

**Gleim Exam Questions and Explanations**  
**Updates to Business Law & Legal Studies**  
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NOTE: Sections with changes are indicated by a vertical bar in the left margin. Text that should be deleted is displayed with a line through it. New text is shown with blue underlined font.

The following edits to Study Units 19 and 20 update the bankruptcy threshold amounts effective April 1, 2025.

### **Study Unit 19 – Bankruptcy Overview and Administration**

Pages 289-293, Outline, beginning with the first paragraph on page 289:

An **involuntary petition** is filed under **Chapter 7 or Chapter 11** (but not Chapter 13) against an eligible debtor. The law imposes no limit on the number or timing of involuntary petitions. An involuntary petition cannot be filed against (1) farmers, (2) banks, (3) insurers, (4) nonprofit corporations, (5) railroads, and (6) persons who owe less than ~~\$18,600~~ 21,050. If the debtor has **12 or more different creditors**, any **three or more** who together hold **unsecured claims** of at least ~~\$18,600~~ 21,050 can file an involuntary petition. If the debtor has **fewer than 12 creditors**, any **one or more** who alone or together have **unsecured claims** of at least ~~\$18,600~~ 21,050 can file an involuntary petition. Any creditors who are the debtor's **employees or insiders**, e.g., (1) officers or directors of a corporation, (2) a corporation controlled by the debtor, (3) relatives, or (4) a partner, are not counted.

[ . . . ]

The creditors involved in the distribution of the debtor's estate are (1) secured creditors, (2) priority creditors (unsecured), and (3) general creditors (other unsecured creditors). **Secured creditors** have property rights that are not affected by the trustee. They are paid in full if the collateral is sufficient. If the collateral is insufficient, the secured creditor is a general unsecured creditor as to the deficiency. After secured claims are paid to the extent of collateral, **priority creditors** (unsecured creditors who have a statutory preference because of the nature of their claims) are paid next. Members of a higher class of priority creditors are paid in full before members of a lower class receive anything. If the assets are insufficient to pay all claims in a given class, the claimants in the class share pro rata. The classes of **priority claims** listed in descending order of rank are as follows: (1) **domestic support obligations**; (2) claims for **administrative expenses** and expenses incurred in preserving and collecting the estate; (3) claims of tradespeople (**gap creditors**) who extend unsecured credit in the ordinary course of business after the filing of an involuntary petition but before the earlier of the appointment of a trustee or the entry of the order for relief; (4) **wages** (compensation) up to ~~\$15,150~~ 17,150 per employee earned within the 180 days prior to the earlier of the filing or cessation of the debtor's business; (5) certain contributions owed to the debtor's **employee benefit plans** arising from employee services rendered within 180 days prior to the earlier of the filing or the cessation of the debtor's business; (6) claims of **grain or fish producers** for up to ~~\$7,475~~ 8,450 each for grain or fish deposited with the debtor but not paid for or returned; (7) claims of **consumers** for the return of up to ~~\$3,350~~ 3,800 each in prebankruptcy deposits paid to the debtor for services not rendered, or for the purchase or rental of property not delivered, if the services or property were for personal, family, or household use; (8) certain claims for unsecured federal, state, and local **taxes**; (9) claims based on a debtor's commitment to a federal depository institutions regulatory agency to maintain the capital of an insured depository institution; and (10) death and injury claims from operation of a motor vehicle or vessel by an intoxicated person.

[ . . . ]

**Exempt assets** of the debtor are considered basic necessities for a fresh start. Exempt assets are defined by either federal or state law. Only **individual debtors**, not corporations, are eligible for exemptions. **States** are permitted to require their citizens to accept the exemptions under state law, and most have done so. Otherwise, the debtor may choose the state or the federal list. The following are the **federal exemptions**: (1) up to \$27,900 31,575 in equity in the debtor's residence and burial plot; (2) an interest in a motor vehicle, up to a value of \$4,450 5,025; (3) an interest, up to a value of \$700 800, in any item of household goods and furnishings, clothing, appliances, books, animals, crops, or musical instruments, with a total limited to \$14,875 16,850; (4) an interest in jewelry, up to a value of \$1,875 2,125; (5) any other property worth up to \$1,475 1,675, plus any unused part of the \$27,900 31,575 equity in the debtor's residence, up to an amount of \$13,950 15,800; (6) an interest in any tools of the debtor's trade, up to a value of \$2,800 3,175; (7) any unmaturred life insurance owned by the debtor; (8) certain interests in accrued dividends or interest under life insurance owned by the debtor not exceeding \$14,875 16,850; (9) professionally prescribed health aids; (10) the right to receive Social Security, certain welfare benefits, veterans' benefits, disability benefits, alimony and support, and certain pension benefits; (11) the right to receive certain personal injury and other awards up to \$27,900 31,575; (12) unemployment compensation; (13) the ability to void certain judicial liens, e.g., on exempt property; and (14), regardless of which exemptions (federal or state) apply, amounts in tax exempt retirement accounts (but **IRAs** are capped at \$1,512,350 1,711,975). However, exempt property is liable for nondischargeable domestic support obligations.

[ . . . ]

The trustee can **void preferential transfers**. The transfer may be (1) a voluntary property conveyance, (2) a voluntary creation of a lien (a mortgage or a security interest), or (3) the involuntary creation of a lien (e.g., a judgment lien obtained by a creditor). A **voidable** preferential transfer is made (1) to or for the benefit of a creditor, (2) for or on account of an antecedent (pre-existing) debt, (3) during the debtor's insolvency, (4) within 90 days prior to filing the petition, and (5) for the purpose of entitling the creditor to receive a larger portion of its claim than otherwise would be received under a distribution in bankruptcy. The trustee may void preferential transfers and grants of security interests to **insiders** if made within **1 year** before the filing of the petition. The debtor must have been insolvent at the time of the transfer or grant. However, property purchased by an **innocent third party** from a preferential transferee cannot be recovered. That transfer is not voidable, but the preferential transferor may be liable for its value. Other transfers **not voidable** as preferences include (1) payments of accounts payable paid in the ordinary course of the debtor's and transferee's business or financial affairs; (2), if the debtor is an individual, payment of up to \$600 on a **consumer debt**; (3), if an individual's debts are primarily nonconsumer debts, any transfer worth less than \$7,575 8,575; (4) asset transfers for current consideration (new value); (5) bona fide transfers for alimony, maintenance, or support to a spouse, former spouse, or child of the debtor; and (6) gifts that are not voidable preferences or fraudulent transfers because they are not on account of a debt. The trustee also can void **preferential liens**, including judgment liens and other liens obtained by any legal or equitable proceeding. These liens arise in the circumstances described for preferential transfers.

Pages 295-300, 303, and 308; Subunit 19.2; Questions 1, 3-5, 8-11, 13-15, 23, 36, and 38:

**19.2.1.** To file for bankruptcy under Chapter 7 of the Federal Bankruptcy Code, an individual must

- A. Have debts of any amount.
- B. Be insolvent.
- C. Be indebted to more than three creditors.
- D. Have debts in excess of ~~\$48,600~~ 21,050.

**Answer (A) is correct.** (CPA, adapted)

**REQUIRED:** The requirement to file for protection under Chapter 7 of the Bankruptcy Code.

**DISCUSSION:** Under Chapter 7, generally, a debtor's nonexempt assets are converted into cash, the cash is distributed among creditors, and the debtor is discharged from most remaining obligations. Any person eligible to be a debtor under Chapter 7 may file a petition.

**Answer (B) is incorrect.** Insolvency is not required to file a voluntary petition. It is only necessary that the person be under Chapter 7. **Answer (C) is incorrect.** Number-of-creditors thresholds apply only to involuntary petitions filed by creditors. **Answer (D) is incorrect.** Amount-of-debt thresholds apply only to involuntary petitions.

**19.2.3.** A voluntary petition filed under the liquidation provisions of Chapter 7 of the Federal Bankruptcy Code

- A. Is not available to a corporation unless it has previously filed a petition under the reorganization provisions of Chapter 11 of the Federal Bankruptcy Code.
- B. Automatically stays collections actions against the debtor except by secured creditors.
- C. Will be dismissed unless the debtor has 12 or more unsecured creditors whose claims total at least ~~\$48,600~~ 21,050.
- D. Does not require the debtor to show that the debtor's liabilities exceed the fair market value of assets.

**Answer (D) is correct.** (CPA, adapted)

**REQUIRED:** The true statement about a voluntary petition under Chapter 7 of the Bankruptcy Code.

**DISCUSSION:** A debtor need not be insolvent to file for protection of Chapter 7 of the Bankruptcy Code. The debtor need merely state (s)he has a debt, and (s)he must be an eligible type of person.

**Answer (A) is incorrect.** A corporation is eligible to file a voluntary petition. It need not previously have filed under Chapter 11. **Answer (B) is incorrect.** The stay operates against a secured creditor. Only if the court grants a petition to vacate the stay might the secured party proceed to repossess the collateral or take other action. **Answer (C) is incorrect.** Number-of-creditors and amount-of-debt thresholds apply only to involuntary petitions.

**19.2.4.** Green owes the following amounts to unsecured creditors: Rice, ~~\$5,700~~ 7,700; Zwick, ~~\$5,200~~ 6,200; Young, ~~\$19,400~~ 22,400; and Zinc, \$7,900. Green has not paid any creditor since January 1, Year 1. On March 15, Year 1, Green's sole asset, a cabin cruiser, was seized by Xeno Marine Co., the holder of a perfected security interest in the boat. On July 1, Year 1, Rice, Zwick, and Zinc involuntarily petitioned Green into bankruptcy under Chapter 7 of the Federal Bankruptcy Code. If Green opposes the involuntary petition, the petition will be

- A. Upheld, because the three filing creditors are owed more than ~~\$48,600~~ 21,050.
- B. Upheld, because one creditor is owed more than ~~\$48,600~~ 21,050.
- C. Dismissed, because there are fewer than 12 creditors.
- D. Dismissed, because the boat was seized more than 90 days before the filing.

**Answer (A) is correct.** (CPA, adapted)

**REQUIRED:** The status of an involuntary petition under Chapter 7.

**DISCUSSION:** If the debtor has fewer than 12 creditors, any one or more creditors who alone or together have unsecured claims of ~~\$48,600~~ 21,050 or more can file an involuntary petition under Chapter 7 or 11. If the debtor has 12 or more creditors, any three or more who together hold unsecured claims of at least ~~\$48,600~~ 21,050 can file an involuntary petition. The three filers are owed ~~\$48,800~~ 21,800 (~~\$5,700~~ 7,700 + ~~\$5,200~~ 6,200 + \$7,900).

**Answer (B) is incorrect.** Young did not join in filing the petition. **Answer (C) is incorrect.** A debtor with fewer than 12 creditors may be involuntarily petitioned into bankruptcy by one or more creditors who alone or together are owed more than ~~\$48,600~~ 21,050. **Answer (D) is incorrect.** A challenged involuntary petition is not dismissed if the debtor is generally not paying his or her bills as they become due or, within 120 days before filing, a custodian or receiver took possession of all or most of the debtor's property to enforce a lien against the property.

**19.2.5.** Willa Wilk owes a total of \$50,000 to eight unsecured creditors and one fully secured creditor. Rusk is one of the unsecured creditors and is owed ~~\$19,200~~\$22,500. Rusk has filed a petition against Wilk under the liquidation provisions of the Bankruptcy Code. Wilk has been unable to pay her debts as they become due, and Wilk's liabilities exceed her assets. Wilk has filed the papers that are required to oppose the bankruptcy petition. Which of the following statements is true?

- A. The petition will be granted because Wilk is unable to pay her debts as they become due.
- B. The petition will be granted because Wilk's liabilities exceed her assets.
- C. The petition will be dismissed because three unsecured creditors must join in the filing of the petition.
- D. The petition will be dismissed because the secured creditor failed to join in the filing of the petition.

**19.2.8.** Which of the following requirements must be met for creditors to file an involuntary bankruptcy petition under Chapter 7 or Chapter 11 of the Federal Bankruptcy Code?

- A. The debtor must owe at least ~~\$18,600~~\$21,050.
- B. The debtor has not been paying its bona fide debts as they become due.
- C. There must not be more than 12 creditors.
- D. At least one fully secured creditor must join in the petition.

**Answer (A) is correct.** (CPA, adapted)

**REQUIRED:** The true statement about the entry of an order for relief in an involuntary bankruptcy case.

**DISCUSSION:** In an involuntary bankruptcy case, a single creditor may file a petition for relief if (s)he is owed ~~\$18,600~~\$21,050 or more, and the debtor has fewer than 12 creditors. The petition will be granted, even if it is contested, if the creditor can prove either that (1) the debtor is not paying his or her debts as they become due or (2) a custodian took possession of the debtor's property within 120 days before the filing of the petition. Thus, Rusk has met the conditions to file the petition, Wilk is unable to pay her debts as they become due, and the petition will be granted even if it is contested.

**Answer (B) is incorrect.** Having liabilities in excess of assets is not a criterion for granting of an involuntary petition for relief. **Answer (C) is incorrect.** Three unsecured creditors must join in filing the petition only if there are 12 or more creditors. **Answer (D) is incorrect.** A secured creditor is not required to join in filing the petition.

**Answer (A) is correct.** (CPA, adapted)

**REQUIRED:** The requirement for creditors to file an involuntary bankruptcy petition.

**DISCUSSION:** An involuntary bankruptcy petition may be filed by one or more creditors who have unsecured claims of at least ~~\$18,600~~\$21,050 if the debtor has fewer than 12 creditors. If the debtor has 12 creditors or more, three or more who have unsecured claims of at least ~~\$18,600~~\$21,050 in the aggregate must sign the petition. The petition will be granted, even if it is contested, if the creditor can prove either that the debtor is not paying his or her undisputed debts as they become due or that, during the 120 days preceding the filing of the petition, a custodian took possession of the debtor's property.

**Answer (B) is incorrect.** The petition also may be filed if a custodian, assignee, or general receiver took possession of the debtor's property during the 120 days preceding the filing of the petition. **Answer (C) is incorrect.** Three unsecured creditors may join in filing the petition if there are 12 or more creditors. **Answer (D) is incorrect.** A secured creditor is not required to join in filing the petition.

Questions 19.2.9 and 19.2.10 are based on the following information.

On May 1, Dart, Inc., a closely held corporation, was petitioned involuntarily into bankruptcy under the liquidation provisions of Chapter 7 of the Federal Bankruptcy Code. Dart contested the petition.

Dart has not been paying its business debts as they become due, has defaulted on its mortgage loan payments, and owes back taxes to the IRS. The total cash value of Dart's bankruptcy estate after the sale of all assets and payment of administration expenses is \$100,000.

A listing of Dart's creditors is presented in the next column.

- Fracon Bank is owed \$76,000 principal and accrued interest on a mortgage loan secured by Dart's real property. The property was valued at and sold, in bankruptcy, for ~~\$74,000~~ 68,000.
- The IRS has a \$12,000 recorded judgment for unpaid corporate income tax.
- JOG Office Supplies has an unsecured claim of ~~\$7,000~~ 10,000 that was timely filed.
- Nanstar Electric Co. has an unsecured claim of \$1,200 that was not timely filed.
- Decoy Publications has a claim of \$15,000, of which \$2,000 is secured by Dart's inventory that was valued and sold, in bankruptcy, for \$2,000. The claim was timely filed.

**19.2.9.** Assuming the IRS does not join in the filing of the involuntary petition against Dart, which of the following must file?

- I. JOG Office Supplies
- II. Nanstar Electric Co.
- III. Decoy Publications
- IV. Fracon Bank

- A. I, II, III, and IV.
- B. II and III only.
- C. I and II only.
- D. III only.

**19.2.10.** Which of the following statements accurately describes the result of Dart's opposing the petition?

- A. Dart will win because the petition should have been filed under Chapter 11.
- B. Dart will win because there are not more than 12 creditors.
- C. Dart will lose because it is not paying its debts as they become due.
- D. Dart will lose because of its debt to the IRS.

**Answer (D) is correct.** (CPA, adapted)

**REQUIRED:** The creditor(s) required to join in the filing of an involuntary petition.

**DISCUSSION:** Under Chapter 7, if a debtor has fewer than 12 creditors, an involuntary bankruptcy petition may be filed by any one or more creditors who alone or together have ~~\$18,600~~ 21,050 or more of unsecured claims (in excess of security interests). Nanstar's unsecured claim is irrelevant because it was not timely filed. But Decoy must file to meet the statutory requirement because it has \$13,000 ( $\$15,000 - \$2,000$ ) of unsecured debt. JOG ( $\$5,750$  8,750) or Fracon ( $\$77,150 - \cancel{\$74,000}$  68,000 =  $\$6,150$  9,150) must join in the petition to meet the ~~\$18,600~~ 21,050 minimum requirement. Given that the IRS does not file, Decoy is an indispensable party.

**Answer (C) is correct.** (CPA, adapted)

**REQUIRED:** The result of the debtor's opposing the petition.

**DISCUSSION:** The two grounds for filing an involuntary petition for bankruptcy under Chapter 7 are (1) the debtor is not paying its undisputed debts on time, or (2) a custodian, assignee, or general receiver took possession of all or most of the debtor's property to enforce a lien against the property within 120 days of the filing of the petition. Because Dart was not paying its bills when they became due, Dart will lose.

**Answer (A) is incorrect.** The involuntary petition could have been filed under Chapters 7 or 11. One of the statutory grounds for involuntary bankruptcy is met because Dart is not paying its bills on time. **Answer (B) is incorrect.** A debtor having fewer than 12 creditors may be petitioned into bankruptcy by any one or more creditors having alone or together at least ~~\$18,600~~ 21,050 unsecured claims. **Answer (D) is incorrect.** IRS claims will not allow the petitioner(s) to win even though the IRS claims against Dart cannot be discharged.

**19.2.11.** A contested involuntary petition in bankruptcy will be dismissed if the debtor

- A. Owes unsecured obligations exceeding ~~\$18,600~~ 21,050 to fewer than three creditors.
- B. Had all its property taken to enforce a lien within 120 days of filing.
- C. Is failing to pay undisputed debts as they become due.
- D. Is an individual engaged in the business of farming.

**Answer (D) is correct.** (CPA, adapted)

**REQUIRED:** The basis for dismissal of an involuntary petition in bankruptcy.

**DISCUSSION:** Creditors may petition a debtor involuntarily into bankruptcy proceedings under Chapters 7 and 11 of the Bankruptcy Code. The debtor must be a person eligible for protection under the particular chapter. But an individual engaged in the business of farming may not be involuntarily petitioned into bankruptcy.

**Answer (A) is incorrect.** If the debtor has fewer than 12 different creditors, any one creditor who has an unsecured claim of at least ~~\$18,600~~ 21,050 can file an involuntary petition. **Answer (B) is incorrect.** An involuntary petition will not be dismissed if, within 120 days before filing, a custodian assigned or general receiver took possession of all or most of the debtor's property to enforce a lien against the property.

**Answer (C) is incorrect.** An involuntary petition will not be dismissed if the debtor is generally not paying his or her bills as they become due in the ordinary course of business.

**19.2.13.** An involuntary petition in a liquidation case under Chapter 7 of the Bankruptcy Code

- A. Will be denied if a majority of creditors in amount and in number have agreed to a common law composition agreement.
- B. Can be filed by creditors only once in a 7-year period.
- C. May be successfully opposed by the debtor by proof that the debtor is solvent in the balance sheet sense.
- D. If not contested will result in the entry of an order for relief by the bankruptcy judge.

**Answer (D) is correct.** (CPA, adapted)

**REQUIRED:** The true statement about an involuntary petition.

**DISCUSSION:** If the uncontested involuntary petition is in proper form, the court will issue an order for relief. The debtor will be required to furnish the court with the same information as would have been contained in a voluntary petition, an interim trustee will be appointed by the U.S. Trustee to take control of the estate, and a creditors' meeting will be called. In general, the procedure is the same whether the bankruptcy is voluntary or involuntary.

**Answer (A) is incorrect.** One creditor (three given 12 or more creditors) with unsecured, noncontingent claims of ~~\$18,600~~ 21,050 or more may petition a debtor into bankruptcy.

**Answer (B) is incorrect.** Under Chapter 7, a discharge may be granted to a debtor only once every 8 years. However, the number of involuntary petitions is unlimited. **Answer (C) is incorrect.** Solvency in the balance sheet sense means that assets at fair value exceed liabilities. A statutory basis for insolvency may exist even though the debtor's assets far exceed liabilities.

**19.2.14.** Which of the following statements is true concerning the voluntary filing of a petition in bankruptcy?

- A. The debtor must be insolvent.
- B. The petition may be filed by husband and wife jointly.
- C. If the debtor has 12 or more creditors, the debtor's unsecured claims must total at least ~~\$18,600~~ 21,050.
- D. If the debtor has fewer than 12 creditors, the debtor's unsecured claims must total at least ~~\$18,600~~ 21,050.

**Answer (B) is correct.** (CPA, adapted)

**REQUIRED:** The true statement about the voluntary filing of a petition in bankruptcy.

**DISCUSSION:** A bankruptcy case may be commenced voluntarily or involuntarily. In a voluntary case, the debtor files the petition with the bankruptcy court. Debtors may include individuals, partnerships, corporations, and couples, if the husband and wife file together.

**Answer (A) is incorrect.** Insolvency is not a prerequisite for filing a voluntary petition. **Answer (C) is incorrect.** The 12-creditor threshold is applicable only to involuntary petitions. **Answer (D) is incorrect.** The 12-creditor threshold is applicable only to involuntary petitions.

**19.2.15.** Which of the following statements is true with respect to a voluntary bankruptcy proceeding under the liquidation provisions of the Bankruptcy Code?

- A. The debtor must be insolvent.
- B. The liabilities of the debtor must total \$18,600 ~~21,050~~ or more.
- C. It may be properly commenced and maintained by any person who is insolvent.
- D. The filing of the bankruptcy petition constitutes an order for relief.

**Answer (D) is correct.** (CPA, adapted)

**REQUIRED:** The true statement about a voluntary bankruptcy proceeding.

**DISCUSSION:** The voluntary bankruptcy petition is a formal request by the debtor to the court for an order for relief. Under the liquidation provisions, an order for relief is automatically given to the debtor upon the filing of the petition.

**Answer (A) is incorrect.** Insolvency is not required.

A statement that the debtor has debts is all that is needed.

**Answer (B) is incorrect.** A voluntary bankruptcy proceeding requires no minimum amount of debtor liabilities. **Answer (C) is incorrect.** The courts have discretion not to grant relief that would constitute a substantial abuse of the bankruptcy laws. Also, certain entities, e.g., banks, are not eligible for voluntary bankruptcy.

**19.2.23.** Which of the following unsecured debts of \$500 each would have the highest relative priority in the distribution of a bankruptcy estate in a liquidation proceeding?

- A. Tax claims of state and municipal governmental units.
- B. Liabilities to employee benefit plans arising from services rendered during the month preceding the filing of the petition.
- C. Claims owed to customers who gave deposits for the purchase of undelivered consumer goods.
- D. Wages earned by employees during the month preceding the filing of the petition.

**Answer (D) is correct.** (CPA, adapted)

**REQUIRED:** The relative priorities of unsecured debts in a bankruptcy liquidation distribution.

**DISCUSSION:** The Bankruptcy Code sets priorities for the claims of unsecured creditors. All of the claims at a higher priority level must be satisfied in full before any lower priority claims will be considered. The priorities are as follows: (1) domestic support obligations; (2) estate expenses; (3) unsecured claims arising in the ordinary course of business after the petition was filed but before the order for relief was granted; (4) unsecured claims up to \$15,150 ~~17,150~~ for wages earned by an individual within 180 days before the earlier of filing or the cessation of the debtor's business; (5) certain unsecured claims for contributions to employee benefit plans; (6) unsecured claims of fish or grain producers up to \$7,475 ~~8,450~~; (7) unsecured claims of depositors of money for the purchase of undelivered consumer goods up to \$3,350 ~~3,800~~ each; (8) unsecured tax claims of governmental units; (9) claims based on a debtor's commitment to a federal depository institutions regulatory agency to maintain the capital of an insured depository institution; and (10) death and injury claims arising from operation of a motor vehicle or vessel by a legally intoxicated person.

**Answer (A) is incorrect.** Tax claims have a lower relative priority in a bankruptcy liquidation than wages.

**Answer (B) is incorrect.** Liabilities to employee benefit plans have a lower relative priority in a bankruptcy liquidation than wages. **Answer (C) is incorrect.** Claims owed to customers who gave deposits for the purchase of undelivered consumer goods have a lower relative priority in a bankruptcy liquidation than wages.

**19.2.36.** In a voluntary bankruptcy proceeding under Chapter 7 of the Federal Bankruptcy Code, which of the following claims incurred within 90 days prior to filing will be paid first?

- A. Unsecured federal taxes.
- B. Utility bills up to \$1,100.
- C. Voluntary contributions to employee benefit plans.
- D. Employee vacation and sick pay up to ~~\$15,150~~ 17,150 per employee.

**Answer (D) is correct.** (CPA, adapted)

**REQUIRED:** The true statement about the relative priorities of claims in a bankruptcy liquidation distribution.

**DISCUSSION:** Secured claims must be satisfied in full before paying any unsecured claims. Unsecured claims with a higher priority are then paid in full before lower priority claims. The list of priorities among unsecured claims is as follows:

1. Domestic support obligations,
2. Administrative expenses,
3. Claims arising in the ordinary course of business after the petition was filed but before the order for relief was granted,
4. Claims up to ~~\$15,150~~ 17,150 for wages earned by an individual within 180 days before filing,
5. Claims for contributions to employee benefit plans,
6. Claims of grain or fish producers up to ~~\$7,475~~ 8,450,
7. Claims of depositors of money for the purchase of undelivered consumer goods up to ~~\$3,350~~ 3,800 each,
8. Tax claims of governmental units,
9. Claims based on a debtor's commitment to a federal depository institutions regulatory agency to maintain the capital of an insured depository institution, and
10. Death and injury claims arising from an intoxicated person's operation of a motor vehicle.

Employee vacation pay and sick pay are forms of compensation (wages).

**Answer (A) is incorrect.** Unsecured federal taxes have a lower relative priority in bankruptcy liquidation distribution.

**Answer (B) is incorrect.** Utility bills due before the petition was filed are not claims of GAP creditors and do not have a priority. **Answer (C) is incorrect.** Voluntary contributions to employee benefit plans have a lower relative priority in bankruptcy liquidation distribution.

**19.2.38.** Under the Federal Bankruptcy Code, an involuntary petition in bankruptcy may not be filed against which of the following parties?

- A. A stockbroker.
- B. A farmer.
- C. A postal worker.
- D. A railroad employee.

**Answer (B) is correct.** (CPA, adapted)

**REQUIRED:** The party protected from involuntary petition.

**DISCUSSION:** An involuntary petition may be filed against an eligible debtor exclusively under Chapter 7 or Chapter 11. However, an involuntary petition may not be filed against farmers, banks, insurers, nonprofit corporations, railroads, and persons who owe less than ~~\$18,600~~ 21,050.

**Answer (A) is incorrect.** A stockbroker is an eligible debtor, and involuntary petitions may be filed against eligible debtors. **Answer (C) is incorrect.** A postal worker is an eligible debtor, and involuntary petitions may be filed against eligible debtors. **Answer (D) is incorrect.** A railroad employee is an eligible debtor, and involuntary petitions may be filed against eligible debtors.

## Study Unit 20 – Bankruptcy Liquidations, Reorganizations, and Adjustments

Pages 309 and 313, Outline:

Individual debtors under Chapter 7 may receive a **discharge from most debts** that remain unpaid after distribution of the debtor's estate. But corporations and partnerships are precluded from Chapter 7 discharge, and most other debtors are eligible for a discharge only **once every 8 years**. Grounds for **denial** of a general discharge include the debtor's (1) waiving discharge, (2) fraudulently transferring or concealing property within 12 months preceding the filing of the bankruptcy petition or the property of the estate after filing, (3) unjustifiably concealing or destroying business records or failing to keep adequate business records, and (4) other conduct that is wrongful or obstructive. **Nondischargeable debts** include the following: (1) federal income tax due within 3 years prior to bankruptcy; (2) debts incurred on the basis of materially false financial statements if (a) issued with the intent to deceive and (b) the creditor reasonably relied on them; (3) debts not included in required filings in time to permit filing of a proof of claim; (4) debts resulting from fraud, misrepresentation, embezzlement, larceny, or violation of a fiduciary duty; (5) debts for alimony, maintenance, or child support awards; (6) debts arising from malicious injury to another person or illegal use or abuse of that person's property; (7) debts for certain educational loans made, funded, or guaranteed by a government; (8) governmental fines and penalties not related to dischargeable taxes; (9) debts arising from liability for operating a motor vehicle while legally intoxicated; (10) credit card debts greater than \$800~~900~~ owed to a single creditor by an individual debtor for luxury goods or services incurred on or within 90 days prior to filing; (11) cash advances aggregating more than \$1,400~~1,250~~ under an open-end credit plan obtained by an individual debtor within 70 days prior to filing; and (12) nondischarged debts from a prior bankruptcy.

[...]

Chapter 13 provides a procedure for the **adjustment of debts of an individual** with regular income who owes **unsecured debts** of less than \$465,275~~526,700~~ and **secured debts** of less than \$1,395,875~~1,580,125~~. Sole proprietorships also are eligible if the debt limitations are met. The debts must be owing and unpaid at the time the debtor files the petition. A proceeding under Chapter 13 may be initiated only by the debtor's filing a **voluntary petition** with the Bankruptcy Court. A trustee is required.

## Pages 321-322, Subunit 20.2, Questions 2 and 7:

**20.2.2.** Englebert is a professor of business at a university. He expected a large raise this year and made a lot of expenditures, including a trip around the world, on credit. However, university funding has been reduced and the raise did not go through. Englebert cannot pay his debts as they become due. Englebert

- A. Can request an adjustment of debts under Chapter 13.
- B. Cannot request a reorganization under Chapter 11.
- C. Can be required to go through a bankruptcy liquidation.
- D. Can be required by creditors to go through an adjustment of debts under Chapter 13.

**20.2.7.** Hall, CPA, is an unsecured creditor of Tree Co. for ~~\$19,000~~ \$22,000. Tree has a total of 10 creditors, all of whom are unsecured. Tree has not paid any of the creditors for 3 months. Under Chapter 11 of the Federal Bankruptcy Code, which of the following statements is true?

- A. Hall and two other unsecured creditors must join in the involuntary petition in bankruptcy.
- B. Hall may file an involuntary petition in bankruptcy against Tree.
- C. Tree may not be petitioned involuntarily into bankruptcy under the provisions of Chapter 11.
- D. Tree may not be petitioned involuntarily into bankruptcy because it has fewer than 12 unsecured creditors.

**Answer (A) is correct.** (Publisher, adapted)

**REQUIRED:** The true statement about an individual who cannot pay his or her debts.

**DISCUSSION:** An individual with regular income may submit a plan for the payment of a portion of his or her debts while retaining sufficient income to live and support a family. The petitioner must be an individual who owes unsecured debts of less than ~~\$465,275~~ \$526,700 and secured debts of less than ~~\$1,395,875~~ \$1,580,125. The court grants a discharge of most remaining debts after the plan has been carried out.

**Answer (B) is incorrect.** Any person who may go through a liquidation bankruptcy (except stockbrokers and commodity brokers) may file for a reorganization under Chapter 11. **Answer (C) is incorrect.** An individual may request relief under Chapter 11 or Chapter 13 to avoid a bankruptcy liquidation if the requirements of those sections are met. **Answer (D) is incorrect.** Chapter 13 is a voluntary provision, and a creditor of the debtor cannot file an involuntary petition under Chapter 13.

**Answer (B) is correct.** (CPA, adapted)

**REQUIRED:** The requirements under Chapter 11 for involuntary bankruptcy.

**DISCUSSION:** An involuntary bankruptcy proceeding can be commenced only under Chapter 7 and Chapter 11 against an eligible debtor. If the debtor has 12 or more different creditors, any three or more creditors who together hold unsecured claims of at least ~~\$18,600~~ \$21,050 can file an involuntary petition. If the debtor has fewer than 12 creditors, any one or more creditors who alone or together have unsecured claims of at least ~~\$18,600~~ \$21,050 can file an involuntary petition. Accordingly, Hall may file an involuntary petition in bankruptcy against Tree because she holds an unsecured claim of ~~\$19,000~~ \$22,000.

**Answer (A) is incorrect.** Hall has at least ~~\$18,600~~ \$21,050 in unsecured claims against Tree and can file the involuntary petition against Tree without the other creditors. **Answer (C) is incorrect.** Involuntary bankruptcy proceedings may be brought in Chapter 7 and Chapter 11 bankruptcy. **Answer (D) is incorrect.** Hall has at least ~~\$18,600~~ \$21,050 in unsecured claims against Tree and can file the involuntary petition even if she is the sole creditor.

## Page 326, Subunit 20.3, Question 4:

**20.3.4.** Assume that your client is in financial difficulty but does not want to go into bankruptcy. However, certain aggressive creditors are threatening to file an involuntary petition. Under the circumstances,

- A. It would be proper to attempt, in every way possible, to prepare financial statements indicating the client is not insolvent in the bankruptcy sense even though this means not following generally accepted accounting principles.
- B. Avoiding bankruptcy may be possible if your client and the creditors can agree to form a creditor's committee with the usual powers incidental to such an arrangement.
- C. Your client cannot be forced into bankruptcy, even though (s)he owes more than \$100,000 and a single creditor's claim is in excess of \$50,000.
- D. Your client can resist involuntary bankruptcy if a custodian has not taken control of his property.

**Answer (B) is correct.** (CPA, adapted)

**REQUIRED:** The true statement about a person threatened with involuntary bankruptcy.

**DISCUSSION:** One alternative to bankruptcy is to place the assets of the business in the hands of a committee of creditors with full power to manage the business of the debtor. The advantages of such an arrangement are that it (1) avoids the stigma of bankruptcy, (2) the attendant formalities and legal expenses, and (3) the losses incurred in a forced liquidation.

**Answer (A) is incorrect.** Preparing misleading financial statements is not only a violation of generally accepted accounting principles but also unethical and illegal. **Answer (C) is incorrect.** A debtor is subject to an involuntary petition for bankruptcy if the debtor has fewer than 12 creditors and a single creditor has unsecured claims of ~~\$48,600~~ 21,050 or more. If the debtor has 12 or more creditors, 3 creditors must have total unsecured claims of ~~\$48,600~~ 21,050 or more.

**Answer (D) is incorrect.** Not paying one's debts as they become due is sufficient to support a petition for involuntary bankruptcy.

## Study Unit 33 – Federal Securities Regulation

### Page 534, Outline:

**Registration** is required by the 1933 act for any offer or sale to the public unless a specific exemption applies. Thus, an issuer must prepare and file a registration statement and a prospectus under the SEC's integrated disclosure system. A **nonreporting issuer** (one who need not file reports under the 1934 act) must use detailed Form S-1. An **unseasoned issuer** is a reporting company under the 1934 act. It must use Form S-1 but provides less detailed information and may include some information by reference to other 1934 act reports. A **seasoned issuer** has timely filed for at least 1 year and has a market capitalization of at least \$75 million. It may use Form S-3 to report even less detail and may include even more information by reference. A **well-known seasoned issuer** has timely filed for at least 1 year and (1) has a worldwide market capitalization of at least \$700 million or (2) has issued for cash in a registered offering at least \$1 billion of debt or preferred stock in the past 3 years. Such an issuer also may use Form S-3. An **emerging growth company** (EGC) is an issuer with annual gross revenues less than \$1.235 billion, an amount periodically adjusted for inflation. An issuer remains an EGC until (1) its annual gross revenues exceed \$1.235 billion (adjusted), (2) 5 years after its initial public offering, (3) it has issued more than \$1 billion in nonconvertible debt in the last 3 years, or (4) it is a large accelerated filer.

The following update to Appendix A reflects the most recent editions of the cited textbooks and revises the Gleim cross-references accordingly. To view the current texts and cross-references without changes showing, go to [www.gleim.com/accounting/eqe/xref/?page=3](http://www.gleim.com/accounting/eqe/xref/?page=3).

## Appendix A – Subunit Cross-References to Business Law and Legal Studies Textbooks

### BUSINESS LAW TEXTBOOKS

Ashcroft, Ashcroft, and Patterson, *Law for Business*, Nineteenth Edition, Cengage Learning, 2017.

Bagley, *Managers and the Legal Environment: Strategies for Business*, Ninth Edition, Cengage Learning, 2019.

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Part I - Introduction to Law

Chapter 1 - Law and Legal Reasoning - SU 1

Chapter 2 - Dispute Settlement - SUs 2-3, SU 5

Chapter 3 - Business Ethics and Corporate Social Responsibility - SU 1

Chapter 4 - Business and the Constitution - SU 4

Chapter 5 - ~~Crimes~~ [Criminal Law and Procedure](#) - SU 6, 22.5

Chapter 6 - Intentional Torts - 7.1-7.3

Chapter 7 - Negligence and Strict Liability - 7.4-7.7

Chapter 8 - ~~Licensing and~~ Intellectual Property - 21.1-21.2, 22.3, 39.2

Part II - Contracts

Chapter 9 - The Nature and Origins of Contracts - 8.1

Chapter 10 - Creating a Contract: Offers - 8.2

Chapter 11 - Creating a Contract: Acceptances - 8.3

Chapter 12 - Consideration - SU 9

Chapter 13 - Capacity to Contract - 10.1

Chapter 14 - ~~Voluntary~~ Consent [to Contract](#) - 10.3

Chapter 15 - Illegality - 10.2

Chapter 16 - ~~The~~ Form and Meaning of Contracts - 10.4, 11.1

Chapter 17 - Third Parties' Contract Rights - SU 12

Chapter 18 - [Contract](#) Performance and Remedies - 11.2-11.4

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**Cheeseman, *Business Law, Eleventh* ~~Twelfth~~ Edition, Pearson, 2021**~~2025~~.

Part I - Legal Environment, of Business and Online Commerce [Judicial System, Dispute Resolution, and Constitutional Law](#)

- Chapter 1 - Legal Heritage and the Digital Age - SU 1
- Chapter 2 - Courts and Jurisdiction - SU 2
- Chapter 3 - Judicial, Alternative, and E-Dispute Resolution - SU 3
- Chapter 4 - Constitutional Law for Business and E-Commerce - SU 4

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Part VIII - Business Organizations, ~~Corporate Governance,~~ [Partnerships, Corporations, Limited Liability Companies,](#)  
Investor Protection, and Business Ethics

- Chapter 34 - Entrepreneurship, Sole Proprietorships, and General Partnerships - 30.1-30.4
- Chapter 35 - Limited Partnerships and Special Partnerships - 30.5
- Chapter 36 - Limited Liability Companies and Limited Liability Partnerships - 30.6
- Chapter 37 - Corporate Formation and Financing - 31.1-31.3
- Chapter 38 - Corporate Governance and the Sarbanes-Oxley Act - 32.1-32.3
- Chapter 39 - Corporate Acquisitions and Multinational Corporations - 32.4
- Chapter 40 - Franchises and Special Forms of Business - 30.6
- Chapter 41 - Securities Law and Investor Protection - SU 33
- Chapter 42 - Ethics and Social Responsibility of Business - 1.1

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Part XI - [The Accounting Profession](#)

- Chapter 51 - Accountants' Duties and Liability - SU 40

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Unit IV - The Business and Employment Environment

- Chapter 16 - Small Business and Franchises - SU 30
- Chapter 17 - Limited Liability Business Forms - 30.5-30.6
- Chapter 18 - ~~Corporations~~ [Corporate Formation and Financing](#) - SUs 31-32
- Chapter 19 - Agency Relationships - SU 29
- Chapter 20 - Employment Law - 38.3-38.6
- Chapter 21 - Employment Discrimination - 38.2
- Chapter 22 - Immigration and Labor Law - 38.1

Unit V - The Regulatory Environment

- Chapter 23 - Administrative Agencies - SU 5
- Chapter 24 - Consumer Protection - SU 37
- Chapter 25 - Environmental Law - SU 35
- Chapter 26 - Real Property and Land Use Control - SUs 23-24
- Chapter 27 - Antitrust Law - SU 36, 39.2
- Chapter 28 - Investor Protection, [Insider Trading](#), and Corporate Governance - SUs 32-33

**Davidson, and Forsythe, and Curry, *Business in the Contemporary Legal Environment, Third* ~~Fourth~~ Edition, Aspen Publishers, 2024**~~2024~~.

Part I - Foundations of the Law [and the U.S. Legal System](#)

- Chapter 1 - Business and its Legal Environment - SU 1
- Chapter 2 - Business Ethics - 1.1, 40.1
- Chapter 3 - The U.S. Legal System and Court Jurisdiction - SUs 1-2
- Chapter 4 - Dispute Resolution - 3.6
- Chapter 5 - International Considerations for Contemporary Businesses - SU 39

Part II - Governmental Influences

- Chapter 6 - Constitutional Regulation of Business - SU 4
- Chapter 7 - Administrative Regulation - SU 5
- Chapter 8 - Protection of Intellectual Property - 21.1, SU 22

Part III - Contracts

Chapter 9 - Contract Formations - 8.2-8.3, SU 9

Chapter 10 - Contracts: Performance and Remedies - 11.3-11.4

Chapter 11 - ~~Contracts for~~ [Contract Writings, Interpretations, Third Parties, and](#) the Sale of Goods [Under the UCC](#) – ~~SU 13.1-13.3~~

Part IV - Torts and Crimes

Chapter 12 - Torts - SU 7

Chapter 13 - Crimes and Business - SU 6, 22.5

Part V - Agency and Business Organizations

Chapter 14 - Agency - SU 29

Chapter 15 - Business Organizations - SUs 30-32

Chapter 16 - Securities Regulation - SU 33

Part VI - The Regulatory Environment

Chapter 17 - Strategic Alliances and Antitrust Law - SU 36, 39.2

Chapter 18 - Consumer Protection - SU 37

Chapter 19 - Environmental Protection and Sustainability – SU 35

Chapter 20 - Labor and Fair Employment Practices - SU 38

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Part IX - Property Protection

Chapter 39 - Real Property and Joint Ownership - SUs 23-25

Chapter 40 - [Protection of](#) Intellectual Property - SU 22

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Part 9 - Partnerships

Chapter 37 - Introduction to Forms of Business and Formation of Partnerships - 30.1

Chapter 38 - Operations of Partnerships and Related Forms - 30.2-30.3

Chapter 39 - Partners' Dissociation and Partnerships' Dissolution and Winding Up - 30.4

Chapter 40 - Limited Liability Companies, [and](#) Limited Partnerships, ~~and Limited Liability Limited Partnerships~~ - 30.5- 30.6

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