Housekeeping

- Dumb questions exist
  - They are those that remain burning in your brain but unasked
  - To have at your disposal a lawyer who bills $275/hour and not ask questions is dumb
  - Interrupt with questions, comments, etc.
- Break times
  - This is a two- or three-hour presentation, and it is heavy-duty material; we’ll take a 10-minute break after about an hour
  - If required, feel free to leave and come back during the discussion
- I will be here after the class to answer any further questions

Nancy Baum Delain

- Intellectual Property & Business Law practice
  - JD from Franklin Pierce Law Center, Concord, NH, 2003
  - Registered Patent Attorney
- 20+ years’ experience in computer industry as a technical documentation specialist (writer/editor/manager)
  - MS from RPI in Technical Writing, 1981
- 2 years’ experience in a virology research lab at Rockefeller University, a think tank in NYC with a faculty containing several Nobel laureates
  - AB from Smith College in Biological Sciences (Zoology and Cell/Molecular Biology), 1978
Order of Presentation
- Formation and Startup Considerations
- Contracts
- Intellectual Property

Business Formation in New York
- New York recognizes four separate types of business entities
  - Sole proprietorship
  - Partnership
  - LLC/LLP
  - Corporation

Sole Proprietorship
- What is it?
  - A single-owner business entity certified by the county to do business in that county
  - Commonly called a DBA because the certificate issued by the county is a license to “Do Business As” an assumed business name (which may, in fact, be the owner’s name)
- How long does it last?
  - Until the owner stops “Doing Business As” in the county of registration, OR
  - Until the owner files a certificate with the County Clerk dissolving the DBA
- How is it taxed?
  - Form 1040, Schedule C
Sole Proprietorship

- Advantages
  - Easiest of all the business forms to set up
    - Register a DBA certificate with the county clerk of the county where the business will operate
    - Pay nominal fee to the county clerk’s office
    - Obtain Employer ID number (EIN) from the IRS
    - If you sell goods or services for which you are required to collect sales tax, obtain a sales tax number from the NY Dept. of Taxation and Finance

- Advantages (continued)
  - Has the fewest formal requirements
    - No seals, no meetings
  - You are the BOSS
    - Very little state oversight leaves you free to operate your business as you see fit
  - Income is reported as personal income and is reported on Schedule C to the IRS

- Disadvantages
  - No protection of owner’s personal assets
    - Total exposure for owner in the event of a catastrophic event such as a lost lawsuit
    - ALL of owner’s assets are at risk
    - “Easily made, easily broken” business
  - Lack of credibility
    - More difficult to raise funds
    - More difficult to attract good customers
    - More difficult to get proper insurance for some types of businesses that elect to be sole proprietorships
Sole Proprietorship

**Disadvantages**
- Registration of the name at only the county level leaves business name up for grabs to anyone who registers a business at the state level
  - DBA is legally valid only in the county in which the DBA is registered
- This causes confusion in the marketplace
  - Expect a trademark infringement lawsuit
  - Hard to win this suit, since the DBA owner did not act properly to protect the name of the business

**Business types for which sole proprietorship can best work**
- Small MLM franchises
- Amway, MaryKay, Herbalife, etc.
- Freelance writers, artists, videographers, musicians, craftsmen
- Businesses with few, if any, walk-in customers
- Businesses with no employees other than the owner/owner’s family
- Businesses that are geographically restricted to one county
- Businesses in which the owner’s DBA is the owner’s own name

**Business types that should stay away from sole proprietorship**
- Professional offices (doctors, lawyers, dentists, architects, real estate brokers, etc.)
- Businesses with walk-in customers
- Businesses that transport people and/or goods
Partnership

- Comes in two flavors:
  - General Partnership
  - Limited Partnership

General Partnership

- What is it?
  - A multiple-owner business entity that may be certified by the county or by the state
    - Certification is NOT needed to form a valid general partnership
  - All partners in a general partnership participate to some degree in the management of the business of the partnership
- How long does it last?
  - Until the partners stop doing business as partners, OR
  - Until the partners file a certificate dissolving the partnership AND present to the public that they are no longer doing business as partners
- How is it taxed?
  - Partnership tax forms, with each partner reporting gains and losses commensurate with that partner’s financial contribution to the partnership

General Partnership

- Advantages
  - Very easy to form
    - Present to the public as a partnership
    - No EIN needed for a partnership to be formed
      - If the partnership plans to do business with the public as a partnership, an EIN is needed
  - No formalities required to maintain partnership status
    - Just keep presenting to the public as a partnership
    - Easy access to partners’ expertise within the partnership
**General Partnership**

- **Disadvantage**
  - Every partner in a general partnership is *personally liable for the debts of every other partner* in the general partnership, regardless of whether those debts are related to the business of the partnership.
  - An example of the workings of partnership law:
    - If your partner in a general partnership files for personal bankruptcy protection, his creditors can come after all of his partners for satisfaction of the debts.

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**Limited Partnership**

- **What is it?**
  - A multiple-owner business entity that may be certified by the county or by the state.
  - No limited partner in a partnership may participate at all in any of the management of the business of the partnership.

- **How long does it last?**
  - Until the partners stop doing business as partners, OR
  - Until the partners file a certificate dissolving the partnership.

- **How is it taxed?**
  - Partnership tax forms, with each partner reporting gains and losses commensurate with that partner’s financial contribution to the partnership.

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**Limited Partnership**

- **Advantages**
  - Those of partnership
  - No personal liability of the limited partners for the liabilities of other partners.
Limited Partnership

- Disadvantages
  - No control by the limited partner over the management or operation of the business of the partnership, regardless of financial or other contribution to the partnership
  - “Silent partner” status
  - General partnership is presumed for all partners until limited partnership is proved
  - Partnership requires at least one general partner to conduct business

Partnership

- What businesses can use partnership as an effective business form?
  - Formerly, partnerships were often formed between professional people such as doctors, lawyers, architects, dentists, etc.
  - Now, partnership is generally used when corporations wish to form strategic alliances
    - Draconian partnership provisions do not generally have as much impact on a large corporation as they do on individuals
    - Insurance can help cover partnership liability between companies, but it generally will not do so between individuals

- Businesses that should avoid general partnership
  - Sole proprietors
  - Any business wishing to avoid liability for partners’ financial decisions
Limited Liability Entities

- Come in two varieties:
  - Limited Liability Company (LLC)
    - Can have only one member or many members
  - Limited Liability Partnership (LLP)
    - Must have more than one member
    - Only available to certain professions
      - Doctor, Lawyer, Dentist, Chiropractor, Engineer, etc., as listed in the Education Law of New York State

Limited Liability Company (LLC)

- What is it?
  - An unincorporated business entity that provides the members with the protection of the "corporate veil"
  - Has its own legal existence, separate from that of its members

- How long does it last?
  - Until it is dissolved, either by the members, by the State, or by the courts

- How is it taxed?
  - Single member LLC may be taxed either as a pass-through entity or as a business entity by the federal government
  - Multiple member LLC is taxed as a business entity (generally as a partnership) by the federal government

Limited Liability Company (LLC)

- Formation formalities
  - File Articles of Organization+filming fee
  - Publish in two newspapers designated by the County Clerk of the county in which the LLC plans to have its main offices once per week for six consecutive weeks
  - File Affidavits of Publication+filming fee
  - Optional but HIGHLY recommended:
    - All members should sign Operating Agreement - within 90 days of formation

- Maintenance formalities
  - Franchise tax payable to NYS within 30 days of the end of the LLC’s fiscal year
  - Annual meeting of members
Limited Liability Company (LLC)

- Advantages
  - Less structured than a corporation
  - Provides the “corporate veil” to protect owners’ personal assets
  - None of the partnership responsibilities toward creditors of members

- Disadvantages
  - Very new business form
    - NYS LLC law was enacted in 1994
    - NYS corporation law was enacted when NYS became a state
  - No one quite knows for sure how it will behave in court
    - It currently behaves like a corporation, but it has enough elements of partnership in it that it could turn on the whim of a judge…
  - Treatment across state lines can vary wildly

Limited Liability Partnership (LLP)

- What is it?
  - Similar to an LLC, an LLP is an unincorporated business entity that provides protection via the “corporate veil” to the partners
  - Has its own existence separate from that of its owner
  - Only available to certain professions
- How long does it last?
  - Until it is dissolved by the members, or by the State or by the courts
- How is it taxed?
  - Generally taxed as a partnership
**Limited Liability Partnership (LLP)**

- **Formation formalities**
  - Same as those for LLCs
- **Maintenance formalities**
  - Same as those for LLCs

**Limited Liability Partnership (LLP)**

- **Advantages**
  - LLP partners can have management control of the partnership without incurring the liabilities of general partnership

**Limited Liability Partnership (LLP)**

- **Disadvantages**
  - Like LLCs, LLPs are fairly new legal entities so no one is quite sure how they work just yet
  - Treatment across state lines can vary wildly
Corporations

- Come in two types:
  - C-corporations
  - S-corporations

Corporations

- Formation formalities
  - File Articles of Formation with the Secretary of State and pay the filing fee
  - Hold and document initial meetings
  - Optional but HIGHLY recommended:
    - Sign Shareholders’ Agreement
- Maintenance formalities
  - Hold and document annual BOD and shareholder meetings
  - Pay taxes

C-Corporation

- What is it?
  - An incorporated entity
    - The entity is separate from its owner(s), having its own legal existence
- How long does it last?
  - Until it is dissolved by its shareholders, by the State or by the courts
- How is it taxed?
  - As a separate entity, it is responsible for income taxes based on the revenues it receives
  - If the corporation holds property, it is responsible for property taxes in most cases
C-Corporation

**Advantages**
- Well established legal entity, well recognized by the law and the courts
- Consistent treatment in different states
- With proper procedures, you can take a C-corp public
  - Unlimited number of shareholders
  - Unlimited as to what types of entities can hold shares

**Disadvantages**
- Double taxation
- Formal requirements for maintenance can be just stupid with a single-shareholder corporation

S-Corporation

**What is it?**
- A so-called “closely held” corporation
- The classic small business form

**How long does it last?**
- Until the shareholders, the state or the courts dissolve it

**How is it taxed?**
- Can elect to be taxed either as a corporation (similar to a C-corp) or as a partnership
## S-Corporation

**Advantages**
- Corporate veil
- Reasonably uniform treatment across state lines
- Small management team —> quick action

**Disadvantages**
- Limitations on number and types of shareholders
  - S corp can have up to 75 shareholders
  - S corp shareholders must be natural persons
    - Your LLC cannot hold stock in your S-corp

## Corporation or LLC?

<table>
<thead>
<tr>
<th>Corporation</th>
<th>LLC</th>
</tr>
</thead>
<tbody>
<tr>
<td>Eliminates personal liability; may have pass-through taxation</td>
<td>Eliminates personal liability while keeping pass-through taxation</td>
</tr>
<tr>
<td>May be taxed as a separate legal entity or as a partnership. No individual taxation</td>
<td>Taxed as a partnership for multiple members; taxed as an individual for single member</td>
</tr>
<tr>
<td>Some hoops to jump through to form</td>
<td>Some hoops to jump through to form</td>
</tr>
</tbody>
</table>
**Issues to Consider After Formation**

- In what business is the entity engaged?
  - What special or unusual requirements might the business have?
- How does the entity perform its business?
- How does the entity make money?
  - Contracts
  - Licensing of assets
- Tax considerations

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**Issues to Consider After Formation**

- Business
  - Your certificate probably says that you’re in business for “any lawful purpose” unless you’re forming a professional company.
  - What is your business?
  - Where will you get customers or clients?
  - How do you plan to market your business?
  - Can your business change over time?
    - How?
    - How flexible are you in terms of market demands?

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**Issues to Consider After Formation**

- Performance
  - Do you do it all or do you hire employees?
  - What kind of equipment do you need?
  - What kind of customer do you need?
  - What kind of service does that customer need?
  - Who is your competition?
  - How can you out-perform your competition?
## Issues to Consider After Formation

**Revenue**
- You need money to stay in business
- How much will you charge for your goods or services?
- How do you know that the market will bear your price?
- Can you use price to attract your customer?
- How can you get a fair price for your goods or services?
  - What IS a fair price for your goods or services?

**Tax considerations**
- Pay your taxes
  - Or the taxing agency WILL put you out of business and possibly in jail
- Different taxes for different entities
  - Franchise tax on corporations and LLP/LLCs does not exist on partnerships and sole proprietorships
- Sales tax
  - To collect sales tax, you need a state-issued sales tax ID number
    - Contact the Dept. of Taxation and Finance to obtain a sales tax ID
- Payroll taxes:
  - YOU are responsible for payment of employer’s portion of your employees’ payroll taxes (FICA, state, federal taxes)
  - YOU are responsible for getting payment to the taxing authorities (federal, state, and local) on time
  - Voluntary pre-tax withholdings (usually used for child care or medical costs) can REDUCE your payroll tax bill and cost you essentially nothing
  - Several payroll outsourcing suppliers exist; use one of these unless you are comfortable with payroll taxes and want to spend your time doing them for your employees

## Doing Business Across State Lines

**May need to register as a “foreign entity” in the state**
**Qualifying to do business in another state**
- Certificate of Authority + filing fees
- Publish
- Annual reporting fees (can be expensive)
- Pay tax on revenue generated by business within the state
- Appointing a Registered Agent

**Lawsuit possibilities in the state**
- Being sued
  - Personal jurisdiction
  - Website —> personal jurisdiction?
- Suing others
Break
10 minutes

Business Agreements

- What IS a contract?
  - Promise
  - Secured by consideration
  - Legally binding (usually)

Every business has at least one contract

Four ways to form a contract
- Bilateral agreement
  - The contract you think of, often memorialized in a signed writing
- Detrimental reliance
  - One party acts to its own detriment in reliance on the word of another
- Unilateral offer accepted by performance
  - Reward offer is a good example
- Formal
  - Sealed writing
  - Not used much
Business Agreements

14 ways out of a contract:
- **Infancy**: A person under age 18 (in NY; 21 in some states) can enter a contract, but that contract is voidable at the infant’s option.
- **Mental incapacity**: A person who is mentally incapacitated and is recognized as such by a court can enter into a contract, but that contract is voidable at the mentally incapacitated person’s option.
- **Impossibility**: If the purpose for which the contract was formed becomes impossible to achieve, the contract is voidable.
- **Impracticability**: If the performance of the contract becomes impractical (that means really impractical), the contract is voidable.
- **Duress**: If the contract was entered into under duress by one party, the contract is voidable at the option of the duressed party.
- **Unconscionability**: If performance of the contract, or the contract itself, is or becomes unconscionable (legal but morally repulsive to a Reasonable Person), the contract is voidable.
- **Bilateral mistake**: If both parties are mistaken in their understanding of each other’s positions and promises, the contract is voidable at the option of either party.
- **Unilateral mistake**: If one party is mistaken in its understanding of the other’s positions and promises, the contract is voidable at the option of the party.
- **Changed circumstances**: If circumstances surrounding the performance of the contract materially change during the course of performance, the contract may be voidable at the option of the affected party.
- **Frustration of purpose**: If the purpose for which the contract was formed is no longer viable, the contract is voidable.
- **Public policy violation**: If a contract is repugnant to public policy, the contract is voidable.
- **Misrepresentation**: If one party misrepresents a material fact to another, the contract is voidable at the option of the party to whom the misrepresentation was made.
- **Nondisclosure**: If one party fails to disclose a material fact to another, the contract is voidable at the option of the party who was the victim of the nondisclosure.
- **Undue influence**: If a person exerts undue influence on a party at the time of contract formation in order to achieve formation of the contract, the contract is voidable at the option of the victim of the undue influence.

Business Agreements

Discuss the ramifications of any contemplated business agreement, including the “fine print,” with your attorney **before** you sign.

When you do sign a contract, follow through on your end of the bargain:
- Remedies exist at law and in equity for not fulfilling a contract obligations
  - Money damages and judgments
  - Specific performance can be enforced

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Business Property

- **Tangible property**
  - Desks, lamps, chairs, office supplies, business equipment, real property, inventory, accounts receivable, cash on hand, etc.
  - Protected with insurance
    - You need adequate insurance to cover replacement cost
- **Intangible property**
  - Intellectual property
    - Contracts, company know-how, inventions, trade secrets, trademarks and service marks, copyright, trade dress, goodwill
    - Replacement-cost insurance is unavailable
    - Intangible property forms 80-97% of the value of most businesses

Protecting Tangible Property

- Put it under lock and key
- Have inventory control systems in place
- Monitor employees and visitors to prevent theft
- Have adequate replacement-cost insurance

Protecting Intangible Property

- What you can’t see, smell, touch, hear or feel makes up the main value of your business
- Insure your life
  - Protect your family
  - Protect your business
- Insure your income
Protecting Intangible Property

• Company know-how
  – The collective knowledge within the company of how the company does business
    • Processes & procedures
    • Data
  – Often reside only in the brain of the owner or key management personnel
  – Protect them
    • Write them down
    • Keep them secure, protected from unauthorized disclosure
    • Have non-disclosure agreements in place with all employees who have access to company know-how

• Inventions
  – Protect by patent or by maintaining the invention as a trade secret
  – Patent « exercise in disclosure
    • Must disclose best mode of practicing the invention as of the date of filing the patent application
    • Can keep improvements from that day forward as trade secret company know-how
    • Patent gives the holder the right to prevent others from making, using, selling, offering for sale, or importing the invention for a limited time
    • Patent cannot be renewed
  – Trade secret dies with disclosure

• Trade secrets
  – Best kept trade secret of all time?
    • Formula for Coca-Cola®
  – Trade secret is just that: a secret
  – Only protection is through secret
    • If another legitimately invents your trade secret and patents it, you can lose the rights to the secret
    • If secret is disclosed, purposefully or not, the cat’s out of the bag and your trade secret is gone forever
Protecting Intangible Property

- **Trademarks and service marks**
  - Identify a good or service as coming from your company
  - Valuable goodwill in the marketplace
  - Trademarks/service marks exist to prevent consumer confusion
  - Can be registered federally if you are engaged in interstate commerce, i.e., if you have the mark on a website
  - If you do not engage in interstate commerce, the mark can be registered in the state in which you do business
  - Trademarks are first come, first served
  - Unlike a patent, to keep a trademark, you must continually use it in commerce

- **Examples of registered marks**
  - XEROX
  - GE
  - Honda
  - Quilter
  - 3M
  - Fly the Friendly Skies.

- **Examples of unregistered marks**
  - OJBDLO
  - Amway
  - House of Facks
Protecting Intangible Property

- Trademarks and service marks
- Use it or lose it
- How to obtain a mark
  - Decide on a mark to associate with your company
  - Have a trademark search done
  - If the search comes back clean, begin using the mark on everything you put into the stream of commerce (goods, services, stationery, website, advertising, all of it) with the ™ designation
  - Register the mark when you begin doing business across state lines
    - For this purpose, Canada is NOT a state
    - Massachusetts IS a state, as is Ohio, Pennsylvania, Vermont, New Jersey, etc.

Protecting Intangible Property

- A trademark has a grammatical part of speech associated with its usage. Is that part of speech a:
  - Noun?
  - Verb?
  - Adjective?
  - Preposition?
Protecting Intangible Property

• Examples of Lost Marks
  – Plastic clingy wrap
    • CELLOPHANE
  – Moving staircase
    • ESCALATOR
  – Pain reliever (and blood thinner, as it turns out)
    • ASPIRIN
  – All lost to improper usage

• Marks In Danger
  – Facial tissue
    • KLEENEX®
      – We do not get a kleenex; we get a KLEENEX facial tissue
  – Photocopy, the act of photocopying
    • XEROX®
      – It is not a xerox, and we do not xerox anything; it is a XEROX copy and we make a photocopy
  – Internet search engine
    • GOOGLE®
      – It’s not possible to google anything. We use the GOOGLE search engine
  – All may be lost to improper usage

• Trade dress
  – The protectable appearance of goods, services, décor, etc. that is associated with business goodwill
  – Protectable under trade dress law
    • Federal
    • State
Protecting Intangible Property

• Copyright
  – Of all the registrations for intellectual property, copyright is probably the easiest to obtain
  – Protects works of authorship (books, music, architecture, artwork)
  – Does NOT protect taglines
  – Cheap to get really good protection: $35 registration fee for online registration
  – In return for registration, statutory damages are available for infringement ($750-$30,000 per infringing act), trebled if you can show willful infringement

Planning

• What happens if you get into a car crash on your way home tonight?
  – Suppose you die (we all will, one day)
  – Suppose you don’t die but can’t work
  – Suppose you will be able to work again in a while
  – Suppose you won’t

Questions?