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# Reporter

## Business & Corporate Law

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### **Business Topics: Part 2** **Key Issues to Consider in the Operation of Your Business**

In these times, business is often conducted at breakneck speeds. Along the way, even business owners with the best intentions sometimes overlook, or don't have the time to address, important legal matters that can enhance the operation of their companies and/or provide important legal protections. Below are key issues that touch upon various aspects of your business, including employee matters, corporate records, intellectual property, and environmental and leasing matters. Addressing these issues in advance based on the needs of your business potentially can shield your businesses in these litigious times and can enhance the value of your company.

**Manage your partners.** Whether the form of your business is a corporation, a limited liability company or a partnership, if your business has more than one owner, it is important to make sure that your fellow shareholders, members or partners are all on board with respect to the management of the business and any decisions regarding a major transaction. Although it is not possible to ensure that your partners share the same viewpoint with respect to management and other matters, it is useful to manage the relationships of the partners by using a buy-sell agreement, shareholders agreement or operating agreement (if your company is a limited liability company). These agreements can guide your relationships by imposing restrictions on the transferability of the shares and providing for other management and decision-making mechanisms. Some of the restrictions on transferability of the ownership interests in

a business include: (1) rights of first refusal (in favor of the company and/or the other owners), (2) repurchase rights upon certain events (e.g., upon the death, disability, divorce or bankruptcy of an owner or upon a "cause" event with respect to an owner (such as fraud, misconduct, drinking habitually on business hours, etc.)), (3) drag-along rights (being able to force your partners to sell their ownership interests if you are selling yours), and (4) tag-along rights (being able to sell your ownership interests if your partners are selling theirs).

**Document your relationships.** Depending on the industry you are in, some or all of your business relationships may not be documented—whether those relationships are with your suppliers, customers, contractors or others. It is important, however, to document those relationships to the extent practical. Doing so will help preserve the value in your company and support the due diligence review of your business that any investor likely will undertake.

**Protect your intellectual property (IP).** It is critical to protect your company's IP (patents, copyrights, trademarks and trade secrets). The actions you should take depend on the type of IP that is important to your business. For example, you may need to file for a patent, or register a trademark or copyright. To protect trade secrets, you want to make sure that your trade secrets are shared only with people who have a "need to know" and who sign a non-disclosure agreement. Your employees and contractors also

should sign an inventions or “work for hire” agreement to make sure that the sole owner of the IP is your company and that employees or contractors do not acquire rights in the IP. In addition, you must monitor your company’s IP and the IP of others to ensure that your company is not infringing on others’ IP rights and that others are not infringing on your company’s IP rights, and, if there is potential infringement, to evaluate whether litigation is the proper next step to take.

**Maintain employee relations.** Employee lawsuits take away time, energy and other resources, preventing management from focusing on the growth of the business. That is why it is important to make sure that employees are being paid properly, that proper payroll deductions are being taken, and that withholding taxes are being paid and returns filed. It is also important to maintain an updated employee handbook that contains policies and procedures to which all employees can refer. These policies include sexual harassment, discrimination, retaliation, disability and medical leave, all of which involve complex laws and regulations.

**Review your lease and environmental matters.** Any business should continually evaluate its real estate needs and its leases. It is important to ensure that the lease for your business (1) is appropriate for the future needs of the business, (2) is assignable in the context of a merger or sale, and (3) has acceptable terms such as rent amount and term. In addition, a myriad of environmental and zoning laws may apply to your business, and it is necessary from time to time to evaluate these laws to determine their impact on your business.

**Protect your customers—digitally.** A lot of business these days is done online, or at least by e-mail. Even if you only collect customer information and store it on a third-party offsite server, your business may be subject to a number of state, federal and international regulations, including the “Red Flags Rule” recently enacted by the Federal Trade Commission. For example, in California, businesses are required to implement and maintain security procedures and practices, as well as notify their customers if there has been a

breach in security of the system. Also, if your company has a website, at the minimum the website should have a privacy policy, terms and conditions, and a copyright/DMCA policy.

**Implement a document retention/destruction policy (DRDP).** A DRDP is an essential feature of a corporate compliance program for companies of any size, and one that is mandated by many statutory and regulatory requirements. An effective DRDP will help eliminate confusion and second-guessing when it comes to determining what documents to retain, and when to destroy them, by (1) providing a system for complying with document retention laws, (2) making documents more conveniently accessible, and (3) providing a mechanism for routinely destroying documents that are either not related to your business, duplicative or, most importantly, outdated. If even the threat of litigation arises, you should consult an attorney to determine how to comply with your company’s DRDP and how to instruct your employees on maintaining and not destroying relevant documents. Of course, like any policy, it is important to enforce your company’s DRDP — your failure to do so can be used in a bad-faith document destruction claim against you.

**Use your outside counsel as your in-house attorney.** Unless you need to hire a full-time attorney on your staff, it is critical to partner with a good business lawyer who will be familiar with your business and available to answer your legal questions, whether big or small. Your outside counsel essentially can act as your in-house attorney, and he or she can help you spot issues and risks and prevent them from becoming large problems.

Addressing these and other issues will not only enhance the value of your company, but also will offer protections in the event your company is threatened with a lawsuit.

The first part of this article, published in the December 2009 issue, addressed key issues to consider in anticipation of a major transaction.

*If you have any questions regarding this bulletin, please contact Ara A. Babaian at (310) 281-6344 or ababaian@ecjlaw.com. If one of your colleagues would like to be a part of the Business & Corporate Law Reporter mailing list, or if you would like to receive copies electronically, please contact Brandi Franzman at (310) 281-6328 or bfranzman@ecjlaw.com.*