

# Look Before You Leap: Legal Issues in Business

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PRESENTED MAY 21, 2016  
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# Upcoming Workshops

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## Licenses, Permits and Taxes, OH MY!

- Tuesday, May 24, 7-8pm

## Choosing the Right Tax Structure

- Tuesday, May 31, 7-8pm

## Financial Statements: What They Say About Your Business

- Saturday, June 4, 10 - 11 a.m.

Where: Kirkwood Community College, Iowa City Campus  
1816 Lower Muscatine Road, Room 262.

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# Before We Get Started...

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Introductions, and one thing you want to learn from today.

Please ask questions – if I don't know the answer, I can take your contact information and track down the answer or point you in the right direction.

Here to discuss starting a for-profit business. Non-profits have some similarities but also differences.

Only talking about Iowa businesses.

I am not your attorney, this is not legal advice and our discussions today are for general education purposes only. Each situation is different. If you need assistance with your specific issues, invest in a lawyer's time to help you get started.

Thank you to our sponsors.

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# Introduction

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*What will we be talking about?* Basic legal issues common to most new small businesses. Books are written on this subject and we will not cover everything.

*How will I benefit?* Through presentation and discussion, you should leave today with an understanding of the major legal concerns you might face when starting up your new business.

After reflection, you will want to do additional research or seek out specific legal advice.

*Who is this guy?*

# What We'll Cover

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Major Topic: Don't go it alone

- Who should I have on my team and how much should I budget

Major Topic: Setting up my business

- First steps, entity types, structure, co-owners, paperwork

Major Topic: Running my business

- Personal liability, insurance, contracts, workers, facilities, financing

Additional Topics (if we had a week)

Questions and Discussion – real life

# Don't Go It Alone

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Your team of advisors: lawyer, accountant, insurance agent, mentor

Interview them before hiring, ok to ask for references

Confidentiality

Bring them together, give them permission to talk with each other

Demand coordination, plain language, and promptness

Others on the team: banker, marketing & design, payroll service provider, financial advisor/pension plan manager, pre-employment screening service

# Don't Go It Alone - 2

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Budget more for startup legal expenses than you think you need.

- Constant back and forth, legal complexity and other factors.
- Consult with your attorney to estimate the total legal fees at the beginning.
- Ask about a project based billing approach, where the attorney and client negotiate in advance on a scope of work and total amount to be charged.
- Consider doing preliminary work with review by attorney.
- Written fee agreement.

A business lawyer can:

- Help you select the right form of business entity
- Draft and file incorporation and governing documents
- Advise you on employee matters, customer contracts, leases, buying a business
- Assist with debt collection
- Represent you in a lawsuit
- Remember – lawyers have specialties, right tool for the job



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# Setting Up My Business

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Research ahead of time the licenses you will need to operate and budget time for getting them. Licenses are a separate workshop in this series.

## Business Name:

- Do your homework (most can be done online) before you start rolling with a business name, logo or brand.
- Business name versus trademarks
- Existing users can sue for infringement
- Registration of a business name
  - (sole proprietor trade name is registered by filing a form at the County Recorder's office. \$7).
  - All other names (legal company names, fictitious names/DBA's) filed with the Secretary of State's office.
- Trademark registration – highly recommended



# Setting Up My Business - 2

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Why not just be my own business? Personal liability.

- incorporating your business can shield you from the debts or liabilities of the entity
- Exception: those liabilities you voluntarily assume (personal guaranties)
- Exception: intentional harm



There are different options for the form of your business

- Sole proprietorship, partnership, LLC (limited liability company), corporation (S- and C-corps for taxation)
- Partnerships may be useful in specialized situations, not common; beware an unintended partnership
- <http://www.iowabar.org/?page=StartingABusiness>

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# Setting Up My Business - 3

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Sole proprietorship – owner is the business

- Unlimited personal liability
- Uncommon except for the smallest of scales, e.g. mom’s houseplant table at the farmers’ market
- Can be done but insurance is critical

Limited Liability Company (LLC)

- Can have a single owner, called a “member”. Can also have multiple members.
- They are easy to set up and run.
- The owner of a single member LLC doesn't have to file a tax return for the LLC, report the activity on their personal tax return.
- Many LLC forms are only a single page for single member LLCs.

# Setting Up My Business - 4

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## Limited Liability Companies – con't.

- In Iowa, you form an LLC by filing a document called a Certificate of Organization with the Iowa Secretary of State. \$50.
- No set form but it must, at a minimum, contain the name of the limited liability company, which must (1) use “limited liability company” or an abbreviation like “LLC”, “LC”, and (2) must be distinguishable from other business names which have been filed in Iowa.
- Certificate of organization must also have the street and mailing addresses of the initial registered office and the name and street and mailing addresses of the initial registered agent for the LLC. You can include other information in the certificate of organization.
- You may want additional documents related to starting up an LLC (minutes, operating agreement). Altogether, with the state filing fee, you should be able to find a local attorney willing to help you do the whole set up for ~\$300 for a single owner LLC.

# Setting Up My Business - 5

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## Limited Liability Companies – con’t.

- Maintaining the records of the LLC is less formal. No requirement for annual meetings or minutes or formal resolutions – but this is all a very good idea to do anyway.
- Recommended formalities for LLCs include: adopting an operating agreement (kind of like bylaws), issuing membership units, holding and documenting annual meetings, and documenting all major company decisions.
- Biennial report: \$45 (discount for online)
- CON: self-employment tax applies to all income from a one-owner LLC
- CON: low paperwork can lead owners to disregard “corporate formalities”
- CON: leaving or selling your stake in an LLC is tough – usually your co-owners must consent. Obviously this isn’t an issue if you’re the sole owner.

# Setting Up My Business - 6

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## Subchapter S Corporations – aka “S-Corps”

- An S-Corp structure can provide a business owner with tax benefits
- Filing Articles of Incorporation with the Iowa Secretary of State costs the same as starting an LLC: \$50. Biennial report: \$45 (discount for online)
- Corporations in Iowa are required to have annual meeting minutes, bylaws, and shares.
- Stock in an S Corp is much more freely transferrable than ownership of an LLC. This is an issue if money needs to be raised by selling shares in the business.
- Have to file a form with the IRS and meet requirements in order to get S-Corp status.
- Business name must include “Inc.,” “Corp.” or similar.

# Setting Up My Business - 7

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## Subchapter S Corporations – aka “S-Corps” con’t.

- CON: amount of additional care and paperwork means tax savings not really useful until your business has more than \$40,000 in net income per year
- CON: have to file the election form with the IRS on time
- CON: have to file a separate tax return for the corporation
- CON: Owners must be U.S. citizen or resident alien (green card or 183 days test) (if a non-resident alien, consult a tax specialist).
- CON: Have to distribute profits proportionally if multiple owners.

# Setting Up My Business - 8

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Business entities filed with the state must file a short form every other year and pay a fee in order to remain in good standing. You do not want to inadvertently lose the good standing of your business entity – personal liability.

After filing your company organization document with the Secretary of State, get an EIN (aka Tax ID Number) from the IRS.

- Bank will need it to set up your business account
- Can be done through an online guided process; 15 minutes

# Setting Up My Business - 9

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## Insurance

- Liability, property, auto
- In addition to your general business liability insurance, aka CGL (commercial general liability), consider a good umbrella policy both at the personal and commercial level. ~\$400 to \$700 per year.
- Errors and omissions insurance varies depending your profession (realtor versus financial advisor versus insurance sales).
- Aside from liability, insurance (e.g. business interruption, “key person”) is a good part of a disaster preparedness plan

# Setting Up My Business - 10

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## Co-owners

- Competing interests
- How are management decisions going to be made? Can one partner fire the other?
- What happens when one of the partners wants to exit? What do they get, and under what terms?
- What happens if a partner gets hit by a bus? If their ownership interest goes to a spouse, does the spouse have a say in management decisions?
- **So much easier** to address these up front than it is when you're making lots of money. Get it on paper in the beginning. Called a “Shareholders’ Agreement” or “Buy-Sell Agreement”.
- If you are thinking of bringing in an investor or co-owner, think about letting them get shares in installments instead of all at once.

# Running My Business

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Remember the liability shield? Six major reasons why the business liability shield may be dropped:

- (i) failure to properly maintain separate corporate records, minutes, and continual good standing with the Secretary of State,
- (ii) inadequate capitalization at the time of formation,
- (iii) not using the company name in your operations or on your documents – sign using your title (“Pres.”, “Manager”, “CEO”),
- (iv) commingling funds,
- (v) fraud/criminal activity, and
- (vi) voluntary agreement to be personally liable (guaranty).

# Running My Business - 2

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## Borrowing Money, Security & Personal Liability, Microloans, Investors

- For a loan, you'll generally need your business plan, projected financials (Financial Statements: What They Say About Your Business, Saturday, June 4, 10 - 11a), and proposed collateral
- Collateral (aka security) is assets the lender can take if you don't pay the loan
- If they are your business assets, losing them can make it impossible to operate
- Personal guaranty = personal liability
- Unsecured debt
- Getting investors? Crowdfunding? Smart to hire a qualified attorney.

# Running My Business - 3

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## Facilities: Zoning, Home Business

- Certain products cannot be produced in the home. Most states outlaw home production of fireworks, drugs, poisons, explosives, sanitary or medical products and toys. Some states also prohibit home-based businesses from making food, drink or clothing.
- Local public health official re: food production
- A note about online businesses

## Facilities: Leases, Remodeling and Fixtures

- Negotiable. For example, landlord's help with renovation expense.
- Be careful about terms longer than a year (ask for an option to renew, but don't lock yourself in) or clauses that excuse a landlord from having to find a replacement tenant.
- Lots of other things to watch out for - May be worth it to pay an attorney for an hour of their time to review and counsel you.

# Running My Business - 4

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## Contracts, incl. with Suppliers, Customers

- Avoid long term contracts if at all possible, especially ones where you are asked to guarantee them personally.
- Use written terms of service agreements with your customers, spelling out what you are agreeing to do, what they must pay for and when.
- Include in your contracts that you can sue the customer if they don't pay, that they will be charged interest on overdue amounts and that you can recover your legal and collection costs.
- Consider including an arbitration clause.
- This is a good area to work up contracts (employees, suppliers, customer orders, etc.) using free resources and your own time, then pay an attorney to review your work.

# Running My Business - 5

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Employees, Eligibility to Work/SSN, Minimum Wage, Withholding of Payroll Taxes, Workers Compensation and Unemployment Insurance

- Independent contractor or employee? If you keep control over your workers, when they work, what they do, where they work, how they do it and the equipment they use to do it, then it looks more like these workers are employees. Misclassification can be expensive.
- Inevitably, some of your favorite employees will move on. Consider offer letters with confidentiality and non-compete clauses; arbitration
- formally document reviews and disciplinary write-ups.
- Minimum wage = \$7.25/hr for covered employees in Iowa, \$9.15/hr in Johnson County, \$5.49/hr for tipped employees. Next increase 1/1/2017.
- Workers compensation – in general, if you have employees, you must have a policy in place.

# Running My Business - 6

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## Miscellaneous

- Document everything that goes on in the business. Hiring, firing, borrowing money, corporate decisions, purchasing equipment, selling assets.
- Guard your intellectual property, customer lists, marketing plans.

# Running My Business - 7

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## Things Go Wrong; Shutting Down

- Lease - do the legwork for your landlord and try to line up a suitable replacement tenant if possible. Could be liable for all the lease payments for the remaining months on the lease. Negotiate with the landlord on exit terms.
- Collateral - if you pledged your equipment and other assets as collateral for a bank loan, you may not be able to sell assets to pay bills without getting your bank's permission first. And they will likely want you to pay down or pay off your loan with them with the proceeds.
- Legal help - heck with a bankruptcy attorney and see what your options are. They can usually help you more if you come to them before you're back is really against the wall.
- Sale - consider selling your business. Selling the business as a whole usually has more value than simply auctioning off the individual parts.
- Cooperation - if you are in a loan situation, strongly consider working with your lender to restructure the terms of your loan. They want your business to succeed and may be willing to work with you if it means that you'll be in a better position to repay the loan.
- Co-owners - this is when it is critical to have your company's structure and agreements among the owners in writing. Who gets to make decisions, who has to pay what, and what is everyone entitled to walk away with at the end are all issues to cover.

# Additional Issues

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Government incentives,  
assistance

Franchises - no guarantee of  
success

Industry-specific regulations: e.g.  
food production has hygiene and  
facility restrictions, clothing  
manufacturing may have testing,  
dry cleaning has chemical  
handling/environmental  
regulations

Workplace safety

Disaster preparedness

Buying an existing business

Sales tax, sales tax exemption

ADA accommodation

More on intellectual property

More on online-specific issues

# Thank You --- Q&A

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It's worth the time to:

- Educate yourself about legal issues relating to your business
- Set up an LLC or S-Corp
- Hire an attorney, accountant and other professionals to consult on specific issues for your business
- keep records and keep your business separate from your personal

Thank you to our sponsors: City of Iowa City – Neighborhood Services, Kirkwood Community College, UofI CCU, Hills Bank & Trust Co., Sankofa Outreach Connection, MidwestOne Bank, CommunityCPA.com

## Discussion

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