



## Choosing a Business Entity

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## Key Considerations

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- Number and types of owners
- Flexibility with respect to management, distributions and allocations, voting
- Transferability
- Taxation
- Personal Liability

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## Sole proprietorship

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- Single owner
- No state filing required
- Dissolves if cease doing business or upon death of sole proprietor
- No personal liability protection
- No separate taxable entity

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## Partnership

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- Two or more owners
- No state filing required; formed by agreement
- Dissolves upon death or withdrawal of any partner, unless otherwise specified
- No personal liability protection
- No separate taxable entity

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## Limited Partnership

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- Two or more owners
- Formed by filing with the state
- Survives death or withdrawal of a partner
- At least one general partner has no liability protection
- Limited partner cannot participate in management of the business
- Files taxes as a separate entity

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## Corporations

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- One or more owners
- Formed by filing Articles of Incorporation with the state
- Existence can be perpetual
- Shareholders shielded from personal liability
- Shares are transferable subject to shareholder agreements, IRS restrictions & securities laws

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## Corporations: Formation and Formalities

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- Formed by filing Articles of Incorporation with Secretary of State
- Bylaws enacted
- Annual meetings of shareholders required
- Annual meetings of directors required
- Annual filing with the state required

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## Corporations: Management

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- Managed by Board of Directors who are elected by the shareholders; directors are not agents
- Operated by Officers who are selected by the Board
- Shareholders are not agents of the corp; do not manage the business
- Most states require at least a President (or CEO) and a Secretary

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## C Corporation v. S Corporation

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- "S Election" filed with the IRS
- C Corporation is taxed at the entity level; shareholders taxed on dividends
- S Corporation is not taxed at the entity level; income/losses passed through to shareholders
- Shares of an S Corp cannot be held by another corporation, a non-resident alien or certain kinds of trusts under IRS regulations
- S corporation can not have more than 100 shareholders

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### C Corporation v. S Corporation (Cont.)

- S Corporation can only have one class of shares, but can have voting and non-voting shares
- S Corporations do not allow special allocations of income and losses; must be pro rate based on shares

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### Limited Liability Company

- One or more owners
- Formed by filing with the state
- Duration determined by organizing documents
- Owners shielded from personal liability
- No federal tax at entity level, unless election made
- Transferable interest, subject to consent of other owners, securities restrictions

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### LLCs: Formation and Formalities

- Formed by filing Certificate of Formation with Secretary of State
- Operating Agreement – recommended but not required
- Owners are “members”
- No annual meetings required
- Annual state filing

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## LLCs: Management

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- Flexibility in determining management
- Member-managed or Manager-Managed

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## Limited Liability: Piercing the veil

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- Liable only to the extent of ownership except:
  - For your own acts or guarantees
  - Underfunded; inadequate assets to cover liabilities
  - Entity used to advance personal interests
  - Entity used to perpetrate a fraud

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## Maintaining Limited Liability

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- Formalities
- Separation of personal and business affairs; No commingling funds, assets
- Make it clear when acting on behalf of entity and in what capacity
- Always use exact company name, including "LLC," "Inc.," "Incorporated," etc. (or register a trade name) on contracts, business cards, letterhead, signs ...

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## Trademarks

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- Trademark rights allow the owner of a mark to exclude others from using a confusingly similar mark for the same or similar goods or services

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## Trademarks

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- What is a trademark?
  - Word, symbol, slogan, tagline, product feature, character (Pillsbury Doughboy®), color, sound (NBC chimes), scent, product shade (Coca-Cola® bottle) and design, trade dress ("look and feel")
  - Source identifier - identifies and distinguishes the goods and services of its owner from those of others.
  - Represents goodwill and reputation

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## Trademarks

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- What isn't a trademark?
  - Generic terms - a common word used to identify a product or service. SHOES for footwear.
  - Methods and processes
  - Trade name, corporate name - names the business, while trademarks tell where goods or services come from; not necessarily trademarks (but can be)

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## Trademarks

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- Selecting a protectible trademark
  - Mark availability
  - Strength of mark
    - Fanciful, coined marks: KODAK for cameras and film; XEROX for photocopying equipment
    - Arbitrary marks: APPLE computer
    - Suggestive marks: COPPERTONE for suntan oil; HEARTWISE for low-fat foods
    - Descriptive: EASYLOAD for tape recorders; QUARTER POUNDER for hamburgers
    - Generic: SHOES for footwear

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## Trademarks

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- How do you acquire rights in mark?
  - Use of the mark in commerce
  - Sole and exclusive use for the goods and services
  - Registration not required
  - TM or SM symbols

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## Trademarks

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- Registration
  - State v. Federal
  - Why register?
    - Notice to others
    - Federal registration confers nationwide rights
    - Intent to use
    - Presumption of ownership and validity
    - Use of ® symbol

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## Trademarks

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- Proper use of trademarks
  - As adjectives followed by a noun
    - CLOROX bleach
    - KODAK brand camera
- Avoiding infringement
  - Clearance searches
  - Use of others marks
  - Licenses

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## Trade Secrets

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- Trade secret laws protect against the misappropriation of certain confidential information

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## Trade Secrets

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- What is a trade secret?
  - Information that derives independent economic value from
    - Not being generally known to others
      - Does not have to be novel or nonobvious
    - Not readily ascertainable by others
      - Published, reverse engineering
  - The subject of reasonable efforts to maintain secrecy

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## Trade Secrets

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- How long does trade secret protection last?
  - Potentially forever

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## Trade Secrets

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- What types of information can be protected?
  - Customer lists
  - Marketing and strategic plans
  - Technical know-how
  - Processes, formulas
  - Drawings, blueprints
  - Form of information – tangible v. in memory

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## Trade Secrets

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- What is not a trade secret?
  - Independent development
  - Employee's general knowledge, skill and experience

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## Trade Secrets

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- How do you protect a trade secret?
  - No registration or examination process
  - Reasonable efforts to maintain secrecy
    - Avoid public disclosure
    - Company Policy and Procedures
      - Limit access to information
      - Mark confidential materials
    - Use non-disclosure agreements
      - Employment agreements
      - Third party Agreements

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## Trade Secrets

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- Avoiding liability
  - Employee entrance interviews
  - Company policies, employee handbooks

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