## ANSWERS TO CHAPTER 35

### True-False Multiple Choice

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### Short Essay

28. A subagent is an agent of an agent, a person appointed by an agent to perform tasks for the agent on behalf of his principal. When an agent appoints a subagent, the agent becomes a principal with respect to the subagent.

29. No sharp line divides the two, but the impost important factor is that a principal has the right to control the physical details of the employee’s work. Independent contractors generally contract to product some result and determine how that result will be accomplished.
30. This liability may result because the former agent may still have apparent authority when dealing with third parties who are unaware of the termination of the agency relationship. Although any form of termination cuts off actual authority, the reasonable appearance of authority may remain. To minimize the danger of being held liable on this basis, the principal should give third parties notice. For third parties who have previously dealt with the agent, a direct actual notification is necessary. For other parties, constructive notification such as a suitable and suitably-placed newspaper ad generally suffices. Of course, apparent authority ends when the agency terminates by the principal’s death or loss of capacity, or by impossibility; and the circumstances of the termination also may negate apparent authority. But why rely on this?

31. Authority is critical to agency’s function of stimulating trade and commerce because it is the concept that enables an agent to legally bind his principal. This, of course, enables principals to greatly increase the number of transactions they can complete.
CHAPTER 36
THIRD-PARTY RELATIONS OF THE PRINCIPAL AND THE AGENT

ANSWERS TO CHAPTER 36

True-False                          Multiple Choice
1. T                                 15. a
2. F                                 16. c
3. T                                 17. d
4. F                                 18. b
5. T                                 19. a
6. T                                 20. a
7. F                                 21. b
8. T                                 22. a
9. T                                 23. c
10. T                                24. c
11. F                                25. d
12. F
13. T
14. T

Short Essay

26. Whether P is liable depends on whether A was an employee or an independent contractor. The facts are such that A would likely be considered an employee because of the considerable control P exercised over the work even though P did not treat A as an employee for tax purposes. This would be especially true if A did no work for anyone else while he worked for P.

27. An example is the above situation. If A is considered an employee, and the tort occurred during the course of the roofing work, P would be liable under this doctrine for the negligence that harmed the third party.
28. Smith is incorrect. She is liable on the contract because Jones had apparent authority to make the contract on her behalf with Fisher. Smith had placed Jones in the position of dealing with third parties on her behalf. Fisher was aware that bookstore managers usually have authority to make purchases for the bookstore. He had no knowledge of any limitation on Jones’s actual authority in that regard. On these facts, apparent authority existed. It should be noted that apparent authority would be the only sort of authority Jones had here. Even if bookstore managers ordinarily have authority to make purchases, Jones had no implied authority to that effect because Smith had expressly forbidden him to take action of that nature. Implied authority cannot conflict with express limitations provided by the principal.

29. Poor Pete is liable on the $3.8 million contract. First, he was contracting on behalf of a partially disclosed principal. Second, he expressly agreed to be bound. But Pete is not liable for contracting in excess of his authority, because he informed Barbara that he might not have authority to go to $3.8 million.

30. Where apparent authority exists, the third party has a reasonable belief that the agent has authority to contract on behalf of some principal. How can this be true where the principal is undisclosed? Here, the third party lacks knowledge or reason to know of both the principal’s existence and the principal’s identity.
CHAPTER 37
INTRODUCTION TO FORMS OF BUSINESS AND FORMATION OF PARTNERSHIPS

ANSWERS TO CHAPTER 37

True-False

1. T
2. T
3. F
4. T
5. T
6. T
7. F
8. F
9. T
10. T

Multiple Choice

11. d
12. a
13. d
14. a
15. a
16. d
17. b
18. a
19. c
20. a

Short Essay

21. A is liable because the individual partners and the partnership are liable for a tort committed by a partner within the scope of the partnership business.

22. George-Boy is liable for the debt because of the operation of the purported partnership doctrine. When Mr. Busch made the partnership representation in the presence of the wholesaler’s representative, George-Boy had the duty to speak up and correct the record if he did not wish to be bound as a partner would be. Having failed to voice his objection at the time, George-Boy must now face the consequences. It makes no difference, with regard to the question of his liability to the wholesaler, that George-Boy later told his father he would not be liable for any of his father’s debts.

23. Monella is incorrect. His business is a sole proprietorship, which is not its own separate legal entity. Monella faces unlimited personal liability for debts connected with his restaurant business.
ANSWERS TO CHAPTER 38

True-False                  Multiple Choice
1. T                        12. d
2. F                        13. c
3. T                        14. d
4. F                        15. b
5. F                        16. d
6. F                        17. d
7. F                        18. a
8. T                        19. c
9. T                        20. b
10. F                       21. c
11. T

Short Essay

22. Partners share profits equally unless otherwise agreed; partners share losses in the same way; a partner’s share of the profits is income to the partner on which taxes must be paid. His share of partnership losses may be deducted in the same manner.

23. Dewey must present the $1,500 to the firm, because he owes his partners the duty to account. Of course, if the other partners agree that Dewey should be allowed to keep the $1,500 for himself, he may do so.

24. Beitz is justified in refusing to pay the debt. Beitz & Barks is a nontrading partnership, so borrowing money would not be in the ordinary course of business. Nothing in the facts leads to a conclusion that Barks would have had express, implied, or apparent authority to bind the partnership (and her partner)
CHAPTER 39
PARTNERS’ DISSOCIATION AND
PARTNERSHIPS’ DISSOLUTION AND WINDING UP

ANSWERS TO CHAPTER 39

True-False

1. T
2. F
3. T
4. F
5. F
6. T
7. F
8. T
9. T
10. F

Multiple Choice

11. c
12. a
13. c
14. b
15. c
16. a
17. c
18. d
19. a
20. d

Short Essay

21. The creditors will be paid first. The remaining $9,000 will go to C to repay the loan. The proceeds of assets are exhausted and C has a claim against the other partners for the unpaid portion of the loan.

22. The decisions and actions of the partners conducting the winding up appear to have been proper. Because the partners handling the winding up are to liquidate partnership assets at their highest value, it may be advantageous for them to decide to complete performance of a contract that was entered into before the partnership dissolution but had not yet been performed as of the time of the dissolution. If it is necessary to enter into new contracts with subcontractors or suppliers in order to facilitate performance of such an existing contract, the partners conducting the winding up would have authority to do so.

23. Among the three partners, Andy’s proper share of the amount still owed to creditors is $14,000. The total partnership loss here is $228,000 ($180,000 in contributed capital plus $48,000 in debt remaining after liquidation of assets). Andy’s share of the loss is $114,000 (50 percent of $228,000), because in the absence of an agreement on loss sharing, losses are shared in the same manner that profits are shared. Because Andy has already lost his $100,000 capital contribution, he must contribute only another $14,000. If creditors compel him to pay more than $14,000, he will have a claim against Barney and Helen for any amounts he pays in excess of $14,000.

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CHAPTER 40
LIMITED LIABILITY COMPANIES, LIMITED PARTNERSHIPS,
AND LIMITED LIABILITY LIMITED PARTNERSHIPS

ANSWERS TO CHAPTER 40

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Short Essay

21. A limited partner is may be expelled by the other partners or by a court. A dissociated limited partner has no rights and is a transferee of the dissociated limited partner’s transferable interest. A general partner’s dissociation are treated the same as the RUPA treats partners’ dissociations. Disassociation ends a general partner’s rights to manage the limited partnership. A dissociated general partner will remain liable on a limited partnership obligation unless the creditors agree to release him. He is not liable for debt incurred after he dissociated if notice has been given.

22. McCartney, Lennon, and Harrison all face the realistic prospect of personal liability on the debt. General partners are jointly liable for contract claims such as that of Starkey. The partnership’s assets are not sufficient to satisfy Starkey’s claim. The general partners therefore are liable to Starkey for the excess, without regard for the amounts of their capital contributions to the partnership. For liability purposes, the designation of “general partner” applies not only to McCartney and Lennon, who clearly were general partners, but also to Harrison, who effectively became one. If Harrison had refrained from becoming involved in the management of the business, she would have remained a limited partner for liability purposes and would have stood to lose only her initial investment of $15,000, without any liability beyond that to Starkey. Instead, Harrison became involved in management and engaged in conduct causing Starkey to have a reasonable belief that she was a general partner. Starkey transacted business with the firm while holding that belief. Therefore, Harrison, despite her original designation as a limited partner, has the liability of a general partner.
23. Under the RULPA rule, profits are distributed on the basis of each partner’s capital contribution, unless there is an agreement to the contrary. This would mean that Tara would be entitled to receive $7000 of the profits (10 percent of $70,000) because her capital contribution of $10,000 was 10 percent of the total capital contributions of $100,000. Kyle and the five limited partners each contributed 15 percent ($15,000) of the firm’s total capital contributions of $100,000. Accordingly, Kyle and each of the limited partners would be entitled to receive 15 percent of the profits. Fifteen percent of the profits would be $10,500—the amount Kyle should receive and each of the five limited partners.
CHAPTER 41
HISTORY AND NATURE OF CORPORATIONS

ANSWERS TO CHAPTER 41

True-False                     Multiple Choice
1. F                           11. a
2. F                           12. d
3. F                           13. d
4. T                           14. b
5. T                           15. a
6. T                           16. c
7. F                           17. d
8. T                           18. b
9. F                           19. c
10. T                          20. a

Short Essay

21. The Supreme Court has held that the state cannot violate the due process rights of the corporation. Subjecting the corporation to the minimum contacts tests means that the exercise of jurisdiction cannot offend “traditional notions of fair play and substantial justice.” There are a number of tests that the courts have devised under this test. Most states have passed long-arm statutes that permit their courts to exercise jurisdiction under these tests.

22. The Idaho court cannot constitutionally assert jurisdiction over Roller World, Inc. Roller World did not conduct any activities in Idaho. It did not have any particular connection with that state. Absent from the facts are the minimum contacts required, under the International Shoe decision’s interpretation of the Due Process Clause, in order for the assertion of jurisdiction to be constitutional. Although isolated incidents may sometimes be enough to create the necessary minimum contacts, the only connection with Idaho mentioned in the facts is that Roller World’s president has occasionally traveled through Idaho on personal matters. That fact is not enough to give the corporation minimum contacts with Idaho. The fact that the plaintiffs are from Idaho does not automatically give an Idaho court the power to render a binding judgment against a foreign corporation. The plaintiff’s suit against Roller World should be filed in an appropriate Missouri state court or, if the plaintiffs so choose, in a federal district court in Missouri (assuming that the amount in controversy in the case is sufficient).
23. On the basis of the facts stated in the problem, the creditor should be entitled to have the corporate veil pierced, so that Oliver and Fawn North-Hall are held personally liable for the debt. The North-Halls operated the corporation as their alter ego and as a mere extension of themselves. They did not properly observe the distinction between their own interests and property and the interests and property of the corporation. Under the circumstances, they dominated the corporation and used that domination for improper personal purposes. Their misuse of the corporate form would justify a court in piercing the corporate veil, so as to eliminate what otherwise would be a fraud on creditors.
ANSWERS TO CHAPTER 42

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Short Essay

24. No. H is only doing interstate business and is not doing business in West Virginia and is not subject to the state’s incorporation laws.

25. The restriction on transfer is not enforceable against Little. Such a restriction generally is not enforceable against a shareholder unless he either agreed to it or purchased his shares with notice of it. Here, the facts show that Little did not agree to the restriction. Neither did he purchase his shares with notice of the restriction, because the restriction was not imposed until after his shares had been issued to him.

26. Under the revised MBCA, Perry will be held personally liable because he meets both of the prerequisites to liability for a defective incorporation: 1) he participated in operational decisions concerning the business; and 2) he knew the corporation did not exist. Darla will not be personally liable even though she participated in management and policy decisions, because she did not know of the defective incorporation. Quentin will not be personally liable because he meets neither of the revised MBCA prerequisites to liability for a defective incorporation. Of course, Perry, Darla, and Quentin all stand to lose their respective investments in the supposed corporation, if creditors’ claims are substantial enough. Only Perry, however, may face personal liability beyond the amount of his investment.
27. Regal is not liable, but Windsor is. A corporation is not liable on a preincorporation contract unless after incorporation has taken place, the board of directors adopts the contract. Regal’s board has not done so. A promoter is liable on a preincorporation contract unless and until he is released from liability by the third party with whom he dealt. This is true, as a general rule, even if the promoter signed the as yet to be formed corporation’s name to the contract. Here, Crown has not released Windsor from liability on the contract.
CHAPTER 43
MANAGEMENT OF CORPORATIONS

ANSWERS TO CHAPTER 43

True-False Multiple Choice

1. F
2. T
3. F
4. T
5. T
6. F
7. F
8. T
9. T
10. T
11. F
12. F
13. b
14. d
15. d
16. c
17. a
18. b
19. c
20. c
21. a
22. d

Short Essay

23. In order for the directors to be entitled to the protection of the business judgment rule, they must have made an informed decision, rather than a decision made without important facts and other relevant information. Further, in making the decision, the directors must have been free from conflicts of interest. Finally, the directors must have had a rational basis for believing the decision was in the best interests of the corporation. This means that the decision must not have been manifestly unreasonable, given the pertinent facts. If all three elements (informed decision; no conflicts of interest; and rational basis for believing decision was in corporation’s best interests) coexisted at the time the decision was made, the directors will be entitled to the protection from liability afforded by the business judgment rule, even though the decision proved to have negative consequences for the corporation.

24. Maynard and Gillis will be held liable to the injured party, but Dobie will not be held liable. Maynard is liable for an obvious reason: his negligence caused the injury. Gillis is liable, because under the doctrine of respondeat superior, employers (including corporate employers) are held liable for torts committed by employees while in the scope of employment. This is true even if the employer has instructed the employee not to commit tortuous acts. Here, Maynard’s negligence occurred within the scope of his employment because he was engaged in the authorized act of driving a truck to make a delivery. Even though Dobie was the supervisor in charge of Maynard, Dobie will not be held liable, because corporate employees who did not personally participate in or authorize the tortuous act are not held liable.
25. Norm is likely to be liable to Kidsco for having usurped a corporate opportunity. Two of the three elements of usurpation are clear, because the opportunity came to Norm in his corporate capacity and Kidsco would have had the ability to take advantage of the opportunity. The only possible question (but not much of one) could be as to the one remaining usurpation element: whether the opportunity was related to the corporation’s business. Kidsco’s business was the production and sale of clothing for children up to approximately the age of five years, whereas Youthful’s business was the production and sale of clothing for elementary school age children. Almost certainly, a court would conclude that the opportunity was closely enough related to an existing or prospective line of business of Kidsco that Norm should be liable for usurping the opportunity.

26. Before a director enters into a contract with the corporation of which she is a director, she must make a disclosure of all of the material facts, and a majority of the disinterested members of the board of directors must approve the contract. Even then, however, the director is not home free, because if the contract is unfair to the corporation, the director may face liability to the corporation despite the disinterested directors’ approval of the contract. Here, however, assuming that Madeline made a full disclosure of the relevant facts before the disinterested board members approved the contract, Madeline probably is in a fairly strong position. The court may be unlikely to find that the contract is unfair to the corporation, although it clearly could do so despite the board’s approval of it. Ordinarily, a director in Madeline’s position would have the burden of proving the fairness of the challenged contract. The effect of the board’s approval is that the burden shifts to the corporation (here, the shareholder suing derivatively on behalf of the corporation) to prove that the challenged contract was unfair.
CHAPTER 44
SHAREHOLDERS’ RIGHTS AND LIABILITIES

ANSWERS TO CHAPTER 44

True-False

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Short Essay

25. The number of shares required to elect one director under cumulative voting in this case is 121. This is reached by dividing the number of share voting by 5 (number of directors to be elected, plus 1) and then adding 1 to that result.

26. The maximum amount of the dividend, under the MBCA’s solvency test, is $3,600,000. Any dividend beyond that amount would make Notbad unable to pay its currently maturing obligations and therefore insolvent. If not for the solvency test’s limitation, Notbad could pay a dividend of $11,000,000—the amount by which the current value of its assets exceeds it liabilities (the balance sheet test). Although some states allow corporations to pay dividends up to the amount of earned surplus, the MBCA governs maximum dividend amounts by requiring that both the balance sheet test and the solvency test be applied and passed.

27. The directors’ motion should be overruled and the dismissal request should be denied. Demand on the board is excused here, because it would be futile. If a demand were made, the directors would be asked to sue themselves. They cannot make a disinterested decision on that question. The directors may ultimately prevail in the suit if they are entitled to the protection of the business judgment rule, but the case should not be dismissed at this early stage on the ground asserted by the directors.
ANSWERS TO CHAPTER 45

True-False Multiple Choice

1. F
2. T
3. F
4. F
5. F
6. F
7. T
8. F
9. T
10. T
11. F
12. T
13. T
14. F
15. T

Multiple Choice

16. d
17. c
18. a
19. b
20. a
21. d
22. c
23. a
24. b
25. c
26. d
27. b

Short Essay

28. No. To use the intrastate offering exemption, the issuer must be organized and do nearly all of its business in that state and sell only to purchasers living in that state.

29. No. Even though Tweed, as Gem’s president, was a statutory insider, Gem cannot recover the profit he made because the purchase and sale did not occur within a six-month period.

30. Probably not. If there is a proper business reason for not disclosing the information, it need not be disclosed. Crabapple has a proper business reason: preventing the competition from discovering the important aspects of the new computer prior to its perfection. In addition, it is not clear from the facts that the new computer actually will be perfected. Those with access to concrete information concerning the invention must be careful not to buy Crabapple shares on the basis of the undisclosed information, however, or they will violate Rule 10b-5.
ANSWERS TO CHAPTER 51

True-False Multiple Choice

1. F 14. d
2. F 15. d
3. T 16. c
4. F 17. c
5. F 18. a
6. F 19. d
7. F 20. c
8. F 21. d
9. T 22. c
10. T 23. a
11. F 24. a
12. T 25. c
13. T

Short Essay

26. Defenses under the ADEA include firing an employee for good cause. Employers may also use reasonable factors other than age in their employment decisions. It also permits bona fide seniority systems and the ADEA recognizes a bona fide occupational qualification defense.

27. Yes. Title VII forbids discrimination against an employee due to the employee’s possession of physical, cultural, or linguistic traits associated with people of a particular national origin.

28. Title VII’s definition of religion covers, or purports to cover, almost any system of beliefs that occupies a place in the believer’s mind paralleling the place occupied by religion in the mind of a believer. So Bob’s cult probably qualifies. Because Title VII covers discrimination on the basis of the behavior required by a religion, the firm can’t dodge Title VII by saying that it only fired Bob because of his nudity. But Title VII also says that the employee behavior in question can’t cause the employer undue hardship. Undue hardship is anything more than a minimal burden on the employer. Almost surely, carrying a dysfunctional employee qualifies.
29. No, XYZ’s argument will not work because other methods of Title VII proof are available. The plaintiffs should use the adverse impact method, under which their chances of success are pretty good. Obviously we have an employment requirement with a disparate impact on black people. One must doubt whether this requirement is job-related and consistent with business necessity. Just how much connection is there between one’s possession of a high school diploma and one’s ability to be a garbage collector? Even if there were a sufficient connection, it is likely that XYZ could find a more discriminating and less discriminatory method of employee selection, so it would fail at the third step in the adverse impact method.