the amendment.
Executed in duplicate on the days and year set forth in the acknowledgements.

Incorporator

Incorporator

STATE OF ____________________ )
COUNTY OF ____________________ ) SS.

On this ______ day of ____________________, 20____, before me, the undersigned notary public, personally appeared ____________________ and ____________________, known to me or satisfactorily proven to be the persons whose names are subscribed to the foregoing instrument and acknowledged that they executed the same for the purposes therein contained.

IN WITNESS WHEREOF I hereunto set my hand and official seal.

(SEAL)

My commission expires: ____________________

Notary Public in and for said County & State

CONSENT OF REGISTERED AGENT

____________________ hereby consents to his appointment as registered agent of ____________________, Inc., as set forth in Article VI of its Articles of Incorporation.

Executed the day and year set forth in the acknowledgement.

____________________, Registered Agent

STATE OF ____________________ )
COUNTY OF ____________________ ) SS.

On this ______ day of ____________________, 20____, before me, the undersigned notary public, personally appeared ____________________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.
3. Persons Involved in a Corporation
Although a corporation is a separate legal person under the laws of the state, it needs "real people" to function.

■ **Incorporators**

Incorporators are the persons who file the articles of incorporation to create the corporation. Many states require only one incorporator, who can be either a natural person (an actual person) or another corporation (a legal person).

■ **Stockholders**

Stockholders, also called shareholders, own shares of stock in the corporation. The articles of incorporation may state the maximum number of shares of stock that may be issued by the corporation. In many states it is possible for a corporation to have only one stockholder. The majority of corporations in the United States are close corporations with only a small number of shareholders. These corporations are sometimes called "Mom and Pop" corporations, because the shareholders are part of the same family operating a family business.

Unless otherwise agreed, shareholders are not personally liable for the debts and obligations of the corporation, except for the amount that they invested to purchase the stock. The corporation continues, even if a shareholder dies.

Although shareholders are not personally liable for the debts of the corporation, it is common for lending institutions to require that shareholders co-sign, or guarantee, loans made to "Mom and Pop" family corporations. In such cases, the shareholders agree to become personally liable for the payment of the loan.

■ **Board of Directors**

A business corporation is managed by its board of directors, whose members are elected by the shareholders in accordance with the corporation's bylaws. Directors owe a fiduciary duty to the shareholders to manage the corporation properly. If the directors fail to manage the corporation properly, the shareholders may sue the directors for any wrongdoing.

■ **Corporate Officers**

The board of directors delegates day-to-day management decisions to corporate officers,
including the corporation's president, vice-presidents, secretary, and treasurer. The duties and responsibilities of the corporate officers are set forth in the corporation's bylaws.

4. Organization Meeting
After filing the articles of incorporation, the first act of the corporation is to conduct an organization meeting by the initial board of directors to:

1. Elect corporate officers
2. Adopt bylaws
3. Authorize the issuance of shares of stock
4. Open an account for the deposit of corporate funds
5. Address such other matters that the board may wish to consider

EXAMPLE

MINUTES OF ORGANIZATION MEETING OF THE BOARD OF DIRECTORS

The organization meeting of the initial Board of Directors of ________________, Inc., a corporation duly organized and existing under the laws of the State of ________________, was held at ______ P.M., ________________, 20__, at __________________. The following director, being all the members of the initial Board of Directors were present and participated in the meeting:

____________________________

____________________________ was chosen as temporary Chairperson and the temporary Secretary of the meeting.

The Chairperson called for the nomination of officers of the corporation. Thereupon, the following persons were nominated as officers of the corporation:

President: ________________
Vice-President: ________________
Director: ________________
 Treasurer: ________________

No further nominations being made, the nominations were closed and the Directors proceeded to vote on the nominees. All of the Directors present at the meeting having voted and the vote having been counted, the Chairperson announced the nominees had been duly elected to the offices set before their respective names.

The permanent officers of the corporation then took charge of the meeting.

The Secretary presented to the meeting a proposed form of bylaws for the regulation and management of the affairs of the corporation. The bylaws were read and considered, and upon motion duly made, seconded and carried, were adopted and ordered filed with the minutes of this meeting.
Upon motion duly made, seconded and carried, it was directed that a corporate seal be procured in accordance with the by-laws.

Upon motion duly made, seconded and carried, the following resolutions were adopted: RESOLVED, by unanimous vote of the Board of Directors, that the following persons are authorized to purchase the following initial amounts of shares in the corporation upon receipt of the sums set forth below:

<table>
<thead>
<tr>
<th>Name</th>
<th>Shares</th>
<th>$ Amount</th>
</tr>
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<tbody>
<tr>
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FURTHER RESOLVED, that the President is authorized and directed to take all actions necessary to qualify the corporation as a Subchapter S corporation; it is

FURTHER RESOLVED, the Treasurer is authorized and directed to open a checking account in the name of this corporation with ________________________, of ______

______________________, for the deposit of funds of the corporation, such funds to be withdrawn only by check of the corporation; it is

FURTHER RESOLVED, that the Treasurer is authorized and directed to prepare checks to pay all fees and expenses incident to and necessary for the organization of this corporation.

Upon motion duly made, seconded and carried, the meeting was adjourned.

Secretary

5. Bylaws
Bylaws adopted by the board of directors must be consistent with the articles of incorporation and may not violate state or Federal law. Bylaws may be amended from time to time according to the procedure set forth in within the bylaws.

______________________, INC.

BYLAWS

ARTICLE I. Offices

The principal office of the corporation in the State of ______________ shall be located in or near ______________. The corporation may have such other offices, either within or without the State of ______________, as the Board of Directors may designate or as the business of the corporation may require from time to time.

ARTICLE II. Shareholders

2.1 Annual Meeting. Unless otherwise agreed by unanimous vote of the shareholders, the annual meeting of the shareholders shall be held during the month of ______________ of each year, beginning in 20_____, for the purpose of electing Directors and for the
transaction of such other business as may come before the meeting. If the day fixed for the annual meeting shall be a legal holiday in the State of South Dakota, such meeting shall be held on the next succeeding business day. If the election of Directors shall not be held on the day designated herein for any annual meeting of the shareholders, or at any adjournment thereof, the Board of Directors shall cause the election to be held at a special meeting of the shareholders as soon thereafter as conveniently may be.

2.2 Special Meetings. Special meetings of the shareholders, for any purpose or purposes, unless otherwise prescribed by statute, may be called by the President or by the Board of Directors, and shall be called by the President at the request of the holders of not less than seventy-five percent (75%) of all the outstanding shares of the corporation entitled to vote at the meeting.

2.3 Place of Meeting. The Board of Directors may designate any place, either within or without the State of South Dakota, unless otherwise prescribed by statute, as the place of meeting for any annual meeting or for any special meeting called by the Board of Directors. Any meeting may be conducted by telephone conference call. A waiver of notice signed by all shareholders entitled to vote at a meeting may designate any place, either within or without the State of South Dakota, unless otherwise prescribed by statute, as the place for the holding of such meeting. If no designation is made, or if a special meeting be otherwise called, the place of meeting shall be the Principal office of the corporation in the State of South Dakota.

2.4 Notice of Meeting. Written notice stating the place, day and hour of the meeting and, in case of special meeting, the purpose or purposes for which the meeting is called, shall, unless otherwise prescribed by statute, be delivered not less than ten (10) nor more than thirty (30) days before the date of the meeting, either personally or by mail, by or at the direction of the President, or the Secretary, or the persons calling the meeting, to each shareholder of record entitled to vote at such meeting. If mailed, such notice shall be deemed to be delivered when deposited in the United States mail, addressed to the shareholder at his address as it appears on the stock transfer books of the corporation, with postage thereon prepaid.

2.5 Closing of Transfer Books or Fixing of Record Date. For the purpose of determining shareholders entitled to notice of or to vote at any meeting of shareholders or any adjournment thereof, or shareholders entitled to receive payment of any dividend, or in order to make a determination of shareholders for any other proper purpose, the Board of Directors of the corporation may provide that the stock transfer books shall be closed for a stated period but not to exceed, in any case, forty-five (45) days immediately preceding such meeting. In lieu of closing the stock transfer books, the Board of Directors may fix in advance a date as the record date for any such determination of shareholders, such date in any case to be not more than forty-five (45) days and, in case of a meeting of shareholders, not less than thirty (30) days prior to the date on which the particular action, requiring such determination of shareholders, is to be taken. If the stock transfer books are not closed and no record date is fixed for the determination of shareholders entitled to notice of or to vote at a meeting of shareholders, or shareholders entitled to receive payment of a dividend, the date on which notice of the meeting is mailed or the date on which the resolution of the Board of Directors declaring such dividend is adopted, as the case may be, shall be the record date for such determination of shareholders. When a determination of shareholders entitled to vote at any meeting of shareholders has been made as provided in this section, such determination shall apply to any adjournment thereof.

2.6 Voting Lists. The officer or agent having charge of the stock transfer books for shares of the corporation shall make a complete list of the shareholders entitled to vote at each meeting of shareholders or any adjournment thereof, arranged in alphabetical order, with the address of and the number of shares held by each. Such list shall be produced and kept open at the time and place of the meeting and shall be subject to the inspection of any shareholder during the whole time of the meeting for the purposes thereof.
2.7 **Quorum.** A majority of the outstanding shares of the corporation entitled to vote, represented in person or by proxy, shall constitute a quorum at a meeting of shareholders. If less than a majority of the outstanding shares are represented at a meeting, a majority of the shares so represented may adjourn the meeting from time to time without further notice. At such adjourned meeting at which a quorum shall be present or represented, any business may be transacted which might have been transacted at the meeting as originally noticed. The shareholders present at a duly organized meeting may continue to transact business until adjournment, notwithstanding the withdrawal of enough shareholders to leave less than a quorum.

2.8 **Proxies.** At all meetings of shareholders, a shareholder may vote in person or by proxy executed in writing by shareholder or by his duly authorize attorney in fact. Such proxy shall be filed with the secretary of the corporation before or at the time of the meeting. No proxy shall be valid after six (6) months from the date of its execution, unless otherwise provided in the proxy.

2.9 **Voting of Shares.** Subject to the provisions of Section 12 of this Article II, each outstanding share entitled to vote shall be entitled to one vote upon each matter submitted to a vote at a meeting of shareholders.

2.10 **Voting of Shares by Certain Holders.** (a) Shares standing in the name of another corporation may be voted by such officer, agent or proxy as the by-laws of such corporation may prescribe, or, in the absence of such provision, as the board of directors of such corporation may determine.

(b) Shares held by an administrator, executor, guardian or conservator may be voted by him, either in person or by proxy, without a transfer of such shares into his name. Shares standing in the name of a trustee may be voted by him, either in person or by proxy, but no trustee shall be entitled to vote shares held by him without a transfer of such shares into his name.

(c) Shares standing in the name of a receiver may be voted by such receiver, and shares held by or under the control of a receiver may be voted by such receiver without the transfer thereof into his name if authority so to do be contained in an appropriate order of the court by which such receiver was appointed.

(d) A shareholder whose shares are pledged shall be entitled to vote such shares until the shares have been transferred into the name of the pledgee, and thereafter the pledgee shall be entitled to vote the shares so transferred.

(e) Shares of its own stock belonging to the corporation shall not be voted, directly or indirectly, at any meeting, and shall not be counted in determining the total number of outstanding shares at any given time.

2.11 **Informal Action by Shareholders.** Unless otherwise provided by law, any action required to be taken at a meeting of the shareholders, or any other action which may be taken at a meeting of the shareholders, may be taken without a meeting if a consent in writing, setting forth the action so taken, shall be signed by all the shareholders entitled to vote with respect to the subject matter thereof.

2.12 **Cumulative Voting.** Unless otherwise provided by law, at each election for Directors every shareholder entitled to vote at such election shall have the right to vote, in person or by proxy, the number of shares owned by him for as many persons as there are Directors to be elected and for whose election he has a right to vote, or to cumulate his votes by giving one candidate as many votes as the number of such Directors multiplied by the
number of his shares shall equal, or by distributing such votes on the same principle among any number of candidates.

ARTICLE III.
Board of Directors

3.1 General Powers. The business and affairs of the corporation shall be managed by its Board of Directors.

3.2 Number, Tenure and Qualifications. The number of directors of the corporation shall be ______________(____). The directors shall hold office until the next annual meeting of shareholders and until his/her successor shall have been elected and qualified.

3.3 Regular Meetings. A regular meeting of the Board of Directors shall be held without other notice than this bylaw immediately after, and at the same place as, the annual meeting of shareholders. The Board of Directors may provide, by resolution, the time and place for the holding of additional regular meetings without other notice than such resolution. Any meeting may be conducted by telephone conference call.

3.4 Special Meetings. Special meetings of the Board of Directors may be called by or at the request of the President or by the directors. The person or persons authorized to call special meetings of the Board of Directors may fix the place for holding any special meeting of the Board of Directors called by them. Any meeting may be conducted by telephone conference call.

3.5 Notice. Notice of any special meeting shall be given at least three (3) days previously thereto by written notice delivered personally or mailed to each director at his business address, or by telegram. If mailed, such notice shall be deemed to be delivered when deposited in the United States mail so addressed, with postage thereon prepaid. If notice be given by next day delivery service, such notice shall be deemed to be delivered when it is delivered to the delivery service company. Any director may waive notice of any meeting. The attendance of a director at a meeting shall constitute a waiver of notice of such meeting, except where a director attends a meeting for the express purpose of objecting to the transaction of any business because the meeting is not lawfully called or convened.

3.6 Quorum. A majority of the number of directors fixed by Section 2 of this Article III shall constitute a quorum for the transaction of business at any meeting of the Board of Directors, but if less than such majority is present at a meeting, a majority of the directors present may adjourn the meeting from time to time without further notice.

3.7 Manner of Acting. The act of the majority of the directors present at a meeting at which a quorum is present shall be the act of the Board of Directors.

3.8 Action Without a Meeting. Any action that may be taken by the Board of Directors at a meeting may be taken without a meeting if a consent in writing, setting forth the action so to be taken, shall be signed before such action by all of the Directors.

3.9 Vacancies. Any vacancy occurring in the Board of Directors may be filled by the affirmative vote of a majority of the remaining directors, though less than a quorum of the Board of Directors, unless otherwise provided by law. A director elected to fill a vacancy shall be elected for the unexpired term of his predecessor in office. Any directorship to be filled by reason of any increase in the number of directors may be filled by election by the Board of Directors for a term of office continuing only until the next election of Directors by the shareholders.
3.10 **Compensation.** By resolution of the Board of Directors, each Director may be paid his expenses, if any, of attendance at each meeting of the Board of Directors, and may be paid a stated salary as director or a fixed sum for attendance at each meeting of the Board of Directors, or both. No such payment shall preclude any director from serving the corporation in any other capacity and receiving compensation therefor.

3.11 **Presumption of Assent.** A director of the corporation who is present at a meeting of the Board of Directors at which action on any corporate matter is taken shall be presumed to have assented to the action taken unless his dissent shall be entered in the minutes of the meeting or unless he shall file his written dissent to such action with the person acting as the secretary of the meeting before the adjournment thereof or shall forward such dissent by registered mail to the Secretary of the corporation immediately after the adjournment of the meeting. Such right to dissent shall not apply to a Director who voted in favor of such action.

**ARTICLE IV.**

**Officers**

4.1 **Number.** The officers of the corporation shall be a President, a Vice-President, a Secretary, and a Treasurer, each of whom shall be elected by the Board of Directors. Such other officers and assistant officers as may be deemed necessary may be elected or appointed by the Board of Directors.

4.2 **Election and Term of Office.** The officers of the corporation to be elected by the Board of Directors shall be elected annually by the Board of Directors at the first meeting of the Board of Directors held after each annual meeting of the shareholders. If the election of officers shall not be held at such meeting, such election shall be held as soon thereafter as conveniently may be. Each officer shall hold office until his successor shall have been duly elected and shall have qualified or until his death or until he shall resign or shall have been removed in the manner hereinafter provided.

4.3 **Removal.** Any officer or agent may be removed by the Board of Directors whenever, in its judgment, the best interests of the corporation will be served thereby, but such removal shall be without prejudice to the contract rights, if any, of the person so removed. Election or appointment of an officer or agent shall not of itself create contract rights.

4.4 **Vacancies.** A vacancy in any office because of death, resignation, removal, disqualification or otherwise, may be filled by the Board of Directors for the unexpired portion of the term.

4.5 **President.** The President shall be the principal executive officer of the corporation and, subject to the control of the Board of Directors, shall in general supervise and control all of the business and affairs of the corporation. He shall, when present, preside at all meetings of the shareholders and of the Board of Directors. He may sign certificates for shares of the corporation, any deeds, mortgages, bonds, contracts, or other instruments which the Board of Directors has authorized to be executed, except in cases where the signing and execution thereof shall be expressly delegated by the Board of Directors or by these Bylaws to some other officer or agent of the corporation, or shall be required by law to be otherwise signed or executed; and in general shall perform all duties incident to the office of President and such other duties as may be prescribed by the Board of Directors from time to time.

4.6 **Vice-President.** In the absence of the President or in the event of his death, inability or refusal to act, the Vice-President(s) shall perform the duties of the President, and when so acting, shall have all the power of and be subject to all the restrictions upon the President. The Vice-President(s) shall perform such other duties as from time to time may be assigned to him by the President or by the Board of Directors.
4.7 Secretary. The Secretary shall: (a) keep the minutes of the proceedings of the shareholders and of the Board of Directors in one or more books provided for that purpose; (b) see that all notices are duly given in accordance with the provisions of these Bylaws or as required by law; (c) be custodian of the corporate records and of the seal of the corporation and see that the seal of the corporation is affixed to all documents the execution of which on behalf of the corporation under its seal is duly authorized; (d) keep a register of the post office address of each shareholder which shall be furnished to the Secretary by such shareholder; (e) sign with the President, certificates for shares of the corporation, the issuance of which shall have been authorized by resolution of the Board of Directors; (f) have general charge of the stock transfer books of the corporation; and (g) in general perform all duties incident to the office of Secretary and such other duties as from time to time may be assigned to him by the President or by the Board of Directors.

4.8 Treasurer. The Treasurer shall: (a) have charge and custody of and be responsible for all funds and securities of the corporation; (b) receive and give receipts for moneys due and payable to the corporation from any source whatsoever, and deposit all such moneys in the name of the corporation in such banks, trust companies or other depositaries as shall be selected in accordance with the provisions of Article V of these Bylaws; and (c) in general perform all of the duties incident to the office of Treasurer and such other duties as from time to time may be assigned to him by the President or by the Board of Directors. If required by the Board of Directors, the Treasurer shall give a bond for the faithful discharge of his duties in such sum and with such surety or sureties as the Board of Directors shall determine.

4.9 Salaries. The salaries of the officers shall be fixed from time to time by the Board of Directors and no officer shall be prevented from receiving such salary by reason of the fact that he is also a director of the corporation.

ARTICLE V.
Contracts, Loans, Checks & Deposits

5.1 Contracts. The Board of Directors may authorize any officer or officers, agent or agents, to enter into any contract or execute and deliver any instrument in the name of and on behalf of the corporation, and such authority may be general or confined to specific instances.

5.2 Loans. No loans shall be contracted on behalf of the corporation and no evidences of indebtedness shall be issued in its name unless authorized by a resolution of the Board of Directors. Such authority may be general or confined to specific instances.

5.3 Checks, drafts, etc. All checks, drafts or other orders for the payment of money, notes or other evidence of indebtedness issued in the name of the corporation, shall be signed by such officer or officers, agent or agents of the corporation and in such manner as shall from time to time be determined by resolution of the Board of Directors.

5.4 Deposits. All funds of the corporation not otherwise employed shall be deposited from time to time to the credit of the corporation in such banks, trust companies or other depositaries as the Board of Directors may select.

ARTICLE VI.
Certificates for Shares and Their Transfer

6.1 Certificates for Shares. Certificates representing shares of the corporation shall be in such form as shall be determined by the Board of Directors. Such certificates shall be signed by the President and by the Secretary or by such other officers authorized by law and by the Board of Directors so to do, and sealed with the corporate seal. All certificates for shares shall be consecutively numbered or otherwise identified. The name and address of the person to whom the shares represented thereby are issued, with the number of shares and date of issue, shall
be entered on the stock transfer books of the corporation. All certificates surrendered to the corporation for transfer shall be canceled and no new certificate shall be issued until the former certificate for a like number of shares shall have been surrendered and canceled, except that in case of a lost, destroyed or mutilated certificate, a new one may be issued therefor upon such terms and indemnity to the corporation as the Board of Directors may prescribe.

6.2 Issuance of Shares. Shares shall only be issued to persons and in amounts approved by a two thirds (2/3) majority of the Board of Directors.

6.3 Transfer of Shares. Subject to the restrictions of Section 4 of this Article, transfer of shares of the corporation shall be made only on the stock transfer books of the corporation by the holder of record thereof or by his legal representative, who shall furnish proper evidence of authority to transfer, or by his attorney thereunto authorized by power of attorney duly executed and filed with the Secretary of the corporation, and on surrender for cancellation of the certificate for such shares. The person in whose name shares stand on the books of the corporation shall be deemed by the corporation to be the owner thereof for all purposes.

6.4 Restrictions on Sale, Transfer, and Creation of Liens. (a) No shareholder of the corporation and no representative of a deceased or incompetent shareholder may sell or transfer any of such shareholder's shares in the corporation to someone other than another shareholder, unless the shareholder or his representative shall have first offered such shares to the corporation for the price and on the terms of any bona fide offer of purchase received by the shareholder. The corporation shall have a period of sixty (60) days after receipt of written notice at its principal office to accept or decline purchasing such shares.

(b) No shareholder of the corporation and no representative of a deceased or incompetent shareholder may create or allow a security interest or lien to attach to any shares, unless first approved by a two thirds (2/3) majority of the Board of Directors.

(c) Each certificate representing shares of the corporation shall contain an endorsement reading substantially as follows: "The shares represented by this certificate are subject to certain requirements and restrictions on their transfer and on the creation of security interests or liens on such shares, as provided by the By-laws of the corporation, a copy of which is on file at the corporation's principal office."

ARTICLE VII.
Fiscal Year

The fiscal year of the corporation shall begin the 1st day of January and end on the 31st day of December of each year.

ARTICLE VIII.
Dividends

The Board of Directors may from time to time declare, and the corporation may pay, dividends on its outstanding shares in the manner and upon the terms and conditions provided by law and its articles of incorporation.

ARTICLE IX.
Corporate Seal

The Board of Directors shall provide a corporate seal which shall be circular in form and shall have inscribed thereon the name of the corporation and the state of incorporation and the words, "Corporate Seal."
ARTICLE X.
Waiver of Notice

Unless otherwise provided by law, whenever any notice is required to be given to any shareholder or director of the corporation under the provision of these Bylaws or under the provisions of the articles of incorporation or under the provisions of the South Dakota Business Corporation Act, a waiver thereof in writing, signed by the person or persons entitled to such notice, whether before or after the time state therein, shall be deemed equivalent to the giving of such notice.

ARTICLE XI.
Amendments

These Bylaws may be altered, amended or repealed and new Bylaws may be adopted by the Board of Directors at any regular or special meeting of the Board of Directors.

Review the differences between bylaws and articles of incorporation in the article How Bylaws Differ from the Articles of Incorporation by LegalFlip.com.

6. Shares of Stock

The corporation raises capital (operating funds) by selling shares of stock. The par value of stock is the value placed on the stock when the corporation is created. Par value does not reflect the actual value of the stock, which is determined by the value of the corporation.

If the corporation is a publicly-traded corporation, such as International Business Machines Corporation (IBM), shares of stock are sold and purchased on a public stock exchange, such as the New York Stock Exchange. Shares in a close corporation, with only a small number of shareholders, are not traded on a public stock exchange. The bylaws of these corporations often restrict the transfer of shares, requiring that they first be offered to other shareholders, before being offered to an outside person.

The sale of stock must comply with all state and Federal laws regulating the sale of corporate securities.

- Classes of Stock

A corporation may have different classes of stock. For example, a corporation may have common stock and preferred stock. As the name indicates, shareholders holding preferred stock enjoy priority over shareholders holding common stock. Shareholders holding common stock are not guaranteed to receive a dividend (return on their investment). By contrast, shareholders holding preferred stock are generally entitled to receive a dividend, if the corporation has generated sufficient profits to pay such dividends.

- Classes of Preferred Stock

Shareholders holding cumulative preferred stock are entitled to receive an established dividend each year that the corporation has sufficient funds to pay such dividends. If the corporation does not have sufficient funds in one year, the missed dividend will be paid in subsequent years, as funds become available. Shareholders holding noncumulative preferred stock lose their right to receive a dividend in any year in which sufficient funds are not available to pay the dividend.
■ Declaration of Dividends
The board of directors determines whether dividends should be paid in any given year. Dividends are usually paid in cash. In some instances, the board of directors may elect to declare a *stock dividend*, rather than a *cash dividend*. In those cases, shareholders receive additional shares of stock, instead of cash.

7. Doing Business outside the State
A corporation is authorized to do business within the state of incorporation. The corporation is not authorized to do business in another state, unless it first registers to do business as a "foreign corporation" within that state. Such registration is usually filed with the Secretary of State.

A corporation that wishes to do business in another country must comply with all the laws of that country, as well as laws of the United States that may restrict or prohibit such business.

8. Dissolution
Although the articles of incorporation may state that the corporation will have a perpetual existence, the corporation may be terminated, either voluntarily or involuntarily.

■ Voluntary Dissolution
Generally, a corporation may be voluntarily dissolved by filing *articles of dissolution* with the designated state office, after a majority vote of the shareholders. After filing the articles of dissolution, the corporation will generally:

1. Collect its assets
2. Dispose of its properties that will not be distributed in kind to its shareholders
3. Discharge or make provision for discharging its liabilities;
4. Distribute its remaining property among its shareholders according to their interests
5. Do all other actions necessary wind up the business

■ Involuntary Dissolution
A corporation may be involuntarily dissolved by the state in which it is incorporated, if it does not comply with statutes governing corporations, including failure to pay fees and failure to file required reports. Similarly, a corporation's authority to do business in another state may be revoked, if it does not comply with the laws of that state.

9. Advantages/Disadvantages
Operating a business as a corporation offers several advantage, including the limited liability of shareholders, the ability to raise capital by selling shares of stock, and perpetual existence of the corporation.

■ Limited Liability
Limited liability of the shareholders is a major advantage of operating a business as a corporation. Unlike a sole proprietorship or a general partner, a shareholder is not personally liable for the debts of the corporate business, unless the shareholder agrees to
become liable by co-signing or guaranteeing a corporate debt. If the corporation is operated properly and observes all statutory formalities, the liability of the shareholder is limited to the amount that the shareholder invested to purchase stock in the corporation.

Note, however, that a shareholder could become personally liable for corporate obligations, if the corporation does not comply with all statutory requirements, or the corporation is used to commit fraud or a crime. In such cases, a court may pierce the corporate veil and hold shareholders personally liable for the obligations of the corporation.

- **Raising Capital**
  Raising capital (operating money) through the sale of stock is another significant advantage of operating a business as a corporation. A corporation may raise funds to operate the business by selling shares of stock. A corporation is not limited to borrowing money from individuals or lending institutions. Dividends are paid to stockholders when the business is profitable. No dividends are paid, if the business is doing poorly, or the corporation wishes to use funds to expand the business. By contrast, a loan must be paid on schedule, whether business is good or bad.

- **Perpetual Existence**
  Perpetual existence is an important benefit of operating a business as a corporation. Unlike a sole proprietorship, general partnership, or limited partnership, a corporation continues to exist despite the death or incompetence of a shareholder.

Disadvantages of operating a business as a corporation include the formalities and expenses necessary to form and operate a corporation, possible double taxation, and the formalities involved in dissolving the corporation.

- **Formalities and Expenses**
  The formalities and expenses involved in starting and running a corporation are greater than other forms of business organizations. Formal articles of incorporation and reports must be filed with the appropriate government office, state and Federal laws regulating the sale of stock must be strictly observed, internal corporate records must be maintained, and required meetings of shareholders and directors must be conducted.

- **Double Taxation**
  Double taxation may occur if the corporation is classified as a C corporation by the U.S. Internal Revenue Service. The corporation pays income tax on profits. A portion of the remaining profits are taxed again as income to shareholders when they are distributed to shareholders as dividends. Double taxation can be reduced, if the corporation qualifies as a Subchapter S corporation under IRS regulations. In such case, the profits are only taxed once as they "flow through" from the corporation to the shareholders.

- **Formalities of Dissolution**
  The formalities involved in dissolving the corporation make terminating the corporation a time-consuming and sometimes expensive process. Corporate assets must be assembled, creditors must be paid, remaining assets distributed to shareholders, and articles of
dissolution filed with the appropriate government office.

10. Summary
A business corporation is a legal entity created under state statutes. A business corporation exists and operates separately from its owners, the stockholders. The corporation is managed by the board of directors, who delegate day-to-day management duties to corporate officers. The corporation sells shares of stock to raise operating capital. Shareholders receive dividends, as declared by the board of directors. Shareholders holding preferred stock enjoy priority in receiving dividends over shareholders holding common stock.

Review the statutes of your state, or a state of your choice governing the creation, operation, and termination of a business corporation. Statutes are available online at the Cornell University Law School Legal Information Institute.

Ask your instructor for assistance, if you have difficulty locating the statutes.

Also, determine if online corporate forms are available for your state, or a state of your choice, at the Website of the chosen state's Secretary of State website. The South Dakota Secretary of State website is linked here as an example.

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### E. Limited Liability Company

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1. Definition
A **limited liability company** is a relatively new form of business organization authorized by many states. In many ways, a limited liability company (LLC) is a hybrid organization that combines the advantages of a partnership and a corporation. Like a corporation, an LLC is considered a separate legal entity, whose owners (called members) are not personally liable for the debts of the LLC. However, the LLC requires fewer formalities to operate than a corporation. In addition, an LLC can avoid double-taxation experienced by corporations that do not qualify as a Subchapter S corporation.

2. Creation
A limited liability company is created by filing *articles of organization* with the designated government office, often the Secretary of State. The contents of the articles of organization are prescribed by statute. Often, state law requires that articles of organization contain certain information, such as:

   1. The name of the company
   2. The address of the initial designated office
   3. The name and street address of the initial agent for service of process
4. The name and address of each organizer
5. The duration of the company if other than perpetual
6. Whether the company is to be manager-managed, and, if so, the name and address for each initial manager
7. Whether one or more of the members of the company are to be liable for its debts and obligations

Some states allow articles of organization to also include other optional information, including:
1. Provisions permitted to be set forth in an operating agreement
2. Other matters not inconsistent with law

**ARTICLES OF ORGANIZATION OF**

L.L.C.

Executed by the undersigned for the purpose of forming a limited liability company under the ________________ Limited Liability Company Act.

**ARTICLE I.**
The name of the limited liability company is ______________________, L.L.C.

**ARTICLE II.**
The period of the limited liability company's duration is thirty (30) years from the date of the filing of these Articles of Organization with the ________________ Secretary of State, unless sooner dissolved in accordance with the provisions of its Operating Agreement.

**ARTICLE III.**
The purpose for which the limited liability company is organized is to ______________________, and to engage in any lawful business for which a limited liability company may be organized.

**ARTICLE IV.**
A. The address of the limited liability company's principal place of business is ______________________.
   B. The address of the limited liability company's initial registered office is ______________________.

**ARTICLE V.**
The limited liability company will not commence business until it has received the initial contribution for membership interest consisting of cash, property, or services. The total amount of cash and a description and agreed value of property or past services initially contributed, or to be initially contributed, by each member is attached hereto as Exhibit "A" and incorporated herein by reference.

**ARTICLE VI.**
Members of the limited liability company will not be required to make additional contributions, unless consented to by all members.
ARTICLE VII.
Additional members may be admitted to the limited liability company only by the consent of all members. The terms and conditions of such admission shall be set forth in the Operating Agreement.

ARTICLE VIII.
Upon the death, retirement, resignation, expulsion, bankruptcy, dissolution of a member, or any other event which terminates the continued membership of a member in the company, the limited liability company may be continued by the consent of all remaining members, provided that there are at least two (2) remaining members.

ARTICLE IX.
The management of the limited liability company is reserved to the members, and the names and addresses of such members are as follows:

ARTICLE X.
The names and addresses of the organizers are:

ARTICLE XI.
The limited liability company shall have the powers provided for in the ____________ Limited Liability Company Act.

ARTICLE XII.
To the full extent permitted by ____________ law, no member of the limited liability company shall be liable to the limited liability company or its members for monetary damages for an act or omission in such member's capacity as a member of the limited liability company, except that this Article does not eliminate or limit the liability of a member to the extent the member is found liable for: (a) a breach of the member's duty of loyalty to the limited liability company or its members; (b) an act or omission not in good faith that constitutes a breach of duty of the member to the limited liability company or an act or omission that involves intentional misconduct or a knowing violation of the law; (c) a transaction from which the member received an improper benefit, whether or not the benefit resulted from an action taken within the scope of the member's office; or (d) an act or omission for which the liability of a member is expressly provided by an applicable statute. Any repeal or amendment of this Article by the members of the limited liability company shall be prospective only and shall not adversely affect any limitation on the liability of a member of the limited liability company existing at the time of such repeal or amendment. In addition to the circumstances in which the member of the limited liability company is not liable as set forth in the preceding sentences, the member shall not be liable to the fullest extent permitted by any provision of the statutes of South Dakota hereafter enacted that further limit the liability of a member or manager of a limited liability company. The foregoing elimination of the liability to the limited liability company or the other members for monetary damages shall not be deemed exclusive of any other rights or limitations of liability or indemnity to which a member may be entitled under any other provisions of the Articles of Organization or the Operating Agreement of the limited liability company, contract, or agreement.

ARTICLE XIII.
Every member and manager, including former members and managers, of the limited liability company shall be indemnified against expenses actually and reasonably incurred by him/her in connection with the defense of an action, suit, or proceeding, civil or criminal, in which he/she is made a party by reason of being, or having been, such member or manager, except in relation to matters as to which he/she may be adjudged in the action, suit, or
proceeding to be liable for negligence or misconduct in the performance of duty.

These Articles may be amended in the manner authorized by law at the time of the amendment.

IN WITNESS WHEREOF, we have hereunto set our hands this ___ day of
______________________, 20__.

Organizer

Organizer

STATE OF __________________________)
COUNTY OF __________________________)
____________________ and __________________________, being each duly sworn upon their oaths,
depose and state that they are residents of __________________________; that they are the organizers
described in and who signed the foregoing Articles of Organization; that they have read said
Articles and know the contents thereof; that they intend in good faith to form a limited liability
company for the purpose of promotion of a lawful business as set forth is said Articles; and that the
matters stated therein are true of their own knowledge.

Organizer

Organizer

Subscribed and sworn to before me this _____ day of _________________, 20__.

(SEAL) Notary Public

My commission expires: ________________________

VERIFICATION

CONSENT OF REGISTERED AGENT

I, __________________________, hereby consent to serve as the registered agent of
______________________________, L.L.C.

Dated this ____ day of _________________, 20__.

Registered Agent
3. Persons Involved in a Limited Liability Company
The persons involved in the creation and operation of a limited liability company include organizers, members, and may include a manager.

- **Organizers**
  *Organizers* are the persons who file the articles of organization to create the limited liability company. An organizer serves the same person as an incorporator who starts a corporation.

- **Members**
  *Members* of a limited liability company contribute capital to the company. If members agree, such contributions may be made in the form of cash, goods, or services. Unless otherwise agreed, profits are distributed to members in proportion to the amount of contribution. Unless otherwise agreed, members are not personally liable for the debts and obligations of the LLC, except for the amount that they contributed to company.
  Members manage the company, unless they designate management duties to a manager. Each member owes a fiduciary duty to the LLC and other members to act in good faith and to refrain from engaging in conduct that would harm the business.

  A member may generally transfer his/her membership interest in the LLC in accordance with the term of the LLC’s operating agreement.

- **Manager**
  The members of an LLC may designate a manager to operate the business. The duties and responsibilities of the manager are set forth in the LLC’s operating agreement. An LLC with a manager is termed a manager managed LLC, while an LLC without a manager is termed a member managed LLC.

- **Registered Agent**
  The registered agent named in the LLC’s articles of organization is designated as the person to be served with legal process (legal papers commencing a lawsuit) in the event that the LLC is named as a defendant in a civil action.

4. Operating Agreement
The operating agreement adopted by the members of the LLC sets forth provisions for the internal operation of the business. The operating agreement may be as simple or as complex as the members agree, but it may not contradict state law.

**OPERATING AGREEMENT OF**

______________________, L.L.C.

ARTICLE I.
OFFICES

  The principal office of ____________________, L.L.C., (the Company) in the State of ____________________ shall be located at or near ____________________. The
Company may have such other offices, either within or without the State of ______________ as the members may designate, or as the Company may from time to time require.

ARTICLE II.

MEETINGS

2.1 Annual Meeting. The annual meeting of the members shall be held on the _____ day of ______________ of each year for the purpose of electing any operating manager or officers, and for the transaction of such other business as may come before the meeting. If the day fixed for the annual meeting shall be a legal holiday, such meeting shall be held on the next succeeding business day. If the election shall not be held on the day designated for the annual meeting of the members, or at any adjournment thereof, the members shall cause the election to be held at a meeting of the members as soon thereafter as it may conveniently be held.

2.2 Regular Meetings. The members may by resolution prescribe the time and place for the holding of regular meetings and may provide that the adoption of such resolution shall constitute notice of such regular meetings. If the members do not prescribe the time and place for the holding of regular meetings, such regular meetings shall be held at the time and place specified in the notice of such regular meetings.

2.3 Special Meetings. Special meetings of the members, for any purpose or purposes, unless otherwise prescribed by statute, may be called by any members.

2.4 Notice of Meeting. Written or telephonic notice stating the place, day, and hour of the meeting and, in case of a special meeting, the purposes for which the meeting is called, shall be delivered not less than ten (10) days before the date of the meeting, either personally or by mail, to each member of record entitled to vote at such meeting. If mailed, such notice shall be deemed to be delivered when deposited in the United States mail, addressed to the member at his address as it appears on the books of the Company, with postage thereon prepaid. When all the members of the company are present at any meeting, or if those not present sign in writing a waiver of notice of such meeting, or subsequently ratify all the proceedings thereof, the transactions of such meeting are as valid as if a meeting were formally called and notice had been given.

2.5 Quorum. At any meeting of the members, a majority of the equity interests, as determined from the capital contribution of each member as reflected by the books of the Company, represented in person or by proxy, shall constitute a quorum at a meeting of members. If less than said majority of the equity interests are represented at a meeting, a majority of the interests so represented may adjourn the meeting from time to time without further notice. As such adjourned meeting at which a quorum shall be present or represented, any business may be transacted which might have been transacted at the meeting as originally notified. The members present at a duly organized meeting may continue to transact business until adjournment, notwithstanding the withdrawal of enough members to leave less than a quorum.

2.6 Proxies. At all meetings of members, a member may vote by proxy executed in writing by the member or by his duly authorized attorney-in-fact. Such proxy shall be filed with another member of the Company before or at the time of the meeting. No proxy shall be valid after three (3) months from the date of its execution, unless otherwise provided in the proxy.

2.7 Voting by Certain Members. Membership certificates (interests) standing in the name of a corporation, partnership, or company, may be voted by such officer, partner, agent, or proxy as the by-laws of such entity may prescribe or, in the absence of such provision, as the board
of directors of such entity may determine. Certificates (interests) held by a trustee, personal representative, administrator, executor, guardian or conservator, may be voted by him either in person or by proxy, without a transfer of such certificates into his/its name.

2.8 Manner of Acting.

2.8.1 Formal Action by Members. Ordinarily, the act of a majority of the members present at a meeting at which a quorum is present shall be the act of the members. Upon demand of any member, voting on a particular issue may be in accordance with the percent- age of equity ownership in the Company.

2.8.2 Procedure. A member of the Company shall preside at meetings of the members. A record shall be maintained of the meetings of the members. The members may adopt their own rules of procedure which shall not be inconsistent with this Operating Agreement.

2.8.3 Presumption of Assent. A member of the Company who is present at a meeting of the members at which action on any matter is taken shall be presumed to have assented to the action taken, unless his dissent shall be entered in the minutes of the meeting, or unless he shall file his written dissent to such action with the person acting as the secretary of the meeting before the adjournment thereof, or shall forward such dissent by certified mail to the secretary of the meeting immediately after the adjournment of the meeting. Such right to dissent shall not apply to a member who voted in favor of such action.

2.8.4. Informal Action by Members. Unless otherwise provided by law, any action required to be taken at a meeting of the members, or any other action which may be taken at a meeting of the members, may be taken without a meeting if a consent in writing, setting forth the action so taken, shall be signed by all the members entitled to vote with respect to the subject matter thereof.

2.9 Order of Business. The order of business at all meetings of the members shall be as follows:

1. Roll Call
2. Proof of notice of meeting or waiver of notice
3. Reading of minutes of preceding meeting
4. Report of the Operating Manager or presiding member
5. Reports of committees
6. Unfinished business.
7. New business

2.10 Telephonic meetings. Members of the Company may participate in any meeting or the members by means of conference telephone or similar communication if all persons participating in such meeting can hear one another for the entire discussion of the matter(s) to be voted upon. Participating in a meeting pursuant to this section shall constitute presence in person at such meeting.

ARTICLE III.
FISCAL MATTERS

3.1 Fiscal Year. The fiscal year the Company shall begin on the 1st day of January, and end on the last day of December, of each year, unless otherwise determined by resolution of the members.

3.2 Deposits. All funds of the Company shall be deposited from time to time to the credit of the Company in such banks, trust companies, or other depositories as the members may select.
3.3 Checks, Drafts, Etc. All checks, drafts, or other orders for the payment of money, and all notes or other evidences of indebtedness issued in the name of the Company shall be signed by any person authorized by resolution of the members.

3.4 Loans. No loan shall be contracted on behalf of the Company or no evidence of indebtedness shall be issued in its name, unless authorized by a resolution of the members. Such authority may be general or confined to specific instances.

3.5 Contracts. The members may authorize any member or agent of the Company to enter into any contract or execute any instrument in the name of, and on behalf of, the Company. Such authority may be general or confined to specific instances.

3.6 Accountants. An accountant or tax consultant may be selected from time to time by the members to perform such tax and accounting services as may, from time to time be required. The accountant may be removed by the members without assigning any cause.

3.7 Legal Counsel. One or more attorneys at law may be selected from time to time by the members to review the legal affairs of the Company and to perform such other services as may be required and to report to the members with respect thereto. The legal counsel may be removed by the members without assigning any cause.

3.8 Cash Method of Accounting. The records of the Company shall be maintained on a cash receipts and disbursements method of accounting.

ARTICLE IV
MEMBERSHIP CERTIFICATES AND THEIR TRANSFER

4.1 Certificates. Membership certificates representing equity interest in the Company shall be in such form as shall be determined by the Operating Manager and any other member, or if there is no Operating Manager, then by the members. Such membership certificates shall be signed by any two (2) members. All membership certificates shall be consecutively numbered or otherwise identified. The names and address of each person to whom a membership certificate is issued, with the capital contribution and the date of issue, shall be entered in the certificate register of the Company. Each member's membership interest in the Company shall by a percentage of the member's agreed value of his capital contribution that bears to the agreed value of all capital contributions outstanding as reflected in the Articles of Organization, as may be amended from time to time. In case of a lost, destroyed, or mutilated membership certificate, a new one may be issued upon such terms and indemnity to the Company as the members may prescribe.

4.2 Certificates of Register. Any and all changes in the amount of capital contribution shall be formalized by filing notice of the same with the office of the South Dakota Secretary of State by amendment of the Articles of Organization. The Company secretary shall maintain a register of certificates, known as a stock or interest transfer ledger.

4.3 Transfer of Interest. Any member proposing a transfer or assignment of his membership interest shall first notify the Company in writing of all the details and consideration for the proposed transfer or assignment. The Company, for the benefit of the remaining members, shall have the first right to acquire the equity under the lesser of: (1) the same terms and conditions as the proposed transfer or assignment; or (2) the terms and conditions (including price) as set forth in Article XI as if such member proposing the transfer had died. Such election shall be made by the Company notifying the transferring member within thirty (30) days of the initial notification by the transferring member.

If the Company does not elect to purchase all the transferring member's interest being offered
within the initial thirty (30) days after notice of intent to transfer, the individual members shall have an additional thirty (30) day period in which to purchase all (or the remaining portion of) the transferring member's interest being offered under the same terms and conditions as the Company was allowed to purchase. Each of the remaining members shall first have the right to acquire the percentage interest of the interest being transferred as each remaining member's interest bears to the total membership interest of all remaining members. If all members do not wish to participate, and there is not otherwise a unanimous agreement, each member electing to participate shall be allowed to acquire the percentage interest of the interest being transferred as each participating member's interest bears to the total membership interest of all members electing participate.

If the remaining members fail or decline to elect to purchase the transferring member's interest, such interest may be sold within a period of sixty (60) days after receipt of notice of other members' declension to purchase under the proposed terms or, if no notice is given by members, then thirty (30) days after expiration of the second thirty (30) day notice period.

For the purpose of this section, a transfer shall not include a transfer to a revocable living trust in which the transferring member is the grantor and a trustee of such trust.

Also, for the purpose of this section, a transfer shall not include a transfer to a spouse, children, corporation, partnership, or another limited liability company in which the transferring member maintains at least fifty-one (51%) control, except that if all members fail to approve such transfer, such transferee shall have no right to participate in the management and business affairs of the Company.

If the transfer or assignment is made as originally proposed and the other members fail to approve the transfer or assignment by unanimous written consent, the transferee or assignee shall have no right to participate in the management of the business and affairs of the Company or to become a member. The transferee or assignee shall only be entitled to receive the share of the profit or other compensation by way of income and return of contribution to which that member would otherwise be entitled.

For the purpose of the foregoing paragraph, a change in the majority ownership or voting control (or reduction of current control ownership below fifty-one (51%) of a corporation, partnership, or limited liability company member shall constitute a transfer requiring all members to approve such change in member ownership or such entity shall have no right to participate in the management and business affairs of the Company.

If an election by the Company or member is made to acquire the interest being transferred, all of such interest being offered must be purchased.

Notwithstanding the above, it is understood that an initial entity (corporation, partnership, or limited liability company) member may be held by a group holding less than a majority of the ownership in an entity and that such status shall not be considered a transfer or effect such member's status in the Company.

ARTICLE V.
BOOKS AND RECORDS

5.1 Books and Records. The books and records of the Company shall be kept at the principal office of the Company, or at such other places within or without the State of South Dakota as the members shall from time to time determine.
5.2 **Right of Inspection.** Any member of record shall have the right to examine, at any reasonable time or times for all purposes, the books and records of account, minutes, and records of members and to make copies thereof. Such inspection may be made by any agent or attorney of the member. Upon the written request of any member of the Company, it shall mail to such member its most recent financial statements, showing in reasonable detail, its assets and liabilities and the results of its operations.

5.3 **Financial Records.** All financial records shall be maintained and reported based on generally accepted accounting principles.

**ARTICLE VI.**

**DISTRIBUTION OF PROFITS**

6.1 **Declaration.** The members may from time to time unanimously declare, and the Company may distribute, accumulated profits agreed not necessary for the cash needs of the Company's business. Unless otherwise provided, retained profits shall not be deemed an increase in the capital contribution of a member.

6.2 **Pro-Rata Distributions.** All distributions of profits (including capital gains and losses) shall be prorated to each member's percentage of membership (equity) interest.

6.3 **Limitation.** No distribution of profits shall be made where, after distribution, the value of the assets of the Company are less than all liabilities of the Company, except liabilities to members.

6.4 **Separate Account.** Any undistributed profits shall be added to a member's income account, but such account shall be identified separately from the member's capital account under the name, income account, accumulated profits, retained earnings, earned surplus, or similar name determined by the members. Any losses shall be subtracted from the balance in this separate income account, and if loss exceed profits, shown as a debit balance in said account.

6.5 **Special Allocation.** By unanimous vote of the members, special allocations of income or expense may be made to certain members, as long as such allocation is established to have substantial economic effect under the tax provisions of the Internal Revenue Code.

6.6 **Drawing Account.** Distributions during the year shall be debited to an individual drawing account. At the end of each fiscal year, the member's drawing account shall be closed into the member's income account described in section 6.4 above, unless such distributions are determined to be a distribution of contributed capital as allowed under this Operating Agreement and the South Dakota Limited Liability Companies Act.

**ARTICLE VII.**

**CAPITAL**

7.1 **Initial Capital.** Each charter member shall have an initial membership interest based upon the assigned value of his initial capital contribution as a percentage of the assigned value of the initial capital contribution of all members as set forth in the initial Articles of Organization.

7.2 **Additional Capital.** Such membership interest may be adjusted by withdrawals and contributions of additional capital, but such percentage of membership may be changed only by unanimous consent of all members. On addition of additional members, the adjustment to the percentage of membership interest shall be by the unanimous agreement of all members.
7.3 **Return of Member's Contributions.** The return of a member's contributions shall be limited as provided in the __________ Limited Liability Companies Act.

7.4 **Value of Capital Accounts.** For bookkeeping purposes, all capital accounts shall be maintained at book value (cost) as opposed to fair market value, even though fair market value shall be used in determining percentage of membership interest. Valuations different from book value shall be maintained only in memorandum accounts. Said memorandum accounts shall consist of: (a) the amount of money contributed by said member to the Company, (b) the agreed upon fair market value of property contributed by said member to the Company, (c) allocations to said member of net income and gain from the sale of assets including income and gain exempt from tax, and (d) the amount of any Company liabilities assumed by that member or that are secured by any Company assets distributed to that member minus the sum of: (e) the amount of money distributed to said member by the Company, (f) the fair market value of property distributed to said member by the Company, (g) the amount of any liabilities of that member assumed by the Company or secured by any property contributed by that member to the Company, other than those taken into account in calculating capital contributions, (h) allocations to said member of expenditures of the Company described in IRS Section 705(a)(2)(B), and (i) allocations to said member of net losses and loss from sale of assets.

With unanimous membership approval, the capital account of each member may be adjusted to reflect revaluation of the Company's assets upon the occurrence of any of the following events:

1. The significant contribution of money or other property to the Company by a new or existing member as consideration for an interest; or
2. The significant distribution of money or other property by the Company to a retiring or continuing member as consideration for an interest; or
3. The liquidation of the Company within the meaning of IRS Regulation Section 1.704-1(b)(2)(ii)(g); or
4. A fifty percent (50%) or more contemporaneous change in ownership of the members.

Adjustments shall be based on the fair market value of Company property on the date of the adjustment, and shall reflect the manner in which the unrealized income, gain, loss, or deduction inherent in the property (that has not previously been reflected in capital accounts) would be allocated among the members if there were a taxable disposition of the property for fair market value on that date.

If any Company asset has a book value that differs from the adjusted tax basis of that asset, then the capital accounts shall be adjusted in accordance with IRS Regulation Section 1.704-1(b)(2)(IV)(g) for allocations of depreciation, depletion, amortization, and gain or loss computed for book purposes rather than tax purposes.

If there is any basis adjustment pursuant to an election under IRS Section 754, then capital accounts shall be adjusted to the extent required by the IRS.

The Company is required to maintain for each member one or more capital accounts which reflect the member's separate distributive share of each class of Company income, gain, loss, deduction, or credit.
The principles governing the adjustments of each member's capital account is intended to satisfy the capital account maintenance requirements of IRS Regulation Section 1.704-1(b)(2)(IV) and shall be construed consistently therewith.

7.5 **Transfer of Capital Account.** In the event of a sale or exchange of some or all of a member's interest in the Company, the capital account of the transferring member shall become the capital account of the assignee to the extent it relates to the portion of the interest transferred.

**ARTICLE VIII. MANAGEMENT RESERVED TO MEMBERS**

The management of the Company shall be vested in its members in proportion to their contribution to the capital of the Company, as adjusted from time to time to properly reflect any additional contributions, withdrawals, or approved transfers by members. Such management may be accomplished through an Operating Manager, officer, or such other members as designated by the members to act on behalf of the members.

**ARTICLE IX. OFFICERS**

9.1 **Operating Manager.** The Operating Manager, if one is appointed, shall be the chief executive officer of the Company responsible for the general overall supervision of the business and affairs of the Company. He shall, when present, preside at all meetings of the members. The Operating Manager may sign, on behalf of the Company, such deeds, mortgages, bonds, contracts, or other instruments which have been appropriately authorized by the members to be executed, except in cases where the signing or execution thereof shall be expressly delegated by the members or by this Operating Agreement or by statute to some other officer or agent of the Company, and, in general, he shall perform all duties as may be prescribed by the members from time to time.

9.2 **Other Officers.** The Company may, at the discretion of the members, appoint additional officers, including, without limitation, one or more Vice-Operating Managers, one or more Secretaries, and one or more Treasurers. Such other officers need not be selected from among the members. One person may hold two or more offices. When the incumbent of an office is (as determined by the incumbent himself or by the members) unable to perform the duties thereof, or when there is no incumbent of an office (both such situations referred to hereafter as the "absence" of the officer), the duties of the office shall be performed by the person specified by the members.

9.3 **Election and Tenure.** The officers of the Company may be elected annually by the members at the annual meeting. Each officer shall hold office from the date of his election until the next annual meeting and until his successor shall have been elected, unless he shall sooner resign or be removed.

9.4 **Resignation and Removal.** Any officer may resign at any time by giving written notice to the Operating Manager, or to all of the other members, and unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective. Any officer may be removed at any time by the members with or without cause.

9.5 **Vacancies.** A vacancy in any office may be filled for the unexpired portion of the term by the members.

9.6 **Salaries.** The salaries (guaranteed payments) of the officers shall be fixed from time to time by the members and no officer shall be prevented from receiving such salary (guaranteed payment) by reason of the fact that he is also a member of the Company.
ARTICLE X. MISCELLANEOUS

10.1 Notice. Any notice required or permitted to be given pursuant to the provisions of any applicable statute, the Company's Articles of Organization, or this Operating Agreement, shall be effective as of the date that it is personally delivered, or if sent by mail, on the date deposited in the United States mail, postage prepaid and addressed to the intended receiver at his last known address as shown in the records of the Company.

10.2 Waiver of Notice. Whenever any notice is required to be given pursuant to the provisions of any applicable statute, the Company's Articles of Organization, or this Operating Agreement, a written waiver thereof, signed by the persons entitled to such notice, whether before or after the time stated therein, shall be deemed equivalent to the giving of such notice.

10.3 Indemnification by Company. The Company may indemnify any person who was or is a party defendant or is threatened to be made a party defendant to any threatened, pending, or completed action, suit or proceeding, whether civil, criminal, administrative, or investigative (other than an action by or in the right of the Company) by reason of the fact that he is or was a member of the Company, officer, employee, or agent of the Company, or is or was serving at the request of the Company, against expenses (including attorney's fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding if the members determine that he acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interest of the Company, and with respect to any criminal action or proceeding, has no reasonable cause to believe his conduct was unlawful. The termination of any action, suit, or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not in itself create a presumption that the person did or did not act in good faith and in a manner which he reasonably believed to be in the best interest of the Company, and, with respect to any criminal action or proceeding, had reasonable cause to believe that his conduct was unlawful.

10.4 Indemnification Funding. The Company shall fund the indemnification obligations provided by Section 10.3 in such manner and to such extent as the members may from time to time deem proper.

10.5 Duality of Interest Transactions. Members of the Company have a duty of undivided loyalty to the Company in all matters affecting the Company's interests.

10.6 Anticipated Transactions. Notwithstanding the provision of Section 10.5, it is anticipated that the members and officers will have other legal and financial relationships. Representatives of the Company, along with representatives of other entities, may from time to time, participate in the joint development of contracts and transactions designed to be fair and reasonable to each participant and to afford an aggregate benefit to all participants. Therefore, it is anticipated that the Company will desire to participate in such contracts and that the participation of the Company in such contracts and transactions may be authorized by the members.

10.7 Gender and Number. Whenever the context requires, the gender of all words used herein shall include masculine, feminine, and neuter, and the number of all words shall include the singular and plural thereof.

10.8 Articles and other Headings. The Articles and other headings contained in this Operating Agreement are for reference purposes only, and shall not affect the meaning and interpretation of the provisions.
10.9 **Reimbursement of Officers and Members.** Officers and members shall receive reimbursement for expenses reasonably incurred in the performance of their duties.

**ARTICLE XI.**

**DEATH OF A MEMBER**

11.1 **Death of a Member.** Upon the death of a member, the Company (or, if the Company shall determine not to purchase the interest of the deceased member, then each member on a pro rata basis) may: (1) purchase the interest of the deceased member in the Company at the value and terms provided below, (2) liquidate the Company business and terminate the Company, or (3) pursuant to the agreement of the parties, continue or form a new limited liability company with deceased member's estate or distributees as member(s). For the purpose of this Article "death of a member" shall mean and include: (a) death of an individual member, (b) death of the grantor under a living trust, and (c) death of an individual owning a controlling interest (fifty percent (50%) or more ownership) in a member corporation, partnership, or limited liability company.

11.2 **Election.** If the Company elects to continue the Company business and purchase the deceased member's interest, it shall serve notice in writing of such election within one hundred (100) days after the death of the deceased member. If the Company does not elect to purchase such interest, and the individual members so elect, then they shall serve notice in writing of such election within one hundred sixty (160) days after the date of the death of the deceased member. If all members do not wish to participate, and there is not otherwise a unanimous agreement, each member electing to participate shall be allowed to acquire the percentage interest of the interest being transferred as each participating member's current interest bears to the total current interests of all members electing to participate.

11.3 **Value.** The value of a deceased member's interest in the Company shall be his proportionate share of undistributed net income of the Company to the date of his death, unless included in his drawing account, and his percentage of membership interest multiplied by the value of the Company as agreed by the members and set forth in Exhibit "A" and incorporated herein by reference if a value has been established or re-established within the two (2) calendar years immediately preceding the death of a member. If no value has been established within the two (2) preceding calendar years, then the value established under Section 11.5 below shall be used.

11.4 **Agreed Value.** The value of the Company previously set forth in Section 11.3 of this Article is subject to change by the members executing Exhibit "A" attached to this Operating Agreement and on file in the office of the Company. The Company shall review not less frequently than annually after the end of each calendar year the fair market value of the Company's property, less its liabilities. The members shall then determine the value of the Company and shall set forth the amount of such value on Exhibit "A" attached hereto and incorporated herein by this reference, which value shall be based upon the fair market value of the Company assets after deduction of all liabilities therefrom; and each member shall then date and sign that amount. For the purpose of this agreement, if a value has been established or reaffirmed within the two (2) calendar years preceding the member's death, the last determination of the Company's value as so determined shall be binding upon all the members and their successors, assigns, administrators, and executors.

11.5 **Formula.** If the members have not agreed on the value of the Company as set forth in Section 11.4 of this Article for the two (2) consecutive calendar years immediately prior to the death of a member, the last agreement with respect to the value shall be disregarded. In that event, the determination as to the value of the member's interest in the Company shall be made by multiplying the member's capital ownership percentage times the adjusted capital
account of the Company. The adjusted capital shall be the capital account as calculated for
the preceding calendar year for income tax purposes with the following adjustments:

1. If a net loss has been incurred to the date of calculation, the loss shall be
deducted.

2. Equipment for the purposes of this valuation shall be valued at depreciated cost or
market value, whichever is lower.

3. Real estate shall be valued at market value.

4. No value for good will or firm name shall be included in any computations of a
member's interest under this Article.

5. Assets held as an interest in a corporation, partnership, or another limited liability
company shall be valued by valuing the separate assets (less liabilities) of the other
entity.

6. Should there be a disagreement regarding the "market value" of real estate, two
appraisers shall be selected to value the Company's real estate or real estate owned
through other entities. One appraiser shall be selected by the personal representative
or beneficiary of the deceased member and one appraiser selected by the continuing
members of the Company. The valuation arrived at by each appraiser shall be
combined and an average of the two shall be used as the "market value" for the
purpose of this valuation.

11.6 Unpaid Salary. Any unpaid salary (guaranteed payment) of a deceased member is
to be treated as an obligation of the Company to the member. The obligation shall be
paid within ninety (90) days after the death of such member.

11.7 Terms. If the Company or individual members shall elect to purchase the deceased
member's interest, then ten percent (10%) of the amount determined under this Article
shall be paid to the deceased member's estate within sixty (60) days after the notice of
interest to purchase is given. Any life insurance owned on the life of the deceased
member shall be used by the Company to the extent of the purchase price, to purchase
the interest of the deceased member and paid to the deceased member's representative
immediately upon receipt. Any insurance proceeds in excess of the amount due to the
deaded member's estate shall belong to and be the sole property of the continuing
Company. The balance of the amount due shall be paid in equal annual installments over
a period of ten (10) consecutive years, the first and each payment thereafter to be made
on the anniversary date of the ten percent (10%) down payment described herein. The
unpaid balance shall bear interest at the interest rate then provided for by Section 7872 of
the Internal Revenue Code of 1986, as amended, or any regulation promulgated
thereunder, with the right of the member or continuing Company to prepay any or all
payments.

ARTICLE XII.
AMENDMENTS

This Operating Agreement may be altered, amended, restated, or repealed and a new
Operating Agreement may be adopted by a majority vote of the members, after notice and
opportunity for discussion of the proposed alteration, amendment, restatement, or repeal.

CERTIFICATION
THE UNDERSIGNED, being all of the members of ____________________, L.L.C., a
limited liability company, hereby certify their adoption and
ratification of the foregoing Operating Agreement of the Company.
EXECUTED by each member on the date indicated.

Date: ___________________________ Member

Date: ___________________________ Member

Read more about the necessity of Operating Agreements in the NOLO article
The LCC Operating Agreement.

5. Dissolution
An LLC's operating agreement may establish a set termination date, at which time the LLC
will dissolve and the business go through a "winding up" process similar to the dissolution of
a corporation. Some state laws have required that an LLC may exist no longer than thirty
years, while other states permit LLC's to have a perpetual existence. Of course, an LLC may
be dissolved by agreement of the members.

6. Advantages/Disadvantages
Operating a business as a limited liability company provides the advantages of both a
corporation and a partnership.

- **Limited Liability**
  The members of a limited liability company are not personally liable for the debts of the
  company. Although such protection is available to shareholders of a corporation, it is not
  available to all partners of a partnership. Recall that partners operating a general partnership
  are personally liable for the debts of the business and at least one general partner in a limited
  partnership must be personally liable for the partnership's obligations.

- **Less Formality**
  A limited liability company may be operated with fewer formalities than a corporation. In
  this regard, an LLC resembles a partnership in its formation and operation. The degree of
  formality is determined by the LLC's operating agreement

- **Tax Advantage**
  A limited liability company is taxed as a partnership with profits and losses "passing
  through" to its members. Although this advantage is also available to Subchapter S
  corporations, a limited liability company is not subject to many of the restrictions that the
  IRS places on Subchapter S corporations, such as limiting a Subchapter S corporation to no
  more than 75 shareholders and prohibiting nonresident aliens from owning stock in the
  corporation.
■ **Perpetual Existence**
In some states, an LLC may be allowed perpetual existence similar to a corporation. Unlike a sole proprietorship, general partnership, or limited partnership, a corporation continues to exist despite the death or incompetence of a member.

As with any business organization, an LLC's advantages must be considered in light of its disadvantages.

■ **Decentralized Management**
In a member managed LLC, management of the business is retained by the company's members. Depending upon the number of members, such decentralization could result in poor communication and/or disagreement regarding management decisions.

■ **Conflict Among Members**
As with any organization, conflict among members is a potential hazard of a limited liability company. Members who hold a minority interest in the LLC may be continually outvoted. In addition, a poorly drafted operating agreement may cause more harm than good.

Review the [statutes](https://example.edu/statutes) of your state, or a state of your choice governing the creation, operation, and termination of a limited liability company. Statutes are available online at the Cornell University Law School Legal Information Institute.

Ask your instructor for assistance, if you have difficulty locating the statutes.

Also, determine if online limited liability company forms are available at the website of the chosen state's Secretary of State website. The South Dakota Secretary of State website is linked here as an example.

*Note:* Some Secretary of State websites include limited liability forms under corporation forms.

7. **Summary**
A limited liability company is a separate legal entity formed by filing of articles of organization in accordance with state law. An LLC combines the advantages of a partnership and a corporation. Similar to shareholders in a corporation, members are not personally liable for the debts of the business. However, the LLC requires fewer formalities to operate than a corporation and can avoid double-taxation experienced by corporations that do not qualify as a Subchapter S corporation. An LLC may be managed by its members or by a designated manager in accordance with the LLC's operating agreement.

F. **Comparing Business Entities**
Review the [Benefits and Drawback of Different Types of Business Entities](https://example.com) at Find Law.
ZINTER, Justice

[¶1.] At the start of each beekeeping season, Ellingson’s Inc. placed its honey bees on the real property of others, a common practice in the beekeeping industry. After Ellingson’s Inc. determined it would no longer own bees, it sought to lease to other beekeepers the right to place bees on the property of some of the landowners with whom Ellingson’s Inc. had been doing business. In the spring of 2011, Jim Ammann (Ammann), a competing beekeeper, sought permission to place his bees on the property of a number of the landowners who had previously given Ellingson’s Inc. permission to place bees. At least six landowners subsequently revoked the permission they had given Ellingson’s Inc. and granted Ammann permission to place his bees on their property. David Ellingson (David), a principal in Ellingson’s Inc., then sued Ammann for interference with a business relationship and other related causes of action. The circuit court granted summary judgment in favor of Ammann on procedural and substantive grounds. We affirm because David had no business interference claim that he could assert in his individual capacity.
Facts and Procedural History

[¶2.] David was the president of Ellingson’s Inc., a corporation involved in beekeeping and the manufacture and marketing of honey. During his years in the beekeeping business, David never personally owned bees outside of Ellingson’s Inc. As is common in the beekeeping industry, Ellingson’s Inc. placed its bees on the property of others during the honey-producing season. In return, at the close of each season, Ellingson’s Inc. provided the landowners with a package of honey, known as “yard rent.”

[¶3.] In the fall of 2010, Ellingson’s Inc. provided its landowners with a letter informing them that David would be retiring. The landowners were also informed that although some aspects of the business would continue, Ellingson’s Inc. would no longer own bees. However, the letter assured the landowners that Ellingson’s Inc. would arrange for other beekeepers to bring bees to the landowners’ property. The record reflects that Ellingson’s Inc. was planning to “lease” to other beekeepers the right to place bees on the landowners’ property.

[¶4.] South Dakota law requires that beekeepers file a permission slip, signed by each landowner, confirming that the beekeeper is authorized to place bees on the landowner’s property. In preparing for the 2011 season, Ellingson’s Inc. obtained permission slips from individual landowners in January 2011. In May 2011, David learned that six landowners cancelled the permission slips given to Ellingson’s Inc. and granted permission slips to Ammann.

[¶5.] David subsequently filed suit against Ammann for interference with a business relationship, fraud and misrepresentation, and unfair competition. After discovery, Ammann moved for summary judgment. The circuit court issued a memorandum decision granting Ammann’s motion. A final order was filed four days later. Although David contends there were issues of fact precluding summary judgment on the merits, it is only necessary to address two questions on appeal: (1) whether David was entitled to relief in his individual capacity, and (2) whether David is entitled to appellate attorney’s fees.

Decision

[¶6.] The circuit court first granted Ammann summary judgment reasoning that David was not entitled to relief in his individual capacity. “The general rule is that the corporation is looked upon as a separate legal entity until there is sufficient reason to the contrary.” Mobridge Cmty. Indus., Inc. v. Toure, Ltd., 273 N.W.2d 128, 132 (S.D. 1978). Further, “[e]very action shall be prosecuted in the name of the real party in interest.” SDCL 15-6-17(a). “The real party in interest rule is satisfied ‘if the one who brings the suit has a real, actual, material, or substantial interest in the subject matter of the action.’” Biegler v. Am. Family Mut. Ins. Co., 2001 S.D. 13, ¶ 27, 621 N.W.2d 592, 600. “The purpose of the real party in interest provision is to assure that a defendant is required only to defend an action brought by a proper party plaintiff and that such an action must be defended only once.” Id.

[¶7.] David brought this suit in his individual capacity. But David conceded that he “does not
and has never personally owned any bees, outside of Ellingson’s [Inc.].” Further, the “Bee Location Permission” slips, which granted the right to place bees on the landowners’ property, granted that right to Ellingson’s Inc., rather than David as an individual. Because David had no business expectancy with the landowners other than through Ellingson’s Inc., the circuit court did not err in granting summary judgment on the basis that David had no individual claims. [¶8.] On appeal, however, David argues that he “should have been given an opportunity to amend his complaint” and that the grant of summary judgment on this basis was “unduly harsh.” We disagree because David failed to seek this relief below. A memorandum decision is not a binding decision ending the case. Poindexter v. Hand Cnty. Bd. of Equalization, 1997 S.D. 71, ¶ 18, 565 N.W.2d 86, 91. “As its name implies, a memorandum opinion is merely an expression of the trial court’s opinion of facts and law.” Jones v. Jones, 334 N.W.2d 492, 494 (S.D. 1983). Therefore, “[i]t is the prerogative of the [circuit] court to re-think a decision from the bench or a memorandum decision.” Id. David did not ask the circuit court to reconsider or move to amend his complaint to substitute parties before the judgment became final. [¶9.] David also failed to seek relief from the final judgment. “On motion and upon such terms as are just, the court may relieve a party . . . from a final judgment, order, or proceeding[.]” SDCL 15-6-60(b). A party may seek such relief on the basis of “[m]istake, inadvertence, surprise or excusable neglect[.]” SDCL 15-6-60(b)(1). But David did not seek relief from the judgment on the ground of surprise or excusable neglect. [¶10.] David’s first request to amend his complaint was made in his reply brief filed with this Court. “A party may not raise an issue for the first time on appeal, especially in a reply brief when the other party does not have the opportunity to answer.” Agee v. Agee, 1996 S.D. 85, ¶ 21 n.4, 551 N.W.2d 804, 807 n.4; see also State v. Engesser, 2003 S.D. 47, ¶ 32, 661 N.W.2d 739, 750. Failing to raise an issue prior to appeal effectively serves as a waiver. Engesser, 2003 S.D. 47, ¶ 32, 661 N.W.2d at 750. Because David failed to move to amend his complaint before final judgment was entered, because he did not seek relief in the circuit court from the final judgment, and because he did not request to amend his complaint until his reply brief filed with this Court, David failed to preserve his appellate arguments that he should have been given the opportunity to amend his complaint and that summary judgment was unduly harsh. [¶11.] Given that David has no individual claims against Ammann, the circuit court’s summary judgment is affirmed. Because David was not the proper party plaintiff, we do not address the grant of summary judgment on the merits. [¶12.] David seeks appellate attorney’s fees under SDCL 15-26A-87.3. SDCL 15-26A-87.3 provides that appellate attorney’s fees may be sought “in actions where such fees may be allowable . . . .” “We have interpreted this to mean that appellate attorney fees may be granted ‘only where such fees are permissible at the trial level.’” Grynberg Exploration Corp. v. Puckett, 2004 S.D. 77, ¶ 33, 682 N.W.2d 317, 324. The failure to cite authority that “appellate attorney fees are proper in this type of action” serves as a waiver of the motion for attorney’s fees. SBS Fin. Servs., Inc. v. Plouf Family Trust, 2012 S.D. 67, ¶ 25, 821 N.W.2d 842, 847. Although
David’s motion demonstrates technical compliance with the requirements of SDCL 15-26A-87.3, his motion fails to demonstrate that “such fees [are] allowable[.]” See SDCL 15-26A-87.3. Further, David has not prevailed on appeal. Accordingly, David’s motion for appellate attorney’s fees is denied.

[13.] GILBERTSON, Chief Justice, and KONENKAMP, SEVERSON, and WILBUR, Justices, concur.

LIEN v. LIEN
2004 SD 8, 674 N.W.2d 816
(2004)

TIEDE, Circuit Judge.

Pete Lien & Sons, Inc. (PLS) was originally founded in 1944 as a partnership with Bruce Lien (Bruce), Charles Lien (Charles) and their father, Pete Lien, Sr., as the co-equal partners. The business operates in the quarrying and lime industries in the Rapid City area as well as several other states. PLS was incorporated in 1952 as a South Dakota corporation with the three partners as equal shareholders. Since its inception, PLS’s corporate governing documents have restricted the right of a shareholder to freely sell or transfer shares except to another shareholder. Over the years Pete Lien, Sr. gifted and sold stock to Bruce and Charles. When he died in 1969, Bruce and Charles inherited the remainder of his stock and each became fifty percent shareholders of the corporation. PLS authorized and issued both voting and non-voting stock.

PLS grew and prospered into a company with approximately 450 employees and an annual payroll of approximately $17 million. Both Bruce and Charles were actively involved in PLS. Bruce testified that he was responsible for most of the company's financing as well as seeking new opportunities for the company's expansion. Bruce resigned from PLS's executive committee in 1982, but continued to serve on the board of directors as the chairman. Charles served as president of PLS between 1982 and 1996. He was also chief operating officer from 1985 until 1996. At the time of trial, Bruce was 75 years old and Charles was 73 years old. While both diminished their day-to-day role in PLS in recent years, they continued to serve on the board of directors.

Bruce is married and has no children. Charles is married and has nine children (collectively referred to as the Nine Liens). Four of Charles' children are presently employed by PLS-defendants Pete Lien and Sandra Lien and defendants in intervention Suzanne Lien Gabrielson and Christian B. Lien (Four Liens). Pete Lien is the president of PLS and on the board of directors. Sandra Lien is currently vice president of corporate development for all PLS divisions. Suzanne Lien Gabrielson is chief financial officer. Also, two of the Four Liens have spouses that are employed in management positions with PLS. Several other children and grandchildren of Charles are either involved with contract work for PLS or work at PLS.
Bruce holds 50 percent of the voting and non-voting shares. Charles holds 50 percent of the voting shares, but has either sold or gifted some of his non-voting shares to his wife and each of his nine children. Over the years, Bruce executed various documents that demonstrated a willingness to either gift his shares in PLS or sell them at a favorable price to the Nine Liens during his lifetime or upon his death. However, all parties testified that it was understood that Bruce was under no obligation to do so.

The current board of directors for PLS consists of seven members. Four Lien family members- Bruce, defendants Charles, Pete Lien, and Sandra Lien, and three non-family, long-time employees-defendants Edwin Hubbeling, Jerrold Brown and Peter Birrenkott. Directors have not been elected since 1998.

Bruce and Charles have often disagreed as to the future direction of PLS. Bruce has pushed for the company to be sold privately or converted to a publicly owned corporation. Charles has resisted both alternatives although, on occasion, he has agreed to consider a proposal. Bruce and Charles are equally compensated from PLS. All dividends are distributed pro rata in accordance with the respective share holdings. As the holder of more shares in the corporation than any other single individual, Bruce receives more income and dividends than any other shareholder. However, as it relates to the distribution of dividends there has been considerable disagreement concerning whether to authorize dividends and, if so, in what amount.

Charles' vision is to preserve PLS for future generations of the Lien family by controlling present returns and thereby allowing for the growth of PLS. Generally, Charles advocates for the distribution of dividends only to meet the payment of a shareholder's individual income tax liability arising from the status of PLS as a subchapter S corporation. Whereas, Bruce wants to increase present returns and desires to maximize current payments of dividends. In support of this position, Bruce pursued a course of action involving subordinated notes. In this regard, Bruce requested that PLS declare dividends equal to 100 percent of net earnings for a year on the condition that the shareholders loan back those amounts to PLS. The shareholders would then receive notes subordinate to PLS's debt to its bank creditors. PLS would then pay interest to the shareholders on this subordinated debt in addition to payment of the principal on the loans. At Bruce's urging, PLS issued subordinated notes from 1992 to 1997.

In December 1998 a board meeting was held and the issue of payment of dividends was addressed. Charles made a motion, supported by his son Pete, to only pay dividends for the purposes of paying shareholders' tax liability until the corporation reduced its debt level to $8.5 million. This was contrary to Bruce's desire to issue subordinated notes. Despite Bruce's strong opposition to this motion, the other six directors agreed that it was not advisable to issue subordinated notes and determined that dividends would be paid for purposes of shareholder tax liability only. After this meeting, Bruce stated that he would vote against the existing board at the next shareholders’ meeting and elect directors that would vote as he desired. He further threatened that if he won control of the board of directors he would fire certain senior members of PLS's management. There was testimony that he contacted directors and told them they would be on his list unless they changed their vote on the issue of dividends, apologized to him for voting against his position as to dividends and resigned from the board.
In response to Bruce's threats, the board passed a resolution at the March 29, 1999, board meeting providing for a director qualification. The director qualification provided that no person could serve as a director unless he or she had previously served on the board or had been an officer of the corporation for at least five years. Bruce has not attended shareholders' meetings or directors' meetings since the passage of the director qualification resolution. Since Bruce and Charles each hold 50 percent of the voting shares in the corporation, Bruce's refusal to attend shareholders' meetings has resulted in the lack of a quorum for purposes of electing new directors.

In April 2000 Bruce brought this action against PLS and the other members of the board of directors alleging minority shareholder oppression, breach of fiduciary duty, and tortious interference with prospective business relations or expectancy. He later amended his complaint to seek dissolution of PLS under SDCL 47-7-34(3) on the grounds of shareholder deadlock. In December 2000 the remaining non-voting/non-director shareholders in PLS (defendants in intervention) filed a motion to intervene as defendants. Their motion was granted by the trial court.

On November 28, 2001, the trial court granted partial summary judgment to Bruce finding that there was shareholder deadlock in failing to elect directors for the requisite period of time as provided in SDCL 47-7-34(3) and ordered that a hearing be held to determine the most appropriate equitable remedy. A petition for intermediate appeal from the summary judgment was denied by this Court.

Following trial, the court entered findings of fact, conclusions of law and an amended judgment determining that the most equitable manner to break the existing deadlock was a blind auction between Bruce and all other shareholders for the sale of the corporation. The trial court included the Lien defendants, except PLS, and the defendants in intervention as comprising one faction competing with Bruce. The trial court set out the procedure to be followed and ordered that the corporation be liquidated in the event that neither faction is able to complete the purchase as directed. By separate findings of fact, conclusions of law and judgment, the trial court dismissed Bruce's claims of oppression, breach of fiduciary duty, and tortious interference with business relations or expectancy with prejudice.

This is a consolidation of three appeals filed as to this case. Defendants in intervention have filed an appeal of the trial court's amended judgment, along with the named defendants. Bruce also filed an appeal of the trial court's dismissal of his tort claims against the Lien defendants and non-Lien defendants.

......

**Whether the trial court erred in finding deadlock under SDCL 47-7-34(3).**

The trial court granted partial summary judgment by its order dated November 28, 2001, finding that there were no genuine issues of material fact and that as a matter of law there existed a deadlock under SDCL 47-7-34(3). The trial court ordered a hearing to determine the most appropriate equitable remedy to address the deadlock after which it determined the remedy to be a blind auction between the parties.
The trial court found that there was no genuine material dispute of fact that Bruce and Chuck each own 50 percent of the voting shares of PLS and that the shareholders have failed for at least two consecutive annual meetings to elect successor directors for those whose terms have expired. Those findings of fact are not clearly erroneous. "Once the facts have been determined, however, the application of a legal standard to those facts is a question of law reviewed de novo." . . .

SDCL 47-7-34(3) provides:

The circuit court shall have full power to liquidate the assets and business of a corporation in an action by a shareholder when it is established:

(3) That the shareholders are deadlocked in voting power, and have failed, for a period which included at least two consecutive annual meeting dates, to elect successors to directors whose terms have expired or would have expired upon the election of their successors;....

Reviewing the trial court's legal conclusions de novo, we do not agree that the facts as found by the trial court constitute deadlock under SDCL 47-7-34(3). There was no showing that the shareholders were deadlocked in voting power simply because Bruce refused to attend shareholders' meetings and participate in a vote as to election of directors. Bruce cannot artificially create a deadlock by refusing to attend and participate at shareholders' meetings and then seek an equitable remedy under SDCL 47-7-34(3). . . . The trial court concluded that there was voting deadlock because Bruce and Charles each hold 50 percent of the voting shares and they disagree as to their vision for the corporation. However, although there were several shareholders' meetings noticed to Bruce, there was never a tie in the vote for director candidates because Bruce refused to attend any of the meetings. If Bruce had attended a shareholders' meeting and a tie vote as to director candidates had resulted, SDCL 47-5-6(3) provided a statutory remedy for breaking a tie vote. SDCL 47-5-6(3) provides:

To render effective the cumulative voting rights provided by article XVII, section 5, of the Constitution of this state, and except as hereinafter provided, where several directors are to be elected for terms of the same duration:

... 

(3) If there exists a tie vote between candidates, with resulting failure of choice as to any place as director, such choice shall be determined by drawing of lots under such procedure that all rights of the candidates involved in such tie are adequately safeguarded.

If Bruce had attended a meeting, directors would have been elected because there would have been a drawing of lots to break any possible tie in the votes. However, the statutory
remedy of SDCL 47-5-6(3) for breaking a tie vote was not invoked because of Bruce's refusal to attend shareholders' meetings.

The trial court excused Bruce's refusal to attend shareholders' meetings by citing to the director qualification. Director qualifications are specifically authorized by SDCL 47-5-1. The trial court found that the directors adopted the director qualification after determining it to be in the company's best interests and that it was not oppressive or a breach of fiduciary duty. While the trial court points out that there were no prior formal director qualifications, a review of the record shows that in the more than fifty year history of the corporation only two directors have ever served that did not meet the director qualification passed by the board. Those two prior outside directors served some years ago and were specifically required by a bank as a condition of financing. The director qualification merely formalized what had been the policy followed by Chuck and Bruce for many years as to selection of directors. The record shows that PLS has thrived and prospered under this policy.

We cannot agree with the trial court's conclusion that the director qualification justified Bruce's refusal to attend shareholders' meetings. A shareholder may not boycott a shareholders' meeting and claim deadlock just because he does not believe that his position or arguments will carry the day. Even if the director qualification narrows the pool of eligible candidates from which Bruce may select directors, any director chosen has a fiduciary duty which obligates him or her to avoid acting as a rubber stamp for either side. Directors are held to a high degree of diligence and due care in the exercise of their fiduciary duties to shareholders. . .

While Bruce alleges that the director candidates eligible under the director qualification are nothing more than figureheads who will follow the wishes of Chuck, Bruce's own testimony is that he wished to elect directors that would be duty bound to act as he told them to act. We cannot and will not assume that any director elected hereafter, including any elected through the tie breaker statute, will not follow the law and exercise their own best judgment as to what action is in the best interests of PLS and all of its shareholders. Certainly, any director who would fail to do so acts at his or her own peril and at risk of liability to the shareholders for breach of fiduciary duty.

Therefore, we reverse the trial court and find as a matter of law that there is no deadlock under SDCL 47-7-34(3) on these facts.

. . .

**Whether the trial court erred in dismissing Bruce's causes of action for oppression, breach of fiduciary duty, tortious interference with business relations or expectancy and a claim for punitive damages with prejudice.**

The trial court entered a judgment dated October 1, 2002, dismissing Bruce's claims of oppression, breach of fiduciary duty, tortious interference with business relations or expectancy and a claim for punitive damages with prejudice. We affirm the trial court's dismissal of these claims.

"Whether conduct is oppressive is a legal conclusion." . . . Also, "[t]he existence of a fiduciary
duty and the scope of that duty are questions of law for the trial court. "... The trial court found that the defendants' actions were not oppressive or a breach of fiduciary duty. The trial court also found that the directors' actions were done in the best interests of the corporation. Bruce receives more income and dividends from PLS than any other single individual. While the record reveals he is disappointed and upset that the other directors have determined it is not in the best interests of the corporation to withdraw as much income from PLS as possible to satisfy Bruce's demands, this does not constitute a cause of action for oppression. Based on the trial court's findings of fact and the evidence presented, Bruce has failed to establish oppression as a matter of law.

Bruce further claimed that the director qualification amounted to tortious interference with his business relations or expectancy. He claimed that the director qualification interfered with his ability to sell his shares as well as reduced the value of his shares in the corporation. The essential elements of tortious interference with business relations or expectancy include:

(1) the existence of a valid business relationship or expectancy;
(2) knowledge by the interferer of the relationship or expectancy;
(3) an intentional and unjustified act of interference on the part of the interferer; (4) proof that the interference caused the harm sustained; and (5) damage to the party whose relationship or expectancy was disrupted.

... In Tibke, we held that to establish a 'valid business relationship or expectancy,' there had to be a showing of a 'contract or business relationship' between the plaintiff and an identifiable third party."... In order for Bruce to prevail on this claim, "there must be a 'triangle'-a plaintiff, an identifiable third party who wished to deal with the plaintiff, and the defendant who interfered with the plaintiff and the third party."... Based on Bruce's own testimony, there is no identifiable third party. Bruce testified as follows:

Q. Well, let me ask you this. Is it your testimony that you've never tried to sell your Pete Lien & Sons stock?

A. That's correct, I have never been real serious about it. I have delved into it to see what my options are to find out what it's worth but I've never really been serious about going through with it.

Q. Is that true even today? A. That true? Yes

Bruce cannot now claim a better version of the facts than he testified to himself... Therefore, Bruce cannot establish the first element of his claim of tortious interference and the trial court did not err in dismissing the claim.
Learning Plan 7

Acquiring & Transferring Property

A. Property Rights

The ability to own *property* in the United States is a fundamental right protected by the U.S. Constitution. The right to own private property is so important that it is included in the same sentence that protects life and liberty.

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No person shall be...deprived of life, liberty, or
property, without due process of law; nor shall private
property be taken for public use, without just
compensation.
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Amendment V, U.S. Constitution

The separate constitutions of the fifty states also contain provisions protecting private property.

Property and property ownership are among the first concepts learned in life. Indeed, one of the first words often spoken by a young child holding a toy is the word, "Mine!" We shall see, however, that property rights include much more than what is "yours" and what is "mine."

Generally, property can be defined as any *right* that can be owned and conveyed. As a legal concept, property does not consist of one right, but several rights. Such rights may be held by one owner or shared among several owners. Property rights may also be divided. For example, in a lease agreement, title to property may be separated from possession of the property.

B. Classification of Property

1. Tangible and Intangible Property
2. Real and Personal Property
3. Public and Private Property

Property can be classified in numerous ways, including tangible and intangible; real and personal; and public and private.
1. **Tangible and Intangible Property**

_Tangible property_ consists of items that can be seen and touched. When people think of property, they often think of tangible property, such as furniture and vehicles. However, property can also be intangible. _Intangible property_ is not physical, but nonetheless can be owned and transferred. Copyrights, trademarks, and investments are examples of intangible property.

Read the following articles that address the following categories of intangible property:

- Copyright
- Trademark
- Law Patent
- Law

The articles are presented by FindLaw and Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

2. **Real and Personal Property**

_Real property_ (often called real estate) is defined by state law and usually includes land and fixtures. A fixture is anything that is permanently attached to the land, such as trees and buildings. Fixtures within buildings are also considered real property. A bathroom sink, bathtub, kitchen cabinets, are all examples of fixtures.

_Personal property_ is generally defined as all property that is not real property. Personal property can be tangible or intangible. Tangible property can be something like an iPod or a car that has physical substance. Intangible property would be something such as stocks or bonds that represent some set of rights but has no real physical existence.

3. **Public and Private Property**

_Public property_ is property owned by the government, including Federal, state, and local governments. Public buildings, public parks, and government office furniture are examples of public property. _Private property_ is property owned by private persons, including corporations.

C. **Real Property**

1. Estates in Real Property
2. Acquiring Title to Real Property
3. Other Interests in Real Property
4. Restrictions on Use of Real Property

1. **Estates in Real Property**

Real property is governed by the state in which the property is situated. Many states utilize terms and concepts that originated in England to define and divide real property into different estates and interests.

Read the article [Real Property](https://www.wex.net/real-property) presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.
Fee Simple Absolute and Life Estate are two examples of estates in real property.

a. Fee Simple Absolute

*Fee simple absolute,* sometimes called fee simple or fee, is the greatest "bundle of rights" that may be acquired in a parcel of real property. A person who owns property in fee simple is entitled to use, possess or dispose of the property as he or she chooses during his or her lifetime. In addition, a person who holds property in fee can use, sell, lease, give away, and convey the property upon the fee holder's death. Fee simple absolute is what most people would consider owning real property.

b. Life Estate

A *life estate* is a lesser interest than fee simple absolute. In a life estate, a person (called the *life tenant*) can possess and use property during his/her lifetime, or the lifetime of designated person. Upon the death of the life tenant, or the designated person, the property passes to another designated person, called the *remainderman.*

*Example:* Farmer McDonald has two adult sons, Bill and Bob. The older son, Bill, stays on the farm and helps his father, while the younger son, Bob, moves to the city. Farmer McDonald wishes to provide for both of his sons after he dies, but does not wish to have the farm sold, because it provides the livelihood for Bill. After visiting with an attorney, Farmer McDonald makes his last will and testament, in which he leaves the farm to Bill during Bill's life, with remainder to Bob. Bill is the life tenant and Bob is the remainderman.

c. Shared Estates in Real Property

States allow two or more persons to share an ownership interest in real property under various forms of joint ownership.

1) Tenancy in Common

Two or more persons may share title to real property as *tenants in common.* Each tenant holds an *undivided interest* in the property. That is, each tenant has a right to use the entire parcel of property. One tenant may not exclude another tenant from using the property.

Tenants in common may hold different ownership interests in the property. For example, one person may own a two-thirds interest in the property, another person may own a one-sixth interest, and two other persons each own a one-twelfth interest. Each tenant may convey the tenant's interest during his/her lifetime or upon the tenant's death.

When more than one person receive title to real property, it is presumed that they receive title as tenants in common, unless specifically stated otherwise.

2) Joint Tenancy

When permitted by state law, two or more persons may hold title to real property as *joint tenants.* Although similar to a tenancy in common, joint tenancy includes the right of survivorship. When a joint tenant dies, the tenant's ownership interest passes to the
surviving joint tenants.

Like tenants in common, each joint tenant owns an undivided interest in the property, with the right to use the entire parcel of property. However, unlike tenants in common, joint tenants must each own an equal interest in the property.

A joint tenancy is created only when the conveyance clearly indicates the intention to create such tenancy. If a joint tenant conveys his/her interest during the joint tenant's lifetime, the joint tenancy is destroyed as the person receiving the joint tenant's share, who takes the share as a tenant in common.

(3) Tenancy by the Entirety
Several states recognize a tenancy by the entirety, which is essentially a joint tenancy between husband and wife.

(4) Community Property
Other states have enacted community property laws, which establish that all property acquired by personal efforts of spouses during a marriage is equally owned by husband and wife. Generally, separate gifts and inheritance are not considered community property.

d. Surface and Mineral Estates
In many states, it is possible to sever (separate) the mineral estate from the surface estate. As a result, it is possible for one person to own the surface of the property and another person to own the minerals below the surface. Mineral estates are especially common in oil producing regions in the western United States. State laws generally require that the surface owner be compensated for any damage done to the surface in the event of mineral production.

2. Acquiring Title to Real Property
Persons may acquire title to real property through various methods, including:
   a. Deeds and Conveyances
   b. Inheritance
   c. Adverse Possession
   d. Foreclosure
   e. Tax Deed
   f. Eminent Domain

a. Deeds and Conveyances
A person may acquire title to real property by a deed, a written document signed by the grantor and delivered to the grantee. The deed may be delivered as part of a sale or as a gift to the grantee.

The format and effect of deeds are governed by state law. Many states provide for different types of deeds that carry different levels of protection for the grantee. A warranty deed is a common type of deed that provides certain warranties or guarantees to the grantee. In many states, when a grantor signs and delivers a warranty deed, the grantor:
1. Warrants marketable title to the property
2. Warrants quiet and peaceable possession of the property
3. Warrants that no encumbrances (e.g., liens) affect the property, except as disclosed

In some states, the protections provided in a warranty deed are specifically listed in the deed. In other states, such warranties are provided by the use of statutorily defined words, such as "grant" and "warrant."

Prepared by:
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Justice City, SD 57709-1234
605.394.1234

WARRANTY DEED

_____________ and ______________, husband and wife, of ______________.
South Dakota ______, Grantors, for One Dollar ($1.00) and other good and valuable
consideration, GRANT, CONVEY and WARRANT to ______________ and ______________,
husband and wife, as joint tenants with right of survivorship and not as tenants in common,
Grantees, of ______________, ______________, the following-described real property
in ______________County, ______________:

The Northeast Quarter of the Southeast Quarter (NE1/4SE1/4), the
Southwest Quarter of the Southeast Quarter (SW1/4SE1/4), the Northeast
Quarter of the Southwest Quarter (NE1/4SW1/4), and the Southwest Quarter
of the Southwest Quarter (SW1/4SW1/4), all in Section Ten (10); and

The South Half of the Southeast Quarter (S1/2SE1/4) of Section Thirteen
(13); and

The Northeast Quarter of the Northeast Quarter (NE1/4NE1/4) and the
Southwest Quarter of the Northeast Quarter (SW1/4NE1/4) of Section
Fifteen (15); and

The South Half (S1/2) Lot Four (4) of Section Twenty-four (24),
All in Township Thirty-five North (T35N), Range Forty-one West (R41W) of
the Sixth Principal Meridian (6th P.M.), Pheasant County, South Dakota.

Executed the day and year stated in the acknowledgment.

Grantor

________________________

Grantor

STATE OF ______________  )
) SS.
COUNTY OF ______________  )
On this _____ day of ______________, 20___, before me, the undersigned notary public, personally appeared ______________ and ______________, husband and wife, known to me or satisfactorily proven to be the persons whose names are subscribed to the foregoing instrument and acknowledged that they executed the same for the purposes therein contained.

(S E A L)                      Notary Public

My commission expires: ______________

A **quitclaim deed** is another common form of deed. The quitclaim deed provides fewer protections than the warranty deed. Although a quitclaim deed can effectively convey title to real property, it is generally understood that a grantee who accepts a quitclaim deed takes title to the property "as is."

Generally, delivery of a deed conveys the grantor's entire interest in the property, unless the grantor expressly *reserves*, or withholds something from the conveyance. For example, a grantor may sign a warranty deed, but include a reservation in the deed, stating that the grantor reserves a right-of-way to cross the property.

Read the article [Real Estate Transactions](http://www.wex.net/real-estate), including the imbedded link, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

b. **Inheritance**

A person may acquire an interest in real property by inheritance. A will is the final declaration of how a person wishes to have his or her property disposed of upon his or her death. It is a formal instrument that must follow exactly the requirements of a state law to be effective. A will becomes effective only after death.

The person or persons who benefit from the will are called *beneficiaries*. The beneficiary often receives an *executor's deed* or *personal representative's deed* conveying title from the decedent's estate.

A person who dies without making a last will and testament directing the distribution of his/her estate is said to have died *intestate*. If the person owned real property died without a will, the property will be distributed to the decedent's heirs according to the state's intestate statutes.

c. **Adverse Possession**

When one party possess the property of another for a certain statutory period of time (three to thirty years depending on state law) that person acquires title to the land and cannot be removed from it by the original owner. In order to acquire property by adverse possession, four elements must be satisfied.
1. The possession must be actual and exclusive, meaning that the possessor must be the sole occupant of the property.
2. The possession must be open, visible and notorious, meaning that it must be so noticeable that the owner can be presumed to know of it. It cannot be a secret.
3. Possession must be continuous and peaceable for the required period of time. The possessor must not have been interrupted in the occupancy by the true owner or courts.
4. Possession must be hostile and adverse, meaning the possessor must claim the property as his or her own without the permission of the owner.

Generally, if all of these conditions are met, the adverse possessor must then bring a civil lawsuit (called a quiet title action in many states) and have a court enter a decree "quieting" title in the adverse possessor.

Review the YouTube video Adverse Possession 1 posted by camillewolpe to learn more about adverse possession.

d. **Tax Deed**
In some states, if a person does not timely pay real estate taxes on his/her real property, another person may pay the taxes and eventually acquire a tax deed to the premises, after notice. Often, the person must pay the taxes for several years (6 years in some states) before a tax deed will be issued. Similar to adverse possession, the tax deed holder usually must bring a quiet title action to have a court declare that he/she has good title to the property.

e. **Foreclosure**
A lender may acquire title to real property through foreclosure of its mortgage or real estate installment contract, if the borrower/buyer defaults in the terms of the secured loan or installment contract.

f. **Eminent Domain**
A governmental unit may obtain a parcel of real property for public purpose by exercising the power of eminent domain. Such power is often used to build or widen highways. Often, the governmental body will first attempt to negotiate a purchase from the landowner. If an agreement cannot be reached, the government may "condemn" the property and acquire title by eminent domain. Through a condemnation proceeding, the governmental unit will pay the landowner the reasonable value of the property, as determined by a court. In such case, private property is converted to public property through due process of law.

3. **Other Interests in Real Property**
A person or business may possess an interest in real property without holding title to the property. Easements and leases are common examples of such interests.

a. **Easement**
A person or business may have the right to cross property. Such rights are often called a right-of-way or an easement. Private roads, electric, telephone, and other utilities often rely on easements to cross real property without owning it.
PRIVATE ROAD EASEMENT

FOR VALUABLE CONSIDERATION, the receipt and sufficiency of which is acknowledged, 

[Blank], a single person, Grantor, of [Blank],
grants and conveys to [Blank], Grantee, of [Blank], a
non-exclusive Forty foot (40') wide private road easement over and across the following-
described servient tenement in [Blank] County, [Blank]:

for the purpose of ingress to, and egress from, the following-described dominant tenement in

[Blank] County, [Blank]:

the location of which easement is more particularly set forth in the attached Exhibit "A". Such
easement shall run with the land and be an appurtenance to the dominant tenement.

Signed the day and year stated in the acknowledgment.

[Blank]

Grantor

STATE OF [Blank] )
COUNTY OF [Blank] ) SS.

On this [Blank] day of [Blank], 20[Blank], before me, the undersigned notary
public, personally appeared [Blank], a single person, known to me or satisfactorily
proven to be the person whose name is subscribed to the foregoing instrument and
acknowledged that he executed the same for the purposes therein contained.

(S E A L) Notary Public

My commission expires: [Blank]

b. Lease

A lease is another extremely common method by which a person may use property without
owning it. A lease could be for an apartment, house, warehouse, office building, or farm and
ranch land. Although many states allow verbal leases, they often require that a lease that is
scheduled to last longer than one year must be written to be enforceable under the state's statute
of frauds. It is not unusual for leases of commercial property to last several years.
Read the article, Landlord-Tenant Law, including the imbedded link, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

LEASE AGREEMENT

THIS AGREEMENT is made by and between ___________________ and ___________________, husband and wife, of ___________________ (Landlords) and ___________________, of ___________________ (Tenant).

In consideration of the mutual promises and covenants contained herein, Landlords lease to Tenant and Tenant leases from Landlords the following-described premises on the terms and conditions set forth below.

1. **Premises.** The leased premises are situated in ________ County, _________ and described as follows:

   Lots Three (3) and Four (4) in Block Fifteen (15) of ____________

   Addition to the City of ________________, __________________________

   County, __________________________, including Landlords' interest in the _________________, located on the above-described real property.

2. **Term.** The initial term of this lease is ten (10) years, commencing at the execution of this lease and ending on the date ten (10) years thereafter, unless renewed or terminated as herein provided.

   At the expiration of the initial lease term, Landlord shall, at Tenant's option, lease to Tenant the above-described premises on the same terms and conditions, including the same rent, for an additional ten (10) years, with a like covenant for future renewals of the lease as is contained in this lease.

   Tenant may terminate this lease or subsequent renewals at any time by giving Landlords sixty (60) days prior written notice.

   The covenants contained in this section shall be construed as covenants running with the land and with the leasehold.

3. **Use.** Tenant may use and occupy the premises for the purpose of ________________.

4. **Utilities.** Tenant shall timely pay all utilities associated with the premises.

5. **Maintenance.** Tenant shall maintain the premises and keep them in good repair at her expense during the term of this lease. Major maintenance and repair of the premises not caused by Tenant's misuse, waste, or neglect, shall be the responsibility of Landlords. Tenant shall notify Landlords of the necessity of any major repair.

6. **Right of Entry.** After reasonable notice, Landlords may enter the premises at all reasonable times to inspect, maintain, and repair the same.
7. **Alterations.** Tenant may not make any significant alterations to the premises without Landlords’ prior approval.

8. **Assignment.** Tenant may not assign this lease or sublet the premises without Landlords’ prior written approval.

9. **Redelivery of Premises.** At the termination of this lease, Tenant shall quietly yield and redeliver the premises to Landlords in as good as condition as they are now, normal wear and tear excepted.

10. **Default.** Time is of the essence to this agreement. In the event Tenant defaults in any provision of this agreement, then Landlords shall give Tenant written notice of the nature of the default and Tenant shall have a period of thirty (30) days from receipt of such notice to correct such default.

11. **Remedies.** In the event Tenant fails to timely cure any default, after receipt of notice, Landlords may, at Landlords’ option, exercise any and all legal or equitable remedies available under the laws of the State of ____________________________________________.

   Failure to exercise any one or more remedies available to the Landlords upon default shall not be deemed as a waiver to exercise such remedies upon any future default.

12. **Binding Effect.** This agreement shall be binding upon and inure to the benefit of the parties, their heirs, legal representatives, and assigns.

13. **Entire Agreement.** This instrument constitutes the entire agreement of the parties and supersedes all previous communications, representations, or agreements, either verbal or written, between the parties. There may be no modification of this agreement, except in writing, executed with the same formalities as this instrument.

    Executed the day(s) and year stated in the acknowledgements.

    ____________________________________________
    Landlord

    ____________________________________________
    Landlord

    ____________________________________________
    Tenant

STATE OF _______________________) SS.
COUNTY OF _______________________

On this ___ day of ________, 20___, before me, the undersigned notary public, personally appeared ___________________ and __________________, husband and wife, known to me or satisfactorily proven to be the persons whose names are subscribed to the foregoing instrument and acknowledged that they executed the same for the purposes therein contained.
(S E A L) Notary Public

My commission expires: ____________________

STATE OF ________________  
SS. COUNTY OF ____________  

On this _____ day of ________________, 20___, before me, the undersigned notary public, personally appeared ________________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.

(S E A L) Notary Public

My commission expires: ____________________

4. Restrictions on Use of Real Property
Although a person or business may own real property, the owner is not free to use the property in any way that the owner wishes.

a. Government Restrictions
Various Federal, state, and local laws and regulations prevent an owner from using real property for unlawful purposes. Certainly, a person may not engage in criminal activity on his/her property, such as selling illegal drugs. However, local zoning and license requirements may prevent a landowner from operating an otherwise lawful business on his/her property. For example, many municipalities restrict the sale of liquor near a school, or the operation of a business in a residential neighborhood.

Although land use is usually a local government issue, the Federal government restricts the operation of certain activities that may have an adverse impact on the environment or may be regulated because the activity involves interstate commerce. For example, a landowner would be required to obtain a permit from the Federal government before beginning excavations for a surface coal mine or starting a toxic waste dump on the owner's property.

Read the article Land Use presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

b. Private Restrictions
A property owner's use of real property may also be limited by private restrictions called covenants. When purchasing real property, inquiry should be made to determine the existence of any covenants that may affect the intended use for the property. Covenants may be enforced if they do not violate any law or infringe any Constitutional protections.
SUBDIVISION
DECLARATION OF COVENANTS, CONDITIONS AND RESTRICTIONS

THIS DECLARATION is made by _____________________________, a __________________ corporation, with offices located at __________________________., __________________________.
Declarant, the owner of the following-described real property in __________ County, __________:

Declarant hereby declares that, from and after the recording of this Declaration, all the above-described property shall be held, sold, and conveyed subject to the following covenants, conditions and restrictions, which are declared to protect the value and desirability of, and which run with, the real property and be binding on all parties having any right, title or interest in the above-described tracts or any part thereof, their heirs, successors and assigns, and shall inure to the benefit of each owner thereof.

1. **Zoning Restrictions.** All tracts shall be governed by the rules and regulations imposed by the appropriate county planning and zoning authority. Any and all improvements and structures placed on any tract and other development of any tract shall comply to with such zoning requirements.

2. **Use of Tract.** Each tract shall be used for residential purposes only and shall not be used for any business, trade, commercial or industrial purpose whatsoever, except that individuals may conduct non-nuisance, unoffensive businesses from their homes.

3. **Single Family Dwelling.** No more than one single family dwelling shall be constructed or placed on any tract. Each single family dwelling shall consist of a minimum of 1,000 square feet of living space on the ground floor, not including an enclosed garage, car port, decks, porches, attached structures used for storage, or guest house. Any barn, shop, or detached garage shall be no more than one story tall, and shall consist of a minimum of 800 square feet and not more than 2,000 square feet of space.

4. **Owners' Association.** (a) Every owner of a tract shall be a member of the __________________Property Owners Association. An annual membership fee of $100.00 will be assessed to all members, except the Declarant, for snow removal and maintenance of subdivision roads, and for any costs and expenses incurred in enforcing these covenants and restrictions. The fee will be due the 1st day of July of each year and such fees, together with interest, costs and reasonable attorney's fees incurred in collecting delinquent fees, shall be a continuing lien against the property and the personal obligation of the person(s) who was the owner of the tract at the time the assessment became due. Membership fees not paid when due shall accrue interest at the statutory rate.

(b) When water is supplied to each owner's property by the Association, each owner shall pay the Association a tap fee and a monthly water charge to operate and maintain the subdivision water system. The amount of the tap fee and monthly charges shall be established by the Association, and may be amended from time to time. Such fees and charges, together with interest, costs and reasonable attorney's fees incurred in collecting delinquent fees, shall be a continuing lien against the property and the personal obligation of the person(s) who was the owner of the tract.
at the time the fees and charges became due. Fees and charges not paid when due shall accrue interest at the statutory rate.

(c) Declarant will collect, disburse, and account for membership fees and water charges until the election of officers of the Association, at which time the authority and responsibility for maintaining the roads and water system, enforcing these covenants and restrictions, and collecting, disbursing and accounting for fees and charges shall be transferred to the Association.

5. **Construction.** (a) All dwellings shall be newly constructed and of wood, stone, brick, or a combination of these materials. Such structures shall be of quality construction and shall harmonize with other structures and the surrounding terrain. To reduce the risk of fire, roofs of all structures shall be covered with asphalt, concrete, or tile shingles. No roof of any structure may be covered with wood or shake shingles. Manufactured homes that comply with the requirements contained in these Declarations are acceptable.

(b) No previously used dwelling, or trailer house, or mobile home, may be placed on any tract, except that a mobile home may be placed on a tract during the actual construction of a permanent residence. The mobile home and all connections and attachments shall be promptly removed from the tract after completion of the permanent residence. All construction shall be completed within eighteen (18) months of its commencement, unless such completion is prohibited by inclement weather or disaster.

6. **Appearance and Improvements.** All structures and improvements on each tract shall be maintained in a state of good repair, and shall be neat and well-kept in appearance. Brick exteriors shall be of an earth tone hue. All exterior surfaces, except roofs and stone and brick surfaces, shall be painted or stained in a muted earth tone color, or sealed with a clear sealer.

7. **Animals.** Two head of horses are permitted for each three acres within a tract, and shall be confined upon the owner's property. No other animals, other than domestic pets, are permitted within the subdivision.

8. **Annoyance.** No obnoxious or offensive activity shall be conducted on any tract or subdivision road, nor shall anything be done which may be, or may become, an annoyance or nuisance to other residents and owners of tracts in the subdivision. No firearms may be discharged within the subdivision.

9. **Garbage and Refuse Disposal.** No tract shall be used or maintained as a dumping ground for old vehicles, junk or rubbish. No garbage and other waste shall be kept, except in sanitary containers prior to removal. Individual owners shall remove garbage from their tract within a reasonable time, or use a garbage pickup service.

10. **Fences.** Barbed wire and plain wire fences are permitted, if they are kept in a state of good repair and do not interfere with access to any easement for utilities or roadways.

11. **Sewage Disposal.** Sewage disposal for each tract shall be accomplished by individual septic tanks. All septic tanks and disposal fields must be approved by the appropriate health authority. No cesspools or outside toilets are permitted.

12. **Enforcement.** The Property Owners' Association, or any owner of a tract, shall have the right to enforce, by any proceeding at law or in equity, all covenants, conditions, restrictions, liens, and charges now, or hereafter, imposed by the provisions of this Declaration. Failure by the Association or any owner to enforce any covenants or restrictions contained in this Declaration shall not be deemed as a waiver to enforce such covenant or restriction in the future.
13. **Severability.** Invalidation of any one of these covenants or restrictions by judgment or court order shall not affect any other provision of this Declaration, which shall remain in full force and effect.

14. **Duration.** The covenants and restrictions of this Declaration shall run with and bind the land for a term of twenty (20) years from the date of recording of this Declaration, after which time they shall be automatically extended for successive periods of ten (10) years.

15. **Amendment.** This Declaration may be amended during the first twenty (20) year period by an instrument signed by not less than seventy-five percent (75%) of the record owners of the tracts and recorded in the office of Register of Deeds of Pennington County, South Dakota. Thereafter, this Declaration may be amended by an instrument signed by not less than sixty-six and two-thirds percent (66-2/3%) of the record owners of the tracts and recorded in the office of Register of Deeds of _______________ County, ________________.

Executed the day and year stated in the acknowledgment.

(SEAL) By: __________________________

Authorized Agent

STATE OF __________________________

) SS.
COUNTY OF __________________________

On this _____ day of ________________, 20___, before me, the undersigned notary public, personally appeared ______________________, who acknowledged himself to be the Authorized Agent of ______________________, a __________ corporation, and that he, as such Agent, being authorized to do so, executed the foregoing instrument for the purposes therein contained, by signing the name of the corporation by himself as Authorized Agent.

IN WITNESS WHEREOF, I hereunto set my hand and official seal.

(SEAL) __________________________

Notary Public

My commission expires: __________________________

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**D. Personal Property**

1. **Ownership Interests in Personal Property**
2. **Transfer of Personal Property**

As previously mentioned, all property that is not real property (land and fixtures) is considered personal property. Personal property can be tangible or intangible.

1. **Ownership Interests in Personal Property**

As with real property, persons can hold sole title to personal property, or share title with other joint owners. In many states, such joint ownership may be either as joint tenants with right of survivorship, or as tenants in common, with the same attributes discussed above.
Personal property by the efforts of spouses in community property is deemed to be jointly owned by both spouses.

Similar to real property, title to personal property may be acquired by purchase, gift, or inheritance.

2. Transfer of Personal Property

In many cases, no particular formalities are necessary to transfer title to tangible personal property. A simple receipt may serve as proof of purchase. However, in other cases it is necessary to sign and deliver documents to transfer title. For example, when transferring title to a motor vehicle, it is necessary to sign and deliver the certificate of title to the buyer. It is also necessary to sign documents evidencing transfer of intangible personal property, such as shares of corporate stock and interests in a mutual fund.

Although it may not be required, when transferring title to a significant item of tangible personal property that does not have a certificate of title or other document of title, the buyer may wish to have the seller execute a simple bill of sale evidencing transfer of title. For example, if Wolfgang Amadeus Mozart purchased a grand piano from Johann Sebastian Bach for $500,000, he may wish to have Bach sign a Bill of Sale showing proof of the sale.

BILL OF SALE

FOR VALUABLE CONSIDERATION, the receipt and sufficiency of which is acknowledged, ________________, of ________________, GRANTS, SELLS, and TRANSFERS to ________________, of ________________, with offices located at _______________________, the following-described personal property:

The undersigned represents and warrants that he has good title to the above-described property, that the same is free of liens and encumbrances, and that he will defend title to the same.

Executed the day and year stated in the acknowledgment.

STATE OF _____________________

SS. COUNTY OF ________________

On this __________ day of _____________________, 20 ____, before me, the undersigned notary public, personally appeared __________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.

(S E A L) Notary Public

My commission expires: _____________________
Review the statutes of your state, or a state of your choice, that address:

- Ownership of property
- Transfer of property
- Leasing property

Statutes are available online at the Cornell University Law School Legal Information Institute. Ask your instructor for assistance, if you have difficulty locating the statutes.

**E. Summary**

The ownership of property is a fundamental right in the United States protected by the U.S. Constitution. Property can generally be defined as any right that can be owned and conveyed. Property does not consist of one right, but several rights. Such rights may be held by one owner or shared among several owners. Property can be classified as tangible and intangible; real and personal; and public and private. Laws and private covenants may restrict a landowner's use of property.

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Read the following case and any other cases assigned by your instructor.

**LEWIS v. ASLESEN**

2001 SD 131, 635 N.W.2d 744

(2001)

KONENKAMP, Justice.

In this case, we decide . . . whether the trial court erred in granting title by adverse possession to a portion of a strip of land between neighboring residential lots. . .

Although they were neighbors on friendly terms for over a quarter century, the Lewises and the Aslesens came to dispute the ownership of a 16-foot-wide strip of land running between their residential lots in Canton, South Dakota. According to the recorded deeds, the disputed property belonged to the Aslesens. They paid all the property tax on it. Both families used this strip for nonessential purposes since they purchased their adjoining lots in the same year, 1972. The uses differed, however. Where the Aslesens used the strip for sports, get-togethers, parking, and occasional access to their property, the Lewises planted three trees roughly along a line in the middle of it and a flower garden on a portion of it. Both families mowed it at various times between 1972 and 1999, the year this action was filed, and both shoveled snow from the sidewalk running across it.
To complicate the dispute, the Lewis's predecessor in title (Olson) had already sold the westernmost 9.8 feet of his lot to the Aslesen's predecessor in title (Robins). The result of this purchase was that the new property line between the lots passed through Olson's garage. The entrance of the driveway and most of its length lies wholly within the remainder of the Olson lot, but as the driveway curves toward the garage, it crosses over the legal boundary. When Olson sold the lot to the Lewises, he showed them a marker about 6.2 feet on the other side of the former boundary (a line at 86.3 feet). The Lewises believed that the line separating their property from that of the Aslesens was at the 92.5 foot mark, rather than at the 76.5 mark as stated on their deed.

Consistent with this belief, the Lewises planted trees and a garden roughly in the middle of the strip between their driveway and the 92.5-foot line, and they sprayed for weeds all the way to that line. The trial court found that the trees had been planted more than twenty years before the start of this action in 1999. The court ruled that the Lewises had established adverse possession of approximately 61% of the disputed strip, defined by a line at the westernmost of the two remaining trees (at the 87.4-foot line and running parallel to the eastern boundary of the Lewis property). The court also assessed against the Aslesens the cost of a new survey to ensure correct placement of the new property line.

On appeal, the Aslesens contend that the circuit court erred in concluding that the Lewises met their burden of proof in establishing the required elements for adverse possession. The Aslesens also challenge the award of disbursements.

The sufficiency of the evidence to constitute adverse possession presents a question of law. We review questions of law under a de novo standard and disbursement awards under the abuse of discretion standard. We give the trial court's factual findings substantial deference, overturning them only when they are clearly erroneous. Those claiming ownership to land through adverse possession must show that their possession was "actual, open, visible, notorious, continuous, and hostile" for over twenty years. Under SDCL 15-3-13, adverse possession can be established only if it "has been protected by a substantial enclosure or [if] it has been usually cultivated or improved." This statute thus provides a prerequisite to a justiciable adverse possession claim. Failure to show either a substantial enclosure or usual cultivation or improvement preempts the claim. Furthermore, adverse possession must be shown by clear and convincing evidence.

According to the expert testimony of Dr. John Ball, the trees planted by the Lewises had been growing on the property for more than twenty years, the period required to establish adverse possession. Planting and maintaining a line of trees on disputed property by those claiming adverse possession constitutes a substantial enclosure of the property under SDCL 15-3-13(1). In reference to the court's findings, the first prong of SDCL 15-3-13 applies here. In addition to planting and maintaining trees, regular mowing of the property constitutes cultivation under SDCL 15-3-13(2). The court's findings support the second prong of SDCL 15-3-13. Finally, landscaping is an improvement to land under SDCL 15-3-13(2). Although there was no claim here that the Lewis's garden planted in the disputed strip had been in existence for twenty
years, its presence for a substantial part of that time provides additional evidence that the Lewises were laying open claim to the property. As both alternative prongs of SDCL 15-3-13 have been satisfied, the prerequisites for adverse possession have been met.

It remains to decide whether the Lewis's possession of the disputed strip was actual, open, visible, notorious, continuous, and hostile for the entire twenty year period. Such a decision is highly fact-specific. Here, the line of trees marking a rough boundary line was open, visible, notorious, continuous, and hostile. So were the regular lawn mowing and snow shoveling, the perennial flower garden, and the spraying against weeds. Therefore, we affirm the trial court's judgment that the Lewises established adverse possession up to the line of trees. We also uphold the court's ruling that, to avoid future difficulties, it was prudent to set the precise boundary line just beyond the westernmost of the two remaining trees, i.e., at the 87.4-foot line.
Learning Plan 8

Agents & Employees

A. Agents
B. Independent Contractor vs. Employee
C. Federal Employment Laws
D. State Employment Laws

A. Agents

1. Authority of Agent
2. Termination of Authority
3. Relationship between Agents & Principals
4. Relationship with Third Parties

1. Authority of Agent

An agent is a person who has the authority to act for a principal. The extent of the agent’s authority is determined by the agency relationship and may be express, implied, or apparent.

a. Express Authority

Express authority exists when a principal explicitly grants to an agent the authority to act on behalf of the principal. Express authority may either limited or general in nature.

A principal may grant to an agent the limited authority to act for the principal in a particular situation or transaction. For example, Joe Cruiser may grant to Sam Seller, the limited authority to sell Joe’s car, while Joe is out of the country. In many instance, the principal signs and delivers to the agent a power of attorney as evidence of such authority. Today, many people sign a power of attorney granting to a family member or close friend the authority to consent or reject medical treatment of the principal, in the event that the principal is unable to make that health care decisions, because the principal is unconscious. Such document is often called a medical power of attorney or health care power of attorney.
LIMITED POWER OF ATTORNEY
TO SELL REAL ESTATE

I, ________________________, of ________________________, appoint my spouse, ________________________, my true and lawful attorney-in-fact for me and in my name, place, and stead, giving her full power to do and perform all and every act necessary to sell and convey to ________________________, my interest in the real property and selected items of personal property located at:

including the power sign the Purchase Agreement, Warranty Deed, Certificate of Real Estate Value, Seller’s Closing Statement, and all other documents required to complete the transaction, and every other power necessary to carry out the purposes for which this power is granted.

Executed on the date stated in the acknowledgment.

Principal

STATE OF ________________________ )
COUNTY OF ________________________ ) SS.

On this ______ day of ____________, 20____, before me, the undersigned officer, personally appeared ________________________, known to me or satisfactorily proven to be the person whose name is subscribed to the foregoing instrument and acknowledged that he executed the same for the purposes therein contained.

IN WITNESS WHEREOF, I hereunto set my hand and official seal.

(SEAL) Notary Public

My commission expires: ________________
LIMITED POWER OF ATTORNEY
Authority to Make Health Care Decision for Children

I, __________________, of _____________________________ (Telephone: ____________) 
appoint ___________________________ and __________________________, my true and lawful 
attorneys-in-fact for me and in my name, place, and stead, giving them full power to act either 
jointly or separately to consent to, to reject, or to withdraw consent for medical treatment or 
intervention, including dental care, provided for the health, care, and welfare of my children, ___ 
and __________________________________, including the authority to take and perform every act 
and thing whatsoever requisite, proper, or necessary to be done in the exercise of any of the 
rights and powers herein granted, as fully and for all intents and purposes as I might or could do 
if personally present, with full power of substitution or revocation, hereby ratifying and 
confirming all that my attorneys-in-fact, or their substitute or substitutes, shall lawfully do or 
cause to be done by virtue of this power of attorney and the rights and powers herein granted.

This power of attorney shall remain in effect until ____________, 20___, or revoked in 
writing, whichever occurs first.

Executed on the date stated in the acknowledgment.

Principal ________________________________

STATE OF ________________________________

SS. COUNTY OF __________________________

On this ______ day of ____________, 20___, before me, the undersigned officer, 
personally appeared __________________________, known to me or satisfactorily proven 
to be the person whose name is subscribed to the foregoing instrument and 
acknowledged that he executed the same for the purposes therein contained.

IN WITNESS WHEREOF, I hereunto set my hand and official seal.

(SEAL) ________________________________ Notary Public

My commission expires: ______________________

An agent may possess general authority to perform acts on behalf of the principal. Such 
authority may be granted through a general power of attorney, in which the principal 
grants to the agent the authority to perform any act that the principal could perform, if 
present.

In most cases, an agent is granted express authority without a written power of attorney. 
For example, an employee may be granted authority under his/her job description or by 
following verbal instructions given by the employee’s supervisor. In this situation, the 
employee is the agent and the employer is the principal.
b. **Implied Authority**
In addition to express authority, an agent may possess implied authority to take actions that are necessary to carry out the powers expressly granted by the principal to the agent. For example, an employee who is expressly authorized and directed to deposit funds in the employer’s bank account, is impliedly authorized to endorse any checks, so that they may be deposited.

c. **Apparent Authority**
In some instances, an agent may possess apparent authority, in which case the agent appears to possess authority, even if such authority was neither expressly nor impliedly granted by the principal. In those instances, the principal allows a third person to believe that the agent has the authority by the principal’s conduct. For example, if the employer allows an employee to wear a name tag with the title, -manager,- engraved on the name tag, a customer would reasonably believe that the employee had the authority to make decisions customarily made by a manager.

2. **Termination of Authority**
An agent’s authority to act for the principal may be terminated by:
   a. Agreement of the principal and
   b. Revocation by the principal
   c. Completion of the purpose of the agency
   d. Death or mental incapacity of the principal

An agent’s authority is always terminated by the death of the principal. The reason is that an agent can do no more than the principal could do. The same is true for the mental incapacity of the principal. However, in many states the authority of an agent may continue after the mental incapacity of the principal, if prior to such incapacity, the principal executes a durable power of attorney, which contains a clause such as:

   -This power of attorney shall not be affected by my disability or incapacity.-

A principal may also sign a power of attorney that does not take effect, unless the principal becomes incapacity. Many persons use this method to provide the management of their affairs if they are unable to do so themselves. In those cases, the power of attorney will contain a clause, such as:

   -This power of attorney shall become effective upon my disability or incapacity.-

3. **Relationship between Principals and Agents**
The principal and agent each owe the following duties to the other during the agency relationship:

<table>
<thead>
<tr>
<th>Agent's Duties Owed to Principal</th>
<th>Principal's Duties Owed to Agent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loyalty to the principal</td>
<td>Compensate the agent according to terms of agreement</td>
</tr>
<tr>
<td>Obey instructions of the principal</td>
<td>Reimburse the agent for expenses</td>
</tr>
<tr>
<td>Use reasonable skill and judgment</td>
<td>Indemnify and hold the agent harmless if a claim is made against the agent for actions taken with the scope of the agent's authority on behalf of the principal</td>
</tr>
<tr>
<td>Communicate with the principal</td>
<td></td>
</tr>
<tr>
<td>Account for funds received</td>
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</tbody>
</table>
4. **Relationship with Third Parties**
The principal is generally liable for all contracts made by an agent on the behalf of principal, within the scope of the agent’s authority. A principal is generally also liable for torts (e.g., personal injury or property damage) committed by the agent with the scope of the agent’s authority. A principal may not be liable if the agent acted outside the scope of the agent’s express, implied, or apparent authority.

Review the statutes of your state, or a state of your choice, which address the creation and termination of agencies. Statutes are available online at the Cornell University Law School Legal Information Institute.

Ask your instructor for assistance, if you have difficulty locating the statutes.

<table>
<thead>
<tr>
<th>B. Independent Contractor vs. Employee</th>
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<tbody>
<tr>
<td>1. Distinction</td>
</tr>
<tr>
<td>2. Independent Contractor</td>
</tr>
<tr>
<td>3. Employee</td>
</tr>
</tbody>
</table>

1. **Distinction**
An agent, who is compensated for services performed for the principal may be either an independent contractor or an employee. The distinction is important for several reasons, including the determination of liability for wrongdoings and responsibility for the payment of Federal income taxes and other withholdings.

According to the Internal Revenue Service, a person performing services for compensation may be an independent contractor, a common law employee, or a statutory employee. The determination of a person's status is critical for Federal income tax purposes. Generally, an employer must withhold income taxes, withhold and pay Social Security and Medicare taxes, and pay unemployment tax on wages paid to an employee. An employer is not generally required to withhold or pay any taxes on payments to independent contractors.

2. **Independent Contractor**
As a general rule, a person is an independent contractor if the person or organization for whom the service is performed has the right to control or direct only the result of the work done by the person and does not the means and methods of accomplishing the result. Examples of independent contractors include, private attorneys and building contractors are examples of independent contractors. Because those who hire an independent contractor has no control over the details of how they perform their work, independent contractors are not considered employees.

3. **Employee**
Employees can be classified into common law employees and statutory employees

   a. **Common Law Employee**
Courts have determined that anyone who performs services for compensation is considered an employee, if the person or organization for whom the service is performed can control what will be done and how it will be done, even if the employer gives the employee freedom
of action. What matters is that the employer has the right to control the details of how the
services are performed.

b. Statutory Law Employee
Some persons are defined as employees by statute. The IRS provides the following
examples of persons who are determined to be statutory employees for Federal income tax
purposes:

- A full-time traveling or city salesperson who solicits orders from wholesalers,
  restaurants, or similar establishments on behalf of a principal. The merchandise
  sold must be for resale (e.g., food sold to a restaurant) or for supplies used in the
  buyer's business.
- A full-time life insurance agent whose principal business activity is selling
  life insurance and/or annuity contracts for one life insurance company.
- An agent-driver or commission-driver engaged in distributing meat,
  vegetables, bakery goods, beverages (other than milk), or laundry or dry
  cleaning services.
- A home worker performing work on material or goods furnished by the employer.

Read the article Employment Law, including all linked material, presented by
Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and
hosted by the Legal Information Institute at Cornell Law School.

C. Federal Employment Laws
   1. Minimum Wage and Overtime Pay
   2. Safety and Health
   3. Child Labor
   4. Family and Medical Leave
   5. Lie Detector Tests
   6. Whistleblower Protection

The United States Department of Labor administers several Federal laws regulating employers
and employees, including laws governing minimum wages and overtime pay, safety and
health, child labor, family and medical leave, lie detector tests, and whistleblower protection.

Explore the website of the U.S. Department of Labor. Visit the various links,
including the Occupational Outlook Handbook.

The following information is adapted from information appearing on the U.S. Department of Labor's website at
http://www.dol.gov/compliance/guide/eppa.htm
1. Minimum Wage and Overtime Pay
The Fair Labor Standards Act of 1938 establishes standards for minimum wages, overtime pay, record-keeping, and child labor for more than 100 million workers, both full-time and part-time, in the private and public sectors.

The Act applies to businesses with employees who engage in interstate commerce, produce goods for interstate commerce, or handle, sell, or work on goods or materials that have been moved in or produced for interstate commerce. Generally, the Act only applies to businesses with at least $500,000 in annual dollar volume of revenue. The Act does not generally apply to businesses with less than $500,000/year revenue.

However, the Act does cover the following regardless of their dollar volume of business: hospitals; institutions primarily engaged in the care of the sick, aged, mentally ill, or disabled who reside on the premises; schools for children who are mentally, or physically disabled or gifted; preschools, elementary, and secondary schools and institutions of higher education; and federal, state, and local government agencies.

Employees of firms that do not meet the $500,000 annual dollar volume test may be covered in any workweek when they are individually engaged in interstate commerce, the production of goods for interstate commerce, or an activity that is closely related and directly essential to the production of such goods.

The Act covers domestic service workers, such as day workers, housekeepers, chauffeurs, cooks, or full-time babysitters, if they receive at least $1,300 (2001) in cash wages from one employer in a calendar year, or if they work a total of more than eight hours a week for one or more employers.

The Act exempts some employees from its overtime pay and minimum wage provisions, and it certain employees from the overtime pay provisions alone. The following are examples of employees exempt from both the minimum wage and overtime pay requirements:

- Executive, administrative, and professional employees (including teachers and academic administrative personnel in elementary and secondary schools), outside sales employees, and certain skilled computer professionals (as defined in the Department of Labor’s regulations)
- Employees of certain seasonal amusement or recreational establishments
- Employees of certain small newspapers and switchboard operators of small telephone companies
- Seamen employed on foreign vessels
- Employees engaged in fishing operations
- Employees engaged in newspaper delivery
- Farm workers employed on small farms (i.e., those that used less than 500 "man-days" of farm labor in any calendar quarter of the preceding calendar year)
- Casual babysitters and persons employed as companions to the elderly or infirm
The following are examples of employees exempt from the overtime pay requirements only:

- Certain commissioned employees of retail or service establishments
- Auto, truck, trailer, farm implement, boat, or aircraft salespersons employed by non-manufacturing establishments primarily engaged in selling these items to ultimate purchasers
- Auto, truck, or farm implement parts-clerks and mechanics employed by non-manufacturing establishments primarily engaged in selling these items to ultimate purchasers
- Railroad and air carrier employees, taxi drivers, certain employees of motor carriers, seamen on American vessels, and local delivery employees paid on approved trip rate plans
- Announcers, news editors, and chief engineers of certain non-metropolitan broadcasting stations
- Domestic service workers who reside in their employers' residences
- Employees of motion picture theaters
- Farmworkers.

The Act requires employers of covered employees who are not otherwise exempt to pay these employees a minimum wage of not less than $7.25 an hour as of July 24, 2009. Youths under 20 years of age may be paid a minimum wage of not less than $4.25 an hour during the first 90 consecutive calendar days of employment with an employer. Employers may not displace any employee to hire someone at the youth minimum wage.

Employers may pay employees on a piece-rate basis, as long as they receive at least the equivalent of the required minimum hourly wage rate. Employers of tipped employees (i.e., those who customarily and regularly receive more than $30 a month in tips) may consider such tips as part of their wages, but employers must pay a direct wage of at least $2.13 per hour if they claim a tip credit. They must also meet certain other conditions.

The Act also permits the employment of certain individuals at wage rates below the statutory minimum wage under certificates issued by the Department of Labor:

- Student learners (vocational education students)
- Full-time students in retail or service establishments, agriculture, or institutions of higher education
- Individuals whose earning or productive capacities for the work to be performed are impaired by physical or mental disabilities, including those related to age or injury

The Act does not limit either the number of hours in a day or the number of days in a week that an employer may require an employee to work, as long as the employee is at least 16 years old. Similarly, the Act does not limit the number of hours of overtime that may be
scheduled. However, the Act requires employers to pay covered employees not less than one and one-half times their regular rates of pay for all hours worked in excess of 40 in a workweek, unless the employees are otherwise exempt.

Employers must keep records on wages, hours, and other information as set forth in the Department of Labor's regulations. Most of this data is the type that employers generally maintain in ordinary business practice.

The U.S. Department of Labor uses a variety of remedies to enforce compliance with the Act's requirements. Willful violators may be prosecuted criminally and fined up to $10,000. A second conviction may result in imprisonment. Employers who willfully or repeatedly violate the minimum wage or overtime pay requirements are subject to civil money penalties of up to $1,000 per violation.

State laws also apply to employment subject to this Act. When both this Act and a state law apply, the law setting the higher standards must be observed.

Review the state minimum wage rates provided by the U.S. Department of Labor.

2. Safety and Health
In general, the Occupational Safety and Health Act of 1970 covers all employers and their employees in the 50 states, the District of Columbia, Puerto Rico, and other U.S. territories. Coverage is provided either directly by the federal Occupational Safety and Health Administration (OSHA) or by an OSHA-approved state job safety and health plan. Employees of the U.S. Postal Service also are covered.

The Act defines an employer as any "person engaged in a business affecting commerce who has employees, but does not include the United States or any state or political subdivision of a State." Therefore, the Act applies to employers and employees in such varied fields as manufacturing, construction, longshoring, agriculture, law and medicine, charity and disaster relief, organized labor, and private education. The Act establishes a separate program for federal government employees and extends coverage to state and local government employees only through the states with OSHA-approved plans.

The Act does not cover the following persons:

- Self-employed persons
- Farms which employ only immediate members of the farmer's family
- Working conditions for which other federal agencies, operating under the authority of other federal laws, regulate worker safety. This category includes most working conditions in mining, nuclear energy and nuclear weapons manufacture, and many aspects of the transportation industries
- Employees of state and local governments, unless they are in one of the states operating an OSHA-approved state plan
The Act assigns OSHA two regulatory functions: setting standards and conducting inspections to ensure that employers are providing safe and healthful workplaces. OSHA standards may require that employers adopt certain practices, means, methods, or processes reasonably necessary and appropriate to protect workers on the job. Employers must become familiar with the standards applicable to their establishments and eliminate hazards. Compliance with standards may include ensuring that employees have been provided with, have been effectively trained on, and use personal protective equipment when required for safety or health. Employees must comply with all rules and regulations that apply to their own actions and conduct.

Even in areas where OSHA has not set forth a standard addressing a specific hazard, employers are responsible for complying with the OSH Act's "general duty" clause. The general duty clause [Section 5(a)(1)] states that each employer "shall furnish . . . a place of employment which is free from recognized hazards that are causing or are likely to cause death or serious physical harm to his employees."

The Act encourages states to develop and operate their own job safety and health programs. OSHA approves and monitors these —state plans,— which operate under the authority of state law. There are currently 22 states and jurisdictions operating complete state plans (covering both the private sector and state and local government employees) and four (Connecticut, New Jersey, New York, and the Virgin Islands) that cover state and local government employees only. States with OSHA-approved job safety and health plans must set standards that are at least as effective as the equivalent federal standard. Most, but not all of the state plan states, adopt standards identical to the federal ones.

The Act grants employees several important rights. Among them are the right to complain to OSHA about safety and health conditions in their workplaces and, to the extent permitted by law, have their identities kept confidential from employers, contest the amount of time OSHA allows for correcting violations of standards, and participate in OSHA workplace inspections.

Private sector employees who exercise their rights under OSHA can be protected against employer reprisal, as described in Section 11(c) of the OSH Act. Employees must notify OSHA within 30 days of the time they learned of the alleged discriminatory action. OSHA will then investigate, and if it agrees that discrimination has occurred, OSHA will ask the employer to restore any lost benefits to the affected employee. If necessary, OSHA can initiate legal action against the employer. In such cases, the worker pays no legal fees. The OSHA-approved state plans have parallel employee rights provisions, including protections against employer reprisal.

A violation that has a direct relationship to job safety and health, but probably would not cause death or serious physical harm. A proposed penalty of up to $7,000 for each violation is discretionary. A violation where a substantial probability that death or serious physical harm could result and where the employer knew, or should have known, of the hazard. A penalty of up to $7,000 for each violation must be proposed. The Act provides that an employer who willfully violates the Act may be assessed a civil penalty of not more than $70,000 but not less than $5,000 for each violation.
If an employer is convicted of a willful violation of a standard that has resulted in the death of an employee, the offense is punishable by a court imposed fine or by imprisonment for up to six months, or both. A fine of up to $250,000 for an individual, or $500,000 for an organization [authorized under the Omnibus Crime Control Act of 1984 (1984 OCCA), not the OSH Act], may be imposed for a criminal conviction.

3. Child Labor
The Fair Labor Standards Act of 1970 contains provisions to protect the educational opportunities of youths and to prohibit their employment in jobs and under conditions detrimental to their health and well-being.

In nonagricultural work, the child labor provisions apply to enterprises with employees engaging in interstate commerce, producing goods for interstate commerce, or handling, selling, or working on goods or materials that have been moved in or produced for interstate commerce. For most firms, an annual dollar volume of business test of not less than $500,000 applies.

The Act covers the following employers regardless of their dollar volume of business: hospitals; institutions primarily engaged in the care of the sick, aged, mentally ill, or disabled who reside on the premises; schools for children who are mentally or physically disabled, or gifted; preschools, elementary and secondary schools, and institutions of higher education; and federal, state, and local government agencies.

Employees of organizations that do not meet the $500,000 annual dollar volume test may be covered in any workweek in which they are individually engaged in interstate commerce, the production of goods for interstate commerce, or an activity that is closely related and directly essential to the production of such goods.

While 16 is the minimum age for most nonfarm work, youths aged 14 and 15 may work outside of school hours in certain occupations under certain conditions. They may, at any age: deliver newspapers; perform in radio, television, movies, or theatrical productions; work for their parents in their solely owned nonfarm businesses (except in mining, manufacturing, or in any other occupation declared hazardous by the Secretary); or gather evergreens and make evergreen wreaths.

The child labor provisions include restrictions on hours of work and occupations for youths under age 16. These provisions also set forth 17 hazardous occupations orders for jobs that the Secretary has declared too dangerous for those under age 18 to perform.

Employers are subject to a civil money penalty of up to $11,000 ($10,000 for violations occurring prior to January 7, 2002) per worker for each violation of the child labor provisions. The Act also provides for a criminal fine of up to $10,000 upon conviction for a willful violation. For a second conviction for a willful violation, the Act provides for a fine of not more than $10,000 and imprisonment for up to six months, or both. The Secretary may also bring suit to obtain injunctions to restrain persons from violating the Act.
Many states have child labor laws. When both this Act and a state law apply, the law setting
the higher standards must be observed.

4. Family and Medical Leave
The Family and Medical Leave Act (FMLA) allows employees to balance their work and family
responsibilities by taking unpaid leave for certain reasons. The Act is intended to promote the
stability and economic security of families as well as the nation's interest in preserving the
integrity of families.

The FMLA applies to any employer in the private sector who engages in commerce, or in
any industry or activity affecting commerce, and who has 50 or more employees each
working day during at least 20 calendar weeks in the current or preceding calendar year.
The law covers all public agencies (state and local governments) and local education
agencies (schools, whether public or private). These employers do not need to meet the "50
employee" test. Title II of FMLA covers most federal employees, who are subject to
regulations issued by the Office of Personnel Management.

To be eligible for FMLA leave, an individual must (1) be employed by a covered employer
and work at a worksite within 75 miles of which that employer employs at least 50 people; (2)
have worked at least 12 months (which do not have to be consecutive) for the employer; and
(3) have worked at least 1,250 hours during the 12 months immediately before the date FMLA
leave begins.

The FMLA provides an entitlement of up to 12 weeks of job-protected, unpaid leave during any
12-month period for the following reasons:

- Birth and care of the employee's child, or placement for adoption or foster care of a
  child with the employee
- Care of an immediate family member (spouse, child, parent) who has a serious
  health condition
- Care of the employee's own serious health condition

If an employee was receiving group health benefits when leave began, an employer must
maintain them at the same level and in the same manner during periods of FMLA leave as if
the employee had continued to work. Usually, an employee may elect (or the employer may
require) the use of any accrued paid leave (vacation, sick, personal, etc.) for periods of unpaid
FMLA leave.

Employees may take FMLA leave in blocks of time less than the full 12 weeks on an
intermittent or reduced leave basis when medically necessary. Taking intermittent leave for the
placement, adoption, or foster care of a child is subject to the employer's approval. Intermittent
leave taken for the birth and care of a child is also subject to the employer's approval except for
pregnancy-related leave that would be leave for a serious health condition.

When the need for leave is foreseeable, an employee must give the employer at least 30 days
notice, or as much notice as is practicable. When the leave is not foreseeable, the employee must provide such notice as soon as possible.

An employer may require medical certification of a serious health condition from the employee's health care provider. An employer may also require periodic reports during the period of leave of the employee's status and intent to return to work, as well as "fitness-for-duty" certification upon return to work in appropriate situations.

An employee who returns from FMLA leave is entitled to be restored to the same or an equivalent job (defined as one with equivalent pay, benefits, responsibilities, etc.). The employee is not entitled to accrue benefits during periods of unpaid FMLA leave, but the employer must return him or her to employment with the same benefits at the same levels as existed when leave began.

Employers are required to post a notice for employees outlining the basic provisions of FMLA and are subject to a $100 civil money penalty per offense for willfully failing to post such notice. Employers are prohibited from discriminating against or interfering with employees who take FMLA leave. FMLA provides that eligible employees of covered employers have a right to take up to 12 weeks of job-protected leave in any 12-month period for qualifying events without interference or restraint from their employers. The FMLA also gives employees the right to file a complaint with the Wage and Hour Division of the Department of Labor's Employment Standards Administration, file a private lawsuit under the Act (or cause a complaint or lawsuit to be filed), and testify or cooperate in other ways with an investigation or lawsuit without being fired or discriminated against in any other manner.

Employees and other persons may file complaints with the Employment Standards Administration. The Department of Labor may file suit to ensure compliance and recover damages if a complaint cannot be resolved administratively. Employees also have private rights of action, without involvement of the Department of Labor, to correct violations and recover damages through the courts.

A number of states have family leave statutes. Nothing in the FMLA supersedes a provision of state law that is more beneficial to the employee, and employers must comply with the more beneficial provision. Under some circumstances, an employee with a disability may also have rights under the Americans with Disabilities Act.

5. Lie Detector Tests
The Employee Polygraph Protection Act (EPPA) prohibits most private employers from using lie detector tests, either for pre-employment screening or during the course of employment. The law does not cover federal, state, and local governments.

Employers generally may not require or request any employee or job applicant to take a lie detector test, or discharge, discipline, or discriminate against an employee or job applicant for refusing to take a test or for exercising other rights under the Act. Employers may not use or inquire about the results of a lie detector test or discharge or discriminate against an employee or job applicant on the basis of the results of a test, or for filing a complaint, or for participating in a proceeding under the Act.

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Subject to restrictions, the Act permits polygraph (a type of lie detector) tests to be administered to certain job applicants of security service firms (armored car, alarm, and guard) and of pharmaceutical manufacturers, distributors, and dispensers. The Act also permits polygraph testing of certain employees of private firms who are reasonably suspected of involvement in a workplace incident (theft, embezzlement, etc.) that resulted in specific economic loss or injury to the employer, subject to certain restrictions.

Where polygraph examinations are allowed, they are subject to strict standards for the conduct of the test, including the pretest, testing, and post-testing phases. An examiner must be licensed and bonded or have professional liability coverage. The Act strictly limits the disclosure of information obtained during a polygraph test.

The Secretary of Labor can bring court action to restrain violators and assess civil money penalties up to $10,000 per violation. An employer who violates the law may be liable to the employee or prospective employee for legal and equitable relief, including employment, reinstatement, promotion, and payment of lost wages and benefits.

The EPPA does not preempt any provision of any state or local law or any collective bargaining agreement that is more restrictive with respect to lie detector tests.

6. Whistleblower Protection

Under the Occupational Safety and Health Act (OSH Act), employees who believe that their employer has discriminated or retaliated against them for raising or reporting safety or health concerns may file a complaint with the Occupational Safety and Health Administration (OSHA). Under the Surface Transportation Assistance Act (STAA), employees in the trucking industry may file complaints with OSHA if they believe that their employer has discriminated against them for reporting safety concerns or for refusing to drive under dangerous circumstances or in violation of safety rules. Similarly, under the other statutes, employees also may file complaints with OSHA if they believe that their employer has discriminated against them for reporting protected safety concerns involving the airline or pipeline industries, for reporting protected environmental concerns including asbestos in schools, or for reporting potential securities fraud.

Generally, the employee protection provisions listed above prohibit an "employer" or any "person" (the definition of which may vary from statute to statute) from discharging or otherwise discriminating against any employee with respect to the employee's compensation, terms, conditions, or privileges of employment because the employee engaged in specified "protected" activities. The protected activities typically include:

- Initiating a proceeding under, or for the enforcement of, any of these statutes, or causing such a proceeding to be initiated
- Testifying in any such proceeding
- Assisting or participating in any such proceeding or in any other action to carry out the purposes of these statutes
- Complaining about a violation
D. State Employment Laws

Each state has enacted various laws regulating employment within the state.

Explore the website of the state labor office of your state, or a state of your choice.

Review the statutes of your state, or a state of your choice, which address labor and employment. Statutes are available online at the Cornell University Law School Legal Information Institute.

Ask your instructor for assistance, if you have difficulty locating the statutes.

Read the following case and any other cases assigned by your instructor.

**SAFFOLD v. CONWAY & ASSOC., INC., et al.**  

Judge Glen A. Tyler

In this chancery suit for specific performance, the Court must decide whether the evidence presented upon trial of the cause, *ore tenus*, is sufficient to establish that one of four owners of a parcel of real estate had authority from the other three, as their agent, to bind them by a written sales agreement signed by the purported agent, and thus be sufficient to permit the Court to compel all four owners to convey the property to the purchasers.

The Bill of Complaint alleges, among other things, and the Answer of all Respondents admits, that a certain parcel of real property in Bay Creek subdivision in Cape Charles, which is the subject of this suit, is owned by deed dated December 3, 2002, in one-half undivided interest by Timothy E Nagle and Maureen E Meehan, husband and wife, as tenants by the entireties, and one-half undivided interest by John D. Conway and Frances D. Conway, husband and wife, as tenants by the entireties. The Bill further alleges that Timothy E. Nagle signed written documents, including a "Virginia Association of Realtors Form Contract for Purchase of Unimproved Property," and an attached letter memorandum, accepting the offer of the Complainants, Scott H. Saffold and Detra R. Saffold, husband and wife, to purchase the property for the sum of $410,000. The Bill alleges that Nagle executed the documents for himself and as the authorized agent for the remaining three owners, binding them to convey. The allegation of agency is denied in the Answer of the Respondents creating the dispute in this litigation. The Complainants contend that they are ready, willing, and able to purchase, that the Respondents are bound to convey, that they have refused to do so, and are thus in breach of their agreement. Complainants sue to compel conveyance and for attorney's fees as allowed in the agreement.

The Bill of Complaint does not allege that the four owners of the subject property are
members of a partnership or engaged in a joint venture with respect to the property. The essential facts are uncomplicated. The owners of the property in question decided to sell their parcel of land and engaged the services of Paul G. Watson, III, of Watson Realty, as their real estate agent to find a buyer. Around the same time, the hopeful purchasers engaged the services of another real estate agent, Jon E. Paul of Parr Properties, to find a parcel of property for them. The two real estate agents learned of their mutual goals and communicated with one another, concluding that the sale and purchase was suitable. Watson provided inaccurate information to Paul about the names of the owners of the property, stating that they were "John Conway, David Hopkins, and Timothy Nagle." Paul, without further inquiry, used those names in writing the form offer dated July 22, 2003.

In response to the offer, Timothy Nagle sent a letter to Watson on the letterhead of Conway & Assoc., Inc., dated July 24, 2003, providing five additional terms and conditions to be included in the agreement. In the letter Nagle also stated "we will accept the offer. . .‖ (Emphasis added.) Nagle did not comment specifically upon the inaccurate recitation in the written offer of the names of the owners. What he stated in his letter in that regard was, "Vesting is as follows [sic] Tim Nagel and Maureen Meehan 1/3; John and Frances Conway 1/3; Conway & Associates, Inc., a California corporation 1/3." 1 Nagle stated in testimony that the word "Vesting" was a word indicating ownership. However, it is obvious that, at the time he wrote the letter, he really meant that was how the sales proceeds were to be credited or distributed. He is bound to have known how the deed titled the property. Nagle wrote further in the letter, "If it is acceptable (presumably, if the five terms and conditions are acceptable to the purchasers), I will annotate the offer to include the terms of this memo." (presumably, incorporate the five terms and conditions into the form agreement by writing or typing them in). (Emphasis added.) However, Nagle also wrote in the letter to Watson, "Please send all correspondence and/or documents to me which I will forward/circulate." In testimony Nagle interpreted this ambiguous language, specifically the word "circulate," to mean to get approval from the other owners, not just to inform them of what he was doing, since he at all times in his testimony denied his agency.

The final contract was the Realtors form agreement to which Nagle's letter of July 24 was attached as a part. Nagle had signed the letter and signed and dated each page of the agreement, including the signature page.

The Saffolds signed the form agreement and the attached letter, all together constituting the contract. Final signatures were secured on July 28, 2003. A signature line on the signature page of the form agreement, under which there were typed the names "John Conway, David Hopkins," contained no signature. Timothy Nagle signed on the signature line under which his name was typed. Nagle did not sign for anyone else. The names of the two wives appear nowhere in the agreement or attached letter.

In the form-language body of the agreement regarding deposit, the agreement stated in paragraph 4 "Purchaser has made a Deposit with Watson Realty (the Escrow Agent) of Ten Thousand Dollars. . ." However, that had not actually happened. In explanation, the agreement included a typed-in provision stating "The deposit referenced in paragraph 4 herein shall be delivered to Watson Realty no later than five business days from acceptance and ratification of
this contract." That was because the purchasers' money was being held by an intermediary, contemplating an Internal Revenue Code § 1031 like-kind exchange. Eleven days after the contract was finally signed by Nagle and the purchasers, on August 8, 2003, an attorney representing the purchasers, Robert C. Oliver, Jr., wrote Watson telling him that he, Oliver, had the Saffold's $10,000 deposit available to be picked up. Then, he wrote in his letter "Please have the remaining owners sign the contract as Mr. Nagle agreed that they would."

The next day, August 9, 2003, Nagle sent a letter to Watson. Contrary to Nagle's testimony at trial, this letter compels the obvious conclusion that Nagle was not confused, as he claimed, about the two provisions in the contract regarding the deposit. The purpose of the August 9th letter is found in Nagle's statement therein to Watson that "If the buyer does not complete their

[sic] specific obligations under the agreement (e.g. delivery of the down payment), you have our authorization to cancel the agreement. . . ." (Emphasis added.) Furthermore, contrary to Nagle's testimony, it is indeed inescapable that he must have believed that there had been "acceptance and ratification" of the agreement and that the window regarding delivery of the deposit had remained open for five and more days and that there was already a binding agreement subject to being cancelled.

On August 11, 2003, the realtor, Jon Paul, hand-delivered a letter and the $10,000 deposit by cashier's check to Watson, who rejected it on behalf of Nagle.² As a result, a meeting was arranged for August 13, 2003, among Nagle, Watson, and Robert Oliver (an attorney who has practiced real estate law in Northampton County for 35 years). Oliver testified that, upon his again asking Nagle to have the other three owners sign the contract, Nagle told Oliver he could speak for the others. Nagle denied it in testimony, even in the face of Oliver's contemporaneous written memorandum of Nagle's statement to him.

On August 22, 2003, Paul sent a letter to C. Albert Turner, III, attorney for Nagle, advising of the Saffolds' compliance with the financing contingency in the agreement and of the removal of all other purchaser contingencies. On August 26, 2003, Turner responded by letter to Oliver to advise that Nagle "does not view the . . . contract as binding. . . ." and that "the owners . . . were entitled to conclude that, when the deposit was not timely made, there was no binding contract" and "Nagel does not agree that he made any representations that he was an for the other owners."

The fat was in the fire.

The Court will first review the general rules of agency as they apply in circumstances where there is no express authority for the purported agent, Timothy Nagle, to bind the purported principals, Maureen Meehan, John Conway, and Frances Conway. There is credible evidence from the alleged agent, as the foregoing review of the testimony and documents in this case discloses, that the alleged agent by words and actions appeared to be an agent for the other three owners authorized to sell, if not convey, their real property. But from what source must the evidence come in order to prove that an alleged principal has clothed an alleged agent with
authority to execute a binding contract for the sale of real estate? We can eliminate the creation of agency by estoppel. In order for the doctrine of estoppel to apply (to prevent the putative principal from pleading lack of authority), there must be words, actions, or failures to speak or act by the principal which are misleading or which the principal should know are misleading, causing the person dealing with the agent to act to his detriment. There is no evidence here that any of the three principals said or did anything misleading.

Probably the owners did authorize Timothy Nagle to conduct all the business affairs and sign all the documents necessary to consummate an agreement to sell their real estate. But Robert Oliver, possibly clairvoyant, recognized the difficulties surrounding proof in such cases. In order to establish apparent agency, the burden of proof is upon the party dealing with the agent to establish the agency by clear and convincing evidence. *Hartzell Fan, Inc. v. Waco, Inc.*, 256 Va. 294, 505 S.E.2d 196 (1998). A purchaser dealing with an agent authorized to sell land must inquire into the extent of the agent's authority and deal with the agent at his peril. *Payne v. Jennings*, 144 Va. 126, 131 S.E. 209 (1926).

The general rule of agency is that authority in the agent is created by written or spoken words of the principal or by conduct of the principal. And apparent authority is created as to third persons by the same words and conduct of the principal that the principal consents to the acts of the agent on the principal's behalf. Restatement (Second) of Agency, §§ 26, 27 (1958). An agent has no apparent authority to a stranger who does not know of the reputation or past conduct of the agent. Restatement (Second) of Agency, § 27, cmt. 6 (1958).

The intention of a principal and an agent to create the fiduciary relationship of agency must find expression either in words or conduct between them. The existence of the relationship is a fact to be proved by tracing it to some act of the alleged principal. 3 Am. Jur. 2d, *Agency*, § 15 (2002). An implied agency may be proved by deductions or inferences from the facts and circumstances of the case, provided there is a natural and reasonable construction of the facts and circumstances. *Id.* at § 16. The party asserting agency must demonstrate that the principal, by his conduct, caused the party to believe that the alleged agent was indeed an agent for the principal. 3 Am. Jur. 2d, *Agency*, § 342 (2002). There is no presumption of agency. And the relation of husband and wife does not raise a presumption of agency. *Id.* at § 343.

Actually, the extrajudicial statements of the alleged agent are not admissible to prove the fact of the agency. They were admitted, nevertheless, but their weight is suspect for that particular purpose. A purported agent cannot unilaterally create an apparent agency through his own words or conduct. 3 Am. Jur. 2d, *Agency*, § 347 (2002). When from extrinsic evidence a prima facie case of agency is made out, then the agent's declarations and statements become competent. *Royal Indemnity Co. v. Hook*, 155 Va. 956, 157 S.E. 414 (1930). There must be other competent evidence establishing the fact of agency other than the declarations, acts, or conduct of the agent, or the declarations, acts, and conduct of the agent must be of such a character as to justify an inference that the principal knew of them and would not have permitted them if unauthorized. *Bardach v. Charleston Port Terminals*, 143 Va. 656, 657, 129 S.E. 687 (1925). The authority disclosed by the declarations, actions, and conduct of a principal must be sufficient to prove clearly and convincingly not just that the agent had

In *Morris v. Mosby*, 227 Va. 517, 317 S.E.2d 493 (1984), there were spoken words, significant relationships, and substantial conduct of the principal, John Morris, illustrating the existence of an agency. Importantly, John Morris, the principal, was at all times during the transaction aware of the agent's actions and that such actions were inescapably those of an agent acting on his behalf. The most important fact was that John Morris knew the real estate agent was going to prepare the agreement in final form and return to John's office with it but John knew only his son, Richard, would be there to sign it and that expeditious action was crucial.

This Court must conclude, sadly for the innocent Saffolds, that there is not in this case evidence from the necessary source, the alleged principals, sufficient to prove clearly and convincingly that Timothy Nagle was their agent authorized to execute a real estate sales contract on their behalf. The Bill of Complaint will be dismissed.
Credit & Bankruptcy

A. Credit & Secured Transactions
   1. Secured Debt
   2. Unsecured Debt
   3. Consumer Lending Regulations
   4. Debt Collection Practices
   5. Summary

A debt is an obligation for money owed to a creditor. Generally, debt can be divided into two categories: secured debt and unsecured debt.

1. Secured Debt
Secured debt refers to any debt in which the creditor possesses a lien or security interest in property of the debtor. The property, often called "collateral," may be either real property (land and fixtures) or personal property (everything other than real property, such as automobiles and furniture).

   a. Real Property
   Typically, a person grants a creditor a lien on real property by signing a mortgage or trust deed. Often when a person buys a house, they obtain a loan that is secured by a mortgage. (Sometimes people say that the bank owns their house. In reality, the bank does not own the house, but possesses a mortgage lien on the property). If the borrower does not pay the debt, then the lender may foreclose the mortgage according to state law. (In some states, the borrower gives the lender a trust deed instead of a mortgage. If those cases, the lender forecloses its trust deed according to state procedures)

   A creditor may also obtain a lien on real property through other means, such as a mechanic's lien, which is usually a lien filed against the property by a contractor who has not been paid for materials or services furnished to the property.

   If a judgment is entered against a person for an obligation unrelated to real property (for example failure to pay a credit card balance), the judgment may become a judgment lien against the person's real property.

   b. Personal Property
   A person may grant a lender a security interest (lien) in personal property by signing a
security agreement and a "financing statement" in accordance with Article 9 of the Uniform Commercial Code, as adopted by that state. The Uniform Commercial Code defines a security interest as an interest or legal right in personal property or fixtures to secure payment or performance of an obligation. If the borrower does not pay the debt, then the creditor may repossess the property (called "collateral") under strict conditions set forth by statute, or may foreclose its security interest and obtain a judgment directing the sale of the collateral, with the sale proceeds applied to the debt.

Creditors often take action to inform other creditors and the public that they possess a security interest in a debtor's personal property. In such cases, a creditor is said to "perfect" the security interest. The type of action necessary to perfect a security interest depends upon the type personal property. Often, state law provides that a creditor must file a UCC Financing Statement with the designated state office, often the Secretary of State. However, a security interest in certain types of personal property may only be perfected a certain way. For example, most states require that a security interest (lien) on a motor vehicle must be noted directly on the vehicle's certificate of title. Filing a UCC Financing Statement with the Secretary of State would be ineffective. Having a perfected security interest becomes very important when two or more creditors seek to enforce their debt against the same item of personal property. The creditor who has perfected first is said to have priority.

2. Unsecured Debt

Unsecured debt refers to debt that is not secured by collateral. Examples of unsecured debt include student loans, credit cards, and medical bills. If a person fails to pay an unsecured debt, the creditor may bring a civil lawsuit and obtain a money judgment against the debtor. The judgment creditor may attempt to enforce the judgment through various post-judgment enforcement methods discussed in the next section.

The following is an example of a simple promissory note, which creates a debt, followed by a mortgage, which creates a mortgage lien on real property to secure the debt.
PROMISSORY NOTE

FOR VALUE RECEIVED, ______________________ and ______________________,
husband and wife, Payors, of ______________________ ______________________;
jointly and severally promise to pay to the order of

______________________________ ______________________,
Payee, at ______________________ ______________________,
the sum of ______________________ ______________________ Dollars
($________________), with interest accruing at the rate of _________ percent

(_______ %) per annum ______________________, 20___, payable in annual from
principal and interest installments of ______________________ ______________________ Dollars

($________); the first installment due the _____ the day of
20___, and a like installment due the _____ the day of each and every
______________________________
thereafter, with the final installment due the___ the day of _________________, 20___.

A late charge of $_____________ shall be added to each installment which is not
received by Payee within ten (10) days of its due date.

Time is of the essence. In the event Payors fail to pay any installment when due, or fail to
comply with any of the provisions of the mortgages securing this note, Payee may declare the
total unpaid balance immediately due and payable, upon twenty (20) days notice to Payors,
and may exercise all legal and equitable rights and remedies available under South Dakota
law and Federal law, including the recovery of attorney's fees and disbursements, as allowed
by law. Payee's failure to exercise any right or remedy shall not prevent Payee from
exercising such right or remedy in the future.

Payors may prepay any amount of the principal balance at any time, without penalty. Any
such prepayments shall be applied to reduce the unmatured principal balance, but shall not
postpone or defer the obligations to make payments in accordance with the above-stated
schedule.

This note shall be construed in accordance with the laws of the State of South Dakota
and is secured by mortgages on certain real property in ____________ County, South Dakota.

Executed the day and year stated in the acknowledgment.

Payor

Payor

STATE OF _____________________________ )

) SS.

COUNTY OF ___________________________

On this _____ day of ________________, 20__, before me the undersigned officer, personally appeared ___________________________ and

____________________, husband and wife, known to me or satisfactorily proven to be the persons whose names are subscribed to the within instrument and acknowledged that they executed the same for the purposes therein contained.

(SEAL) Notary Public

My commission expires: ________________
MORTGAGE - ONE HUNDRED EIGHTY DAY REDEMPTION

_______________________ and _______________________, husband and wife, Mortgagors, of _________________________________ hereby mortgage to _________________________________, with offices located at _________________________________, the following-described real property in _________________ County, South Dakota:

and all buildings, fixtures, and improvements, now existing or hereafter placed upon the property, as security for the payment to Mortgagee of the principal sum of ________________________________ Dollars ($ ______________) and interest, payable according to terms of a certain promissory note of even date herewith, with the final installment due _________________, and as security for the payment to Mortgagee of any advances and interest which Mortgagee may, at its option make to Mortgagors, or make on behalf of Mortgagors to protect the property.

Mortgagors further agree: (a) to pay all taxes and assessments and other charges that may be levied upon or become due on the premises before the same become delinquent; (b) to keep buildings and improvements, now existing or hereafter placed upon the premises, insured to Mortgagee's satisfaction with a loss payable clause to Mortgagee, and promptly deliver the insurance policies to Mortgagee, upon Mortgagee’s request; (c) to keep all buildings, fixtures, and other improvements, now existing or hereafter placed on the property, in good repair and neither commit nor permit any acts of waste or any impairment of the value of the property.

In the event Mortgagors fail to timely pay taxes, assessments, insurance premiums, or other charges on the property, Mortgagee, at its option, may make such payments and the amounts so paid will become part of the indebtedness secured by this mortgage, accruing interest from the date of payment at the rate stated in the promissory note. The advancement by Mortgagee of any such amounts will in no manner limit the right of Mortgagee to declare Mortgagors in default or exercise any of Mortgagee's other rights or remedies.

As additional security, Mortgagors hereby assign to Mortgagee all rents of the property, provided that Mortgagor shall have the right, prior to default or abandonment of the property, to collect and retain such rents as they become due and payable. The assignment of rents shall be effective until the payment of all indebtedness secured by this mortgage, or in the case of foreclosure, until the period of redemption expires. Regardless of the extinguishment of the debt by a foreclosure sale, this benefit shall continue for the benefit of the purchaser at such sale.
Mortgagors hereby relinquish all rights of homestead and warrant that the premises are free of encumbrances, except for encumbrances of record.

If the mortgaged premises are sold without the prior consent of Mortgagee, the entire balance owing may, at Mortgagee's option, become immediately due and payable upon sixty (60) days notice to Mortgagors, and this mortgage may be foreclosed as provided by law.

In the case of default in the payment of the principal sum, or any part thereof, or interest thereon at the time specified for payment, or in the case of non-payment of any taxes, assessments, insurance, or other charges as required, or of breach of any covenant or agreement contained in this mortgage, then the total debt, principal and interest, shall at the option of the holder of the mortgage, become immediately due and payable upon twenty (20) days notice to Mortgagors, and this mortgage may be foreclosed as provided by law.

In the case of foreclosure, the holder of this mortgage is authorized to appoint a receiver to take possession of the mortgaged premises if the premises are abandoned, or to have a receiver appointed by the circuit court upon sufficient proof being established therefor.

In the case of foreclosure, Mortgagors shall pay to the holder of this mortgage the difference between the net proceeds of sale, if less that the total debt due.

In the case of foreclosure by action, the holder of the certificate of sale may apply to the court for a reduction of the redemption period if the property has been abandoned by Mortgagors. If, after notice to the parties as the court directs, the court finds the property has been abandoned, the redemption period may be reduced to not less than sixty (60) days from the date of recording the certificate of sale.

In the case of foreclosure, the holder of this mortgage shall recover reasonable attorney fees and disbursements necessarily incurred.

THE PARTIES AGREE THAT THE PROVISIONS OF THE ONE HUNDRED EIGHTY DAY REDEMPTION MORTGAGE ACT GOVERN THIS MORTGAGE. THERE IS HEREBY GRANTED TO MORTGAGEE A POWER OF SALE FOR THE PURPOSES OF SDCL 21-49.

Executed the day and year stated in the acknowledgment.

Mortgagor: ____________________________________________  

Mortgagor: ____________________________________________  

STATE OF ___________________________ )

)  

SS. COUNTY OF ________________ )

)  

On this ______ day of _____________________, 20___, before me the undersigned

 officer, personally appeared__________________________ and
3. Liens
A lien is a claim against property to satisfy a debt or protect a claim for the payment of a debt. Liens can be placed on property in various ways.

Mechanic’s Lien: When a person contracts for labor, services or material to be furnished for the purpose of making improvements on real property but does not immediately pay for the improvements, a creditor can place a mechanic’s lien on the property. The real property itself becomes security for the debt and the property can be taken and held to guarantee payment of the debt or it can be sold through foreclosure proceedings to effect actual payment. In order to foreclose, however, the lienholder must give notice to the property owner.

Artisan’s Lien: This lien was created through common law so that a creditor could recover payment from a debtor for labor and materials furnished in the repair of personal property. An artisan’s lien is possessory meaning that the lienholder must have retained possession of the property and have expressly or impliedly agreed to provide the services on a cash, not a credit, basis. The lien exists as long as the lienholder maintains possession. The lien ends when possession is voluntarily surrendered. Modern statutes generally permit the holder of such a lien to foreclose and sell the personal property subject to the lien to satisfy the payment of the debt after notice is given to the owner. The sale proceeds are then used to pay the debt and the surplus, if any, is paid to the former owner.

Judicial Lien: When a debt is past due, a creditor can bring a legal action against the debtor to collect the debt. If the creditor succeeds in the action, the court awards the creditor a judgment against the debtor. The amount of judgment is usually the amount of the debt plus any interest and legal costs. This proceeding often takes place in a small claims action. Unfortunately the creditor is often unable to collect the awarded amount. To ensure that a judgment in the creditor’s favor is collectable, the creditor can request that certain property of the debtor be seized to satisfy the debt.

Certain property of the debtor is exempt from creditors’ actions. In most states, for example, certain types of property are exempt from judgment liens.

Homestead exemption: Each state permits the debtor to retain the family home, either in its entirety or up to a specified dollar amount, free from the claims of unsecured creditors or trustees in bankruptcy.
Personal property: Personal property that is most often exempt under state laws includes household furniture up to a specified dollar amount; clothing and certain personal possessions such as family photos; a vehicle for transportation, up to a specified dollar amount; certain classified animals including pets; and equipment that the debtor uses in a business or trade, up to a specified dollar amount.

4. Consumer Lending Regulations
Lending institutions are subject to numerous state and Federal regulations when extending credit to consumers, including the Federal Equal Credit Opportunity Act, which ensures that all consumers are given an equal opportunity to obtain credit.

The following information is adapted from information provided by the Federal Trade Commission on its website at http://www.ftc.gov/bcp/conline/pubs/credit/ecoa.htm on November 21, 2005.

The Equal Credit Opportunity Act (ECOA), protects consumers when they deal with any creditor who regularly extends credit, including banks, small loan and finance companies, retail and department stores, credit card companies, and credit unions. Anyone involved in granting credit, such as real estate brokers who arrange financing, is covered by the law. Businesses applying for credit also are protected by the law.

When Considering a Credit Application, a Creditor May Not:

1. Discourage a person from applying because of your sex, marital status, age, race, national origin, or because you receive public assistance income.

2. Ask a person to reveal his/her sex, race, national origin, or religion. A creditor may ask a person to voluntarily disclose this information (except for religion) if the person is applying for a real estate loan. This information helps federal agencies enforce anti-discrimination laws. A person may be asked about his/her residence or immigration status.

3. Ask if a person is widowed or divorced. When permitted to ask marital status, a creditor may only use the terms: married, unmarried, or separated.

4. Ask about a person's marital status if the person is applying for a separate, unsecured account. A creditor may ask a person to provide this information if the person lives in "community property" states: Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, and Washington. A creditor in any state may ask for this information if a person applies for a joint account or one secured by property.

5. Request information about a person's spouse, except when the spouse is also applying for a loan; the spouse will be allowed to use the account; the person is relying on his/her spouse’s income or on alimony or child support income from a former spouse; or if a person resides in a community property state.

6. Inquire about a person's plans for having or raising children.

7. Ask if a person receives alimony, child support, or separate maintenance payments, unless
the person first told that the person doesn't have to provide this information if the person won't rely on these payments to get credit. A creditor may ask if a person has to pay alimony, child support, or separate maintenance payments.

**When Determining Whether to Extend Credit, a Creditor May Not:**

1. Consider a person's sex, marital status, race, national origin, or religion.
2. Consider whether a person has a telephone listing in your name. A creditor may consider whether a person has a phone.
3. Consider the race of people in the neighborhood where the person wants to buy, refinance or improve a house with borrowed money.
4. Consider a person's age, unless:
   a. The person is too young to sign contracts, generally younger than 18 years of age;
   b. The person is 62 or older, and the creditor will favor you because of your age;
   c. Such information is used to determine the meaning of other factors important to creditworthiness. For example, a creditor could use a person's age to determine if the person's income might drop because the person is about to retire;
   d. Such information is used in a valid scoring system that favors applicants age 62 and older. A credit-scoring system assigns points to answers a person provides to credit application questions. For example, a person's length of employment might be scored differently depending on the person's age.

**When Evaluating a Person's Income, A Creditor May Not:**

1. Refuse to consider public assistance income the same way as other income.
2. Discount income because of a person's sex or marital status. For example, a creditor cannot count a man's salary at 100 percent and a woman's at 75 percent. A creditor may not assume a woman of childbearing age will stop working to raise children.
3. Discount or refuse to consider income because it comes from part-time employment or pension, annuity, or retirement benefits programs.
4. Refuse to consider regular alimony, child support, or separate maintenance payments. A creditor may ask a person to prove that the person has received this income consistently.

**A Person has a Right To:**

1. Have credit in the person's birth name (Mary Smith), the person's first and your spouse's last name (Mary Jones), or the person's first name and a combined last name (Mary Smith-Jones).
2. Get credit without a cosigner, if the person meets the creditor’s standards.
3. Have a cosigner other than the person's husband or wife, if a cosigner is necessary.
4. Keep the person's own accounts after the person changes names, marital status, reach a certain age, or retire, unless the creditor has evidence that the person is not willing or able to pay.
5. Know whether the application was accepted or rejected within 30 days of filing a
complete application.

6. Know why the application was rejected. The creditor must give the person a notice that tells the person either the specific reasons for the person's rejection or the person's right to learn the reasons if the person asks within 60 days.

7. Acceptable reasons include: "Your income was low," or "You haven’t been employed long enough." Unacceptable reasons are: "You didn’t meet our minimum standards," or "You didn’t receive enough points on our credit-scoring system." Indefinite and vague reasons are illegal, so ask the creditor to be specific.

8. Find out why the person was offered less favorable terms than the person applied for—unless the person accepts the terms. Ask for details. Examples of less favorable terms include higher finance charges or less money than the person requested.

9. Find out why the person's account was closed or why the terms of the account were made less favorable unless the account was inactive or delinquent.

4. Debt Collection Practices

Debt collection practices are regulated by the *Fair Debt Collection Practices Act*, which requires that debt collectors treat debtor's fairly and prohibits certain methods of debt collection.

The following information is adapted from information provided by the Federal Trade Commission on its website at http://www.ftc.gov/bcp/conline/pubs/credit/fdc.htm on November 21, 2005.

The Fair Debt Collection Practices Act covers personal, family, and household debts, such as money owed for the purchase of an automobile, for medical care, or for charge accounts.

Under the Act, a debt collector is any person who regularly collects debts owed to others. This includes attorneys who collect debts on a regular basis. A collector may contact a debtor in person, by mail, telephone, telegram, or fax. However, a debt collector may not contact a debtor at inconvenient times or places, such as before 8 a.m. or after 9 p.m., unless the debtor agrees. A debt collector also may not contact a debtor at work if the collector knows that the debtor's employer disapproves of such contacts.

A debtor can stop a debt collector from contacting the debtor by writing a letter to the collector telling the collector to stop. Once the collector receives the letter, the collector may not contact the debtor again except to say there will be no further contact or to notify the debtor that the debt collector or the creditor intends to take some specific action.

If a debtor has an attorney, the debt collector must contact the attorney, rather than the debtor. If the debtor does not have an attorney, a collector may contact other people, but only to find out where the debtor lives, the debtor's phone number, and where the debtor works. Collectors usually are prohibited from contacting such third parties more than once. In most cases, the collector may not tell anyone other than the debtor and the debtor's attorney that the debtor owes money.
Within five days after the debtor is first contacted, the collector must send the debtor a written notice telling the debtor the amount of money owed; the name of the creditor to whom the money is owed; and what action to take if the debtor believes that the money is not owed. A collector may not contact a debtor if, within 30 days after the debtor receives the written notice, the debtor sends the collection agency a letter stating that the debtor does not owe money. However, a collector can renew collection activities if the debtor sent proof of the debt, such as a copy of a bill for the amount owed.

Debt collectors may not harass, oppress, or abuse a debtor or any third parties the collector contacts. For example, debt collectors may not:

1. use threats of violence or harm;
2. publish a list of consumers who refuse to pay their debts (except to a credit bureau);
3. use obscene or profane language; or repeatedly use the telephone to annoy someone.

Debt collectors may not use any false or misleading statements when collecting a debt. For example, debt collectors may not:

1. falsely imply that they are attorneys or government representatives;
2. falsely imply that the debtor has committed a crime;
3. falsely represent that they operate or work for a credit bureau;
4. misrepresent the amount of the debt;
5. indicate that papers being sent to the debtor are legal forms when they are not; or
6. indicate that papers being sent to the debtor are not legal forms when they are. Debt collectors also may not state that:

1. the debtor will be arrested if the debt is not paid;
2. they will seize, garnish, attach, or sell the debtor's property or wages, unless the collection agency or creditor intends to do so, and it is legal to do so; or
3. actions, such as a lawsuit, will be taken against the debtor, when such action legally may not be taken, or when they do not intend to take such action.

Debt collectors may not:

1. give false credit information about the debtor to anyone, including a credit bureau;
2. send the debtor anything that looks like an official document from a court or government agency when it is not; or
3. use a false name.

Debt collectors may not engage in unfair practices when they try to collect a debt. For example, collectors may not:

1. collect any amount greater than the debt, unless the debtor's state law permits such a charge;
2. deposit a post-dated check prematurely;
3. use deception to make the debtor accept collect calls or pay for telegrams;
4. take or threaten to take the debtor's property unless this can be done legally; or
5. contact the debtor by postcard.

Review briefly the statutes of your state, or a state of your choice, which address:
- Secured transactions
- Real estate mortgages

Statutes are available online at the Cornell University Law School Legal Information Institute.\(^{xv}\)

Ask your instructor for assistance, if you have difficulty locating the statutes.

5. Summary
A debt is an obligation for money owed to a creditor. Generally, debt can be divided into two categories: secured debt and unsecured debt. A lien or security interest upon real or personal property secures payment of the debt. Lending and collection practices are regulated by Federal statutes.

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Read the following case and any other cases assigned by your instructor.

**METZGER v. AMERICREDIT FINANCIAL SERVICES, INC.**
273 Ga. App. 453, 615 S.E.2d 120
(2005)

BERNES, Judge.

Theresa Metzger appeals from an order entered by the Superior Court of Clayton County granting partial summary judgment to Americredit Financial Services, Inc. on her claim for conversion based on the alleged wrongful repossession of her vehicle. Metzger contends that the superior court erred by failing to conclude that she took her vehicle free of Americredit's security interest under the special good faith purchaser rule for goods covered by a certificate of title set forth in OCGA § 11-9-337(1). We agree and reverse.

The underlying facts are not in dispute. On or about October 1, 2002, Americredit repossessed a 1997 Ford Taurus from Metzger, who had purchased the vehicle from a used car dealership in March of 2002. Metzger did not realize that Americredit had a prior lien on the vehicle or that it had been repossessed. As a result, she reported the vehicle as stolen to the police. Metzger later learned that Americredit had obtained a security interest in the vehicle in 1998, when the company financed James Strong's purchase of the vehicle in the State of New York.
The New York certificate of title issued to Strong reflected Americredit's security interest in the vehicle.

Strong later moved from New York to Georgia and submitted a "MV1Z" application form, along with the existing title and the required fee, to the Cobb County tag agent for the Georgia Department of Motor Vehicles ("DMV") in order to convert the existing New York certificate of title to a Georgia one. The DMV processed the application, but as a result of a clerical data entry error, the DMV issued a Georgia certificate of title that did not reflect Americredit's security interest in the vehicle.

Strong later transferred the vehicle to an automobile dealer owner, and the vehicle thereafter passed through a non-dealer owner and additional dealer owners before Metzger purchased it in March of 2002. None of the subsequent Georgia certificates of title issued for the vehicle in connection with these transfers reflected Americredit's security interest.

After Metzger purchased the vehicle and registered it with the DMV, Americredit, having finally located the vehicle, repossessed it from Metzger's residence and sold it at auction. Once she learned from the police department that her vehicle had been repossessed rather than stolen, Metzger filed suit against Americredit in the Superior Court of Clayton County. She contended that Americredit wrongfully repossessed her vehicle and kept her personal belongings contained therein, and, as a consequence, should be held liable for conversion, negligence, deceptive trade practices, breach of the peace, breach of good faith, racketeering, unjust enrichment, and breach of sale.

Metzger subsequently filed a motion seeking partial summary judgment on her claim of conversion. Americredit filed its response and a cross motion for summary judgment on all of Metzger's claims. The superior court denied Metzger's motion for partial summary judgment and granted summary judgment in favor of Americredit on Metzger's conversion claim only. The superior court concluded that Americredit had a perfected security interest in the vehicle that it could enforce against Metzger. Metzger now appeals from that order.

. . . In order to establish a claim for conversion, "the complaining party must show (1) title to the property or the right of possession, (2) actual possession in the other party, (3) demand for return of the property, and (4) refusal by the other party to return the property." (Citation omitted.) . . . The sole issue regarding Metzger's conversion claim is whether Metzger had the exclusive right of possession to the vehicle, making Americredit's seizure unlawful, or whether Americredit's security interest instead empowered it to practice self-help and repossess the vehicle from Metzger. See, e.g., . . . Because the material facts are undisputed, resolution of this issue turns on our interpretation of the applicable statutory framework.

"[I]n construing [Georgia statutes], we apply the fundamental rules of statutory construction that require us to construe a statute according to its terms, to give words their plain and ordinary meaning, and to avoid a construction that makes some language mere surplusage." . . . With these rules in mind, we turn to the Motor Vehicle Certificate of Title Act, OCGA § 40-3-1 et seq. (the "Act"), which provides the exclusive procedure for perfecting a security interest in a motor vehicle in Georgia. . . .

Under the Act, a security interest in a motor vehicle is perfected, at the
latest, on the date when the application documents for obtaining a certificate of title are delivered to the DMV or local tag agent, so long as the application documents properly reflect the existence of the security interest:

(b) (1) A security interest is perfected by delivery to the commissioner or to the county tag agent of the county in which the seller is located, of the county in which the sale takes place, of the county in which the vehicle is delivered, or of the county wherein the vehicle owner resides, of the required fee and:

(A) The existing certificate of title, if any, and an application for a certificate of title containing the name and address of the holder of a security interest; or

(B) A notice of security interest on forms prescribed by the commissioner.

Perfection occurs on that date, irrespective of whether the certificate of title subsequently issued by the DMV fails to reflect the security interest:

(b) (2) The security interest is perfected as of the time of its creation if the initial delivery of the application or notice to the commissioner or local tag agent is completed within 20 days thereafter, regardless of any subsequent rejection of the application or notice for errors; otherwise, as of the date of the delivery to the commissioner or local tag agent. The local tag agent shall issue a receipt or other evidence of the date of filing of such application or notice. When the security interest is perfected as provided for in this subsection, it shall constitute notice to everybody of the security interest of the holder. OCGA § 40-3-50(b).

"Compliance with the filing requirements of the Act has the effect of imputing constructive notice to all who may subsequently acquire an interest in or lien against the property." . . .

Based on this statutory language and case law, it might appear that because Strong delivered proper application forms reflecting Americredit's security interest to the Cobb County tag agent, Americredit could enforce its security interest against Metzger, who under OCGA § 40-3-50(b)(2) would have constructive notice of the security interest despite the clerical error contained in the Georgia certificate of title that was later issued. However, OCGA § 40-3-50 contains three statutory exceptions:

(a) Except as provided in Code Sections 11-9-303, 11-9-316, and 11-9-337, the security interest in a vehicle of the type for which a certificate of title is required shall be perfected and shall be valid against subsequent creditors of the owner, subsequent transferees, and the holders of security interests and liens on the vehicle by compliance with this chapter. (Emphasis supplied.) OCGA § 40-3-50(a).
Significantly, one of those exceptions, OCGA § 11-9-337, states:

If, while a security interest in goods is perfected by any method under the law of another jurisdiction, this state issues a certificate of title that does not show that the goods are subject to the security interest or contain a statement that they may be subject to security interests not shown on the certificate:

(1) A buyer of the goods, other than a person in the business of selling goods of that kind, takes free of the security interest if the buyer gives value and receives delivery of the goods after issuance of the certificate and without knowledge of the security interest.

(Emphasis supplied.) OCGA § 11-9-337(1) [FN2] An explanation of this provision is set forth in Comment 2 to Uniform Commercial Code § 9-337:

This section affords protection to certain good-faith purchasers for value who are likely to have relied on a "clean" certificate of title, i.e., one that neither shows that the goods are subject to a particular security interest nor contains a statement that they may be subject to security interests not shown on the certificate. Under this section, a buyer can take free of, and the holder of a conflicting security interest can acquire priority over, a security interest that is perfected by any method under the law of another jurisdiction.

UCC § 9-337 cmt. 2.

In the present case, the undisputed evidence of record shows that the six requirements of the statutory exception contained in OCGA § 11-9-337(1) have been met. First, the parties agree that, at the time that Strong filed his application for a Georgia certificate of title with the Cobb County tag agent, Americredit had previously perfected its security interest in the vehicle under New York law, and the security interest remained perfected. Second, the certificate of title issued by the DMV to Strong failed to show that the vehicle was subject to a security interest.

Third, Metzger is not a person in the business of selling automobiles. Fourth, Metzger gave value for the vehicle. Fifth, Metzger received delivery of the vehicle after issuance of the Georgia certificate of title by the DMV erroneously omitting reference to Americredit's security interest. Sixth and finally, Metzger was without knowledge of the security interest that Americredit held in the vehicle. Thus, Metzger was entitled to invoke OCGA § 11-9-337(1). It necessarily follows that Metzger took the vehicle free of Americredit's security interest. However, Americredit contends that two additional statutes found in Georgia's Uniform Commercial Code, OCGA §§ 11-9-303 and 11-9-316, indicate that Metzger took the vehicle subject to the security interest. Based on these two statutes, Americredit argues that the special good faith purchaser rule set forth in OCGA § 11-9-337(1) has no application in this case, because its perfected security interest in Metzger's vehicle was no longer governed by New York law once the proper application documents and required fee for a Georgia certificate of title were submitted to the Georgia DMV by James Strong.
Thus, in Americredit's view, OCGA § 11-9-337(1) does not apply under the circumstances here because the erroneous Georgia certificate of title was not issued "while" its security interest in the vehicle was perfected "under the law of another jurisdiction."

Americredit's statutory argument is based on a strained reading of the interplay between OCGA §§ 11-9-303, 11-9-316(d) and (e), and 11-9-337. OCGA § 11-9-303, entitled "Law governing perfection and priority of security interests in goods covered by a certificate of title," is a choice of law provision, as its title suggests. OCGA § 11-9-303(b) provides that: Goods become covered by a certificate of title when a valid application for the certificate of title and the applicable fee are delivered to the appropriate authority. Goods cease to be covered by a certificate of title at the earlier of the time the certificate of title ceases to be effective under the law of the issuing jurisdiction or the time the goods become covered subsequently by a certificate of title issued by another jurisdiction.

Section 11-9-303(c) then provides that "[t]he local law of the jurisdiction under whose certificate of title the goods are covered governs perfection." These provisions indicate that even when a security interest in goods has been perfected in another state, Georgia law determines perfection and priority issues once the goods become "covered" by a Georgia certificate of title, which occurs when a valid application and fee are submitted to the Georgia DMV.

Once it becomes clear that Georgia law governs because the goods are covered by a Georgia certificate of title, the next question is whether the security interest previously perfected in another state remains perfected. That issue is addressed by OCGA § 11-9-316, entitled "Continued perfection of security interest following change in governing law," specifically subsections (d) and (e), which deal with certificates of title. These subsections set forth the general rules for when a security interest perfected in another state remains perfected in Georgia, once the goods are "covered" by a Georgia certificate of title.

"A statute must be construed in relation to other statutes of which it is a part, and all statutes relating to the same subject-matter, briefly called statutes in pari materia, are construed together, and harmonized wherever possible, so as to ascertain the legislative intention and give effect thereto." . . . When read in pari materia with OCGA § 11-9-303 and 11-9-316(d) and (e), OCGA § 11-9-337(1) gives protection to a good faith purchaser for value who is not "in the business of selling goods of that kind," when there is continued perfection of the security interest under OCGA § 11-9-316(d) and (e), but the Georgia certificate of title fails to reflect the security interest. Consequently, in the present case, although Americredit's security interest in the vehicle remained perfected at the time that Metzger purchased the vehicle, that security interest could not be enforced as against Metzger, a good faith purchaser as that term is defined in OCGA § 11-9-337(1), since the security interest was not properly reflected on the Georgia certificate of title.

Furthermore, "a specific statute will prevail over a general statute, absent any indication of a contrary legislative intent, to resolve any inconsistency between them." . . . are general statutory provisions addressing continued perfection of an out-of-state security interest once goods become covered by a Georgia certificate of title. In contrast, OCGA § 11-9-337(1) sets forth a more specific rule addressing what occurs in the unique circumstance where the
Georgia certificate of title that covers the goods erroneously fails to reflect the security interest originally perfected in another state. Because OCGA § 11-9-337(1) is the more specific statute, it controls, even if there were a perceived inconsistency between the various statutory provisions. Accordingly, Americredit's statutory interpretation argument is unavailing.

Finally, we conclude that the superior court erred by relying on OCGA § 40-3-31(4) and our decision in Strother Ford, Inc. v. First Nat. Bank of Maryland, 132 Ga.App. 268, 208 S.E.2d 25 (1974), instead of OCGA § 11-9-337(1). OCGA § 40-3-31 by its terms only applies when a certificate of title has been "lost, stolen, mutilated, or destroyed or becomes illegible" (OCGA § 40-3-31(a)), and none of those circumstances occurred here. Furthermore, Strother is distinguishable from the instant action. The certificate of title at issue in that case failed to reflect a security interest on the vehicle due to fraud by the party that submitted the application to the DMV (see Strother, Ford Inc. 132 Ga.App. at 268 and 272(2), 208 S.E.2d 25), whereas here the certificate omitted the security interest information as a result of clerical error, not intentional wrongdoing. Moreover, at the time Strother was decided in 1974, Georgia statutory law did not yet contain an exception to its priority statutes akin to OCGA § 11-9-337 for security interests on automobiles perfected in another state but not reflected in a later issued Georgia certificate of title. See Ga.Code Ann. § 68-421a (Supp.1974). Thus, the superior court improperly relied on OCGA § 40-3-31(4) and Strother as a basis for its decision in this case.

For these reasons, we reverse the partial grant of summary judgment in favor of Americredit. We remand to the superior court to enter summary judgment in favor of Metzger on her conversion claim.

B. Bankruptcy
   1. The Discharge in Bankruptcy
   2. Chapter 7
   3. Chapter 13
   4. Chapter 11
   5. Chapter 12


The site contains the following disclaimer: While the information presented is accurate as of the date of publication, it should not be cited or relied upon as legal authority. It should not be used as a substitute for reference to the United States Bankruptcy Code (title 11, United States Code) and the Federal Rules of Bankruptcy Procedure, both of which may be reviewed at local law libraries, or to local rules of practice adopted by each bankruptcy court. Finally, this publication should not substitute for the advice of competent legal counsel.

Bankruptcy law in the United States is intended to protect a debtor by giving him or her a fresh start from creditors’ claims and to ensure equitable treatment of creditors who are
competing for a debtor’s assets. Bankruptcy proceedings are held in federal bankruptcy courts which are under the authority of U.S. district courts. There is a bankruptcy court for each judicial district in the country. Each state has one or more districts. There are 90 bankruptcy districts across the country. The bankruptcy courts generally have their own clerk’s offices.

The most frequently used bankruptcy plans are contained in specified chapters of the Bankruptcy Code. Chapter 7 is liquidations, Chapter 11 is reorganizations and Chapter 13 is adjustments of debt.

Bankruptcy can either be done by the debtor filing a voluntary petition or it can be initiated on an involuntary basis by the debtor’s creditors forcing the debtor into bankruptcy proceedings. An involuntary proceeding cannot be commenced against a farmer or a charitable institution and can only be done if one of the following requirements is met:

1. If the debtor has twelve or more creditors, three or more of those having unsecured claims adding up to at least $14,425 must join in the petition.
2. If the debtor has fewer than twelve creditors, one or more creditors having an unsecured claim of $14,425 may file.

Although a debtor can challenge the involuntary petition, a court will generally go ahead with the proceedings if it finds either of the following:

1. That the debtor is generally not paying debts as they become due.
2. That a custodian took possession of, or was appointed to take charge of, substantially all of the debtor’s property within 120 days before the filing of the petition.

Please review the YouTube video Bankruptcy Overview posted by LegalAidKY before continuing your reading.

1. The Discharge in Bankruptcy
The bankruptcy discharge varies depending on the type of case a debtor files.

a. What is a discharge in bankruptcy?
A bankruptcy discharge releases the debtor from personal liability for certain specified types of debts. In other words, the debtor is no longer legally required to pay any debts that are discharged. The discharge is a permanent order prohibiting the creditors of the debtor from taking any form of collection action on discharged debts, including legal action and communications with the debtor, such as telephone calls, letters, and personal contacts.

Although a debtor is not personally liable for discharged debts, a valid lien (i.e., a charge upon specific property to secure payment of a debt) that has not been avoided (i.e., made unenforceable) in the bankruptcy case will remain after the bankruptcy case. Therefore, a secured creditor may enforce the lien to recover the property secured by the lien.

b. When does the discharge occur?
The timing of the discharge varies, depending on the chapter under which the case is filed. In a chapter 7 (liquidation) case, for example, the court usually grants the discharge promptly on expiration of the time fixed for filing a complaint objecting to discharge and the time fixed for filing a motion to dismiss the case for substantial abuse (60 days following the first date set for the 341 meeting). Typically, this occurs about four months after the date the debtor files the
petition with the clerk of the bankruptcy court. In individual chapter 11 cases, and in cases under chapter 12 (adjustment of debts of a family farmer or fisherman) and 13 (adjustment of debts of an individual with regular income), the court generally grants the discharge as soon as practicable after the debtor completes all payments under the plan. Since a chapter 12 or chapter 13 plan may provide for payments to be made over three to five years, the discharge typically occurs about four years after the date of filing. The court may deny an individual debtor's discharge in a chapter 7 or 13 case if the debtor fails to complete "an instructional course concerning financial management." The Bankruptcy Code provides limited exceptions to the "financial management" requirement if the U.S. trustee or bankruptcy administrator determines there are inadequate educational programs available, or if the debtor is disabled or incapacitated or on active military duty in a combat zone.

c. How does the debtor get a discharge?
Unless there is litigation involving objections to the discharge, the debtor will usually automatically receive a discharge. The Federal Rules of Bankruptcy Procedure provide for the clerk of the bankruptcy court to mail a copy of the order of discharge to all creditors, the U.S. trustee, the trustee in the case, and the trustee's attorney, if any. The debtor and the debtor's attorney also receive copies of the discharge order. The notice, which is simply a copy of the final order of discharge, is not specific as to those debts determined by the court to be nondischargeable, i.e., not covered by the discharge. The notice informs creditors generally that the debts owed to them have been discharged and that they should not attempt any further collection. They are cautioned in the notice that continuing collection efforts could subject them to punishment for contempt. Any inadvertent failure on the part of the clerk to send the debtor or any creditor a copy of the discharge order promptly within the time required by the rules does not affect the validity of the order granting the discharge.

d. Are all of the debtor's debts discharged or only some?
Not all debts are discharged. The debts discharged vary under each chapter of the Bankruptcy Code. Section 523(a) of the Code specifically excepts various categories of debts from the discharge granted to individual debtors. Therefore, the debtor must still repay those debts after bankruptcy. Congress has determined that these types of debts are not dischargeable for public policy reasons (based either on the nature of the debt or the fact that the debts were incurred due to improper behavior of the debtor, such as the debtor's drunken driving).

There are 19 categories of debt excepted from discharge under chapters 7, 11, and 12. A more limited list of exceptions applies to cases under chapter 13.

Generally speaking, the exceptions to discharge apply automatically if the language prescribed by section 523(a) applies. The most common types of nondischargeable debts are certain types of tax claims, debts not set forth by the debtor on the lists and schedules the debtor must file with the court, debts for spousal or child support or alimony, debts for willful and malicious injuries to person or property, debts to governmental units for fines and penalties, debts for most government funded or guaranteed educational loans or benefit overpayments, debts for personal injury caused by the debtor's operation of a motor vehicle while intoxicated, debts owed to certain tax-advantaged retirement plans, and debts for certain condominium or cooperative housing fees.
The types of debts described in sections 523(a)(2), (4) and (6) (obligations affected by fraud or maliciousness) are not automatically excepted from discharge. Creditors must ask the court to determine that these debts are excepted from discharge. In the absence of an affirmative request by the creditor and the granting of the request by the court, the types of debts set out in sections 523(a)(2), (4) and (6) will be discharged.

A slightly broader discharge of debts is available to a debtor in a chapter 13 case than in a chapter 7 case. Debts dischargeable in a chapter 13, but not in chapter 7, include debts for willful and malicious injury to property, debts incurred to pay non-dischargeable tax obligations, and debts arising from property settlements in divorce or separation proceedings. Although a chapter 13 debtor generally receives a discharge only after completing all payments required by the court-approved (i.e., "confirmed") repayment plan, there are some limited circumstances under which the debtor may request the court to grant a "hardship discharge" even though the debtor has failed to complete plan payments. Such a discharge is available only to a debtor whose failure to complete plan payments is due to circumstances beyond the debtor's control. The scope of a chapter 13 "hardship discharge" is similar to that in a chapter 7 case with regard to the types of debts that are excepted from the discharge. A hardship discharge also is available in chapter 12 if the failure to complete plan payments is due to "circumstances for which the debtor should not justly be held accountable."

e. Does the debtor have the right to a discharge or can creditors object to the discharge?

In chapter 7 cases, the debtor does not have an absolute right to a discharge. An objection to the debtor's discharge may be filed by a creditor, by the trustee in the case, or by the U.S. trustee. Creditors receive a notice shortly after the case is filed that sets forth much important information, including the deadline for objecting to the discharge. To object to the debtor's discharge, a creditor must file a complaint in the bankruptcy court before the deadline set out in the notice. Filing a complaint starts a lawsuit referred to in bankruptcy as an "adversary proceeding."

The court may deny a chapter 7 discharge for any of the reasons described in section 727(a) of the Bankruptcy Code, including failure to provide requested tax documents; failure to complete a course on personal financial management; transfer or concealment of property with intent to hinder, delay, or defraud creditors; destruction or concealment of books or records; perjury and other fraudulent acts; failure to account for the loss of assets; violation of a court order or an earlier discharge in an earlier case commenced within certain time frames (discussed below) before the date the petition was filed. If the issue of the debtor's right to a discharge goes to trial, the objecting party has the burden of proving all the facts essential to the objection.

In chapter 12 and chapter 13 cases, the debtor is usually entitled to a discharge upon completion of all payments under the plan. As in chapter 7, however, discharge may not occur in chapter 13 if the debtor fails to make a required course on personal financial management. A debtor is also ineligible for a discharge in chapter 13 if he or she received a prior discharge in another case commenced within time frames discussed the next paragraph. Unlike chapter 7, creditors do not have standing to object to the discharge of a chapter 12 or chapter 13 debtor. Creditors can object to confirmation of the repayment plan, but cannot object to the discharge if the debtor has completed making plan payments.
f. Can a debtor receive a second discharge in a later chapter 7 case?
The court will deny a discharge in a later chapter 7 case if the debtor received a discharge under chapter 7 or chapter 11 in a case filed within eight years before the second petition is filed. The court will also deny a chapter 7 discharge if the debtor previously received a discharge in a chapter 12 or chapter 13 case filed within six years before the date of the filing of the second case unless (1) the debtor paid all “allowed unsecured” claims in the earlier case in full, or (2) the debtor made payments under the plan in the earlier case totaling at least 70 percent of the allowed unsecured claims and the debtor's plan was proposed in good faith and the payments represented the debtor's best effort. A debtor is ineligible for discharge under chapter 13 if he or she received a prior discharge in a chapter 7, 11, or 12 case filed four years before the current case or in a chapter 13 case filed two years before the current case.

g. Can the discharge be revoked?
The court may revoke a discharge under certain circumstances. For example, a trustee, creditor, or the U.S. trustee may request that the court revoke the debtor's discharge in a chapter 7 case based on allegations that the debtor: obtained the discharge fraudulently; failed to disclose the fact that he or she acquired or became entitled to acquire property that would constitute property of the bankruptcy estate; committed one of several acts of impropriety described in section 727(a)(6) of the Bankruptcy Code; or failed to explain any misstatements discovered in an audit of the case or fails to provide documents or information requested in an audit of the case. Typically, a request to revoke the debtor's discharge must be filed within one year of the discharge or, in some cases, before the date that the case is closed. The court will decide whether such allegations are true and, if so, whether to revoke the discharge.

In a chapter 11, 12 and 13 cases, if confirmation of a plan or the discharge is obtained through fraud, the court can revoke the order of confirmation or discharge.

h. May the debtor pay a discharged debt after the bankruptcy case has been concluded?
A debtor who has received a discharge may voluntarily repay any discharged debt. A debtor may repay a discharged debt even though it can no longer be legally enforced. Sometimes a debtor agrees to repay a debt because it is owed to a family member or because it represents an obligation to an individual for whom the debtor's reputation is important, such as a family doctor.

i. What can the debtor do if a creditor attempts to collect a discharged debt after the case is concluded?
If a creditor attempts collection efforts on a discharged debt, the debtor can file a motion with the court, reporting the action and asking that the case be reopened to address the matter. The bankruptcy court will often do so to ensure that the discharge is not violated. The discharge constitutes a permanent statutory injunction prohibiting creditors from taking any action, including the filing of a lawsuit, designed to collect a discharged debt. A creditor can be sanctioned by the court for violating the discharge injunction. The normal sanction for violating the discharge injunction is civil contempt, which is often punishable by a fine.
j. May an employer terminate a debtor's employment solely because the person was a debtor or failed to pay a discharged debt?
The law provides express prohibitions against discriminatory treatment of debtors by both governmental units and private employers. A governmental unit or private employer may not discriminate against a person solely because the person was a debtor, was insolvent before or during the case, or has not paid a debt that was discharged in the case. The law prohibits the following forms of governmental discrimination: terminating an employee; discriminating with respect to hiring; or denying, revoking, suspending, or declining to renew a license, franchise, or similar privilege. A private employer may not discriminate with respect to employment if the discrimination is based solely upon the bankruptcy filing.

2. Chapter 7: Liquidation under the Bankruptcy Code
Chapter 7 of the Bankruptcy Code, entitled Liquidation, contemplates an orderly, court-supervised procedure by which a trustee takes over the assets of the debtor's estate, reduces them to cash, and makes distributions to creditors, subject to the debtor's right to retain certain exempt property and the rights of secured creditors. Because there is usually little or no nonexempt property in most chapter 7 cases, there may not be an actual liquidation of the debtor's assets. These cases are called "no-asset cases." A creditor holding an unsecured claim will get a distribution from the bankruptcy estate only if the case is an asset case and the creditor files a proof of claim with the bankruptcy court. In most chapter 7 cases, if the debtor is an individual, he or she receives a discharge that releases him or her from personal liability for certain dischargeable debts. The debtor normally receives a discharge just a few months after the petition is filed. Amendments to the Bankruptcy Code enacted in to the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 require the application of a "means test" to determine whether individual consumer debtors qualify for relief under chapter 7. If such a debtor's income is in excess of certain thresholds, the debtor may not be eligible for chapter 7 relief.

a. Alternatives to Chapter 7
Debtors should be aware that there are several alternatives to chapter 7 relief. For example, debtors who are engaged in business, including corporations, partnerships, and sole proprietorships, may prefer to remain in business and avoid liquidation. Such debtors should consider filing a petition under chapter 11 of the Bankruptcy Code. Under chapter 11, the debtor may seek an adjustment of debts, either by reducing the debt or by extending the time for repayment, or may seek a more comprehensive reorganization. Sole proprietorships may also be eligible for relief under chapter 13 of the Bankruptcy Code.

In addition, individual debtors who have regular income may seek an adjustment of debts under chapter 13 of the Bankruptcy Code. A particular advantage of chapter 13 is that it provides individual debtors with an opportunity to save their homes from foreclosure by allowing them to "catch up" past due payments through a payment plan. Moreover, the court may dismiss a chapter 7 case filed by an individual whose debts are primarily consumer rather than business debts if the court finds that the granting of relief would be an abuse of chapter 7. 11 U.S.C. § 707(b).

If the debtor's "current monthly income"(1) is more than the state median, the Bankruptcy Code requires application of a "means test" to determine whether the chapter 7 filing is
presumptively abusive. Abuse is presumed if the debtor's aggregate current monthly income over 5 years, net of certain statutorily allowed expenses, is more than (i) $10,000, or (ii) 25% of the debtor's nonpriority unsecured debt, as long as that amount is at least $6,000. (2) The debtor may rebut a presumption of abuse only by a showing of special circumstances that justify additional expenses or adjustments of current monthly income. Unless the debtor overcomes the presumption of abuse, the case will generally be converted to chapter 13 (with the debtor's consent) or will be dismissed. 11 U.S.C. § 707(b)(1).

Debtors should also be aware that out-of-court agreements with creditors or debt counseling services may provide an alternative to a bankruptcy filing.

b. Background
A chapter 7 bankruptcy case does not involve the filing of a plan of repayment as in chapter 13. Instead, the bankruptcy trustee gathers and sells the debtor's nonexempt assets and uses the proceeds of such assets to pay holders of claims (creditors) in accordance with the provisions of the Bankruptcy Code. Part of the debtor's property may be subject to liens and mortgages that pledge the property to other creditors. In addition, the Bankruptcy Code will allow the debtor to keep certain "exempt" property; but a trustee will liquidate the debtor's remaining assets. Accordingly, potential debtors should realize that the filing of a petition under chapter 7 may result in the loss of property.

c. Chapter 7 Eligibility
To qualify for relief under chapter 7 of the Bankruptcy Code, the debtor may be an individual, a partnership, or a corporation or other business entity. 11 U.S.C. §§ 101(41), 109(b). Subject to the means test described above for individual debtors, relief is available under chapter 7 irrespective of the amount of the debtor's debts or whether the debtor is solvent or insolvent. An individual cannot file under chapter 7 or any other chapter, however, if during the preceding 180 days a prior bankruptcy petition was dismissed due to the debtor's willful failure to appear before the court or comply with orders of the court, or the debtor voluntarily dismissed the previous case after creditors sought relief from the bankruptcy court to recover property upon which they hold liens. 11 U.S.C. §§ 109(g), 362(d) and (e). In addition, no individual may be a debtor under chapter 7 or any chapter of the Bankruptcy Code unless he or she has, within 180 days before filing, received credit counseling from an approved credit counseling agency either in an individual or group briefing, 11 U.S.C. §§ 109, 111. There are exceptions in emergency situations or where the U.S. trustee (or bankruptcy administrator) has determined that there are insufficient approved agencies to provide the required counseling. If a debt management plan is developed during required credit counseling, it must be filed with the court.

One of the primary purposes of bankruptcy is to discharge certain debts to give an honest individual debtor a "fresh start." The debtor has no liability for discharged debts. In a chapter 7 case, however, a discharge is only available to individual debtors, not to partnerships or corporations. 11 U.S.C. § 727(a)(1). Although an individual chapter 7 case usually results in a discharge of debts, the right to a discharge is not absolute, and some types of debts are not discharged. Moreover, a bankruptcy discharge does not extinguish a lien on property.

d. How Chapter 7 Works
A chapter 7 case begins with the debtor filing a petition with the bankruptcy court serving the
area where the individual lives or where the business debtor is organized or has its principal place of business or principal assets. (3) In addition to the petition, the debtor must also file with the court: (1) schedules of assets and liabilities; (2) a schedule of current income and expenditures; (3) a statement of financial affairs; and (4) a schedule of executory contracts and unexpired leases. Fed. R. Bankr. P. 1007(b). Debtors must also provide the assigned case trustee with a copy of the tax return or transcripts for the most recent tax year as well as tax returns filed during the case (including tax returns for prior years that had not been filed when the case began). 11 U.S.C. § 521. Individual debtors with primarily consumer debts have additional document filing requirements. They must file: a certificate of credit counseling and a copy of any debt repayment plan developed through credit counseling; evidence of payment from employers, if any, received 60 days before filing; a statement of monthly net income and any anticipated increase in income or expenses after filing; and a record of any interest the debtor has in federal or state qualified education or tuition accounts. Id. A husband and wife may file a joint petition or individual petitions. 11 U.S.C. § 302(a). Even if filing jointly, a husband and wife are subject to all the document filing requirements of individual debtors. (The Official Forms may be purchased at legal stationery stores or downloaded from the internet at the United States Courts website. They are not available from the court.)

In order to complete the Official Bankruptcy Forms that make up the petition, statement of financial affairs, and schedules, the debtor must provide the following information:

1. A list of all creditors and the amount and nature of their claims;
2. The source, amount, and frequency of the debtor's income;
3. A list of all of the debtor's property; and
4. A detailed list of the debtor's monthly living expenses, i.e., food, clothing, shelter, utilities, taxes, transportation, medicine, etc.

Married individuals must gather this information for their spouse regardless of whether they are filing a joint petition, separate individual petitions, or even if only one spouse is filing. In a situation where only one spouse files, the income and expenses of the non-filing spouse is required so that the court, the trustee and creditors can evaluate the household's financial position.

Among the schedules that an individual debtor will file is a schedule of "exempt" property. The Bankruptcy Code allows an individual debtor (4) to protect some property from the claims of creditors because it is exempt under federal bankruptcy law or under the laws of the debtor's home state. 11 U.S.C. § 522(b). Many states have taken advantage of a provision in the Bankruptcy Code that permits each state to adopt its own exemption law in place of the federal exemptions. In other jurisdictions, the individual debtor has the option of choosing between a federal package of exemptions or the exemptions available under state law. Thus, whether certain property is exempt and may be kept by the debtor is often a question of state law. The debtor should consult an attorney to determine the exemptions available in the state where the debtor lives.

Filing a petition under chapter 7 "automatically stays" (stops) most collection actions against the debtor or the debtor's property. 11 U.S.C. § 362. But filing the petition does not stay certain types of actions listed under 11 U.S.C. § 362(b), and the stay may be effective only for
a short time in some situations. The stay arises by operation of law and requires no judicial
action. As long as the stay is in effect, creditors generally may not initiate or continue
lawsuits, wage garnishments, or even telephone calls demanding payments. The bankruptcy
clerk gives notice of the bankruptcy case to all creditors whose names and addresses are
provided by the debtor.

Between 20 and 40 days after the petition is filed, the case trustee (described below) will hold a
meeting of creditors. If the U.S. trustee or bankruptcy administrator (5) schedules the meeting
at a place that does not have regular U.S. trustee or bankruptcy administrator staffing, the
meeting may be held no more than 60 days after the order for relief. Fed. R. Bankr. P. 2003(a).
During this meeting, the trustee puts the debtor under oath, and both the trustee and creditors
may ask questions. The debtor must attend the meeting and answer questions regarding the
debtor's financial affairs and property. 11 U.S.C. § 343. If a husband and wife have filed a joint
petition, they both must attend the creditors' meeting and answer questions. Within 10 days of
the creditors' meeting, the U.S. trustee will report to the court whether the case should be
presumed to be an abuse under the means test described in 11 U.S.C. § 704(b).

It is important for the debtor to cooperate with the trustee and to provide any financial records
or documents that the trustee requests. The Bankruptcy Code requires the trustee to ask the
debtor questions at the meeting of creditors to ensure that the debtor is aware of the potential
consequences of seeking a discharge in bankruptcy such as the effect on credit history, the
ability to file a petition under a different chapter, the effect of receiving a discharge, and the
effect of reaffirming a debt. Some trustees provide written information on these topics at or
before the meeting to ensure that the debtor is aware of this information. In order to preserve
their independent judgment, bankruptcy judges are prohibited from attending the meeting of

In order to accord the debtor complete relief, the Bankruptcy Code allows the debtor to convert
a chapter 7 case to case under chapter 11, 12 or 13 (6) as long as the debtor is eligible to be a
debtor under the new chapter. However, a condition of the debtor's voluntary conversion is that
the case has not previously been converted to chapter 7 from another chapter. 11 U.S.C. §
706(a). Thus, the debtor will not be permitted to convert the case repeatedly from one chapter
to another.

e. Role of the Case Trustee
When a chapter 7 petition is filed, the U.S. trustee (or the bankruptcy court in Alabama and
North Carolina) appoints an impartial case trustee to administer the case and liquidate the
debtor's nonexempt assets. 11 U.S.C. §§ 701, 704. If all the debtor's assets are exempt or subject
to valid liens, the trustee will normally file a "no asset" report with the court, and there will be
no distribution to unsecured creditors. Most chapter 7 cases involving individual debtors are no
asset cases. But if the case appears to be an "asset" case at the outset, unsecured creditors (7)
must file their claims with the court within 90 days after the first date set for the meeting of
creditors. Fed. R. Bankr. P. 3002(c). A governmental unit, however, has 180 days from the date
the case is filed to file a claim. 11 U.S.C. § 502(b)(9). In the typical no asset chapter 7 case,
there is no need for creditors to file proofs of claim because there will be no distribution. If the
trustee later recovers assets for distribution to unsecured creditors, the Bankruptcy Court will
provide notice to creditors and will allow additional time to file proofs of claim. Although a
A discharging creditor does not need to file a proof of claim in a chapter 7 case to preserve its security interest or lien, there may be other reasons to file a claim. A creditor in a chapter 7 case who has a lien on the debtor's property should consult an attorney for advice.

Commencement of a bankruptcy case creates an "estate." The estate technically becomes the temporary legal owner of all the debtor's property. It consists of all legal or equitable interests of the debtor in property as of the commencement of the case, including property owned or held by another person if the debtor has an interest in the property. Generally speaking, the debtor's creditors are paid from nonexempt property of the estate.

The primary role of a chapter 7 trustee in an asset case is to liquidate the debtor's nonexempt assets in a manner that maximizes the return to the debtor's unsecured creditors. The trustee accomplishes this by selling the debtor's property if it is free and clear of liens (as long as the property is not exempt) or if it is worth more than any security interest or lien attached to the property and any exemption that the debtor holds in the property. The trustee may also attempt to recover money or property under the trustee's "avoiding powers." The trustee's avoiding powers include the power to: set aside preferential transfers made to creditors within 90 days before the petition; undo security interests and other prepetition transfers of property that were not properly perfected under nonbankruptcy law at the time of the petition; and pursue nonbankruptcy claims such as fraudulent conveyance and bulk transfer remedies available under state law. In addition, if the debtor is a business, the bankruptcy court may authorize the trustee to operate the business for a limited period of time, if such operation will benefit creditors and enhance the liquidation of the estate. 11 U.S.C. § 721.

Section 726 of the Bankruptcy Code governs the distribution of the property of the estate. Under § 726, there are six classes of claims; and each class must be paid in full before the next lower class is paid anything. The debtor is only paid if all other classes of claims have been paid in full. Accordingly, the debtor is not particularly interested in the trustee's disposition of the estate assets, except with respect to the payment of those debts which for some reason are not dischargeable in the bankruptcy case. The individual debtor's primary concerns in a chapter 7 case are to retain exempt property and to receive a discharge that covers as many debts as possible.

f. The Chapter 7 Discharge

A discharge releases individual debtors from personal liability for most debts and prevents the creditors owed those debts from taking any collection actions against the debtor. Because a chapter 7 discharge is subject to many exceptions, though, debtors should consult competent legal counsel before filing to discuss the scope of the discharge. Generally, excluding cases that are dismissed or converted, individual debtors receive a discharge in more than 99 percent of chapter 7 cases. In most cases, unless a party in interest files a complaint objecting to the discharge or a motion to extend the time to object, the bankruptcy court will issue a discharge order relatively early in the case – generally, 60 to 90 days after the date first set for the meeting of creditors. Fed. R. Bankr. P. 4004(c).

The grounds for denying an individual debtor a discharge in a chapter 7 case are narrow and are construed against the moving party. Among other reasons, the court may deny the debtor a discharge if it finds that the debtor: failed to keep or produce adequate books or financial
records; failed to explain satisfactorily any loss of assets; committed a bankruptcy crime such as perjury; failed to obey a lawful order of the bankruptcy court; fraudulently transferred, concealed, or destroyed property that would have become property of the estate; or failed to complete an approved instructional course concerning financial management. 11 U.S.C. § 727; Fed. R. Bankr. P. 4005.

Secured creditors may retain some rights to seize property securing an underlying debt even after a discharge is granted. Depending on individual circumstances, if a debtor wishes to keep certain secured property (such as an automobile), he or she may decide to "reaffirm" the debt. A reaffirmation is an agreement between the debtor and the creditor that the debtor will remain liable and will pay all or a portion of the money owed, even though the debt would otherwise be discharged in the bankruptcy. In return, the creditor promises that it will not repossess or take back the automobile or other property so long as the debtor continues to pay the debt.

If the debtor decides to reaffirm a debt, he or she must do so before the discharge is entered. The debtor must sign a written reaffirmation agreement and file it with the court. 11 U.S.C. § 524(c). The Bankruptcy Code requires that reaffirmation agreements contain an extensive set of disclosures described in 11 U.S.C. § 524(k). Among other things, the disclosures must advise the debtor of the amount of the debt being reaffirmed and how it is calculated and that reaffirmation means that the debtor's personal liability for that debt will not be discharged in the bankruptcy. The disclosures also require the debtor to sign and file a statement of his or her current income and expenses which shows that the balance of income paying expenses is sufficient to pay the reaffirmed debt. If the balance is not enough to pay the debt to be reaffirmed, there is a presumption of undue hardship, and the court may decide not to approve the reaffirmation agreement. Unless the debtor is represented by an attorney, the bankruptcy judge must approve the reaffirmation agreement.

If the debtor was represented by an attorney in connection with the reaffirmation agreement, the attorney must certify in writing that he or she advised the debtor of the legal effect and consequences of the agreement, including a default under the agreement. The attorney must also certify that the debtor was fully informed and voluntarily made the agreement and that reaffirmation of the debt will not create an undue hardship for the debtor or the debtor's dependants. 11 U.S.C. § 524(k). The Bankruptcy Code requires a reaffirmation hearing if the debtor has not been represented by an attorney during the negotiating of the agreement, or if the court disapproves the reaffirmation agreement.11 U.S.C. § 524(d) and (m). The debtor may repay any debt voluntarily, however, whether or not a reaffirmation agreement exists. 11 U.S.C. § 524(f).

An individual receives a discharge for most of his or her debts in a chapter 7 bankruptcy case. A creditor may no longer initiate or continue any legal or other action against the debtor to collect a discharged debt. But not all of an individual's debts are discharged in chapter 7. Debts not discharged include debts for alimony and child support, certain taxes, debts for certain educational benefit overpayments or loans made or guaranteed by a governmental unit, debts for willful and malicious injury by the debtor to another entity or to the property of another entity, debts for death or personal injury caused by the debtor's operation of a motor vehicle while the debtor was intoxicated from alcohol or other substances, and debts for certain
criminal restitution orders. 11 U.S.C. § 523(a). The debtor will continue to be liable for these types of debts to the extent that they are not paid in the chapter 7 case. Debts for money or property obtained by false pretenses, debts for fraud or defalcation while acting in a fiduciary capacity, and debts for willful and malicious injury by the debtor to another entity or to the property of another entity will be discharged unless a creditor timely files and prevails in an action to have such debts declared nondischargeable. 11 U.S.C. § 523(c); Fed. R. Bankr. P. 4007(c).

The court may revoke a chapter 7 discharge on the request of the trustee, a creditor, or the U.S. trustee if the discharge was obtained through fraud by the debtor, if the debtor acquired property that is property of the estate and knowingly and fraudulently failed to report the acquisition of such property or to surrender the property to the trustee, or if the debtor (without a satisfactory explanation) makes a material misstatement or fails to provide documents or other information in connection with an audit of the debtor's case. 11 U.S.C. § 727(d).

3. Chapter 13: Individual Debt Adjustment
Chapter 13 of the Bankruptcy Code, entitled Adjustment of Debts of an Individual With Regular Income, is designed for an individual debtor who has a regular source of income. Chapter 13 is often preferable to chapter 7 because it enables the debtor to keep a valuable asset, such as a house, and because it allows the debtor to propose a "plan" to repay creditors over time – usually three to five years. Chapter 13 is also used by consumer debtors who do not qualify for chapter 7 relief under the means test. At a confirmation hearing, the court either approves or disapproves the debtor's repayment plan, depending on whether it meets the Bankruptcy Code's requirements for confirmation. Chapter 13 is very different from chapter 7 since the chapter 13 debtor usually remains in possession of the property of the estate and makes payments to creditors, through the trustee, based on the debtor's anticipated income over the life of the plan. Unlike chapter 7, the debtor does not receive an immediate discharge of debts. The debtor must complete the payments required under the plan before the discharge is received. The debtor is protected from lawsuits, garnishments, and other creditor actions while the plan is in effect. The discharge is also somewhat broader (i.e., more debts are eliminated) under chapter 13 than the discharge under chapter 7.

a. Background
A chapter 13 bankruptcy is also called a wage earner's plan. It enables individuals with regular income to develop a plan to repay all or part of their debts. Under this chapter, debtors propose a repayment plan to make installments to creditors over three to five years. If the debtor's current monthly income is less than the applicable state median, the plan will be for three years unless the court approves a longer period "for cause." (1) If the debtor's current monthly income is greater than the applicable state median, the plan generally must be for five years. In no case may a plan provide for payments over a period longer than five years. 11 U.S.C. §1322(d). During this time the law forbids creditors from starting or continuing collection efforts.

This chapter discusses six aspects of a chapter 13 proceeding: the advantages of choosing chapter 13, the chapter 13 eligibility requirements, how a chapter 13 proceeding works, what may be included in chapter 13 repayment plan and how it is confirmed, making the plan work, and the special chapter 13 discharge.
b. Advantages of Chapter 13
Chapter 13 offers individuals a number of advantages over liquidation under chapter 7. Perhaps most significantly, chapter 13 offers individuals an opportunity to save their homes from foreclosure. By filing under this chapter, individuals can stop foreclosure proceedings and may cure delinquent mortgage payments over time. Nevertheless, they must still make all mortgage payments that come due during the chapter 13 plan on time. Another advantage of chapter 13 is that it allows individuals to reschedule secured debts (other than a mortgage for their primary residence) and extend them over the life of the chapter 13 plan. Doing this may lower the payments. Chapter 13 also has a special provision that protects third parties who are liable with the debtor on "consumer debts." This provision may protect co-signers. Finally, chapter 13 acts like a consolidation loan under which the individual makes the plan payments to a chapter 13 trustee who then distributes payments to creditors. Individuals will have no direct contact with creditors while under chapter 13 protection.

c. Chapter 13 Eligibility
Any individual, even if self-employed or operating an unincorporated business, is eligible for chapter 13 relief as long as the individual's unsecured debts are less than $307,675 and secured debts are less than $922,975. 11 U.S.C. § 109(e). These amounts are adjusted periodically to reflect changes in the consumer price index. A corporation or partnership may not be a chapter 13 debtor. Id.

An individual cannot file under chapter 13 or any other chapter if, during the preceding 180 days, a prior bankruptcy petition was dismissed due to the debtor's willful failure to appear before the court or comply with orders of the court or was voluntarily dismissed after creditors sought relief from the bankruptcy court to recover property upon which they hold liens. 11 U.S.C. §§ 109(g), 362(d) and (e). In addition, no individual may be a debtor under chapter 13 or any chapter of the Bankruptcy Code unless he or she has, within 180 days before filing, received credit counseling from an approved credit counseling agency either in an individual or group briefing. 11 U.S.C. §§ 109, 111. There are exceptions in emergency situations or where the U.S. trustee (or bankruptcy administrator) has determined that there are insufficient approved agencies to provide the required counseling. If a debt management plan is developed during required credit counseling, it must be filed with the court.

d. How Chapter 13 Works
A chapter 13 case begins by filing a petition with the bankruptcy court serving the area where the debtor has a domicile or residence. Unless the court orders otherwise, the debtor must also file with the court: (1) schedules of assets and liabilities; (2) a schedule of current income and expenditures; (3) a schedule of executory contracts and unexpired leases; and (4) a statement of financial affairs. Fed. R. Bankr. P. 1007(b). The debtor must also file a certificate of credit counseling and a copy of any debt repayment plan developed through credit counseling; evidence of payment from employers, if any, received 60 days before filing; a statement of monthly net income and any anticipated increase in income or expenses after filing; and a record of any interest the debtor has in federal or state qualified education or tuition accounts. 11 U.S.C. § 521. The debtor must provide the chapter 13 case trustee with a copy of the tax return or transcripts for the most recent tax year as well as tax returns filed during the case (including tax returns for prior years that had not been filed when the case began). Id. A husband and wife may file a joint petition or individual petitions. 11 U.S.C. § 302(a). (The
Official Forms may be purchased at legal stationery stores or downloaded from the Internet at the United States Courts website. They are not available from the court.)

As of October 17, 2005, the courts must charge a $150 case filing fee and a $39 miscellaneous administrative fee. Normally the fees must be paid to the clerk of the court upon filing. With the court's permission, however, they may be paid in installments. 28 U.S.C. § 1930(a); Fed. R. Bankr. P. 1006(b); Bankruptcy Court Miscellaneous Fee Schedule, Item 8. The number of installments is limited to four, and the debtor must make the final installment no later than 120 days after filing the petition. Fed. R. Bankr. P. 1006(b). For cause shown, the court may extend the time of any installment, as long as the last installment is paid no later than 180 days after filing the petition. Id. The debtor may also pay the $39 administrative fee in installments. If a joint petition is filed, only one filing fee and one administrative fee are charged. Debtors should be aware that failure to pay these fees may result in dismissal of the case. 11 U.S.C. § 1307(c)(2).

In order to complete the Official Bankruptcy Forms that make up the petition, statement of financial affairs, and schedules, the debtor must compile the following information:

1. A list of all creditors and the amounts and nature of their claims;
2. The source, amount, and frequency of the debtor's income;
3. A list of all of the debtor's property; and
4. A detailed list of the debtor's monthly living expenses, i.e., food, clothing, shelter, utilities, taxes, transportation, medicine, etc.

Married individuals must gather this information for their spouse regardless of whether they are filing a joint petition, separate individual petitions, or even if only one spouse is filing. In a situation where only one spouse files, the income and expenses of the non-filing spouse is required so that the court, the trustee and creditors can evaluate the household's financial position.

When an individual files a chapter 13 petition, an impartial trustee is appointed to administer the case. 11 U.S.C. § 1302. In some districts, the U.S. trustee or bankruptcy administrator (2) appoints a standing trustee to serve in all chapter 13 cases. 28 U.S.C. § 586(b). The chapter 13 trustee both evaluates the case and serves as a disbursing agent, collecting payments from the debtor and making distributions to creditors. 11 U.S.C. § 1302(b).

Filing the petition under chapter 13 "automatically stays" (stops) most collection actions against the debtor or the debtor's property. 11 U.S.C. § 362. Filing the petition does not, however, stay certain types of actions listed under 11 U.S.C. § 362(b), and the stay may be effective only for a short time in some situations. The stay arises by operation of law and requires no judicial action. As long as the stay is in effect, creditors generally may not initiate or continue lawsuits, wage garnishments, or even make telephone calls demanding payments. The bankruptcy clerk gives notice of the bankruptcy case to all creditors whose names and addresses are provided by the debtor.

Chapter 13 also contains a special automatic stay provision that protects co-debtors. Unless
the bankruptcy court authorizes otherwise, a creditor may not seek to collect a "consumer debt" from any individual who is liable along with the debtor. 11 U.S.C. § 1301(a). Consumer debts are those incurred by an individual primarily for a personal, family, or household purpose. 11 U.S.C. § 101(8).

Individuals may use a chapter 13 proceeding to save their home from foreclosure. The automatic stay stops the foreclosure proceeding as soon as the individual files the chapter 13 petition. The individual may then bring the past-due payments current over a reasonable period of time. Nevertheless, the debtor may still lose the home if the mortgage company completes the foreclosure sale under state law before the debtor files the petition. 11 U.S.C. § 1322(c). The debtor may also lose the home if he or she fails to make the regular mortgage payments that come due after the chapter 13 filing.

Between 20 and 50 days after the debtor files the chapter 13 petition, the chapter 13 trustee will hold a meeting of creditors. If the U.S. trustee or bankruptcy administrator schedules the meeting at a place that does not have regular U.S. trustee or bankruptcy administrator staffing, the meeting may be held no more than 60 days after the debtor files. Fed. R. Bankr. P. 2003(a). During this meeting, the trustee places the debtor under oath, and both the trustee and creditors may ask questions. The debtor must attend the meeting and answer questions regarding his or her financial affairs and the proposed terms of the plan. 11 U.S.C. § 343. If a husband and wife file a joint petition, they both must attend the creditors' meeting and answer questions. In order to preserve their independent judgment, bankruptcy judges are prohibited from attending the creditors' meeting. 11 U.S.C. § 341(c). The parties typically resolve problems with the plan either during or shortly after the creditors' meeting. Generally, the debtor can avoid problems by making sure that the petition and plan are complete and accurate, and by consulting with the trustee prior to the meeting.

In a chapter 13 case, to participate in distributions from the bankruptcy estate, unsecured creditors must file their claims with the court within 90 days after the first date set for the meeting of creditors. Fed. R. Bankr. P. 3002(c). A governmental unit, however, has 180 days from the date the case is filed file a proof of claim. 11 U.S.C. § 502(b)(9).

After the meeting of creditors, the debtor, the chapter 13 trustee, and those creditors who wish to attend will come to court for a hearing on the debtor's chapter 13 repayment plan.

e. The Chapter 13 Plan and Confirmation Hearing

Unless the court grants an extension, the debtor must file a repayment plan with the petition or within 15 days after the petition is filed. Fed. R. Bankr. P. 3015. A plan must be submitted for court approval and must provide for payments of fixed amounts to the trustee on a regular basis, typically biweekly or monthly. The trustee then distributes the funds to creditors according to the terms of the plan, which may offer creditors less than full payment on their claims.

There are three types of claims: priority, secured, and unsecured. Priority claims are those granted special status by the bankruptcy law, such as most taxes and the costs of bankruptcy proceeding. (3) Secured claims are those for which the creditor has the right take back certain property (i.e., the collateral) if the debtor does not pay the underlying debt. In contrast to secured claims, unsecured claims are generally those for which the creditor has no special
rights to collect against particular property owned by the debtor.

The plan must pay priority claims in full unless a particular priority creditor agrees to different treatment of the claim or, in the case of a domestic support obligation, unless the debtor contributes all "disposable income" - discussed below - to a five-year plan. 11 U.S.C. § 1322(a).

If the debtor wants to keep the collateral securing a particular claim, the plan must provide that the holder of the secured claim receive at least the value of the collateral. If the obligation underlying the secured claim was used the buy the collateral (e.g., a car loan), and the debt was incurred within certain time frames before the bankruptcy filing, the plan must provide for full payment of the debt, not just the value of the collateral (which may be less due to depreciation). Payments to certain secured creditors (i.e., the home mortgage lender), may be made over the original loan repayment schedule (which may be longer than the plan) so long as any arrearage is made up during the plan. The debtor should consult an attorney to determine the proper treatment of secured claims in the plan.

The plan need not pay unsecured claims in full as long it provides that the debtor will pay all projected "disposable income" over an "applicable commitment period," and as long as unsecured creditors receive at least as much under the plan as they would receive if the debtor's assets were liquidated under chapter 7. 11 U.S.C. § 1325. In chapter 13, "disposable income" is income (other than child support payments received by the debtor) less amounts reasonably necessary for the maintenance or support of the debtor or dependents and less charitable contributions up to 15% of the debtor's gross income. If the debtor operates a business, the definition of disposable income excludes those amounts which are necessary for ordinary operating expenses. 11 U.S.C. § 1325(b)(2)(A) and (B). The "applicable commitment period" depends on the debtor's current monthly income. The applicable commitment period must be three years if current monthly income is less than the state median for a family of the same size - and five years if the current monthly income is greater than a family of the same size. 11 U.S.C. § 1325(d). The plan may be less than the applicable commitment period (three or five years) only if unsecured debt is paid in full over a shorter period.

Within 30 days after filing the bankruptcy case, even if the plan has not yet been approved by the court, the debtor must start making plan payments to the trustee. 11 U.S.C. § 1326(a)(1). If any secured loan payments or lease payments come due before the debtor's plan is confirmed (typically home and automobile payments), the debtor must make adequate protection payments directly to the secured lender or lessor - deducting the amount paid from the amount that would otherwise be paid to the trustee. Id.

No later than 45 days after the meeting of creditors, the bankruptcy judge must hold a confirmation hearing and decide whether the plan is feasible and meets the standards for confirmation set forth in the Bankruptcy Code. 11 U.S.C. §§ 1324, 1325. Creditors will receive 25 days' notice of the hearing and may object to confirmation. Fed. R. Bankr. P. 2002(b). While a variety of objections may be made, the most frequent ones are that payments offered under the plan are less than creditors would receive if the debtor's assets were liquidated or that the debtor's plan does not commit all of the debtor's projected disposable income for the three or five year applicable commitment period.
If the court confirms the plan, the chapter 13 trustee will distribute funds received under the plan "as soon as is practicable." 11 U.S.C. § 1326(a)(2). If the court declines to confirm the plan, the debtor may file a modified plan. 11 U.S.C. § 1323. The debtor may also convert the case to a liquidation case under chapter 7. (4) 11 U.S.C. § 1307(a). If the court declines to confirm the plan or the modified plan and instead dismisses the case, the court may authorize the trustee to keep some funds for costs, but the trustee must return all remaining funds to the debtor (other than funds already disbursed or due to creditors). 11 U.S.C. § 1326(a)(2).

Occasionally, a change in circumstances may compromise the debtor's ability to make plan payments. For example, a creditor may object or threaten to object to a plan, or the debtor may inadvertently have failed to list all creditors. In such instances, the plan may be modified either before or after confirmation. 11 U.S.C. §§ 1323, 1329. Modification after confirmation is not limited to an initiative by the debtor, but may be at the request of the trustee or an unsecured creditor. 11 U.S.C. § 1329(a).

f. Making the Plan Work
The provisions of a confirmed plan bind the debtor and each creditor. 11 U.S.C. § 1327. Once the court confirms the plan, the debtor must make the plan succeed. The debtor must make regular payments to the trustee either directly or through payroll deduction, which will require adjustment to living on a fixed budget for a prolonged period. Furthermore, while confirmation of the plan entitles the debtor to retain property as long as payments are made, the debtor may not incur new debt without consulting the trustee, because additional debt may compromise the debtor's ability to complete the plan. 11 U.S.C. §§ 1305(c), 1322(a)(1), 1327.

A debtor may make plan payments through payroll deductions. This practice increases the likelihood that payments will be made on time and that the debtor will complete the plan. In any event, if the debtor fails to make the payments due under the confirmed plan, the court may dismiss the case or convert it to a liquidation case under chapter 7 of the Bankruptcy Code. 11 U.S.C. § 1307(c). The court may also dismiss or convert the debtor's case if the debtor fails to pay any post-filing domestic support obligations (i.e., child support, alimony), or fails to make required tax filings during the case. 11 U.S.C. §§ 1307(c) and (e), 1308, 521.

g. The Chapter 13 Discharge
The bankruptcy law regarding the scope of the chapter 13 discharge is complex and has recently undergone major changes. Therefore, debtors should consult competent legal counsel prior to filing regarding the scope of the chapter 13 discharge.

A chapter 13 debtor is entitled to a discharge upon completion of all payments under the chapter 13 plan so long as the debtor: (1) certifies (if applicable) that all domestic support obligations that came due prior to making such certification have been paid; (2) has not received a discharge in a prior case filed within a certain time frame (two years for prior chapter 13 cases and four years for prior chapter 7, 11 and 12 cases); and (3) has completed an approved course in financial management (if the U.S. trustee or bankruptcy administrator for the debtor's district has determined that such courses are available to the debtor). 11 U.S.C. § 1328. The court will not enter the discharge, however, until it determines, after notice and a hearing, that there is no reason to believe there is any
pending proceeding that might give rise to a limitation on the debtor's homestead exemption. 11 U.S.C. § 1328(h).

The discharge releases the debtor from all debts provided for by the plan or disallowed (under section 502), with limited exceptions. Creditors provided for in full or in part under the chapter 13 plan may no longer initiate or continue any legal or other action against the debtor to collect the discharged obligations.

As a general rule, the discharge releases the debtor from all debts provided for by the plan or disallowed, with the exception of certain debts referenced in 11 U.S.C. § 1328. Debts not discharged in chapter 13 include certain long term obligations (such as a home mortgage), debts for alimony or child support, certain taxes, debts for most government funded or guaranteed educational loans or benefit overpayments, debts arising from death or personal injury caused by driving while intoxicated or under the influence of drugs, and debts for restitution or a criminal fine included in a sentence on the debtor's conviction of a crime. To the extent that they are not fully paid under the chapter 13 plan, the debtor will still be responsible for these debts after the bankruptcy case has concluded. Debts for money or property obtained by false pretenses, debts for fraud or defalcation while acting in a fiduciary capacity, and debts for restitution or damages awarded in a civil case for willful or malicious actions by the debtor that cause personal injury or death to a person will be discharged unless a creditor timely files and prevails in an action to have such debts declared nondischargeable. 11 U.S.C. §§ 1328, 523(c); Fed. R. Bankr. P. 4007(c).

The discharge in a chapter 13 case is somewhat broader than in a chapter 7 case. Debts dischargeable in a chapter 13, but not in chapter 7, include debts for willful and malicious injury to property (as opposed to a person), debts incurred to pay nondischargeable tax obligations, and debts arising from property settlements in divorce or separation proceedings. 11 U.S.C. § 1328(a).

h. The Chapter 13 Hardship Discharge
After confirmation of a plan, circumstances may arise that prevent the debtor from completing the plan. In such situations, the debtor may ask the court to grant a "hardship discharge." 11 U.S.C. § 1328(b). Generally, such a discharge is available only if: (1) the debtor's failure to complete plan payments is due to circumstances beyond the debtor's control and through no fault of the debtor; (2) creditors have received at least as much as they would have received in a chapter 7 liquidation case; and (3) modification of the plan is not possible. Injury or illness that precludes employment sufficient to fund even a modified plan may serve as the basis for a hardship discharge. The hardship discharge is more limited than the discharge described above and does not apply to any debts that are nondischargeable in a chapter 7 case. 11 U.S.C. § 523.

4. Chapter 11: Reorganization Under the Bankruptcy Code
Chapter 11 of the Bankruptcy Code, entitled Reorganization, ordinarily is used by commercial enterprises that desire to continue operating a business and repay creditors concurrently through a court-approved plan of reorganization. The chapter 11 debtor usually has the exclusive right to file a plan of reorganization for the first 120 days after it files the case and must provide creditors with a disclosure statement containing information adequate to enable creditors to evaluate the plan. The court ultimately approves (confirms) or disapproves the plan of
reorganization. Under the confirmed plan, the debtor can reduce its debts by repaying a portion of its obligations and discharging others. The debtor can also terminate burdensome contracts and leases, recover assets, and rescale its operations in order to return to profitability. Under chapter 11, the debtor normally goes through a period of consolidation and emerges with a reduced debt load and a reorganized business.

a. Background
A case filed under chapter 11 of the United States Bankruptcy Code is frequently referred to as a "reorganization" bankruptcy.

An individual cannot file under chapter 11 or any other chapter if, during the preceding 180 days, a prior bankruptcy petition was dismissed due to the debtor's willful failure to appear before the court or comply with orders of the court, or was voluntarily dismissed after creditors sought relief from the bankruptcy court to recover property upon which they hold liens. 11 U.S.C. §§ 109(g), 362(d)-(e). In addition, no individual may be a debtor under chapter 11 or any chapter of the Bankruptcy Code unless he or she has, within 180 days before filing, received credit counseling from an approved credit counseling agency either in an individual or group briefing. 11 U.S.C. §§ 109, 111. There are exceptions in emergency situations or where the U.S. trustee (or bankruptcy administrator) has determined that there are insufficient approved agencies to provide the required counseling. If a debt management plan is developed during required credit counseling, it must be filed with the court.

b. How Chapter 11 Works
A chapter 11 case begins with the filing of a petition with the bankruptcy court serving the area where the debtor has a domicile or residence. A petition may be a voluntary petition, which is filed by the debtor, or it may be an involuntary petition, which is filed by creditors that meet certain requirements. 11 U.S.C. §§ 301, 303. A voluntary petition must adhere to the format of Form 1 of the Official Forms prescribed by the Judicial Conference of the United States. Unless the court orders otherwise, the debtor also must file with the court: (1) schedules of assets and liabilities; (2) a schedule of current income and expenditures; (3) a schedule of executory contracts and unexpired leases; and (4) a statement of financial affairs. Fed. R. Bankr. P. 1007(b). If the debtor is an individual (or husband and wife), there are additional document filing requirements. Such debtors must file: a certificate of credit counseling and a copy of any debt repayment plan developed through credit counseling; evidence of payment from employers, if any, received 60 days before filing; a statement of monthly net income and any anticipated increase in income or expenses after filing; and a record of any interest the debtor has in federal or state qualified education or tuition accounts.11 U.S.C. § 521. A husband and wife may file a joint petition or individual petitions. 11 U.S.C. § 302(a). (The Official Forms are not available from the court, but may be purchased at legal stationery stores or downloaded from the Internet at the United States Courts website.)

As of October 17, 2005, the courts are required to charge an $1,000 case filing fee and a $39 miscellaneous administrative fee. The fees must be paid to the clerk of the court upon filing or may, with the court's permission, be paid by individual debtors in installments. 28 U.S.C. § 1930(a); Fed. R. Bankr. P. 1006(b); Bankruptcy Court Miscellaneous Fee Schedule, Item 8. Fed. R. Bankr. P. 1006(b) limits to four the number of installments for the filing fee. The final
installment must be paid not later than 120 days after filing the petition. For cause shown, the court may extend the time of any installment, provided that the last installment is paid not later than 180 days after the filing of the petition. Fed. R. Bankr. P. 1006(b). The $39 administrative fee may be paid in installments in the same manner as the filing fee. If a joint petition is filed, only one filing fee and one administrative fee are charged. Debtors should be aware that failure to pay these fees may result in dismissal of the case. 11 U.S.C. § 1112(b)(10).

The voluntary petition will include standard information concerning the debtor's name(s), social security number or tax identification number, residence, location of principal assets (if a business), the debtor's plan or intention to file a plan, and a request for relief under the appropriate chapter of the Bankruptcy Code. Upon filing a voluntary petition for relief under chapter 11 or, in an involuntary case, the entry of an order for relief, the debtor automatically assumes an additional identity as the "debtor in possession." 11 U.S.C. § 1101. The term refers to a debtor that keeps possession and control of its assets while undergoing a reorganization under chapter 11, without the appointment of a case trustee. A debtor will remain a debtor in possession until the debtor's plan of reorganization is confirmed, the debtor's case is dismissed or converted to chapter 7, or a chapter 11 trustee is appointed. The appointment or election of a trustee occurs only in a small number of cases. Generally, the debtor, as "debtor in possession," operates the business and performs many of the functions that a trustee performs in cases under other chapters. 11 U.S.C. § 1107(a).

Generally, a written disclosure statement and a plan of reorganization must be filed with the court. 11 U.S.C. §§ 1121, 1125. The disclosure statement is a document that must contain information concerning the assets, liabilities, and business affairs of the debtor sufficient to enable a creditor to make an informed judgment about the debtor's plan of reorganization. 11 U.S.C. § 1125. The information required is governed by judicial discretion and the circumstances of the case. In a "small business case" (discussed below) the debtor may not need to file a separate disclosure statement if the court determines that adequate information is contained in the plan. 11 U.S.C. § 1125(f). The contents of the plan must include a classification of claims and must specify how each class of claims will be treated under the plan. 11 U.S.C. § 1123. Creditors whose claims are "impairment," i.e., those whose contractual rights are to be modified or who will be paid less than the full value of their claims under the plan, vote on the plan by ballot. 11 U.S.C. § 1126. After the disclosure statement is approved by the court and the ballots are collected and tallied, the court will conduct a confirmation hearing to determine whether to confirm the plan. 11 U.S.C. § 1128.

In the case of individuals, chapter 11 bears some similarities to chapter 13. For example, property of the estate for an individual debtor includes the debtor's earnings and property acquired by the debtor after filing until the case is closed, dismissed or converted; funding of the plan may be from the debtor's future earnings; and the plan cannot be confirmed over a creditor's objection without committing all of the debtor's disposable income over five years unless the plan pays the claim in full, with interest, over a shorter period of time. 11 U.S.C. §§ 1115, 1123(a)(8), 1129(a)(15).
c. The Chapter 11 Debtor in Possession
Chapter 11 is typically used to reorganize a business, which may be a corporation, sole proprietorship, or partnership. A corporation exists separate and apart from its owners, the stockholders. The chapter 11 bankruptcy case of a corporation (corporation as debtor) does not put the personal assets of the stockholders at risk other than the value of their investment in the company's stock. A sole proprietorship (owner as debtor), on the other hand, does not have an identity separate and distinct from its owner(s). Accordingly, a bankruptcy case involving a sole proprietorship includes both the business and personal assets of the owners—debtors. Like a corporation, a partnership exists separate and apart from its partners. In a partnership bankruptcy case (partnership as debtor), however, the partners' personal assets may, in some cases, be used to pay creditors in the bankruptcy case or the partners, themselves, may be forced to file for bankruptcy protection.

Section 1107 of the Bankruptcy Code places the debtor in possession in the position of a fiduciary, with the rights and powers of a chapter 11 trustee, and it requires the debtor to perform of all but the investigative functions and duties of a trustee. These duties, set forth in the Bankruptcy Code and Federal Rules of Bankruptcy Procedure, include accounting for property, examining and objecting to claims, and filing informational reports as required by the court and the U.S. trustee or bankruptcy administrator (discussed below), such as monthly operating reports. 11 U.S.C. §§ 1106, 1107; Fed. R. Bankr. P. 2015(a). The debtor in possession also has many of the other powers and duties of a trustee, including the right, with the court's approval, to employ attorneys, accountants, appraisers, auctioneers, or other professional persons to assist the debtor during its bankruptcy case. Other responsibilities include filing tax returns and reports which are either necessary or ordered by the court after confirmation, such as a final accounting. The U.S. trustee is responsible for monitoring the compliance of the debtor in possession with the reporting requirements.

Railroad reorganizations have specific requirements under subsection IV of chapter 11, which will not be addressed here. In addition, stock and commodity brokers are prohibited from filing under chapter 11 and are restricted to chapter 7. 11 U.S.C. § 109(d).

d. The U.S. trustee or bankruptcy administrator
The U.S. trustee plays a major role in monitoring the progress of a chapter 11 case and supervising its administration. The U.S. trustee is responsible for monitoring the debtor in possession's operation of the business and the submission of operating reports and fees. Additionally, the U.S. trustee monitors applications for compensation and reimbursement by professionals, plans and disclosure statements filed with the court, and creditors' committees. The U.S. trustee conducts a meeting of the creditors, often referred to as the "section 341 meeting," in a chapter 11 case. 11 U.S.C. § 341. The U.S. trustee and creditors may question the debtor under oath at the section 341 meeting concerning the debtor's acts, conduct, property, and the administration of the case.

The U.S. trustee also imposes certain requirements on the debtor in possession concerning matters such as reporting its monthly income and operating expenses, establishing new bank accounts, and paying current employee withholding and other taxes. By law, the debtor in possession must pay a quarterly fee to the U.S. trustee for each quarter of a year until the case
is converted or dismissed. 28 U.S.C. § 1930(a)(6). The amount of the fee, which may range from $250 to $10,000, depends on the amount of the debtor's disbursements during each quarter. Should a debtor in possession fail to comply with the reporting requirements of the U.S. trustee or orders of the bankruptcy court, or fail to take the appropriate steps to bring the case to confirmation, the U.S. trustee may file a motion with the court to have the debtor's chapter 11 case converted to another chapter of the Bankruptcy Code or to have the case dismissed. In North Carolina and Alabama, bankruptcy administrators perform similar functions that U.S. trustees perform in the remaining forty-eight states. The bankruptcy administrator program is administered by the Administrative Office of the United States Courts, while the U.S. trustee program is administered by the Department of Justice. For purposes of this publication, references to U.S. trustees are also applicable to bankruptcy administrators.

e. Creditors' Committees
Creditors' committees can play a major role in chapter 11 cases. The committee is appointed by the U.S. trustee and ordinarily consists of unsecured creditors who hold the seven largest unsecured claims against the debtor. 11 U.S.C. § 1102. Among other things, the committee: consults with the debtor in possession on administration of the case; investigates the debtor's conduct and operation of the business; and participates in formulating a plan. 11 U.S.C. § 1103. A creditors' committee may, with the court's approval, hire an attorney or other professionals to assist in the performance of the committee's duties. A creditors' committee can be an important safeguard to the proper management of the business by the debtor in possession.

In some smaller cases the U.S. trustee may be unable to find creditors willing to serve on a creditors' committee, or the committee may not be actively involved in the case. The Bankruptcy Code addresses this issue by treating a "small business case" somewhat differently than a regular bankruptcy case. A small business case is defined as a case with a "small business debtor." 11 U.S.C. § 101(51C). Determination of whether a debtor is a "small business debtor" requires application of a two-part test. First, the debtor must be engaged in commercial or business activities (other than primarily owning or operating real property) with total non-contingent liquidated secured and unsecured debts of $2,000,000 or less. Second, the debtor's case must be one in which the U.S. trustee has not appointed a creditors' committee, or the court has determined the creditors' committee is insufficiently active and representative to provide oversight of the debtor. 11 U.S.C. § 101(51D).

In a small business case, the debtor in possession must, among other things, attach the most recently prepared balance sheet, statement of operations, cash-flow statement and most recently filed tax return to the petition or provide a statement under oath explaining the absence of such documents and must attend court and the U.S. trustee meeting through senior management personnel and counsel. The small business debtor must make ongoing filings with the court concerning its profitability and projected cash receipts and disbursements, and must report whether it is in compliance with the Bankruptcy Code and the Federal Rules of Bankruptcy Procedure and whether it has paid its taxes and filed its tax returns. 11 U.S.C. §§ 308, 1116.
In contrast to other chapter 11 debtors, the small business debtor is subject to additional oversight by the U.S. trustee. Early in the case, the small business debtor must attend an "initial interview" with the U.S. trustee at which time the U.S. trustee will evaluate the debtor's viability, inquire about the debtor's business plan, and explain certain debtor obligations including the debtor's responsibility to file various reports. 28 U.S.C. § 586(a)(7). The U.S. trustee will also monitor the activities of the small business debtor during the case to identify as promptly as possible whether the debtor will be unable to confirm a plan. Because certain filing deadlines are different and extensions are more difficult to obtain, a case designated as a small business case normally proceeds more quickly than other chapter 11 cases. For example, only the debtor may file a plan during the first 180 days of a small business case. 11 U.S.C. § 1121(e). This "exclusivity period" may be extended by the court, but only to 300 days, and only if the debtor demonstrates by a preponderance of the evidence that the court will confirm a plan within a reasonable period of time. When the case is not a small business case, however, the court may extend the exclusivity period "for cause" up to 18 months.

g. The Single Asset Real Estate Debtor
Single asset real estate debtors are subject to special provisions of the Bankruptcy Code. The term "single asset real estate" is defined as "a single property or project, other than residential real property with fewer than four residential units, which generates substantially all of the gross income of a debtor who is not a family farmer and on which no substantial business is being conducted by a debtor other than the business of operating the real property and activities incidental." 11 U.S.C. § 101(51B). The Bankruptcy Code provides circumstances under which creditors of a single asset real estate debtor may obtain relief from the automatic stay which are not available to creditors in ordinary bankruptcy cases. 11 U.S.C. § 362(d). On request of a creditor with a claim secured by the single asset real estate and after notice and a hearing, the court will grant relief from the automatic stay to the creditor unless the debtor files a feasible plan of reorganization or begins making interest payments to the creditor within 90 days from the date of the filing of the case, or within 30 days of the court's determination that the case is a single asset real estate case. The interest payments must be equal to the non-default contract interest rate on the value of the creditor's interest in the real estate. 11 U.S.C. § 362(d)(3).

h. Appointment or Election of a Case Trustee
Although the appointment of a case trustee is a rarity in a chapter 11 case, a party in interest or the U.S. trustee can request the appointment of a case trustee or examiner at any time prior to confirmation in a chapter 11 case. The court, on motion by a party in interest or the U.S. trustee and after notice and hearing, shall order the appointment of a case trustee for cause, including fraud, dishonesty, incompetence, or gross mismanagement, or if such an appointment is in the interest of creditors, any equity security holders, and other interests of the estate. 11 U.S.C. § 1104(a). Moreover, the U.S. trustee is required to move for appointment of a trustee if there are reasonable grounds to believe that any of the parties in control of the debtor "participated in actual fraud, dishonesty or criminal conduct in the management of the debtor or the debtor's financial reporting." 11 U.S.C. § 1104(e). The trustee is appointed by the U.S. trustee, after consultation with parties in interest and subject to the court's approval. Fed. R. Bankr. P. 2007.1. Alternatively, a trustee in a case may be elected.
if a party in interest requests the election of a trustee within 30 days after the court orders the appointment of a trustee. In that instance, the U.S. trustee convenes a meeting of creditors for the purpose of electing a person to serve as trustee in the case. 11 U.S.C. § 1104(b).

The case trustee is responsible for management of the property of the estate, operation of the debtor's business, and, if appropriate, the filing of a plan of reorganization. Section 1106 of the Bankruptcy Code requires the trustee to file a plan "as soon as practicable" or, alternatively, to file a report explaining why a plan will not be filed or to recommend that the case be converted to another chapter or dismissed. 11 U.S.C. § 1106(a)(5).

Upon the request of a party in interest or the U.S. trustee, the court may terminate the trustee's appointment and restore the debtor in possession to management of bankruptcy estate at any time before confirmation. 11 U.S.C. § 1105.

i. The Role of an Examiner
The appointment of an examiner in a chapter 11 case is rare. The role of an examiner is generally more limited than that of a trustee. The examiner is authorized to perform the investigatory functions of the trustee and is required to file a statement of any investigation conducted. If ordered to do so by the court, however, an examiner may carry out any other duties of a trustee that the court orders the debtor in possession not to perform. 11 U.S.C. § 1106. Each court has the authority to determine the duties of an examiner in each particular case. In some cases, the examiner may file a plan of reorganization, negotiate or help the parties negotiate, or review the debtor's schedules to determine whether some of the claims are improperly categorized. Sometimes, the examiner may be directed to determine if objections to any proofs of claim should be filed or whether causes of action have sufficient merit so that further legal action should be taken. The examiner may not subsequently serve as a trustee in the case. 11 U.S.C. § 321.

j. The Automatic Stay
The automatic stay provides a period of time in which all judgments, collection activities, foreclosures, and repossessions of property are suspended and may not be pursued by the creditors on any debt or claim that arose before the filing of the bankruptcy petition. As with cases under other chapters of the Bankruptcy Code, a stay of creditor actions against the chapter 11 debtor automatically goes into effect when the bankruptcy petition is filed. 11 U.S.C. § 362(a). The filing of a petition, however, does not operate as a stay for certain types of actions listed under 11 U.S.C. § 362(b). The stay provides a breathing spell for the debtor, during which negotiations can take place to try to resolve the difficulties in the debtor's financial situation.

Under specific circumstances, the secured creditor can obtain an order from the court granting relief from the automatic stay. For example, when the debtor has no equity in the property and the property is not necessary for an effective reorganization, the secured creditor can seek an order of the court lifting the stay to permit the creditor to foreclose on the property, sell it, and apply the proceeds to the debt. 11 U.S.C. § 362(d).

The Bankruptcy Code permits applications for fees to be made by certain professionals during
the case. Thus, a trustee, a debtor's attorney, or any professional person appointed by the court may apply to the court at intervals of 120 days for interim compensation and reimbursement payments. In very large cases with extensive legal work, the court may permit more frequent applications. Although professional fees may be paid if authorized by the court, the debtor cannot make payments to professional creditors on prepetition obligations, i.e., obligations which arose before the filing of the bankruptcy petition. The ordinary expenses of the ongoing business, however, continue to be paid.

k. Who Can File a Plan
The debtor (unless a "small business debtor") has a 120-day period during which it has an exclusive right to file a plan. 11 U.S.C. § 1121(b). This exclusivity period may be extended or reduced by the court. But, in no event, may the exclusivity period, including all extensions, be longer than 18 months. 11 U.S.C. § 1121(d). After the exclusivity period has expired, a creditor or the case trustee may file a competing plan. The U.S. trustee may not file a plan. 11 U.S.C. § 307.

A chapter 11 case may continue for many years unless the court, the U.S. trustee, the committee, or another party in interest acts to ensure the case's timely resolution. The creditors' right to file a competing plan provides incentive for the debtor to file a plan within the exclusivity period and acts as a check on excessive delay in the case.

l. Avoidable Transfers
The debtor in possession or the trustee, as the case may be, has what are called "avoiding" powers. These powers may be used to undo a transfer of money or property made during a certain period of time before the filing of the bankruptcy petition. By avoiding a particular transfer of property, the debtor in possession can cancel the transaction and force the return or "disgorgement" of the payments or property, which then are available to pay all creditors. Generally, and subject to various defenses, the power to avoid transfers is effective against transfers made by the debtor within 90 days before filing the petition. But transfers to "insiders" (i.e., relatives, general partners, and directors or officers of the debtor) made up to a year before filing may be avoided. 11 U.S.C. §§ 101(31), 101(54), 547, 548. In addition, under 11 U.S.C. § 544, the trustee is authorized to avoid transfers under applicable state law, which often provides for longer time periods. Avoiding powers prevent unfair prepetition payments to one creditor at the expense of all other creditors.

m. Cash Collateral, Adequate Protection, and Operating Capital
Although the preparation, confirmation, and implementation of a plan of reorganization is at the heart of a chapter 11 case, other issues may arise that must be addressed by the debtor in possession. The debtor in possession may use, sell, or lease property of the estate in the ordinary course of its business, without prior approval, unless the court orders otherwise. 11 U.S.C. § 363(c). If the intended sale or use is outside the ordinary course of its business, the debtor must obtain permission from the court.

A debtor in possession may not use "cash collateral" without the consent of the secured party or authorization by the court, which must first examine whether the interest of the secured party is adequately protected. 11 U.S.C. § 363. Section 363 defines "cash collateral" as cash,
negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents, whenever acquired, in which the estate and an entity other than the estate have an interest. It includes the proceeds, products, offspring, rents, or profits of property and the fees, charges, accounts or payments for the use or occupancy of rooms and other public facilities in hotels, motels, or other lodging properties subject to a creditor's security interest.

When "cash collateral" is used (spent), the secured creditors are entitled to receive additional protection under section 363 of the Bankruptcy Code. The debtor in possession must file a motion requesting an order from the court authorizing the use of the cash collateral. Pending consent of the secured creditor or court authorization for the debtor in possession's use of cash collateral, the debtor in possession must segregate and account for all cash collateral in its possession. 11 U.S.C. § 363(c)(4). A party with an interest in property being used by the debtor may request that the court prohibit or condition this use to the extent necessary to provide "adequate protection" to the creditor.

Adequate protection may be required to protect the value of the creditor's interest in the property being used by the debtor in possession. This is especially important when there is a decrease in value of the property. The debtor may make periodic or lump sum cash payments, or provide an additional or replacement lien that will result in the creditor's property interest being adequately protected. 11 U.S.C. § 361.

When a chapter 11 debtor needs operating capital, it may be able to obtain it from a lender by giving the lender a court-approved "superpriority" over other unsecured creditors or a lien on property of the estate. 11 U.S.C. § 364.

n. Motions

Before confirmation of a plan, several activities may take place in a chapter 11 case. Continued operation of the debtor's business may lead to the filing of a number of contested motions. The most common are those seeking relief from the automatic stay, the use of cash collateral, or to obtain credit. There may also be litigation over executory (i.e., unfulfilled) contracts and unexpired leases and the assumption or rejection of those executory contracts and unexpired leases by the debtor in possession. 11 U.S.C. § 365. Delays in formulating, filing, and obtaining confirmation of a plan often prompt creditors to file motions for relief from stay, to convert the case to chapter 7, or to dismiss the case altogether.

o. Adversary Proceedings

Frequently, the debtor in possession will institute a lawsuit, known as an adversary proceeding, to recover money or property for the estate. Adversary proceedings may take the form of lien avoidance actions, actions to avoid preferences, actions to avoid fraudulent transfers, or actions to avoid post-petition transfers. These proceedings are governed by Part VII of the Federal Rules of Bankruptcy Procedure. At times, a creditors’ committee may be authorized by the bankruptcy court to pursue these actions against insiders of the debtor if the plan provides for the committee to do so or if the debtor has refused a demand to do so. Creditors may also initiate adversary proceedings by filing complaints to determine the validity or priority of a lien, revoke an order confirming a plan, determine the dischargeability of a debt, obtain an injunction, or subordinate a claim of another creditor.
p. Claims
The Bankruptcy Code defines a claim as: (1) a right to payment; (2) or a right to an equitable remedy for a failure of performance if the breach gives rise to a right to payment. 11 U.S.C. § 101(5). Generally, any creditor whose claim is not scheduled (i.e., listed by the debtor on the debtor's schedules) or is scheduled as disputed, contingent, or unliquidated must file a proof of claim (and attach evidence documenting the claim) in order to be treated as a creditor for purposes of voting on the plan and distribution under it. Fed. R. Bankr. P. 3003(c)(2). But filing a proof of claim is not necessary if the creditor's claim is scheduled (but is not listed as disputed, contingent, or unliquidated by the debtor) because the debtor's schedules are deemed to constitute evidence of the validity and amount of those claims. 11 U.S.C. § 1111. If a scheduled creditor chooses to file a claim, a properly filed proof of claim supersedes any scheduling of that claim. Fed. R. Bankr. P. 3003(c)(4). It is the responsibility of the creditor to determine whether the claim is accurately listed on the debtor's schedules. The debtor must provide notification to those creditors whose names are added and whose claims are listed as a result of an amendment to the schedules. The notification also should advise such creditors of their right to file proofs of claim and that their failure to do so may prevent them from voting upon the debtor's plan of reorganization or participating in any distribution under that plan. When a debtor amends the schedule of liabilities to add a creditor or change the status of any claims to disputed, contingent, or unliquidated, the debtor must provide notice of the amendment to any entity affected. Fed. R. Bankr. P. 1009(a).

q. Equity Security Holders
An equity security holder is a holder of an equity security of the debtor. Examples of an equity security are a share in a corporation, an interest of a limited partner in a limited partnership, or a right to purchase, sell, or subscribe to a share, security, or interest of a share in a corporation or an interest in a limited partnership. 11 U.S.C. § 101(16), (17). An equity security holder may vote on the plan of reorganization and may file a proof of interest, rather than a proof of claim. A proof of interest is deemed filed for any interest that appears in the debtor's schedules, unless it is scheduled as disputed, contingent, or unliquidated. 11 U.S.C. § 1111. An equity security holder whose interest is not scheduled or scheduled as disputed, contingent, or unliquidated must file a proof of interest in order to be treated as a creditor for purposes of voting on the plan and distribution under it. Fed. R. Bankr. P. 3003(c)(2). A properly filed proof of interest supersedes any scheduling of that interest. Fed. R. Bankr. P. 3003(c)(4). Generally, most of the provisions that apply to proofs of claim, as discussed above, are also applicable to proofs of interest.

r. Conversion or Dismissal
A debtor in a case under chapter 11 has a one-time absolute right to convert the chapter 11 case to a case under chapter 7 unless: (1) the debtor is not a debtor in possession; (2) the case originally was commenced as an involuntary case under chapter 11; or (3) the case was converted to a case under chapter 11 other than at the debtor's request. 11 U.S.C. § 1112(a). A debtor in a chapter 11 case does not have an absolute right to have the case dismissed upon request.

A party in interest may file a motion to dismiss or convert a chapter 11 case to a chapter 7 case "for cause." Generally, if cause is established after notice and hearing, the court must
convert or dismiss the case (whichever is in the best interests of creditors and the estate) unless it specifically finds that the requested conversion or dismissal is not in the best interest of creditors and the estate. 11 U.S.C. § 1112(b). Alternatively, the court may decide that appointment of a chapter 11 trustee or an examiner is in the best interests of creditors and the estate. 11 U.S.C. § 1104(a)(3). Section 1112(b)(4) of the Bankruptcy Code sets forth numerous examples of cause that would support dismissal or conversion. For example, the moving party may establish cause by showing that there is substantial or continuing loss to the estate and the absence of a reasonable likelihood of rehabilitation; gross mismanagement of the estate; failure to maintain insurance that poses a risk to the estate or the public; or unauthorized use of cash collateral that is substantially harmful to a creditor.

Cause for dismissal or conversion also includes an unexcused failure to timely comply with reporting and filing requirements; failure to attend the meeting of creditors or attend a Fed. R. Bankr. P. 2004 examination without good cause; failure to timely provide information to the U.S. trustee; and failure to timely pay post-petition taxes or timely file post-petition returns. Additionally, failure to file a disclosure statement or to file and confirm a plan within the time fixed by the Bankruptcy Code or order of the court; inability to effectuate a plan; denial or revocation of confirmation; inability to consummate a confirmed plan represent "cause" for dismissal under the statute. In an individual case, failure of the debtor to pay post-petition domestic support obligations constitutes "cause" for dismissal or conversion.

Section 1112(c) of the Bankruptcy Code provides an important exception to the conversion process in a chapter 11 case. Under this provision, the court is prohibited from converting a case involving a farmer or charitable institution to a liquidation case under chapter 7 unless the debtor requests the conversion.

s. The Disclosure Statement
Generally, the debtor (or any plan proponent) must file and get court approval of a written disclosure statement before there can be a vote on the plan of reorganization. The disclosure statement must provide "adequate information" concerning the affairs of the debtor to enable the holder of a claim or interest to make an informed judgment about the plan. 11 U.S.C. §1125. In a small business case, however, the court may determine that the plan itself contains adequate information and that a separate disclosure statement is unnecessary. 11 U.S.C. § 1125(f). After the disclosure statement is filed, the court must hold a hearing to determine whether the disclosure statement should be approved. Acceptance or rejection of a plan usually cannot be solicited until the court has first approved the written disclosure statement. 11 U.S.C. § 1125(b). An exception to this rule exists if the initial solicitation of the party occurred before the bankruptcy filing, as would be the case in so-called "prepackaged" bankruptcy plans (i.e., where the debtor negotiates a plan with significant creditor constituencies before filing for bankruptcy). Continued post-filing solicitation of such parties is not prohibited. After the court approves the disclosure statement, the debtor or proponent of a plan can begin to solicit acceptances of the plan, and creditors may also solicit rejections of the plan.

Upon approval of a disclosure statement, the plan proponent must mail the following to the U.S. trustee and all creditors and equity security holders: (1) the plan, or a court approved
summary of the plan; (2) the disclosure statement approved by the court; (3) notice of the time within which acceptances and rejections of the plan may be filed; and (4) such other information as the court may direct, including any opinion of the court approving the disclosure statement or a court-approved summary of the opinion. Fed. R. Bankr. P. 3017(d).

In addition, the debtor must mail to the creditors and equity security holders entitled to vote on the plan or plans: (1) notice of the time fixed for filing objections; (2) notice of the date and time for the hearing on confirmation of the plan; and (3) a ballot for accepting or rejecting the plan and, if appropriate, a designation for the creditors to identify their preference among competing plans. Id. But in a small business case, the court may conditionally approve a disclosure statement subject to final approval after notice and a combined disclosure statement/plan confirmation hearing. 11 U.S.C. § 1125(f).

t. Acceptance of the Plan of Reorganization

As noted earlier, only the debtor may file a plan of reorganization during the first 120-day period after the petition is filed (or after entry of the order for relief, if an involuntary petition was filed). The court may grant extension of this exclusive period up to 18 months after the petition date. In addition, the debtor has 180 days after the petition date or entry of the order for relief to obtain acceptances of its plan. 11 U.S.C. § 1121. The court may extend (up to 20 months) or reduce this acceptance exclusive period for cause. 11 U.S.C. § 1121(d). In practice, debtors typically seek extensions of both the plan filing and plan acceptance deadlines at the same time so that any order sought from the court allows the debtor two months to seek acceptances after filing a plan before any competing plan can be filed.

If the exclusive period expires before the debtor has filed and obtained acceptance of a plan, other parties in interest in a case, such as the creditors' committee or a creditor, may file a plan. Such a plan may compete with a plan filed by another party in interest or by the debtor. If a trustee is appointed, the trustee must file a plan, a report explaining why the trustee will not file a plan, or a recommendation for conversion or dismissal of the case. 11 U.S.C. § 1106(a)(5). A proponent of a plan is subject to the same requirements as the debtor with respect to disclosure and solicitation.

In a chapter 11 case, a liquidating plan is permissible. Such a plan often allows the debtor in possession to liquidate the business under more economically advantageous circumstances than a chapter 7 liquidation. It also permits the creditors to take a more active role in fashioning the liquidation of the assets and the distribution of the proceeds than in a chapter 7 case.

Section 1123(a) of the Bankruptcy Code lists the mandatory provisions of a chapter 11 plan, and section 1123(b) lists the discretionary provisions. Section 1123(a)(1) provides that a chapter 11 plan must designate classes of claims and interests for treatment under the reorganization. Generally, a plan will classify claim holders as secured creditors, unsecured creditors entitled to priority, general unsecured creditors, and equity security holders.

Under section 1126(c) of the Bankruptcy Code, an entire class of claims is deemed to accept a plan if the plan is accepted by creditors that hold at least two-thirds in amount and more than one-half in number of the allowed claims in the class. Under section 1129(a)(10), if there are impaired classes of claims, the court cannot confirm a plan unless it has been accepted by at
least one class of non-insiders who hold impaired claims (i.e., claims that are not going to be paid completely or in which some legal, equitable, or contractual right is altered). Moreover, under section 1126(f), holders of unimpaired claims are deemed to have accepted the plan.

Under section 1127(a) of the Bankruptcy Code, the plan proponent may modify the plan at any time before confirmation, but the plan as modified must meet all the requirements of chapter 11. When there is a proposed modification after balloting has been conducted, and the court finds after a hearing that the proposed modification does not adversely affect the treatment of any creditor who has not accepted the modification in writing, the modification is deemed to have been accepted by all creditors who previously accepted the plan. Fed. R. Bankr. P. 3019. If it is determined that the proposed modification does have an adverse effect on the claims of non-consenting creditors, then another balloting must take place.

Because more than one plan may be submitted to the creditors for approval, every proposed plan and modification must be dated and identified with the name of the entity or entities submitting the plan or modification. Fed. R. Bankr. P. 3016(b). When competing plans are presented that meet the requirements for confirmation, the court must consider the preferences of the creditors and equity security holders in determining which plan to confirm.

Any party in interest may file an objection to confirmation of a plan. The Bankruptcy Code requires the court, after notice, to hold a hearing on confirmation of a plan. If no objection to confirmation has been timely filed, the Bankruptcy Code allows the court to determine whether the plan has been proposed in good faith and according to law. Fed. R. Bankr. P. 3020(b)(2). Before confirmation can be granted, the court must be satisfied that there has been compliance with all the other requirements of confirmation set forth in section 1129 of the Bankruptcy Code, even in the absence of any objections. In order to confirm the plan, the court must find, among other things, that: (1) the plan is feasible; (2) it is proposed in good faith; and (3) the plan and the proponent of the plan are in compliance with the Bankruptcy Code. In order to satisfy the feasibility requirement, the court must find that confirmation of the plan is not likely to be followed by liquidation (unless the plan is a liquidating plan) or the need for further financial reorganization.

u. The Discharge
Section 1141(d)(1) generally provides that confirmation of a plan discharges a debtor from any debt that arose before the date of confirmation. After the plan is confirmed, the debtor is required to make plan payments and is bound by the provisions of the plan of reorganization. The confirmed plan creates new contractual rights, replacing or superseding pre-bankruptcy contracts.

There are, of course, exceptions to the general rule that an order confirming a plan operates as a discharge. Confirmation of a plan of reorganization discharges any type of debtor – corporation, partnership, or individual – from most types of prepetition debts. It does not, however, discharge an individual debtor from any debt made nondischargeable by section 523 of the Bankruptcy Code. (1) Moreover, except in limited circumstances, a discharge is not available to an individual debtor unless and until all payments have been made under the plan. 11 U.S.C. § 1141(d)(5). Confirmation does not discharge the debtor if the plan is a liquidation
plan, as opposed to one of reorganization, unless the debtor is an individual. When the debtor is an individual, confirmation of a liquidation plan will result in a discharge (after plan payments are made) unless grounds would exist for denying the debtor a discharge if the case were proceeding under chapter 7 instead of chapter 11. 11 U.S.C. §§ 727(a), 1141(d).

v. Postconfirmation Modification of the Plan At any time after confirmation and before "substantial consummation" of a plan, the proponent of a plan may modify the plan if the modified plan would meet certain Bankruptcy Code requirements. 11 U.S.C. § 1127(b). This should be distinguished from preconfirmation modification of the plan. A modified postconfirmation plan does not automatically become the plan. A modified postconfirmation plan in a chapter 11 case becomes the plan only "if circumstances warrant such modification" and the court, after notice and hearing, confirms the plan as modified. If the debtor is an individual, the plan may be modified postconfirmation upon the request of the debtor, the trustee, the U.S. trustee, or the holder of an allowed unsecured claim to make adjustments to payments due under the plan. 11 U.S.C. § 1127(e).

w. Postconfirmation Administration
Notwithstanding the entry of the confirmation order, the court has the authority to issue any other order necessary to administer the estate. Fed. R. Bankr. P. 3020(d). This authority would include the postconfirmation determination of objections to claims or adversary proceedings, which must be resolved before a plan can be fully consummated. Sections 1106(a)(7) and 1107(a) of the Bankruptcy Code require a debtor in possession or a trustee to report on the progress made in implementing a plan after confirmation. A chapter 11 trustee or debtor in possession has a number of responsibilities to perform after confirmation, including consummating the plan, reporting on the status of consummation, and applying for a final decree.

x. Revocation of the Confirmation Order
Revocation of the confirmation order is an undoing or cancellation of the confirmation of a plan. A request for revocation of confirmation, if made at all, must be made by a party in interest within 180 days of confirmation. The court, after notice and hearing, may revoke a confirmation order "if and only if the [confirmation] order was procured by fraud." 11 U.S.C. § 1144.

y. The Final Decree
A final decree closing the case must be entered after the estate has been "fully administered." Fed. R. Bankr. P. 3022. Local bankruptcy court policies generally determine when the final decree is entered and the case closed.

5. Chapter 12: Adjustment of Debts of a Family Farmer or Fisherman with Regular Annual Income
Chapter 12, entitled Adjustment of Debts of a Family Farmer or Fisherman with Regular Annual Income, provides debt relief to family farmers and fishermen with regular income. The process under chapter 12 is very similar to that of chapter 13, under which the debtor proposes a plan to repay debts over a period of time – no more than three years unless the court approves a longer period, not exceeding five years. There is also a trustee in every chapter 12 case whose duties are very similar to those of a chapter 13 trustee. The chapter 12 trustee's disbursement of
payments to creditors under a confirmed plan parallels the procedure under chapter 13. Chapter 12 allows a family farmer or fisherman to continue to operate the business while the plan is being carried out.

Explore the following Websites:
U.S. Bankruptcy Code (Cornell University Law School Legal Information Institute)
Federal Rules of Bankruptcy Procedure (Cornell University Law School Legal Information Institute)
Federal Bankruptcy Forms (Cornell University Law School Legal Information Institute)
Ask your instructor for assistance, if you have difficulty locating these sites.

Read the letter decision entered by the U.S. Bankruptcy Court for the District of South Dakota in the Stepp v. Fuller Chapter 7 proceeding.
Learning Plan 10

Estate Planning

A. Estate Planning
B. Dying Intestate
C. Last Will and Testament
D. Probate
E. Living Trusts
F. Other Estate Planning Tools
G. Estate & Gift Taxes
H. Living Wills & Health Care Powers of Attorney

A. Estate Planning

Depending upon a person's circumstances, estate planning can be a complicated matter that often involves the services of an attorney, accountant, financial planner, and insurance professional. The purpose of an estate plan is to effectively distribute a person's estate in accordance with the person's wishes, while reducing taxes and expenses. Although information provided on the Internet and through other resources may be helpful, it is advisable to approach such information with caution. Each person should carefully consider his/her own goals when devising a plan to transfer property and provide care for his/her family upon the person's death.

Read the article, Estate Planning, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

B. Dying Intestate

1. Dying Intestate

For various reasons, millions of people die without a making a will. If a person dies without a will, the person is said to have died intestate. In those cases, the statutes of the person's state of residence will determine how the person's estate is distributed. Such distribution may be different than how the person would have wanted his/her assets divided. In some cases, the state may also appoint a guardian of the decedent's children.

If a person dies intestate with more than a small estate, the state will appoint an administrator to distribute the assets. State statutes usually divide a person's estate among the surviving spouse and children, if any. If the decedent was not married and died without children, then state laws will often direct that the decedent's property be distributed to the person's surviving parents and, if no parents are then living, to the decedent's surviving brothers and sisters.

Read the following article presented by FindLaw:

Understanding Intestacy: If You Die Without an Estate Plan

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C. Last Will & Testament

Through a well-written will, often formally called a "Last Will & Testament" a person can direct how he/she wishes to have assets distributed to beneficiaries upon the person's death. The person who makes a will, called the testator, can also name the personal representative (often called the executor) who will distribute the assets. If the testator has minor children, then he/she may also be able to designate a guardian for the children, if the other parent has previously died.

The types of wills and the requirements to create a valid will are prescribed by state statute. The statutes of all states provide the requirements for creating a formal written will, which often requires that the testator sign the will before two or three witnesses, who also sign the will, attesting that the testator signed the will before them. Many states also allow a provision to be added to the will, in which the testator and witnesses sign under oath before a notary public, attesting that the testator freely and voluntarily signed the will in the presence of the witnesses, that the testator was of legal age, of sound mind, and under no constraint or undue influence. Such will is called a self-proving will.

Many states also provide for less formal types of wills, including a holographic will and a nuncupative will. A holographic will is will that is entirely written in the testator's handwriting and signed by the testator without witnesses. Some states also recognize a nuncupative will in very limited situations. A nuncupative will is an oral will that may only be effective to transfer personal property of a limited value and often when the testator is in fear of eminent death. Some states limit nuncupative wills to persons in the military.

In all types of wills the testator must possess testamentary capacity to create a valid will. That is the testator must be of sound mind, of legal age, and under no undue influence. The person must understand the purpose and effect of the will at the time he/she signs the will.

A will becomes effective upon the death of the testator. At any time before the testator dies or loses the required mental capacity, he/she can revoke or amend the will. An amendment is called a codicil. A codicil either modifies or adds a provision to the original will and is signed with the same formalities as a will i.e., witnesses, etc. The testator may also revoke or cancel a will by demonstrating his/her intent to do so by destroying the will, or signing a new will that expressly revokes the previous will.

As previously mentioned, a testator can direct how the testator's estate is to be distributed upon the testator's death. However, it should be recognized that the testator may not be able to devise or bequest certain property in which the testator holds an interest. For example, an interest in property that the testator holds in joint tenancy cannot be distributed by will, because by operation of law the testator's joint interest passes to the surviving joint tenant. (See Learning Plan 7). Other property, such as life insurance and investments with designated beneficiaries will be distributed according to the terms of those instruments.

Read the article Wills presented by FindLaw.

Read through some of the Wills of Famous People provided by TrueTrust.com or Wills of the Rich and Famous provided by the Living Trust Network.
D. Probate

A person who dies with a valid will is said to have died testate. Probate, which means "to prove," is the process by which the personal representative appointed in the will gathers the decedent's assets, pays debts and taxes, and distributes the remaining assets to beneficiaries in accordance with the provisions of the will. Many states provide for different types of probate proceedings in which the court is involved to a greater or lesser degree. In many cases, the assets of a small estate may be distributed without any court proceeding. Several states have adopted the Uniform Probate Code to promote effective probate administration.

At times, certain matters may become disputed in probate proceedings. For example, a person may contest the validity of a will, called a will contest, or dispute how the assets of the estate are distributed. In such cases, the court would be called upon to render a decision to resolve the dispute.

Read the article The Probate Basics presented by FindLaw.

E. Living Trusts

After meeting with their estate planning advisors, some people choose to use a living trust (also called an inter vivos trust) as part of their estate plan. A trust is generally created by the execution of a trust document which creates a separate legal entity, called a trust, that has the legal authority to own property. The person who creates the trust is called the trustor or grantor. Property is then transferred to the trust and administered by trustee, a person or entity, such as the trust department of a bank, designated in the trust document. The trustee administers the trust in accordance with the provisions of the trust document.

Usually, the trustee of a living trust is directed to manage the property in the trust for the benefit of the designated beneficiary during the beneficiary's lifetime. For example, the trustee may invest the property to create income to be distributed to the beneficiary for living expenses. Upon the death of the beneficiary, the trustee is often directed to distribute the trust property outright to other designated beneficiaries, or to continue to hold the property and manage it for the benefit of the surviving beneficiaries.

Read the following articles:

Estates and Trusts, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.

Trusts, presented by FindLaw.

F. Other Estate Planning Tools

A will and/or trust are only parts of an estate plan. Other potential tools to consider when planning the disposition of a person's estate include:

1. Joint checking and savings accounts
2. Real estate owned in joint tenancy (See Learning Plan 7)
3. Life Insurance
4. Gifting prior to death
5. IRA or other retirement plan with a designated beneficiary

Each of the foregoing tools provides advantages, as well as disadvantages, that should be carefully considered after consulting with estate planning professionals, including an attorney, financial planner, and insurance professional.

G. Estate & Gift Taxes
You've heard the old saying, "The only thing certain in life is death and taxes." An effective estate plan should carefully consider the tax consequences associated with the types of distributions, as well as the timing of such distributions.

Read the following articles:

- Estate and Gift Tax, presented by Wex, a collaboratively-edited legal dictionary and encyclopedia sponsored and hosted by the Legal Information Institute at Cornell Law School.
- Estate Tax Issues, presented by FindLaw.
- Explore the website of the Internal Revenue Service to learn about estate and gift taxes.

H. Living Wills & Health Care Powers of Attorney
Although an estate plan focuses on the distribution of a person's estate after his/her death, it is important to provide plans for health care and end of life decisions as part of the plan.

Read the following articles, presented by FindLaw:

- Living Wills
- Health Care Power of Attorney
- Health Care Power of Attorney Form
Gilbertson, Chief Justice

[¶1.] Brenda Chafin challenges the validity of her father’s estate plan. After a formal probate proceeding, the circuit court determined that the estate plan was valid. We affirm.

Facts and Procedural History

[¶2.] Earl Long passed away at the age of 78 on February 26, 2010. He was survived by four daughters: Vicky, Lynda, Diann, and Brenda. Earl’s daughters are the only heirs of the estate.

[¶3.] Prior to his death, Earl and his late wife, Shirley, had operated two seasonal resorts. One of the resorts, Long’s Seasonal Resort, was active at the time of Earl’s death. Although each daughter worked at the Seasonal Resort, Vicky and her husband, Dean, worked there most consistently and for the longest period of time.

[¶4.] Earl began the process of planning his estate in 2005. His first step in the planning process was a meeting with his attorney, Mark Walters. Three of Earl’s daughters also attended the meeting; however, Vicky and Dean did not attend. Among the topics discussed at the meeting were strategies to reduce conflict upon Earl’s death, trust protection for Brenda, gifting of land, and a creation of a limited liability
company (LLC) to hold property separate from Earl’s trust.

[¶5.] On August 30, 2008, Earl properly executed a “pourover” will. The will stated that all property would be distributed to his trust “as amended.” On the same day, Earl executed The Earl W. Long Trust, which was a revocable trust with Earl appointed as trustee.

[¶6.] Following the execution of his will and trust, Earl began gifting some of his assets. On October 3, 2009, Earl executed a memorandum of gifts, which was notarized by Walters and witnessed by Vicky and Dean. Earl executed a second memorandum of gifts on October 5, which was witnessed by Dean and Lynda. The contents of both memorandums were relatively the same. The memorandums documented gifts to Earl’s four daughters of approximately $250,000 each.

[¶7.] In accordance with the memorandums of gifts, Earl acquired land from Vicky so that the land could be given to the other three daughters. In return, Earl deeded Vicky his half interest in the “home place.” Earl intended for the value of the home place to be greater than the value of the land deeded by Vicky so that the difference in value between the two properties was a gift to Vicky. The October 5 memorandum specified that Vicky acquired the home place subject to a life estate, which reserved the income from the Seasonal Resort in favor of Earl.

[¶8.] Earl next gave property to his other daughters. Diann received a gift of land free of encumbrances by warranty deed on October 3. Lynda also received a gift of land free of encumbrances on October 3. In July 2007, Earl had purchased both a piece of property and a mobile home for Brenda, which became her permanent residence. In September 2008, Brenda deeded her half interest as a joint tenant in the property to Earl. In exchange, Earl created a trust for Brenda to provide for her after his passing. Brenda raised no objection to the trust and she continued to live on the property. On October 3, 2009, Earl transferred the property into Brenda’s trust. In addition, Earl gave Brenda $100,000 to fund her trust and $20,000 cash outside the trust.

[¶9.] Later in the fall of 2009, Earl began assessing which property, apart from the property he had already given, would be put into his trust to be distributed upon his death. To carry out his estate plan Earl developed color-coded “maps” that outlined how the remaining land would be divided. Land allocated to Brenda’s trust was colored pink. Land allocated to Diann was green. Lynda’s land was blue; and Vicky’s land was yellow. Land in trust, to be distributed at death to the LLC, was orange. Lastly, “striped” land represented the land that had previously been given to the daughters through the memorandum of gifts. Earl ultimately selected a map, which was dated December 12, 2009, and initialed “EWL.”

[¶10.] On January 23, 2010, Earl amended Brenda’s trust so that all income from the trust would no longer be distributed to Brenda on a monthly basis. Instead, the income would pay for her basic housing expenses and maintenance of her residence. Brenda’s amended trust gave discretion to the trustee to pay health, dental, and car insurance.
Earl also amended his trust on January 23. The amendment added “Section 6.3,” which referenced the map created on December 12, 2009. The amendment also set forth the color-coded property designation. Additionally, the amendment stated that the trustee would create an LLC to hold designated land to be sold. Vicky was selected to manage the LLC “for the four children equally after [Earl was] gone.”

Earl died on February 26, 2010. Following his death, Vicky filed the Articles of Organization for Long Land Company, LLC on April 13, 2010. After Earl’s passing, Brenda executed a document accepting the plan of distribution of the color-coded map. Brenda also executed a document consenting to the use of certain equipment, machinery, and other personal property for maintaining the lots held by the LLC. The four daughters agreed to the sale of two parcels of property by the LLC and each daughter received an equal share of the sale proceeds.

In accordance with Earl’s will, Vicky and Dean were named co-personal representatives for the estate. Prior to the closing of the estate under informal probate, Brenda filed a petition for formal probate of the will. Brenda and Diann had retained counsel to interpret the language of Earl’s trust because they had concerns about the income from the Seasonal Resort and the restrictive language of Brenda’s trust. Brenda also requested that Diann be named as the personal representative of the estate. In hopes of limiting conflict between the sisters, Vicky did not object to Diann serving as personal representative.

The formal probate proceeding was conducted on December 5, 6, and 17, 2012. The circuit court concluded that Earl’s estate plan was valid. The court determined: (1) Earl was competent; (2) neither Vicky nor Dean exercised undue influence over Earl; (3) the trust documents did not call for an equalization of the remaining property; (4) Brenda’s trust was properly amended; and (5) Brenda was not entitled to attorney’s fees.

Brenda appeals the decision of the circuit court. She raises the following issues on appeal:

1. Whether Earl lacked the requisite testamentary capacity to carry out his estate plan.
2. Whether Earl’s estate plan was the result of undue influence.
3. Whether Earl’s Trust required the distributions to be equalized.
4. Whether the doctrine of promissory estoppel barred the modification of Brenda’s trust.
5. Whether Brenda and her attorney are entitled to attorney fees.

Analysis and Decision

1. Whether Earl lacked the requisite testamentary capacity to carry out his estate plan.

Brenda argues that the circuit court erred when it determined that Earl had the
requisite testamentary capacity to carry out the 2009 gifts and the 2010 amendments to his trust.

[¶18.] Whether Earl possessed the requisite testamentary capacity is a mixed question of law and fact, which requires a compound inquiry. Stockwell v. Stockwell, 2010 S.D. 79, ¶ 15, 790 N.W.2d 52, 58. Therefore, we are required to not only review the circuit court’s findings of fact, but also the court’s application of settled law to those facts. Id. For purposes of making a testamentary document, one has a sound mind “if, without prompting, he is able to comprehend the nature and extent of his property, the persons who are the natural objects of his bounty and the disposition that he desires to make of such property.” In re Estate of Dokken, 2000 S.D. 9, ¶ 13, 604 N.W.2d 487, 491 (quoting In re Estate of Long, 1998 S.D. 15, ¶ 21, 575 N.W.2d 254, 257).

Additionally, “[t]estamentary capacity is not determined by any single moment in time, but must be considered as to the condition of the testator’s mind a reasonable length of time before and after the [testamentary document] is executed.” Stockwell, 2010 S.D. 79, ¶ 27, 790 N.W.2d at 62 (citation omitted). Because the 2009 gifts and the 2010 amendments to Earl’s trust were executed with a mind toward disposition of the property after death, we treat them as testamentary in nature. See In re Estate of Pringle, 2008 S.D. 38, ¶ 24, 751 N.W.2d 277, 285.

[¶19.] To illustrate that Earl lacked testamentary capacity, Brenda relies on Dr. Heather Cwach’s medical evaluation. Dr. Cwach examined Earl on October 6, 2009, the day after Earl completed a memorandum of gifts. Dr. Cwach administered a series of tests, including a mini mental-state exam, and found that “[Earl] was alert.” She also observed that Earl’s exam score was “common,” but showed that he was “mildly impaired.” Dr. Cwach did acknowledge, however, that educational background could play a role in the score and that Earl had a 9th grade education. Although Dr. Cwach noted “Dementia, probably Alzheimer’s disease” in her assessment, she testified that this was not an official diagnosis.

[¶20.] Beyond Dr. Cwach’s evaluation, however, Brenda’s evidence reveals little about Earl’s capacity. In fact, but for that brief moment in time, the evidence proved that Earl had the requisite capacity to execute his estate plan. After his visit with Dr. Cwach, Earl was seen by Dr. John Knecht and was admitted to the Fall River Hospital Swing Bed unit for physical therapy, occupational therapy, and respiratory therapy. No mention was made of dementia or Alzheimer’s as a chief complaint. Following his urological surgery, Earl was monitored by Dr. Knecht. Again, there was no mention in Dr. Knecht’s notes that Earl suffered from confusion, dementia, or Alzheimer’s. Dr. Knecht saw Earl on a number of other occasions after Earl was discharged from the hospital. Notably, Dr. Knecht conducted a mental health examination of Earl, which was recommended by Walters. After examining Earl on February 9, 2010, Dr. Knecht concluded that Earl had performed so well that it was unnecessary to conduct additional testing. He also noted that Earl was “absolutely normal as far as his mental health status exam today.” Dr. Knecht testified that he never observed any indications that Earl suffered from an inability to make decisions for himself.

[¶21.] The circuit court also heard testimony from a number of other individuals who
recalled interacting with Earl, both personally and professionally, during the relevant times in question. None of these individuals believed that Earl lacked the mental capacity to make decisions. Some even described him as “sharp as a tack.” By contrast, in addition to the testimony of Dr. Cwach, Brenda only offered testimony from one of her coworkers who did not know Earl personally. The circuit court ultimately determined that the evidence overwhelmingly supported that Earl was competent to execute his estate plan. In determining testamentary capacity we have stressed the importance of giving “due regard to the trial court’s opportunity to observe the witnesses and the evidence.” Dokken, 2000 S.D. 9, ¶ 10, 604 N.W.2d at 491 (quoting In re Estate of Unke, 1998 S.D. 94, ¶ 11, 583 N.W.2d 145, 148). In light of the evidence presented, the circuit court did not err in determining that Earl had the requisite capacity to carry out his estate plan.

[¶22.] 2. Whether Earl’s estate plan was the result of undue influence.

[¶23.] Brenda next argues that the 2009 gifts and the 2010 amendments to Earl’s trust were the result of undue influence. Like testamentary capacity, undue influence is a mixed question of fact and law. Stockwell, 2010 S.D. 79, ¶ 15, 790 N.W.2d at 58.

[¶24.] The circuit court concluded that because of Vicky’s confidential relationship with Earl, a presumption of undue influence arose. “A presumption of undue influence arises when there is a confidential relationship between the testator and a beneficiary who actively participates in preparation and execution of the will and unduly profits therefrom.” Id. ¶ 31 (quoting Pringle, 2008 S.D. 38, ¶ 39, 751 N.W.2d at 289). “A confidential relationship exists whenever a decedent has placed trust and confidence in the integrity and fidelity of another.” Id. (quoting In re Estate of Duebendorfer, 2006 S.D. 79, ¶ 27, 721 N.W.2d 438, 445). In the instant case, the presumption arose in part because Vicky assisted Earl with writing checks in his later years, helped with the color-coded maps, and offered advice at several meetings.

[¶25.] Once a presumption of undue influence arises, “the burden of going forward with the evidence shifts to the beneficiary to show he took no unfair advantage of the decedent.” Unke, 1998 S.D. 94, ¶ 13, 583 N.W.2d at 148 (citation omitted). However, “[t]he ultimate burden remains on the person contesting the will to prove the elements of undue influence by a preponderance of the evidence.” Id. (citation omitted).

[¶26.] To show the existence of undue influence, the following elements must be established: “(1) [the] decedent’s susceptibility to undue influence; (2) [the] opportunity to exert such influence and effect the wrongful purpose; (3) a disposition to do so for an improper purpose; and, (4) a result clearly showing the effects of undue influence.” Stockwell, 2010 S.D. 79, ¶ 35, 790 N.W.2d at 64 (citation omitted). “For influence to be undue it must be of such a character as to destroy the free agency of the testator and substitute the will of another for that of the testator.” Id. (quoting Pringle, 2008 S.D. 38, ¶ 44, 751 N.W.2d at 291).

[¶27.] Brenda argues that the value of the “home place” property Vicky received
demonstrates the effects of undue influence. Brenda alleges that the home place produces an income of approximately $50,000 a year. Furthermore, Brenda contends that Vicky received a property distribution that was valued at $700,550 more than Brenda’s property distribution. The circuit court determined that Brenda failed to establish both Earl’s susceptibility to undue influence and a result showing the effects of undue influence.

[¶28.] Brenda’s evidence did not establish that Vicky exercised undue influence because Brenda did not prove that Earl was susceptible to undue influence. The circuit court highlighted that Earl was an independent person, a rancher, and a businessman. Earl also had the testamentary capacity to carry out his estate plan. Brenda offered little evidence to dispute these facts. Therefore, because Earl was not susceptible to undue influence, the circuit court was correct in determining that the 2009 gifts and the 2010 amendments to the trust were not the product of undue influence.

[¶29.] Additionally, Brenda did not prove a result clearly showing the effects of undue influence. Brenda fails to account for whether Earl, in choosing how to divide his assets, may have considered the role each daughter played in the acquisition and maintenance of his land and seasonal resorts. The circuit court noted that Vicky worked with Earl more often than the other sisters. She and her husband assisted Earl with the Seasonal Resort and with ranching responsibilities. While a presumption of undue influence did arise, Vicky has rebutted that presumption. The ultimate burden remains with Brenda, who has failed to establish by a preponderance of the evidence that Vicky exercised undue influence.

[¶30.] 3. Whether Earl’s trust required the distributions to be equalized.

[¶31.] Brenda next argues that the circuit court erred by not requiring the trustee to equalize all the remaining property under a review of Earl’s entire estate plan. “Trust interpretation is a question of law reviewed de novo.” In re Sunray Holdings Trust, 2013 S.D. 89, ¶ 11, 841 N.W.2d 271, 274 (citation omitted). When interpreting a trust instrument, we must “ensure that the intentions and wishes of the [settlor] are honored.” Id. ¶ 14 (quoting In re Florence Y. Wallbaum Revocable Living Trust, 2012 S.D. 18, ¶ 20, 813 N.W.2d 111, 117). To carry out the settlor’s intentions, “we first ‘look to the language of the trust instrument.’” Id. (quoting In re Schwan 1992 Great, Great Grandchildren’s Trust, 2006 S.D. 9, ¶ 12, 709 N.W.2d 849, 852). “If the language of the trust instrument makes the intention of the [settlor] clear, it is our duty to declare and enforce it.” Id. (quoting In re Florence Y. Wallbaum Revocable Living Trust, 2012 S.D. 18, ¶ 20, 813 N.W.2d at 117).

[¶32.] Brenda claims that the circuit court erred by concluding that Earl did not intend for Section 7.3.1 to be active at his death.3 She alleges that Earl’s trust required all four daughters to receive equal shares of Earl’s estate plan; however, Vicky received property that was more valuable than the property the other three daughters received. Therefore, Brenda requests that the remaining assets in Earl’s estate be distributed in
a matter that accounts for the property that Vicky received.

¶33.] The circuit court concluded that a plain reading of Earl’s trust, the 2010 amendments to the trust, and the 2009 memorandums of gifts all illustrated that Earl did not intend for the contingent language of Section 7.3.1 to be active at his death. Additionally, the circuit court noted that Article 7.1 of the trust required that “any property remaining in the Trust (Trust Residue) shall be divided into four shares, one for each of the Grantor’s children.” But the court observed that the trust did not contain language suggesting that these shares must be divided equally or redistributed to account for the value of the land Vicky received.

¶34.] A plain reading of Earl’s trust supports the circuit court’s conclusion. Attorney Walters testified that Section 7.3.1 was intended to be a “catch all” or contingency provision.

Section 7.3.1 of Earl’s trust provided in part: The trustee is hereby directed to make a summary of all distributions of the Grantor’s property . . . . The trustee shall determine each beneficiary’s total share of the estate and shall make adjustments to each beneficiary’s trust distribution, if necessary, to achieve the percentage of total distribution to each beneficiary as provided for in Article Seven (7) of this trust agreement.

However, it was unnecessary for this contingency language to be active at Earl’s death because Earl had already disposed of his property during his life through the memorandum of gifts and subsequent amendment to his trust, which divided his property into four shares.

¶35.] Brenda maintains, however, that Section 7.3.1 should be used to distribute the estate’s remaining property, such as Earl’s life insurance plan, to account for the fact that Vicky received more valuable land than the other sisters. But contrary to Brenda’s position, Article 7 does not contain any percentages of total distribution for the four daughters. It is true that Section 7.3.2 requires that any distribution “calculation include the value of any property passing as a specific bequest as stated in Section 6.2.” And Section 6.2 references any gifts made, specifically stating that any gifts to be contemplated are set forth in “Schedule B.” But there is no Schedule B. Additionally, none of the memorandums of gifts reference a Schedule B. Therefore, it would be inappropriate for this Court to give meaning to a nonexistent provision.

¶36.] It would also be inconsistent with a plain reading of the trust instrument to assume that Earl intended to equalize land he had already distributed. This is especially true when Article 7.1 of the trust instrument does not require an equalization process to account for the value of the land Vicky received. Furthermore, prior to Earl’s death, four shares of property were divided among the four daughters referenced in the land map. The remaining property was placed in the LLC and held for the four daughters “equally,” as provided in the trust instrument. Had Earl
intended the result Brenda now requests for the remaining property, he would have used language requesting that result. But no such language exists. Therefore, a plain reading of the trust instrument supports the circuit court's conclusion. We affirm the circuit court's decision.

[¶37.] KONENKAMP, ZINTER, SEVERSON, and WILBUR, Justices, concur.

PERSCHE v. JONES and TRI-STATE NATIONAL BANK
387 N.W.2d 32 (S.D. 1986)

HENDERSON, J.

ACTION/PARTIES

This is an appeal from a Judgment entered on a jury verdict awarding plaintiffs-appellees $125,000 damages resulting from defendants-appellants' unauthorized practice of law. We affirm.

Ernest Persche (Ernie) was a Butte County rancher who died October 15, 1981. Matthew Persche (Matt) and Erna Persche (Erna) are Ernie's children and plaintiffs-appellees herein. Defendants-appellants are Arthur W. Jones (Jones) and the Tri-State National Bank (Bank). The Bank is located in Belle Fourche and Jones was its president and loan officer. Jones was also Ernie's long-time friend and financial advisor. Betty Craft Persche (Betty) was Ernie's friend, live-in housekeeper, and purported wife.

FACTS

In October 1978, Betty began working as Ernie's live-in housekeeper and this arrangement continued until the Fall of 1980 when Betty moved to Montana. Thereafter, Ernie fell ill and on November 19, 1980, Ernie executed a will drawn by Attorney Ken Graves. This will appointed Matt and Attorney Graves co-executors and gave the bulk of Ernie's estate to Matt and Erna. No provision for Betty was contained in this will.

In December 1980, Ernie visited Jones at the Bank. Ernie was upset about his will and he insisted that Jones help him revise it -- help him change it, so that the will was the way he wanted it. Ernie told Jones the changes he wanted to make and Jones had a Bank secretary type a new will. This second will was signed by Ernie on December 16, 1980, in the Bank, and witnessed by two Bank secretaries. This second will made changes in specific bequests and appointed Jones as executor of Ernie's estate. The propriety of the second will's attestation, however, is highly suspect for it is uncertain whether all parties signed in the presence of each other.

On February 16, 1981, Ernie was again at the Bank requesting changes in this second will. It appears Ernie wanted to add another specific bequest. Jones then had a Bank secretary type this
bequest onto the will, cross out the December 1980 date, and type in February 1981. Ernie, Jones, and the two secretary-witnesses then initialed these changes.

In March 1981, Betty returned as Ernie's live-in housekeeper. On April 28, 1981, Ernie had Attorney Leroy Hill draw a codicil to the second will. This codicil gave Betty a life estate in Ernie's ranch house and provided her a specific bequest of $10,000. This codicil was duly executed in Attorney Hill's office. At this time, Ernie told Attorney Hill that Jones had drawn the will to which the codicil pertained and Attorney Hill explained why it was wrong to have a banker draw a will.

On June 1, 1981, Ernie and Betty were purportedly married. Prior to this marriage, however, Ernie and Betty executed an antenuptial agreement which limited Betty's rights to $2,500 from Ernie's estate. This marriage, however, was void because Betty, although previously married four times, had never obtained a formal divorce from her first husband. Thus, under SDCL 25-1-8, the marriage of Ernie and Betty was void. Betty's first marriage was formally dissolved some two or three years after Ernie's death.

In August 1981, Ernie left a copy of his second will with Jones at the Bank. On this copy Ernie had made several handwritten changes. On August 31, 1981, Ernie was in a Belle Fourche hospital. On this date, Ernie contacted Attorney Hill and requested him to come to the hospital so as to construct a new testamentary instrument. Attorney Hill went to the hospital but after seeing Ernie's condition, Attorney Hill determined that Ernie was unable to attend to the requested business. On this same date, and apparently after Attorney Hill's visit, Ernie called Jones at the Bank and requested that a will incorporating his changes be typed up. Jones told Ernie that this had to stop, but Jones had a Bank secretary type a third will. This third will eliminated Betty's life estate, reduced the $10,000 bequest to Betty to $5,000, and divided the bulk of the estate between Matt and Erna. On the same date, August 31, 1981, Jones took this third will to the hospital. While Jones was out of the room, Ernie signed it. Jones then took the third will back to the Bank and asked the two previous secretary-witnesses if they recognized Ernie's signature and would witness his signature. Both secretaries recognized Ernie's signature and both signed the third will, at the Bank, as witnesses, but outside the presence of each other and outside the presence of Ernie who was still at the hospital. On October 15, 1981, Ernie died at his ranch near Belle Fourche.

Jones offered the third will of August 31, 1981, for probate but Betty objected to its admission. The circuit court determined that the third will was not properly executed. Probate was refused. Matt thereafter offered the first will of November 19, 1980, for probate. Betty objected to probate of this first will. She filed a Petition for Elective Share of Surviving Spouse and a Petition to Set Apart Exempt Personal Property and for Family Allowances.

On January 6, 1983, Matt and Betty executed a Stipulation for Settlement wherein Betty agreed not to contest probate and to release Ernie's estate from all claims and demands. In return, Betty was to receive $50,000 from Ernie's estate; the first $50,000 recovered from a suit against Jones and the Bank to be brought by Ernie's estate; the payment of some $13,000 in debts; and all furniture, appliances, and household goods located in Ernie's ranch residence.

Suit was thereafter brought against Jones and the Bank by the Estate seeking to recover
damages allegedly resulting from their negligence and unauthorized practice of law. After a jury trial on the merits, a verdict was returned awarding Matt and Erna $125,000. Thereupon, the trial court entered judgment.

From the whole of this Judgment, Jones and the Bank now appeal asserting some nine issues and subissues for our determination. We group these issues into three categories and address their merits seriatim.

**LIABILITY**

Jones and the Bank make various assertions relating to nonliability. The first such contention is that this action is not maintainable because a duty was not owed to the beneficiaries of Ernie's third will as no privity existed between the beneficiaries with Jones and the Bank. Numerous courts, however, under third party and/or tort theories, have upheld beneficiary actions against the attorney responsible for drafting or supervising the execution of a defective testamentary instrument, see *Lucas v. Hamm*, 56 Cal.2d 583, 364 P.2d 685, 15 Cal.Rptr. 821 (1961), *cert. denied*, 368 U.S. 987, 82 S. Ct. 603, 7 L. Ed. 2d 525 (1962); *Licata v. Spector*, 26 Conn.Supp. 378, 225 A.2d 28 (1966); *Needham v. Hamilton*, 459 A.2d 1060 (D.C.App. 1983); *Lorraine v. Grover, Ciment, Weinstein & Stauber, P.A.*, 467 So.2d 315 (Fla.App. 1985); *Ogle v. Fuiten*, 102 Ill.2d 356, 80 Ill.Dec. 772, 466 N.E.2d 224 (1984); *Woodfork v. Sanders*, 248 So.2d 419 (La.App. 1971), *writ denied*, 259 La. 759, 252 So. 2d 455 (1971); *Guy v. Liederbach*, 501 Pa. 47, 459 A.2d 744 (1983); *Auric v. Continental Cas. Co.*, 111 Wis.2d 507, 331 N.W.2d 325 (1983); and in *Biankanja v. Irving*, 49 Cal.2d 647, 320 P.2d 16, 65 A.L.R.2d 1358 (1958), a duty was found to exist and a beneficiary action was upheld when a layman negligently failed to have a will properly attested. The reasoning of *Biankanja* for upholding the beneficiary's action despite an absence of privity is persuasive. Based thereon, and under the facts and circumstances of this case, we determine that Jones and the Bank owed a duty to Matt and Erna. Therefore, Matt and Erna can properly maintain this action. One who negligently fails to direct proper attestation of a will becomes liable in tort to an intended beneficiary who suffered damage because of the invalidity of the testamentary instrument. *Biankanja; Heyer v. Flaig*, 70 Cal.2d 223, 449 P.2d 161, 163, 74 Cal.Rptr. 225, 227 (1969).

Jones and the Bank next contend the evidence fails to reveal that they supervised the signing and witnessing of Ernie's third will; moreover, that mere supervision of a will's execution does not constitute the unauthorized practice of law. After examining the record and pertinent law, however, we are unable to concur in these contentions.

"Supervise" is defined in *Black's Law Dictionary* 1290 (5th ed. 1979), as: "To have general oversight over, to superintend or to inspect." In the present case, the record reveals that Ernie went to Jones at the Bank on three separate occasions to have his will changed, that Jones directed a Bank secretary to type the changes and two Bank secretaries were directed to sign the wills as witnesses. The record further reveals that on August 31, 1981, Ernie requested changes in his will, that Jones had a Bank secretary type a new will, that Jones delivered this
third will to Ernie at the hospital for his signature, and that Jones thereafter directed two
Bank secretaries to sign as witnesses. The trial court instructed the jury that Jones supervised
the signing and witnessing of Ernie's August 1981 will. Based on the record, we find no
error with such an instruction. Not only did Jones violate this licensure statute, he failed to
exercise a degree of care in the will's execution. SDCL 16-18-1 provides that no person shall
engage in the practice of law unless duly licensed as an attorney at law and an active
member of the state bar. The evidence clearly shows that Jones had general oversight and
direction over the signing and witnessing of Ernie's third will.

As for the contention that a mere supervision of the execution of a will does not constitute an
unauthorized practice of law, we also disagree. Practicing law "is not limited to conducting
litigation, but includes giving legal advice and counsel, and rendering services that require the
use of legal knowledge or skill and the preparing of instruments and contracts by which legal
rights are secured, whether or not the matter is pending in a court." Annot., 22 A.L.R.3d 1112,
§ 2, at 1114 (1968). Thus, "drafting and supervising the execution of wills for others is clearly
practicing law. . . ." 7 Am.Jur.2d Attorneys at Law § 104, at 176 (1980). It was determined in
Matter of Flynn's Estate, 142 Misc. 7, 253 N.Y.S. 638 (1931), that a bank employee's
supervision of a will's execution was an invasion of the legal profession and we determine that
the activities complained of in this case constitute the unauthorized practice of law. The
execution of a will requires the use of legal knowledge and skill and the implementation of
statutes so as to assure proper execution and attestation. Law books are replete with cases
where maturely considered plans for the disposition of estates, whose creation were the fruit of
lives of industry and self-denial, were destroyed because of technical errors during execution
and attestation. Flynn, 253 N.Y.S. at 639. Here, action was taken on Ernie's behalf which was
totally unrelated to banking business. Holding that there was no error with the instruction
concerning Jones' unauthorized practice of law, Jones is thus liable for damages proximately
causely thereby. Proximate cause is a requisite to establishing damage by the plaintiff. There
were sufficient facts to create an issue of proximate cause and the jury determined this
favorably for Matt and Erna. Jury Instruction No. 16 explicitly set forth the manner in which
the jury should determine what constituted proximate cause.

Appellants thirdly contend the trial court improperly denied testimony concerning Betty's
homestead rights, elective share rights, a "contract to make a will" claim, and the valuation
thereof if valid. On appeal, Jones and the Bank contend this testimony was improperly
excluded as it pertained to proximate cause and damages. Betty's marriage to Ernie, however,
was void, as her marriage to her first husband was never dissolved. SDCL 25-1-8. Thus, the
trial court did not abuse its discretion on an evidentiary ruling via the exclusion of such
testimony. Furthermore, it would create tangential spinouts triggering confusion for the jury.
As for testimony regarding a "contract to make a will" claim, the record reveals that no such
claim was ever asserted by Betty and we conclude its denial was not erroneous.

A final advocacy for nonliability centers around Ernie being admonished that a lawyer should
attend to changes in his will, and that Ernie, despite these admonishments, continued to seek
Jones' assistance when making will changes. Based on these facts, Jones and the Bank contend
the jury should have been instructed on contributory negligence and assumption of risk. We
disagree for two reasons.
First, Ernie's behavior, as revealed by the facts, did not constitute the breach of a duty to protect his own safety nor the voluntary assumption of a known or apparent danger. *Starnes v. Stofferahn*, 83 S.D. 424, 160 N.W.2d 421 (1968); *Underberg v. Cain*, 348 N.W.2d 145 (S.D. 1984). Thus, Ernie was not contributorily negligent and he did not assume a risk. Second, the duty owed to Matt and Erna, his children, was separate and distinct from the duty owed to Ernie. *Heyer*, 70 Cal. 2d 223, 449 P.2d 161, 74 Cal. Rptr. 225. Ernie's contributory negligence or assumption of risk cannot be imputed to Matt or Erna to thereby abrogate the violation of the duty owed to them.

**PROCEDURAL ERRORS**

Jones and the Bank raise two issues we categorize as alleged procedural errors. The first claimed error pertains to the absence of Betty as a party plaintiff. Under the terms of the Stipulation for Settlement, Betty would receive the first $50,000 recovered in a suit against Jones and the Bank. Based on this fact, Jones and the Bank filed a motion to dismiss for failure to name Betty as a party plaintiff. This motion was denied. The trial court's denial is claimed to be error, but we disagree.

SDCL 15-6-17 (a) states in part: "Every action shall be prosecuted in the name of the real party in interest." In interpreting the mandate of this statute, this Court has stated that the statutory "requirement is met if the one who brings the suit has a real, actual, material, or substantial interest in the subject matter of the action." *Vander Vorste v. Northwestern Nat'l Bank*, 81 S.D. 566, 572, 138 N.W.2d 411, 414, 20 A.L.R.3d 960, 965 (1965).

Here, the parties bringing the suit are the executor and children of Ernie Persche, to wit, Matt and Erna Persche, the intended beneficiaries of Ernie's defectively executed third will. Without question, they have a definite and substantial interest in the subject matter of this action and it is the violation of the duty owed directly to them which permits their bringing of this suit. Indeed, it is the intended beneficiaries of the defective testamentary instrument that must bring the suit, for it is their interests that were defeated. *Heyer*. We therefore hold the statutory requirement of SDCL 15-6-17(a) is met. Betty was not an indispensable nor a proper party to this action. The motion to dismiss was properly denied.

A second alleged procedural error advanced is the addition of Matt and Erna as individual party plaintiffs. This suit was originally brought in the name of Matt as executor of Ernie's estate. A motion was then filed to amend the complaint for the express purpose of including a claim for punitive damages. This amended complaint, however, also added Matt and Erna as individual plaintiffs, but a motion to add party plaintiffs was never filed. Jones and the Bank moved to strike Matt and Erna as individual plaintiffs, but the trial court denied the motion. Although we do not condone the civil procedure by which Matt and Erna were originally added as individual plaintiffs, we cannot substantively conclude that the trial court erred in denying the motion to strike. Matt and Erna are the only correct plaintiffs to bring this action. They are the real parties in interest, it was their interests which were defeated by the defective third will, and it is they, as beneficiaries of the defective instrument, who must bring this action, for the executor cannot normally bring an action such as this. *Heyer; Guy*, 501 Pa. 47, 459 A.2d 744. Thus, Matt and Erna were necessary and indispensable parties and the only persons with standing to prosecute this case. Additionally, the record reveals no prejudice to Jones and the Bank. The trial court did rule on their motion to strike. Appellants did have a meaningful opportunity to be heard and
fully argued this aspect of the case. Thus, appellants were not taken advantage of by initial faulty civil procedure and their substantive advocacy was ruled upon. We affirm the trial court's denial of the motion to strike.

DAMAGES

Jones and the Bank contend the $125,000 verdict awarded by the jury to Matt and Erna is clearly excessive and either contrary to the evidence or the result of passion and prejudice. We disagree.

The measure of damages cannot be left to the mere speculation of the jury, for the evidence must show facts which afford a basis for measuring the loss with reasonable certainty. Drier v. Perfection, Inc., 259 N.W.2d 496, 506 (S.D. 1977). In the case at bar, the evidence reveals that if Ernie's third will was valid, Betty would have received a bequest of $5,000. Instead, because of the third will's invalidity, Ernie's second will and the codicil thereto were valid and Betty received a life estate in Ernie's ranch house and a $10,000 bequest. This life estate, however, was relinquished when Betty and Matt entered the Stipulation for Settlement. At trial, Matt, as then owner of the ranch property, valued Betty's life estate at $100,000. The owner of property is qualified to express his or her opinion as to its value, and the weight to be accorded such testimony is for the trier of fact. See Gross v. Connecticut Mut. Life Ins. Co., 361 N.W.2d 259, 271 (S.D. 1985); Fredrick v. Dreyer, 257 N.W.2d 835, 840 (S.D. 1977); and Hannahs v. Noah, 83 S.D. 296, 301-02, 158 N.W.2d 678, 681 (1968). Under the settlement, Betty received $50,000 and would receive the first $50,000 recovered in this suit. Additionally, some $13,000 in debts were paid; Betty received all furniture, appliances, and household goods located at the ranch house; and some $10,000 plus in legal fees were incurred in getting Betty to relinquish or settle her interests. This evidence afforded a basis for measuring Matt and Erna's loss with reasonable certainty. The amount awarded was within the realm of the evidence and not manifestly actuated by passion or prejudice. Weidner v. Lineback, 82 S.D. 8, 20, 140 N.W.2d 597, 603 (1966). The award is not excessive, contrary to the evidence, or the result of passion or prejudice.

The Judgment appealed from is accordingly affirmed.

FOSHEIM, Chief Justice, MORGAN and WUEST, Justices, and HERTZ, Circuit Judge, Acting as Supreme Court Justice, concur.

SABERS, Justice, not having been a member of the Court at the time this action was submitted to the Court, did not participate.
Article XXX, Part the First, Constitution of the Commonwealth of Massachusetts


Constitution of the United States


Figure 2: U.S. map image, NOAA-Cires, Climate Diagnostic Center, http://www.cdc.noaa.gov/USclimate/states.fast.html (public domain)

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National Conference of Commissioners on Uniform State Laws (http://www.nccusl.org/Update/)

Uniform Partnership Act

Please note: This unit discusses businesses corporations and does not address nonprofit corporations, such as nonprofit hospitals, etc. Please also note that a relatively small number of corporations are incorporated under Federal statutes, such as Farm Credit Services and the Tennessee Valley Authority.

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