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Business Law
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Legal Matters®

Should you change your business structure in the wake of tax reform?

Following the enactment of the Tax Cuts and Jobs Act, many businesses are wrestling with whether to change their company structure.

The issue is whether to shift to a C corporation, which pays business taxes, or to remain a pass-through company, which pays taxes through the owners' individual returns.

Although taxes are not the only concern when choosing a company structure, they can be a deciding factor. The new tax bill cut the maximum corporate tax rate to 21 percent, down from a top rate of 35 percent.

However, most small businesses don't qualify for that reduced rate. That's because pass-through entities, which include LLCs, sole proprietorships and S corporations, are taxed at the owner's personal rate. And while personal tax rates also dropped, they can still be as high as 37 percent.

But the math isn't that simple. Many pass-through firms are eligible to deduct 20 percent of their income, effectively reducing their top rate, although the deduction phases out for service businesses



and others generating more than \$157,500 in individual income.

Immediate tax savings are not the only numbers that should factor into calculations. Owners should also consider how soon they expect to sell. Pass-through entities offer tax advantages at the time of sale, while gains from the sale of a C corporation may be

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Legal cautions when crowdsourcing your product

Crowdfunding is a growing resource for innovators and entrepreneurs.

Typically associated with startup innovations, it's a way to fund a special project by collecting money from a large group of people in exchange for a future, not-yet-built reward. In concept, crowd-funders get a good deal on your new product while you get the resources to get it off the ground.

Among the more notable products launched this way: Oculus Rift, a virtual-reality headset, which raised \$2.4 million in 30 days and was later sold to Facebook; the Pebble smartwatch, which raised \$30 million over two campaigns but ultimately shut down; Tile, a small Bluetooth-connected tag that can help you locate misplaced items; and Flow Hive, a honey tap for your beehive, which raked in over \$12 million.

Now, even well-established brands like GE, Hasbro, and Anheuser-Bush are using crowdfunding as a tool to test new ideas. Whether you're a hopeful startup or an established company, there are some legal issues you should consider before launching a crowdsourcing campaign of your own.

Fulfilling your contract

Crowdfunding campaigns through platforms such as Kickstarter, IndieGoGo and others are typically connected with some reward model: Fund us at X level, we'll give you Y. When you enter into such an agreement, you're creating what likely constitutes a legal contract. If your project is funded, you're obligated to deliver on your promises.

If something goes awry and you fail to deliver, you could be held in breach of contract. Depending on the size of your campaign, you could face claims from individual funders or a larger class action suit.

Truth in marketing

Overpromising or failure to deliver can open you to more than just breach of contract claims. You may be subject to false advertising or consumer protection laws or claims for fraud or misrepresentation.

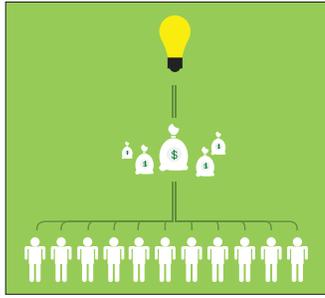
Reducing risk

Not that long ago, few companies could have successfully sold a product before it existed. But now crowdfunding has provided a relatively low risk way to validate your ideas and launch something new.

Here are some tips for using crowdfunding:

- ▶ **Protect yourself.** Before initiating a crowdfunding project, consider forming an LLC or other business entity that offers some personal asset protection.
- ▶ **Be realistic.** Think carefully about the rewards you offer. Be sure you can deliver the promised product.
- ▶ **Watch your wording.** Ensure the word "invest" (and variations thereof) does not appear anywhere in your pitch, unless you are actually engaging in an equity-based crowdfunding project.
- ▶ **Communicate.** If you're experiencing delays, be transparent with funders. Good communication can head off a lot of problems.
- ▶ **Plan for taxes.** Recognize that proceeds from the campaign are taxable. Include tax planning in your budget and consult an advisor about proper accounting methods.

Crowdfunding can be a successful way to launch a new project. But before you kick off a campaign, understand the legal risks and structure your project appropriately.



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Planning for the unplanned exit

What happens to business value when you die? If you're the CEO of a publicly traded company, stocks typically drop. Investors see risk and volatility and decide to get out before things go sour. If you're the owner of a privately held business, your entire legacy could evaporate.

A sudden death or disability can wreak havoc on your business. Who takes over and makes decisions in your absence? Will employees know what to do? Will customers have confidence that your company can meet commitments? Will lenders?

No one likes to think about issues like death and disability, but planning ahead is a way to protect continuity and preserve value. It's a way to ensure that everyone who depends on your business can

continue depending on it after you're gone.

Here are some of the things that could go wrong but could be avoided with proper planning:

- Business performance declines while family members and employees try to sort out new roles.
- Employees leave the business rather than risk an uncertain future, straining customer relationships and business value.
- Customers may switch vendors, not knowing if your company can continue to deliver on commitments.
- The business may default on contracts and owe penalties.

Should you change your business structure after tax reform?

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subject to both corporate and individual taxes.

If you do switch from an S corp to a C corp, you'll have to wait five years to switch back again. Then, for five years after you return to an S-corp, gains tied to the C-corp's assets will be taxed twice upon a sale.

The new law gives some businesses tax breaks, but the calculations aren't simple. Deductions

available to some businesses are not available to others. Other factors such as dividends, losses and estate planning may also impact your decision. There's no one size fits all answer. Consult an attorney to review the new tax rules and the specifics of your business operation.



'Warranty void' claims illegal

Let's say you make Acme Product 334, designed to work in tandem with Acme Widget 338. But one of your competitors sells a viable alternative to Widget 338. Can you predicate Product 334's warranty on the condition that it's only paired with Acme widgets? No, you can't.

It's an old law, actually, and one the Federal Trade Commission is enforcing. This spring, the FTC sent warning letters to six major companies that market and sell automobiles, cellular devices, and video gaming systems. (The FTC did not identify the companies by name.)

The FTC warned these companies against warranty agreements with provisions like these:

- The use of [company name] parts is required to keep ... manufacturer's warranties and any extended warranties intact.
- This warranty shall not apply if this product ... is used with products not sold or licensed by [company name].
- This warranty does not apply if this product

... has had the warranty seal on the [product] altered, defaced, or removed.

"Provisions that tie warranty coverage to the use of particular products or services harm both consumers who pay more for them as well as the small businesses who offer competing products and services," said Thomas B. Pahl, acting director of the FTC's Bureau of Consumer Protection, in a statement.

Language like the examples above are commonly found on many company websites. After the FTC statement was released, media outlet *Ars Technica* reported finding such language on websites for Hyundai, Nintendo, and Sony.

It's a good time to check your own warranty language to ensure you haven't included similar clauses, and if you still happen to be pasting one of those "warranty void if seal is broken" stickers over any of your components, it's time to peel them off. Just like the provisions above, those stickers are illegal under the Magnuson-Moss Warranty Act, which forbids blanket voiding of warranties based on aftermarket repair.

Planning for the unplanned exit

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- Banks may call in loans or terminate lines of credit due to uncertainty and a fiduciary responsibility to their stakeholders.
- Long-term, trusted employees may not receive the kind of severance pay you would have wished.
- Family conflict and litigation may ensue.
- The business may have to be liquidated or sold at a bargain value.

If the worst happens, your business needs to be ready to react almost immediately. Without a

plan, your spouse or family members may flail around in uncertainty, mourning your loss while learning how to oversee a business. Perhaps worse yet, the courts may appoint someone to take charge, running your company with no idea of your wishes.

Talk to your attorney about continuity plans that protect your company value and legacy. Without a plan, you leave behind cost, confusion, stress and anxiety. With one, you show a distinct level of care and courtesy for everyone who counts on you today.



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Companies facing web access lawsuits

The U.S. Department of Justice (DOJ) is no longer planning to issue regulations around website accessibility. Yet businesses around the country continue to face lawsuits claiming their websites are inaccessible to blind or low-vision users.

In late 2017, the DOJ announced it was rescinding its advance notices of proposed rulemaking on the issue of website accessibility under the Americans with Disabilities Act (ADA). That means there will be no regulation concerning website accessibility for the foreseeable future, leaving businesses with an unclear standard for compliance.

While fewer regulations may seem to be a positive development, the lack of an official standard means businesses are subject to the body of case law in this area. Unfortunately, the courts are filling the void with a patchwork of sometimes conflicting decisions.

In one case, a court held that Hobby Lobby Stores' website constitutes a "public accommodation" under the ADA. The court noted that the site allows consumers to purchase products, search

for store locations, view special offers, obtain coupons, and purchase gift cards.

In another case, a blind customer sued Winn-Dixie Stores because he could not use his vocalizing software to read the store's website. A federal judge ruled the lack of accessibility violated the man's rights under the ADA, even though no purchases can be made through the site.

In a case against CVS, a court held that the ADA applies to mobile apps and rejected the argument that it should dismiss the case because there are no legally binding standards for website and mobile accessibility. But another court held that it would violate Dominos' due process rights to find that its websites violate the ADA when the DOJ has not provided regulations around accessibility.

Despite the lack of regulations, plaintiffs are still bringing suits. *CBS News* reported that more than 800 website accessibility lawsuits were filed in 2017. While big name retail outlets are a prime target, recent filings suggest that credit unions and the hospitality industry may be next.

With the threat of a lawsuit (and customer



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convenience) in mind, it makes good business sense to have an accessible website. Talk to your web vendor or use one of the numerous scanning services available to determine if your site is accessible. If changes need to be made, find out if your vendor can comply with WCAG 2.0, accessibility guidelines issued by an independent industry consortium.

If you receive a letter threatening suit, consult an attorney before responding. This may also be a good time to review your insurance and determine whether you have any cyber or liability coverage that could cover the cost of defending a website accessibility lawsuit.