

Chapter 10

Agency, Business Organizations, and Employment

Chapter Outline

1. Introduction
2. Agency Law
3. Forms of Business Organization
4. Employment Law

Chapter Objectives

After completing this chapter, you will know:

- What agency relationships are and why they are established.
- The significance of agency law for business relationships.
- The most common forms of business organizations and how each type of business organizational form is created and operated.
- How profits, losses, risks, and liabilities are distributed in each business organizational form.
- How the government regulates employer-employee relationships.

Chapter 10 Agency, Business Organizations, and Employment

Chapter Outline

- I. INTRODUCTION
 - A. Legal concepts overlap considerably.
 - B. Tort law and contract law both overlap with the law of agency.
 - C. Agency relationships provide an excellent background for an examination of business organizations and employment law.

- II. AGENCY LAW
 - A. In an *agency* relationship, the *agent* agrees to represent or act for the *principal*.
 - B. Employees and Independent Contractors
 - i. Normally, all employees who deal with third parties are deemed to be agents of their employers.
 - ii. An *independent contractor* is a person who is hired to perform a specific undertaking but who is free to choose how and when to perform the work.
 - C. Agency Formation
 - i. An agency agreement can be formed by:
 - 1. Express written contract
 - 2. Oral agreement
 - 3. Implied by conduct.
 - D. Fiduciary Duties
 - i. An agency relationship is a *fiduciary relationship*.
 - ii. A fiduciary relationship is one that involves a high degree of trust and confidence and gives rise to certain legal duties.
 - E. Agency Relationships and Third Parties
 - i. The principal is bound by an agent's authorized actions and contacts with third parties.
 - ii. However, the principal is only liable for the authorized actions of his agent.
 - iii. Contract Liability
 - 1. If an agent is not authorized to enter into a contract on behalf of the principal, then normally the principal will not be bound by the contract.
 - 2. The agent's authority may be *implied by custom*, that is, an agent normally has the authority to do whatever is customary or necessary to fulfill the purpose of the agency.
 - iv. Tort Liability
 - 1. The principal may be liable, under the doctrine of *respondeat superior*, for the agent's torts committed within the scope of the agency.

2. The doctrine imposes *vicarious liability* on the employer, that is, liability without regard to the personal fault of the employer for the torts committed by the employee in the course or scope of the employment.
 - v. Liability for Independent Contractor's Torts
 1. Generally, the principal is not liable for physical harm caused to a third person by the negligent act of an independent contractor in the performance of the contract.
- F. Agency Law and the Paralegal
- i. Knowledge of agency law is important for the paralegal because they will be directly involved in an agency relationship with their attorney.
 - ii. Further, paralegals also deal with agents in their work.

Exciting Entities

There are several different business entities. You read about these in Chapter 4, as they pertain to different types of law offices. Now you know the advantages and disadvantages of these entities. There is a lot of paperwork and a need for attention to detail when working in this practice area. Good thing you are organized.

III. FORMS OF BUSINESS ORGANIZATIONS

A. Sole Proprietorships

- i. This is the simplest form of business
- ii. Anyone who does business without creating an organization is a sole proprietor.
- iii. Formation of a Sole Proprietorship
 1. No papers need to be filed with the state.
 2. At most, there is only minor paperwork involved, depending on the law of the city in which the business is located.
- iv. Advantages of a Sole Proprietorship
 1. A major advantage is that the sole proprietorship is entitled to all of the profits made by the firm.
 2. The sole proprietor is also free to make any decision he or she wishes concerning the business.
 3. The sole proprietor is allowed to establish tax-exempt retirement accounts, such as Keogh plans.
- v. Disadvantages of a Sole Proprietorship
 1. A major disadvantage is that the proprietor alone is personally liable for any losses, debts, and obligations incurred in the business.

2. If the owner wishes to expand the business, it is difficult to obtain capital.
- vi. Taxation and Sole Proprietorships
 1. A sole proprietor must pay income taxes on business profits.
 2. The sole proprietor does not have to file a separate tax return for the business; profits are reported on the owner's personal tax return.
- vii. Termination of the Sole Proprietorship
 1. When the owner dies, the business is automatically dissolved.
 2. If the business is transferred or sold, the new owner creates a new business organization.

B. Partnerships

- i. A *partnership* arises when two or more individuals undertake to do business together as *partners*.
- ii. Each partner owns a portion of the business and shares jointly in the firm's profits or losses.
- iii. Partners are personally liable for the debts and obligations of the business if the business fails.
- iv. Partnership Formation
 1. Under the Uniform Partnership Act (UPA), to create a partnership, two or more persons simply agree to establish a profit-making business as partners.
 2. The partnership agreement can be expressed orally or in writing, or it can be implied by conduct.
- v. Rights and Duties of Partners
 1. Partners have a special relationship with one another.
 2. Each partner is the agent of the other partner(s) and the partnership.
 3. Rights of partners are often written into a partnership agreement.
- vi. Liability of Partners
 1. Partners have *joint liability* or shared liability. They may be held personally liable for their own actions, those of the partnership, and those of the other partner(s).
 2. Partners may also be subject to *joint and several (individual) liability*. This allows a plaintiff to sue and seek judgment against any one, or all, of the jointly liable defendant(s)/partner(s).
 3. Fault is not an issue. Even a partner who had no knowledge of circumstances giving rise to the action can be sued.
- vii. Taxation of Partnership
 1. The partnership does not pay federal income taxes.

2. The partnership files an information return with the IRS, but the partners declare their shares of partnership profits on their personal income tax returns and pay accordingly.
- viii. Limited Partnerships
1. Ordinary partnerships are referred to as *general partnerships*.
 2. The *limited partnership* is a special form of partnership involving two different types of partners:
 - a. *General partners* manage the business and have the rights and liabilities of partners in a general partnership.
 - b. The *limited partners* are simply investors in the business.
 - 1) They do not participate in the management of the partnership.
 - 2) They enjoy limited liability status.
 - 3) They are only liable up to the amount that they have invested.
 - 4) To be considered a limited partner, they must sign and file a *certificate of limited partnership*.

C. Corporations

- i. The owners of the corporation are called *shareholders*.
- ii. Shareholders purchase corporate *shares*, or stock.
- iii. The *directors* are persons elected by the shareholders to direct corporate affairs.
- iv. The *officers* of the corporation are the persons hired by the directors to manage the day-to-day operations.
- v. Corporate Formation
 1. Forming a corporation requires two steps:
 - a. The first step is the organizational and promotional undertakings, particularly raising capital for the future corporation.
 - 1) People investing in the proposed corporation are *subscribers*.
 - 2) *Promoters* (those who take the preliminary steps in organizing the corporation) issue a *prospectus*. A prospectus is a document that describes the corporation and its operation.
 - b. The second step is the process of incorporation.
 - 1) The primary document needed to begin the incorporation is called the *articles of incorporation*.

- 2) After the articles of incorporation is signed and filed, the secretary of state issues a *certificate of incorporation*.

vi. Classifications of Corporations

1. A *private corporation* is a corporation that is privately owned.
2. A *public corporation* is formed by the government for a political or governmental purpose.
3. A *publicly held corporation* is a corporation whose shares are publicly traded in securities markets, such as the New York Stock Exchange.
4. A *close corporation* (or *closely held corporation*) is owned by a small group of shareholders, such as family members.

vii. Directors and Officers

1. Directors

- a. The board of directors is elected by a majority vote of the shareholders.
- b. Each director has one vote, and generally the majority rules.
- c. Director's rights include participating in board meetings and the right to inspect corporate books and records.
- d. The director's responsibilities include declaring and paying *dividends* (payments to shareholders representing their share of corporate profits).
- e. The board of directors appoints the corporate officers.

2. Officers

- a. Officers manage the day-to-day operations of the company.
 - b. The officers are employees of the corporation.
 - c. The officers are also agents of the corporation.
3. Directors and officers have a fiduciary duty to the corporation and its shareholder-owners.

viii. Shareholders

1. The *shareholders* are the owners of the corporation.
2. At shareholder meetings, shareholders elect the directors who control the corporation.
3. Shareholders have the right to one vote per share on decisions affecting the corporation.
4. Shareholders have *limited liability*—a key advantage of the corporate form of business.

ix. Corporate Taxation

1. The corporation as an entity pays income taxes on corporate profits.
 2. The shareholders pay personal income taxes on the income they receive.
 3. This double-taxation feature of the corporate form of business is one of its major disadvantages.
 4. A *Subchapter S* corporation is permitted to avoid the double taxation of corporate profits.
- x. Corporate Merger and Consolidation
1. A *merger* is a process through which one corporation acquires all of the assets and liabilities of another corporation.
 2. A *consolidation* is a similar process. The difference is that both existing corporate entities disappear, and a completely new corporation is formed.
- xi. Corporate Termination
1. The first step in terminating a corporation is *dissolution*, or extinguishing the legal existence of the corporation.
 2. The second step is *liquidation*, which involves the winding up of the corporation's business affairs.
 3. After all creditors are paid, all remaining assets are distributed to the shareholders.

D. Limited Liability Organization

- i. Two relatively new forms of business organizations are:
1. Limited Liability Companies
 - a. The *limited liability company* (LLC) combines the pass-through tax benefits of S corporations and partnerships with the limited liability of limited partners and corporate shareholders.
 - b. To form an LLC, *articles of incorporation* must be filed and the business's name must include the word "Limited Liability Company" or the initials "L.L.C."
 2. Limited Liability Partnerships
 - a. The *limited liability partnership* (LLP) is similar to the LLC. It is designed for professionals such as attorneys.
 - b. To form an LLP, the appropriate form must be filed and the business's name must include either "Limited Liability Partnership" or the initials "L.L.P."
 - c. The major advantage of the LLP is that it allows a partnership to function as a tax pass-through but limits the personal liability of the partners for tort liability.

- E. Business Organizations and the Paralegal
 - i. Paralegals must understand business organizations because they often work on behalf of clients who run their businesses as sole proprietors, partnerships, or corporations.
 - ii. Paralegals may also work for law firms that are one of these business organizations.

Employing Employees

Employment law is another practice area that requires knowledge and awareness of many areas of law. Additionally, employment law is governed by federal and state statutory law as well as case law and administrative law. A paralegal who can keep all the governing acts straight is an exceptional employee.

IV. EMPLOYMENT LAW

A. Employment at Will

- i. Under the common law, employment in the United States has traditionally been *employment at will*.
- ii. Under employment at will doctrines, both the employer and the employee can terminate the employment relationship at any time for any reason.
- iii. Exceptions, such as discrimination, can prevent the doctrine from being applied.
- iv. Wrongful Discharge
 - 1. When an employer discharges an employee in violation of an employment contract or a statute protecting employees, the employee may bring an action for *wrongful discharge*.
- v. Labor Laws
 - 1. State and federal statutes relating to employment now govern employment relationships.
 - 2. *Collective bargaining* is bargaining between union representatives and employers.

B. Family and Medical Leave

- i. The 1993 Family and Medical Leave Act (FMLA) protects employees who need time off work for family or medical reasons.

C. State Workers' Compensation Laws

- i. State *workers' compensation laws* establish an administrative procedure for compensating workers injured on the job.
- ii. Some employers are *self-insured*. This means that employers who show an ability to pay claims do not need to buy workers' compensation insurance.
 - 1. The right to recover benefits is based on whether
 - a. The injury was *accidental*, and

- b. The injury *occurred on the job or in the course of employment*, regardless of fault.

D. Employment Discrimination

i. Title VII of the Civil Rights Act of 1964

1. This act prohibits employment discrimination against job applicants and employees on the basis of:
 - a. Race
 - b. Color
 - c. National Origin
 - d. Gender
 - e. Religion.
2. Sexual Harassment
 - a. The courts have extended Title VII protection to those subject to *sexual harassment* in the workplace.
 - b. Sexual harassment (*quid pro quo*) occurs when a superior doles out awards to a subordinate in exchange for sexual favors.
3. The Equal Employment Opportunity Commission
 - a. The EEOC is a federal agency that administers and enforces Title VII and the laws prohibiting employment discrimination based on disability or age.
4. Employers' Liability Under Title VII
 - a. An employer's liability under Title VII can be extensive.
 - b. The court can order injunctive relief, retroactive promotions, past wages, and damages.
5. Discrimination Based on Age
 - a. The 1967 Age Discrimination in Employment Act (ADEA) prevents employers from discriminating against workers between the ages of forty and seventy based on their age.
6. Discrimination Based on Disability
 - a. The 1990 Americans with Disabilities Act (ADA) requires employers with fifteen or more employees to satisfy its requirements.
 - b. Under the ADA, employers must make *reasonable accommodations* to assist the worker in satisfactorily performing the job.

E. Employment Law and the Paralegal

- i. As an employee, the paralegal is subject to the laws governing employment relationships.
- ii. As a legal professional, the paralegal may be extensively involved in work relating to labor and employment laws.