In the Eyes of the Law

Legal Issues Associated with Direct Farm Marketing

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ABOUT THE PUBLICATION

This project was coordinated by Kent Gustafson, extension educator, tourism, and professor. He can be reached at the Tourism Center—see the information below.

The Tourism Center of the University of Minnesota Extension Service, in cooperation with the Minnesota Office of Tourism and the Minnesota Department of Agriculture, has been exploring the potential of agritourism in Minnesota. Increased income for farm families as well as additional visitor attraction sites for communities are two major benefits of agritourism. One of the potential obstacles, however, is the perceived—as well as real—liability and risk farmers assume when they invite the public onto their property. This publication has been developed to respond to producer concerns about the liability issue and steps they can take to reduce the risks.

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The Tourism Center conducts tourism research and provides education and outreach programs for the tourism industry, community groups, and students. It is part of the University of Minnesota Extension Service and operates in partnership with various academic units, government agencies, and industry associations.

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Many agricultural producers today are taking advantage of the opportunity to increase the value of their products by processing, shipping, packaging, and selling them directly to consumers. Consumers benefit by obtaining a product from a known source. The community benefits because the dollars generated by processing and marketing stay in the local economy.

This publication provides producers who are considering becoming direct marketers a brief introduction to legal issues that may affect their business so they can avoid or minimize risk and liability. It is not intended to constitute legal advice or address every situation, since direct marketing can be as varied and expansive as creativity, ambition, intuition, and resources allow.

Don’t let the number of issues raised in this publication deter you from pursuing direct marketing. Because it is an overview, this publication necessarily addresses many general legal principles, any one or more of which may or may not be applicable to your situation. Use this publication as a discussion tool as you seek specific advice from an attorney and an accountant familiar with your goals and business plan.

You will notice case studies inserted in various places throughout this text. These are summaries of actual cases in which courts have applied the principles discussed in the immediately surrounding paragraphs. These summaries are not intended to take the place of legal advice, since many of the factual, legal, and procedural nuances of the cases had to be deleted in the process of condensing the information.
Negligence: The failure to exercise the care that a reasonable person would exercise. It means doing something that a reasonable person would not do, or failing to do something that a reasonable person would do.

Liability: Being legally responsible or obligated, or exposed to the possibility or likelihood of legal accountability.

Breach: Failure to act in conformity with a duty or standard of conduct required of a person.

Reasonable Care: The quality of care a reasonable person would exercise in the same or similar circumstances.

If you sell products from the site where they were produced, from a shop, or from your home, you have an obligation to make such areas reasonably safe for entry. The following section discusses general negligence and premises liability principles related to that obligation.

Negligence and Liability

If a customer is injured on the site at which you are conducting business, the customer may claim that you were negligent for allowing the condition that caused the accident. The injured customer alleging negligence will claim that he or she was hurt as a result of your breach of the duty to use reasonable care in keeping the premises free from dangerous conditions. The legal burden is on the customer to prove that you owed the customer a duty to keep the premises clear of such conditions, that you failed to fulfill that duty, and that the customer was injured as a result.

You have a legal duty to use reasonable care for the safety of customers invited onto your premises. How that duty is satisfied depends on the circumstances. In all cases the care you exercised will be judged as to whether it was reasonable under the circumstances. In many cases, the question of whether the direct marketer has acted reasonably is determined by the type of person involved.

You must exercise ordinary reasonable care toward children. When children are involved, the diligence required of you is expanded to take into account their smaller size and lack of caution or knowledge of particular dangers. However, you are not responsible for supervising children unless it is clear the parent is transferring supervision to you and you accept that responsibility. For example, in a case involving a child who drowned after falling from the dock of a social host, the court held that the social host did not have a special duty to the child because the child’s parents were present and were responsible for supervising the child. However, if you accept responsibility for the care and custody of children, you are...
assuming the responsibility to act as that child’s parent or guardian and will be judged according to that heightened standard.

You generally owe no duty of care to adult trespassers, and the law recognizes that trespassers are required to be alert to conditions of the premises. An exception is that you must exercise reasonable care to warn trespassers about hidden, artificial (not solely the work of nature) dangers created or maintained on site. Whether a condition is hidden depends upon whether it is visible, not whether the trespasser actually sees it.

Minnesota courts apply a different standard when the trespasser is a child and artificial conditions exist on the premises that are considered highly dangerous or attractive to children. According to case law, artificial conditions include, but are not limited to, buildings, swimming pools, retaining walls, wood piles, large machinery, and dividing walls. With respect to children, a possessor of land is subject to liability for harm to trespassing children caused by an artificial condition if

1. the place is one upon which the possessor knows or has reason to know that children are likely to trespass; AND
2. the possessor knows or has reason to know that children are likely to trespass; AND
3. the children because of their youth do not discover the condition or realize the risk involved in it or in coming within the area made dangerous by it; AND
4. the utility to the possessor of maintaining the condition and the burden of eliminating the danger are slight as compared with the risk to children involved; AND
5. the possessor fails to exercise reasonable care to eliminate the danger or otherwise protect the children.

Each of these five elements must be proven to establish your liability to trespassing children.

**Case Study**

A snowmobiler trespassing on railroad property sued the railroad for failing to warn snowmobilers of the existence of a trestle after she drove off the edge in inclement weather and was injured. Due to the nature of a procedural question involved, the Minnesota Court of Appeals did not make a decision regarding the liability of the railroad, but did state that a possessor of land who knows (or should know) that trespassers consistently intrude on a limited area of the possessor’s land is subject to liability for harm caused to the trespasser by an artificial condition on the land if the condition was created or is maintained by the possessor, the condition is likely to cause death or serious bodily harm to trespassers, the condition is of the nature that the possessor has reason to believe the trespasser will not discover the dangerousness of the condition, and the possessor fails to exercise reasonable care to warn the trespasser of the condition and the risks involved.

**Trespasser:** A person who is on the property of another without permission.

**Possessor:** One or more who have direct physical control over land at a given time; for title insurance purposes, possessor has open, visible, and exclusive use.
Owners, Occupiers, and Possessors

The nature or extent of your responsibilities to keep safe the premises on which you conduct business are affected by whether you own the site, have entered into a lease or another kind of arrangement that allows you to use the area, or are sharing the site with another person or entity.

The most important factor is the identity of the person or entity responsible for keeping the premises safe. If you own the premises, you will likely have the greatest ability to control the conditions of the premises and the greatest amount of exposure to risk. If you do not own the premises, you can still exercise some degree of control over the area by virtue of your presence and use, and therefore have some responsibility to keep the premises safe.

You will need to assess your duty to use reasonable care for the safety of persons invited to the premises in light of the following factors:

1. the circumstances under which the person enters the premises;
2. the foreseeability or possibility of harm;
3. the duty to inspect, repair, or warn;
4. the reasonableness of inspection or repair; and
5. the opportunity and ease of repair or correction.

Simply put, you will owe your customers a duty to exercise reasonable care for their safety commensurate with the circumstances involved.

Lease: A contract to rent property on the terms, for the period of time, and for the amount of rent agreed to by all parties to the contract.

Landlord: A person or entity with a legal right to possession of property and who rents the property to others.

Tenant: A person or entity that by contract has the temporary use or possession of the property of another.

Landlords and Tenants

The rights and obligations of landlords and tenants are affected not only by the written lease agreement, but also by Minnesota statutes and rules. This section outlines the premises liability obligations of each party in a lease situation. It does not address other aspects of landlord-tenant law. You should consult an attorney when considering any lease relationship.
Landlords are responsible for safely maintaining areas over which they retain control, such as hallways, stairways, and other common areas. If the landlord does not retain control of the premises, he or she normally will not be liable for injuries caused by the negligence of the tenant/occupant, provided the site was turned over to the tenant in good condition.

If a landlord performs repairs on the property, he or she is liable for injuries resulting from the negligent performance of the repairs, whether he or she performed such repairs voluntarily or was obligated to do so as part of the lease.

Tenants are obligated to exercise reasonable care for their guests and co-tenants, including both the tenant’s use of the area and any repairs undertaken by the tenant.

**Negligence Per Se**

**Negligence per se** is negligence that results from violation of a statute or ordinance enacted for the protection of others (e.g., a traffic law or fire code) or of regulatory rules.

Merely breaking the law can constitute negligence because it is a departure from a legally defined standard of conduct. Such a violation constitutes negligence if the person harmed is within the class of persons intended to be protected by the statute, ordinance, or regulation and the harm suffered is of the type the statute, ordinance, or regulation was intended to prevent. For example, you may be liable if you maintain a site that does not comply with the Minnesota Building Code and a customer is injured as a result.

**Foreseeability**

The duty you owe a customer is affected by the foreseeability or probability of harm. You generally are not liable for failing to prevent unforeseeable injuries. If a danger is obvious, you will not be liable for injury caused by that danger unless the harm can be anticipated.

If injured, a customer must show that you had either actual or constructive knowledge of a hazard, and that the hazard could foreseeably produce injuries of the nature that harmed the customer. In Minnesota law,
actual knowledge means possession of knowledge or notice of a hazard that involved danger to another. Constructive knowledge means knowledge that should have been possessed through the exercise of reasonable care.

To avoid being charged with constructive knowledge, you must satisfy your continuing duty to inspect the area to identify dangerous conditions and repair them or provide adequate and appropriate warning about them. The effort you expend toward discovering the hazard through inspection must be reasonable, and you must exercise reasonable care when carrying out the warning or repair.

Limits on Liability

Your responsibility to your customers is not absolute. All persons entering the premises have a duty to safeguard themselves, as is recognized by general legal principles as well as Minnesota’s comparative fault statute. Therefore, if an entrant is injured and alleges the injury is due to your negligence, the entrant’s own conduct should be scrutinized for fault.

Any damages recovered by the entrant may be reduced or avoided by comparing the fault of the direct marketer and the entrant. A permitted entrant is allowed to assume that you have exercised proper care to make the premises safe, and is not required to be alert for unusual circumstances or to use extraordinary caution. However, he or she must exercise reasonable care for his or her own safety.

Insurance

Many events are beyond our control, no matter how diligent or careful we are. Insurance can help you manage risks and increase your ability to recover from such events. However, you must make sure you have adequate coverage. To adequately cover your business, objectively review the activities occurring or promoted on the premises, including known hazards and foreseeable misconduct, and assess all facets of the business activities—for example, entrance by delivery persons, prospective employees, inspectors, and refuse haulers as well as customers.

Establish a relationship with your insurance agent(s) and maintain consistent communication. Keep the agent fully apprised of all changes to your business, including expansion, use of new sites, and addition of machinery or new products, so he or she can adjust your coverage accordingly. If you fail to adequately inform your agent of something in an effort to maintain a lower premium, you could be denied coverage if a problem does arise.
Homeowner’s Liability Insurance vs. Business Liability Insurance

Even if you conduct your business at or around your home, a standard homeowner’s insurance policy will likely not be adequate because commercial uses are generally excluded. Thus, a standard homeowner’s policy will likely not cover a customer if he or she is injured on the premises. Work with your agent to inquire into, and obtain, the necessary business insurance. This may be as simple as adding a commercial enterprise rider to your homeowner’s policy.

Language in Policies

A common area causing disputes between the insurance company and the insured is the language used in the policy. It is important that you carefully review your policy or have an attorney review and explain your coverage to you with particular emphasis on exclusions from or limitations on the policy’s coverage.

First, make sure the proper persons or entities are insured. Does the definition of the insured person include the business entity (if one exists) or you personally?

Second, be sure you understand what premises are insured. Do the insured premises include your retail business, manufacturing site, distribution site, production area, barn, or warehouse? Review your insurance policy to make sure the definition of “premises” is sufficiently broad to encompass all structures and aspects of the operation.

Third, confirm that the damages or injuries most likely to be suffered are covered by the policy. Be careful that what constitutes damage or injury is not too narrowly defined to provide the necessary coverage.

Be sure you understand how conduct affects your coverage. Insurance policies generally do not cover willful, intentional, or even reckless conduct. For example, a reckless environmental spill, failure to repair a particularly dangerous hazard, or intentionally harmful or violent acts of an insured or its employees or agents generally are not covered.

Notice and Cooperation

To trigger coverage, you must inform the insurance company that a covered event has occurred and describe the nature of the injury. You most likely are required to provide the notice within a certain period of time, usually measured in terms of hours. Failure to do so may void coverage. This is especially true in situations involving physical injury to a person, since the insurance company may want to move quickly to preserve evidence, interview witnesses, and conduct other aspects of investigation.

Following timely notice you normally will be required to cooperate with the insurance company’s efforts to determine the cause and amount of damages. You may be required to provide
sworn statements and access to your premises and employees. Failure to do so may result in the denial of coverage.

**Deductibles**

A deductible is a dollar value that damage must exceed before the insurer will compensate the insured for a loss. Coverage excludes the amount of the deductible. Scrutinize your policy and speak with your agent to make sure you understand both the amount of the various deductibles, and under what circumstances they apply.

**Workers’ Compensation Insurance**

Minnesota’s workers’ compensation law requires employers to pay compensation for the personal injury or death of an employee in the workplace. The compensation includes wage replacement, payment of medical and rehabilitation costs, and benefits paid to an employee’s dependents in case of death. If you have employees, confer with several licensed insurance agents who sell workers’ compensation insurance to review your business and obtain quotes before choosing workers’ compensation insurance.

Individually run or family-run sole proprietorships in which all employees are the operator’s spouse, parents, or children may not have to obtain workers’ compensation coverage. Partnerships in which the employees are a partner or a spouse, parent, or child of a partner may be exempt. Certain closely held corporations, limited liability companies, and family farm operations may also be exempt. Contact the Minnesota Department of Labor and Industry to determine whether your enterprise is subject to Minnesota’s workers’ compensation law.

**Risk Management Strategies**

The following suggestions can help you manage the risks associated with any business enterprise, including direct marketing.

**Inspect, Repair, Warn**

Regularly inspect your premises for hazards or hidden conditions. How often and thoroughly you need to inspect depends on factors such as the location, type and constancy of use and whether the hazards likely to appear are open and obvious or are within the reasonable expectation of the persons entering your property. For example, a slippery substance on the floor of a grocery store left for an hour in a highly trafficked area is clearly a breach of duty to inspect. A mud puddle covering a path in an outdoor nursery is not so clearly a breach, provided it isn’t covering another hazard.

When you discover a hazard, repair it or warn customers about it. Providing a warning may be less difficult or costly than repairing the hazard. However, some dangers remain unreasonably
dangerous even with a warning, and should always be addressed. For example, say you had a leaky gutter directly above the only entrance to your shop that resulted in formation of a large sheet of ice in front of the entrance during winter. Merely warning about the existence of the hazard would be insufficient in this circumstance.

**Learn and Follow Laws, Regulations, and Ordinances**

It takes time to learn about all laws, regulations, and ordinances applicable to your business. However, the law requires you to be aware of all such regulations. Considering the legal and financial consequences of failing to adhere to such requirements, it is time well spent.

Your business site may be subject to zoning requirements and other city or county ordinances limiting the uses to which it may be put. The premises are likely subject to building and fire codes, and possibly restrictive covenants as to use. The building may be a landmark, or located on property protected by state or federal law. Inquire with the appropriate officials to learn about any use restrictions.

Your direct marketing activity may require oversight by a regulatory agency (e.g., sale of edible products is regulated by state and federal laws and regulations that require inspection and licensing). A business or its employees and agents must be certified or licensed to conduct certain activities. Contact trade associations and agencies charged with oversight for more information.

**Use Disclaimers**

You can attempt to limit your liability by having the customer or other entrant, in advance of entering or engaging in the business enterprise, sign an **exculpatory contract** (more commonly known as a disclaimer or waiver and release from liability). The purpose of such a contract is to limit your exposure to liability by having customers acknowledge the risk and indicate that they are proceeding at their own discretion despite the risk.

Exculpatory contracts are considered valid if the service does not involve abnormally hazardous activities and if the contracts are not ambiguous or overbroad; do not purport to exonerate the landowner from liability for intentional, willful, or wanton acts; and are not against public policy. However, the courts may consider them invalid if there is a disparity of bargaining power between the parties or the service being offered is a public or essential service (e.g., services offered by common carriers, hospitals, public utilities, and innkeepers). For example, there is no disparity of bargaining power between the parties when a person voluntarily chooses to pursue an activity that is readily available elsewhere.

**Exculpatory contract:** An agreement to forgo or waive one's right to a legal claim of negligence. Also known as a disclaimer or waiver.

**Case Study**

A student who enrolled in a skydiving course sued his instructor for injuries incurred when the parachute failed to open properly. The court concluded that there was no disparity of bargaining power between the parties, skydiving lessons were not an “essential service,” and the exculpatory clause was not vague or overbroad, as it limited only the instructor’s negligence (as opposed to attempting to waive liability for intentional wrongs).
A manufacturer or seller may be found at fault for products-related injuries to a person or property. If a product you produce or sell is involved in an injury, a suit may be brought against you on the theories of negligence, strict liability, or breach of warranty. In any of these situations, the injured person must be able to prove that he or she was injured by the product.

You are expected to produce and sell products that are fit for their intended use and for uses that are unintended but reasonably foreseeable. This means that you are expected to design, manufacture, and give instructions relating to or warning about the product’s intended use and about misuse that is unintended but is nonetheless reasonably foreseeable.

**Negligence**

You must use reasonable care in designing, manufacturing, and providing sufficient instructions or warnings about your product. A person is negligent and will be found liable for damages if (1) a duty of care is owed to another; (2) that duty is breached; (3) the breach causes injury; and (4) the injury results in damages.

When designing a product, you must exercise reasonable care to avoid unreasonable risk of harm to the consumer when the product is put to its intended use or to an unintended but reasonably foreseeable use. What “reasonable care” means in this case depends on the circumstances, including the likelihood and seriousness of the potential harm compared to the feasibility and burden of precautions that would prevent it.

Sometimes a safely designed product leaves the possession of the producer in a condition that wasn’t intended by its design, making it unreasonably dangerous. For example, you design a safe product, but something happens during construction or manufacture that renders it unsafe, such as failing to follow the design specifications. If an injury occurs, the person injured may allege that the product

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**Case Study**

A child’s parent sued a window screen manufacturer after the child fell through a second-story apartment window, on the basis that the screen was defectively designed so as to fail to keep persons from falling through it. The court determined that the window screen manufacturer had no duty to design a screen that would prevent a child’s accidental dislodging of it and fall through the window, that the screen was not unreasonably dangerous when used for ventilation, that the child was not injured by a danger inherent to the product or by the screen itself, and that the screen manufacturer had no duty to warn potential users that screens would not keep children from falling through the window.
was manufactured in a negligent manner. To avoid this, exercise reasonable care in manufacturing, inspecting, testing, and assembling your product so that it is safe when used for its intended purpose, and for unintended purposes that could be reasonably expected.

An injured person also may allege negligent warning or instruction, meaning that you didn’t provide sufficient instructions or warnings about the product. You must provide adequate instructions for the safe use of the product and warn of dangers inherent in the improper use of the product when those improper uses are reasonably foreseeable.

**Strict Liability**

Strict liability differs from negligence in that negligence focuses on the conduct of the direct marketer, whereas strict liability focuses on the condition of the product. Strict liability imposes the costs of the injury caused by a defect in a product upon the direct marketer without requiring proof of negligence or even proof of a contractual relation between the direct marketer and the person injured.

To establish strict liability for a defective product, the person injured must show that the product was purchased in a defective condition unreasonably dangerous for its use, that this defective condition existed when the product left the hands of the direct marketer, and that the defect caused the injury suffered. The defect may be due to a defective design, the use of defective materials, defective manufacture, defective installation, or defective warning or instruction.

To avoid strict liability, exercise reasonable care in performing all of the above responsibilities. If you do not and the product is in a defective condition, you will be liable if that defective condition makes a product unreasonably dangerous to the consumer and causes injury.

**Breach of Warranty**

Product liability may also arise due to a claim of breach of warranty. When a consumer claims breach of warranty, he or she is saying that the product did not perform appropriately or as promised. To claim breach of warranty, a consumer must prove that a warranty exists, that the warranty was breached, and that the breach harmed him or her.

The law recognizes three types of warranties: implied warranties of merchantability, implied warranties of fitness for a particular purpose, and express warranties. The difference between implied and express warranties is that an implied warranty is created as a matter
of law and solely by virtue of the existence of the sales transaction, whereas an express warranty exists when the manufacturer or seller creates it.

**Implied Warranty of Merchantability**

Implied warranty of merchantability means the product is fit for the ordinary purpose for which it was intended. This warranty attaches automatically to a product when the manufacturer or seller is also a merchant of the product (i.e., deals in, or purports to have knowledge or skill peculiar to, the product). You are a merchant if you engage in commercial activity that involves selling a product to consumers. A breach of the implied warranty of merchantability occurs when the product fails to perform for the purpose it was reasonably intended.

You can disclaim implied warranties of merchantability by using expressions such as “As Is” or “With All Faults.” However, you must put these expressions in writing and make them conspicuous so as to clearly inform the buyer (prior to the sale) that (1) the product is being sold on an “As Is” or “With All Faults” basis, and (2) all risk as to the quality and performance of the product is on the buyer.

**Implied Warranty of Fitness**

An implied warranty of fitness exists automatically if you know the buyer’s purpose for buying the product, you know the buyer is relying on your skill or judgment to provide a product appropriate for that purpose, and the buyer relies on your skill or judgment in that way. A breach occurs when the product’s performance fails to conform with the specific purpose for which the buyer purchased it. Again, you can avoid this warranty by providing the conspicuous written disclaimer.

**Express Warranties**

Express warranties are created by the direct marketer. If you represent that a product will perform a certain way, and if the buyer relies on that statement to purchase the product, your representation becomes an express warranty. If you describe a product and the buyer relies on the description when purchasing the product, the description becomes an express warranty. If you use a sample or model and the buyer relies on the fact that the product will be identical to the sample or model used, then the buyer’s impression or beliefs based upon the

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**Case Study**

A lumber company that used a faulty design and inadequate materials in building a grain storage building that later collapsed could be held liable for breach of implied warranty of fitness where the lumber company held itself out as competent to perform the contract, and the farmers’ cooperative that owned the building had no particular expertise in the kind of work contemplated; did not furnish any plans, designs, specifications, details, or blueprints; and indicated its reliance on the experience and skill of the lumber company after making known to it the specific purposes for which the building was intended.
sample becomes the warranty. A breach of an express warranty occurs when the product does not confirm to the representation made.

Defenses to Product Liability Claims

Minnesota law recognizes several defenses to products-related claims.

Useful Life

You can argue that the product’s useful life had expired by the time the injury or breach of warranty occurred. The period of time in which a product is expected to be useful will be determined by referencing similar products, taking into account present conditions and past developments within the industry.

State-of-the-Art

You can assert that you should only be expected to guard against or warn about defects if it was technologically feasible to detect them at the time of production. In this type of defense, known as a state-of-the-art defense, the law focuses on the consumer’s expectation of the product. You argue that the consumer should have lowered his or her expectations.

Whether this is an effective defense depends on whether there is a significant lapse in time between the period during which the product was state-of-the-art and the time of purchase. The passage of a significant period of time supports your argument that the purchaser was on notice that the product was not new, since it did not look like it had been manufactured recently. The argument is most effective if you have tried to keep the product line state-of-the-art.

You can assert that you should only be expected to guard against or warn about hazards if it was technologically feasible to detect them at the time of production. Again, efficacy of this type of defense depends on the existence of a discrepancy between the period during which the product was state-of-the-art
and the time of purchase and on whether you have tried to keep the product line state-of-the-art. You may have a duty to warn when the state of the art changes and existing products are rendered unreasonably dangerous.

**Alteration or Misuse**

You must provide a product that will be safe when used as intended and when misused in a way that is reasonably foreseeable. However, you will not be responsible if the product is altered or abused in a way that is not foreseeable, or put to a use that is not foreseeable. Alteration or misuse by the consumer can be used to show that the product was not unreasonably dangerous at the time it left you.

**Inherent Danger**

Some products (e.g., knives or explosives) are inherently dangerous and can’t be designed in a way that is totally safe because the safety features would render the product useless. In such cases where the danger is open and obvious, the consumer’s conduct will be scrutinized to see if his or her actions reveal appropriate consideration for his or her own safety.

**Comparative Fault**

Minnesota’s comparative fault and statute law allows the consumer’s conduct when using the product to be compared with yours. This statute prohibits any recovery by a consumer if his or her fault is greater than yours. Even if you are more at fault than the consumer, the law allows the consumer’s damages to be reduced by the percentage of fault attributable to the consumer.

**Statute of Limitation**

A claim may be barred by a statute of limitation if it is brought too long after the alleged injury or damage occurred. Statutes of limitation can range from three to six years, depending on the injury incurred.
Risks Associated With Food Products

If you sell products to be consumed by humans or animals, you are subject to possible claims of negligence if the product is spoiled or unwholesome. Sale of unwholesome food may also expose you to regulatory enforcement action. Regulations governing the site, methods, and personnel associated with preparing, processing, packaging, and selling edibles are beyond the scope of this publication. If you offer edible products for human or animal consumption, you will likely be required to undergo licensing and inspection processes mandated by the state and/or federal government. It is recommended that you also seek legal assistance before you begin your operation to determine the identity of the regulatory agencies by which you will be regulated.
You can conduct your business through one of a variety of business structures. Each has advantages and disadvantages. Some are legally considered a separate legal identity, and, if established correctly, provide a liability shield. Each structure is accompanied by tax-related issues, so consult your accountant when choosing your business structure. Depending on your circumstances, the tax consequences may be the determining factor.

**Sole Proprietorship**

In a sole proprietorship, you own and operate the business essentially as yourself. Therefore, you are personally responsible for it. This structure lets you minimize start-up costs, simplify management, address fewer regulatory/reporting requirements than are required of certain business entities, and avoid the burden of corporate formalities. Disadvantages include personal liability for the debts and liabilities of the business, difficulties in transferring ownership, and exposure of personal assets to the claims of business creditors.

**General Partnership**

A general partnership is a contractual relationship between two or more persons to carry on an activity as co-owners for profit. General partnerships are easy to form and require no corporate formalities. They provide a pass-through taxation structure (the partnership’s income is not taxed at the partnership level but instead is taxed once it is received by the partners) and low start-up costs. A significant disadvantage is joint and several liability for all part-
ners. This means that each partner is liable for some or all of the debts and liabilities of the general partnership if the general partnership is unable or unwilling to pay them.

**Limited Partnership**

A limited partnership is a business structure formed by two or more persons, at least one of whom is a general partner, and at least one of whom is a limited partner. General partners are allowed to manage the partnership, but are also exposed to liability for partnership debts and obligations. Limited partners are protected from partnership liability, have an expectation of receiving the income of the partnership, but are not allowed any role in managing the limited partnership. This type of structure is also useful because it allows general partners to benefit from capital provided by limited partners without relinquishing management and control of the entity.

**Corporation**

A corporation’s biggest advantage over sole proprietorships and general partnerships is the liability shield it offers. This means that the owners of the corporation (the shareholders) can be “shielded” from the debts and liabilities of the corporation. Other advantages include transferability of ownership and perpetual life. Disadvantages include the necessity of conducting regular shareholder and director meetings, detailed record-keeping requirements, start-up costs, and the need to maintain corporate formalities to protect the liability shield. Tax implications should also be considered when deciding whether to incorporate.

**Sub-Chapter C Corporations**

In sub-chapter C corporations, income is taxed once at the corporate level and again at the individual shareholder level upon distribution. Qualifying corporations can avoid this double taxation by electing to be a sub-chapter S corporation.

**Sub-Chapter S Corporations**

In sub-chapter S corporations, profits and losses “pass through” the corporation and are reflected on the individual shareholders’ taxes. In order to qualify as a sub-chapter S corporation, the corporation has to meet
certain requirements and file a sub-chapter S corporation election with the Internal Revenue Service. Many corporations whose shareholders are few or are family members choose this option. However, you should consult your accountant to determine the best structure for you.

**Limited Liability Partnership**

A limited liability partnership (LLP) is a general partnership that registers as an LLP with the Minnesota secretary of state. The advantage of an LLP is its ability to shield individual partners from personal liability that arises merely because they are partners while still allowing for pass-through tax treatment of revenue. An LLP is also more flexible than a corporation because it does not require the formal management procedures or arrangements required by corporations.

**Limited Liability Company**

Like an LLP, a limited liability company offers both limited liability and the tax status of a partnership. The LLC ownership form is therefore substantially similar to LLPs and sub-chapter S corporations.

**Cooperative**

Minnesota cooperatives are entities organized on a “cooperative plan,” established primarily to provide services to their members and controlled on a democratic basis. Because cooperatives are formed for the purpose of providing services to members at the lowest possible cost, they are not organized to produce a profit for investors. Rather, any income remaining after expenses is distributed to members as a patronage refund.

**Entity:** A loose description of legal structures that separate ownership of the business enterprise and liability therefor from the ownership of the legal structure. For example, corporations, limited liability partnerships, limited liability companies, and cooperatives are entities. Sole proprietorships and general partnerships are not.
<table>
<thead>
<tr>
<th>Form of Business Entity</th>
<th>Advantages</th>
<th>Disadvantages</th>
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</table>
| **Sole Proprietorship** | • Easy start-up  
• Minimum start-up costs  
• Streamlined management  
• Minimal business formalities | • Personal responsibility for the debts and liabilities of the business  
• Creditors can reach personal assets  
• Difficulty transferring ownership  
• Finite duration |
| **General Partnership** | • Low start-up costs  
• Simple formation  
• Minimal business formalities  
• Pass-through taxation | • Personal responsibility for the debts and liabilities of the business  
• Limited duration |
| **Limited Partnership** | • Partners have the flexibility of choosing to be a limited partner or a general partner  
• Allows general partners to find a source for influx of cash from a limited partner without relinquishing control of managing the partnership to limited partners  
• Allows limited partners to benefit from the liability shield and income stream of the partnership | • Initial registration with the state  
• General partners are subject to personal responsibility for the debts and liabilities of the business  
• Limited partners are not allowed to participate in managing the partnership  
• Formal management and record-keeping requirements |
| **Corporation** | • Liability shield  
• Perpetual life  
• Relative ease in transferring ownership interests | • Start-up costs  
• Initial filing with the state  
• Annual registration  
• Requires regular shareholder and board of directors meetings  
• Detailed record-keeping requirements  
• Maintenance of liability shield requires maintaining corporate formalities |
| **Limited Liability Partnership** | • Liability shield  
• Pass-through taxation  
• Less formal management procedures than are required for corporations | • Requires an initial filing with the state  
• Annual registration and fee  
• Requires more than one person to form |
| **Limited Liability Company** | • Liability shield  
• Can be formed by one or more persons  
• Perpetual duration  
• Members can choose benefits of partnership taxation method | • Requires initial filing with the state  
• Annual registration  
• Management and formal record-keeping formalities must be observed |
| **Cooperative** | • Created by persons with common economic interests  
• Can be organized by one or more persons | • Requires initial filing with the state  
• Periodic registration  
• Limited purpose  
• Management, taxation, and record-keeping formalities must be observed |
If you hire employees, you must comply with state and federal regulations regarding hours, wages, conditions of employment, and workers’ compensation insurance. You also may be responsible for employees’ actions if you fail to take reasonable precautions to guard against employee misconduct. This section addresses the bases for such liability, and methods commonly used to avoid or minimize exposure.

**Liability for Employees’ Acts**

In Minnesota, an employer can be held responsible for damages caused by an employee acting within the scope of employment. The employer can also be held liable for the situations involving negligent hiring, negligent retention, and negligent supervision whether or not the employee’s actions are considered to be within the scope of employment.

**Negligent Hiring**

You may be accused of negligent hiring if you hire a person with known or reasonably discoverable dangerous propensities when you should have foreseen that he or she posed a threat of injury to others.

The law requires the employer to exercise reasonable care under the circumstances. The definition of “reasonable care” depends on the responsibilities of the job. The primary consideration in determining whether an employer breached the duty of reasonable care is whether the employer made a reasonable investigation before hiring the individual.
Negligent Retention

Negligent retention occurs when, during the course of employment, the employer becomes aware or should have become aware of problems with an employee that indicated the employee’s unfitness for the position, but fails to take further action such as investigation, discharge, or reassignment. The employer is expected to minimize the risks created by exposing members of the public to particularly dangerous individuals. The difference between negligent hiring and negligent retention focuses on when the employer was on notice that an employee posed a threat and failed to take steps to insure the safety of third parties.

Negligent Supervision

Negligent supervision is the failure of an employer to exercise ordinary care in supervising the employment relationship so as to prevent the foreseeable misconduct of an employee from causing harm to other persons. This means you can be liable if your employee, acting within the scope of employment, injures another person or property. Negligent supervision requires that the person injured prove the employee’s actions occurred within the scope of his or her employment.

Minimizing Risk

You can minimize the risk of being liable for negligent hiring, retention, or supervision by conducting appropriate background checks before hiring the employee and exercising reasonable care in supervising the employee. Be consistent about enforcing procedures for oversight of employee work-related responsibilities and maintain strict adherence to disciplinary procedures.

Case Study

A company had employed a man from 1977 to 1979 and again from 1984 to 1988. The gap in employment occurred when the man was imprisoned for killing a co-employee. Upon release from prison, the man was rehired as a custodian but due to repeated workplace confrontations (harassing female co-employees and challenging a male co-employee to a fight) was transferred twice, landing at another facility in August 1987. A woman was assigned to his maintenance crew in April 1988. He began to harass and threaten her at work and at home. Near the end of June, the woman asked the company to transfer her. On July 1 she found a death threat scratched on her locker door at work. The man did not appear for work on or after July 1, and the company accepted his formal resignation July 11. On July 19, the man shot and killed the woman in her driveway. A wrongful death suit was subsequently brought against the company based on the theories of negligent hiring, retention, and supervision of a dangerous employee.

The court held that the claim of negligent supervision was not viable because the man was neither on company property nor using company property when he killed the woman. Further, unlike the apartment manager case (case study, page 20), the company’s act of hiring the man did not breach a legal duty to the woman because the specific nature of his employment did not create a foreseeable risk of harm. However, the court found that the man’s work history and escalation of abusive behavior revealed the foreseeability of his acting violently against the woman. The court also determined that further proceedings would be required to determine whether the company breached its duty to the woman by failing to terminate or discipline the man, or whether the breach was the cause of her death.
Hiring Issues

Background Checks and Testing

Some forms of background checks and pre-employment testing are allowed for all applicants, while others are allowed only for applicants who have received a conditional offer of employment contingent upon passing the check or test. Most employee testing is highly regulated by law. Minnesota law contains very complex requirements regarding drug and alcohol testing. Application of laws regarding physical, psychological, and personality testing differ depending on whether the person is a pre-offer applicant, post-offer but pre-employment applicant, or employee. Obtain legal advice when considering such testing.

Inappropriate Questions

You may not ask a prospective employee questions that don’t reasonably relate to the job. Generally speaking, do not ask questions regarding marital status, employment history beyond the previous five years, gender, race, creed, disability, color, religion, national origin, sexual orientation, date of military discharge, pregnancy, children, use of birth control, test status with respect to any disease, spouse’s occupation, arrests, languages spoken at home, credit rating, physical impairments, receipt of workers’ compensation benefits, height and weight, or tobacco use.

Criminal Background Check

You can obtain limited criminal background information by contacting individual counties, the Minnesota Bureau of Criminal Apprehension (BCA), and the federal court. The county can release information without the consent of the applicant, but the information provided by the county will include only adult convictions for the past 15 years. It will not include juvenile records or arrests. To obtain criminal history from the BCA, you will need the applicant’s consent. The results will include all arrests and criminal convictions, but exclude any juvenile records.
Driving Record

If the job requires the employee to drive, you may conduct a driver’s license check to obtain information about license validity, driving-related convictions, suspensions, and revocations. At a minimum, the potential employee should affirm in writing that he or she has a valid driver’s license.

Credit Check

While a great deal of information is available from credit reporting agencies, the Federal Fair Credit Reporting Act and the Minnesota Access to Consumer Reports Act restrict the compilation and use of such information. Both acts establish disclosure, notice, and consent requirements for both consumer reports and investigative reports. A consumer report is prepared by a consumer reporting agency, and addresses credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, and mode of living. An investigative report obtains information regarding a consumer’s character, general reputation, personal characteristics, or mode of living by personal interviews with friends, colleagues, associates, or neighbors.

Numerous restrictions apply to obtaining and using such reports for employment purposes. Obtain legal advice before demanding either type of report.

Additional Requirements

Minnesota law requires some form of background check under certain circumstances. For example, home care and board and lodging providers and personal care attendants are subject to background checks. Property owners are required to perform background checks on property managers who have access to a tenant’s dwelling unit. Contact an attorney or a trade association to determine whether certain background checks are mandated for your employees.
Conclusion

The legal considerations associated with forming a direct marketing business can initially appear quite formidable. However, once you identify them, you can take the necessary steps to eliminate or manage the risks. This publication is not intended to be legal advice. Use it to become acquainted with the numerous legal principles you should discuss with your attorney. The publication points out circumstances where liability can arise. It explains how exposure to these circumstances can be limited.

We hope that after reading this publication you feel more comfortable in your own knowledge of the challenges that accompany the opportunities of owning and operating your own business.
The following checklist is intended to provide a list of items for which you should seek legal or other professional advice as you become involved in direct marketing. This list will not apply to all endeavors; nor is it intended to be comprehensive.

____ Choose, form, and name a business structure, properly filing the entity with the office of the Minnesota Secretary of State, if necessary, and registering it with the proper regulatory agencies.

____ Obtain all federal and state tax and employer identification numbers.

____ Obtain workers’ compensation insurance, if necessary.

____ Obtain employee withholding information, if necessary.

____ Obtain a Minnesota unemployment compensation employer identification number, if necessary.

____ Determine whether you will need to purchase or lease any structure and/or real estate on which it is located.

____ Determine whether you will require any occupational or environmental licenses, permits, or bonds.

____ If you seek financing to help with your start-up costs, have your attorney review all loan agreements and related financing documents.

____ Confer with your accountant to determine what type of information should be compiled to make the necessary tax-related filings.

____ Confer with your insurance agent to make sure you have the appropriate liability and property damage insurance coverage. If you feel it necessary, ask your attorney to review your policy with you.

____ You may wish to protect your intellectual property rights by seeking patent, trademark, or copyright protection.

____ Seek legal advice when hiring, testing, disciplining, and terminating employees.
This glossary is intended to help you understand terms used in this publication. Keep in mind that all legal terms are to some extent context specific. Therefore, consider the following definitions only in the specific context in which they are used within this publication.

**Actual knowledge:** Possession of knowledge or notice of a hazard that involved danger to another.

**Breach:** Failure to act in conformity with a duty or standard of conduct required of a person.

**Constructive knowledge:** Knowledge that should have been possessed through the exercise of reasonable care.

**Deductible:** A dollar value damage must exceed before an insurer will compensate for loss.

**Defect:** A condition not contemplated by the user that renders the product unreasonably dangerous to the user.

**Disclaimer:** See exculpatory contract.

**Entity:** A loose description of legal structures that separate ownership of the business enterprise and liability therefor from the ownership of the legal structure. For example, corporations, limited liability partnerships, limited liability companies, and cooperatives are entities. Sole proprietorships and general partnerships are not.

**Exculpatory contract:** An agreement to forgo or waive one’s right to a legal claim of negligence. Also known as a disclaimer or waiver.

**Landlord:** A person or entity with a legal right to possession of property and who rents the property to others.

**Lease:** A contract to rent property on the terms, for the period of time, and for the amount of rent agreed to by all parties to the contract.

**Liability:** Being legally responsible or obligated, or exposed to the possibility or likelihood of legal accountability.

**Merchant:** Someone who deals in, or purports to have knowledge or skill peculiar to, a particular product.

**Negligence:** The failure to exercise the care that a reasonable person would exercise. It means doing something that a reasonable person would not do, or failing to do something that a reasonable person would do.

**Negligence per se:** Negligence that results from violation of a statute or ordinance enacted for the protection of others.

**Possessor:** One or more who have direct physical control over land at a given time; for title insurance purposes, possessor has open, visible, and exclusive use.

**Product liability:** A term that encompasses a substantive area of law addressing the claims of persons who have been injured by a product, and a determination of responsibility for those damages on the part of all persons or entities in the chain of custody of the product.

**Reasonable care:** The quality of care a reasonable person would exercise in the same or similar circumstances.

**Tenant:** A person or entity that by contract has the temporary use or possession of the property of another.

**Trespasser:** A person who is on the property of another without permission.

**Waiver:** See exculpatory contract.

**Warranty:** A promise regarding the quality or quantity of goods made in conjunction with their sale or lease.
Resources

Internal Revenue Service
Warren E. Burger Federal Building
316 North Robert Street
Room 400
St. Paul, MN 55101
651-312-7777
www.irs.ustreas.gov

Minnesota Department of Agriculture
90 West Plato Boulevard
St. Paul, MN 55107
651-297-2200
www.mda.state.mn.us

Minnesota Department of Commerce
85 7th Place East
Suite 500
St. Paul, MN 55101-2198
651-296-4026
www.commerce.state.mn.us

Minnesota Department of Labor and Industry
443 Lafayette Road N.
St. Paul, MN 55155-4307
651-296-6107
800-342-5354
www.doli.state.mn.us

Minnesota Department of Revenue
600 North Robert Street
St. Paul, MN 55146-7100
651-296-3403
800-657-3605
www.taxes.state.mn.us

Minnesota Department of Trade and Economic Development
500 Metro Square Building
121 East 7th Place
St. Paul, MN 55101-2146
651-296-6424
800-657-3858
www.dted.state.mn.us

Minnesota Office of Environmental Assistance
520 Lafayette Road N, Floor 2
St. Paul, MN 55155-4100
651-296-3417
800-657-3843
www.moea.state.mn.us

Minnesota Secretary of State
180 State Office Building
100 Constitution Avenue
St. Paul, MN 55155-1299
651-296-2803
877-551-6767
www.sos.state.mn.us

USDA Rural Development Division
Rural Development State Office
410 Farm Credit Service Building
375 Jackson Street
St. Paul, MN 55101-1853
651-602-7800
www.rurdev.usda.gov

U.S. Department of Labor
220 South Second Street
Room 100
Minneapolis, MN 55401
612-370-3111
www.dol.gov

U.S. Equal Employment Opportunity Commission
330 Second Avenue South
Suite 430
Minneapolis, MN 55402-2224
612-335-4040
www.eeoc.gov

U.S. Small Business Administration
Minnesota District Office
100 North Sixth Street
Suite 610-C Butler Square
Minneapolis, MN 55403
612-370-2324
www.sba.gov/mn