

# MENDENFREIMAN<sub>LLP</sub>

YOUR FUTURE IS HERE<sup>®</sup>

5565 GLENRIDGE CONNECTOR NE, SUITE 850, ATLANTA, GA 30342

PHONE: (770) 379-1450 FAX: (770) 379-1455

WWW.MENDENFREIMAN.COM

## **Do Not Overlook These Legal Checkpoints When Making a Business Investment**

If you are considering buying or investing in a business, you may already have talked to an accountant, business broker and a banker. A lawyer also should be on your list of advisers.

Lawyers are trained to see the big picture and how all the moving parts of a deal touch each other. They are well suited to lead a team of specialists who bring together your business investment.

As a business person, you are naturally excited about the opportunity a new investment brings. As a risk manager, your lawyer is looking ahead to the inevitable disputes and threats of litigation that eventually emerge in most businesses. Relatively minor changes in business entity structure (that are much harder to effect down the road) can result in tax savings, separate assets for the purpose of liability protection, and align with your overall estate and business succession plans.

Here are some things your lawyer will consider in a business investment.

### **Do not neglect the legal aspect of due diligence.**

While your accountant looks at the books, your lawyer will assure there are no surprises such as liens against business assets, lawsuits, government enforcement actions or lapsed registrations. A lawyer can also draw up a contract for the seller to warrant there are no pending or hidden legal problems.

Legal counsel should review all legal paperwork that the business relies on in day-to-day operations. This includes employment agreements, contracts with customers and suppliers, leases and property deeds, all financial instruments, business formation papers, and environmental or other industry-specific inspections. Be sure vendor and supplier contracts fit your plan for the business. If not, you may want to terminate these contracts; and if there is a premium to be paid for termination, factor it into the purchase price.

### **Protect yourself from upheaval.**

If you are a minority investor, be sure you are comfortable with your rights. That includes the right to financial records and bank statements, to participate in major decisions (such as changes in management or the business model), to attend regular board/management meetings, and other corporate formalities. Do not just go a long for the ride.

## **Anticipate divorce.**

The divorce anticipated here is a business divorce, where a partner or investor wants out of the business, dies, is disabled or retires. This is most problematic in a limited liability company (LLC) where the operating agreement places restrictions on how a member's interest can be transferred to family members or heirs. It can be a problem in a corporation as well when the operators/owners of a small business suddenly find themselves saddled with partners they do not want.

You may consider giving other investors or the company the right of first refusal at a predetermined price before another partner can sell his or her interest in a company. This can be particularly problematic in family businesses when an heir wants to cash out an interest. A lawyer can walk you through all possible scenarios you might face and the pros and cons of various strategies.

## **Do not just kick the tires.**

Sometimes business owners drag their feet when it comes to opening their books, sharing customer and supplier information, inventory, and other vital data needed to make a buying decision. Often this simply reflects a seller's understandable reluctance to lift the veil on private financial matters, as well as a fear that premature news of a pending sale will spook customers or disrupt the workplace. But a deal will stall if a buyer cannot open the books and explore the business. A nondisclosure agreement will reassure the seller, and experienced business counsel will know how to conduct due diligence in a discreet manner.

## **Inventory the intellectual property.**

Be sure that trademarks, patents and other IP registrations are up to date; and be aware that any licenses are part of the package you buy. On the negative side, be sure the business is not expropriating someone else's IP, which could lead to a rude shock if you receive a demand letter and have to change your signage or other trade dress.

## **The proverbial ounce of prevention.**

Just a few hours of due diligence – reviewing contracts, searching public records or revising a sales agreement – can save thousands of dollars and countless hours of frustration down the road. Along with the balance sheet, consider the long-range legal aspects of any business investment; and you will increase your opportunity for success.