INSIGHTful DISCUSSIONS

Sponsors' Content Distributed By Greater Wilmington Business Journal

MITIGATING RISK AMID THE LAWS OF BUSINESS

ADAM M. BEAUDOIN
Attorney,
Ward and Smith, P.A.

MATTHEW B. DAVIS
Partner,
Marshall, Williams & Gorham, LLP

GEOFFREY A. LOSEE
Partner,
Rountree Losee LLP

ELLEN P. WORTMAN
Partner, Hedrick Gardner Kincheloe & Garofalo LLP

WARD AND SMITH, P.A. ATTORNEYS AT LAW

MWG MARSHALL, WILLIAMS & GORHAM, LLP

ROUNTREE LOSEE LLP Est. 1896

HEDRICK GARDNER Hedrick Gardner Kincheloe & Garofalo LLP Attorneys at Law

Business owners and executives often try to save money by waiting to call an attorney. However, a modest investment in legal advice to prevent problems usually results in significant savings in time, money and headaches. Below and on the following pages, four area attorneys offer insights on questions they commonly hear from business people seeking to mitigate risk in numerous areas, including employment, cybercrime and succession planning.

When forming a new entity such as an LLC, S-Corp or C-Corp, what factors do business owners often not consider that they should?

ADAM BEAUDOIN: Most business owners focus on the desired tax treatment and management of the entity, but fail to address changes in circumstances that could have an effect on the ownership or control of the entity.

Regardless of the form of entity chosen by the business owners, it is highly recommended that they enter into a shareholders' agreement (in the case of a corporation) or operating agreement (in the case of an LLC) which sets out what happens in the event of: death, disability, bankruptcy, termination of employment, and involuntary transfer. These types of agreements can also provide buy-sell language that comes into play in the event the owners no longer want to be in business together, and establish valuation formulas for any buy-out event. Thinking about these issues on the front-end of the business relationship can save time and money on the back-end if things don't go as planned.

MATTHEW DAVIS: One consideration that is sometimes overlooked is that there are certain formalities that corporations must observe. For example, corporations are obligated by statute to hold an annual shareholders' meeting even if there's only one shareholder. Failure to observe this formality could jeopardize its limited liability benefits in the event someone tried to pierce the

INSIGHTful DISCUSSIONS

Sponsors' Content Distributed By Greater Wilmington Business Journal

"Many businesses fail in their first year because they underestimate the funding needed for long-term sustainability, and the owners pay themselves too much."

ELLEN P. WORTMAN
Hedrick Gardner Kincheloe & Garafalo

"Often, a meeting with counsel to brainstorm through "what ifs" ...can help avoid significant costs and delays later in the process."

GEOFFREY A. LOSEE
Rountree Losee LLP

corporate veil. LLCs, on the other hand, are not statutorily obligated to conduct annual meetings, and therefore have one less box to check.

An issue that is likely well outside most owners' thoughts when contemplating the formation of a business entity is workers' compensation. The Workers' Compensation Act defines "employee" to include corporate officers, but not members of an LLC. Thus, a closely held corporation with one spouse as president and the other as secretary would have two employees for workers' compensation purposes, even if one of them does not work for the corporation in the ordinary sense. Consequently, the corporation could unknowingly hit the statute's three-employee trigger.

ELLEN WORTMAN: If two or more people form a business entity together, they should have a written operating agreement (for an LLC) or a shareholders' agreement (for a corporation). The operating agreement or shareholders' agreement helps to clarify the owners' expectations for each other and the new business. These agreements also provide a roadmap for the new business entity and its owners in the event that disputes or other problems arise in the future.

The new business should also have sufficient funding for its startup activities and to see it through until the new entity begins generating revenue (through capital contributions, loans from its owners, or a loan or line of credit from a financial institution or other investors.) Many businesses fail in their first year because they underestimate the funding needed for long-term sustainability, and the owners pay themselves too much.

Finally, the new business should be adequately insured against risk. The new business must carry workers' compensation coverage if it employs three or more people, and should have a general liability insurance policy in place.

What are common legal mistakes in real estate development and other real estate transactions?

GEOFFREY LOSEE: In my opinion, the most common mistakes really result from "assumptions" … and we all know the old saying about assumptions. In this context, it can take the form of failing to spot an issue during due diligence that should precede every planned development, or even from failing to plan out the scope of that due diligence and the division of labor for the due diligence items. Often, a meeting with counsel to brainstorm through "what ifs" – a meeting that might only last a couple of hours – can help avoid significant costs and delays later in the process.

DAVIS: Drafting errors and the failure to convey ancillary rights or interests are common legal mistakes in the realm of real estate development. In the context of planned communities, common drafting errors range from the use of wrong or inconsistent names all the way to recording declarations of covenants containing inapplicable or conflicting terms.

Though the reasons are legion, these drafting errors often stem from a well-intended attempt to repurpose old documents from other projects by simply changing dates, names and other basics, but without performing a comprehensive review to ensure that they actually fit the reality of the new development.

Another common form of legal mistake is the failure of developers to convey common property, such as roads and amenities, to an association in advance of turnover from declarant control. Similarly, a particularly pervasive mistake is the failure to transfer stormwater permits at the time of conveyance.

The good news regarding all these mistakes, though, is that they are easily avoided through careful review and the use of checklists.

What potential liabilities do companies have for cybercrimes, such as when customer credit cards are stolen from their systems? How can they limit their legal exposure?

DAVIS: Companies that electronically store customer data should consider three points:

- First, data breach notification laws, including North Carolina's Identity Theft Protection Act, require businesses that maintain personal information to timely notify the affected person of a security breach. Under North Carolina law, failure to do so may constitute an unfair or deceptive trade practice. Thus, if you experience a data breach, immediately determine what notice obligations, if any, you're under.
- Second, legal commentators report that it remains difficult for plaintiffs alleging data breaches, usually as a class, to prosecute such claims. A primary obstacle is their frequent inability to establish a concrete injury, as opposed to the mere fear of identity theft or other harm. Also, the lack of a common set of laws governing civil liability for data breaches forces claimants to rely on largely inapplicable statutes or common law claims, such as negligence and breach of contract.
- Third, from a risk management perspective, businesses maintaining customer data should contact their insurance agents regarding cyber-risk coverage. Additionally, businesses may consider adopting an information security program that includes, among other things, performing a risk assessment and then designing and implementing reasonable safeguards based on that assessment.

BEAUDOIN: I referred this question to Matthew A. Cordell, a colleague at Ward and Smith: A study by the cybersecurity firm NetDiligence of cyber-insurance policy claims from 2012 to 2015 showed the average claim amount was $673,767, and smaller companies account for the majority of claims in recent years. The greatest risk, in terms of dollar amounts, is the risk of an enforcement action by the Federal Trade Commission (or for companies in regulated industries, another regulatory agency) for inadequate practices or deceptive privacy policy statements, which have frequently resulted in settlements in the seven- and eight-figure range.

The most likely source of loss, however, is the reputational risk that companies suffer when they are forced by law to disclose the existence of a breach and to notify the affected. The loss of customer loyalty and the diminution of the brand are difficult to measure, but are nonetheless significant. There are many things a company can do to prevent a breach and to mitigate the harm following a breach, some of which are technological and some of which are administrative or legal. Unfortunately, there is no silver bullet; a strong defense or response requires a multifaceted approach and advisers with different areas of expertise.

LOSEE: Businesses may be liable to individuals for harms occasioned by data breaches, and taking prompt action to curtail leaks will limit liability. North

Carolina regards a security breach as an occurrence when unencrypted records containing a person's name and personal information (such as Social Security, taxpayer identification, driver's license or state identification, checking and savings account, credit and debit card, and financial resource access numbers) are improperly accessed. An occurrence requires notice to the state attorney general's Consumer Protection Division, the affected person, and the three major credit reporting agencies.

If your business regularly accepts credit cards, we recommend that you conduct a security audit (or engage an auditor) to audit your protections and have an emergency action plan in place should a breach occur. Even the federal government did this – after the General Services Administration was hacked.

How can companies balance employees' privacy and free speech rights, while also trying to ensure they don't post things on social media and elsewhere online that reflect poorly on their employers?

BEAUDOIN: I referred this question to Devon D. Williams, a colleague at Ward and Smith: First and foremost, employers should develop clear policies and appropriate standards on social media use in the workplace. Employers can and should educate their workforce on social media use – a well-written and compliant social media policy can help in this regard. Secondly, employers should educate their management-level employees, early and periodically, on the appropriate responses to unpleasant posts from employees on social media websites. Employers must avoid reacting immediately and possibly unlawfully to employees' offensive use of social media.

The National Labor Relations Act (NLRA), among other laws, gives employees wide latitude in discussing the terms and conditions of their employment, including wages, benefits and disciplinary action. The NLRA prohibits employers from retaliating against employees for engaging in this "protected concerted activity." Discipline or termination from employment based on an employee's use of social media may result in an unfair labor charge with the National Labor Relations Board (NLRB). As such, it is well-advised that employers consult legal counsel before taking any type of disciplinary action against an employee related to social media posts.

LOSEE: Employees have limited privacy and free speech rights in private workplaces. However, the National Labor Relations Board has become increasingly broad-minded about interpreting employee discussions in social media contexts (including such conduct as "liking" a statement on Facebook) as covered by the National Labor Relations Act. This act protects employees' ability to communicate freely with one another in an effort to combat negative workplace conditions or unionize.

Employers are not without control in this area, but they should be thoughtful and specific in creating appropriate policies. Employers should work with counsel to craft social media and computer use policies that are most likely to satisfy the evolving demands of the NLRB.

Employers may generally require employee conduct – even on private social media – to comply with major safety and conduct policies, such as anti-discrimination, anti-harassment, and anti-violence policies. What employers may not do is prevent or discourage employees from critically discussing the terms and conditions of the workplace. Employers should apply the same logic to their confidentiality, anti-solicitation, posting, and other policies that govern the non-electronic communication conduct that is now commonly accomplished through social media.

DAVIS: Generally speaking, at-will private sector employees enjoy little protection against speech-related terminations. Constitutional guarantees, including free speech, do not apply to the actions of private entities as a general matter. As such, private employers cannot violate an employee's freedom of speech. To paraphrase the great American jurist Oliver Wendell Holmes, Jr., "You have a constitutional right to speech, but not your job."

It is important to stress, though, that general principles are nearly always subject to exceptions, and pitfalls abound. Or as Justice Holmes also observed: "The young man knows the rules but the old man knows the exceptions."

Take for instance a federal labor law that protects the rights of employees to work together to address work conditions, with or without a union. The regulatory board responsible for enforcing this law maintains that these protections extend to certain work-related conversations conducted by social media. Thus, what an employer may view as employee badmouthing on Facebook, the law may view as a protected right for co-workers to discuss wages and working conditions.

Ultimately, given the sensitive nature of free-speech concerns, employers faced with these issues should exercise caution and confer with knowledgeable counsel before acting.

Companies increasingly use contractors, particularly because of rules included in the Affordable Care Act, which is also known as ObamaCare. What advice do you give companies when they are deciding whether to hire employees or contractors?

LOSEE: Generally, an employer should use an independent contractor where the employer needs services that are not in its ordinary-course business conduct and when the employer does not intend to exercise the degree of control over the contracting party that it would normally exercise over an employee. True independent contractors may have exclusive relationships with single employers, but they must generally exercise control over their own method, means and timing of work.

Hiring an "independent contractor" to do what existing employees do, and exercising the same degree of control over the "independent contractor" that the employer exercises over employees is risky. The Internal Revenue Service uses 20 factors to assess whether a relationship is truly an "independent contractor" relationship. As you might guess, the IRS frequently construes purported independent contractor relationships as tax-avoidance arrangements. Audits may result in employers and "independent contractors" being liable for back employment taxes as well as other "avoided" mandates (such as health care).

BEAUDOIN: My colleague, Devon D. Williams, provided this response to this question: Now more than ever, business owners must closely scrutinize their contractor relationships. The use and misuse of independent contractor status has been one of the most talked about issues facing businesses over the past decade. Major newspapers have published exposés, lawmakers have threatened new legislation, and attorneys have authored countless articles attempting to explain the rules. Still, despite all this discussion and debate, the rampant misclassification of employees as independent contractors and a general misunderstanding of the law continue.

In July 2015, however, the Department of Labor clearly stated its position that "most workers are employees under the FLSA's (Fair Labor Standards Act's) broad definitions." As such, the default rule is that workers hired to perform services for a company will be employees of that company, until proven otherwise.

While there are instances where a true independent contractor relationship can exist, those situations are limited and should involve work that is not integral to the company's operations (for example, janitorial services for an office building). Nevertheless, with all of the misconceptions on who is or is not an independent contractor, employers will do themselves a favor by erring on the side of caution and assuming the relationship is that of employee-employer, until legal counsel is consulted and analyzes the relationship in accordance with the Department of Labor's guidance.

What is the best way to structure a non-compete so it serves its purpose and can stand up in court?

INSIGHTful DISCUSSIONS

Sponsors' Content Distributed By Greater Wilmington Business Journal

WORTMAN: To stand up in a North Carolina court, a non-compete provision (also known as a restrictive covenant) must be part of an employment contract, supported by consideration, and reasonable as to time, scope and territory. New employment can serve as consideration for a non-compete; however, it is very important that the new employee sign the employment contract on or before the employees' first day of work. If an employer wishes to impose a non-compete on existing employees, the employer must give the employee something in return – often a cash payment.

The restrictions imposed upon the employee in the non-compete should be as limited as possible to protect the legitimate business interests of the employer. The scope of the non-compete should be restricted to the employer's actual business and the employee's precise duties. For instance, if the employer manufactures and sells gaskets for the automotive industry, the non-compete should not prevent the employee from working for a parts supplier in the automotive industry. The restrictive time period should never exceed three years, and the shorter the time period, the better. The territory should be limited to the area where the employee actually works.

DAVIS: An initial distinction should be made between non-competes made in the employment context and those that relate to a business sale. Although the courts approach both with skepticism, employment covenants receive greater scrutiny because they impact an employee's livelihood. North Carolina case law also cites the public's interest in access to services as a reason for disfavoring non-competes.

Balanced against the interests of employees and the public are the rights of employers to protect legitimate business interests using reasonable efforts. What constitutes "legitimate interests" and "reasonable efforts" is a fact-specific inquiry, but a guiding principle for businesses should be not to overreach.

For instance, the North Carolina Supreme Court recently found that a non-compete provision included in a purchase agreement was unreasonable, and therefore unenforceable, because the territorial restriction covered "large swaths" of North Carolina and South Carolina, yet the business had no "presence in sizeable portions of either state." If the territorial restriction had been limited to the area in which the business actually served customers, the court likely would have upheld the non-compete.

In addition to passing the subjective reasonableness test, there are technical requirements that must be satisfied, including that the non-compete be in writing and supported by consideration.

BEAUDOIN: My colleague, Devon D. Williams, provided an answer to this question: In North Carolina, non-compete agreements are enforceable if employees are required to agree to only those reasonable restrictions on their future employment that are necessary to protect their former employer's legitimate business interests.

However, to be enforceable, the restrictions must be reasonable in duration, territory and scope. Specifically, to be enforceable in North Carolina, any non-compete agreement you implement must be:

- In writing;
- Reasonable as to time and territory;
- Made a part of the employment contract;
- Based on valuable consideration; and
- Designed to protect your legitimate business interests.

Reasonableness will depend on factors specific to the individual business and the duties of the particular employee involved. Employers will need to take into consideration the method of manufacture, market, range of distribution, and business plan, as well as the particular employee's own specific knowledge, skills and interactions with customers or suppliers to craft an enforceable non-compete agreement that will actually serve the employer's legitimate business interests.

Furthermore, with a plan in place and the expectations made clear, valuable business information can be protected as a trade secret and employees will think twice before choosing to exploit the employer's investment and innovation for their own or someone else's advantage.

LOSEE: The key factor in structuring a non-compete to stand up in court is to make sure you actually need one. A non-compete is just one of several options employers have for protecting confidential information and employee and client relationships.

Employers frequently may achieve strong legal protection of these resources with confidentiality policies and covenants not to take employees, clients or both on departure from the company. These types of covenants generally are viewed more favorably by courts than non-competes.

Where an employer must use a non-compete because of the unique nature of its products, services or place in the market, then the non-compete should be drafted narrowly to protect only the competitive interest. A good non-compete limits only conduct that competes with the product or service with which the employee was entrusted at the original employer. This substantive limitation must be further limited to only the geographic scope that is actually relevant to the employer's product or service. Finally, the restriction should last only for a period of time that reasonably protects the employer.

What other aspects of employment law should most companies consider more?

DAVIS: Depending on size, many businesses would be well-served by adopting a consistent records policy regarding personnel issues, including the creation and maintenance of employee files to capture employee performance or incidents in which employee redirection was necessary. Thus, if there's ever an employee allegation of discrimination or retaliation, the supporting information has already been captured.

Another general recommendation is that if a business has an employment handbook or employment agreements in place, review it before taking any material action related to an employee. If there's a long-forgotten termination procedure buried in there, it would be good to rediscover it.

Finally, because the cost of failing to carry workers' compensation insurance can be severe, small businesses should confirm whether they're required to carry it. The short answer is that all businesses having three or more employees are required to obtain workers' compensation insurance. As discussed here, though, who qualifies as an "employee" depends on statute, and not one's ordinary understanding of the term.

BEAUDOIN: I asked my colleague, Devon D. Williams, to provide the answer to this question: Consider and understand when you may be subject to the Fair Credit Reporting Act (FCRA) and what the requirements are. Employers who hire an outside third party, known as a "consumer reporting agency," to perform credit and background checks on employees and prospective employees must abide by specific, detailed requirements of the FCRA. On the other hand, where an employer conducts background checks on its own without a consumer reporting agency's assistance (for example, the employer calls previous employers of an applicant directly), the FCRA is not implicated.

Keep in mind that employment at-will means an employer or employee can terminate the employment relationship at any time, with or without notice, for any reason, or no reason at all – so long as it does not violate law. The latter half of that phrase carries the most punch.

LOSEE: First, employers should adequately value the role of the Human Resources professional and view him or her as cost saver. Low employee turnover, standardized employee procedures, and appropriate counseling and separation of employees go a long way to prevent claims and lawsuits and prevent expensive, frequent onboarding. Human Resources professionals are often best-situated to stay on top of employment law developments, troubleshoot potential issues, and assure consistent delivery of corporate messaging to employees.

Second, employers should audit their pay practices for compliance with the Fair Labor Standards Act. Long-time practices – even those common in an industry – may be improper. Auditing and correcting to head off trouble with the Department of Labor can save employers significant long-term liability for back pay and attorney fees.

Third, employers frequently do not have procedures in place that encourage consistency among supervisors in treatment of employees. Having standard interview, counseling, evaluation and discharge procedures in place may help to prevent allegations of unlawful discriminatory treatment. Employee perceptions of unfairness drive demands and lawsuits (even where the employee is wrong in the perception or the "different" treatment is not unlawful).

WORTMAN: Companies should be wary of misclassifying employees as independent contractors and failing to pay overtime when required. True independent contractors are not subject to an

INSIGHTful DISCUSSIONS

Sponsors' Content Distributed By Greater Wilmington Business Journal

employer's control or guidance and are not economically dependent on a single employer. Employers who misclassify employees as independent contractors typically do so reduce labor costs and avoid state and federal taxes. A company risks significant financial penalties if it is determined that its employees were misclassified as independent contractors.

Many companies also misunderstand the laws governing overtime. Often, employers mistakenly believe that if an employee is paid a salary rather than an hourly wage, overtime pay is not required. There is a complex set of factors that must be evaluated in determining whether a specific employee is exempt from overtime pay.

Companies should be aware that the U.S. Department of Labor has proposed to update its regulations under the Fair Labor Standards Act that will extend overtime pay protection to many more white collar workers. Almost all companies will need to analyze whether their employees will be exempt from overtime pay before the anticipated 2016 effective date of the new regulations.

How should companies decide what intellectual property to protect, and how can they best protect it?

WORTMAN: Companies should first identify the intellectual property (IP) they own and assess the role IP plays in their business. A company's IP may include words or designs that distinguish its products or services, confidential business information, inventions, domain names, and company literature or other copyright content.

Emphasis should be placed on protecting IP that is truly important to the business. Consideration should be given to what IP assets are necessary for the business to brand and sell its products or services; which IP is most economically valuable to the business and its competitors; and which IP assets are at the greatest risk of being misused by others if not appropriately protected.

To fully protect its IP, a company must understand what the various forms of IP are and how they can help a business protect its creative assets. There are many different forms of IP protection, but the vast majority fall into four categories: copyright, patents, trademarks and trade secrets. A critical first step in protecting a company's IP is recognizing which of these categories best protects the specific IP at issue. The company must then determine what, if any, additional steps must be taken to secure the necessary IP rights and protections.

BEAUDOIN: I referred this question to Angela P. Doughty, a colleague at Ward and Smith: Although attorneys will put intellectual property into various categories, a business person can generally think of it as anything and everything that distinguishes or gives a company, product or service a competitive edge. IP-driven businesses, such as those selling patented or copyrighted material (think pharmaceuticals, music and software, for example) need no introduction to the economic calculus of what to protect. But every business likely possesses or uses some form of IP, whether it knows it or not. For most businesses, their IP includes, at a minimum, the names and logos that distinguish their goods and services in the marketplace. But IP can also include information such as customer lists, marketing plans and non-patentable processes and formulas if they give you a competitive edge for being valuable and are generally unknown to competitors.

Identifying what to protect typically requires answering some basic questions:

1. What aspects of my company, product, or service give me a competitive edge?
2. What legal avenues are available to protect that competitive edge from use by competitors?
3. Is the available protection worth the cost considering the potential impact of losing that edge on my business?

An IP attorney can assist you with identifying your protection options.

DAVIS: Of the four types of intellectual property – copyrights, trademarks, patents and trade secrets – trade secrets seem to receive the least attention yet arguably require the most sustained effort from businesses to earn and maintain legal protection.

Trade secrets are defined as commercially valuable business information not generally known or readily ascertainable through independent development or reverse engineering. Usually developed through the investment of time and money, they may include secret formulas, cost histories, price and customer lists, pricing and bidding formulas, and even the compilation of business information.

To qualify as a trade secret, reasonable efforts, as determined by the circumstances, must be taken to guard the information's secrecy. Such efforts may include: sharing the information, whether with employees or counterparties, on a need-to-know basis only; marking the information as "confidential;" notifying those with whom the information is shared that the information is confidential or even requiring execution of a non-disclosure agreement; and storing it in a secure manner, which may mean encryption for a corporation like Anheuser-Busch or hidden under a mattress for a one-man micro-brewery.

Unlike the other types of intellectual property that derive much of their protection through registration, what constitutes a trade secret is often a subjective, fact-specific inquiry.

"Ultimately, given the sensitive nature of free-speech concerns, employers faced with these issues should exercise caution and confer with knowledgeable counsel before acting."

MATTHEW B. DAVIS
Marshall, Williams & Gorham, LLP

LOSEE: Intellectual property that is not commonly known to the public, and that the employer takes affirmative steps to keep confidential, is worthy of protection. Often, strong internal confidentiality policies are adequate to achieve such protection. However, where necessary, it may be necessary to have written confidentiality agreements and other restrictive covenants.

Employees who will be developing and executing the unique products and services of the employer may need to sign intellectual property assignment agreements to avoid any doubt as to employer ownership of employee developments.

What issues should business owners consider when starting a succession plan, whether that includes selling the company or passing it down to a family member?

BEAUDOIN: Anytime a business owner is getting ready to start succession planning, he or she should make sure the corporate books and records are in order, including the financial records. Once these are in place, it is recommended that business have a valuation performed. Knowing what the business is worth is vital to any succession planning regardless of whether the business will pass to the next generation or be sold to a third-party.

LOSEE: If you've heard it once, you've heard it a thousand times – Ben Franklin's age-old axiom "an ounce of prevention is worth a pound of cure." In succession planning, we believe you should always treat your business as if you were going to sell it to a stranger, whose due diligence would include a review of the company's books and records.

We've found that often, small businesses take the attitude of, "If it ain't broke, don't fix it." While that axiom rings true, it is not on point in this case. When planning for succession, a business owner should treat the situation "as if" he or she were planning to sell their business and should do so with legal consultation at an early stage of the business. Rather than avoiding your attorney because you associate us with being problem solvers, our experience is that early (and periodic) consultation with your lawyer can help identify opportunities and avoid future problems.

INSIGHTful DISCUSSIONS

Sponsors' Content Distributed By Greater Wilmington Business Journal

DAVIS: An important element of business planning is simply getting started, which is often easier said than done, given the day-to-day demands of running a business; the often painstaking nature of the process; and the tough personal issues that surface, such as the prospect of retirement. Extended delay, though, makes it harder for owners to meet their goals and increases the risk that the business will experience succession-related interruptions.

Once started, owners should identify their personal goals. These considerations may include the owners' income needs, the degree to which they'll remain involved in the business, and how the succession plan might further their legacies and values. Framing these goals should then guide much of the technical aspects of succession planning.

For instance, if the goal is to sell the business to an outsider, then the issue of management succession becomes the buyer's issue. Conversely, if the owners' goals are to have family or employees assume the mantle, then a suitable successor must be identified and groomed.

With a plan in hand, business owners should rest easy knowing they've charted a way forward for not only themselves, but also their families and employees.

WORTMAN: If two or more people own the business, and at least one of the original owners would like to continue with the business, the succession plan should clearly set out the roles of all owners and the method of calculating their compensation. In many cases, heirs may have no desire to be involved in daily management of the business, or the existing owner may have no desire to work with a new owner. Operating agreements (for an LLC) or shareholders' agreements (for corporations) should address business succession, including whether the original owners have the right to receive notice of the sale or intent to transfer the ownership and a right of first refusal. Business owners should also agree on how they will allow the value of the business to be calculated, and a procedure that would allow disputes between owners to be resolved quickly and economically. If a business succession planning is an afterthought to the operating agreement or the shareholders' agreement, it should be very specific and consider the current and future plans of the business.

What common legal mistakes do business owners and executives make that can be avoided?

WORTMAN: The most common mistakes involve well-meaning, casual agreements either internally between owners, with employees, or with other businesses. Although written documentation of these agreements may seem onerous at the time, a clear record of the intent of the parties can save time and money in the future. Many legal conflicts arise because parties come into the arrangement with different expectations.

> "Anytime a business owner is getting ready to start succession planning, he or she should make sure the corporate books and records are in order, including the financial records."

ADAM M. BEAUDOIN
Ward and Smith, P.A.

In the age of electronic communication, email messages should be read carefully before sending. While legally enforceable agreements can be formed over email, an unclear or poorly worded email can be responsible for starting legal conflict. Also, to take advantage of the protection business entities like LLCs and corporations provide, business owners must "respect the corporate form;" file annual reports with the secretary of state; maintain separate financial business accounts; file separate taxes; and hold annual meetings, among other requirements. There is no exception for small or closely held businesses.

Business owners and executives should have a trusted team of advisers, including attorneys and accountants, with whom they can consult if questions arise.

DAVIS: Like medical issues, legal problems are best addressed sooner than later, and left unattended can become more difficult, painful and expensive to cure. Unlike most doctors, attorneys can be reached by phone and email. The point being that owners and executives should consider adopting a preventive approach to identifying and resolving legal issues, rather than waiting until they develop into full-blown problems.

What is something new or coming soon in business law that executives and business owners should be aware of?

DAVIS: There are two developments, both viewed as pro-business, that I have followed with interest as a litigator. The first is proposed federal legislation that would expand federal protection for trade secrets. The so-called Defend Trade Secret Act (DTSA) was passed unanimously by the U.S. Senate earlier this month, and is now pending in the U.S. House of Representatives. The White House has already expressed strong support.

Unlike the three other forms of intellectual property, trade secrets do not currently enjoy strong federal protection. Instead, businesses claiming misappropriation must rely on state courts to maintain a private right of action, which is an outdated framework in today's digital and global economy where trade secrets are commonly stored and shared across state lines and internationally.

The second development is an amendment to the Federal Rules of Civil Procedure regarding the pretrial evidentiary process known as discovery. Before the amendment, relevancy controlled the scope of discovery. Under the amended rule, though, discovery must not only be "relevant," but also "proportional to the needs of the case, considering the importance of the issues at stake in the action, the amount in controversy … ." The hope for businesses is that the revised rule will reduce litigation costs.

LOSEE: The Department of Labor announced in February that it will publish its final rule on a new minimum salary for administratively exempt employees this July. This rule will raise the minimum salary for this exemption substantially and result in many employees losing their eligibility for the exemption.

What is the administrative exemption? The Fair Labor Standards Act assures most employees a minimum wage and overtime pay. A minority of employees are exempt only if they receive a threshold salary and have qualifying "white collar" duties. The administrative white collar exemption requires that an employee perform non-manual duties relating to management or business operations of the employer or its customers and be paid at least $455 a week. The upcoming rule change will almost double this pay threshold to $970 a week.

In light of the change, we recommend that all employers review pay practices and change them as necessary to stay ahead of a government audit. I wrote more about this in April for the Business Journal's Insights, and you can find my article online.