



FARALLON LAW GROUP LLP
459 FULTON STREET, SUITE 102
SAN FRANCISCO CA 94102

FARALLON LAW GROUP NEWSLETTER

(JULY, 2010)

Avoid Expensive Litigation! Eight Tips For Every Small Business.

In the current economic climate, we understand that often the best way to assist a small-business client is to work proactively to prevent litigation whenever possible. Of course, if your small business already finds itself on the verge of suing or being sued, FLG's litigators are ready to assist you. But for those small businesses forward-thinking (or lucky) enough not to be facing a court case, or which have already been through litigation and wish to avoid it the next time around, here are some tips to stay out of court:

- **Tip 1: Create the appropriate legal entity for your business.** Your business can take one of several legal forms: a corporation, a partnership (general or limited), a limited liability corporation (known as an LLC), or a sole proprietorship. Most small businesses become either an LLC or a sole proprietorship. An LLC is relatively easy to create and flexible to operate. As an independent entity, an LLC creates a liability buffer: Normally, a member's legal responsibility for the business activities of the LLC will be limited. The downside is that there are strict recordkeeping, tax and reporting requirements. A sole proprietorship has fewer creation, reporting and tax requirements, but lacks the same buffer. The law sees no difference between a sole proprietor and his/her business. Choose the appropriate business form to minimize regulatory cost as well as to maximize legal protection for you and your business.
- **Tip 2: Make sure your business name and mark are unique.** There is little

worse than to realize that the name of your business and/or the brand of your goods and services is already in use and registered as a trademark to a competitor. If you use the same or a substantially similar name or mark as an existing business, you run the risk of local and state regulation violations, as well as federal trademark issues. Before committing resources to a particular business name, research it. We highly recommend using a reputable search service to conduct a thorough review of federal and state databases, internet domain names and sites, trade periodicals and other sources.

- **Tip 3: Keep good relations with investors and lenders, in good times and bad.** Always keep an open communication channel with your business investors. Investors should receive candid, periodic updates about business performance. By keeping an open and regular communication channel with your business investors, you leverage their skills while avoiding conflict (and lawsuits) arising from poor disclosure of business developments.
- **Tip 4: Proactively manage your relationships with employees and contractors.** For small businesses with employees and/or independent contractors, there are many legal requirements which extend beyond the scope of this discussion. But the surest way to avoid problems with employees is to have written offer letters and create an employee handbook. The handbook should cover such topics as hours, pay and benefits, respectful treatment of co-workers, workplace safety, use of company

This Newsletter is intended as a general guide to law issues and developments. It does not contain a general legal analysis or constitute a legal opinion of Farallon Law Group LLP or any member of the firm on the legal issues described. It is recommended that readers not rely on this general guide in structuring individual transactions but that professional advice be sought in connection with individual transactions.

property, performance reviews, protection of confidential information, discipline and termination. For independent contractors, a written agreement is essential, and should confirm the contractor's status as an independent contractor rather than an employee, and address confidentiality and intellectual property ownership. Compensation, deadlines and duties should be made clear. The agreement should reserve to the contractor control over the manner of completing job tasks- this is important to avoid the contractor's status subsequently being called into question by the IRS or labor authorities (see our April 2010 Newsletter titled "Independent Contractor vs. Employee"). Clear expectations reduce the chance of misunderstandings and lawsuits for lost wages, a missed promotion, or dismissal.

➤ **Tip 5: Schedule your tax and other regulatory obligations.** What tax and other regulatory obligations are incurred by a business is largely a function of what kind of legal entity the business has formed, the business activities and whether the business has employees. Avoid expensive penalties and fines by accurately calculating, scheduling, paying and reporting all taxes on time.

➤ **Tip 6: When selling your product or service, contract in writing, and take special care that your advertising is not deceptive.** Nothing creates upset customers, competitors and regulators more than if you sell a product or service differently from the way you advertise it. Fraudulent and deceptive trade practices are prohibited. Your business advertising should include only true and verifiable information about your product or service, including accurate photos, endorsements, prices, guarantees and descriptions of what is included. The cardinal rule to avoid most conflicts with clients is to enter into a written contract whenever feasible. By clearly laying out in writing what your clients can expect, by providing them with the product or service advertised at the promised price and level of quality, and by

working with clients informally to resolve their customer service concerns, you will earn their respect and continued business, and avoid costly legal disputes.

➤ **Tip 7: Don't Litigate, Mediate!**

If disputes do arise, consider using alternative dispute resolution (known as "ADR") services to resolve them. Many legal disputes lend themselves to resolution by a trained "neutral"—usually a former judge or experienced lawyer. Mediation is a common form of ADR., during which an agreed-upon neutral hears both sides' arguments, and then tries to bring the two sides closer together based on a practical assessment of the case. Most mediated disputes settle, either at the mediation, or at some point later based on the settlement groundwork laid during the mediation. This track record makes ADR a good investment—and often much less costly than going to court.

➤ **Tip 8: Consider small claims court for small disputes.** If you cannot avoid litigation, and your dispute concerns less than \$7,500 (\$5,000 in the case of corporations or other business entities), or you are willing to waive any amount above that limit, consider small claims court. It is within your county Superior Court, and often has its own staff and self-help center. No lawyers are permitted. You represent yourself or your business and support your side of the case with testimony and documents. The presentations to the judge are informal, with questions from the judge and answers from the parties. A decision is rendered after a short hearing. This manner of resolution is quick and cost-effective -- the only charges are the case filing and service fees. The only significant downside is that there is no appeal.

Observe these litigation-avoidance and management tips to preserve your limited resources for running and growing your business rather than fighting in court.

Please feel free to contact Ceide Zapparoni, David Lavine, or Michelle Reed at (415) 255-2450 if you have any questions or concerns about litigation avoidance.