



Legal Checklist for Entrepreneurs

Getting you out on the Road, and keeping you safe

A 30 minute briefing on legal issues for New Businesses, with forms and lots of Q & A
UC Berkeley Law's New Business Practicum



BerkeleyLaw | New Business Practicum
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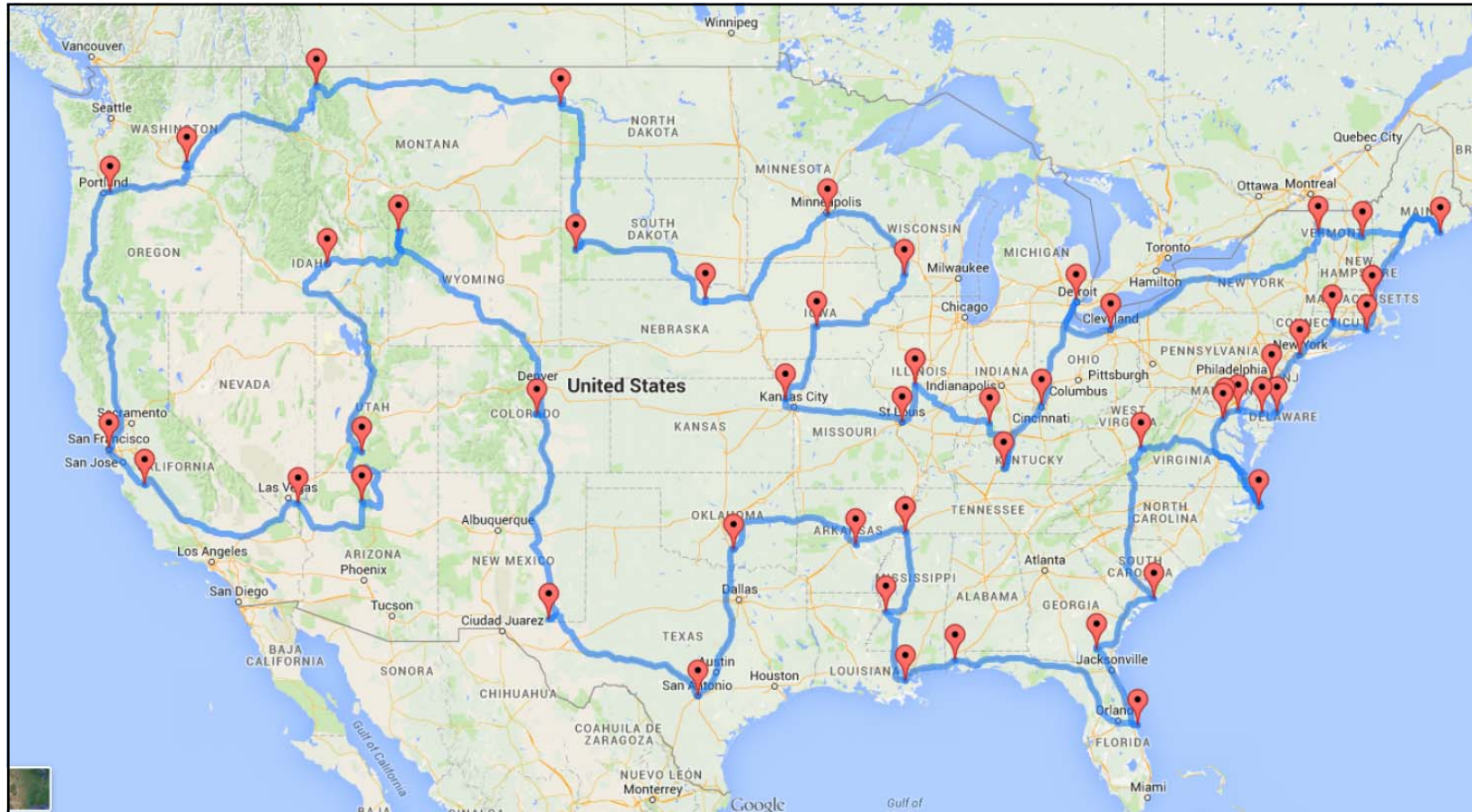
Starting a New Business – How it Feels at First



- 
- ☐ Business Modeling
 - ☐ Entity Formation
 - ☐ Capitalization
 - ☐ Operational Relationships
 - ☐ Manage Risks
 - ☐ Extra Permits/Licenses



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a Survivor!

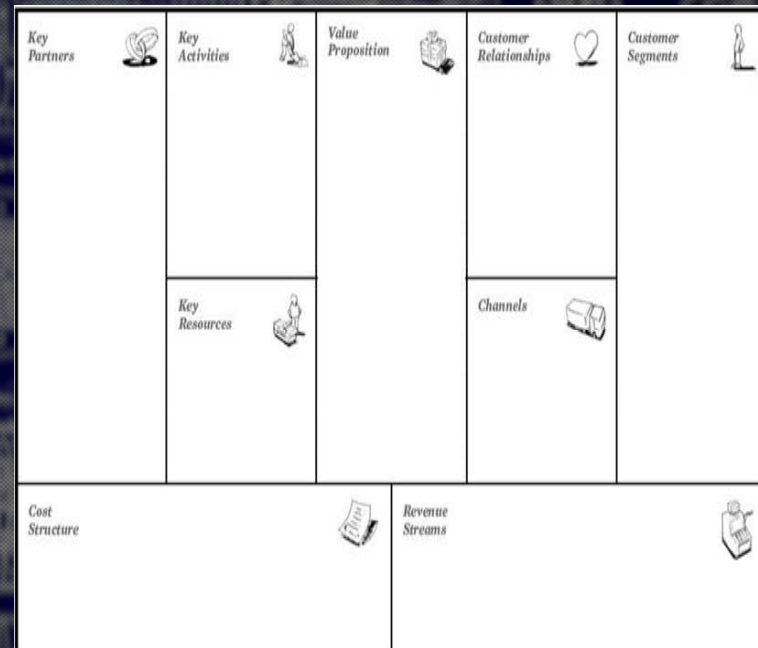











BUSINESS MODELING

Business Modeling – Why First?

Internal Uses: to clarify what's involved, organize thinking, prioritize tasks, spot issues, & bring together co-venturers.

External Uses: to enlist key stakeholders such as investors and banks) – the canvas can easily be formalized and directed to a particular audience (a “Business Plan”).



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| <h1>Business Model Canvas</h1> | | | | |
| Key Partners  | Key Activities  | Value Proposition  | Customer Relationships  | Customer Segments  |
| | Key Resources  | | Channels  | |
| Cost Structure  | | Revenue Streams  | | |
| <div style="display: flex; justify-content: space-between; align-items: center;"> <div> BerkeleyLaw <small>UNIVERSITY OF CALIFORNIA</small> </div> <div> New Business Practicum </div> <div> 6 </div> </div> | | | | |

| The Business Model Canvas | | SOUTHWEST AIRLINES | | |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------|
| Key Partners <ul style="list-style-type: none"> Cheap Airports as “Hubs” Car Rental Companies Hotels Insurance Web Search Engines – (e.g., Kayak, Expedia) | Key Activities <ul style="list-style-type: none"> Fly and Maintain Fleet of Planes Book Flights; Process Payments Hire and train Staff Market | Value Proposition <ul style="list-style-type: none"> Cheap Flights No Frills | Customer Relationships <ul style="list-style-type: none"> Web: automated searches; Impersonal Counter and in-Flight: Friendly, can-do attitude | Customer Segments <ul style="list-style-type: none"> Travelers on a Budget |
| | Key Resources <ul style="list-style-type: none"> Single Aircraft Model (e.g., 737's) Branding Large Inventory of Aircraft Model Parts Maintenance staff knowledgeable about Aircraft Model Enthusiastic, Friendly customer-facing staff | | Channels <ul style="list-style-type: none"> Call Centers Web In-person (Counter & In-flight) | |
| Cost Structure <ul style="list-style-type: none"> Purchase Planes and Equipment Maintenance Labor Costs/Staff Training Costs Airport Fees Call Centers Insurance Marketing Costs | | | Revenue Streams <ul style="list-style-type: none"> Airline Tickets Fees for Extra Services: e.g., Early Loading, Meals | |
| Source: www.businessmodelgeneration.com | | | | |
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ENTITY FORMATION

Choosing an Entity

The Options

- Sole Proprietorship
- Partnership (several kinds)
- Corporation (several kinds)
- Limited Liability Company (LLC)

>> **CAREFUL-!!**

Presumptions if NO CHOICE is made:

- **If Single/Married Couple:** Sole Proprietorship
- **If 2+ People:** Partnership

>> Neither are “limited liability” entities

How to Choose an Entity

IMPORTANT QUESTIONS:

- **Governance:** Who should make decisions for my business?
- **Tax:** How should the business's income be taxed?
- **Liability:** Do I need a legal liability backstop to protect myself?
- **Capital:** Do I need a vessel for capital providers to pay into?

NOT Important:

- What's Easiest to Form?
- What are Lowest Filing Fees?
- What's the Least Amount of Paperwork?


How to Choose an Entity


IMPORTANT QUESTIONS:

Ask Yourself:

- **Governance:** Who should make decisions for my business? ---> *Will decisions be shared with others? Do I want a formal structure (i.e., a Board)?*
- **Tax:** How should the business's income be taxed? ---> *Should the entity pay tax, or only report the income "passed through" to the owners?*
- **Liability:** Do I need a legal liability backstop to protect myself? ---> *Should I separate myself from the business's obligations, by paying \$800 CA Franchise Tax?*
- **Capital:** Do I need a vessel for capital providers to pay into? ---> *Will the business be seeking venture capital in the next couple years?*

The Most Common Entities

| Corporation (for-p/non-p) | LLC | Sole Prop/Partnership |
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| Governance: <ul style="list-style-type: none"> Board makes decisions Tax: <ul style="list-style-type: none"> <u>For-p C-Corp</u>: Entity level taxation & CA franchise tax: \$800/year min.; owners pay cap gains on any dividends <u>Non-p Corp</u>: No tax (if apply & obtain tax exemption) Liability: <ul style="list-style-type: none"> Limited liability Capitalization: <ul style="list-style-type: none"> <u>For-p</u>: Personal funds, Debt & Shareholders' equity <u>Non-p</u>: Debt, Grants, & Donations (NO equity) | Governance: <ul style="list-style-type: none"> Entrepreneur(s) make decisions or appoint a Manager to manage most operations Tax: <ul style="list-style-type: none"> Pass-through taxation Gross Receipts Tax (if > \$250K); CA franchise tax: \$800/year min. Active owners pay self-employment tax Liability: <ul style="list-style-type: none"> Limited liability Capitalization: <ul style="list-style-type: none"> Personal funds, Debt & Members' equity | Governance: <ul style="list-style-type: none"> Entrepreneur(s) make decisions; Partnerships can have Limited Partners Tax: <ul style="list-style-type: none"> Pass-through taxation Sole-p and active partners pay self-employment tax Liability: <ul style="list-style-type: none"> Personal liability Capitalization: <ul style="list-style-type: none"> Personal funds & Debt (Partnerships can have Partners' equity) |
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| New/Less Common Entities – | | |
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| Benefit Corp/Social Purpose Corp | S Corp | Cooperatives (LLC or Cooperative Corporation) |
| Governance: <ul style="list-style-type: none"> Shareholders elect Board, Board makes decisions Tax: <ul style="list-style-type: none"> Entity level taxation & CA franchise tax: \$800/year min.; owners pay cap gains on any dividends Liability: <ul style="list-style-type: none"> Limited liability Capitalization: <ul style="list-style-type: none"> Same as For-p C-Corp, but Shareholders must be okay with dual purpose – profit making + social mission | Governance: <ul style="list-style-type: none"> Shareholders elect Board, Board makes decisions Tax: <ul style="list-style-type: none"> Pass-through taxation; active owners pay income tax on salaries; owners pay cap gains tax on passive profits CA franchise tax: \$800/year min. Liability: <ul style="list-style-type: none"> Limited liability Capitalization: <ul style="list-style-type: none"> Same as For-p C-Corp but Shareholders must be humans w/ legal status | Governance: <ul style="list-style-type: none"> Workers are owners and share decisionmaking Tax: <ul style="list-style-type: none"> Pass-through taxation CA franchise tax: \$800/year min. Liability: <ul style="list-style-type: none"> Limited liability Capitalization: <ul style="list-style-type: none"> Same as For-p C-Corp, but only very limited passive investment possible |
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Where to Form



Articles or
Certificate of
Incorporation



Primary Pros:

- Generally low franchise taxes & fees (min. of \$800/year)
- Well-developed corporate code

Primary Cons:

- VCs & Public Investors less familiar with it



Primary Pros:

- Well-developed law; specialized biz courts
- Choice for most publicly traded co.'s and startups
- Filings are fast!

Primary Cons:

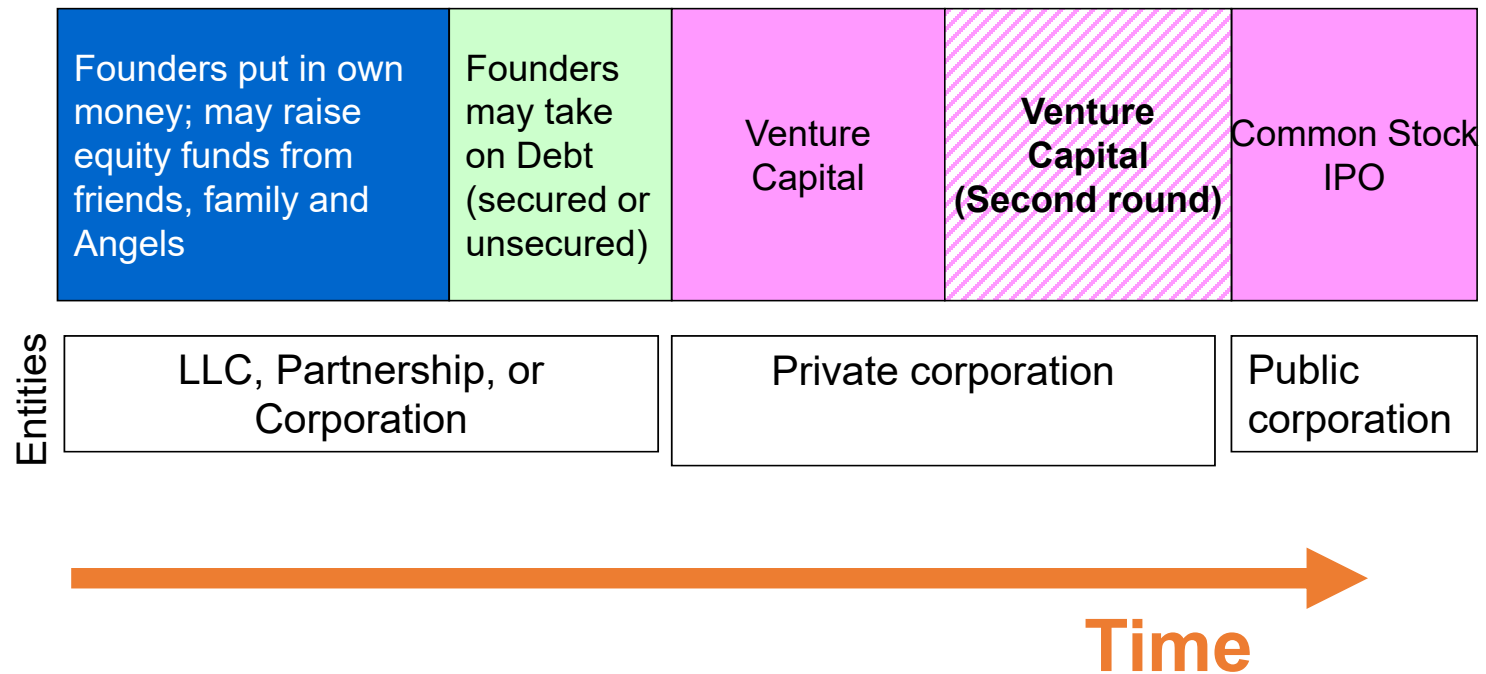
- More expensive franchise taxes & fees

CAUTION: Forming in DE, but Operating in CA makes you subject to BOTH States' Taxes and Laws (= Expensive; Need to register in CA as foreign corporation)




CAPITALIZATION

A Typical Capitalization



Raising Equity Capital



| Traditional Securities | Kickstarter | Crowdfunding |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> • Highly regulated by Federal SEC and State • If use one of the Small Business EXCEPTIONS, possible to have limited sales without much paperwork • Generally no advertising • Generally can only sell to Insiders and Accredited Investors (= RICH people) | <ul style="list-style-type: none"> • Presales of product, to raise money to fund prototypes or initial production • These are technically NOT sales of securities • Have contractual obligations to follow through to provide product purchased. | <ul style="list-style-type: none"> • Federal JOBS Act allows limited sales of securities over the web to non-accredited investors • Limits on company re: amount of equity that can be raised per year • Limits on % of income and total \$ amount can invest per year • Arranged through funding portals, which monitor above limits • Usually arranged via convertible notes |
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OPERATIONAL RELATIONSHIPS

Most Common Relationships to Know

- CAPITAL PROVIDERS - Who help fund the business
- WORKERS - Who will work to offer/produce the services or products
- SUPPLIERS – Who will provide other essentials needed to operate the business
- CONSUMERS - Who will receive the services/products

Focus on ***how to LEGALLY set up each relationship***

Need to know what is:

- Government-Required
- Minimally Necessary
- Optimal/Optional

Workers: The 3 Buckets

Employees (PRESUMPTION: ALL Workers are Employees)

- Highly regulated, 17+ federal/state requirements
- California = At Will State
- Best to use Payroll Service to manage the requirements



Independent Contractors (IC) -- New “ABC Test”:

- A. Can't control the IC much – pay by the PROJECT, not via salary; usually can't set hours or use for key positions (e.g. CEOs)
- B. Can't be used to provide regular or continuous services of the business
- C. IC needs to have own business and be able to work for others

NOTE: > Big penalties for misclassification

> Need to arrange in written contract, address IP & Liability Issues

Volunteers/Interns:

- Non-profits =OK, For-profits = Highly Regulated (need educ. purpose)



MANAGE RISKS

What are Reasonable Steps to Manage Risks?

- Form a Limited Liability Business Entity (Corporation or LLC)
 - Purchase Insurance (use a broker)
 - Control Your Agents (e.g., employees, volunteers)
 - screen
 - hire
 - train
 - supervise carefully
 - Indemnify Your Agents (e.g., employees, board, volunteers)
 - Use Contracts to Share/Limit Liability with Others
 - Choose your Activities Carefully
 - Avoid Risky Activities if Possible
- >> Note: All of the above efforts = helps the leadership meet *FIDUCIARY DUTIES*

* *Duty of Care*

* *Duty of Loyalty*

Intellectual Property –Legal Protections



Trade Secrets

- To protect a company's ***secret information*** regarding products or services
- Requires ***reasonable steps*** to protect secrecy, (e.g., use NDAs, lock-up, pass protection)
- **No formal filing required** to obtain State law protection

Patents

- To protect a ***product*** or ***process*** with unique design or utility
- Patents are **public documents** that expire after 20 years
- Patents **must be filed** with the **USPTO** to obtain Federal protection

Copyrights

- To protect the ***content*** of creative works (e.g. books, music) from unauthorized copying or use
- Copyright protection attaches automatically to tangible expression of the content
- To enforce copyright in a lawsuit: must file with the **USCO** to obtain Federal protection

Trademarks / Service Marks

- To protect ***marketing*** aspect of products or services, rather than utility or design
- The main goal is to **protect consumers** from confusion in the marketplace (e.g. Rolex).
- Trademarks must be filed with the **USPTO** to obtain Federal protection

IP by Contract

- Agreements can create/restrict IP rights: NDAs, Terms of Use, Creative Commons licenses

****For more information, see our IP PowerPoint****

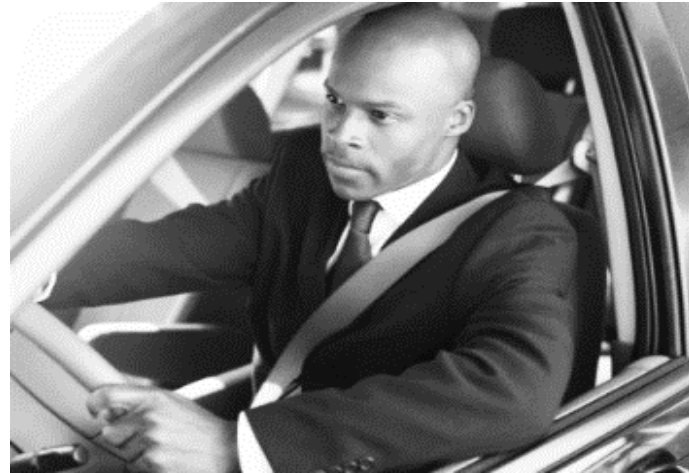


EXTRA PERMITS & LICENSES REQUIRED

Key Questions for Permits & Licenses

- As to my business's activities, would government care:
 - What activities I do? – Answer: USUALLY you will have to file for a business license/DBA (“doing business as”) form
 - Where I do my activities? – Answer: USUALLY there will be zoning restrictions to observe, even with home-based businesses
- Doing regulated activities without approval = major lawsuit risk
- Most regulations will come from state or local government – good search engine to find them:
- >> Check out “*CALGOLD*” = www.calgold.ca.gov

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QUESTIONS?

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