

LAWYERS' COMMITTEE FOR

**CIVIL
RIGHTS**

OF THE SAN FRANCISCO BAY AREA

LEGAL SERVICES FOR ENTREPRENEURS

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BUSINESS LAW BASICS

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DISCLAIMER

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OVERVIEW

1. Choosing a Business Entity
2. Licensing and Permits
3. Contracts and Commercial Leases
4. Employment
5. Intellectual Property
6. General Considerations and Resources

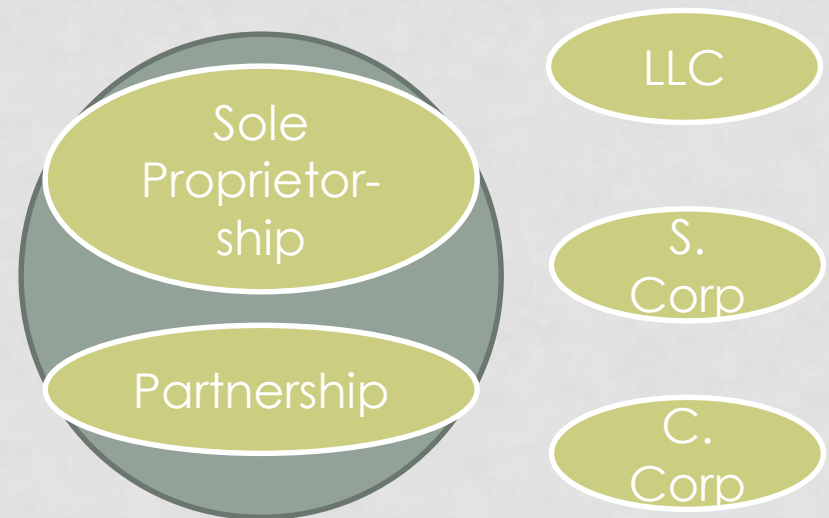
CHOOSING A BUSINESS ENTITY

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WHY DO I NEED A BUSINESS ENTITY AND HOW DO I CHOOSE?

- **Liability** – protecting your personal assets
- **Management and Shared Ownership** – determining who gets what in the organization
- **Taxes and Fees** – managing taxes and accounting

Entity Types



ENTITY TYPES – BREAKDOWN

Limited Liability Company (LLC)

- Unlimited members
- Members or managers manage
- Limited liability (*more on this later*)
- Fewer legal formalities

C-Corporation

- Unlimited shareholders
- Board of directors manages
- Limited liability
- Easy to expand
- Double taxation

S-Corporation

- Up to 100 shareholders
- Board of directors manages
- Limited liability
- No foreign shareholders
- Shareholders must be natural persons (w/ some exceptions)
- Only one class of stock allowed

ENTITY TYPES – WEIGH OPTIONS

C-Corp

- Generally, if the entity will receive investor-financing (VC-funding)
- Usually inappropriate for a cash-producing business

LLC

- Flexible corporate structure
- Favorable taxation
- Single-member LLC ignored for federal income tax

S-Corp

- Less flexible corporate structure
- Favorable taxation

LIMITED LIABILITY - HOW THE ENTITY PROTECTS YOU

Liability limited *to the assets in the business*

- Business creditors cannot reach personal assets of owners
- Lawsuits cannot reach personal assets of owners

Limited Liability	S-Corp or C-Corp, LLC
No Limited Liability	Sole Proprietorship, Partnership

- *Note: This occurs only when you observe corporate “formalities” and are careful to respect the company as separate from yourself (if you don’t respect it, the creditors won’t have to either)*

LIMITED LIABILITY – IMPORTANT TIPS

Keep business and personal assets separate

- Sign contracts as the entity, not as an individual
- Maintain good records of board/manager decisions
- Pay company liabilities only from company funds and document all money in and out. **NO “JUST-IN-TIME” FINANCING.**

Consider insurance instead (or in addition)

- Obtain insurance through a broker or trade association
- Understand exceptions from coverage
- Obtain the correct type and an adequate amount of coverage for your business

OWNERSHIP AND MANAGEMENT STRUCTURE – BASICS

LLCs

- Managers usually have decision-making power
- Members have ownership (but can also manage directly)

Corporations

- Directors and officers have decision-making power
- Stockholders have ownership

Partnerships

- Each partner usually has unlimited management power and unlimited liability (**ALMOST NEVER A GOOD CHOICE**)

OWNERSHIP AND MANAGEMENT STRUCTURE – IMPORTANT TIPS

Clarify Ownership in Formal Legal Documents

- Who owns what percentage of the company? Will it change over time? How is it determined?

Clarify Incentives / Vesting in Formal Legal Documents

- Use % ownership to bring on new expertise or resources; set milestones to be reached
- Stockholder / member contributes time or resources before receiving full benefits of ownership

Clarify Management in Formal Legal Documents

- Put down on paper who is responsible for decision-making in the company – including who has the power to change management. Top management should meet regularly.

ENTITY CONSIDERATIONS: FEES & TAXES

- Initial fee + maintenance fees
- Annual tax requirements

	Sole Proprietorship	Limited Liability Company (LLC)	“C” Corporation	“S” Corporation	
Filing Fees (one time)	\$47 for fictitious name statement (SF County)	\$70 for SOS filing	\$100 for SOS filing	\$100 for SOS filing	
Statement of Information (yearly)	None	\$10 (\$20 every other year)	\$25	\$25	
State Franchise Taxes (yearly)	None	Minimum of \$800 (+LLC fee if revenues exceed \$250k)	Minimum of \$800* (actual tax is 8.84% of net income)	Minimum of \$800* (actual tax is 1.5% of net income)	

**Tax waived first year as long as 1.5% of net income is less than or equal to \$800*

ENTITY CONSIDERATIONS: FEES & TAXES

	Sole Proprietorship Single Member LLC	LLC	"C" Corporation	"S" Corporation
Taxation	Net profit is computed on Schedule C and is reported as income on the owner's Form 1040.	Company income and expenses flow through to the members.	C corporation pays tax on profits. If shareholders take profits, the distributions are taxable dividends.	Generally taxed like LLC.
Tax Rate	Taxed at individual level.	Taxed at individual member level	35% federal (with slight increase for very high taxable income)	Generally taxed at individual shareholder level.
Use of Tax Credits/ Losses	Used to offset individual's taxes.	Passed through to members (losses deductible to the extent of basis).	Used to offset corporate taxes.	Generally passed through to shareholders.
Distribution to Owners	Nontaxable	Generally not taxable	Not deductible by corporation. Generally ordinary income to shareholder.	Generally not taxable

ENTITY CONSIDERATIONS: FEES & TAXES

	Sole Proprietorship/Sin- gle-Member LLC	LLC	“C” Corporation	“S” Corporation
Wages and Self- Employment (SE) Taxes	Owner subject to SE tax of 15.3% of net earnings. Computed on Schedule SE and reported on owner's tax return.	Member's share of business income is subject to SE tax. Passive items are passed through to members.	Shareholders who perform services for corporation are treated as employees. Wages of all corporate employees are subject to payroll tax and withholdings. Other distributions not subject to SE tax.	Same as for “C” corporation. Wages must be reasonable. Additional profits are passed through to the shareholder, but are not subject to SE tax.
Fringe Benefits	Amounts paid on behalf of owner are not deductible.	Generally amounts paid on behalf of members must be included in members' income.	Fringe benefits to shareholder-employees treated the same to other employees.	Same as for “C” corporation, except must be included in wages of employee-shareholders that own more than 2% of the corporation.

ENTITY CONSIDERATIONS: FEES & TAXES

C-Corp has “Double Taxation”: taxed once on net business income + taxed again on shareholder dividends

- **Avoid, unless:** no plans to declare dividends (*often when those who plan to make money from the biz are working for the biz, and are not passive shareholders*) or otherwise need C-Corp

Double Taxation

C-Corp

No Double Taxation
 (“pass through” taxation)

Sole Proprietorship,
Partnership, LLC, S-Corp

**BOTTOM LINE: Tax analysis is very fact-specific.
Ask an accountant or tax attorney about your business.**

LICENSING AND PERMITS

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LICENSING AND PERMITS: WHAT YOU NEED

Local

- Zoning
- Fictitious Business Name (DBA)
- Business Tax Registration Certificate
- Other Permits & Licenses

Federal

- Business Tax
- Withholding Employee taxes

State

- Seller's permit
- Business qualification
- Withholding, insurance, taxes
- Employer Identification Number (EIN)
- Worker's comp
- Licenses

For a list of required permits for your specific business visit the
California Governor's Office of Economic Development:
<http://www.calgold.ca.gov/>

LICENSING AND PERMITS: TIPS

- **Get organized early** – finding out you owe taxes may prevent your company from moving forward
- **Hire an accountant/payroll service** to help you stay on top of filings, tax payments, and payroll
- **Keep permits and qualifications current** – keep your business operational and legal
- **“Doing business” out-of-state** – if you have employees, offices, sales, or inventory in different states, you may need to qualify to do business and to pay taxes in those states / jurisdictions

CONTRACTS

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LEGAL TIPS FOR A HEALTHY BUSINESS

(to keep your business out of court)

Review:

- **Keep good records**
 - Set up a recordkeeping system for all payments to and from your business
- **Licensing and permits**
 - Local, state, and federal
- **Use formal contracts**
 - With all the people you do business with
(doesn't have to be complicated, just clear)

CONTRACT TIPS TO PROTECT YOUR BUSINESS

A contract is a promise, or a set of promises, that are enforceable in court.

A contract can be oral or written, but **it is always a best practice to have business contracts in writing**

CONTRACT TIPS TO PROTECT YOUR BUSINESS

- **Why is written preferred?**

- Easier to prove the contents of a written contract.
- Various people may review a written contract
- It is clear that the people involved *intended* to enter into a contract when the contract is written
- Writing it down can clarify the agreement (or highlight any disagreement while you can fix it).
- Some contracts must be written (e.g. real property leases and commission contracts).

CONTRACT TERMS

- Does the contract clearly describe your and the other party's **obligations**?
- Does the contract clearly establish **payment terms**?
- Does the contract clearly establish **time frames**?
- Does the contract provide for **ways to change** / terminate the contract?
- Does it provide for **dispute resolution** / liability burden?
- **Can you live with this contract?**



CONTRACT TIPS TO KEEP YOUR BUSINESS OUT OF COURT

Use Formal Contracts

- Clients and vendors
 - sales contracts
- Employees and independent contractors
 - offer letters, employment agreements, nondisclosure agreements
- Potential partners
 - non-disclosure agreements



Keep Good Records

- Performance of contracts
- Employee performance

COMMERCIAL LEASES: TOP 10 THINGS TO REMEMBER

1. Write it down!
2. Read and negotiate!
3. Know what the rent is (including any shared building expenses)
4. Understand the term and any options
5. Know the condition of the premises
6. Know who pays for improvements
7. Understand who fixes what
8. Get and keep insurance
9. Know if you can assign/sublease
10. Get notice and cure period for defaults

COMMERCIAL LEASE CONSIDERATIONS

Terms Most Important to Tenants

- Annual Increase in Rent
- Ability to Assign Lease, or Sublet
- Option to Renew
- Rent Abatement for Interruption in Use
- Broad “Permitted Use” Clause
- Maintenance Obligations/tenant charges for building expenses
- Liability for Non-Compliance With Laws
- Hazardous Waste Representation by Landlord
- Alterations/Surrender Obligations
- Specific Needs of Business

* ALL terms are negotiable if landlord is willing*

EMPLOYMENT

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EMPLOYMENT: IMPORTANT TIPS

- **Get Everything on Paper, Even if it Seems Unnecessary**
- **Use a Payroll/Compliance Service**
- **Use Offer Letters**
 - Include “at will” language
 - State:
 - whether the employee is salaried or hourly
 - compensation and benefits (vacations)
 - Include non-disclosure agreements and/or invention assignment agreements
 - ✓ Note: non-compete agreements are generally not valid in CA after termination of employment (important exception for person selling a business)
 - Labor Code Section 2810.5 Notice
- **Consider Employee Handbook (not a DIY project)**

INDEPENDENT CONTRACTORS ARE NOT EMPLOYEES

Independent
Contractor

Differences

Employee

Not owed benefits, leave, or
overtime

Owed benefits, leave, &
overtime.

Independent
Contractor

Factors

Employee

Less control or supervision by
employer; work off-site

More control or supervision by
employer; work on site

Worker's services are less central to
employer's business

Worker's services are more central to
employer's business

Paid by project

Paid by time worked

IS THAT WORKER REALLY AN INDEPENDENT CONTRACTOR?

- **IMPORTANT – EDD/IRS/DOL are going after employers who classify employees as independent contractors—don't be one of them**
- **Hiring Independent Contractors**
 - To perform a specific job
 - Do not hire an independent contractor on a permanent or “at will” basis
 - Pay by the job
 - Do not supervise or control an independent contractor
 - Give a timeframe for services to be completed
 - Do not say when/where/how a contractor works
 - Contractors may hire assistants to do the work
 - Hire contractors for work that is not part of the day-to-day operation of the business
 - Be clear that independent contractor is responsible for own liability, worker's comp, taxes, and benefits

BOTTOM LINE: the IRS/DOL/EDD have the last word. Be careful.

EMPLOYEE TREATMENT: MINIMUM WAGE & OVERTIME

- **Minimum Wage For Hourly Employees:**

	CA Min Wage	SF Min Wage	Oakland Min Wage
Hourly	\$10/hr (\$10.5/hour for more than 25 EEs), increasing annually through 2023	\$14/hr (\$15 after 7/1/18, then increasing annually with inflation)	\$12.86/hr (increasing annually with inflation)

EMPLOYEES CANNOT WAIVE OR SIGN AWAY RIGHTS TO A MINIMUM WAGE
TIPS CANNOT COUNT TOWARD MINIMUM WAGE

- **Overtime Rates For Hourly Employees:**

Situation	Pay Rate
Over 8 hours a day	1.5x hourly rate per overtime hour
Over 40 hours a week	1.5x hourly rate per overtime hour
7 th consecutive day worked	1.5x hourly rate per hour on 7 th day
Over 12 hours in 1 day	2x hourly rate per overtime hour
Over 8 hours on 7 th consecutive day	2x hourly rate per overtime hour that day

PAID SICK LEAVE

- Accrues at the rate of 1 hour per every 30 hours worked. Paid at the employee's regular wage rate
- Use can be limited to 24 hours each year of employment. It is eligible to be carried over but can be capped at 48 hours.
- Employers can instead provide at least 24 hours sick leave available at the beginning of each year.
- Paid sick leave is required to be provided to all employees after their 90th day of employment.

<http://www.dir.ca.gov/dlse/ab1522.html>

EMPLOYEE TREATMENT: HEALTH CARE

SF Health Care Security Ordinance

- Depending on company size, employers must spend a minimum amount on health care for each employee who works 10+ hours per week

# of Employees	Requirement
100+ employees	\$2.48/hr.
20-99 employees	\$1.65/hr.
19 or less employees	Not Applicable; exempt from coverage

Learn More: <http://sfgsa.org/index.aspx?page=418>

EMPLOYEE TREATMENT: WORKERS' COMP

California requires all businesses to carry workers' compensation insurance for their employees

Usually does not apply to:

- Independent contractors
- Volunteers
- Business partners
- Household employees who work less than 52 hours or earned less than \$100 in the 90 calendar days before the injury

Benefits of Workers Comp:

- For workers: faster, standardized process
- For employers: reduces liability for workplace injuries

EMPLOYMENT: FIRING

BEFORE Firing / Layoffs / Closing Business

- Keep record of employee performance
- Make sure you have a documented reason for firing

WHEN Firing / Layoffs / Closing Business

- Pay final wages on time
- Review employment agreement and pay all amounts due
- Remind employee to keep employer trade secrets and proprietary information confidential
- Consider having employee sign a release (supported by some kind of severance benefit that the employee did not have a right to get otherwise)

EMPLOYMENT & IMMIGRATION

- **Employer *must* complete Form I-9 (Employment Eligibility Verification) for all employees**
 - File within **3 days** of beginning employment
 - Keep records for **3 years** after date of hire or **1 year** after employment is terminated (whichever is later)
 - If employee's work authorization has expiration date, employer must update I-9 when authorization expires

- ✓ Tip! Employer **may** ask generally if applicant has legal right to work in the U.S., but **cannot** ask if he/she is a U.S. Citizen, or has a "green card"

EMPLOYMENT & IMMIGRATION

- For more information about I-9 completion:
<http://www.uscis.gov/USCIS/Resources/E3en.pdf>
- **WHEN IN DOUBT** – talk to an immigration attorney

INTELLECTUAL PROPERTY

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INTELLECTUAL PROPERTY

Protect your name, brand, company information, design or invention with:

- **Trademarks** (business names, logos, slogans)
- **Copyright** (artistic creations / software code)
- **Trade Secrets** (company secrets)
- **Patents** (inventions)



TRADEMARKS

- **Available for:** your brand—a name, phrase, or design used to identify the source of goods or services (e.g., Mary's Pizza Shack, McDonalds' "I'm lovin it," Nike's "swoosh" logo)
- **Not available for:** generic or descriptive marks (e.g., "Grocery Store," "Sugar Cookies")
- **Protection:** No one else can use your mark in your field of business so long as you continue to use it (this is much more limited if you do not obtain federal registration)
- **Exceptions:** Fair Use, naming competitors

OBTAINING AND ENFORCING TRADEMARKS

Obtaining TM Protection

- Check eligibility: Conduct a trademark search for FREE at www.uspto.gov
- Also consider checking for an available domain name
- Registration: \$275 if filed online; can use ® symbol
- Consult with an attorney, if possible (your free search will not be reliable)

Enforcing Trademarks

- Cease and Desist Letter (first stop)
- Litigation (if necessary)



AVOIDING TRADEMARK INFRINGEMENT

Beware using trademarked or copyrighted artwork on your webpage, logos, or other materials

- Electronic tags on images allow trademark holders to track unauthorized uses of images

For free artwork, consider using Creative Commons

Go to www.flickr.com/creativecommons for images and licensing information

For low-cost artwork, consider using stock images (with license)



COPYRIGHT

Available for: a work of original authorship (e.g., book, movie, art, music, or software code)

Not available for: names, title, short phrases, ideas not yet written/painted/created

Protection: Work generally protected for the life of creator plus 70 yrs.

- Exception: Fair Use (for non-commercial purposes, educational uses, small excerpts)
- Registering: © symbol may be used, \$35 if filed online, www.copyright.gov



TRADE SECRETS

Available for: confidential financial, business, technical, economic or engineering information (e.g. client lists, recipes, algorithms) if:

- information is **economically valuable because it is secret**
- It is not generally known, and
- You take reasonable measures to keep it secret

Not available for: public information

Protect by:

- Keeping your information secret
- Using a nondisclosure agreements before disclosing confidential information

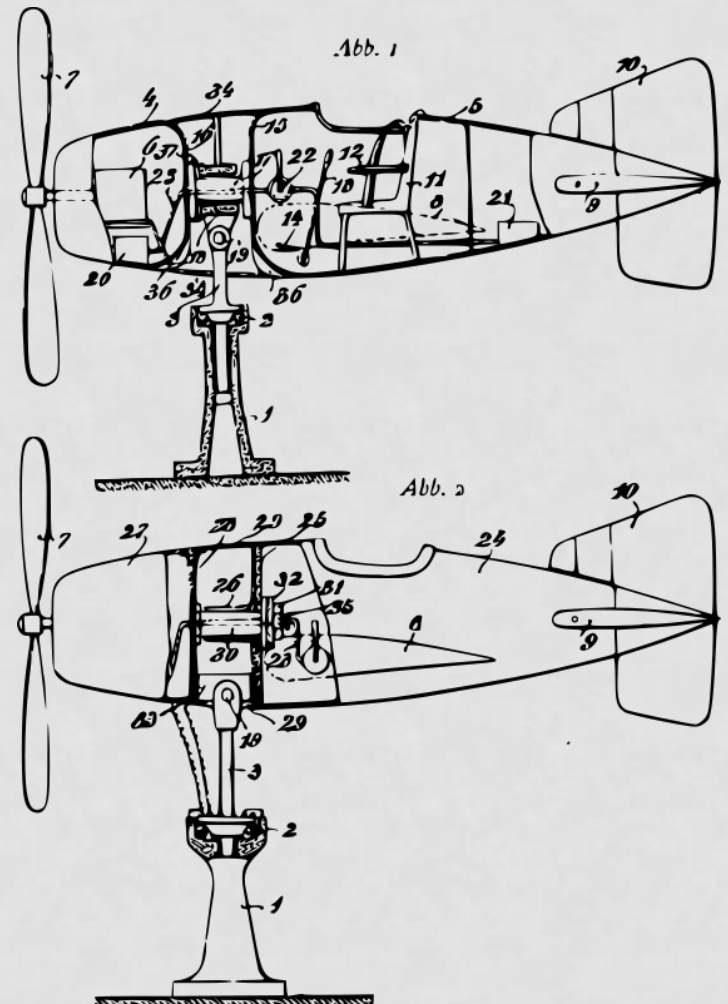
PATENTS

Available for: new and non-obvious inventions (e.g. machines, processes, medicines)

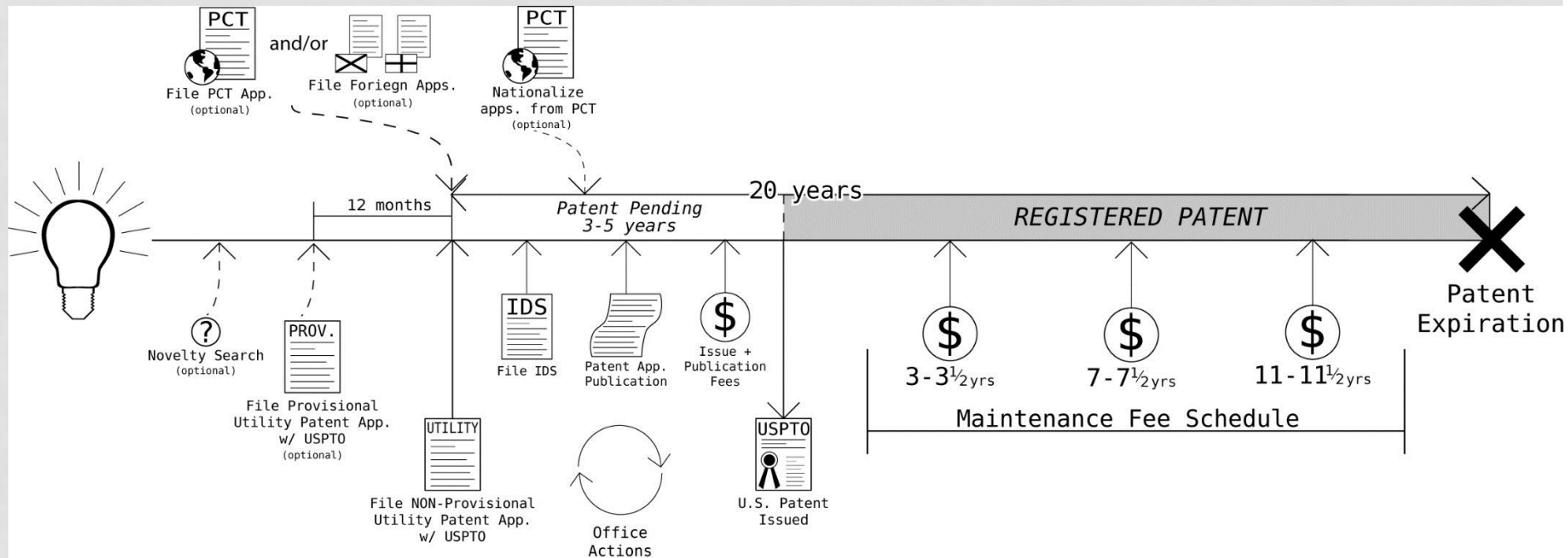
Not available for: obvious inventions / inventions previously published

Protection: you can prevent anyone else from practicing or using your invention for 20 years, BUT you must make your invention public

NOTE: Patent law is extremely complex. If you are considering filing a patent, consult an attorney.



PATENT TIMELINE



U.S. Filing Fees: \$2,000-\$15,000
U.S. Maintenance Fees: \$3,500-\$7,000

DECIDING WHETHER TO PURSUE A PATENT

Considerations

Costs

- Time
- Money
- Method made public
- Cost of litigation to enforce patent

Benefits

- Is there a real risk of losing business from copycats?
- Does the risk outweigh the costs?

Alternatives

Filing a Provisional Application

- Much lower cost
- Start the application process to demonstrate that you had the idea first
- 1 year to figure out if you would benefit from a patent
 - Locate funding for the patent
 - Market to see if anyone would be interested in licensing your invention

Trade Secret

- Can you keep it secret?

IP – GENERAL TIPS

Branding – consider your brand, logo and domain name early and file / register for these early on. Be aware of others who may be using your name

Ownership – make sure all service providers assign what they create to your company

Company policies – have clear guidelines on use of company information and resources

Internet – protect what is on the company website

THANK YOU FOR COMING!

Legal Services for Entrepreneurs (LSE) provides free legal assistance to low-income entrepreneurs and entrepreneurs who invest in low-income neighborhoods.



For more information:

415-543-9444 ext. 217

<http://lccr.com/lse>

OTHER RESOURCES

- **Nolo:** www.nolo.com (small business legal guide)
- ***ABA Legal Guide for Small Business***
- **U.S. Patent & Trademark Office:** www.uspto.gov
- **U.S. Copyright Office:** <http://www.copyright.gov/>
- **CA Governor's Office of Economic Development:**
<http://www.calgold.ca.gov/> (licensing information)
- **Creative Commons:**
www.flickr.com/creativecommons (artwork with few copyright restrictions)
- **sf.license123.com** – find the permits you need

OTHER RESOURCES

- **California Minimum Wage:**

https://www.dir.ca.gov/dlse/faq_minimumwage.htm

- **San Francisco Minimum Wage:**

<http://sfgov.org/olse/minimum-wage-ordinance-mwo>

- **Oakland Minimum Wage:**

<http://www2.oaklandnet.com/government/o/CityAdministration/d/MinimumWage/index.htm>

OTHER RESOURCES (CONT.)

Entity Formation

Minority Business Certification

- 51% ownership by socially or economically disadvantaged individuals
- California Unified Certification Program:
www.californiaucp.com

Employment

Minimum wage

- San Francisco 415-703-5444
DLSE Hotline
- Oakland 510-622-2660
DLSE Hotline

Employment General FAQs

- [California Department of Industrial Relations:](http://www.dir.ca.gov/)
[http://www.dir.ca.gov./](http://www.dir.ca.gov/)