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## Memo

**To:** Client and Friend  
**From:** Joseph R. Pozzuolo, Esquire  
**Date:** September 19, 2023  
**In Re:** Fall Seminar

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Dear Client and Friend:

Pozzuolo Rodden Pozzuolo are pleased to invite you to the first of 3 of its fall 2023 business/estate law seminar titled "Business Law Symposium For The Closely Held Business Entity". The seminar will be held Wednesday, September 27, 2023 from 3 to 5 PM via ZOOM. The Zoom mobile app is:

The link is: <https://zoom.us/j/96741362729?pwd=N29YZ3ZnSjljREE3bTVYZGk3VHNXdz09>

Meeting ID: 967 4136 2729

Passcode: 574435

If you plan to attend, please complete and email me the form below to confirm attendance. The email contact is [Chrissy@pozzuolo.com](mailto:Chrissy@pozzuolo.com).

If any of you have a particular question or business item of interest, kindly include the issue with specificity on the form below and it will be addressed. If the seminar extends beyond 2 hours the firm will complete this seminar in two sessions to be scheduled appropriately.

Lastly, attached please find an outline for the seminar which I hope you find useful and informative.

We look forward to working with you next week.

Regards,

NAME:

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FIRM

NAME:

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EMAIL ADDRESS:

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PHONE

NUMBER:

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QUESTIONS/INTEREST:

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## BUSINESS LAW SYMPOSIUM FOR THE CLOSELY HELD BUSINESS ENTITY

### COURSE DESCRIPTION AND LEARNER OBJECTIVES:

In advising clients on privately held businesses it is necessary to understand the important intertwining of the legal and business concepts involved. This course provides a comprehensive and practical overview of the most important legal concepts business persons must know in this area. This course will bring you through from the initial formation of the business to the final winding up of business. More specifically this course will discuss important documents, provisions and considerations for; 1) business formation such as choice of entity, buy-sell agreements, shotgun clauses, LLC operating agreements, partnership agreements, restrictive covenants, and stock option agreements; 2) managing and running the business including employment agreements, shareholder agreements, and changing the choice of entity; and, 3) the winding down, selling, or business succession plan. This seminar will focus on the day to day, wheeling and dealing of the privately held business world.

#### A. SELECTION OF A BUSINESS ENTITY.

1. INITIAL MEETING WITH CLIENT
  - (a) Role of Attorney
  - (b) Role of CPA
  
2. FACTORS BEARING UPON CHOICE OF ENTITY
  - (a) Level of control desired
  - (b) Personal vulnerability to lawsuits
  - (c) Tax implications
  - (d) Regulation/business formalities
  - (e) Cost
  - (f) Rendering professional services
  - (g) Number of employees
  - (h) Type of business
  
3. BASIC CLOSELY-HELD ENTITIES
  - (a) Sole proprietor
  - (b) General partnership
  - (c) Limited partnership
  - (d) "C" corporation
  - (e) "S" corporation
  - (f) Limited Liability Company
  - (g) Professional corporation
  
4. EQUITY ALLOCATION
  - (a) Sweat equity/"know how"
  - (b) Passive investment
  - (c) Idea person
  - (d) Growth investors

B. INCORPORATION.

1. NAME
2. FICTITIOUS NAMES
3. ARTICLES OF INCORPORATION
  - (a) Publication
4. BY-LAWS
  - (a) Organizational meeting/ Adoption
  - (b) Shareholders
  - (c) Directors
  - (d) Officers
5. "S" ELECTION
  - (a) Default is "C"
  - (b) Must qualify under section 1361 of IRC
  - (c) Must timely file Fed. Form 2553 and PA Form REV-1640

C. LLC & LP FORMATION.

1. NAME
2. FICTITIOUS NAMES
3. CERTIFICATE OF FORMATION/ LIMITED PARTNERSHIP
  - (a) Business purpose
4. OPERATING AGREEMENT/ PARTNERSHIP AGREEMENT
  - (a) Capital contributions
  - (b) Members/Partners
  - (c) Management
  - (d) Profit and Loss allocations
  - (e) Distributions
  - (f) Admission of new members/partners
  - (g) Absence of opening agreement or partnership agreement
5. PARTNERSHIP TAXATION DEFAULT FOR LLCs
  - (a) Corporate election
  - (b) Single member LLCs

D. SUCCESSION PLANNING.

1. OPERATING/ SHAREHOLDERS' AGREEMENT

- (a) Triggering events
  - (i) death
  - (ii) disability
  - (iii) lifetime
    - (A) attempting to sell interest to third party
    - (B) pledging interest as security
    - (C) judicial declaration of incompetence/ bankruptcy
    - (D) receipt of bona fide offer for interest
  - (iv) put & call options
  - (v) shotgun/ estrangement
  - (vi) permitted transferee(s)
- (b) Form of buyout
  - (vii) optional or mandatory
  - (viii) redemption
  - (ix) cross-purchase
  - (x) wait-and-see
- (c) Valuation
  - (i) stale valuation
- (d) Funding/ Method of payment
  - (i) cash
  - (ii) insurance proceeds
  - (iii) promissory note/ installment sale

E. BUYING & SELLING A BUSINESS.

1. INITIAL NEGOTIATIONS
2. LETTERS OF INTENT
  - (a) Agreement in principle
  - (b) Exclusivity
  - (c) Dates for execution of definitive agreements and closing
  - (d) Non-binding but for certain terms
3. FORM OF TRANSACTION
  - (a) Asset purchase
    - (i) Buyer prefers
    - (ii) Seller remains subject to liabilities not expressly assumed by buyer
      - (A) product liability, environmental liability, and labor law liability are a potential pitfall for buyer in an asset purchase
    - (iii) Requires preparation of additional documentation such as deeds, bill of sale, lease/contract assignments, etc, not required in stock purchase
  - (b) Stock purchase

- (i) Seller prefers
- (ii) Buyer is subject to all seller liability, including unforeseen liabilities

4. DEFINITIVE AGREEMENT

- (a) Price
- (b) Method of payment
  - (i) Buyer may “reserve” an amount for indemnification purposes through escrow of portion of purchase funds, payment in installments, or requesting a letter of credit.
- (c) Representations and warranties
  - (i) Seller wants to limit to “material items” and to the “best of seller’s knowledge”
  - (ii) Buyer wants absolute representations and warranties
  - (iii) Resolving contentious items
  - (iv) Basket vs. Floor/Ceiling
- (d) Indemnification
- (e) Preconditions of closing
- (f) Restrictive covenant & confidentiality
- (g) Identification/exclusion of assets (asset purchase)
- (h) Exclusion/ assumption of liabilities (asset purchase)
- (i) Price allocations (asset purchase)
  - \*Buyer cannot write off amount paid for stock, but can amortize amounts paid for restrictive covenants
- (j) Receivable collection
- (k) Inventory Valuation
- (l) Pennsylvania laws relating to sales in bulk
- (m) Termination

5. DUE DILIGENCE

- (a) Verification of corporate compliance
  - (i) providing legal opinion letters
- (b) Financial review
- (c) Environmental testing
- (d) Employment contracts & ERISA
- (e) Validity of customer lists & contracts
- (f) Contracts affecting assets
- (g) Intellectual property rights
- (h) Product warranties
- (i) Many other ancillaries

6. DISSENTERS’ RIGHTS: 15 Pa. C.S. §1930 for SHAREHOLDERS

- (a) No statutory dissenter’s rights for LLC members, but may be provided for by contract

F. FINANCING.

1. FUNDING SOURCES
  - (a) Equity
  - (b) Debt
  - (c) Cash reserves
  
2. BANKS MUST MAKE LOANS
  - (a) Do not be apprehensive
  - (b) Without loans, banks would not stay in business
  - (c) Footwork, attention to fine print and a working knowledge of legal issues in loan documents will make a business stronger and build a positive working relationship with banks
  
3. RESEARCH LENDERS
  - (a) Zero in on appropriate targets
  - (b) Some banks lend on a conventional basis (without government support) while some banks participate in government programs
  - (c) Look for bank familiar with your loan type, industry, and geographic locale and has done business with clients like you or businesses like yours
  - (d) Seek out banks that give loans of the size and type you want
  - (e) Network and introduce your clients to competing banks, lawyers, accountants, local business owners for referrals or simply contact a commercial loan manager
  - (f) Ask competitors and other local related businesses for referrals
  
4. NEGOTIATION OF COMMITMENT LETTERS
  - (a) How to shop a commercial/real estate loan
  - (b) Who should shop the loan on behalf of the client
  - (c) Documentation required to shop loan:
    - i. Keep it real- broad unsubstantiated statements should be avoided.
    - ii. Prepare for meeting:
      1. ask for detailed description of all the materials the lender wants to review
      2. complete loan application
      3. business and personal tax returns
      4. financial statements
      5. projections
      6. executive summary that details what you will use the money for and how you will pay it back
      7. promotional materials about your business

such as brochures, ads, articles, press releases,  
etc.

8. anticipate questions
5. IF AT FIRST YOU DO NOT SUCEEEED
  - (a) Keep trying one lender after another until you get your loan
  - (b) Most businesses have to have another bank to get better terms
  - (c) Once you are approved, take the same loan package to a competing bank and negotiate terms
6. ALTERNATIVES TO BANK FIANCING
  - (a) Insurance companies
  - (b) Private placement/Equity investors
  - (c) Finance companies
  - (d) Non-bank lenders
  - (e) Factoring
  - (f) Leasing
  - (g) Options/Warrants for equity investors, insurance companies and non-bank lenders with Put/Call Options
7. NEGOTIATING FACTORS WHICH CAN HAVE AN IMPACT ON CLIENT'S FINANCIAL PERFORMANCE
  - (a) Better interest rates
  - (b) Lower loan fees
  - (c) Higher lending ratio on inventory
  - (d) Higher lending ratio on receivables
  - (e) Lower attorney fees
  - (f) Cap on Attorney fees
  - (g) Audit fees
  - (h) Longer amortization periods
  - (i) Longer loan terms
  - (j) No prepayment penalties
  - (k) Limitations on collateral, underlying security and loan coverage
  - (l) Notice of right to cure defaults
  - (m) No "confession of judgment" default remedy- nuclear bomb remedies
  - (n) No unlimited guaranty
    - i. sales are growing steadily-fast
    - ii. debt to equity ratio continues to trend downward
    - iii. customers pay on time
    - iv. three or more years of substantial profitability
  - (o) Reduce loan coverage
  - (p) All loans as package
  - (q) Better representations and warranties
  - (r) No security interest on "hereafter acquired equipment"- could affect business ability to finance equipment in the

future

(s) Letters of credit including foreign letters of credit

8. COMMERCIAL/REAL ESTATE LOAN AGREEMENTS

(a) Construction loans v. mortgage/post-construction

(b) Term loan agreement

(c) Accounts receivable lending agreement

(d) Inventory loan agreement

(e) Mortgage agreement

(f) Participation agreement

(g) Suretyship/Guarantee Agreement

(h) Promissory Note

(i) Security Agreement

(j) Assignment of Leases and Rents

(k) Control Agreement

9. LEGAL OPINION LETTER

G. EMPLOYMENT CONTRACTS.

(a) Who should negotiate?

(b) How to choose an attorney to negotiate for you?

(c) Terms to negotiate

(1) Duties

(2) Location of duties

(3) Service as an officer and director

(4) Check signing privileges

(5) Term of Contract

(6) Compensation

(7) Business Expenses

(8) Vacation, sick leave and leave of absence

(9) Disability

(10) Medical and financial records

(11) Billings and fees

(12) Insurance

a. Health Insurance

b. Life Insurance

c. Malpractice Insurance- claims made and Tail Coverage

(13) Death Benefits

(14) Fringe Benefits

a. Qualified Corporate Retirement Plans

(i) Money Purchase Pension

(ii) Profit Sharing Plan

(iii) Deferred Benefit Pension

b. Non-Qualified Deferred Compensation Plan

c. Medical Reimbursement

- (15) Restrictive Covenants
- (16) Termination
- (17) Arbitration of Disputes
- (18) Interpretation of Contract
- (19) Separation Agreement

(d) Discrimination Considerations

H. PROTECTING PROPRIETARY INFORMATION.

1. Confidentiality Agreements;
  - (a) Absence of confidentiality agreement/ state law protections.
2. Restrictive Covenants
  - (a) Reasonable covenant must serve a legitimate protectable interest and be reasonable in: 1)scope, 2)duration, and, 3) geographic area
    - (1) Should not be so broad as to create a monopoly or interfere with the public interest
  - (b) Sale of business vs. employment contract
    - (1) Business sale- not enforced if they extend beyond the existing territory of the business or the territory in which the buyer and seller contemplated the business might expand
  - (c) Modification
  - (d) Assignment
  - (e) The New Jersey Supreme Court factors:
    - (1) Bargained for
    - (2) Clearly expressed meaning
    - (3) In writing and recorded
    - (4) Reasonable as to geographic, scope, and duration
    - (5) Does not impose an unreasonable restraint on trade or secure monopoly for the covenantor
    - (6) Does not interfere with the public interest
    - (7) Intention of the parties when the covenant was executed
    - (8) Changed circumstances
  - (f) Blue Pencil Rule

I. INCENTIVE AGREEMENTS

- (a) Restrictive equity awards
  - (i) 83(b) election provides for immediate vesting/ income inclusion
    - (A) if expecting an increase in value
    - (B) risk that value may decline below 83(b) price
  - (ii) Will not become worthless unless value drops to zero

(iii) Awards forfeited if not vested

J.

ETHICAL ISSUES.

1. REPRESENTATION OF THE BUSINESS ENTITY

(a) Conflicts

(i) Shareholders

(ii) Directors and officers

(iii) Employees