Points of Business Interest

●*Avoiding One of the Headaches in Building Construction*

Anyone who has ever built a home or a commercial building knows that the best laid plans are quickly torn asunder by unforeseen changes. We have noted that it is far more common to ignore the modification term in almost all construction contracts that it is to comply with that term. Under the requirements of most construction contracts, modifications must be spelled out in a written change order and signed off by the parties. In the environment of a construction site, that often does not occur. This almost invariably leads to disputes that could otherwise be avoided, and work to the benefit of neither side.

When working on site as a contractor, subcontractor or owner, it is in your best interest to make sure that all change orders are spelled out in writing, numbered consecutively, list the additional costs or rebates, are dated and signed by all of the parties pursuant to the contract. In this way a running record and paper trail is kept of the costs of the project, and at the end of the project the total bill will be clear, free from arguments or misunderstandings that occur all too often. It is a pain to do this, with the contractor trying to orchestrate the work of several different subcontractors simultaneously, and the owner being on the site some of the time, but not at the right time, but consider that headache when compared to the headache of litigation that could have been avoided.

●*Buy-Sell Agreements: or How to Dodge a Bullet when Dying*

Many of the companies we set up, being corporations, LLC's, etc., involve several owners. An axiom I am fond of repeating is that the advantage of going into business together is that it is a marriage in which you can plan your divorce from the very beginning, and do so amicably. With several owners, should one become disabled of die, serious problems may arise. Should one of the owners die, the deceased's family will own the stock and be free to vote it, use it for purposes of control, or sell it to a third party. In most small businesses, people who get along well combine to join their strengths. That will be thrown out of whack when one of the individuals is gone and possibly replaced with another person with no or different qualifications and strengths; personalities may not match.

In another scenario, many small businesses operate because all of the owners work for the company full time. If one of the owners is disabled for any reason, this may cause a severe hardship to the company, as well as ethical questions: How long does the company pay the disabled owner who has put in years of hard work? How long can the company afford to do that and pay someone else to do the disabled owner's job?

A third scenario is equally imaginable. The owners work together happily and successfully for a number of years, and one of the owners announces that Illinois winters are just too much and she/he is moving to Florida.

In each of these scenarios, a buy-sell or redemption agreement can provide solutions. These agreements should be set up at the beginning of the enterprise, although they can be modified by

the agreement of all of the parties as circumstances merit. The agreement can provide that the entity or surviving owners will purchase the deceased's shares for a set sum, which is usually based upon a formula to determine the value of the company and therefore the value of the owners' interest. This can be funded with term life insurance, including policies that insure two or more lives but pay out only once. This is a cost effective way to fund this buyout while not crippling the company financially.

In the case of the disabled owner, the definition of *disabled* needs to be crafted to the services performed by the employees. Obviously, what would be disabling for the owner of a plumbing business would not necessarily be disabling for an attorney, as technology can work around the loss of one's arms for an attorney, but not so with a plumber. Once the term disability is defined, then the duration of the disability should be arrived at. If someone is unable to work for a month, for example, due to a heart attack, but is able to return to work, that may be wholly acceptable, while inability to work for six months may cripple a business. Disability insurance can provide a tool to pay for the stock over a period of time, which may be in the financial best interest of both the company and the disabled owner, who would then have a guaranteed income.

As to the owner who decides to retire to the land of Mickey Mouse and oranges, this allows the remaining owner(s) to purchase the interest of the retiring owner, eliminating an absentee owner who would have a claim on company profits but who is not contributing to those profits, and allows that person to cash out and buy a home in the depressed real estate market in Florida.

The bottom line is that there is really no excuse for going into business with one or more "partners" and not arranging for the inevitable, be it death, disability, retirement, or voluntary withdrawal.

●*More on Buy-Sell Agreements: The Tax Man*

Having extolled the virtues of buy-sell agreements, it is only fitting to indicate that they must be done properly. While most contracts are fine, or they are simply acceptable to the parties, buy-sell agreements have another party lurking in the shadows: the Internal Revenue Service. If the IRS determines that the amount paid an individual for his or her interest in the business is improperly low, they will file a Notice of Deficiency, seeking additional taxes. To pass muster with the IRS, the buy-sell agreement must satisfy the following requirements:

1. be a bona fide business arrangement;
2. not be a device to transfer wealth to family members for less than full consideration;
3. be comparable to similar arrangements negotiated at arms length;
4. establish a price that is either fixed or determinable and is reasonable at the time the agreement was made;
5. require a shareholder's estate or beneficiaries to sell the shares at the price specified, either automatically or at the other parties' option;
6. restrict the shareholders' disposition of their shares during their lifetime and at their death.

If a buy-sell agreement fails on any of these requirements, the IRS will ignore the buy-sell agreement and attach its own value to the company. It is therefore essential to make sure that the buy-sell agreement is properly drafted initially, and to review it annually to make sure that circumstances do not require any modifications.

●*The Great American Paperchase*

All business owners recognize that one of the great headaches of running one's own business is the paperwork. The required paperwork falls into several categories, and several issues arise from those categories. This article is not meant to be exhaustive, but should help you fill in a few holes.

When hiring, make sure that you obtain or check I-9 forms to make sure that your employees are citizens or are legally within the United States. This must be done within three business days from the date the employee begins working. You must also report new hires to the State Directory of New Hires, which forwards the information to a federal database to check for outstanding child support obligations and this applies to all employees. An employee is anyone who is issued a W-2 form.

In terms of record keeping, as long as an employee is with your company, you should maintain the amounts and dates of all wage, annuity and pension payments, the amounts of tips reported (if applicable), the market value of in-kind wages paid, the dates of employment, the periods for which the employees and recipients were paid while absent due to illness or injury, and the amount of the individual's pay.

Finally, a question that frequently comes up is how long records must be retained. We suggest the following:

Type of records	**Time to be retained**
Travel records	1 year
Time cards	2 years
Employee personnel file	3 years
Employment tax records	4 years
Contracts	10 years after termination
Insurance records	permanently
Retirement and pension plan documentation	permanently
Employee handbooks and training manuals	permanently

●*Whose e-mail is it anyway?*

As most employers and employees know, employers have the right to monitor e-mail activity on their equipment and their work place. Unfortunately, most employers do not require staff to acknowledge that policy in writing. In order to avoid an invasion of privacy or wrongful termination lawsuit, it is wise to secure employees' written consent to have their electronic messages read.

It is essential to have a policy regarding document retention and deletion. Aside from an awareness that there is pending or possible litigation that could be affected by retention of documents, in which case ***documents should not be deleted***, for an employer under normal circumstances, a thirty day retention period for e-mails is a good idea. It is appropriate to repeat, however, that if you think that the subject of e-mails may end up in litigation, the e-mails should be retained, perhaps in a separate folder.