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Proper Counsel Can Help You Pursue the American Dream – and Avoid Nightmares

By Frank Lafalce

The economic recovery following the great recession has led to increased interest in the purchase and sale of small businesses. Anthony & Partners' experience is that a shockingly high percentage of buyers and sellers are not represented by counsel.

Many people may not remember the old Fram oil filter commercial of the early 1970s, during which a mechanic said, "you either pay me now for a relatively inexpensive oil change, or pay me a lot more later to replace your engine." Unfortunately, this rings true when applied to business buyers and sellers who fail to engage competent representation to guide them through the process.

Over the last few months, Anthony & Partners has come across several situations in which the parties to a small-business transaction tried to save a few thousand dollars of legal costs at inception, only to end up spending tens of thousands of dollars in costly litigation. Many relied on business brokers, who may be quite helpful in locating a desirable business, but who should not be relied upon to provide advice about due diligence and structuring of the transaction. In fact, their standard brokerage agreement disclaims responsibility for the accuracy of information provided by the seller and liability to either party to the transaction.

When buying or selling a business, there are several competing legal, tax, and business considerations depending on the structure of the transaction. There are two basic types:

1. Asset sales. This is preferable to most buyers because buying the equity of an existing company saddles a buyer with potential unknown liabilities, existing contracts and generally poor tax treatment. In an asset sale, buyers must make sure that the assets being transferred are free and clear of liens, are actually owned by the seller, and are in the condition consistent with the seller's representations and fit for continued business use.

2. Stock or purchase of an LLC's membership interest. This is preferable to the seller, as the buyer assumes the company's liabilities. In addition, the seller generally receives better tax treatment and there is no need to assign existing contracts and leases, or to transfer title to specific assets.

The financing of the purchase of a small business is also an area in which competent counsel and good tax advice can add value, saving clients from misery down the road. Often buyers are required or asked to pledge personal assets to secure the financing of the acquisition, and when seller financing is involved, there are risks on both sides. The seller takes the risk that the buyer will be unhappy with the purchase, and refuse to pay on the loan. The buyer takes the risk that the seller will use payment or other defaults to take the business back from the buyer quickly, and the buyer will thereby lose any equity that was already paid to the seller.

A new strategy that has been utilized over the last few years is the use of accumulated wealth in 401(k) plans or IRAs as the source of funds for a business acquisition. The IRS calls this strategy "Rollovers for Business Startups," or ROBS for short. This is a very complex area and there are many pitfalls with the use of retirement assets to purchase businesses, including the ones cited above. When properly structured, a ROBS is available, but it is a fluid area of tax law. A buyer contemplating this strategy should make sure they fully understand the risk and structure of the transaction with the help of their counsel and accountants.

While many people consider owning a business to be part of the American dream, don't let it become an expensive nightmare. Engage competent counsel at the outset to ensure you can sleep easy when the deal is done.

CASE NOTES

Whitney Bank v. Grant 2017 WL 3360822 (1st DCA)

The Grants entered into a short-sale agreement with Whitney Bank that specifically reserved the right for Whitney to pursue any "deficiency balance owed." The closing took place on May 11, 2012. Approximately $99,000 was left unpaid on the loan after the short sale. The bank filed suit on January 15, 2015, claiming that the Grants breached the promissory notes and still owed the deficiency balance.

The Grants claimed that the one-year statute of limitations applicable for deficiency judgments in residential mortgage foreclosures precluded the bank from collecting any deficiency. That statute states that an action to enforce a claim of a deficiency shall commence "within one year of the day after the issuance of the certificate of title by the clerk of the court or the day after the lender accepts a deed in lieu of foreclosure."

The appeals court reversed the lower court's decision that a short sale was intended to be covered by the statute, and stated that the bank still had the right to pursue the deficiency. The appeals court ruled that the plain language of the statute required either a certificate of title or a deed in lieu to trigger the shorter limitations period, and that the five-year limitations based on the promissory note would apply.

Saunders v. St. Cloud 192 Pet Doc Hospital LLC 2017 WL 3442736 (5th DCA)

This case concerned the interpretation of an arbitration clause in an employment contract. Dr. Saunders had an employment contract with the veterinary hospital, which required arbitration of any claim or controversy that "arises out of, or relates to, this agreement or breach thereof." Dr. Saunders subsequently filed a lawsuit alleging constructive termination due to a hostile work environment with claims of unlawful discrimination.

The hospital argued that the claim should be subject to arbitration as it arose out of her employment with the hospital. The appeals court disagreed, reasoning that she could have brought those claims even if she did not have an employment agreement, and that the claims did not arise out of the contract. The mere fact that the dispute would not have arisen but for the existence of the contract is not sufficient to make it "arising out of, or relating to," the agreement.

NEWS TO NOTE

Anthony & Partners was pleased to sponsor the cocktail reception at the 2017 FBA conference.

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STAFF NEWS

BRADLEY W. CROCKER

Bradley W. Crocker is an associate at Anthony and Partners, where his practice focuses on commercial litigation and advising startup companies. After studying accounting at Georgetown University, Bradley pursued his Juris Doctorate at the University of Florida Levin College of Law. As a law student, Bradley influenced the strategic direction of a D.C.-based hedge fund through legal-based research and served as a research assistant to Professor Robert Emerson.

Bradley was a member of the university's Antitrust Moot Court team, which earned national runner-up honors at the 2015 Global Antitrust Institute Invitational. He was also a member of the Business Moot Court Team, Florida Journal of International Law, and Florida Journal of Law and Public Policy.

Prior to joining Anthony and Partners, Bradley was an associate with a large, Florida-based litigation firm where he focused on litigation, transportation law, and business transactions. While there, he counseled a telehealth startup raising a $1MM seed round and assisted with multiple trials.

Education:

- University of Florida Levin College of Law, J.D. (2015)
  - *Cum Laude*
  - Antitrust Moot Court (Runner-Up, Global Antitrust Institute Invitational)
  - Business Moot Court
  - Florida Journal of International Law
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  - Book Award: Law & Entrepreneurship
- Georgetown University, McDonough School of Business, B.S.B.A. (Accounting, 2012)

Professional:

- The Florida Bar
- Associate Editor, ABA's TYL Magazine (2016-2017)
- Orange County Bar Association
- Executive Board Member, OCBA Insurance Law Committee (2016-2017)
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Practice Areas:

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