

BUSINESS LAW NOTES

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ABOUT OUR FIRM

Our law firm has provided exceptional legal services to clients throughout the state and the U.S. for more than 45 years. A full-service firm founded in 1955, we have built a reputation for helping clients solve difficult problems with sound counsel, sophisticated analysis and superior performance.

A hallmark of our firm is personalized client service. Recognizing that each of our clients has a unique set of issues, objectives and needs, our firm is committed to individualized attention and works as an integrated team to respond to our clients' needs. We serve diverse clients, including Fortune 500 companies, government agencies, professional associations, closely held corporations, limited liability companies, partnerships and individuals.

Part One

BUYING A FRANCHISE

M. Blen Gee

The best *legal* advice that can be given to someone considering purchasing or opening a franchised business is to do a thorough due diligence investigation of the *business* issues first. If you are looking to acquire a franchise from one of the larger and better known franchisors, you can expect all but the most minor legal issues to be non-negotiable. For smaller and lesser-known franchises, you may have more negotiating leverage on legal issues, but you will also be dealing with a franchise that has weaker trademarks, little or no track record and no real security that the franchise will even be around in a few years. So, the best legal advice is to do your business analysis first and do it thoroughly. Here are some key points for your business investigation:

- Talk to as many other franchisees as possible. Visit their operations. Do not just visit the franchisees recommended by the franchisor.

- Is there a franchisee association for your brand? A franchisee association can be a great resource. Also, the existence of a franchisee association means more bargaining leverage with the franchisor.
- Exclusive Territory and Encroachment – Does the franchisor give you an exclusive territory and is the territory sufficiently large? Is there any protection from internet and catalogue sales into your market?
- Collective Buying – Franchisees can benefit tremendously from a franchisor's ability to obtain volume discounts for its franchisees. However, be certain that the franchisor consistently passes on these discounts to the franchisees and does not favor its own company-owned stores.
- Collective Advertising – This is a huge issue in franchising. You will

almost certainly be required to pay into an advertising fund. How is this money used? Do other franchisees consider the advertising effective and evenly distributed? Will your proposed franchise be in an area benefitting from national and local collective advertising?

- What immediate, up-front benefits does the purchase of a franchise entitle you to? Training? Site selection and lease negotiations? Start-up assistance? Marketing assistance and marketing materials?
- Is there a long-term commitment by the franchisor to franchisee support?
- What is your franchisor's track history? Is the franchisor frequently involved in litigation with franchisees? Has the franchisor lost large numbers of franchisees? Is the franchisor financially healthy?
- Does the franchisor enforce quality and uniformity standards?
- Will the franchisor negotiate modifications of its standard franchise agreement?

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BUSINESS ENTITIES

F. Stephen Glass

LIMITED LIABILITY ENTITY DIS-COUNTING STRATEGIES

Many persons establish limited liability companies (LLCs) as part of their overall business, investment planning and estate planning strategies. *[This discussion also applies to family limited partnerships (FLPs).]*

There are many significant non-tax reasons to establish and maintain an LLC. An LLC is an effective way to control and centralize management of family assets and to restrict the transfer of interests in such property. An LLC also provides certain protective rights against creditors and may entitle an LLC member (owner) to minority and lack of marketability discounts when interests in the LLC are transferred during the member's lifetime or upon death.

Members generally contribute assets to the LLC in exchange for LLC interests. Upon the death of the member, the tax value of the member's LLC interests may be discounted for lack of marketability and, where appropriate, for ownership of a minority interest.

Members may also make lifetime gift-transfers of LLC interests (as provided in the LLC's operating agreement). The value of the gifted LLC interests may also be discounted for lack of marketability and, where appropriate, for ownership of a minority interest.

While the amount of the discounts allowed for lack of marketability and minority ownership depend on the individual fact situation, tax case law indicates that a combined discount is usually between the 10 to 60 percent range. In some situations it may be reasonable to discount LLC interests to non-managing members by 30 to 35 percent. An appraisal is necessary to determine the applicable amount of each discount.

DUTIES OF A CORPORATE DIRECTOR OR OFFICER

In the current climate of financially strained corporations, officers and directors are becoming increasingly concerned about personal liability for decisions that they must make on behalf of their corporations.

Certain duties are imposed by law upon the conduct of a director or officer of a business corporation. The North Carolina Business Corporation Act codifies the general rule that a corporate director or officer must carry out his or her duties (1) in good faith, (2) with the care an ordinarily prudent person

in a like position would exercise under similar circumstances, and (3) in a manner he or she reasonably believes to be in the best interest of the corporation.

The corporate director and officer's duty of good faith is to act in the best interest of the corporation and not in his or her own interest or in the interest of another person or organization. One should not use his or her position as a corporate director or officer to make a personal profit. To do so could be a conflict of interest and a breach of that duty of good faith to the corporation.

A corporate officer or director cannot take the business of the business corporation for himself.

North Carolina courts have long held that directors and officers are generally not liable for mere errors of business judgment, nor for slight omissions from which a questioned loss could not have been reasonably expected. The "**business judgment rule**" protects a director or officer, with no personal interest in the transaction, from

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personal liability to the corporation and its shareholders, even though a corporate decision by the officer turns out to be unwise or unsuccessful. A court will not substitute its judgment for that of

a *disinterested* director or officer if the director officer acted in good faith, was reasonably informed, and rationally believed the action taken was in the best interests of the corporation.

Officers and directors owe a fiduciary duty and obligation of good faith to minority shareholders as well as to the business corporation.

When a corporation is insolvent or in the "vicinity of insolvency" courts have required officers and directors to consider the corporation's creditors when making decisions.

In summary, every corporate director and officer owes duties of *fidelity, honesty, good faith* and *fair dealing* to the business corporation.

Consultation with the corporation's attorney before making decisions regarding corporate issues may keep officers and directors from straying over the line into personal liability. Preventive involvement is less expensive than costs of remedial action.

EMPLOYMENT LAW UPDATE

F. Stephen Glass

WHAT TO DO WHEN AN EEOC CHARGE IS FILED AGAINST YOUR COMPANY

What should you do if you receive a charge form from the Equal Employment Opportunity Commission (EEOC) that alleges a discrimination claim -- a violation of federal law -- against your business?

Ordinarily the charge must be filed by someone who has contacted the EEOC and alleged that a company has discriminated against him or her. The fact that the EEOC has taken a charge does not mean that the government is accusing your company of discrimination. The charging party has alleged that your company has discriminated against him or her ; it is the EEOC's job to investigate the matter to determine whether there is reasonable cause to believe that discrimination has occurred.

The EEOC Notice of Charge

EEOC will notify the employer within 10 days of receiving a charge. Notification normally includes a copy of the charge briefly identifying the charging party, the basis (e.g., race, religion, sex, etc.) and issue(s) (e.g., hiring, promotion, discharge, etc.) of the allegation, and the date(s) of the alleged discrimination. Ordinarily, a plain language explanation of the EEOC charge process will be included, as well as explanations of the employer's obligation to retain records pertaining to the charge and of the non-retaliation provisions of the EEOC laws. An invitation to mediate the charge may also be included in the notification package.

The EEOC Investigation

After a charge is filed, you may be asked to provide a position statement responding to the allegations in the charge. **Early involvement by your business attorney is essential at this stage to protect your company's rights and assure fairness in the process.** You may also be asked to provide documents or information related to the investigation. The EEOC may also ask to visit your worksite or to interview some of your employees. When an employer refuses to provide information, or does not do so in a reasonably timely manner, the EEOC may issue a subpoena.

The *Notice of Charge* should explain the record retention requirements. When an EEOC charge has been filed against your company, you should retain personnel or employment records relating to the issues under investigation as a result of the charge, including those related to the charging party or other persons alleged to be aggrieved and to all other employees holding or seeking positions similar to that held or sought by the affected individual(s). Once a charge is filed, these records must be kept until the final disposition of the charge or any lawsuit

based on the charge. When a charge is not resolved after investigation, and the charging party has received a *notice of right to sue*, "final disposition" means the date of expiration of the 90-day statutory period within which the aggrieved person may bring suit or, where suit is brought by the charging party or the EEOC, the date on which the litigation is terminated, including any appeals.

Even if you believe that the charge is frivolous, you should respond. Under the EEOC's procedures, if the EEOC believes the charge is invalid or frivolous, it will dismiss the charge. If the charge is not dismissed by the EEOC when it is received, there is usually some further investigation. There are many cases where it is unclear whether discrimination may have occurred and an investigation is necessary. Your attorney can assist you in presenting the facts that you believe show the allegations to be false.

If the EEOC dismisses a charge, it will not proceed further with an investigation. The charging party is notified of his or her right to file a lawsuit in court (*notice of right to sue*). A charging party may file a lawsuit within 90 days of receiving the dismissal notice. A charging party may go to court instead of waiting for the EEOC to complete its investigation.

If the EEOC determines that there is reasonable cause to believe that discrimination occurred, a written determination and invitation to enter into conciliation discussions are issued to the parties. If conciliation efforts are not successful, the EEOC and/or the charging party may bring suit.

Penalties For Violating the Law

The remedies for unlawful discrimination include an order to eliminate discriminatory practices in hiring, wage adjustments, promotion or reinstatement, depending upon the nature of the company's action taken against the aggrieved individual. Monetary remedies available under the laws enforced by the EEOC are as follows:

- lost wages and prejudgment interest
- liquidated/double damages (ADEA and EPA)
- compensatory damages (Title VII and ADA cases involving intentional discrimination)
- punitive damages (Title VII and ADA cases in which the employer acts with reckless disregard of the federally protected rights of the individual).

Early involvement by your company's business attorney is essential to protect your company's rights at every stage of the process.



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BUYING A FRANCISE

(Continued from page 1)

- Run the Numbers – Look carefully at earnings claims. Sit down with your CPA and see if it all makes financial sense for you.

Additional information can be obtained from the American Franchisee Assoc. (<http://www.franchisee.org>) and the American Association of Franchisees and Dealers (<http://www.aafd.org>).

When you feel that you have finished your business due diligence evaluation, take your Uniform Franchise Offering Circular (UFOC) and the proposed franchise agreement and make an appointment with your business attorney.

OSHA's ILLNESS AND INJURY LOG UPDATED FOR 2004

F. Stephen Glass

Form 300, the OSHA log of work-related illnesses and injuries, is used to track each recordable workplace injury or illness.

A revised Form 300 is required **beginning January 1, 2004**. The directions on the revised Form 300 state: "You must record information about every work-related injury or illness that involves loss of consciousness, restricted work activity or job transfer, days away from work, or medical treatment beyond first aid. You must also record significant work-related injuries and illnesses that are diagnosed by a physician or licensed

health care professional. You must also record work-related injuries and illnesses that meet any of the specific recording criteria listed in 29 CFR 1904.8 through 1904.12. . . . You must complete an injury and illness incident report (OSHA Form 301) or equivalent form for each injury or illness recorded on this form."

The instructions also warn the user about the medical privacy of workers whose injuries or illness are recorded on Form 300: "*Attention: This form contains information relating to employee health and must be used in a manner that protects the confidentiality of employees to the extent possible while the information is being used for occupational safety and health purposes.*"

The revised Form 300 is found at <http://www.osha.gov/>