

# PROACTIVE LEGAL CONSIDERATIONS

for small businesses

## CO-SPONSORED BY:



## FACILITATOR:

JoAnn Schmitz  
Schmitz Law Firm, LLC

## PRESENTED BY:



719-667-3803  
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## ***About the facilitator...***

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### **JoAnn Schmitz, Esq Schmitz Law Firm, LLC**



JoAnn Schmitz, Esq., tapped her entrepreneurial spirit and founded Schmitz Law Firm, LLC in 2002. She has a wide range of experience representing entities, individuals and non-profit corporations in lawsuits and transactional matters involving business formation, ownership agreements, leases, contracting, licensing of intellectual property, copyright and trade mark filings, business divorce, real estate disputes and other civil matters. She was previously elected to the Peak Venture Group and Colorado Springs Children's Chorale board of directors and is currently serving on the SBDC Advisory and the Colorado Institute for Social Impact Boards. She earned her JD from the University of Denver College of Law in the evenings while consulting as a strategic advisor with Digital, Compaq and HP computer companies during the day in decisions involving product management and marketing, end of life planning, operations, strategic planning, technology merger and executive speech writing.

Recently, JoAnn has begun investigating the intricacies of corporate formation in the context of social impact, reviewing Colorado and Delaware's Public Benefit Corporation Acts and particularly studying the Chan Zuckerberg formation decision to incorporate as a limited liability company versus a 501(c)(3) non-profit for their \$36B contribution to advance social initiatives. Along with Jeff Zearfoss, she presented the initial social impact training module in November 2017 addressing entity formation on behalf of the then Colorado Coalition for Social Impact.

JoAnn has also been tapped to lead the Ben S. Wendelken Inn of Court Inner Temple pupillage. Last May, the Inner Temple presented an eye-opening program entitled "Unintended Consequences of Implicit Bias" to the members comprised of local judges and lawyers. This year's Inner Temple January program is examining the legal and moral questions presented by the actions of Edward Snowden, a United States intelligence operative who has made numerous classified documents public showing the extent and depth of US surveillance on the American public as well as international figures.

In her spare time, JoAnn enjoys her family, music, playing and accompanying on the piano, mandolin, violin and ukulele, throwing parties, reading (currently reading Conscious Capitalism) and studying art. She is currently serving as an Elder and children's choir accompanist at her local church.

JoAnn is an attorney duly admitted since May 14, 2002 to practice before the courts of the State of Colorado, along with the United States Bankruptcy Court, the United States District Court for the District of Colorado, and the Supreme Court of the United States.

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**PROACTIVE LEGAL ACTIONS FOR SMALL BUSINESS**

JoAnn Schmitz, Esq.  
April 25, 2018  
Pikes Peak SBDC

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## DISCLAIMER



The purpose of this presentation is for education only and is not intended to be legal advice.

It should not be interpreted as legal advice specific to you and or your business.

If you have legal questions, you should consult your legal advisor for advice specific to the facts of your question.

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## PURPOSE OF TODAY'S PRESENTATION



This presentation is focused on actions you may want to consider taking to:

- (1) protect yourself from **PERSONAL LIABILITY EXPOSURE** emanating from your business activities; and
- (2) actions you may want to take as a business owner to **MAXIMIZE THE VALUE** of your business and **REDUCE LIABILITY RISK** to the entity.

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## AGENDA



- Insights
- Care and Keeping of You
- Your Corporate Book
  - Formation, ownership, meeting minutes, financial info and tax filings, external reports, IP, contracts, employees, certifications and awards
- Additional ways to maximizing revenue
- Questions?

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## INSIGHT



- Sad story number 1 – SW Engineer
- Sad story number 2 – 35+ Years
- Sad story number 3 – YOU?

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## INTRODUCTION The Care and Keeping of You



- What is the purpose for forming an entity?
- Does it make a difference which entity type you would select for your business?
- When to form your business or formalize a partnership?
  - Have met several times
  - Product and service development ownership
  - Contracts
  - Happy phase
  - Before raising money

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## INTRODUCTION The Care and Keeping of You



- A word about Colorado partnership law
- “The association of two or more persons to carry on as co-owners a business for profit forms a partnership whether or not the persons intend to form a partnership.”
- When property becomes partnership property
  - Partnership liable for partner’s actionable conduct
  - Partner’s liability – jointly and severally
  - CRS 7-64-202, 204, 305 and 306

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## INTRODUCTION

### The Care and Keeping of You



- How do you maintain the liability transfer?
  - Corporate formalities
  - Separate bank account
  - No comingling of funds
  - Maintain fiduciary duties
- Impact of personal actions
  - Action outside the scope of business
  - Maybe statutorily specific

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## INTRODUCTION

### The Care and Keeping of You



- Be wary of personal guaranties requiring you to be responsible for business debt
  - Lease
  - Business loans
  - Franchise agreements

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## MAXIMIZING BUSINESS VALUE

### Your Corporate Book



#### CORPORATE BOOK CHAPTERS

1. Formation documents, amendments, annual reports
2. Ownership records and agreements
3. BOD/Manager annual & interim meeting minutes
4. Year end financials and tax filings
5. Licensing
6. External reports, Statutorily required reports
7. Intellectual property documentation
8. Contracts
9. Employee agreements
10. Business Insurance
11. Certifications
12. Awards

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# MAXIMIZING BUSINESS VALUE

## Chapter 1 – Formation Docs, Amendments & Annual Report



Formalize your business

- Register your entity with the Colorado Secretary of State's Office (COSOS)
  - Articles of Organization or Incorporation
- Finish Operating Agreement or Bylaws
- Draft and file with COSOS and internally any Amendments if appropriate
- File COSOS Annual Reports

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# MAXIMIZING BUSINESS VALUE

## Chapter 1 – Formation Docs, Amendments & Annual Report



Formalize your business - 2

- Operating Agreement
  - Sweat equity – the amount of cash and a description of the agreed to value of other property or services to be contributed
  - When additional contributions may be required
  - When distributions are made
  - Who can bind the company
  - Spending limits without further authorization
  - Events of dissolution
  - Electronic meeting participation

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# MAXIMIZING BUSINESS VALUE

## Chapter 1 – Formation Docs, Amendments & Annual Report



Formalize your business

- Apply for Employer Identification Number (EIN)
- Apply for any business specific required licensing and sales tax
- Complete S-corp filing with IRS
- Conduct annual meetings
- Trade name filings (dba)
- Foreign jurisdictions

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# MAXIMIZING BUSINESS VALUE

## Chapter 1 – Formation Docs, Amendments & Annual Report



- Legitimize your business - Professionals
- Bookkeeper
  - CPA and tax preparer
  - Attorney – business and employment law
  - Capital advisor
  - Mentor(s)
  - May want to establish an advisory board

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# MAXIMIZING BUSINESS VALUE

## Chapter 2 – Ownership Docs



- Document and track entity's ownership
- Current list of full name and last known address of each owner and manager
  - For corporations – stock ledger
    - Track dates of any transfer of ownership interest
    - Identify any stock sale limitations on the actual shares (ex. S-corp limitations, social impact profit diversion)
  - For LLCs – membership units
    - Track dates of any transfer of ownership interest
    - Identify any ownership limitations on unit certificate (ex. social impact profit diversion)

Be sure to faithfully update records when ownership changes.

Check for any statutorily required record keeping.

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# MAXIMIZING BUSINESS VALUE

## Chapter 2 – Ownership Docs



- Shareholder/Member Agreements - 1
- Sale of ownership upon triggering event
  - Termination of employment, death, disability, retirement, divorce, seizure by creditors, bankruptcy, 3<sup>rd</sup> party offer to purchase, change of control, dispute between owners, S-corp share transfer to ineligible holder, initial public offering (IPO), merger, acquisition

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## MAXIMIZING BUSINESS VALUE Chapter 2 – Ownership Docs



### Shareholder/Member Agreements - 2

- Address Voluntary Triggering Event through
  - A right of first refusal
  - A right of second refusal
  - A right of first offer
  - Co-sale or tag-along rights (3<sup>rd</sup> party sale)
  - Drag-along rights (3<sup>rd</sup> party sale with specific ownership percentage)

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## MAXIMIZING BUSINESS VALUE Chapter 2 – Ownership Docs



### Shareholder/Member Agreements - 3

- Address disputes between owners
- The 50/50 deadlock issue
  - Shotgun – buyout of opposite party
  - Texas shoot out – sealed bid, umpire decides most favorable bid
  - Dutch auction – higher of minimum bids
  - Informal discussions, mediation, arbitration and litigation

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## MAXIMIZING BUSINESS VALUE Chapter 2 – Ownership Docs



### Shareholder/Member Agreements - 4

- Decide valuation method in advance
  - Annual revaluation
  - Book value
  - Multiple of revenues, earnings or EBITDA
  - Advice of particular valuation expert
  - Minority or lack of liquidity discounts
- Payment terms

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## MAXIMIZING BUSINESS VALUE Chapter 2 – Ownership Docs



### Shareholder/Member Agreements - 5

- Shareholder/Member Agreements are worth every penny when negotiated between founders upfront during the happy stage
- Extremely difficult and costly if terms are not negotiated in advance
- LEAVES MORE VALUE to distribute versus paying professionals to sort it out

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## MAXIMIZING BUSINESS VALUE Chapter 3 – Meeting Minutes



### BOD/Managers/Member Manager Annual and Regular Meeting Minutes - 1

- Draft and file regularly in Corporate Book
- Memorialize management's decisions
  - Bank account authorization, entity name, trade name, contract or real property decisions, delegation of authority, managers and their roles, distributions of profits/losses, capital contributions, admission of new and withdrawal of existing members, approval of salaries, indemnification considerations, loans to insiders, tax considerations
- Should cover all major management and policy decisions
- Imperative when mood or memory may change between managers and or owners

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## MAXIMIZING BUSINESS VALUE Chapter 3 – Meeting Minutes



### BOD/Manages/Member Manager Annual and Regular Meeting Minutes - 2

Minutes should include:

- Date, time place
- Who was present, who called
- Whether decision needed member or manager vote
- Approval of previous meeting minutes
- Election of managers/directors and period elected for
- Document any resolutions that were approved
- Signed and dated by secretary

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## MAXIMIZING BUSINESS VALUE Chapter 4 – Financial and Tax Info



File annual and complete financial statements

- Profit and Loss
- Income statement
- Balance Sheet

File annual state and federal tax returns

- Consult CPA on length of time to keep tax returns and supporting records/receipts

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## MAXIMIZING BUSINESS VALUE Chapter 5 – Licensing



Copies of any licenses obtained

- State and Local Sales Tax License
- Restaurant and Liquor License

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## MAXIMIZING BUSINESS VALUE Chapter 6 – External Reports



File any external reports

- Benefit corporation reports
- Social impact reporting
- Green reporting

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Non-Disclosure Agreements (NDA) - 1

- Used anytime you are discussing corporate business with a person or entity external to the business
  - Potential partners or owners
  - Merger or acquisition
  - Investors (VCs will probably not sign)
  - Joint programs
  - Vendors

**NO NEED TO SHARE ALL INFORMATION,  
CURB YOUR ENTHUSIASM!**

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Non-Disclosure Agreements (NDA) - 2

- Keep a file of all NDAs
  - Topic of discussion
  - Any slides that were presented
  - Date, time and location of discussion
  - Who was present
  - Signatures from all attendees
- One-way versus mutual NDAs

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade Secrets – EXTREMELY VALUABLE! - 1

- Protect the company's private, not publically known information
- Inventions, product plans, technical specifications, strategies, costs, prices, names, finances, marketing plans, business opportunities, personnel, research and development information, KNOW-HOW, customer lists, tangible or intangible
- Derives INDEPENDENT ECONOMICAL VALUE, ACTUAL OR POTENTIAL
- INEXPENSIVE TO DO; LASTS AS LONG AS IT IS KEPT A SECRET – Think Coca Cola Recipe

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade Secrets – EXTREMELY VALUABLE! - 2

- Protection mechanisms
  - Identify all trade secrets
  - Mark ALL documents containing trade secrets CONFIDENTIAL
  - Educate staff on the difference between CONFIDENTIAL and non-confidential
  - Never post trade secrets in a public domain
  - Implement guidelines to keep them secret
  - Have staff sign off that they read and will adhere to guidelines
  - Include a confidentiality provision in every Independent Contractor and or Consultant Agreement requiring them and any of their employees to keep trade secrets confidential
  - Use NDAS
  - DO NOT SHARE UNLESS ABSOLUTELY NECESSARY
  - LIMIT STAFF ACCESS WHERE POSSIBLE

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Copyrights – Inexpensive Insurance - 1

- Duration – generally author's life + 70 years
- Prevents others from copying, preparing derivative works, distributing, performing or publically displaying your works
- An (1) original (2) work of art that is (3) fixed in a tangible medium (4) of expression
- Protection for text, audio and visual content, articles, literary, pictorial, graphic works, and but not limited to websites
- Does not protect an idea, procedure or discovery
- Ex. © 2018 Schmitz Law Firm, LLC

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Copyrights – Additional tips – 2

- Be careful to maintain entity's ownership
- Generally, it is owned by the authors who created the work, and those deriving rights through the authors
- Owned until made publically available, ownership rights are transferred via assignment or licensing or duration of copyright expires

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Copyrights – Ownership Matters - 3

- Works Made for Hire
  - Authored by an employee and owned by employer if prepared within the scope of employee's employment
  - Should be articulated in contracts with outside advertising agencies, graphic designers, independent contractors and consultants
  - Can also include a copyright assignment in case there is any dispute over ownership

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Copyrights – Ownership Matters - 4

- Joint Ownership
  - Prepared by two or more authors with the intention that the contributions be merged into inseparable or interdependent parts of a unitary whole at the time the respective contributions were made
  - Rats nest of co-owners, can independently transfer their ownership rights w/o others consent, etc.

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Copyrights – Valuable Statutory Damages - 5

- Register with US Copyright Office
- Registration form fairly simple to complete
- Costs \$55-65 per registration
- Registration provides statutory damages in the case of infringement

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade or Service Marks - 1

- Used to distinguish your goods or services from another's
- A word, name, symbol, device or any combination used by a merchant to identify its goods and services from those manufactured by others
- Generally mark names associated with products, programs or services

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade or Service Marks - 2

- Prior to any state or federal application, use the common law trademark symbol of <sup>TM</sup> for products and <sup>SM</sup> for service products
- Also use the common descriptive name of the product after the mark. Ex. Band-Aid® brand adhesive bandages (showing federally registered trade mark symbol for Band-Aid®)
- Never use as verb, possessive, noun or plural forms. Ex. Xerox this.
- Use or loose -> escalator, kerosene, shredded wheat, aspirin

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade or Service Marks - 3

- Creating a strong mark
  - Fanciful – Exxon or Xerox
  - Arbitrary – Ivory soap, PBS Nova
  - Suggestive – some quality or ingredient
  - Descriptive – intended purpose, requires a secondary meaning
  - Generic – not trade markable

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade or Service Marks - 4

- Generally more expensive than trade secret and copyright protections
- File federal mark with USPTO
- Need interstate commerce for federal mark
- Need to conduct a search confirming availability of mark, including USPTO TESS
- Federal registration requires identification of classes specific to the goods and or services

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade or Service Marks - 5

- Duration – 10 years of continued protection with affidavit of use filed between the 5<sup>th</sup> and 6<sup>th</sup> years of registration
- OK to file with state registration for notice of first use purposes
- Can assign or license trade mark's use

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Trade Names

- Trade names are alternate names for your entity that you may use
- Register with the state the entity is located in so that the entity can be identified
- Generally known as a "dba"

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## MAXIMIZING BUSINESS VALUE Chapter 7 – Intellectual Property



### Patents

- Strongest level of protection for some products
- Expensive, national and international levels
- Definitely talk with a patent attorney if you believe some part of your product or service is patentable
- The entity will need to be prepared to defend the patent if infringed upon

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## MAXIMIZING BUSINESS VALUE Chapter 8 - Contracts



Some of the many, many types of contracts

- Vendor and supplier contracts
- Customer agreements
- Employee agreements
- Real Property leases
- Shareholder/Member agreements
- Operating agreement and bylaws
- Independent contractor agreements
  - Don't forget IP protection
- Purchase orders/agreements
- Joint Venture Agreements (remember partnership law discussed earlier?)
- Website terms of use

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## MAXIMIZING BUSINESS VALUE Chapter 7 - Contracts



### Contract basics – 8

It is imperative to have as many of your entity's agreements committed to writing as possible to maximize corporate value.

- Its good to get paid, consider milestone payments
- To know what the entity is committed to and when for product delivery
- To know what price the entity is purchasing materials at, etc.

Memorialize in writing before memory and mood fade and misinterpretation arises.

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## MAXIMIZING BUSINESS VALUE Chapter 8 - Contracts



### Contract basics – 3

- Know who you are contracting with
- Confirm the terms of the contract
- Consistency in basic contractual terms
- Develop the entity's own set of standard terms and conditions that can be leveraged across multiple contracts
- Consistency in dispute resolution

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## MAXIMIZING BUSINESS VALUE Chapter 8 – Contracts - Boilerplate



- |   |   |
|---|---|
| 1. Parties                                | 14. Dispute Resolution                    |
| 2. Subject of the Agreement               | 15. Choice of law and jurisdiction        |
| 3. Definitions                            | 16. Survival of certain provisions        |
| 4. Term                                   | 17. Breach and right of cure              |
| 5. Compensation or Consideration          | 18. Lawyer's fees and costs               |
| 6. Relationship of the parties            | 19. Notices                               |
| 7. Termination; the effect of termination | 20. Entire agreement; manner of amendment |
| 8. Confidentiality                        | 21. Severability                          |
| 9. Intellectual property                  | 22. Waiver                                |
| 10. Title and risk of loss                | 23. Force majeure                         |
| 11. Limitations on liability              | 24. Further assurances                    |
| 12. Limitations on warranty               | 25. Authority                             |
| 13. Indemnification                       | 26. Counterparts                          |

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## MAXIMIZING BUSINESS VALUE Chapter 8 – Contracts - Standard Terms and Conditions of Sale



- |   |   |
|---|---|
| 1. PRICES                                 | 11. LIMITATION OF LIABILITY   |
| 2. TERMS OF PAYMENT                       | 12. SUBSTITUTIONS AND MODIFICATIONS                                     |
| 3. DELIVERY AND TITLE                     | 13. PROPRIETARY RIGHTS  |
| 4. SHIPMENTS                              | 14. NOTICES   |
| 5. ACCEPTANCE                             | 15. IMPORT AND EXPORT REQUIREMENTS                                      |
| 6. DEFAULT, CANCELLATION and RESCHEDULING | 16. APPLICABLE LAW, JURY WAIVER, JURISDICTION AND LIMITATION OF ACTIONS |
| 7. SECURITY INTEREST                      | 17. ATTORNEY'S FEES/COSTS   |
| 8. LIMITED WARRANTY, Returns policies     | 18. ASSIGNMENT  |
| 9. EXPRESS WARRANTY                       | 19. US GOVERNMENT CONTRACTS CONFIDENTIALITY                             |
| 10. INDEMNITY                             | 20. ERRORS AND VALIDITY OF AGREEMENT                                    |
| a) Customer Indemnity                     | 21. ENTIRE AGREEMENT  |
| b) Company Indemnity                      |   |

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# MAXIMIZING BUSINESS VALUE

## Chapter 8 – Contracts – Member or Shareholder Agreements



1. Cancellation of previous agreement
2. Restrictions against transfer
3. Permitted transfers
4. Voluntary sales
5. Purchase of shares upon termination of employment
6. Involuntary transfer
7. Sales of shares upon permanent disability
8. Sale of shares upon death
9. Determination of agreement price
10. Payment of agreement price
11. Unrestricted shares of deceased or disabled shareholder
12. Legends on stock or member certificates
13. New stockholders
14. Termination of the agreement
15. Miscellaneous provisions

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# MAXIMIZING BUSINESS VALUE

## Chapter 8 – Contracts – Member or Shareholder Agreements



Do not forget to have an attachment for spousal consent to the Member or Shareholder Agreement.

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# MAXIMIZING BUSINESS VALUE

## Chapter 9 – Employee Agreements



- Independent Contractor vs. Employee
- Law is somewhat vague on this issue
  - General criteria
    - The right to control the activities of the person
    - Who supplies the tools?
    - Who supplies the place where work will be done?
    - What costs are borne by the worker
    - What are the worker's managerial skills
    - Length of the relationship
    - Ancillary or routine to your business
    - How is payment structured? (Fixed pay versus pay for the job at completion)
    - Do fringe benefits apply to the person?
    - How do the parties treat the transaction?
    - What is customary for the trade or industry?

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## MAXIMIZING BUSINESS VALUE

### Chapter 9 – Employee Agreements



Common (read Expensive) Hiring Mistakes

- Hiring full time employee before determining the actual type of help needed
  - PT, seasonal or temporary employees, consultant(s), outsourcing, expanding responsibilities of current staff
- Failing to complete sufficient diligence on the applicant before making an offer
  - Conduct adequate interviews, check references, and other basic hiring activities
- Make hiring decisions consistent with the strategic plan identifying critical resources

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## MAXIMIZING BUSINESS VALUE

### Chapter 9 – Employee Agreements



Now That You have an Employee

- Must withhold federal income tax and social security tax from taxable wages
- Must file a quarterly federal tax return
- Any person charged with the withholding of taxes may become personally liable for a 100% penalty if they fail to pay or file the proper forms
- Must withhold state income tax
- Must pay unemployment taxes
- Need worker's compensation insurance

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## MAXIMIZING BUSINESS VALUE

### Chapter 9 – Employee Agreements



Employment agreements

- Identify the employee's wage, term of employment, and benefits information
- Typically includes
  - A confidentiality agreement
  - An assignment of rights provision
  - Non-solicitation of other employees provision
  - Non-complete provision
- May also consider a separate proprietary information and inventions agreement
- **Severance**, vesting acceleration upon termination in the case of senior management with significant negotiation leverage
- State law specific – definitely seek counsel from a knowledgeable source

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## MAXIMIZING BUSINESS VALUE Chapter 10 - Insurance



Get it

- General Business Liability and Asset Protection
- Professional Insurance
- Workers Compensatino

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## MAXIMIZING BUSINESS VALUE Chapter 11 - Certifications



File all certifications the entity achieves:

- Green certification
- BBB Accredited Business certification
- Minority or Woman-Owned business classification
- Social impact certifications

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## MAXIMIZING BUSINESS VALUE Chapter 12 - Awards



Demonstrate your brand strength and market presence.

File all awards, press releases and media articles relating to the business

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## MAXIMIZING BUSINESS VALUE Miscellaneous



- A business that can run on its own, without you there for every decision, is the most valuable.
- Consider and work on your exit plan from the very beginning.
- Have a business continuation plan in the event you become disabled, ill or just want to take a vacation at some point.
- Make sure you and your significant other are on the same page with respect to the entity in your estate plans.

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## MAXIMIZING BUSINESS VALUE In Review



Take care to keep the corporate shield in place to protect your personal assets from the entity's assets if needed.

Fill your corporate binder with the entity's information supporting these 12 chapters.

Add your own corporate book chapters if needed.

Avoid the costly expense and time required to "clean up" your entity when you are ready to exit.

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## MAXIMIZING BUSINESS VALUE Questions?



Contact the Pikes Peak Small Business Development Center to schedule an appointment with a counselor to review your next step(s).

**THANK YOU!**  
And Best of Luck to you!

April 25, 2018

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**Pikes Peak Small Business Development Center**

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