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Representing the Start Up Venture:

Basic Business Skills for Running a Successful Practice

Part I

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Representing a Start-Up Venture Part I

Basic Business Skills for Starting & Running a Small Practice

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Friday, November 16, 2018
NYC

9:00 a.m. – 4:30 p.m.

7.0 MCLE Credits; 7.0 Areas of Professional Practice

Sponsored by the Committee on Continuing Legal Education and the Law Practice Management Committee of the New York State Bar Association

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Program Description

The New York State Bar Association is pleased to present Representing a Start-Up Venture Part I.

Technically, any new business is a “startup,” regardless of what it does. But there are significant differences between a “small business” engaged in a basic retail or service business operated by its founders, and a “venture startup” backed by outside investors that is engaged in a manufacturing, high technology, e-commerce, Internet or media business. One of the most common mistakes business attorneys make is to confuse the two, assuming that what works for an antiques store will also work for an e-commerce website.

When representing an entrepreneurial company, you cannot afford to be a “specialist”. Your client will expect at least a certain level of familiarity with corporate, contract, intellectual property, employment, international, immigration, tax and securities law issues they will face in building its business and raising capital. As fast-moving, demanding risk takers with limited funds to pay for legal services, startup ventures and their founders will also challenge your time management, client management and ethical practice skills to the utmost.

This program focuses on representing the venture startup and dealing with the often complicated legal, tax, financial and ethical issues involved in working with fast-growing enterprises run by time-challenged entrepreneurs and backed by professional investors.

Program Agenda

8:30 a.m. **Registration**

9:00 a.m. – 9:10 a.m. **Introduction and Overview: The Small Business vs. The "Startup" Venture**

Clifford R. Ennico, Esq.
Law Offices of Clifford R. Ennico
Fairfield, CT

9:10 a.m. - 10:00 a.m. **Choosing the Right Legal Entity for a Startup Venture**

- Limited Liability Companies vs. S Corporations
- When is a "C" Corporation the Right Choice?
- Should your form an LLC in New York City?
- Forming in New York vs. Delaware or Nevada
- Finding Out if a License is Needed for the Client's Business

Maureen Crush, Esq.
Crush & Varma Law Group, P.C.
Fishkill, NY
(1.0 Areas of Professional Practice)

10:00 a.m. – 10:10 a.m. **Break**

10:10 a.m. – 11:00 a.m. **Corporate Shareholders' Agreements and LLC Operating Agreements**

- Identifying the Owners and their Percentage Ownership
- Management Provisions
- Voting Provisions Including Supermajority Voting Requirements
- Confidentiality, Non-compete and "Assignment of Invention" Provisions
- Tag-Along, Drag-Along, Pre-Emptive and Other Rights of Investor-Shareholders
- "Buy-Sell" Proviosions
- Other Common Provisions

Maureen Crush, Esq.
Crush & Varma Law Group, P.C.
Fishkill, New York

Clifford R. Ennico, Esq.
Law Offices of Clifford R. Ennico
Fairfield, CT
(1.0 Areas of Professional Practice)

11:00 a.m. – 11:50 a.m.

Your Client's "Social Mission": For-Profit, Not-for-Profit, Benefit Corporation or "B Corp"?

- Benefit Corporations in New York
- Benefit Corporations vs. "B Corps"
- Pros and Cons of Not-for-Profit Corporations under New York's Nonprofit Revitalization Act
- "Even Bad Wolves Can Be Good": Structuring the Business (For Profit) Corporation for Social Benefit

Clifford R. Ennico, Esq.
Law Offices of Clifford R. Ennico
Fairfield, CT
(1.0 Areas of Professional Practice)

11:50 a.m. – 1:00 p.m. **Lunch** (on your own)

1:00 p.m. – 1:50 p.m.

Basic Tax Issues for the Startup Venture

- Income Tax Issues for LLCs and Corporations
- Sales and Use Tax Issues for Online Businesses
- Working with your Client's Accountant or Tax Advisor

John M. D'Aquila, CPA, CGMA
D'Aquila & Company LLP
Jacksonville Beach, FL and New Rochelle, NY

Clifford R. Ennico, Esq.
Law Offices of Clifford R. Ennico
Fairfield, CT
(1.0 Areas of Professional Practice)

1:50 p.m. – 2:40 p.m.

Capitalize the Startup Business

- Debt vs. Equity
- Putting Money Into, and Taking Money Out Of, a Limited Liability Company
- Shares of Stock vs. "Units of Membership Interest"
- Voting vs. Nonvoting Equity
- Can You Have Preferred Equity in a LLC?
- Options, Warrants and Convertible Notes
- "Strip Rights" Contingent on Change in Control
- "Friends and Family" Offerings

John M. D'Aquila, CPA, CGMA
D'Aquila & Company LLP
Jacksonville Beach, FL and New Rochelle, NY

Clifford R. Ennico, Esq.
Law Offices of Clifford R. Ennico
Fairfield, CT

(1.0 Professional Practice)

2:40 p.m. – 2:50 p.m. **Break**

2:50 – 3:40 p.m. **Intellectual Property Issues of the Startup Venture**

- Best Practices for Trade Secret Protection
- Requirement and Procedure for Obtaining and Enforcing Patents
- Establishing and Protecting Trademark Rights
- Scope of Copyright Protection and Registration

Teige Sheehan, Esq.
Heslin Rothenberg Farley & Mesiti, P.C.
Albany, NY
(1.0 Areas of Professional Practice)

3:40 – 4:30 p.m. **Representing the Web-Based Venture**

- Legal Review of Your Client's Website
- Drafting the User's Agreement, Privacy Policy and Other Web Contracts
- Your Client's Liability for Third Party Activities Their Sites: Does 47 USC § 230 Still Hold?
- Our Privacy vs. Their Privacy: Should You Be Concerned About Europe's New GDPR?
- Taxation of e-Commerce and Internet Sales
- Buying and Selling the Web-Based Business

Clifford R. Ennico, Esq.
Law Offices of Clifford R. Ennico
(1.0 Areas of Professional Practice)

4:30 p.m. **Adjournment**

Accessing the Online Course Materials

Below is the link to the online course materials. These program materials are up-to-date and include supplemental materials that were not included in your course book.

www.nysba.org/StartUpVenturePartOneMaterials

All program materials are being distributed online, allowing you more flexibility in storing this information and allowing you to copy and paste relevant portions of the materials for specific use in your practice. WiFi access is available at this location however, we cannot guarantee connection speeds. This CLE Coursebook contains materials submitted prior to the program. Supplemental materials will be added to the online course materials link.


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These Rules of Professional Conduct were promulgated as Joint Rules of the Appellate Divisions of the Supreme Court, effective April 1, 2009, and amended on several occasions thereafter. They supersede the former part 1200 (Disciplinary Rules of the Code of Professional Responsibility).

The New York State Bar Association has issued a Preamble, Scope and Comments to accompany these Rules. They are not enacted with this Part, and where a conflict exists between a Rule and the Preamble, Scope or a Comment, the Rule controls.

This unofficial compilation of the Rules provided for informational purposes only. The official version of Part 1200 is published by the New York State Department of State. An unofficial on-line version is available at www.dos.ny.gov/info/nycrr.html (Title 22 [Judiciary]; Subtitle B Courts; Chapter IV Supreme Court; Subchapter E All Departments; Part 1200 Rules of Professional Conduct; § 1200.0 Rules of Professional Conduct).

http://nycourts.gov/rules/jointappellate/NY-Rules-Prof-Conduct-1200.pdf

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Representing the Start Up Venture Part I:
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Topic One:

Choosing the Right Legal Entity for a Startup Venture

CHOOSING THE RIGHT LEGAL ENTITY FOR A START-UP BUSINESS

Presented by: Maureen Crush, Esq.
Crush & Varma Law Group P.C.
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A. Limited Liability Companies vs. S Corporations

1. General Overview.

The most common legal structures for small businesses in the United States are sole proprietorships, partnerships, limited liability companies and corporations.

Although we all know that many successful technology and product companies have started in garages, most choose at some point to form an entity and the most common legal structures in the United States for a start-up ventures are the corporation and limited liability company.

Some of the aspects to be considered when deciding upon the legal structure for a start-up business are:

•Requirements, complexity, and costs involved in setting up the legal structure
•Ownership and control of the business
•Liability for business obligations or losses
•Continuity of the business and transferability of ownership
•Taxes on earnings
•Sources of Capital

The details that make the choice of limited liability company or corporation relevant will be discussed at length further on. No matter which entity is selected, the relationship of the owners is set out in written agreement – an operating agreement in the case of an LLC and a shareholders' agreement in the case of a corporation.

As lawyers, we understand that creating a legal entity for a startup will establish much-needed separation between the owners and the business and that shielding the owners' personal assets is the first and foremost reason to think about forming an entity.

But, when it comes down to choosing a business structure, small business owners are typically concerned about one thing: cost. Costs, includes filing fees, legal fees to advise and draft necessary documents, and a large concern, taxes on an ongoing basis. Somewhat hidden costs also include those which can vary from state to state:

- Costs to transfer property to the entity
- Commercial registered agent fees if required
- Ongoing costs of entity maintenance – franchise fees
- Annual costs to maintain status and protect liability for the owners (maintaining required formalities of annual meeting minutes, etc.; tax filings and returns)
- Bank fees
- Cost of revised stationery, signs, business cards, form contracts, etc. to reflect corporate name and business titles.

2. Double Taxation

We are discussing the LLC and S Corporation primarily, because of the issue of "double taxation" which tends to drive the choice for the start-up venture. There are solid reasons to incorporate as a C Corporation which we will discuss later, for example, the C Corporation is the preferred structure if you intend on seeking venture capital funding or taking the company public. But forming a C Corporation is not necessary at the start-up phase in most instances and does involve potential double taxation.

When it comes to taxes, a C Corp is a separate "person" a separate tax payer that files its own federal and state (where applicable) tax returns. This means that profits are first taxed with the corporation at the corporate level. Then, if the corporation decides to take that profit and distribute dividends to shareholders, the dividends are taxed again on each shareholder's personal tax return.

Both the LLC and the S Corporation avoid this double taxation burden. With these business structures, the company is taxed more like a sole proprietor or a partnership than as a separate entity, like the C Corporation.

Company profits are "passed through" and reported on the personal income tax return of the shareholders or members in the case of the LLC. In fact, if the LLC has only one member, the LLC would be deemed a 'disregarded entity" for IRS tax purposes and income would be reported on the Schedule C of the owner as if he was operating a sole proprietorship.

As expected, nothing is ever so simple when it comes to the world of business taxes. Discussing your client's particular situation with his or her trusted tax advisor or accountant can go a long way to helping the client determine which business structure and tax treatment is optimal.

3. The LLC and S Corporation Benefits and Disadvantages

All corporations start as C Corporations. In the absence of filing the "S Election Form (remember to file both at the Federal (IRS) level Form 2553 and the state level New York Form CT-6 or other state equivalent), the entity will be taxed as a C Corporation.

Both the LLC and S Corporation offer pass-through tax treatment. Both offer liability protection and will protect owners' personal assets from potential liabilities of the entity with limited exceptions (e.g., trust fund taxes, OSHA violations, certain environmental liabilities).

Yet, the LLC and S Corporation feature some key differences as well. Choosing the right business structure can be a daunting task for the start-up business owner or entrepreneur.

If we set aside the traditional C Corporation for a moment as overkill for most small businesses simply because of double taxation, how do you choose to advise your client between S Corporation and LLC?

The similarities between these two business entities are significant, but the differences can be even more striking. While circumstances vary for each individual and his or her business, here are some general guidelines to help you understand the differences and their impact on your client's business.

1. Business Formality

With its roots as a C Corporation, the S Corporation involves structure, formalities and compliance obligations, which can be seen as burdensome for the solo entrepreneur, in other words, a "payroll of one." If a client incorporates as an S Corporation, the client will need to set up a board of directors, file annual reports and other business filings, hold shareholder's meetings, keep records of meeting minutes, and generally operate at a higher level of regulatory compliance than the client might need or want to deal with. With the LLC, this is not the case. LLCs once formed operate more informally through an operating agreement.

IN SUM: If a client wants less red tape and formality, the LLC can provide greater simplicity. But there are other factors to consider.

2. Who Can Be an Owner?

The S Corporation has more restrictions in terms of who can be an owner. For example, an S Corporation cannot have more than 100 shareholders. Of course, this limitation is probably not of much consequence to many small businesses. In addition, all individual shareholders of an S Corp must be either U.S. citizens or permanent residents (with a small exception for certain trusts not covered in this program). Historically, a trust could be a shareholder of an S-corporation in extremely limited circumstances. The Tax Cuts and Jobs Act expands the circumstances in which a trust can hold shares in an S-corporation, enabling a nonresident alien to be a current potential beneficiary if the trust qualifies as an E.S.B.T. (Electing Small Business Trust).

By contrast, LLC's have no limit on the number of owners, but importantly, owners can be individuals or other entities, including other LLCs, corporations, partnerships, etc. This is great flexibility depending on the owners/founders involved with the entity.

IN SUM: If you have nonresident alien owners (or would like an LLC or Corporation or other entity to be a shareholder), you cannot form an S Corporation and should opt for the LLC unless they owners meet the limited exceptions of a qualified trust or an Electing Small Business Trust.

3. Income Allocation

In an LLC, income and loss can be allocated disproportionately among the owners provided there is a rationale business justification for the allocation being made. By contrast, in the S Corporation, income and loss are assigned to each shareholder strictly based on their pro-rata share of ownership which is mandated by the S Corporation tax rules of operation.

IN SUM: If a client needs flexibility when it comes to division of profits among owners, the LLC is the preferred structure.

4. Pass-Through Losses

With LLCs and S Corporations, members and shareholders are able to pass company losses to their personal income reporting. In some circumstances, the LLC allows clients to pass through more loss than in an S Corporation, most notably when the entity has financed real property. In an LLC used for real estate investments, members are allowed to add the amount of the mortgage to their basis for the purpose of computing a loss. Clearly, that can add up to a significant difference in a client's tax situation.

IN SUM: If a client is setting up a business structure for real estate investments, the LLC allows the client to write off more losses on his or her personal tax reporting.

5. One Class of Stock Rule

In an S Corporation, all shareholders own only one class of stock. An S Corporation can have voting and non-voting shares, but cannot have distinctions like common stock and preferred stock. It cannot give preferential decision making (superior voting/veto voting) rights to one owner over others (although it can have voting and non-voting shares) or preference on sale or dissolution. It cannot pay a premium return to one shareholder, the basis for many start-up arrangements. In an LLC, however, these priorities and preferences are allowed, and you can have different membership classes with different rights and premium payments.

IN SUM: A client cannot offer common and preferred stock classes or similar preferences in operations in an S Corporation. If a client likes or needs flexibility in ownership classification and rights, the LLC is the choice.

B. Should You Form an LLC in New York City?

LLC's have a requirement for publication in local newspapers selected by the County Clerk of the county in which the LLC claims to be operating. Unfortunately, in New York City, the cost of publication is very expensive. The New York County Clerk has designated the New York Law Journal being one of the approved and in fact, a mandated newspaper, for purposes of publication.

Clients who have alternative places of business outside New York City will often seek to use those as the place of record for the business if feasible.

C. When is a "C" Corporation the Right Choice?

1. Reinvesting Profits

As pass-through entities, individual owners of an S Corporation or members of an LLC are liable for any taxes owed on profits — whether that money is retained in the company or distributed to owners. This is known as "phantom income," and can obviously cause a problem for owners who have to report and pay without necessarily receiving the cash to do so.

If your client plans to retain money in the company and would prefer not to have shareholders/members be personally taxed on this money as would happen in the S Corporation or LLC, the recommendation could be that the client should consider the C Corporation over both the LLC and S Corporation. Of course, each client's specific situation may vary and other factors may weigh more heavily. This is another reason to consult with your client's accountants on the choice of entity for the start-up business.

2. Venture Capital Funding

Lastly, since we are discussing technology and product start-ups, if a client is considering raising venture capital down the road, VC firms will most likely choose the C Corporation as the type of legal entity for their investments. This does not necessarily mean your client's business needs to start as a C Corporation, the client will need to convert the business to a C Corporation (check state laws to

be sure your state permits such conversions-notably LLC's which are frequently problematic). This conversion may also require additional filings and fees. If the client believes venture capital financing may be likely, and other factors are not weighing in favor of the LLC too heavily, you should consider the S Corporation as the preferred option for that client as converting an S Corporation to a C Corporation can be done simply with a new tax election form filing with both the Federal government (IRS) and State.

Choosing the right business structure is a multi-faceted decision, and will ultimately depend on all the unique aspects of your client's particular business needs, vision and circumstances.

Consulting with an accountant or tax advisor can go a long way in helping you assist your start-up client determine which business structure offers the biggest advantage for their situation.

There will be further discussion in more detail on the tax aspects of entity selection later in the program.

D. Forming in New York vs. Delaware or Nevada-What about Wyoming?

For purposes of this seminar, we will discuss four prevalent locations for incorporation currently in the United States and basic factors of each, Commonwealth of Delaware, State of New York, State of Wyoming and State of Nevada. There is a continuing discussion of the "best" place to incorporate and my advice to each client is to think through the benefits, advantages and disadvantages before leaping to a conclusion and to recheck the facts as state laws frequently change in this area. Each of Nevada, Delaware and Wyoming are typically referred to as "corporate havens" due to perceived friendliness and lower

cost of doing business. New York is also discussed in this section of where to incorporate both because it is the local jurisdiction to many taking this seminar, but also because it has well developed laws and protections and many of the "special" reasons people seek to incorporate outside of New York do not apply to the bulk of businesses being formed.

I. Nevada:

Once an incredibly popular place to incorporate, times have changed as Nevada has adopted certain fees and license payments that are making Wyoming more attractive. Notwithstanding, the benefits of Nevada incorporation are:

- Protects directors and officers from personal liability for acts committed on behalf of the corporation or by the corporation (except for fraud). In fact, such protection is statutory in Nevada and protection is offered for
  - Acts or omissions not in good faith
  - Acts or omissions that occurred prior to the date of an indemnification statute
  - Transactions involving undisclosed personal benefit to an officer or director
  - Breach of duty of loyalty by a director
  - Monetary damages incurred through acts of officers (directors are exempt)
- High degree of privacy – does not share information with the Internal Revenue Service and no shareholder information is publicly available.
- No corporate income tax.

- No franchise taxes.
- No taxes on corporate shares.
- No personal income tax.
- Law requires only one director.
- No minimum capital is required.
- Established case law.
- No gift or estate tax.

The negatives of incorporating in Nevada are:

- Continued union and educational factions push for business taxes to be put in place.
- "Business License" fee of $200 per corporation per year has been imposed for all "non-resident" corporations and Officer Fee of $125 must be paid thirty (30) days after incorporation (looks like a substitute for the annual "franchise fee" paid in other jurisdictions.
- Since limited information is provided to the IRS, Nevada corporations are more frequently audited.

II. Wyoming.

Wyoming has become much more popular as a place to incorporate lately. Incorporation in Wyoming offers the following benefits:

- Cost (about 75% less to incorporate in Wyoming than Nevada).
- No state income taxes and no push for such a tax.
- No information collected to be shared with the Internal Revenue Service.
- Shareholders are not listed with the state.

The negatives of Wyoming incorporations:

- Case law is less established.

- Lack of prestige.

III. Delaware

Delaware is still the choice of incorporation for publicly-traded entities due to the well-developed body of case law and familiarity of the Delaware courts in interpreting it.

Benefits and advantages of Delaware Incorporation:

- Court of Chancery – a court which hears only business disputes and has over a 100 year history of well-developed case law. This removes the corporations from the whims of civil court that might see big businesses with suspicion or deep pockets.

- Corporate income tax only applies to entities doing business in Delaware (most entities formed there do business in a foreign jurisdiction so they have no corporate tax). Tax is proportional to the business done in the state.

- Image and prestige of being incorporated in Delaware which can be important in instances such as raising capital.

- Business friendly atmosphere should keep fees in check.

Disadvantages:

- There are franchise fees payable which are higher than most states.

- Disclosure of information is required as to shareholders, directors and officers.

- There is a personal income tax.

IV. New York

New York still has a large number of corporations filed with its Secretary of State.

Benefits and Advantages of New York incorporation:

- Local and if doing business here, your client will be paying taxes here.

- Start-up breaks (see later discussion under Financing the Entity and "StartUp New York program, generally)

- Well-developed law

- Good reputation

Disadvantages of New York incorporation:

- High taxes

- Franchise fees

- Cost of publication for LLC's

Notwithstanding, more often than not, a small business operating out of New York is well advised to incorporate in the Empire State. While you could theoretically incorporate your client in any of the 50 states (including Delaware), incorporating in another state such as Delaware adds additional costs and almost no benefits to the small business corporation.

Let's look at the usual statements offered in favor of Delaware:

You do not pay income taxes in Delaware (if you are not doing business there): That may be true, but your client will pay taxes in New York if you do business in New York regardless of the state of incorporation. All corporations doing business in New York are subject to New York's franchise taxes. (See Section 209 New York Tax Law).

More than 50% of all corporations listed at the New York Stock exchange are incorporated in Delaware: True; but just because larger, publicly-traded

companies are doing this, small start-up companies do not traditionally do this. If there are no plans to go public soon, this is not a benefit. Your client can always form a Delaware corporation and merger with it to establish Delaware as its state of formation.

Delaware is the most sophisticated jurisdiction when it comes to corporations: Granted, Delaware and its laws are known to be very business friendly. A small business corporation doing business in New York is unlikely to encounter situations where the differences in New York law and legal system to Delaware law and legal system really matter.

It saves you money to incorporate in Delaware: While actual filing fees may be less, as mentioned previously, if your client incorporates in Delaware, but does business in New York, there are additional expenses:

1. A foreign corporation has to get authorization to do business in New York (Section 1304 Business Corporation Law). There is a fee.

2. A foreign corporation has to pay a license fee to do business in New York (Section 181 (1) New York Tax Law). The one-time fee depends on the number of issued shares (par value or non par value).

3. A foreign corporation has to pay an annual maintenance fee (Section 181 (2) New York Tax Law).

4. A Delaware corporation has to appoint a registered agent in Delaware who is responsible for receiving governmental and legal papers for the corporation. There is an ongoing fee to maintain the registered agent.

E. Is a License Needed for the Client's Business?

As just mentioned, a foreign corporation has to pay a license fee to do business in New York. See Section 181(1) New York Tax Law. The same is true in Nevada, businesses incorporating in Nevada will have to obtain a business license whether they are operating their business in Nevada or not. This is not the case in Delaware, as entities incorporating do not have to have a business license if their business is not physically located in Delaware.

Other forms of license which a business may need have to do with the nature of the business itself and both state law and federal law should be consulted to determine what is necessary. As we are familiar, many professional entities require owners to maintain licenses to operate. A significant number of health care entities require licenses to provide services. Entities affecting the safety of the general public are also often licensed – auto mechanics, home inspection, insect abatement and removal. License requirements affect both technology/service industries as well as product industries. In New York, the Office of the Professions website can be viewed and discusses licenses in general.

Topic Two:

Corporate Shareholders' Agreements and LLC Operating Agreements

What Are “Buy-Sell” Provisions?

- Owners of closely-held businesses want to keep ownership of business “in the family”, with no ownership by “outsiders” who don’t add value
- When an owner dies, his/her shares may be transferred to an “outsider”
- When an owner withdraws from the business (or is forced out), he/she becomes an “outsider”
- When an owner divorces or files for bankruptcy, his/her shares may be transferred to an “outsider” by operation of law

Your Goals in Drafting “Buy-Sell” Provisions

- Provide for a repurchase of shares/equity by the company and/or the other owners when an owner dies or otherwise withdraws (voluntarily or involuntarily) from the business;
- At a price that is fair to both the company and the withdrawing owner; and
- In a way that ensures that any dispute about the value of a shareholder’s/member’s shares is resolved cleanly and quickly, so the remaining owners can get on with their business

The Bad News

"It is virtually impossible to
draft a buy-sell agreement that
will satisfy all three of these goals.
This is one of the many reasons
you carry malpractice insurance."

--- Clifford R. Ennico
November 16, 2018

The Best You Can Do

- Formulas usually don't work for tech ventures
  - Often no revenue, profits, only intangible IP assets
- Comparables fall within a wide range
  - In 2015 Facebook paid $2.0BB for What's App, a company with no revenue or profits!
- See handout for a possible solution

CORPORATE SHAREHOLDERS' AGREEMENTS AND LLC OPERATING AGREEMENTS

Presented by: Maureen Crush, Esq.
Crush & Varma Law Group P.C.
21 Old Main Street, Fishkill, NY
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Identifying the Owners and Their Percentage Ownership

Because owners usually share in the future value of the company— whether in the form of profits, stock holdings, membership units or other arrangements—decisions as to who will be an owner should be made according to the expected contribution of each individual to the enterprise. It is not an easy task to look into the future to determine who will share and in what proportion, in the value created by the company.

The owners usually are comprised not only of the founders, but also frequently key management personnel that are identified as being necessary for the success of the venture. Some people refer to them as the "five C's" or the "C Suite" (CEO, CMO, COO, CTO and CFO). Although not required, it is common for the C Suite to receive some level of stock or membership rights in connection with their commitment and service to the start-up. There may also be owners who have made available the capital, contributed intellectual property and those who have provided sweat equity. Above all, is the person or persons who have developed the idea/concept for the business. Some or all of the roles of the five C's can be filled by persons who have contributed capital, IP, sweat equity, etc.

A brief summary of these management roles is as follows:

The CEO/President is typically the founder within a startup, but not always. Sometimes the founder does not have the required skill set to be the visionary, set long term strategy and direction and achieve placement for the company in the competitive environs. Personality-wise, the CEO needs to be able to meet with key investors and strategic partners. Some organizations have both a CEO and President with the CEO continuing the outward presence and the President facing inward to manage the day-to-day operations.

The CMO (sometimes called CSO) of an organization is in charge of all marketing or sales driven activities of the business. This role drives new leads for the business whether B2B or B2C and getting customers to engage in repeat sales. Revenue will make or break a business so this role is sometimes called a Chief Revenue Officer, as without effective marketing or sales leadership, there will be no revenues.

The COO is in charge of operations of the company (can be duplicative of the President role) with the exception that the President manages all of the 5 C roles.

The CTO is in charge of all technology for the company. This technology could be the entire lifeblood of an "e-commerce company." Or more routine as in management of the back office systems and software that keep the business functioning. The more critical the role that IT plays in your company, the more important the CTO is to the organization.

The CFO is in charge of all financial activities - accounting, budgeting, cash management and reporting for the company – and supervision of office staff supporting those functions. The CFO also maintains the relationships with outside CPA firms and bankers. In a startup, the CFO is also the controller and treasurer of the business, managing all accounting and cash decisions themselves, until the business gets to the scale it can afford a bigger staff.

Owners can also be other key employees your client desires to incentivize to stay and perform or to reward for loyalty and service already given. Once you have identified the owners, you will need to decide how much of a percentage interest they should receive and in what form that interest will be granted.

Due to the different types of contributions made by owners as well as their continuing value to the company, it is difficult to make determinations as to percentages – how to divide up the equity stake in the company.

Although there are different schools of thought, it is common to place a big premium on being the originator of the idea for the product or technology on which the company is based. Assuming two founders in a small entity, that would mean that a 50/50 split between the two co-founders might be along the lines of two-thirds/one-third if a premium is given to the original idea and for starting the initial development efforts and finding the original management team.

It would also follow that people who fund the business should get a premium, because cash funding founders are acting no different than a seed stage investor. If we start again with the 50/50 split, an adjustment would seem warranted for cash investment.

Key executives (five-C's) should get a premium stake over non-key executives (e.g. office manager or graphic designer).

If we accept that hierarchy, total ownership would be divided by employee tiers. So, in this case, something like the following:

Owner	Ownership %	Total for Tier	Total
Founder (idea)	20%		
Founder (development)	10%		
Founder (funding)	10%	40%	40%
CEO	5%		
CFO	5%		
CSO	5%		
CMO	5%		
CTO	5%	25%	65%
VP	2%		
(Assume 10 persons receiving 2%)		20%	85%
Director and Manager Level Staff	1%		
(Assume 15 persons at this level)		15%	100%

As happens in start-up ventures, there are sometimes people who do not take a salary. Leaving the cash in the company is similar to financing the business. If a person is deferring salary, the amount deferred should also be considered a stake in the company in some percentage as others.

Once there is an understanding of how the percentages of ownership should be aligned, there is then the further discussion of vesting of owners' stock and mechanisms to get back unearned equity into the company in the event of an owner's departure. The later section on options and warrants provides further details.

Management Provisions

Management provisions in a shareholders or operating agreement are critical to enabling the Founders to continue to manage and control the operations of the Company. A corporation has several documents which impact management. The bylaws will set out the authority of each person, including the directors and officers which may include all of the C Suite members previously discussed. In addition, the provisions of the shareholders agreement or operating agreement can set forth any special management authority granted to one or more classes of shares or membership units. The shareholders agreement or operating agreement will also set forth authority agreements as to the selection of board members (in a limited liability company, you can keep the traditional hierarchy of a board of managers if desired or required by funders, but it is not that common). In Venture Capital financing it is common for the VC to request a seat on the Board of a corporation as a director more to monitor and advise than to exert control in any way. Those provisions are set out in the term sheet provided and in the final documents for the investment transaction. In addition to the bylaws and shareholders agreement or operating agreement, there are also employment term sheets or employment contracts with key persons which may also contain provisions relating to management authority or responsibilities. It is therefore incumbent on counsel to be sure that all relevant documents are checked and provisions included to be certain management of the company in its various capacities stays in the hands of those who have negotiated that right.

An LLC can be established as a member-managed entity or as a manager-managed entity. As a startup's decision making and power is often driven by ownership, it is more common that management is by the members to preserve each owner's say in certain matters as a percentage of vote. There certainly can be an operating manager appointed for the day-to-day operations (or a board of managers as discussed above) and the flexibility of LLC's permits titles, such as the Five C's, to be given to employees/owners. As owners of an LLC are not traditional employees, but most often partners who are given draws rather than W-2 wages, the equivalent of an employment term sheet or contract would be a guaranteed payment agreement, which may also spell out the obligations and rights of the particular partner as to management. The LLC operating agreement, however, is the most relevant document and traditionally sets out which person shall act as manager, successor manager and tax matters partner (to deal with all tax return and tax election issues).

Voting Provisions including Supermajority Voting Requirements

While management of a corporation or limited liability company can be included in various agreements as discussed above, a shareholders agreement or operating agreement will also set out the voting provisions both as to common and preferred shares or membership units (if voting preferred). Again, as it is not the intention of investors in the traditional sense to impact management, vote by investors is usually limited to those aspects that could impact its investment in a serious way rather than day-to-day determinations. In those instances where the investor vote is required, either it is required that the investor consent affirmatively to the action or that the action require a supermajority vote of 66 2/3rd or higher in order for it to pass. Note that for any corporate entity with differing voting rights, only a C corporation can be used. S corporations cannot permit different rights to vote or preferred shares.

While not exactly a management issue per se, in order to prevent their ownership interest from being diluted by future issuances of shares, investors will typically require that they be given the right to participate in any subsequent offering of shares, options, warrants or other securities.

Restricting Transfers of Shares and Membership Units

A shareholder agreement or operating agreement should clearly set out any restrictions or obligations related to the equity units and will typically include a general prohibition on transferring equity, or any rights or obligations under the shareholder agreement or LLC operating agreement, except as specifically permitted in the agreement or as consented to by the equity owners (or a defined group of equity owners, e.g., holders of x percent of the preferred shares or units).

There normally is some flexibility built into the agreement so that shareholders or membners can deal with their shares efficiently for tax planning purposes – known as "permitted transfers". For example, where the shareholder/member is an individual (e.g., a founder), such equity owner should ensure that the shareholder/operating agreement permits him to transfer his ownership to an entity wholly-owned by him or his family members, a custodian, trustee (including RRSP, RIF, IRA or similar retirement or investment fund) or other fiduciary for the owner, and/or his family members, or any other person if such transfer is effected pursuant to the owner's last will and testament, or, where there is no will, applicable laws dealing with the succession of property upon death.

In case of a permitted transfer, the shareholders agreement or operating agreement should state that any transfer is conditional upon the transferee agreeing to be bound by and becoming a party to the applicable agreement.

In addition to the general restrictions on transfer, in startup ventures where it is anticipated that professional investors may be sought, the shareholders or operating agreement should include a right for the entity to repurchase the equity owned by a founder on the death, disability or insolvency of the founder, or on the involvement of the founder in a division of net family property as a result of marital breakdown or in the event of such investment possibility (which investment may require control of 100% of issued shares). Such a repurchase right may instead be included in a separate founder share or equity repurchase agreement. This is discussed in more detail below as are rights of first refusal and other preemptive rights.

Confidentiality, Noncompete and "Assignment of Invention" Provisions

In a startup product or technology company, the product idea or technology under development is often the most valuable asset of the company. It is critical to have not only confidentiality agreements respecting the confidential nature of the company's information, but, in many instances, noncompetition agreements with key employees and founders. The company must restrict those who have the capacity to impact the company's success if their knowledge developed in connection with their service to the company or knowledge/product idea which they or others sold or transferred to the company for consideration, could be harmful if made public or used in competition with the company or transferred to a third party for use. In the technology and product development communities, Assignment of Invention agreements are required to the extent such key employees or founders have rights to same under law. These rights can be both brought to the company upon employment or can be acquired during employment as services are provided, so both instances must be covered. There are also Assignment of IP and Other Assets agreements entered into in which the owner of rights is assigning and contributing those rights to the company in exchange for compensation – which could be ownership equity in the company. In these Assignment agreements the assignor also makes representations as to ownership and rights to the property assigned and a schedule is attached describing the intellectual property or other property being assigned in connection with the agreement. It is also proper to have the spouse of the assignor sign these agreements to avoid any claim of marital property rights in the asset being assigned.

Other Common Provisions

Shareholders Agreements and Operating Agreements also contain other more standard provisions relating to the following:

- Valuation – it is critical that the method of valuing shares and membership interests be set forth. Valuation methods may change depending upon who the member or shareholder is that

requires the valuation and the circumstances requiring the valuation to occur. Death, disability and withdrawal of an owner being the most common. In the startup venture arena, valuation for purposes of investor equity is of huge importance and impacts further investment potential once valuation is determined.

- Permitted Transferees – as discussed above, there are numerous persons or possibilities for sale, transfer, repurchase and assignment of shares and membership units, each with unique terms dependent upon the deal.

- Payment Terms – Once valued, if shares or membership interests are to be repurchased, the terms of repayment (number of payments, down payment, interest rate, security, voting during repayment, default rights) must all be put in place at the time the interests are reacquired by the company or a third party (if permitted as a transferee).

- Jurisdiction and Governing Law – important to be clear if the requirements of law of a particular jurisdiction are to be applied and a convenient forum used in the case of litigation.

- Amendment of the Operating Agreement or Shareholders Agreement – this provision should contain the percentage of vote required to amend the agreement and specification of any provisions which cannot be amended without consent of particular parties or supermajority vote should be clearly specified.

Grant of Power of Attorney – it is often useful to have all shareholders or members grant a power of attorney to the company to arrange for the transfers of all shares or membership interests as provided in the agreement and to have such power coupled with an interest.

Dissolution – consideration needs to be given to whether or not the owners of the entity should agree that the entity cannot be dissolved except by a certain percentage of vote and that otherwise, shareholders and members waive any right to seek dissolution.

Co-Terminus Provisions – it may be prudent to provide that termination of rights as a shareholder or member also terminate rights as an officer, director or manager as the case may be. Frequently, these provisions specify that the terms of any employment or similar agreement that are not dependent upon share or membership ownership are not affected by the sale or transfer.

Topic Three:

Your Client's "Social Mission": For-Profit, Not-For-Profit, Benefit Corporation or "B Corp"?

Text of Article 17 of New York Business Corporation Law
(Benefit Corporations)

ARTICLE 17
BENEFIT CORPORATIONS

§ 1701. Application and effect of article.

(a) This article shall be applicable to all benefit corporations.

(b) The existence of a provision of this article shall not of itself create any implication that a contrary or different rule of law is or would be applicable to a business corporation that is not a benefit corporation. This article shall not affect any statute or rule of law that is or would be applicable to a business corporation that is not a benefit corporation.

(c) Except as otherwise provided in this article, this chapter shall be applicable to all benefit corporations. The specific provisions of this article shall control over the general provisions of this chapter.

(d) A provision of the certificate of incorporation or bylaws of a benefit corporation may not relax, be inconsistent with or supersede any provision of this article.

§ 1702. Definitions.

As used in this article, unless the context otherwise requires, the term:

(a) "Benefit corporation" means a business corporation incorporated under this article and whose status as a benefit corporation has not been terminated as provided in this article.

(b) "General public benefit" means a material positive impact on society and the environment, taken as a whole, assessed against a third-party standard, from the business and operations of a benefit corporation.

(c) "Independent" means that a person has no material relationship with a benefit corporation or any of its subsidiaries. A material relationship between a person and a benefit corporation or any of its subsidiaries will be conclusively presumed to exist if:

(1) the person is, or has been within the last three years, an employee of the benefit corporation or any of its subsidiaries;

(2) an immediate family member of the person is, or has been within the last three years, an executive officer of the benefit corporation or any of its subsidiaries; or

(3) the person, or an entity of which the person is a director, officer or other manager or in which the person owns beneficially or of record five percent or more of the equity interests, owns beneficially or of record five percent or more of the shares of the benefit corporation. A percentage of ownership in an entity shall be calculated

as if all outstanding rights to acquire equity interests in the entity had been exercised.

(d) "Minimum status vote" means that, in addition to any other approval or vote required by this chapter, the certificate of incorporation or a bylaw adopted by the shareholders:

(1) The holders of shares of every class or series that are entitled to vote on the corporate action shall be entitled to vote as a class on the corporate action; and

(2) The corporate action must be approved by vote of the shareholders of each class or series entitled to cast at least three-quarters of the votes that all shareholders of the class or series are entitled to cast thereon.

(e) "Specific public benefit," includes:

(1) providing low-income or underserved individuals or communities with beneficial products or services;

(2) promoting economic opportunity for individuals or communities beyond the creation of jobs in the normal course of business;

(3) preserving the environment;

(4) improving human health;

(5) promoting the arts, sciences or advancement of knowledge;

(6) increasing the flow of capital to entities with a public benefit purpose; and

(7) the accomplishment of any other particular benefit for society or the environment.

(f) "Subsidiary" means an entity in which a person owns beneficially or of record fifty percent or more of the equity interests. A percentage of ownership in an entity shall be calculated as if all outstanding rights to acquire equity interests in the entity had been exercised.

(g) "Third-party standard" means a recognized standard for defining, reporting and assessing general public benefit that is:

(1) developed by a person that is independent of the benefit corporation; and

(2) transparent because the following information about the standard is publicly available:

(A) the factors considered when measuring the performance of a business;

(B) the relative weightings of those factors; and

(C) the identity of the persons who developed and control changes to the standard and the process by which those changes are made.

§ 1703. Formation of benefit corporations.

A benefit corporation shall be formed in accordance with this chapter except that its certificate of incorporation shall also state that it is a benefit corporation.

§ 1704. Election of an existing business corporation to become a benefit corporation.

(a) A business corporation may become a benefit corporation under this article by amending its certificate of incorporation so that it contains a statement that the corporation is a benefit corporation. The amendment shall not be effective unless it is adopted by at least the minimum status vote.

(b) Any corporation that is not a benefit corporation that is a party to a merger or consolidation in which the surviving or consolidated corporation will be a benefit corporation must approve the plan of merger or consolidation by at least the minimum status vote in addition

to any other vote required by this chapter, the certificate of incorporation or the bylaws.

(c) Any corporation that is not a benefit corporation that is party to a merger or consolidation in which shares of stock of such corporation will be converted into a right to receive shares of stock of a benefit corporation must approve the plan of merger or consolidation by at least the minimum status vote in addition to any other vote required by this chapter, the certificate of incorporation or the bylaws.

§ 1705. Termination of benefit corporation status.

(a) A benefit corporation may terminate its status as such and cease to be subject to this article by amending its certificate of incorporation to delete the statement that the corporation is a benefit corporation. The amendment shall not be effective unless it is adopted by at least the minimum status vote.

(b) If a benefit corporation is a party to a merger or consolidation in which the surviving or new corporation will not be a benefit corporation, the plan of merger or consolidation shall not be effective unless it is adopted by at least the minimum status vote in addition to any other vote required by this chapter, the certificate of incorporation or the bylaws.

(c) Any benefit corporation that is party to a merger or consolidation in which shares of stock of such benefit corporation will be converted into a right to receive shares of stock of a corporation that is not a benefit corporation must approve the plan of merger or consolidation by at least the minimum status vote in addition to any other vote required by this chapter, the certificate of incorporation or the bylaws.

(d) A sale, lease, conveyance, exchange, transfer, or other disposition of all or substantially all of the assets of a benefit corporation, unless the transaction is in the usual and regular course of business of the benefit corporation, shall not be effective unless the transaction is approved by at least the minimum status vote in addition to any other vote required by this chapter, the certificate of incorporation or the bylaws.

§ 1706. Corporate purposes.

(a) Every benefit corporation shall have a purpose of creating general public benefit. This purpose is in addition to its purposes under section two hundred one of this chapter and any specific purpose set forth in its certificate of incorporation under paragraph (b) of this section. The purpose to create general public benefit shall be a limitation on the other purposes of the benefit corporation, and shall control over any inconsistent purpose of the benefit corporation.

(b) The certificate of incorporation of a benefit corporation may identify one or more specific public benefits that it is the purpose of the benefit corporation to create in addition to its purposes under section two hundred one of this chapter and paragraph (a) of this section. The identification of a specific public benefit under this paragraph does not limit the obligation of a benefit corporation to create general public benefit.

(c) The creation of general and specific public benefits as provided in paragraphs (a) and (b) of this section is in the best interests of the benefit corporation.

(d) A benefit corporation may amend its certificate of incorporation to add, amend or delete the identification of a specific public benefit that it is the purpose of the benefit corporation to create. The amendment shall not be effective unless it is adopted by at least the

minimum status vote.

§ 1707. Standard of conduct for directors and officers.

(a) In discharging the duties of their respective positions, the board of directors, committees of the board and individual directors and officers of a benefit corporation:

(1) shall consider the effects of any action upon:

(A) the ability for the benefit corporation to accomplish its general and any specific public benefit purpose;

(B) the shareholders of the benefit corporation;

(C) the employees and workforce of the benefit corporation and its subsidiaries and suppliers;

(D) the interests of customers as beneficiaries of the general or specific public benefit purposes of the benefit corporation;

(E) community and societal considerations, including those of any community in which offices or facilities of the benefit corporation or its subsidiaries or suppliers are located;

(F) the local and global environment; and

(G) the short-term and long-term interests of the benefit corporation, including benefits that may accrue to the benefit corporation from its long-term plans and the possibility that these interests may be best served by the continued independence of the benefit corporation;

(2) may consider:

(A) the resources, intent and conduct (past, stated and potential) of any person seeking to acquire control of the corporation; and

(B) any other pertinent factors or the interests of any other group that they deem appropriate; and

(3) shall not be required to give priority to the interests of any particular person or group referred to in subparagraphs one and two of this paragraph over the interests of any other person or group unless the benefit corporation has stated its intention to give priority to interests related to a specific public benefit purpose identified in its certificate of incorporation.

(b) The consideration of interests and factors in the manner required by paragraph (a) of this section:

(1) shall not constitute a violation of the provisions of sections seven hundred fifteen or seven hundred seventeen of this chapter; and

(2) is in addition to the ability of directors to consider interests and factors as provided in section seven hundred seventeen of this chapter.

(c) A director does not have a fiduciary duty to a person that is a beneficiary of the general or specific public benefit purposes of a benefit corporation arising from the status of the person as a beneficiary, unless otherwise stated in the certificate of incorporation or the bylaws of the benefit corporation.

§ 1708. Annual benefit report.

(a) A benefit corporation must deliver to each shareholder an annual benefit report including:

(1) a narrative description of:

(A) the process and rationale for selecting the third party standard used to prepare the benefit report;

(B) the ways in which the benefit corporation pursued general public benefit during the year and the extent to which general public benefit was created;

(C) the ways in which the benefit corporation pursued any specific

public benefit that the certificate of incorporation states it is the purpose of the benefit corporation to create and the extent to which that specific public benefit was created; and

(D) any circumstances that have hindered the creation by the benefit corporation of general or specific public benefit;

(2) an assessment of the performance of the benefit corporation, relative to its general public benefit purpose assessed against a third-party standard applied consistently with any application of that standard in prior benefit reports or accompanied by an explanation of the reasons for any inconsistent application and, if applicable, assessment of the performance of the benefit corporation, relative to its specific public benefit purpose or purposes;

(3) the compensation paid by the benefit corporation during the year to each director in that capacity; and

(4) the name of each person that owns beneficially or of record five percent or more of the outstanding shares of the benefit corporation.

(b) The benefit report must be sent annually to each shareholder within one hundred twenty days following the end of the fiscal year of the benefit corporation. Delivery of a benefit report to shareholders is in addition to any other requirement to deliver an annual report to shareholders.

(c) A benefit corporation must post its most recent benefit report on the public portion of its website, if any, except that the compensation paid to directors and any financial or proprietary information included in the benefit report may be omitted from the benefit report as posted.

(d) Concurrently with the delivery of the benefit report to shareholders pursuant to paragraph (b) of this section, the benefit corporation must deliver a copy of the benefit report to the department for filing, except that the compensation paid to directors and any financial or proprietary information included in the benefit report may be omitted from the benefit report as filed under this section.

(e) The annual benefit report shall be in addition to all other reporting requirements under this chapter.

§ 1709. Conspicuous language on the face of certificates.

All certificates representing shares of a benefit corporation shall contain, in addition to any other statements required by the business corporation law, the following conspicuous language on the face of the certificate:

"This entity is a benefit corporation organized under article seventeen of the New York business corporation law."

Affidavit of shareholder of benefit corporation (B corp)

STATE OF [state where affiant resides)
) ss.: [city and state]
COUNTY OF [county where affiant resides)

Personally appeared [name of affiant] of [city and state where affiant resides] who, being first duly sworn, deposes and says that:

1. I am over the age of eighteen, suffer no legal liabilities, and have personal knowledge of the facts set forth below.

2. I am in the process of acquiring [number of shares of benefit corporation to be owned by affiant] shares of the Common Stock, $[par value of shares] par value per share, of [name of benefit corporation], a benefit corporation organized and existing under the laws of the State of [state of incorporation].

3. I acknowledge that [name of benefit corporation] is a benefit corporation or "B Corp.".

4. I acknowledge that a B corp, although legally "for profit," has a social and environmental purpose that may take precedence over its obligations to shareholders.

5. I acknowledge that decisions regarding dividends and other distributions to shareholders are in the sole discretion of a benefit corporation's directors and officers.

6. I acknowledge that it is possible I will never receive a return on his or her investment if [name of benefit corporation]'s directors and officers view its social/environmental purpose as paramount.

7. I acknowledge that any return on my investment in [name of benefit corporation] will be subject to federal and state income taxes, and that I will not be entitled to a charitable deduction in connection with my investment in [name of benefit corporation].

8. I agree that I will not sue [name of benefit corporation], or any of its shareholders, directors or officers, or join in any lawsuit against any of them, because of any decision made by the corporation's management in furtherance of its social, environmental or other purposes.

9. I agree that, in addition to any other restrictions on transfer that may be set forth in the organizational documents or shareholders' agreement (if any) of [name of benefit corporation], any person to whom I may transfer all or any of my shares of Common Stock in [name of benefit corporation] will be required to sign an affidavit in form

and substance substantially similar to this affidavit as a condition precedent to such transfer, and that any transfer made by me without obtaining such an affidavit shall be null and void ab initio.

All statements and representations in this affidavit are made to induce [name of benefit corporation] to issue shares of its Common Stock to me, and are true, correct and complete in all material respects, made under penalty of perjury.

/s/ _____
Print Name:

Subscribed and sworn to before me
As of the [effective date of affidavit].

_____
Notary Public

Provision for bylaws of a benefit corporation – preparation of annual benefit report

ARTICLE ___
ANNUAL BENEFIT REPORT

Section 1. Selection of Third Party Standard.

Each year, the board shall select a third party standard for use in preparing the annual benefit report. The third party standard shall be a recognized a standard for defining, reporting and assessing general public benefit that is developed by a person or organization that is independent of the corporation, and transparent because the following information about the standard is publicly available:

(a) The factors considered when measuring the performance of a business;
(b) The relative weightings of those factors; and
(c) The identity of the persons who developed the standard and control changes to the standard and the process by which those changes are made.

Section 2. Preparation of Annual Benefit Report.

(a) The Treasurer shall prepare, or cause to be prepared, the annual benefit which shall contain a narrative description of:

(1) The process and rationale for selecting the third party standard used to prepare the benefit report;
(2) The ways in which the benefit corporation pursued general public benefit during the year and the extent to which general public benefit was created;
(3) The ways in which the benefit corporation pursued its specific public benefit(s) as set forth in its Certificate of Incorporation, which consists of [describe specific public benefit purpose] and the extent to which that specific public benefit was created; and
(4) Any circumstances that have hindered the creation by the benefit corporation of general or specific public benefit.

(b) The annual report shall also include:

(1) An assessment of the performance of the corporation, relative to its general public benefit purpose assessed against a third-party standard applied consistently with any application of that standard in prior annual benefit reports or accompanied by an explanation of the reasons for any inconsistent application and, assessment of the performance of the benefit corporation, relative to its specific public benefit purpose or purposes;
(2) The compensation paid by the benefit corporation during the year to each director in that capacity; and
(3) The name of each person that owns beneficially or of record five percent or more of the outstanding shares of the corporation.

Topic Four:

Basic Tax Issues for the Startup Venture

Tax Issues of the Startup Venture

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Every Startup Venture Needs a Lawyer . . . AND an Accountant!

- Every good business attorney must be "half a tax lawyer", BUT:
- You should insist that your startup venture client retain an accountant, and GET HIS/HER CONTACT INFORMATION IN YOUR INTAKE FORM, for several reasons:
  - The decisions you help the client make now will impact the tax returns and other documents the accountant will be preparing;
  - The client's accountant often has a prior relationship with the company or its founder(s) and can offer insight into key history that will impact your relationship with the client;
  - "Two minds are better than one," especially when it comes to tax analysis; and
  - Shared responsibility and accountability.

At the Formation Stage

- Implications of Tax Cuts and Jobs Act of 2017
- C corporation (21% tax rate) vs. S corporation or LLC (up to 35%)
  - See attached article
- Can your LLC or S corporation client take the 20% deduction for "qualified small business income"?
  - See attached article
- Other deductions under the 2017 Act
  - Section 179, cash basis of accounting, NOLs, excess business losses
- Impact of the new Congress

At the Formation Stage

- S corporation vs. limited liability company: can be a tricky decision
  - With an S corporation, founders cannot always deduct losses on their personal tax returns
  - New York City does not recognize the S Corporation election. NYC has the UBIT.
- Filings and registrations: you and the accountant can share the load, but GET IT IN WRITING:
  - Obtaining federal and state tax ID numbers;
  - Filing Forms 2553 and CT-6 (for S corporations);
  - If LLC is to be taxed under subchapter S, must file Forms 8832 and 2553 within 75 days of formation.
- If registering a foreign LLC (Delaware) that has been doing business in NY for a while, must attach consent of NYS Dep't of Taxation & Finance to the filing
- **Nexus, Nexus, Nexus**: watch out for home offices, employees (even leased employees), merchandise warehoused/fulfilled in other states (NJ states a home office is income tax nexus)
- Registering for state and local taxes is different than registration with Department of State.
- If the entity is located in NYC, does it have to register for NYC taxes?

During the Operations Phase

- Making sure all the tax stuff in the LLC Operating Agreement really works
  - Sharing of profits, losses, equity
  - Guaranteed payments vs. distributions
- Dealing with "phantom income" issues: should you "gross up" the venture's founders?
- "Preferred equity" and "profits interests" in a limited liability company
- W-8s (for overseas partners), W-9s and 1099s
- Drafting "buy-sell" provisions in an Operating or Shareholders' Agreement
- NYS tax credits for startup ventures
  - Empire State Development Corp. [http://esd.ny.gov/BusinessPrograms/Taxes_Incentives.html]
  - START-UP NY [http://startup-ny.com]

FAQs CPA's receive in 2018

- Reasonable compensation for S Corporation owner vs. distributions
- Basis in LLC versus S corp.
- Independent contractor versus employee.
  - Can trigger nexus in other states (level of w2 wages & sales contractors)
  - NYS Dept of Labor is aggressively auditing in this area
- New York State apportionment rules (stopped using rent/payroll).
- Will the EBAY letter for de minimus exception to Wayfair be accepted.
- Compensating the early stage company executives and planning in most effective AND tax advantageous manner. (i.e. NQSO's)
- SEP IRA, 401K (safe harbor), Defined Benefit, Simple IRA, ROTH IRA.
- Form W8-BEN –payments to non tax individuals.
- IRC 1202 C Corp Small Business Stock.

When Doing Transactions for Your Client

- Every business transaction has tax consequences for the parties
- 83(b) elections and "profits interests" in a limited liability company
- IMPORTANT: Allocating the purchase price in an asset sale (IRS Form 8594)
  - If representing the seller, allocate as little as possible to noncompete agreements
- Dealing with NY's "bulk sales tax" and Form AU-196.10
- Net operating loss carryforwards (the 2015 PNOLC rules in NYS)
- Structuring the transaction:
  - Installment sales
  - Avoid "overstructuring" to maximize tax benefits
- Do you need to bring in a tax lawyer?

During the "Winding Down" Phase

- Someone's got to file final tax returns!
- Getting tax clearance in New York State (for corporations)
- Complying with BCL section 630 (for LLCs and corporations)
- If there is shareholder debt that is not paid, does that create "forgiveness of indebtedness" income to the company?
- Can the owners write off their investment as "worthless"?

Limits on the Lawyer-Accountant Relationship

- Confidentiality (Model Rule 1.6)
- Attorney-Client Privilege
- Referral Arrangements
- Joint Marketing with Accountants and Other Professionals
  - Impact of NYSBA Ethics Opinion 1132 (June 2017)

Thank You!

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CHOOSING THE RIGHT LEGAL ENTITY UNDER THE NEW TAX LAW

By Cliff Ennico

It's official.

Except for a handful of provisions that have later effective dates, the nearly 1100-page Tax Cuts and Jobs Act is now the law of the land.

A ton of ink has already been spilled about the Act's impact on small business, but the big question for most of my readers is: should I change from my current legal entity to another to take advantage of the lower tax rates promised by the Act's proponents?

Short Answer #1: talk to your accountant or tax advisor.

With a single exception – the reduction of the top tax rate on regular or C corporations from 35 percent to 21 percent – virtually all of the small business tax cuts made by the Act come with a host of "ifs", "ands" and "buts." Someone (preferably a tax professional) will need to sit down and crunch your business' numbers to determine if you should switch your legal status or stay as you are.

Short Answer #2: unless there is a compelling economic reason to change status, stay as you are.

Having said that, here are a couple of personal ruminations that SHOULD NOT be relied on as tax advice:

C Corporations vs. Pass-Throughs. Despite the much lower tax rates for C corporations, I don't see a lot of small businesses switching from "pass through" entity types such as limited liability companies (LLCs) and subchapter S corporations (S corps) to C corporation status, for two reasons.

First, a C corporation's income is taxed twice – once at the corporate level, and then a second time when distributed to individual shareholders. That second tax is at the shareholder's individual tax rate, which for many business owners will top out at 37 percent (slightly less than the previous 39.6 percent rate). While existing C corporations will benefit greatly from the tax reduction at both levels, the advantage for "pass through" entities that newly convert to C corporation status won't be as clear. The single level of taxation for "pass throughs", especially those that can benefit from the new 20% deduction for self-employment income (see below), may actually result in a lower overall tax rate than a doubly-taxed C corporation that distributes most of its income to shareholders.

Second, and more significantly, C corporations are lots more complex to operate than "pass-throughs," and require considerably more legal compliance and paperwork. For example, a single member LLC converting to a C corporation will now:

O have to file the complex IRS Form 1120 rather than the relatively simple Schedule C; and

O have to document business decisions made "outside the ordinary course of business" with formal resolutions of the directors and shareholders, even if they all occupy the same human body.

Any marginal tax benefit from switching to a C corporation will have to be weighed against these (possibly) higher legal and tax compliance costs.

<u>LLC vs. Subchapter S Corporation.</u> This decision has never been easy but has been made more complicated by the Act.

For small businesses other than professional service firms, the 20% deduction from net income created by the Act applies to both LLCs and S corps, but the deduction for S corps applies only to that portion of business income that qualifies as "distribution of profit" rather than "salary" (S corp shareholders divide their income between "salary" and "distribution of profit" in order to reduce their FICA and Medicare Tax liability). Accordingly, there may be a slight – slight – incentive for a small business organized as an S corp to convert into an LLC, as that would extend the 20% deduction to 100% of the company's income.

Before doing that, however, think about the following:

O the cost of liquidating the S corp and contributing the resulting capital to a newly formed LLC may be greater than the tax savings generated by the conversion; and

O the 20% deduction for "pass-throughs" is scheduled to expire in 2025, maybe sooner if the Democrats recapture Congress in 2018 and change everything again.

For professional service firms organized as sole proprietorships or single member LLCs that are at or slightly above the income ceilings for the 20% deduction ($157,500 for single taxpayers, $315,000 for married couples filing jointly), there may be a slight – slight – incentive to switch to an S corp and take a small salary, thereby saving some money on FICA and Medicare taxes (on the portion treated as "salary") and ensuring that your remaining income (treated as a "distribution of profit") will qualify for the 20% deduction.

But again, if the additional cost of filing S corp tax returns and dealing with the complexity of operating in corporate form exceeds the tax savings, fuhgeddaboudit. Also

you just know the IRS will be auditing professional service S corps that get too creative, since accountants and lawyers cannot claim ignorance as a defense.

High-Tax vs. Low-Tax States. For many "pass-through" businesses, the biggest tax savings under the Act may come not from changing their legal status but from moving from a high-tax state to a "low or no" tax state if possible. Under the Act deductions for state and local income, sales and property taxes are capped at $10,000. Businesses in high-tax states in the Northeast especially may well be migrating soon to Florida, Nevada and Texas, where the sun shines brightly.

And there are no state income taxes.

Cliff Ennico (cennico@legalcareer.com) is a syndicated columnist, author and host of the PBS television series 'Money Hunt'. This column is no substitute for legal, tax or financial advice, which can be furnished only by a qualified professional licensed in your state. To find out more about Cliff Ennico and other Creators Syndicate writers and cartoonists, visit our Web page at www.creators.com.

DOES YOUR SMALL BUSINESS QUALIFY FOR THE 20% DEDUCTION?

By Cliff Ennico

If you're like most small business owners, you are scratching your head trying to figure out the new small business tax deduction.

The Tax Cuts and Jobs Act of 2017, which went into effect January 1, offers a 20% deduction for "pass through" entities such as partnerships, limited liability companies and subchapter S corporations.

Like all tax benefits, the deduction is designed to accomplish "social engineering" goals as well as raise tax revenue for the Government.

Specifically:

(1) the current Administration wants to bring manufacturing back to the U.S. so such businesses will have the easiest time qualifying for the deduction; and

(2) the current Administration wants to encourage small businesses to hire more people as employees, so small businesses who do so will have an easier time qualifying for the deduction than others.

Here are the five questions you will have to ask to determine if you qualify for the 20% deduction.

Step # 1: Is Your Business a "Pass-Through" for Tax Purposes?

The 20% deduction applies only to "pass through entities", which are basically anything (including a sole proprietorship) other than a C corporation. Hey, those guys got a HUGE reduction in their federal income tax rate, so don't feel too sorry for them.

Step # 2: Is Your Business Engaged in a "Specified Service Trade or Business"?

The 20% deduction applies only to small businesses engaged in manufacturing, retail, nonprofessional services (think restaurants and lawn care), and SOME professional services (such as architecture and engineering). Congress did not want the new deduction to enrich accountants and lawyers (but no fear – the extra fees they will earn from helping clients figure the deduction out will more than make up for not having the deduction).

A "Specified Service Trade or Business" is defined as health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or "any trade or business where the principal asset of such trade or business is the reputation or skill of one or more of its employees". So, if you are a barber or hair stylist, are you a "specified service trade or business" ineligible for the deduction?

The new law doesn't offer any guidance, but here are two "rules of thumb":

(1) if your state requires or permits you to form a "professional corporation" or "professional limited liability company" in lieu of a regular corporation or LLC, you probably are engaged in a "specified service trade or business" (ask your lawyer about this).

(2) if your state requires you to obtain a "professional license" (as opposed to an occupational license) to do whatever you do, you probably are engaged in a "specified service trade or business."

Step # 3: Do You Make Less Than the Minimum Income Thresholds?

If you have less than $157,500 in taxable income (for a single taxpayer) or $315,000 in taxable income (for a married taxpayer filing jointly), then you can take the 20% deduction even if you are engaged in a "specified service trade or business".

Although if you are a doctor making less than $157,500 a year, I'm wondering how good a doctor you are □.

If you are a shareholder in an S corporation, your taxable income is based on what is distributed to you each year as an owner/partner in the business, not the amount you take out in salary for the services you render to the corporation.

Question: if you are slightly over the taxable income threshold, can you increase your deductions to bring your taxable income below the threshold – for example, by leasing a car through your company? You bet you can, as long as the deduction qualifies as an "ordinary and necessary" business deduction (forget the personal masseuse, unless you are a Hollywood actor).

Step # 4: Does the Deduction Exceed Certain Caps?

Whether or not your taxable income exceeds the minimum income thresholds, your deduction cannot exceed 20% of the excess of your taxable income over your "net capital gains".

If you are NOT engaged in a "specified service trade or business" AND your taxable income exceeds the minimum income threshold ($157,500 for a single taxpayer, $315,000 for a married taxpayer filing jointly), you can still take the 20% deduction. The bad news is that your deduction is further limited or "capped" to the greater of:

(1) 50% of all wages paid to W-2 employees of the business, or

(2) 25% of all wages paid to W-2 employees plus 2.5% of the "unadjusted basis" (i.e. before any depreciation deductions) of tangible depreciable property that your company owns as determined at the end of the tax year.

Step # 5: Hire a Tax Professional.

Got all that? I didn't think so. Unless you are trained in accounting, you probably will need the help of a qualified tax professional to determine whether or not your business qualifies for the 20% deduction. This should really be Step # 1.

Pay them well. After all, they don't get the deduction.

Cliff Ennico (cennico@legalcareer.com) is a syndicated columnist, author and host of the PBS television series 'Money Hunt'. This column is no substitute for legal, tax or financial advice, which can be furnished only by a qualified professional licensed in your state. To find out more about Cliff Ennico and other Creators Syndicate writers and cartoonists, visit our Web page at www.creators.com.

Part III - Administrative, Procedural, and Miscellaneous

Methods for Calculating W-2 Wages for Purposes of Section 199A

Notice 2018-64

SECTION 1. PURPOSE

This notice (Notice) contains a proposed revenue procedure that provides guidance on methods for calculating W-2 wages for purposes of section 199A of the Internal Revenue Code (Code) and proposed §§ 1.199A-1 through 1.199A-6 of the Income Tax Regulations (26 CFR part 1), which are contained in a notice of proposed rulemaking (REG-107892-18) being published contemporaneously with this Notice. Specifically, this Notice provides methods for calculating W-2 wages (1) for purposes of section 199A(b)(2), which, for certain taxpayers, provides a limitation based on W-2 wages to the amount of the deduction for qualified business income under section 199A(a); and (2) for purposes of section 199A(b)(7), which, for certain specified agricultural and horticultural cooperative patrons, provides a reduction to the section 199A(a) deduction based on W-2 wages.

SECTION 2. BACKGROUND

Section 199A was enacted on December 22, 2017 as part of the act entitled “An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018,” P.L. 115-97 (Act), and was amended on March 23, 2018 retroactively to January 1, 2018, by H.R.1625 - Consolidated Appropriations Act,

2018, P.L. 115-141, (H.R. 1625). Congress enacted section 199A to provide a deduction to non-corporate taxpayers of up to 20 percent of the taxpayer's qualified business income (QBI) from each of the taxpayer's qualified trades or businesses, including those operated through a partnership, S corporation, or sole proprietorship, as well as a deduction of up to 20 percent of aggregate qualified REIT dividends and qualified publicly traded partnership income. For each qualified trade or business, section 199A(b)(2) limits the amount of the section 199A deduction to the lesser of (1) 20 percent of the taxpayer's QBI with respect to the qualified trade or business, or (2) the greater of (A) 50 percent of the W–2 wages with respect to the qualified trade or business, or (B) the sum of 25 percent of the W–2 wages with respect to the qualified trade or business plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property. Under section 199A(b)(3), this limitation is phased in above a threshold amount of taxable income.

Section 199A(b)(7) provides that in the case of any qualified trade or business of a patron of a specified agricultural or horticultural cooperative, the amount determined under section 199A(b)(2) with respect to such trade or business shall be reduced by the lesser of (A) 9 percent of so much of the qualified business income with respect to such trade or business as is properly allocable to qualified payments received from such cooperative, or (B) 50 percent of so much of the W-2 wages with respect to such trade or business as are so allocable.

Section 199A(b)(4)(A) of the Code defines the term "W-2 wages" to mean, with respect to any person for any taxable year of such person, the amounts described in

section 6051(a)(3) and (8) paid by such person with respect to employment of employees by such person during the calendar year ending during such taxable year. Proposed § 1.199A-2 further defines W-2 wages for purposes of section 199A. The proposed revenue procedure included in this Notice would provide methods for calculating the amount of W-2 wages, as defined in section 199A(b)(4) and proposed § 1.199A-2, for purposes of determining the deduction limitation in section 199A(b)(2) and the reduction in section 199A(b)(7). Section 1.199A-2(b)(2)(iv)(A) of the proposed regulations provides the Internal Revenue Service with authority to issue guidance providing the methods that may be used to calculate W-2 wages.

SECTION 3. REQUEST FOR COMMENTS

The Treasury Department and the IRS request comments on this proposed revenue procedure. In particular, the Treasury Department and the IRS request comments concerning the calculation of "W-2 wages" with respect to remuneration paid for services performed in Puerto Rico. Section 199A(f)(1)(C)(ii) provides that in the case of a taxpayer with qualified business income from sources within the commonwealth of Puerto Rico, the determination of W-2 wages of such taxpayer shall be made without regard to any exclusion under section 3401(a)(8) for remuneration paid for services performed in the Commonwealth of Puerto Rico. Because bona fide residents of the Commonwealth of Puerto Rico are not subject to federal income tax and do not receive Forms W-2, the methods provided in the proposed revenue procedure will be difficult to apply with respect to employees who are residents of Puerto Rico. The Treasury Department and the IRS request comments concerning

appropriate methods for calculating W-2 wages with respect to remuneration paid for services performed in Puerto Rico by bona fide residents of Puerto Rico.

Interested parties are invited to submit comments on this Notice by **[INSERT DATE 45 DAYS AFTER DATE THE SECTION 199A PROPOSED REGULATIONS ARE PUBLISHED IN THE FEDERAL REGISTER].** Comments should be submitted to: CC:PA:LPD:PR (Notice 2018-64), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, D.C., 20044. Submissions may be hand-delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (Notice 2018-64), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. Alternatively, taxpayers may submit comments electronically to Notice.comments@irscounsel.treas.gov. Please include "Notice 2018-64" in the subject line of any electronic submission.

SECTION 4. EFFECTIVE DATE AND IMMEDIATE RELIANCE

This Notice is effective on **[INSERT DATE THIS DOCUMENT IS PUBLISHED IN THE INTERNAL REVENUE BULLETIN].** The proposed revenue procedure is proposed to apply generally to taxable years ending after December 31, 2017.

Until such time that the proposed revenue procedure is published in final form, taxpayers may use the methods described in the proposed revenue procedure in calculating W-2 wages, as defined in section 199A(b)(4)(A), for purposes of determining the limitation in section 199A(b)(2) and the reduction in section 199A(b)(7) .

SECTION 5. DRAFTING INFORMATION

The principal authors of this Notice are Andrew Holubeck and Mikhail Zhidkov of

the Office of the Associate Chief Counsel (Tax Exempt and Government Entities) and Frank J. Fisher and Benjamin H. Weaver of the Office of the Associate Chief Counsel (Passthroughs & Special Industries). However, other personnel from the Treasury Department and the IRS participated in its development. For further information regarding this Notice, contact Andrew Holubeck or Mikhail Zhidkov at (202) 317-4774, or Frank J. Fisher or Benjamin H. Weaver at (202) 317-6850.

SECTION 6. FORM OF PROPOSED REVENUE PROCEDURE

Set forth below is the form of the proposed revenue procedure that is proposed in this Notice:

FORM OF PROPOSED REVENUE PROCEDURE

Part III

Administrative, Procedural, and Miscellaneous

26 CFR 1.199A-2: Determination of W-2 Wages

(Also: [XX, XXX, XXX])

Rev. Proc. 2018-XX

SECTION 1. PURPOSE

This revenue procedure provides methods for calculating W-2 wages, as defined in section 199A(b)(4) and § 1.199A-2 of the Income Tax Regulations, (1) for purposes of section 199A(b)(2) of the Internal Revenue Code (Code) which, for certain taxpayers, provides a limitation based on W-2 wages to the amount of the deduction for qualified business income (QBI); and (2) for purposes of section 199A(b)(7), which, for certain specified agricultural and horticultural cooperative patrons, provides a reduction to the section 199A deduction based on W-2 wages.

SECTION 2. BACKGROUND

For taxpayers above a certain amount of taxable income, section 199A(b)(2)

limits the amount of a taxpayer's section 199A deduction for each qualified trade or business to the lesser of (1) 20 percent of the taxpayer's QBI with respect to the qualified trade or business, or (2) the greater of (A) 50 percent of the W–2 wages with respect to the qualified trade or business, or (B) the sum of 25 percent of the W–2 wages with respect to the qualified trade or business plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property. Section 199A(b)(7) provides that in the case of any qualified trade or business of a patron of a specified agricultural or horticultural cooperative, the amount determined under section 199A(b)(2) with respect to such trade or business shall be reduced by the lesser of (A) 9 percent of so much of the qualified business income with respect to such trade or business as is properly allocable to qualified payments received from such cooperative, or (B) 50 percent of so much of the W-2 wages with respect to such trade or business as are so allocable.

Section 199A(b)(4)(A) defines the term "W-2 wages" to mean, with respect to any person for any taxable year of such person, the amounts described in section 6051(a)(3) and (8) paid by such person with respect to employment of employees by such person during the calendar year ending during such taxable year. Section 199A(b)(4)(B) provides that W-2 wages does not include any amount which is not properly allocable to qualified business income for purposes of section 199A(c)(1). Section 199A(b)(4)(C) provides that W-2 wages shall not include any amount that is not properly included in a return filed with the Social Security Administration (SSA) on or before the 60th day after the due date (including extensions) for such return.

Section 1.199A-2(b)(2)(iv)(A) of the regulations provides the Internal Revenue Service with authority to issue guidance providing the methods that may be used to calculate W-2 wages.

This revenue procedure provides three methods for calculating W-2 wages, as defined in section 199A(b)(4) and § 1.199A-2, for purposes of section 199A(b) and the regulations thereunder. The first method (the unmodified Box method) allows for a simplified calculation while the second and third methods (the modified Box 1 method and the tracking wages method) provide greater accuracy.

W-2 wages calculated under this revenue procedure are not necessarily eligible for use in computing the section 199A limitations. As mentioned above, only W-2 wages which are properly allocable to QBI may be taken into account in computing the section 199A(b) W-2 wage limitations. Under § 1.199A-2(g), the taxpayer must determine the extent to which the W-2 wages calculated under this revenue procedure are properly allocable to QBI. Then, the properly allocable W-2 wages amount is used in determining the W-2 wages limitation under section 199A(b)(2) for that trade or business as well as any reduction for income received from cooperatives under section 199A(b)(7).

SECTION 3. RULES OF APPLICATION

.01 *In general*. In calculating W-2 wages for a taxable year under the methods described in this revenue procedure, include only wages properly reported on Forms W-2 that meet the applicable rules of § 1.199A-2(b). Specifically, § 1.199A-2(b)(2)(i) provides that, except as provided in § 1.199A-2(b)(2)(iv)(C)(2) (concerning short taxable

years that do not include December 31) and § 1.199A-2(b)(2)(iv)(D) (concerning remuneration for services performed in the Commonwealth of Puerto Rico), the Forms W-2, "Wage and Tax Statement," or any subsequent form or document used in determining the amount of W-2 wages are those issued for the calendar year ending during the person's taxable year for wages paid to employees (or former employees) of the person for employment by the person. Section 1.199A-2(b)(2)(i) also provides that, for purposes of § 1.199A-2, employees of the person are limited to employees of the person as defined in section 3121(d)(1) and (2) (that is, officers of a corporation and employees of the person under the common law rules). Therefore, Forms W-2 provided to statutory employees described in section 3121(d)(3) (that is, Forms W-2 in which the "Statutory Employee" box in Box 13 is checked) should not be included in calculating W-2 wages under any of the methods described in this revenue procedure.

.02 *No application in determining whether amounts are wages for employment tax purposes.* The discussions of "wages" in this revenue procedure and in the regulations under section 199A are for purposes of section 199A only and have no application in determining whether amounts are wages under section 3121(a) for purposes of the Federal Insurance Contributions Act, under section 3306(b) for purposes of the Federal Unemployment Tax Act, or under section 3401(a) for purposes of the Collection of Income Tax at Source on Wages (federal income tax withholding), or any other wage-related determination. See § 1.199A-2 of the regulations.

SECTION 4. DEFINITION OF W-2 WAGES AND CORRELATION WITH BOXES ON

FORM W-2

.01 *Definition of W-2 wages.* Section 199A(b)(4)(A) provides that W-2 wages means, with respect to any person for any taxable year of such person, the sum of the amounts described in section 6051(a)(3) and (8) paid by such person with respect to employment of employees by such person during the calendar year ending during such taxable year. Thus, W-2 wages include: (i) the total amount of wages as defined in section 3401(a); (ii) the total amount of elective deferrals (within the meaning of section 402(g)(3)); (iii) the compensation deferred under section 457; and (iv) the amount of designated Roth contributions (as defined in section 402A).

.02 *Correlation with Form W-2.* Under the 2018 Forms W-2, the elective deferrals under section 402(g)(3) and the amounts deferred under section 457 directly correlate to coded items reported in Box 12 on Form W-2. Box 12, Code D is for elective deferrals to a section 401(k) cash or deferred arrangement plan (including a SIMPLE 401(k) arrangement); Box 12, Code E is for elective deferrals under a section 403(b) salary reduction agreement; Box 12, Code F is for elective deferrals under a section 408(k)(6) salary reduction Simplified Employee Pension (SEP); Box 12, Code G is for elective deferrals and employer contributions (including nonelective deferrals) to any governmental or nongovernmental section 457(b) deferred compensation plan; Box 12, Code S is for employee salary reduction contributions under a section 408(p) SIMPLE (simple retirement account); Box 12, Code AA is for designated Roth contributions (as defined in section 402A) under a section 401(k) plan; and Box 12, Code BB is for designated Roth contributions (as defined in section 402A) under a

section 403(b) salary reduction agreement. However, designated Roth contributions are also reported in Box 1, Wages, tips, other compensation and are subject to income tax withholding.

SECTION 5. METHODS FOR CALCULATING W-2 WAGES

For any taxable year, a taxpayer must calculate W-2 wages for purposes of section 199A(b)(2) using one of the three methods described in section 5.01, 5.02, and 5.03 of this revenue procedure. For a taxpayer with a short taxable year, see Section 6 of this revenue procedure. In calculating W-2 wages for a taxable year under the methods below, the taxpayer includes only those Forms W-2 that arefor the calendar year ending with or within the taxable year of the taxpayer and that meet the rules of application described in section 3 of this revenue procedure..01 *Unmodified box method*. Under the unmodified box method, W-2 wages are calculated by taking, without modification, the lesser of—

(A) The total entries in Box 1 of all Forms W-2 filed with SSA by the taxpayer with respect to employees of the taxpayer for employment by the taxpayer; or

(B) The total entries in Box 5 of all Forms W-2 filed with SSA by the taxpayer with respect to employees of the taxpayer for employment by the taxpayer.

.02 *Modified Box 1 method*. Under the Modified Box 1 method, the taxpayer makes modifications to the total entries in Box 1 of Forms W-2 filed with respect to employees of the taxpayer. W-2 wages under this method are calculated as follows—

(A) Total the amounts in Box 1 of all Forms W-2 filed with SSA by the taxpayer with respect to employees of the taxpayer for employment by the

taxpayer;

(B) Subtract from the total in paragraph .02(A) of this section amounts included in Box 1 of Forms W-2 that are not wages for Federal income tax withholding purposes, including amounts that are treated as wages for purposes of income tax withholding under section 3402(o) (for example, supplemental unemployment compensation benefits within the meaning of Rev. Rul. 90-72); and

(C) Add to the amount obtained after paragraph .02(B) of this section the total of the amounts that are reported in Box 12 of Forms W-2 with respect to employees of the taxpayer for employment by the taxpayer and that are properly coded D, E, F, G, and S.

.03 *Tracking wages method*. Under the tracking wages method, the taxpayer actually tracks total wages subject to Federal income tax withholding and makes appropriate modifications. W-2 wages under this method are calculated as follows—

(A) Total the amounts of wages subject to Federal income tax withholding that are paid to employees of the taxpayer for employment by the taxpayer and that are reported on Forms W-2 filed with SSA by the taxpayer for the calendar year; and

(B) Add to the amount obtained after paragraph .03(B) of this section the total of the amounts that are reported in Box 12 of Forms W-2 with respect to employees of the taxpayer for employment by the taxpayer and that are properly coded D, E, F, G, and S.

SECTION 6. APPLICATION IN CASE OF SHORT TAXABLE YEAR

.01 *Special rule for taxpayers with a short taxable year.* In the case of a taxpayer with a short taxable year, subject to the rules of application described in section 3 of this revenue procedure, the W-2 wages of the taxpayer for the short taxable year shall include only those wages paid during the short taxable year to employees of the taxpayer, only those elective deferrals (within the meaning of section 402(g)(3)) made during the short taxable year by employees of the taxpayer, and only compensation actually deferred under section 457 during the short taxable year with respect to employees of the taxpayer. See §1.199A-2(b)(2)(iv)(C) of the regulations.

.02 *Method required for a short taxable year and modifications required in application of method.* The W-2 wages of a taxpayer with a short taxable year shall be determined under the tracking wages method described in section 5.03 of this revenue procedure. In applying the tracking wages method in the case of a short taxable year, the taxpayer must apply the method as follows—

(A) For purposes of section 5.03(A), the total amount of wages subject to Federal income tax withholding and reported on Form W-2 must include only those wages subject to Federal income tax withholding that are actually or constructively paid to employees during the short taxable year and reported on Form W-2 for the calendar year ending with or within that short taxable year (or, for a short taxable year that does not contain a calendar year ending with or within such short taxable year, wages subject to Federal income tax withholding that are actually or constructively paid to employees during the short taxable year

and reported on Form W-2 for the calendar year containing such short taxable year); and

(B) For purposes of section 5.03(B), only the portion of the total amounts reported in Box 12, Codes D, E, F, G, and S on Forms W-2, that are actually deferred or contributed during the short taxable year are included in W-2 wages.

SECTION 7. EFFECTIVE DATE

This revenue procedure applies to taxable years ending after December 31, 2017.

SECTION 8. DRAFTING INFORMATION

The principal authors of this revenue procedure are Andrew Holubeck and Mikhail Zhidkov of the Office of the Associate Chief Counsel (Tax Exempt and Government Entities) and Frank J. Fisher and Benjamin H. Weaver of the Office of the Associate Chief Counsel (Passthroughs & Special Industries). However, other personnel from the Treasury Department and the IRS participated in its development. For further information regarding this revenue procedure contact Andrew Holubeck or Mikhail Zhidkov at (202) 317-4774, or Frank J. Fisher or Benjamin H. Weaver at (202) 317-6850.

Tax Cuts and Jobs Act, Provision 11011 Section 199A - Deduction for Qualified Business Income FAQs

Basic questions and answers on new 20-percent deduction for pass-through businesses

Below are answers to some basic questions about the new 20-percent deduction for pass-through businesses. Also known as the section 199A deduction or the deduction for qualified business income, the deduction was created by the 2017 Tax Cuts and Jobs Act.

Q1. What is the Deduction for Qualified Business Income?

A1. Section 199A of the Internal Revenue Code provides many taxpayers a deduction for qualified business income from a qualified trade or business operated directly or through a pass-through entity. The deduction has two components.

1) Eligible taxpayers may be entitled to a deduction of up to 20 percent of qualified business income (QBI) from a domestic business operated as a sole proprietorship or through a partnership, S corporation, trust or estate. For taxpayers with taxable income that exceeds $315,000 for a married couple filing a joint return, or $157,500 for all other taxpayers, the deduction is subject to limitations such as the type of trade or business, the taxpayer's taxable income, the amount of W-2 wages paid by the qualified trade or business and the unadjusted basis immediately after acquisition (UBIA) of qualified property held by the trade or business. Income earned through a C corporation or by providing services as an employee is not eligible for the deduction.

2) Eligible taxpayers may also be entitled to a deduction of up to 20 percent of their combined qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income. This component of the section 199A deduction is not limited by W-2 wages or the UBIA of qualified property.

The sum of these two amounts is referred to as the combined qualified business income amount. Generally, this deduction is the lesser of the combined qualified business income amount and an amount equal to 20 percent of the taxable income minus the taxpayer's net capital gain. For details on figuring the deduction, see Q&A 6 and 7. The deduction is available for taxable years beginning after Dec. 31, 2017. Most eligible taxpayers will be able to claim it for the first time when they file their 2018 federal income tax return in 2019. The deduction is available, regardless of whether an individual itemizes their deductions on Schedule A or takes the standard deduction.

Q2. Who may take the section 199A deduction?

A2. Individuals, trusts and estates with qualified business income, qualified REIT dividends or qualified PTP income may qualify for the deduction. In some cases, patrons of horticultural or agricultural cooperatives may be required to reduce their deduction. The IRS will be issuing separate guidance for co-ops.

Q3. How do S corporations and partnerships handle the deduction?

A3. S corporations and partnerships are generally not taxpayers and cannot take the deduction themselves. However, all S corporations and partnerships report each shareholder's or partner's share of QBI, W-2 wages, UBIA of qualified property, qualified REIT dividends and qualified PTP income on Schedule K-1 so the shareholders or partners may determine their deduction.

Q4. What is qualified business income (QBI)?

A4. QBI is the net amount of qualified items of income, gain, deduction and loss from any qualified trade or business. Only items included in taxable income are counted. In addition, the items must be effectively connected with a U.S. trade or business. Items such as capital gains and losses, certain dividends and interest income are excluded.

Q5. What is a qualified trade or business?

A5. A qualified trade or business is any trade or business, with two exceptions:

1) Specified service trade or business (SSTB), which includes a trade or business involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, investing and investment management, trading, dealing in certain assets or any trade or business where the principal asset is the reputation or skill of one or more of its employees. This exception only applies if a taxpayer's taxable income exceeds $315,000 for a married couple filing a joint return, or $157,500 for all other taxpayers

2) Performing services as an employee

Q6. How is the deduction for qualified business income computed?

A6. The SSTB limitation discussed in Q&A 5 does not apply if a taxpayer's taxable income is below $315,000 for a married couple filing a joint return and $157,500 for all other taxpayers; the deduction is the lesser of:

A) 20 percent of the taxpayer's QBI, plus 20 percent of the taxpayer's qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income

B) 20 percent of the taxpayer's taxable income minus net capital gains.

If the taxpayer's taxable income is above the $315,000/$157,500 thresholds, the deduction may be limited based on whether the business is an SSTB, the W-2 wages paid by the business and the unadjusted basis of certain property used by the business. These limitations are phased in for joint filers with taxable income between $315,000 and $415,000, and all other taxpayers with taxable income between $157,500 and $207,500. The threshold amounts and phase-in range are for tax-year 2018 and will be adjusted for inflation in subsequent years.

Q7. I have income from a specified service trade or business. How does that affect my deduction?

A7. The SSTB limitation does not apply to any taxpayer whose taxable income is below the $315,000/$157,500 threshold amounts discussed in Q&A #6. For taxpayers whose taxable income is within the phase-in range discussed in Q&A #6, the taxpayer's share of QBI, W-2 wages and UBIA of qualified property related to the SSTB may be limited. If the taxpayer's taxable income exceeds the phase-in range, no deduction is allowed with respect to any SSTB. The threshold amounts and phase-in range are for tax year 2018 and will be adjusted for inflation in subsequent years.

Q8. In 2018, I will report taxable income under $315,000 and file married filing jointly. Do I have to determine if I am in an SSTB in order to take the deduction? Is there any limitation on my deduction?

A8. No, if your 2018 taxable income is below $315,000, if married filing jointly, or $157,500 for all other filing statuses, it doesn't matter what type of business you are in. You will be able to deduct the lesser of:

a) Twenty percent (20%) of your QBI, plus 20 percent of your qualified REIT dividends and qualified PTP income, or

b) Twenty percent (20%) of your taxable income minus your net capital gains.

Q9. In 2018, I will report taxable income between $157,500 and $207,500 and file as single. I receive QBI. Does it matter if it is from an SSTB?

A9. Yes, because your taxable income is above the threshold amount, your section 199A deduction with respect to any SSTB will be limited. However, because you are within the phase-in range, you may be allowed some section 199A deduction with respect to an SSTB. In addition, for taxpayers above the threshold amount, the section 199A deduction with respect to any trade or business, including an SSTB, may be limited by the amount of W-2 wages paid by the trade or business and the UBIA of qualified property held by the trade or business. The phase-in range is $315,000 to $415,000 for joint filers and $157,500 to $207,500 for all other filing statuses. Section 1.199A-1 of the proposed regulations provides additional information.

Q10. In 2018, I am single and will report taxable income over $207,500. My only income is from an SSTB. Am I entitled to the deduction with respect to the SSTB?

A10. No. The same is true for a married couple filing a joint return whose taxable income exceeds $415,000. However, you may be entitled to a deduction for QBI earned from another trade or business that is not an SSTB or from qualified REIT dividends or qualified PTP income.

Q11. In 2018, I am single and will report taxable income over $207,500. I am NOT in an SSTB. Am I entitled to the deduction?

A11. Yes, if you have QBI, qualified REIT dividends or qualified PTP income. For eligible taxpayers with total taxable income in 2018 over $207,500 ($415,000 for married filing joint returns), the deduction for QBI may be limited by the amount of W-2 wages paid by the qualified trade or business and the UBIA of qualified

property held by the trade or business. The proposed rules provide additional information on these limitations. The IRS also issued a notice of proposed revenue procedure providing methods for determining W-2 wages for purposes of the limitation.

Q12. How do co-ops qualify for the 199A deduction?

A12. The IRS will be issuing separate guidance for co-ops.

Page Last Reviewed or Updated: 08-Aug-2018

EVEN MORE TAX LAW CHANGES AFFECTING SMALL BUSINESS

By Cliff Ennico

By now you're probably sick and tired of hearing about the Tax Cuts and Jobs Act of 2017. I know I am.

Previous columns have dealt with the two biggest changes brought about by the law:

o the lowering of tax rates on regular or C corporations from up to 35% to a flat 21%; and

o the creation of a 20% deduction on "pass through" income of (some) small business partnerships, limited liability companies (LLCs), and S corporations.

The new law has made other significant changes that as a small business owner you will want to know about. Here they are:

Section 179 Deduction. For tax years beginning after December 31, 2017, you can expense up to $1 million in equipment. They've also expanded the definition of eligible property to include certain depreciable tangible personal property used predominantly to furnish lodging. The definition of qualified real property eligible for the Section 179 deduction is also expanded to include qualified expenditures for roofs, HVAC equipment, fire protection and alarm systems, and security systems for nonresidential real property.

Depreciation Deductions. You can now deduct 100% of the cost of depreciable tangible personal property that has a depreciable life for tax purposes of 20 years or less (such as machinery, equipment, furniture, fixtures, sidewalks, roads, landscaping, computers, computer software, farm buildings, and qualified motor fuels facilities), as

long as you place it in service after September 27, 2017 and before January 1, 2023. After that, the deduction phases out over five years to zero.

For new or used passenger vehicles that are placed in service after December 31, 2017 and used over 50% for business, the maximum annual deductions allowed are $10,000 for Year 1, $16,000 for Year 2, $3,050 for Year 3, and $1,875 for Year 4 and thereafter. Slightly higher limits apply to light trucks and light vans.

Cash Basis of Accounting. Under prior law, regular or C corporations were required to use the accrual basis of accounting if the corporation's average gross receipts for the three prior years was more than $5 million. The new law raises that limit to $25 million.

Business Interest Deductions. Prior law generally allowed full deductions for interest paid or accrued by a business. Under the new law, affected corporate and noncorporate businesses generally cannot deduct interest expense in excess of 30% of "adjusted taxable income," starting with tax years beginning after December 31, 2017. For S corporations, partnerships, and LLCs, this limitation is applied at the entity level rather than at the owner level.

The "Net Operating Loss" Deduction. Under prior law, "net operating losses" (NOLs) could be carried back for up to five years and carried forward for up to 25 years. The new law provides that for tax years beginning after December 31, 2017, NOLs can be carried forward indefinitely but may no longer be carried back (except for farm businesses which can still carry back NOLs for two years. Also, NOLs arising in taxable years beginning after December 31, 2017 and carried to future years cannot offset more than 80% of taxable income before the NOL deduction.

"Excess Business Losses." For taxable years beginning after December 31, 2017, "excess business losses" of a taxpayer other than a C corporation are not allowed for the taxable year. Such losses are carried forward and treated as part of the taxpayer's NOL carryforward in subsequent taxable years. An "Excess Business Loss" for the taxable year is the excess of a taxpayer's aggregate business deductions (determined without regard to the limit) over the sum of aggregate gross income or gain of the taxpayer plus $500,000 on a joint return ($250,000 on other returns), indexed for inflation.

For partnerships, LLCs and S corporations, the limit applies at the partner or shareholder level.

Reduced or Eliminated Deduction for Business Entertainment. Under prior law, small businesses could deduct 100% of business travel costs, and 50% of meal and entertainment costs while traveling. The 100% deduction for travel costs and the 50% deduction for meals both remain unchanged in the new law (whew!), but for tax years beginning after December 31, 2017 no deductions are allowed with respect to (1) an activity generally considered to be entertainment, amusement or recreation, (2) membership dues with respect to any club organized for business, leisure, recreation or other social purposes, or (3) a facility or portion of a facility used in connection with any of the above, EVEN IF the entertainment, amusement or recreation is directly related to the active conduct of the taxpayer's trade or business.

No Deduction for "Sexual Harassment" Case Defense. And now for my favorite provision in the new law: no deduction is allowed for any settlement, payout, or attorney fees related to sexual harassment or sexual abuse claims involving you or your employees

if the payments are subject to a nondisclosure agreement. To take the deduction, you must make the settlement terms public.

If you needed any further incentive to police "hanky panky" in your workplace, there it is.

Cliff Ennico (cennico@legalcareer.com) is a syndicated columnist, author and host of the PBS television series 'Money Hunt'. This column is no substitute for legal, tax or financial advice, which can be furnished only by a qualified professional licensed in your state. To find out more about Cliff Ennico and other Creators Syndicate writers and cartoonists, visit our Web page at www.creators.com.

Topic Five:

Capitalize the Startup Business

Capitalizing the Startup Business

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Debt vs. Equity

- Debt
  - Someone loans money to startup, and is repaid over time
  - With interest (at least AFR or else IRS will "impute" interest)
  - No right to manage startup business
  - Must be repaid or else startup is in default
  - Can be secured by startup's assets (including IP)
  - May be personally guaranteed by startup's founders
- Equity
  - Someone makes a capital contribution and receives % of startup
  - In an LLC, can distinguish between "capital interest" and "profits interest"
  - Can be voting or nonvoting
  - May also have the right to manage the startup business
  - Dividends/distributions are paid only in discretion of management

Putting Money Into a Limited Liability Company

- There are two ways. The founders can either:
  - Make loans to the company and be repaid with interest
  - Make capital contributions to the company and get "founders' shares
- If founders make loans, consider a "grid" promissory note
  - Loans DO NOT need to be "pro rata"
- If founders make capital contributions:
  - Must be "pro rata" (may be difficult for all founders to do)
  - Will establish "basis" of their shares for tax purposes
- Solution: form company with as little capital as possible, with any future contributions being made via "grid" promissory notes

Taking Money out of a Limited Liability Company

- There are three ways. The founders can either:
  - Receive compensation (in the form of "guaranteed payments")
  - Receive principal and interest on any loans they've made to the company
  - Receive periodic dividends/distributions as a return on their investment
- Compensation should be spelled out in formation documents
  - Consider a "founders' agreement"
- Loans should be documented by promissory notes
- Distributions must be "pro rata" or else capital account changes
  - For corporations, dividends can be paid only out of profits/surplus

Shares of Stock (Corp) vs. Units of Membership Interest (LLC)

- Shares of stock in a corporation
  - Are usually certificated (BCL requires notation of certain matters on certificates)
  - Are either "par value" or "no par value"
  - Must pay "franchise tax" on authorized shares [in Delaware and some other states, but not New York any longer]
- Units of membership interest in a limited liability company
  - Are usually not certificated (no notation requirements in LLCL)
  - No need to designate "par value"
  - Can provide in Operating Agreement for one-on-one conversion to shares of stock if LLC converts to corporation
  - No requirement to pay "franchise tax" of any kind (except maybe on conversion)

Rights of Shareholders and LLC Members

- Right to Appoint Directors/Managers
- Limited Voting Rights for Nonvoting Shareholders/Members
- Anti-Dilution Protections
- Pre-Emptive Rights
- "Tag Along" and "Drag Along" Rights

Preferred Equity in a Corporation

- Preferred (pun intended) by investors
- Must be authorized in the Certificate of Incorporation!
- Can't use with a S corporation!
- Can be voting or nonvoting
- Remember the acronym "CCREPL" – preferred stock can be:
  - Cumulative (as to dividends)
  - Convertible (into common equity)
    - Either by holder or by company
  - Redeemable (into cash)
  - Exchangeable (into debt)
  - Participating (when common get dividends, so do holders)
  - Liquidation preference (if the Titanic goes down, holders have the lifeboats)

Preferred Equity in a Limited Liability Company

- Can be authorized in the Operating Agreement (no need to mention in Articles of Organization)
- Same rights as preferred stock in a corporation
- Can be voting or nonvoting
- Upon conversion of the LLC into a corporation, should provide for:
  - One-for-one exchange for preferred stock, OR
  - Mandatory conversion into common stock

Options and Warrants [Part 1 of 2]

- What's the difference? [pop quiz – will give book to winner]
- Allow holder to buy equity in the future at TODAY's price
- Upside: allows holder to prove his/her worth to the company
- Downside: can be adverse tax consequences to holder
- Must specify:
  - Exercise price
  - Vesting schedule
  - (Perhaps) anti-dilution protection
  - (Perhaps) automatic vesting upon a change in control of company
  - Expiration upon termination of relationship with holder
    - Vested warrants should expire within X days of termination date

Options and Warrants [Part 2 of 2]

Must consider consequences of IRC § 409A

- Section 409A was added to the Internal Revenue Code (Code) by section 885 of the American Jobs Creation Act of 2004, Public Law 108-357 (118 Stat.1418). Section 409A generally provides that unless certain requirements are met, amounts deferred under a nonqualified deferred compensation plan for all taxable years are currently includible in gross income to the extent not subject to a substantial risk of forfeiture and not previously included in gross income. *Option plans are considered deferred compensation plans.*

Convertible Securities

- Convertible Notes or Convertible Preferred
  - Must specify "conversion ratio"
  - If converting to a percentage, should state whether based on actual equity outstanding on date of issue or "fully diluted"
  - Can be convertible:
    - At holder's option
    - At company's option upon sale of company or "qualified financing"
    - At company's option on maturity [IRS might treat debt as "equity" in this case]
  - Upside: allows holders to "straddle the fence"
  - Downside: may inhibit subsequent financing if not structured properly

"Phantom Equity"

- Holder does not receive actual stock or membership interest in company
- Company creates "book entry" based on the value today of a specific number of shares
- Then, if value of those shares increases annually, holder receives cash in the amount of the difference between today's value and value at time book entry was created
- Can "ratchet" based on increase in value from year to year, rather than cumulative increase from date of issue
- Upside: no adverse tax consequences to holder, doesn't dilute other equity holders
- Downside: holder gets nothing if company loses money, or if there is a change in control of the company

"Strip Rights" Contingent on Change in Control

- Holder does not receive actual stock or membership interest in company
- Merely a promise to pay a percentage of the "net proceeds" of a change in control transaction if and when it occurs
  - Net proceeds = gross proceeds less transaction costs (brokers, professional fees)
- If issued by the company, will dilute all other equity holders – should be disclosed in company cap table and financial statements
- If issued by an equity holder, will dilute only him/her – may not need to be disclosed in company cap table and financial statements
- Upside: no adverse tax consequences – right has no value because there is a "substantial risk of forfeiture"
- Downside: not a meaningful "incentive" because change in control transaction may never happen

"Friends and Family" Offerings [Part 1 of 2]

- Sometimes the only way startups can get capital
- Beware of informal arrangements: family members' memories can get "fuzzy" about whether an investment was debt or equity . . . or even a "gift"
  - If someone "gives" you money, get it in writing (and watch out for gift taxes . . .)!
- Also, family members may feel their investment entitles them to make demands upon your company
- If more than 5 to 10 family members participate, may have to register offering in some states

"Friends and Family" Offerings [Part 2 of 2]

- ***Make sure you get the same documentation you would get from an "arm's length" investor***
  - Subscription agreement with "accredited investor" questionnaire and investor reps
  - Make sure they sign Shareholders' Agreement or LLC Operating Agreement
  - Promissory note, stock certificate or LLC membership certificate
- Consider the convertible promissory note:
  - Can be converted into [nonvoting] equity by the family member at any time
  - Can be converted into [nonvoting] equity by you if the family member becomes a "noodge" or a "time vampire
- Consider the "grid" promissory note:
  - Enables family member to make small contributions over a period of time, or charge expenses to his/her credit card (as long as company authorizes them to do that!)

Equity Crowdfunding: Entrepreneurs, Start your Engines

- Under SEC Rule 506(b), you can raise capital via the Internet or otherwise via "general solicitation and general advertising" as long as you sell only to "accredited investors"!
- You can now raise capital via crowdfunding websites (such as Kickstarter, SeedInvest), BUT:
  - You will have to prepare a prospectus and post it on a Web portal approved by the SEC – there will be fees;
  - You cannot raise more than $1 million (or $500K in two or more offerings) without audited financial statements;
  - You can communicate with investors ONLY through the portal; and
  - Ordinary investors cannot invest more than $2,000 a year (or 5% of their net income/net worth if greater) in crowdfunded offerings.
- SEC Release No. 33-9974 (October 30, 2015)
- "The Crowdfunding Handbook" by Clifford R. Ennico (AMACOM 2016)

Suggestions for Further Reading

- "Forms for Small Business Entities" by Cliff Ennico (ThomsonWest, west.Thomson.com);
- "Advising Small Businesses" by Cliff Ennico (ThomsonWest, west.Thomson.com;
- Business/Corporate and Banking Law and Practice 2017-2018 (NYSBA)
- Limited Liability Companies 2017-2018 (NYSBA)
- "The Crowdfunding Handbook" by Cliff Ennico (AMACOM)

Thank You!

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CONVERTIBLE PROMISSORY NOTE TO INITIAL INVESTOR –
CONVERTIBLE AFTER 5 YEARS OR EARLIER CHANGE IN CONTROL

CONVERTIBLE PROMISSORY NOTE

THIS NOTE HAS NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, OR UNDER THE SECURITIES LAWS OF ANY STATES. THIS NOTE HAS BEEN ISSUED IN RELIANCE UPON THE REPRESENTATION OF THE HOLDER THAT IT HAS BEEN ACQUIRED FOR INVESTMENT PURPOSES AND NOT WITH A VIEW TOWARDS THE RESALE OR OTHER DISTRIBUTION THEREOF. THIS NOTE IS SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER THE ACT AND THE APPLICABLE STATE SECURITIES LAWS, PURSUANT TO REGISTRATION OR EXEMPTION THEREFROM. HOLDERS SHOULD BE AWARE THAT THEY MAY BE REQUIRED TO BEAR THE FINANCIAL RISKS OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME.

[interest rate of note, in numbers]% CONVERTIBLE NOTE
DUE [maturity date of note]

US $[original principal amount of note] [date of note]

FOR VALUE RECEIVED, [name of borrower] a [jurisdiction of borrower's incorporation] corporation (the "**Company**"), having an address of [address of borrower], promises to pay to the order of [name of lender] (collectively, the "**Holder**"), or his heirs, executor, personal representative, or permitted successors and assigns, at the Holder's address at [lender's address] or as otherwise designated by the Holder in writing, the aggregate principal sum of $[original principal amount of note], together with interest on the unpaid principal balance of this Convertible Note (this "***Note***") at a rate equal to [interest rate, in words] percent ([interest rate of note, in numbers]%) (computed on the basis of a 360 day year of twelve consecutive 30 day months) per annum, compounded annually (the "**Interest Rate**"). Interest shall accrue from the date hereof and shall continue to accrue on the outstanding principal balance of this Note until paid in full or converted (such unpaid principal balance is referred to as the "**Outstanding Balance**"). Except as expressly provided herein, all payments of principal and interest by the Company under this Note shall be made in United States dollars in immediately available funds to an account specified by the Holder.

In no event shall any interest charged, collected or reserved under this Note exceed the maximum rate then permitted by applicable law and if any such payment is paid by the Company, then such excess sum shall be credited by the Holder as a payment of principal.

1. Transfer. This Note is transferable and assignable by the Holder only to any Person approved, in writing, by the Company, provided, however, no approval shall be required in connection with any transfer or assignment of this Note to an Affiliate of the Holder in compliance with applicable securities laws. Upon such approval, the Company agrees to issue from time to time a replacement Note in the form hereof to facilitate such transfers and assignments. In addition, after delivery of an indemnity in form and substance reasonably satisfactory to the Company, the Company also agrees to promptly issue a replacement Note if this Note is lost, stolen, mutilated or destroyed.

2. Term. To the extent not previously paid or converted in accordance with the terms herein on or prior to [maturity date of note] (the "**Maturity Date**"), the Company will repay the entire Outstanding Balance plus all interest accrued thereon on the Maturity Date.

3. Payment of Principal and Interest; Prepayment.

(a) Interest on this Note shall accrue from the date hereof and shall be payable, in arrears, and with the Principal then outstanding on the Maturity Date, unless prepaid pursuant to Section 3(b) hereof or converted pursuant to Section 4 hereof.

(b) The Company may prepay all or any portion of the Outstanding Balance, together with accrued interest to and including the date of prepayment, at any time without premium or penalty. Any such prepayment shall be applied first to interest, then to principal.

4. Conversion Rights.

(a) Conversion by the Holder.

(i) For a period of two (2) years from the date of this Note, the Holder shall not have the right to convert the Outstanding Balance plus any accrued and unpaid interest due thereon into shares of the Company's Common Stock, $[par value of corporation's stock] par value per share ("Common Stock"). Thereafter, at any time on or prior to the Maturity Date, the Holder shall have the right, upon written notice to the Company, to convert the entire Outstanding Balance plus any accrued and unpaid interest due thereon into shares of Common Stock at a conversion price equal to the fair market value of the shares of Common Stock as of the date of conversion set forth in such notice (which shall be not less than 60 days following the date of such notice), which fair market value shall be determined by the Company in good faith. Shares of the Company's Common Stock received by the Holder under this paragraph may be voting or nonvoting Common Stock, as determined by the Company's Board of Directors at the time of issuance.

(b) Conversion by the Company.

(i) If either (i) the Company has not paid the Outstanding Balance plus any accrued and unpaid interest due thereon on or prior to the Maturity Date or (ii) a Sale of the Company occurs on or prior to the Maturity Date, then the Company shall have the right, upon written notice to the Holder, to convert, effective immediately prior to the closing of the Sale of the Company or on or after the Maturity Date, as applicable, the Outstanding Balance plus any accrued and unpaid interest due thereon into shares of Common Stock at a conversion price equal to (i) in the event that the Company has not paid the Outstanding Balance plus any accrued and unpaid interest due thereon on or prior to the Maturity Date, the fair market value of the shares of Common Stock as of the Maturity Date, which fair market value shall be determined by the Company in good faith, or (ii) in the event that the Company consummates a Sale of the Company on or prior to the Maturity Date, the price per share of the Common Stock paid to the existing equity holders of the Company in connection with such Sale of the Company. Shares of the Company's Common Stock received by the Holder under this paragraph may be voting or nonvoting Common Stock, as determined by the Company's Board of Directors at the time of issuance.

(ii) A "**Sale of the Company**" shall mean (i) the reorganization, consolidation or merger of the Company in which the holders of the Company's outstanding voting securities pre-closing of that event do not retain voting securities representing a majority of the voting power of the surviving entity, (ii) the sale, transfer or exclusive license of all or substantially all of the assets of the Company, or (iii) the sale of equity by the existing holders of capital stock of the Company the result of which is that more than fifty percent (50%) of the Company's outstanding voting securities immediately following such transaction are owned by persons or entities who were not equity holders of the Company immediately prior to any such transaction.

(c) No fractional shares shall be issued upon conversion of this Note. In lieu of the Company issuing any fractional shares to Holder upon the conversion of this Note, the Company shall pay to Holder an amount equal to the product obtained by multiplying the conversion price by the fraction of a share not issued pursuant to the previous sentence. Upon conversion of this Note in full and the payment of any amounts specified in this Section 4(c), this Note shall be canceled and the Company shall be forever released from all its obligations and liabilities under this Note.

(d) The Holder hereby acknowledges, agrees and confirms that he has received a copy of the Shareholders' Agreement of the Company (the "Shareholders' Agreement"), that he has reviewed the Shareholders' Agreement with his legal counsel and has been afforded the opportunity to ask questions of the Company regarding same, and that by his execution of this Note, the Holder shall be deemed to be a party to the Shareholders' Agreement as of the effective date of conversion of this Note and shall have all of the rights and obligations of a "Shareholder" thereunder as if he had executed the Shareholders' Agreement. The Holder hereby ratifies, as of the date hereof, and agrees to be bound by, all of the terms, provisions and conditions contained in the Shareholders' Agreement, including but not limited to any and all restrictions on transfer of shares received by the Holder upon conversion of this Note.

5. Representation and Warranties of the Company. The Company hereby represents and warrants to Holder that:

(a) Organization. The Company is a corporation duly organized, validly existing and in good standing under the laws of the State of Delaware and has all requisite corporate power and authority to carry on its business as currently conducted.

(b) Corporate Power. The Company has all requisite legal and corporate power to enter into, execute and deliver this Note. This Note is a valid and binding obligation of the Company, enforceable in accordance with its terms, except as the same may be limited by bankruptcy, insolvency, reorganization, fraudulent conveyance, moratorium, usury or other laws of general application relating to or affecting enforcement of creditors' rights and the rules or laws governing specific performance, injunctive relief or other equitable remedies.

(c) Authorization. All corporate and legal action on the part of the Company, its board of directors and stockholders necessary for the sale and issuance of this Note, and the Company's performance of its obligations under this Note, have been taken.

6. Representations and Warranties of the Holder. Holder hereby represents and warrants to the Company that:

(a) Authorization. The Holder has full power and authority to enter into this Agreement. The Agreement, when executed and delivered by the Holder, will constitute valid and legally binding obligations of the Holder, enforceable in accordance with its terms, except as limited by applicable bankruptcy, insolvency, reorganization, moratorium, fraudulent conveyance and other laws of general application affecting enforcement of creditors' rights generally and as limited by laws relating to the availability of specific performance, injunctive relief or other equitable remedies.

(b) Purchase for Own Account. This Note and the shares of Common Stock issued to the Holder in connection with this Note will be acquired for investment for the Holder's own account, not as a nominee or agent, and not with a view to the public resale or distribution thereof within the meaning of the Securities Act of 1933, as amended (the "**Securities Act**"), and the Holder has no present intention of selling, granting any participation in, or otherwise distributing the same.

(c) Disclosure of Information. The Holder has received or has had full access to all the information the Holder considers necessary or appropriate to make an informed investment decision with respect to this Note and the Shares. The Holder further has had an opportunity to ask questions and receive answers from the Company regarding the terms and conditions of the offering of the Note and the Shares and to obtain additional information (to the extent the Company possessed such information or could acquire it without unreasonable effort or expense) necessary to verify any information furnished to the Holder or to which the Holder had access.

(d) Investment Experience. The Holder understands that the purchase of this Note and the Shares involves substantial risk. The Holder (i) has experience as an investor in securities of companies in the development stage and acknowledges that the Holder is able to fend for itself, can bear the economic risk of the Holder's investment in the Note and the Shares and has such knowledge and experience in financial or business matters that the Holder is capable of evaluating the merits and risks of this investment in the Note and the Shares and protecting its own interests in connection with this investment and/or (ii) has a preexisting personal or business relationship with the Company and its manager and member of a nature and duration that enables the Holder to be aware of the character, business acumen and financial circumstances of such persons.

(e) Accredited Investor Status.

(i) The Holder is either (a) an accredited investor as defined in Rule 501(a) of Regulation D promulgated under the Securities Act or (b) a sophisticated investor with adequate investment experience and opportunities to have discussions concerning the Company's business, management, financial affairs and the terms and conditions of the offering of the Securities with the Company's management.

(ii) The Holder is not or has not been subject to or has not experienced (in each case, within the period of time prescribed by the applicable disqualifying or disclosable event under Rule 506(d)) any of the disqualifying events described in Rule 506(d)(1)(i)-(viii).

(f) Foreign Investors. If the Holder is not a United States person (as defined by Section 7701(a)(30) of the Internal Revenue Code of 1986, as amended), the Holder hereby represents that it has satisfied itself as to the full observance of the laws of its jurisdiction in connection with the transactions contemplated by this Note, including (i)

the legal requirements within its jurisdiction for the purchase of the Note, (ii) any foreign exchange restrictions applicable to such purchase, (iii) any governmental or other consents that may need to be obtained, and (iv) the income tax and other tax consequences, if any, that may be relevant to the purchase, holding, redemption, sale, or transfer of the Note. The Holder's payment for and continued beneficial ownership of the Note will not violate any applicable securities or other laws of the Holder's jurisdiction.

(g) "S" Corporation Status. The Holder acknowledges and agrees that the Company has elected to be taxed under subchapter "S" of the U.S. Internal Revenue Code of 1986, as amended. The Holder represents and warrants that he is and will be eligible to become a shareholder of the Company upon conversion of this Note, and agrees that the provisions of Section 4 of this Note shall be rendered null and void ab initio in the event the Holder is rendered ineligible to become a shareholder of the Company upon conversion of this Note or if conversion of this Note, in the opinion of the Company's legal counsel, would otherwise terminate the Company's election to be taxed under subchapter "S" of the U.S. Internal Revenue Code of 1986, as amended.

(h) Restricted Securities. The Holder understands that the Shares are characterized as "restricted securities" under the Securities Act and Rule 144 promulgated thereunder inasmuch as they are being acquired from the Company in a transaction not involving a public offering, and that under the Securities Act and applicable regulations thereunder such securities may be resold without registration under the Securities Act only in certain limited circumstances. In this connection, the Holder is familiar with Rule 144, as presently in effect, and understands the resale limitations imposed thereby and by the Securities Act. The Holder understands that the Company is under no obligation to register any of the securities sold hereunder.

(i) No Solicitation. At no time was the Holder presented with or solicited by any publicly issued or circulated newspaper, mail, radio, television or other form of general advertising or solicitation in connection with the offer, sale and purchase of the Securities.

7. Events of Default.

(a) Events of Default. Each of the following defaults shall constitute an "**Event of Default**" if such default is not cured during such period of time as is specified below (or if no period of time is specified below, immediately upon such default) after the Holder has given the Company written notice of such default; provided, however, that no such notice shall be required for an Event of Default pursuant to Sections 7(a)(i), 7(a)(iii) and 7(a)(iv) below:

(i) the failure of the Company to pay principal, interest or other amounts owing, if any, under this Note when due;

(ii) unless waived by the Holder, the Company's material breach of any representations or warranties of the Company under this Note which breach is not cured by the Company within ten (10) days of notice thereof from the Holder;

(iii) if the Company shall (1) make a determination to discontinue its business, (2) apply for or consent to the appointment of a receiver, trustee, custodian or liquidator of it or any of its property, (3) admit in writing its inability to pay its

debts, (4) make a general assignment for the benefit of creditors, or (5) file a voluntary petition in bankruptcy, or a petition or an answer seeking reorganization or an arrangement with creditors, or to take advantage of any bankruptcy, reorganization, insolvency, readjustment of debt, dissolution or liquidation laws or statutes, or an answer admitting the material allegations of a petition filed against it in any proceeding under any such law; or

(iv) if there shall be filed against the Company an involuntary petition seeking reorganization of the Company or the appointment of a receiver, trustee, custodian or liquidator of the Company or a substantial part of its assets, or an involuntary petition under any bankruptcy, reorganization or insolvency law of any jurisdiction, whether now or hereafter in effect (any of the foregoing petitions being hereinafter referred to as an "**Involuntary Petition**") and such Involuntary Petition shall not have been dismissed within ninety (90) days after it was filed.

(b) Acceleration Upon Event of Default. Upon each and every such Event of Default pursuant to Sections 7(a)(i) and 7(a)(ii) (subject to cure), this Note and any and all indebtedness of the Company to the Holder under this Note shall immediately become due and payable, and upon an Event of Default pursuant to each of the other subsections under Section 7(a) above, and at any time thereafter during the continuance of such Event of Default, at the election of the Holder, this Note and any and all indebtedness of the Company to Holder under this Note shall immediately become due and payable both as to principal and interest (including any accrued and unpaid interest thereon), without presentment, demand, or protest, all of which are hereby expressly waived, anything contained herein or other evidence of such indebtedness to the contrary notwithstanding.

(c) Other Remedies. In case any one or more Events of Default shall occur and be continuing, whether or not any acceleration of the Note shall have occurred, the Holder may, among other things, proceed to protect and enforce Holder's rights by an action at law, suit in equity or other appropriate proceeding, whether for the specific performance of any agreement contained herein, or for an injunction against a violation of any of the terms hereof or thereof or in and of the exercise of any power granted hereby or thereby or by law. The Holder shall have a full right of offset for any amounts due upon such an Event of Default against any amounts payable by the Holder to the Company. No right conferred upon the Holder hereby shall be exclusive of any other right referred to herein or therein or now or hereafter available at law, in equity, by statute or otherwise.

8. Miscellaneous.

(a) To the extent that, prior to the Maturity Date, the Company issues notes in connection with a subsequent round of note financing (the "**Subsequent Notes**"), and the Subsequent Notes contain a cap with respect to the conversion of the outstanding balance thereunder upon a qualified financing, the Company hereby covenants and agrees to amend this Note, such that this Note shall contain the same conversion cap provisions as the Subsequent Notes. The Company hereby agrees to take, or cause to be taken, all actions, and to do, or cause to be done, all things reasonably necessary under applicable laws to in order to carry out the purpose and intent of this provision.

(b) This Note does not by itself entitle the Holder to any voting rights or other rights as a stockholder of the Company. No provisions of this Note, and no enumeration herein of

the rights or privileges of the Holder, shall cause the Holder to be a stockholder of the Company for any purpose.

(c) This Note shall be governed in all respects by the laws of the State of [jurisdiction where borrower is incorporated] without regard to principles of conflict of laws. Any action, claim or proceeding under this Note shall be commenced exclusively in the federal courts of the United States of America courts of the State of [jurisdiction where borrower is located] having jurisdiction over the [county where borrower is located], and the parties hereby irrevocably waive any objection they may now or hereafter have to the exclusive jurisdiction and venue of such courts.

(d) The titles, captions and headings of this Note are included for ease of reference only and will be disregarded in interpreting or construing this Note. Unless otherwise specifically stated, all references herein to "sections" and "exhibits" will mean "sections" and "exhibits" to this Note.

(e) All notices and other communications given or made pursuant to this Note shall be in writing and shall be deemed effectively given: (a) upon personal delivery to the party to be notified, (b) when sent by confirmed electronic mail or facsimile if sent during normal business hours of the recipient, and if not so confirmed, then on the next business day, (c) five days after having been sent by registered or certified mail, return receipt requested, postage prepaid, or (d) one day after deposit with a nationally recognized overnight courier, specifying next day delivery, with written verification of receipt. All communications shall be sent to the Holder at the address set forth below, or at such other place as may be designated by a Holder in writing to the Company, and to the Company at the address set forth below, or to such e-mail address, facsimile number or address as subsequently modified by written notice given in accordance with this Section 8. A party may change or supplement the addresses given below, or designate additional addresses, for purposes of this section by giving the other party written notice of the new address in the manner set forth above.

If To Holder:	If to the Company:
[name and address of lender]	[name and address of borrower]
Fax Number: _____	Fax Number: _____
Email: _____	Email: _____

(f) No delay or omission to exercise any right, power or remedy accruing to the Holder, upon any breach or default of the Company under this Note, shall impair any such right, power or remedy of the Holder nor shall it be construed to be a waiver of any such breach or default, or an acquiescence therein, or of any similar breach of default thereafter occurring or any waiver of any other breach or default theretofore or thereafter occurring. The acceptance at any time by the Holder of any past-due amount shall not be deemed to be a waiver of the right to require prompt payment when due of any other amounts then or thereafter due and payable. Any waiver, permit, consent or approval of any kind or character on the part of the Holder of any breach of default under this Note or any waiver on the part of the Holder of any provisions or conditions of this Note, must be in writing

and shall be effective only to the extent specifically set forth in such writing. All remedies, either under this Note, or by law or otherwise afforded to the Holder shall be cumulative and not alternative.

(g) This Note may be executed in any number of counterparts, each of which shall be an original, but all of which together shall constitute one instrument.

(h) If any paragraph, provision or clause of this Note shall be found or be held to be illegal, invalid or unenforceable, the remainder of this Note shall be valid and enforceable and the parties shall use good faith to negotiate a substitute, valid and enforceable provision that most nearly effects the parties' intent in entering into this Note.

(i) The Company hereby waives presentment, demand, protest, notice of dishonor, diligence and all other notices, any release or discharge arising from any extension of time, discharge of a prior party, release of any or all of any security given from time to time for this Note, or other cause of release or discharge other than actual payment in full hereof.

(j) The Holder shall not be deemed, by any act or omission, to have waived any of the Holder's rights or remedies hereunder unless such waiver is in writing and signed by the Holder and then only to the extent specifically set forth in such writing. A waiver with reference to one event shall not be construed as continuing or as a bar to or waiver of any right or remedy as to a subsequent event. No delay or omission of the Holder to exercise any right, whether before or after a default hereunder, shall impair any such right or shall be construed to be a waiver of any right or default, and the acceptance at any time by the Holder of any past-due amount shall not be deemed to be a waiver of the right to require prompt payment when due of any other amounts then or thereafter due and payable.

(k) Each party hereto shall be responsible for the fees and disbursements of attorneys, accountants, consultants and any other representative or agent retained by such party in regard to this Agreement.

(l) Any term of this Note may be amended, and the observance of any term of this Note may be waived (either generally or in a particular instance and either retroactively or prospectively), only with the written consent of the Company and the Holder.

IN WITNESS WHEREOF, the Company and the Holder have executed this Note as of the date first above written.

COMPANY:

[Name of Borrower]

By: _____
Print Name and Title:

HOLDER:

/s/_____

Print Name:

[Reprinted with permission from "Forms for Small Business Entities," by Clifford R. Ennico]

LETTER GRANTING KEY EMPLOYEE RIGHT TO RECEIVE PERCENTAGE OF CHANGE IN CONTROL ("STRIP RIGHT")

[date]

Mr./Ms. _____
_____
_____

RE: *Your Investment in [Name of Company]*

Dear _____:

This will confirm our recent telephone conversations and e-mail exchanges, and acknowledge receipt from you of the performance of certain services which you intend as an investment in [name of company, a [corporation/partnership/limited liability company] organized and existing under the laws of the State of [state where company is organized or incorporated] ("Company").

In exchange for these services, the undersigned hereby grants you the unconditional and irrevocable right to receive _____ percent (____%) of the "net proceeds" actually received by the undersigned upon the consummation of any of the following events (each a "Triggering Event"):

(i) the merger or consolidation of Company with or into any corporation, limited liability company or other person or legal entity whatsoever, the result of which is that an unrelated third party controls the entity surviving such merger or consolidation;

(ii) the sale of all or substantially all of the assets of Company to an unrelated third party; or

(iii) the sale of more than fifty percent (50%) of the aggregate issued and outstanding LLC membership interests in Company to an unrelated third party.

For purposes of this letter, "net proceeds" shall be the gross amount actually received by Company or its members in any of the above Triggering Events, less brokers' commissions, investment banking fees, legal and accounting fees, and other usual and customary transaction costs incurred by Company in consummating such Triggering Event.

In the event the members of Company determine to reorganize Company as a subchapter "S" or subchapter "C" corporation under the laws of the State of Delaware or any other jurisdiction, the right evidenced by this letter shall be converted into ____ percent (___%) of the non-voting common stock of such corporation effective the date of such reorganization. In addition, at any time at the option of Company, the right evidenced by this letter may be converted into a ____ percent (___%) "Economic Interest" in Company, as such quoted term is defined in the Operating Agreement of Company. You agree in either such event to execute and deliver any and all documents, certificates and instruments Company or its advisors may require you to sign as a condition to such conversion.

You acknowledge and agree that you will not be entitled to membership in [Name of Company] by virtue of the right granted by this letter, and as such will not have any right to participate in the management of the business and affairs of Company, any right to vote on, consent to, or otherwise participate in any decision or action of or by the members of Company,

or any right to receive distributions of cash or property made to the members of Company from time to time, except for such rights as may be granted to you as a member of Company under the Operating Agreement of Company as now or hereafter in effect.

The right granted by this letter is non-assignable and non-transferable, except for transfers by operation of law in the event of your death.

You hereby represent and warrant that (a) you are acquiring the right granted by this letter for your own account, for purposes of investment and not with a view to the distribution thereof, as those terms are used in the U.S. Securities Act of 1933, as amended (the "Act") and the rules and regulations of the Securities and Exchange Commission (SEC) thereunder, (b) you have sufficient knowledge and experience in financial and business matters so as to be capable of evaluating the merits and risks of acquiring this right, (c) you have received copies of such documents and such other information as you have deemed necessary in order to make an informed investment decision with respect to Company and the right granted by this letter, and (d) you understand, and have the financial capability of assuming, the economic risk of an investment in Company for an indefinite period of time.

This letter contains the entire agreement of the parties relating to the subject matter hereof, and supersedes any and all prior agreements or understandings. This letter agreement is governed by Connecticut law, and any action, claim or proceeding hereunder will be commenced exclusively in the state or federal courts located in the State of [state where company is organized or incorporated]. This letter agreement may be amended and changed, and any provision of this letter may be waived, only by a written instrument signed by both parties.

Please indicate your acceptance of and agreement to the foregoing terms and conditions by signing this letter in the space provided below and returning one (1) original signed counterpart to my attention.

Yours very truly,

[Name of Company]

By: _____
Print Name and Title: _____

ACCEPTED AND AGREED TO this
_____ day of _____, 20__:

Signature: _____

Print Name: _____

Address: _____

Social Security No.: _____

[Reprinted with Permission from "Forms for Small Business Entities," By Clifford R. Ennico, Thomson/West]

"GRID" PROMISSORY NOTE BETWEEN SMALL BUSINESS ENTITY AND INDIVIDUAL OWNER

$_____ [date]
[city and state]

FOR VALUE RECEIVED, _____, a [corporation/partnership/limited liability company] organized and existing under the laws of the State of New York having its principal place of business at _____ (the "Borrower") promises to pay to the order of _____, an individual residing at _____ (the "Lender") at the Lender's residence address or such other place as the holder hereof shall designate, amounts loaned by the Lender to the Borrower from time to time up to the maximum principal amount of _____ and 00/100 Dollars ($_____), in same day or other immediately available funds together with interest on unpaid balances, at an interest rate per annum equal to ____ percent (___%) per annum. In the event that Borrower fails to make any principal or interest payment due hereunder within ____ (___) business days following the due date therefor, then the entire unpaid principal balance of this Note, along with all other amounts due hereunder, shall accelerate and be immediately due and payable.

To the extent not sooner repaid, the entire principal balance made hereunder shall be due and payable in a single installment on _____, 20__, together with any accrued and unpaid interest and all other sums due hereunder. Payments of principal and interest under this Note shall be made in lawful currency of the United States and shall be applied, in order, first to costs of collection, second to interest, and third to principal. As long as the Borrower is not in default under this Note, amounts repaid to Lender may be reborrowed from time to time with the Lender's approval, up to the maximum principal amount set forth herein.

Borrower may pay or prepay the outstanding principal amount of this Note, in whole or in part, at any time without premium or penalty. Prepayments shall be applied first to accrued and unpaid interest on this Note, and then to the outstanding principal balance hereof.

All loans hereunder and all payments and prepayments on account of principal and interest hereof shall be recorded by the Lender and, prior to any transfer hereof, endorsed on the grid on the reverse hereof which is part of this Note, the entries on the records of the Lender (including any appearing on this Note) shall be prima facie evidence of amounts outstanding hereunder. Any failure of Lender or any note holder to make any such notation shall not affect the unconditional obligation of Borrower to pay all amounts due hereunder as and when due.

Upon the happening of any of the following events, each of which shall constitute a default hereunder, this Note shall become immediately due and payable at the option of Holder: (1) failure of the Maker or any other obligor (which shall include each maker, endorser, surety and guarantor of this Note) to perform any agreement or obligation hereunder within any applicable grace or cure period; (2) death, dissolution or liquidation of the Maker or any endorser, surety or guarantor of this Note; (3) filing of an petition in bankruptcy by or against the Maker or any endorser, surety or guarantor of this Note; (4)

application for appointment of a receiver for, making of a general assignment for the benefit of creditors by, or insolvency of the Maker or either of them or any endorser, surety or guarantor of this Note; or (5) a default or event of default under any document, instrument or certificate providing collateral security to Holder for Maker's obligations under this Note and the expiration of any applicable grace or cure period.

If this Note is placed with an attorney for collection upon any default, Maker agrees to pay to Holder all attorneys' fees and all lawful costs and expenses of collection, whether or not a suit is commenced.

Maker agrees that no delay or failure on the part of Holder in exercising any power, privilege, remedy, option or right hereunder shall operate as a waiver thereof or of any other power, privilege, remedy, option or right; nor shall any single or partial exercise of any power, privilege, remedy, option or right hereunder preclude any other or future exercise thereof or the exercise of any other power, privilege, remedy, option or right; nor shall Holder be liable for exercising or failing to exercise any such power, privilege, remedy, option or right. The rights and remedies expressed herein are cumulative, and may be enforced successively, alternately or concurrently and are not exclusive of any rights and remedies which Holder may or would otherwise have under the provisions of applicable law.

Maker waives presentment, demand, protest and all other demands in connection with the delivery, acceptance, performance, default or enforcement of this Note.

THE MAKER WAIVES ALL RIGHT TO TRIAL BY JURY IN ANY ACTION OR PROCEEDING TO ENFORCE OR DEFEND ANY RIGHTS UNDER THIS NOTE OR UNDER ANY AGREEMENT, INSTRUMENT OR OTHER DOCUMENT CONTEMPLATED HEREBY OR RELATED HERETO AND IN ANY ACTION DIRECTLY OR INDIRECTLY RELATED TO OR CONNECTED WITH THE INDEBTEDNESS OR THIS NOTE, OR ANY CONDUCT RELATING TO THE ADMINISTRATION OR ENFORCEMENT OF THE INDEBTEDNESS OR ARISING FROM THE DEBTOR/CREDITOR RELATIONSHIP OF THE MAKER AND THE LENDER. THE MAKER ACKNOWLEDGES THAT THIS WAIVER MAY DEPRIVE MAKER OF AN IMPORTANT RIGHT AND THAT SUCH WAIVER HAS BEEN KNOWINGLY AND VOLUNTARILY MADE BY THE MAKER.

This Note represents a loan negotiated, executed and to be performed in the State of New York, and shall be construed, interpreted and governed by the laws of said State. Maker hereby consents to the personal jurisdiction of the state and federal courts located in the State of New York in connection with any controversy related to this Note, waives any argument that venue in such forums is not convenient, and agrees that any litigation in connection with this Note shall be venued in either the County of _____ in the State of New York or the United States District Court for the _____ District of New York.

[NAME OF LEGAL ENTITY]

By: _____

Print Name and Title:

GRID
ADVANCES AND PAYMENTS OF PRINCIPAL

Date	Amount of Loan	Outstanding Principal Balance	Amount of Payment	Accrued Interest	Principal Portion	Notation Made By (Initials)
01/01/2014	$100.00	$100.00				CRE
12/31/2014			$ 50.00	$ 3.00	$ 47.00	CRE

[reprinted with permission from "Forms for Small Business Entities," By Clifford R. Ennico, Thomson/West]

PHANTOM STOCK PLAN

[N.B. Traditionally, phantom stock plans have been used exclusively by corporations. In theory, there is no reason why a limited liability company (LLC) could not adopt a similar plan. In order to do so, however, the LLC would need to create "units" of its membership interest in its Operating Agreement. These "units" would be the functional equivalents of shares of common stock in a corporation.]

1. **Purpose of the Plan.** The purposes of the _____ *[name of sponsoring entity]* Phantom Stock Plan (the "Plan") are to provide a means to attract, reward, and retain strong management, and to align the interests of key managers participating in the Plan with the interests of shareholders by offering an incentive compensation vehicle based upon the growth in shareholders' equity and the value of *[name of sponsoring entity]*.

2. **Definitions.** In this Plan, the following terms shall have the meanings as set forth below:

(a) "Board" means the Board of Directors of the Company.

(b) "Book Value" means the Company stockholders' equity as adjusted for the possible exercise of Stock Options and conversion of debentures divided by the total number of shares outstanding, on a fully diluted basis.

(c) "Committee" means the Phantom Stock Plan Committee of the board, or any other committee the Board may subsequently appoint to administer the Plan, as defined in this document. The Committee shall be composed entirely of directors who meet the requirements as set forth in Section III of this Plan.

(d) "Common Stock" means the common stock of the Company, having a par value of $_____ per share.

(e) "Company" means _____ and any present subsidiary corporations or any successor to such corporations.

(f) "Deferred Compensation Agreement" means the voluntary election on behalf of an Employee in the Plan to defer all or stipulated portions of the payment of the value of such Employee's Phantom Share Awards to a specified future date, including any interest or increase in value credited thereon. The Employee who elects to participate in the deferral arrangement pursuant to this Plan must do so in accordance with Section VIII of the Plan and participate in the Deferred Compensation Agreement, as set forth in this agreement.

(g) "Employee" means any employee of the Company selected to participate in the Plan.

(h) "Grant Date" means the date as of which a Phantom Share is granted by the Committee pursuant to this Plan.

(i) "Grantee" means an individual to whom a Phantom Share is granted by the Committee pursuant to this Plan.

(j) "Phantom Share" means a fictitious share of Company stock equal to the Common Stock's Book Value; each Phantom Share will be equal to 100% of the Book Value per share of Common Stock on a fully diluted basis.

(k) "Phantom Share Award" means the appreciation in value of each Phantom Share from the date of grant until the date of exercise, not to exceed $_____ per share.

3. **The Committee as Plan Administrators.** The Plan shall be administered by the Phantom Stock Plan Committee (the "Committee"), which shall consist of not fewer than _____ persons who shall be appointed by the Board and each of whom shall be a "disinterested person," as that term is defined in Rule 16b-3 under the Securities Exchange Act of 1934, as amended. Subject to the provisions of the Plan, the Committee shall have exclusive power to select the Employees entitled to participate in the Plan, to determine the size of the awards to be made to each such Employee, and to determine the time or times when awards shall be made. The Committee's interpretation of the Plan and any action it takes with respect to awards granted pursuant to it shall be final and binding unless otherwise determined by the Board. The Committee shall have the authority, subject to the provisions of the Plan, to establish, adopt, revise or repeal such rules, regulations and procedures with respect to the Plan as it may deem necessary or appropriate to accomplish the objectives of the Plan.

4. **Aggregate Limitation on Phantom Shares Subject to the Plan.** The number of Phantom Shares that may be awarded under this Plan shall not exceed an aggregate of _____ . If any Phantom Shares granted under the Plan shall expire or terminate or be forfeited or cancelled, such Phantom Shares may again be granted pursuant to the Plan.

5. **Terms and Conditions of Grant of Phantom Shares.** Each Phantom Share granted under this Plan shall be subject to the following terms and conditions;

(a) Each Phantom Share granted shall continue in effect for a period of _____ years from the Grant Date; subject, however, to earlier termination and exercise as hereinafter provided.

(b) Each grant shall be evidenced by a written instrument specifying to the grantee the number of Phantom Shares granted and the terms and conditions of such grant.

(c) No Phantom Share may be granted on or after the tenth anniversary of the date upon which this Plan was adopted by the Board.

(d) Except as provided in this Plan, the grant of a Phantom Share shall not be transferable other than by will or the laws of descent and distribution. During the Grantee's lifetime, a Phantom Share grant shall be exercisable only by the Grantee, except as otherwise provided in this Plan. The Committee may permit the transfer, upon the Grantee's death, to beneficiaries designated by the Grantee in a manner authorized by the Company and may permit the exercise, during the Grantee's lifetime, by Grantee's guardian or legal representative; provided that the Committee determine that such transfer and such exercise are consonant with requirements for exemption from Section 16(b) of the Securities Exchange Act of 1934, as amended.

6. **The Valuation of Phantom Share Awards.** The following conditions pertain to the valuation of Phantom Share Awards granted pursuant to this Plan:

(a) The maximum value which will be placed on the value to be paid from the exercise of a Phantom Share grant pursuant to this Plan will be equal to 100% of the value of the Phantom Share on the Grant Date. Should the Grantee elect to exercise the Phantom Shares granted, and the Book Value of the common Stock on the date of exercise exceeds the Book Value of the Common Stock on the Grant Date by an amount equal to or greater than 100%, the maximum payment made to the Grantee shall be 100% of the Common Stock's Book Value on the Grant Date or $_____ per share whichever is less.

(b) The payment for all Phantom Share Awards shall be made in cash. All Phantom Share Awards paid pursuant to the Plan, whether at the time of exercise or subject to the terms of the Deferred Compensation Agreement, shall be in the form of cash.

7. **Exercise of Phantom Shares.**

(a) A Phantom Share granted pursuant to this Plan may be exercised, to the extent it is then exercisable, by giving written notice to the Secretary of the Company. Upon exercise of the Phantom Shares, the Employee shall be entitled to receive a payment equal to the appreciation in the Book Value per share of Common Stock from the Grant Date for each Phantom Share then exercisable, subject to the maximum value of Phantom Share Awards as set forth in Section 6(a).

(b) Phantom Shares granted to participants in the Plan which have not been exercised shall become automatically exercised in the event of a Company Change in Control, as set forth in Section 13.

8. **Deferred Compensation Agreement.** Employees may voluntarily elect to defer all or stipulated portions of the payment of their Phantom Share Awards to a specified future date such as their normal retirement date. The voluntary decision to defer the Phantom Share Awards must meet the following terms and conditions as set forth in the Deferred Compensation Agreement:

(a) The Employee must make his election to defer on the Grant Date and provide written notice as specified in the Deferred Compensation Agreement.

(b) On the Grant Date, the Employee must specify within the written agreement the future date at which such payment shall be made.

(c) The Employee must specify within the written agreement that the decision to defer his Phantom Share Award payments is voluntary and irrevocable.

(d) The Phantom Shares granted, if the Employee elects the Deferred Compensation Agreement, shall become automatically exercised upon the earlier of the following three events and shall be credited to the Employee's deferred compensation account when:

(i) The 10-year term of the Phantom Share grant has expired;

(ii) The value of the potential Phantom Share Award has reached its maximum of 100% of the Phantom Shares' value on the Grant Date or $_____ per share whichever is less. This will occur will the release of annual/quarterly Company financial statements when the computation of Book Value can be completed; or

(iii) The Company experiences a company Change in Control, as defined and set forth in Section 13 of this Plan.

(e) Should the Employee elect to defer his Phantom Share Awards and the Phantom Share grant expires with a value of less than the value on the Grant Date, the Phantom Shares shall have no value and cannot be credited to the Employee's deferred compensation account.

9. **Dilution and Changes in Capitalization.** In between the date of grant of a Phantom Share and the date of its exercise, any change that shall occur in the number of shares of the Company's Common Stock outstanding as the result of any stock split or any stock dividend of _____ % or more during any calendar year, then the unexercised portion of any such Phantom Shares granted shall be adjusted proportionately to the adjustment in the Company's Common Stock. In the event of any other change in the number or character of the outstanding securities of the Company as the result of any recapitalization, reclassification, consolidation or any analogous change in capitalization or of any distribution to holders of the Company's Common Stock other than a cash or stock dividend, the Committee shall make such adjustments, if any, in the manner of calculating the valuation of any Phantom Shares then exercisable or thereafter becoming exercisable as it, in the reasonable exercise of its discretion, deems equitable and appropriate.

10. **Factors To Be Considered on Grant of Phantom Shares.** In making any determination as to the Employees to whom Phantom Shares shall be granted and as to the number of Phantom Shares in any single grant, the Committee shall take into account the duties and responsibilities of the respective Employees, their present and potential contributions to the success of the Company, and such other factors as the Committee shall deem important in connection with accomplishing the purposes of the Plan.

11. **Termination of Employment.** If the employment of an Employee to whom Phantom Shares have been granted shall be terminated by the Company without cause (which shall be determined solely by the Committee) and otherwise than as provided for in Section 12, such Phantom Shares may be exercised (to the extent that they would have been exercisable on the date of termination if such employment had not been terminated) at any time within _____ months after such termination. If the employment of an Employee to whom Phantom Shares shall have been granted shall be terminated by the Company with cause or by the Employee's voluntary resignation with or without cause (all of which shall be determined solely by the Committee) and otherwise than as provided for in Section 12, such Phantom Shares shall expire simultaneously with such termination of employment. So long as the Grantee of Phantom Shares shall continue to be an Employee of the Company or of one or more of its subsidiaries, his Phantom Shares shall not be affected by any change of duties or position. Nothing in the Plan or in any Phantom Share agreement shall confer upon any Employee any right to continue in the employ of the Company or interfere in any way with the right of the Company to terminate his employment at anytime whether for cause, or not.

12. **Death or Incapacity of an Employee.** If an Employee to whom Phantom Shares have been granted shall die or become physically or mentally incapacitated, as determined solely by the Committee, while he shall be employed by the Company or within _____ months after the termination by the Company of his employment without cause, which shall be determined solely by the Committee, all Phantom Shares then held by such Employee exercisable immediately prior to such Employee's death or incapacity may be exercised by the employee or his personal or other legal representative at any time within _____ months after his death or incapacity or _____ months after the date of termination of his employment by reason of incapacity, whichever is later.

13. **The Effect of Company Change in Control.**

(a) This Plan shall be affected by the event of a Company Change in Control. A Company Change in Control, for the sole purposes of this Plan, shall mean one or both of the following events:

(i) The event that the voting control of more than 50% of the voting securities of the Company are in the ownership of a single party or entity other than the existing principal shareholders of Company Common Stock at the time this Plan was adopted by the Board, and/or

(ii) The event that the Company is either acquired by and/or merged with another organization or corporate entity, resulting in the Company's Common Stock no longer being available as the registered voting securities or surviving Common Stock subsequent to the establishment of the merged organization.

(b) At the time a Company Change in Control becomes effected, all Phantom Shares granted pursuant to the Plan shall become automatically exercised and paid to Participants, either in the form of cash awards or credited to the Participant's Deferred Compensation Account if the Participant elected to participate in the Deferred Compensation Agreement addendum to this Plan.

(c) In the event of a Company Change in Control, the value of the Phantom Shares awarded will be adjusted by a multiple. The multiple will be calculated by dividing the purchase

price per share by the net book value per share. This will result in the value of the Phantom Share Awards to be computed by the following formula:

(i) value of the Phantom Share on the Grant Date, multiplied by

(ii) a factor resulting from dividing the per share purchase price arising from the change in control by the per share net book value, less

(iii) the value of the Phantom Share on the Grant Date.

The result of the above formula may yield a Phantom Share Award equal to or greater than 100% of the value of the Phantom Share on the Grant Date. In that event, the Grantee will be entitled only to 100% of the Phantom Share on the Grant Date or $_____ per share, whichever is less, as stipulated in Section 6 of the Plan.

(d) It is not this Plan's intent to make "excess parachute payments," as defined in Section 280G of the Internal Revenue Code of 1986, as amended (the "Code"), which would be nondeductible for federal income tax purposes by the Company. Consequently, if gains resulting solely from the operation of this paragraph would be nondeductible by the Company for federal income tax purposes due to Section 280G of the Code, such payments would be reduced by the smallest amount required (but not below zero) so that no payments are nondeductible under Section 280G of the Code. If any payments previously made to or for the benefit of an Employee from this or any other Plan or Agreement are subsequently determined to be nondeductible because of Section 280G of the Code, such Employee shall be required to promptly repay the Company, at its request, the smallest amount necessary so that, after giving effect to such repayments to the Company, no payments to or for the benefit of the Employee (or the smallest amount possible) will be nondeductible under Section 280G; provided, however, that any such repayments, adjusted for the time value of such amounts under the principles of Section 1274(b)(4) of the Code, may not exceed the amount of payments originally made from this or any other Plan or agreement, nor may they reduce the amount that would otherwise be nondeductible to the Company.

(e) The terms and provisions of this Section 13 of the Plan shall only become effective in the event of a Company Change in Control as defined in this Section of the Plan.

14. **Effective Date of the Plan.** This Plan shall become effective on the date of its adoption by the Board; provided, however, that the Plan shall automatically terminate and all Phantom Shares theretofore granted shall be null and void, in the event that the Plan shall not have been duly and validly approved by the affirmative vote of a majority of the stockholders of the Company present or represented at the annual meeting of the stockholders of the Company next following the adoption of the Plan by the Board.

15. **Amendment, Suspension, or Termination of Plan.** The Committee may at any time terminate, suspend or amend this Plan; however, no amendment shall, without the approval of stockholders of the Company:

(a) increase the number of Phantom Shares which may be granted pursuant to the Plan;

(b) change the maximum period during which Phantom Shares may be granted;

(c) extend the effective date of the Plan; or

(d) materially modify the requirements as to eligibility for participation in the Plan.

16. **Duration of the Plan.** No Phantom Shares shall be granted under this Plan 10 years after the date the Plan was adopted by the Board. Phantom Shares granted before that date shall remain valid thereafter in accordance with their terms.

This Plan was adopted by the Board of Directors on _____ *[date]*.

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COMMON STOCK WARRANT AGREEMENT

[date]

NEITHER THIS WARRANT, NOR THE STOCK TO BE ISSUED UPON EXERCISE HEREOF, HAS BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "1933 SECURITIES ACT"), OR QUALIFIED OR REGISTERED UNDER ANY STATE SECURITIES LAWS (THE "STATE SECURITIES LAWS"), AND THIS WARRANT HAS BEEN, AND THE COMMON STOCK TO BE ISSUED UPON EXERCISE HEREOF WILL BE, ACQUIRED FOR INVESTMENT AND NOT WITH A VIEW TO, OR FOR RESALE IN CONNECTION WITH, ANY DISTRIBUTION THEREOF. NO SUCH SALE OR OTHER DISPOSITION MAY BE MADE WITHOUT AN EFFECTIVE REGISTRATION STATEMENT UNDER THE 1933 SECURITIES ACT AND COMPLIANCE WITH THE APPLICABLE STATE SECURITIES LAWS, OR AN OPINION OF COUNSEL, REASONABLY SATISFACTORY TO THE ISSUER AND ITS COUNSEL, THAT SAID REGISTRATION IS NOT REQUIRED UNDER THE 1933 SECURITIES ACT AND THAT APPLICABLE STATE SECURITIES LAWS HAVE BEEN COMPLIED WITH.

This certifies that *[name]* ("Purchaser"), a corporation organized and existing under the laws of *[state]* having its principal place of business at *[address]*, or any party to whom this Warrant is assigned in compliance with the terms hereof (Purchaser and any such assignee being hereafter sometimes referred to as "Holder"), is entitled to subscribe to and purchase, during the period commencing at the date first set forth above and ending at 11:59 p.m. local time in *[city and state where issuer has principal place of business]*, on *[date]*, *[number]* shares of fully paid and nonassessable common stock, having a par value of _____ dollars ($_____) per share (the "Common Stock") of *[name of issuing corporation]* (the "Company"), a corporation organized and existing under the laws of *[state]* with its principal place of business at *[address]*. The purchase price of each such share shall be the Warrant Price as defined below. This Warrant was originally issued to Purchaser pursuant to the Agreement (as defined below).

ARTICLE I. DEFINITIONS

1.1 "Agreement" shall mean that certain Loan Agreement entered into by and between Purchaser and the Company of even date herewith.

1.2 "Common Stock Equivalents" shall mean Convertible Securities and Rights.

1.3 "Convertible Securities" means any securities which are directly or indirectly convertible into Common Stock.

1.4 "Effective Price" means the quotient obtained by dividing (i) Minimum Consideration by (ii) Maximum Shares Upon Exercise.

1.5 "Maximum Shares Upon Exercise" means the maximum number of shares of Common Stock issuable under a Common Stock Equivalent upon complete exercise and full conversion of all Rights or Convertible Securities represented thereby, computed without regard to contingent adjustments to the number of shares issuable upon exercise

and conversion (other than adjustments caused solely by the passage of time which increase the number of shares issuable upon exercise and conversion).

1.6 "Minimum Consideration" means the minimum aggregate consideration paid or payable at any time for the purchase of the Common Stock Equivalents during the term of the Common Stock Equivalents, and upon complete exercise and full conversion of the Common Stock Equivalents, computed without regard to contingent adjustments to exercise or conversion price (other than adjustments caused solely by the passage of time which reduce such minimum aggregate consideration).

1.7 "Rights" means any options, warrants, or rights to purchase Common Stock or Convertible Securities.

1.8 "Warrant Price" shall mean _____ dollars ($_____).

ARTICLE II. EXERCISE AND PAYMENT

2.1 *Cash Exercise.* The purchase rights represented by this Warrant may be exercised by Holder, in whole or in part, by the surrender of this Warrant at the principal office of the Company, and by the payment to the Company, by certified, cashier's or other check acceptable to the Company, of an amount equal to the aggregate Warrant Price of the shares being purchased.

2.2 *Net Issue Exercise.* In lieu of exercising this Warrant pursuant to Section 2.1, Holder may elect to receive shares of Common Stock equal to the value of this Warrant (or of any portion thereof remaining unexercised) by surrender of this Warrant at the principal office of the Company together with notice of such election, in which event the Company shall issue to Holder a number of shares of the Company's Common Stock computed using the following formula:

$$X = Y (A-B)/A$$

Where

X = the number of shares of Common Stock to be issued to Holder.

Y = the number of shares of Common Stock purchasable under this Warrant (at the date of such calculation).

A = the fair market value of one share of the Company's Common Stock (at the date of such calculation).

B = Warrant Price (as adjusted to the date of such calculation).

2.3 *Fair Market Value.* For purposes of this Section 2, fair market value of one share of the Company's Common Stock shall mean:

(i) The average of the closing bid and asked prices of the Company's Common Stock quoted in the Over-The-Counter Market Summary or the closing price quoted on any exchange on which the Common Stock is listed, whichever is applicable, as

published in the *[city]* Edition of The Wall Street Journal for the *[number]* trading days prior to the date of determination of fair market value; or

(ii) If the Company's Common Stock is not traded Over-The-Counter or on an exchange, the per share fair market value of the Common Stock shall be as determined by an independent appraiser appointed in good faith by the Company's Board of Directors. The cost of such appraisal shall be borne by the Company.

2.4 *Stock Certificate.* In the event of any exercise of the rights represented by this Warrant, certificates for the shares of Common Stock so purchased shall be delivered to Holder within a reasonable time and, unless this Warrant has been fully exercised or has expired, a new Warrant representing the Aggregate Price with respect to which this Warrant shall not have been exercised shall also be issued to Holder within such time.

2.5 *Automatic Exercise.* To the extent this Warrant is not previously exercised, and if the fair market value of one share of the Company's Common Stock is greater than the Warrant Price, as adjusted, this Warrant shall be deemed automatically exercised in accordance with section 2.2 hereof (even if not surrendered) immediately before its expiration. For purposes of such automatic exercise, the fair market value of one share of the Company's Common Stock upon such expiration shall be the fair market value determined pursuant to Section 2.3 above. To the extent this Warrant or any portion thereof is deemed automatically exercised pursuant to this Section 2.5, the Company agrees to notify Holder within a reasonable period of time of the number of shares of the Company's Common Stock, if any, Holder is to receive by reason of such automatic exercise.

2.6 *Stock Fully Paid; Reservation of Shares.* The Company covenants and agrees that all Common Stock which may be issued upon the exercise of the rights represented by this Warrant will, upon issuance, be fully paid and nonassessable and free from all taxes, liens and charges with respect to the issue thereof (excluding taxes based on the income of Holder). The Company further covenants and agrees that during the period within which the rights represented by this Warrant may be exercised, the Company will at all times have authorized and reserved for issuance a sufficient number of shares of its Common Stock as would be required upon the full exercise of the rights represented by this Warrant.

2.7 *Fractional Shares.* No fractional share of Common Stock will be issued in connection with any exercise hereof, but in lieu of a fractional share upon complete exercise hereof, Holder may purchase a whole share at the then effective Warrant Price.

ARTICLE III. CERTAIN ADJUSTMENTS OF NUMBER OF SHARES PURCHASABLE AND WARRANT PRICE

The number and kind of securities purchasable upon the exercise of this Warrant and the Warrant Price shall be subject to adjustment from time to time upon the happening of certain events, as follows:

3.1 *Reclassification, Consolidation or Merger.* In case of: (i) any reclassification or change of outstanding securities issuable upon exercise of this Warrant; (ii) any consolidation or merger of the Company with or into another corporation (other than a merger with another corporation in which the Company is a continuing corporation and

which does not result in any reclassification, change or exchange of outstanding securities issuable upon exercise of this Warrant); or (iii) any sale or transfer to another corporation of all, or substantially all, of the property of the Company, then, and in each such event, the Company or such successor or purchasing corporation, as the case may be, shall execute a new Warrant which will provide that Holder shall have the right to exercise such new Warrant and purchase upon such exercise, in lieu of each share of Common Stock theretofore issuable upon exercise of this Warrant, the kind and amount of securities, money and property receivable upon such reclassification, change, consolidation, merger, sale or transfer by a holder of one share of Common Stock issuable upon exercise of this Warrant had this Warrant been exercised immediately prior to such reclassification, change, consolidation, merger, sale or transfer. Such new Warrant shall provide for adjustments which shall be as nearly equivalent as may be practicable to the adjustments provided in this Section 3 and the provisions of this Section 3.1, shall similarly apply to successive reclassifications, changes, consolidations, mergers, sales and transfers.

3.2 *Subdivision or Combination of Shares.* If the Company shall at any time while this Warrant remains outstanding and unexercised in whole or in part: (i) divide its Common Stock, the Warrant Price shall be proportionately reduced; or (ii) combine shares of its Common Stock, the Warrant Price shall be proportionately increased.

3.3 *Adjustment for Issue or Sale of Shares at Less Than the Warrant Price.* If, in a transaction other than an issuance excepted from these provisions as set forth below or an issuance that causes an adjustment under Sections 3.1 or 3.2, the Company shall at any time or from time to time, issue any additional shares of Common Stock without consideration or for a net consideration per share less than the Warrant Price in effect immediately prior to such issuance, then, and in each case, the Warrant Price shall be lowered to an amount equal to the lowest per share price received, or deemed received, by the Company as consideration for such Shares.

For purposes of this Section 3.3:

(i) There shall be no adjustment under this Section 3.3 for any sales or issuances: (a) in a transaction in which an adjustment will be made pursuant to Section 3.1 or 3.2; (b) of any shares of Common Stock or Common Stock Equivalents issued pursuant to any equity incentive plan approved by the Company's shareholders and Board of Directors; or (c) upon exercise or conversion of Common Stock Equivalents outstanding on the original date of issuance of this Warrant;

(ii) The issuance of Common Stock Equivalents shall be deemed an issuance at such time of the shares of Common Stock underlying the Common Stock Equivalents. If the Effective Price shall be less than the Warrant Price at the time of such issuance, then an adjustment in the Warrant Price shall be made upon each such issuance in the manner provided in this Section 3.3. No adjustment of the Warrant Price shall be made under this Section 3.3 upon the issuance of shares of Common Stock upon the exercise or conversion of Common Stock Equivalents if an adjustment has previously been made as above provided. Any adjustment of the Warrant Price shall be disregarded, if, as and when such Common Stock Equivalents expire or are cancelled without being exercised so that the Warrant Price effective immediately upon such cancellation or expiration shall be equal to the Warrant Price in effect at the time of the issuance of the expired or cancelled Common Stock Equivalents, with such additional adjustments as would have been made to the Warrant Price had the expired or cancelled Common Stock Equivalents not been issued.

3.4 *Other Action Affecting Common Stock.* If the Company takes any action affecting its Common Stock after the date hereof (including dividends and distributions), other

than an action described in any of Sections 3.1 and 3.2 hereof, which would have a material effect upon Holder's rights hereunder, the Warrant Price shall be adjusted downward in such manner and at such time as the Board of Directors of the Company shall in good faith determine to be equitable under the circumstances.

3.5 *Time of Adjustments to the Warrant Price.* All adjustments to the Warrant Price and the number of shares purchasable hereunder, unless otherwise specified herein, shall be effective as of the earlier of:

(i) the date of issue (or date of sale, if earlier) of the security causing the adjustment;

(ii) the effective date of a division or combination of shares;

(iii) the record date of any action of holders of the Company's capital stock of any class taken for the purpose of dividing or combining shares or entitling shareholders to receive a distribution or dividends.

3.6 *Notice of Adjustments.* In each case of an adjustment in the Warrant Price and the number of shares purchasable hereunder, the Company, at its expense, shall cause the Treasurer of the Company to compute such adjustment and prepare a certificate setting forth such adjustment and showing in detail the facts upon which such adjustment is based. The Company shall promptly mail a copy of each such certificate to Holder pursuant to Section 7.9 hereof.

3.7 *Duration of Adjusted Warrant Price.* Following each adjustment of the Warrant Price, such adjusted Warrant Price shall remain in effect until a further adjustment of the Warrant Price.

3.8 *Adjustment of Number of Shares.* Upon each adjustment of the Warrant Price pursuant to this Section 3, the number of shares of Common Stock purchasable hereunder shall be adjusted to the nearest whole share, to the number obtained by dividing the Aggregate Price by the Warrant Price as adjusted.

ARTICLE IV. TRANSFER, EXCHANGE AND LOSS

4.1 *Transfer.* This Warrant is transferable on the books of the Company at its principal office by the registered Holder hereof upon surrender of this Warrant properly endorsed, subject to compliance with federal and state securities laws. The Company shall issue and deliver to the transferee a new Warrant or Warrants representing the Warrants so transferred. Upon any partial transfer, the Company will issue and deliver to Holder a new Warrant or Warrants with respect to the Warrants not so transferred.

4.2 *Securities Laws.* Upon any issuance of shares of Common Stock upon exercise of this Warrant, it shall be the Company's responsibility to comply with the requirements of: (1) the 1933 Securities Act; (2) the Securities Exchange Act of 1934, as amended; (3) any applicable listing requirements of any national securities exchange; (4) any state securities regulation or "Blue Sky" laws; and (5) requirements under any other law or regulation applicable to the issuance or transfer of such shares. If required by the Company, in connection with each issuance of shares of Common Stock upon exercise of this Warrant, the Holder will give: (i) assurances in writing, satisfactory to the Company, that such shares are not being purchased with a view to the distribution thereof in violation of applicable laws, (ii) sufficient information, in writing, to enable the Company to rely on exemptions from the registration or qualification requirements of applicable laws, if available, with respect to such exercise, and (iii) its cooperation to the Company in connection with such compliance.

4.3 *Exchange.* This Warrant is exchangeable at the principal office of the Company for Warrants to purchase the same Aggregate Price purchasable hereunder, each new Warrant to represent the right to purchase such Aggregate Price as Holder shall designate at the time of such exchange. Each new Warrant shall be identical in form and content to this Warrant, except for appropriate changes in the number of shares of Common Stock covered thereby, the Aggregate Price of such shares, the percentage stated in Section 4.1 above, and any other changes which are necessary in order to prevent the Warrant exchange from changing the respective rights and obligations of the Company and the Holder as they existed immediately prior to such exchange.

4.4 *Loss or Mutilation.* Upon receipt by the Company of evidence satisfactory to it of the ownership of, and the loss, theft, destruction or mutilation of, this Warrant and (in the case of loss, theft, or destruction) of indemnity satisfactory to it, and (in the case of mutilation) upon surrender and cancellation hereof, the Company will execute and deliver in lieu hereof a new Warrant.

ARTICLE V. HOLDER RIGHTS

5.1 *No Shareholder Rights Until Exercise.* No Holder hereof, solely by virtue hereof, shall be entitled to any rights as a shareholder of the Company. Holder shall have all rights of a shareholder with respect to securities purchased upon exercise hereof at the time of cash or net issue exercise pursuant to Sections 2.1 and 2.2 hereof, or at the time of automatic exercise hereof (even if not surrendered) pursuant to Section 2.5 hereof.

ARTICLE VI. REGISTRATION RIGHTS

6.1 *Company Registration.*

(a) *Notice of Registration.* If the Company shall determine to register any of its securities either for its own account or the account of a security holder or holders, other than a registration relating solely to employee benefit plans, or a registration relating solely to a Rule 145 transaction, or a registration on any registration form which does not permit secondary sales, the Company will:

(i) promptly give to each Holder written notice thereof (which shall include a list of the jurisdiction in which the Company intends to attempt to qualify such securities under the applicable Blue Sky or other state securities laws); and

(ii) include in such registration (and any related qualification under Blue Sky laws or other compliance), and in any underwriting involved therein, all shares of Common Stock held by any Holder and specified in a written request or requests, made by any Holder within *[number]* days after receipt of the written notice from the Company described in clause (i) above, subject to any limitations on the number of shares as set forth in Section 9.1(b) below.

(b) *Underwriting.* If the registration of which the Company gives notice is for a registered public offering involving an underwriting, the Company shall so advise each Holder as part of the written notice given pursuant to Section 6.1(a)(i). In such event, the right of any Holder to registration pursuant to Section 6.1 shall be conditioned upon such Holder's participation in such underwriting and the inclusion of such Holder's shares of Common Stock in the underwriting to the extent provided herein. All Holders proposing to distribute their shares of Common Stock through such underwriting shall (together with the Company, directors and officers and the other shareholders distributing their securities through such underwriting) enter into an underwriting agreement in customary form with the underwriter or underwriters selected for underwriting by the Company.

Notwithstanding any other provision of this Section 6.1, if the underwriter determines that marketing factors require a limitation on the number of shares to be underwritten, the underwriter may (subject to the allocation priority set forth below) exclude from such registration and underwriting some or all of the shares which would otherwise be underwritten pursuant hereto. The Company shall so advise all Holders requesting registration, and the number of shares of Common Stock that are entitled to be included in the registration and underwriting shall be allocated in the following manner. The number of shares that may be included in the registration and underwriting on behalf of such Holders, directors and officers and other shareholders shall be allocated among such Holders, directors and officers and other shareholders in proportion, as nearly as practicable, to the respective amounts of securities which they had requested to be included in such registration at the time of filing the registration statement.

If any Holder or any officer, director or other shareholder disapproves of the terms of any such underwriting, he may elect to withdraw therefrom by written notice to the Company and the underwriter. Any securities excluded or withdrawn from such underwriting shall be withdrawn from such registration.

6.2 *Registration Rights.* In the event that the Company grants registration rights, including demand registration rights, to any other holder of securities of the Company, the Company will promptly give to the Holder written notice thereof and, if in the opinion of the Holder such registration rights are more favorable than the registration rights provided under this Warrant, the Holder shall so notify the Company within *[number]* days of receipt of the foregoing notice from the Company, whereupon such registration rights shall automatically be deemed to be incorporated in this Warrant.

6.3 *Expenses of Registration.* The Company shall bear all registration expenses incurred in connection with any registration, qualification and compliance by the Company pursuant to Section 6.1 hereof. All selling expenses shall be borne by the holders of the securities so registered pro rata on the basis of the number of their shares so registered.

6.4 *Registration Procedures.* In the case of each registration effected by the Company pursuant to this Article VI, the Company will keep each Holder advised in writing as to the initiation of each registration and as to the completion thereof. The Company will, at its expense:

(a) keep such registration effective for a period of *[number]* days or until the Holder or Holders have completed the distribution described in the registration statement relating thereto, whichever first occurs;

(b) furnish such number of prospectuses and other documents incident thereto as a Holder from time to time may reasonably request; and

(c) use its best efforts to register or qualify the Holder's shares of Common Stock under the securities laws or Blue Sky laws of such jurisdiction as any Holder may request; provided, however, that the Company shall not be obligated to register or qualify such shares in any particular jurisdiction in which the Company would be required to execute a general consent to service of process in order to effect such registration, qualification or compliance, unless the Company is already subject to service in such jurisdiction and except as may be required by the 1933 Securities Act or applicable rules or regulations thereunder.

6.5 *Indemnification.*

(a) The Company, with respect to each registration, qualification and compliance effected pursuant to this Article VI, will indemnify and hold harmless each Holder, each Holder's officer, director, partner, and agent, and each party controlling such Holder, and each underwriter, if any, and each party who controls any underwriter, against all claims, losses, damages and liabilities (or actions in respect thereof) arising out of or based on any untrue statement (or alleged untrue statement) of a material fact contained in any prospectus, offering circular or other document (including any related registration statement, notification or the like) incident to any such registration, qualification or compliance, or based on any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, or any violation by the Company of the 1933 Securities Act or any rule or regulation thereunder applicable to the Company and relating to action or inaction required of the Company in connection with any such registration, qualification or compliance, and will reimburse each such Holder, each Holder's officer, director, partner, and agent, and each party controlling such Holder, each such underwriter and each party who controls any such underwriter, if any, for any legal and any other expenses incurred in connection with investigating or defending any such claim, loss, damage, liability or action, provided that the Company will not be liable in any such case to the extent that any such claim, loss, damage, liability or expense arises out of or is based on any untrue statement or omission based solely upon written information furnished to the Company by such Holder or underwriter, as the case may be, and stated to be specifically for use in any prospectus, offering circular or other document (including any related registration statement, notification or the like) incident to any such registration, qualification or compliance.

(b) Each Holder will, if shares of Common Stock held by such Holder are included in the securities as to which such registration, qualification or compliance is being effected, indemnify and hold harmless the Company, each of its directors and officers and each underwriter, if any, of the Company's securities covered by such a registration statement, each party who controls the Company or such underwriter, each other Holder and other shareholders and each of their respective officers, directors, partners, and agents, and each party controlling such other Holder or other shareholders, against all claims, losses, damages and liabilities (or actions in respect thereof) arising out of or based on any untrue statement (or alleged untrue statement) of a material fact contained in any such registration statement, prospectus, offering circular or other document, or any omission (or alleged omission) to state therein a material fact required to be stated therein or necessary to make the statements therein not misleading, and will reimburse the Company and such Holders, other shareholders, directors, officers, partners, agents, parties, underwriters or control persons for any legal or any other expenses reasonably incurred in connection with investigating or defending any such claim, loss, damage, liability or action, in each case to the extent, but only to the extent, that such untrue statement (or alleged untrue statement) or omission (or alleged omission) is made in such registration statement, prospectus, offering circular or other document solely in reliance upon and in conformity with written information furnished to the Company by such Holder and stated to be specifically for use in any prospectus, offering circular or other document (including any related registration statement, notification or the like) incident to any such registration, qualification or compliance; provided, however, that the obligations of such Holders hereunder shall be limited to an amount equal to the proceeds to each such Holder or other shareholder of securities sold as contemplated herein.

(c) Each party entitled to indemnification under this Section 6.5 (the "Indemnified Party") shall give notice to the party required to provide indemnification (the "Indemnifying Party") promptly after such Indemnified Party has actual knowledge of any claim as to which indemnity may be sought, and shall permit the

Indemnifying Party to assume the defense of any such claim or any litigation resulting therefrom, provided that counsel for the Indemnifying Party, who shall conduct the defense of such claim or any litigation resulting therefrom, shall be approved by the Indemnified Party (whose approval shall not unreasonably be withheld), and the Indemnified Party may participate in such defense at such party's expense (unless the Indemnified Party shall have been advised by counsel that actual or potential differing interests or defenses exist or may exist between the Indemnifying Party and the Indemnified Party, in which case such expense shall be paid by the Indemnifying Party), and provided further that the failure of any Indemnified Party to give notice as provided herein shall not relieve the Indemnifying Party of its obligations under this Article VI. No Indemnifying Party, in the defense of any such claim or litigation, shall, except with the consent of each Indemnified Party, consent to entry of any judgment or enter into any settlement which does not include as an unconditional term thereof the giving by the claimant or plaintiff to such Indemnified Party of a release from all liability in respect to such claim or litigation. Each Indemnified Party shall provide such information as may be reasonably requested by an Indemnifying Party in order to enable such Indemnifying Party to defend a claim as to which indemnity is sought.

6.6 *Information by Holder*. Each Holder shall furnish to the Company such information regarding such Holder as the Company may reasonably request in writing and as shall be reasonably required in connection with any registration, qualification or compliance referred to in this Article VI.

6.7 *Rule 144 Reporting.* With a view to making available the benefits of certain rules and regulations of the Securities and Exchange Commission (the "Commission") which may permit the sale of the registrable securities to the public without registration, the Company agrees to:

(a) Make and keep public information available, as those terms are understood and defined in Rule 144 under the 1933 Securities Act, at all times from and after ninety (90) days following the effective date of the first registration under the 1933 Securities Act filed by the Company for an offering of its securities to the general public;

(b) File with the Commission in a timely manner all reports and other documents required of the Company under the 1933 Securities Act and the Securities Exchange Act of 1934, as amended (the "Exchange Act") at any time after it has become subject to such reporting requirements; and

(c) So long as the Holder owns any shares of Common Stock, furnish to the Holder forthwith upon request a written statement by the Company as to its compliance with the reporting requirements of Rule 144 (at any time from and after *[number]* days following the effective date of the first registration statement in connection with an offering of its securities to the general public), and of the 1933 Securities Act and the Exchange Act (at any time after it has become subject to such reporting requirements), a copy of the most recent annual or quarterly report of the Company, and such other reports and documents so filed as the Holder may reasonably request in availing itself of any rule or regulation of the Commission allowing the Holder to sell any such securities without registration.

ARTICLE VII. MISCELLANEOUS

7.1 *Additional Covenants by the Company*. The Company further covenants and agrees that it will:

(a) Give each Holder prompt written notice of any intended changes to the composition of its capital structure, whether by issuance of new securities or otherwise;

(b) Give each Holder written notice of any shareholders' meeting and will allow a representative of each Holder to attend such meetings;

(c) Give each Holder *[number]* days' prior written notice of any action that the Company intends to take by shareholders' written consent;

(d) Allow, upon reasonable notice and at reasonable times, the inspection of its minute book and other corporate records by a representative of the Holder;

(e) Not engage, other than on arm's-length terms, in any transaction with any of its shareholders or affiliates (as such term is defined under Rule 144 issued by the Securities and Exchange Commission under the 1933 Securities Act, as amended);

(f) Provide Holder, within *[number]* days after the end of the first, second and third quarterly accounting periods in each fiscal year of the Company, quarterly financial statements reflecting its operations for the quarter, and within *[number]* days following the end of each fiscal year, consolidated financial statements for the fiscal year; and

(g) Keep its properties insured in terms reasonably acceptable to Holder.

7.2 *Governmental Approvals.* The Company will from time to time take all action which may be necessary to obtain and keep effective any and all permits, consents and approvals of governmental agencies and authorities and securities acts filings under federal and state laws, which may be or become requisite in connection with the issuance, sale, and delivery of this Warrant, and the issuance, sale and delivery of the shares of Common Stock or other securities or property issuable or deliverable upon exercise of this Warrant.

7.3 *Governing Laws.* It is the intention of the parties hereto that except as set forth below, the internal laws of *[state]* (irrespective of its choice of law principles) shall govern the validity of this warrant, the construction of its terms, and the interpretation and enforcement of the rights and duties of the parties hereto. Notwithstanding the foregoing, if the Company is organized under the laws of a state other than *[state]*, the corporation laws of that state shall govern the procedural and substantive matters pertaining to the due authorization, issuance, delivery and exercise of this Warrant and the shares of Common Stock upon exercise hereof. Except as set forth below, the parties hereby agree that any suit to enforce any provision of this Warrant arising out of or based upon this Warrant or the business relationship between any of the parties hereto shall be brought in the federal district courts located in *[state]* or the courts of such State. Each party hereby agrees that such courts shall have personal jurisdiction and venue with respect to such party, and each party hereby submits to the personal jurisdiction and venue of such courts. In addition to the foregoing jurisdiction, Holder, at its sole option, may commence any such suit in any jurisdiction in which the Company has a business office or is incorporated.

7.4 *Binding Upon Successors and Assigns.* Subject to, and unless otherwise provided in, this Warrant, each and all of the covenants, terms provisions, and agreements contained herein shall be binding upon, and inure to the benefit of the permitted successors, executors, heirs, representatives, administrators and assigns of the parties hereto.

7.5 *Severability.* If any one or more provisions of this Warrant, or the application thereof, shall for any reason and to any extent be invalid or unenforceable, the remainder of this Warrant and the application of such provisions to other persons or circumstances shall be interpreted so as best to reasonably effect the intent of the parties hereto. The parties further agree to replace any such void or unenforceable provisions of this Warrant with valid and enforceable provisions which will achieve, to the extent possible, the economic, business and other purposes of the void or unenforceable provisions.

7.6 *Default, Amendment and Waivers.* This Warrant may be amended upon the written consent of the Company and the Holder. The waiver by a party of any breach hereof for default in payment of any amount due hereunder or default in the performance hereof shall not be deemed to constitute a waiver of any other default or any succeeding breach or default. The failure to cure any breach of any term of this Warrant within *[number]* days of written notice thereof shall constitute an event of default under this Warrant. Upon such event of default, the Warrant Price shall be reduced by one-half and thereafter shall continue to be reduced by one-half from the then adjusted Warrant Price for each successive *[number]*-day period in which such breach is not cured.

7.7 *No Waiver.* The failure of any party to enforce any of the provisions hereof shall not be construed to be a waiver of the right of such party thereafter to enforce such provisions.

7.8 *Attorneys' Fees.* Should suit be brought to enforce or interpret any part of this Warrant, the prevailing party shall be entitled to recover, as an element of the costs of suit and not as damages, reasonable attorneys' fees to be fixed by the court (including, without limitation, costs, expenses and fees on any appeal). The prevailing party shall be the party entitled to recover its costs of suit, regardless of whether such suit proceeds to final judgment. A party not entitled to recover its costs shall not be entitled to recover attorneys' fees. No sum for attorneys' fees shall be counted in calculating the amount of a judgment for purposes of determining if a party is entitled to recover costs or attorneys' fees.

7.9 *Notices.* Whenever any party hereto desires or is required to give any notice, demand, or request with respect to this Warrant, each such communication shall be in writing and shall be effective only if it is delivered by personal service or mailed, United States certified mail, postage prepaid, return receipt requested, addressed to such party at its address stated at the beginning of this Warrant or to such other address as such party may designate by written notice delivered hereunder. Such communication shall be effective when they are received by the addressee thereof; but if sent by certified mail in the manner set forth above, they shall be effective *[number]* business days after being deposited in the United States mail. Any party may change its address for such communications by giving notice thereof to the other party in conformity with this Section.

7.10 *Time.* Time is of the essence of this Warrant.

7.11 *Construction of Agreement.* This Warrant has been negotiated by the respective parties hereto and their attorneys and the language hereof shall not be construed for or against any party.

7.12 *No Endorsement.* Holder understands that no federal or state securities administrator has made any finding or determination relating to the fairness of investment in the Company or purchase of the Common Stock hereunder and that no federal or state securities administrator has recommended or endorsed the offering of securities by the Company hereunder.

7.13 *Pronouns.* All pronouns and any variations thereof shall be deemed to refer to the masculine, feminine or neuter, singular or plural, as the identity of the person, persons, entity or entities may require.

7.14 *Further Assurances.* Each party agrees to cooperate fully with the other parties and to execute such further instruments, documents and agreements and to give such further written assurances, as may be reasonably requested by any other party to better evidence and reflect the transactions described herein and contemplated hereby, and to carry into effect the intents and purposes of this Warrant.

[name of issuing corporation]

By: *[name and title of signatory]*

[signature]

Topic Six:

Intellectual Property Issues of the Start Up Venture (Materials online only)

Topic Seven:

Representing the Web-Based Venture in New York

Representing the Web-Based Venture in New York

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Legal Disclaimers

- Views expressed in this program are Cliff Ennico's own, and do not reflect the views of NYSBA, its subsidiaries and affiliates.
- Legal and tax information presented in this program SHOULD NOT be relied upon as legal or tax advice, which can only be given by a lawyer, accountant or other professional licensed to practice in your state.

PART I

SETTING UP THE WEB-BASED BUSINESS

The Legal Environment of the Web-Based Business

- Patent, Trademark, Copyright, and Trade Secrets Law
- Sales Law (UCC Article 2) and Electronic Contracts
- Advertising and Marketing Law [anti-spam]
- Defamation and Unfair Competition
- Privacy Law
- Tax Law
- International Law [EEC privacy regulations]
- Cybercrime
- eBay, Amazon, etsy User's Agreements, rules and regulations

Role of Counsel to the Web-Based Business

- Trademarking Website URL
- Drafting Web Contracts [in “clickwrap” format] for client’s website
- Drafting and negotiating agreements with third parties “offline”
- [Maybe] fending off third-party claims for trademark/copyright infringement
- Dealing with Internet tax issues

Trademarking Client’s URL

- Is your client’s name or URL trademarkable?
  - Cannot be “descriptive”
  - Best names are:
    - Words unrelated to the business
    - Made-up words
    - An unexpected combination of words
- Client’s URL must not infringe another person’s registered trademark
- Grab all available domain name extensions (.com, .net, .org, .biz, .us, .co, .info)

Drafting Web Contracts [Part I]

- Six Basic Documents:
  - The User's Agreement or TOS ("Terms of Service")
  - The Privacy Policy
  - The Copyright and Permissions Policy [if there is original content on the website]*
  - The Refunds and Cancellation Policy*
  - The Blog/Social Media Policy*
  - Sweepstakes/Contest Rules and Regulations

* -- may be included in client's TOS but "best practice" is that they be standalone documents

Drafting Web Contracts [Part 2]

- Must review User's Agreement and Privacy Policies of:
- All platforms where client is selling online
  - eBay, Amazon, etsy, Apple iTunes, Google Store
- All social media websites where client is advertising/promoting its business
  - Facebook, Twitter, etc.
- Consider a "traffic cop" provision in client's TOS saying which governs in the event of conflict

Drafting the User's Agreement or "Terms of Service" (TOS)

- Content depends on what client is doing
- Don't be afraid of "legalese"
- Okay to look at TOS' of comparable sites
- Make sure it covers client's website, related sites and mobile phone "apps"
- Make sure user "accepts" TOS when registering or logging onto website
  - Use "scroll" feature where "I Agree" button is activated only when user scrolls through TOS

Recommended Provisions in TOS

- Payment terms
- Shipping/fulfillment terms
- Return and cancellation policy
- Credit card chargeback policy
- Warranty disclaimers
- Limitation of liability
- Modification of TOS
  - Can't do it unilaterally anymore
  - Best practice: send e-mail to customers with link to revised/amended TOS

Drafting the Privacy Policy

- "Privacy" vs. "Data Use"
- Must set forth:
  - Types of information collected
  - Whether is "personally identifiable" or "statistical aggregate" information
  - How you will use/share that information
  - Specific language regarding use of "cookies"
  - References to California statutes protecting privacy
- DON'T BE OVERLY RESTRICTIVE!
- Include Child Online Privacy Protection Act of 1998 (COPPA) language if children under age 13 can access the website/purchase goods
  - Include parental consent form and mailing or e-mail address

Drafting the Copyright and Permissions Policy

- Copyright notice should appear as "footer" at bottom of each website page (not just home page)
- Should contain assignment of third-party content and permission to use "without restriction or limitation"
- Digital Millennium Copyright Act (DMCA) of 1998
  - Provides safe harbor if specific "takedown" language is included in Policy
  - Copyright owner must send complaint to specific e-mail address (usually, copyright@[nameofwebsite].com)
  - Website forwards complaint to alleged infringer – if no answer received within X days, client must agree to take down infringing content
  - Best practice: include language allowing client to take down infringing content "at any time in client's sole discretion"

Drafting the "Returns and Cancellation Policy"

- Review eBay and Amazon requirements
- Generally, should permit returns within X days of confirmed receipt
  - In original packaging, and
  - For exchange rather than refund unless inventory is depleted
- Client may refuse refund if returned merchandise nonconforming and/or damaged during return
- Client may prohibit credit card chargebacks where merchandise not returned

Drafting the "Blog/Social Media Policy"

- Section 230 of the Communications Decency Act of 1996 [47 U.S.C. § 230] shields Web businesses from liability for defamation, etc. arising from third party posts on social media
- Still, "best practice" is to include language saying client will remove content that:
  - Is "unlawful, fraudulent, threatening, abusive, libelous, defamatory, indecent, obscene, disparaging, hateful, confidential, spam, pornographic or otherwise objectionable";
  - Is used for commercial, advertising or sales activities not authorized by the client;
  - Contains material, nonpublic information about any person or entity without proper authorization; or
  - In client's sole discretion, harms the client or any other person or entity in any way.

Drafting Sweepstakes and Contest Regulations

- Unlawful Internet Gambling Enforcement Act of 2006, 18 U.S.C. §§ 1831 et seq.
- State antilottery laws -- distinguish between “games of chance” and “games of skill”
- Keep prizes small (see Fla. Stat. Ann. § 849.094]
- “Void where prohibited by law”
- “No purchase necessary” (see Calif. Bus. & Prof. Code § 17539.15)

PART II

GROWING AND SELLING THE WEB-BASED BUSINESS

Agreements with Vendors and Other Third Parties

- Confidentiality and Nondisclosure Agreement
- Exclusive Online Distributor Agreement (EODA) with local manufacturer or other source of exclusive inventory
- "Private Label" merchandising agreement
- Copyright license with content providers
- Employee policies re social media use

Fending Off Copyright/Trademark Infringement Claims

- The "first sale" doctrine in trademark and copyright law
- The growth of "retail arbitrage" online
- *Kirtsaeng v. John Wiley & Sons, Inc.*,133 S.Ct. 1351 (2013)
- Increasing efforts by manufacturers to enforce "no wholesale transaction" clauses in their retail agreements

Buying/Selling the Web-Based Business

- Include ALL of seller's URLs (incl. domain name extensions)
- Transferring e-mail accounts
- Consider "escrowing" domain names with escrow.com
- Is the seller operating other (unrelated) websites?
  - If so may need a "buyer noncompete"

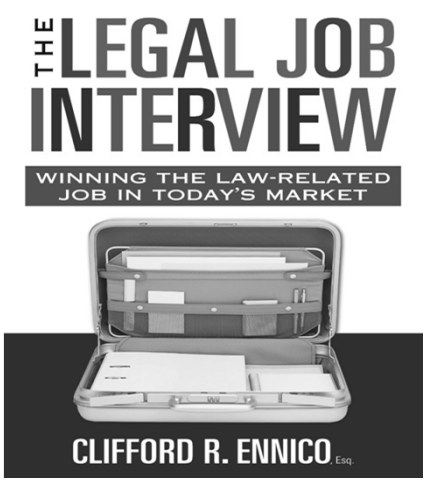
Tax Issues of the Web-Based Venture

- Client MUST register for NYS sales tax [Form DTF-17], and
- Charge and collect sales tax on in-state transactions
- EVEN if selling solely on eBay and Amazon!
- Client may have "nexus" in other states if inventory is stored, shipped and/or fulfilled from there
- Most states have "Amazon" taxes – apply if client:
  - "directly targets" in-state residents (e.g. by advertising on in-state websites or targeting e-mail "blitzes" to state residents); AND
  - sells above a certain threshold into the state (usually $10,000 to $20,000 in annual sales volume)
- South Dakota v. Wayfair, 585 U.S. ___ 2018
  - Your client may have sales tax liability in State X if it sells more than $Y in merchandise to residents and/or engages in Z transactions with residents within a 12-month period
  - A very useful web page: www.avalara.com/us/en/learn/nexus/find_your_nexus.html

Suggestions for Further Reading

- "Forms for Small Business Entities" by Cliff Ennico (ThomsonWest, west.Thomson.com)
- "Advising eBusinesses" by Cliff Ennico (ThomsonWest, west.Thomson.com)
- "Advising Small Businesses" by Cliff Ennico (ThomsonWest, west.Thomson.com)
- "The eBay Seller's Tax and Legal Answer Book" by Cliff Ennico (AMACOM, www.amanet.org)

Thank You!



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FORM OF EXCLUSIVE AGREEMENT TO RESELL MANUFACTURER'S MERCHANDISE ON AMAZON.COM

[date]

[name and address of [manufacturer]

RE: *Reseller Agreement*

Dear Mr./Ms. _____:

Per our telephone conversations and e-mail exchanges over the past few days, this agreement ("Agreement") sets out the terms and conditions under which [name of reseller] ("Reseller") will resell your products listed on the attached Exhibit "A" (the "Products") on Amazon.com and its affiliated websites worldwide.

We hereby agree as follows:

1. Exclusive Appointment to Sell on Amazon. You hereby appoint Reseller as an independent distributor and reseller of the Products, and Reseller hereby accepts such appointment, subject to the terms and conditions of this Agreement. Such appointment shall be exclusive as to the wholesale or retail sale of the Products on Amazon.com and its affiliated websites worldwide (collectively, "Amazon"), and shall otherwise be non-exclusive. As long as this Agreement is in effect, you will not cause or permit anyone other than Reseller to market, distribute, sell, advertise or promote the Products anywhere on Amazon. In the event Reseller becomes aware that a person or company other than Reseller is selling Products on Amazon while this Agreement is in effect, Reseller will promptly notify you and you will either (a) refuse to sell Products to such person or company or (b) pay to Reseller twenty-five percent (25%) of all gross revenue you have realized from Product sales by such person or company, as liquidated damages for breach of this Agreement as not as a penalty.

2. Term; Termination. Reseller's appointment will commence on the date of this Agreement and will continue for a period of one (1) year thereafter. During the initial term this Agreement can be terminated by either party only upon a material breach by the other party which has not been cured within thirty (30) days after written notice of same. After the expiration of such one (1) year period, this Agreement shall be automatically renewed for successive periods of one (1) year each, but may be terminated by either party for any reason or no reason upon at least one hundred and eighty (180) days' prior written notice to the other party. If you should terminate this Agreement other than by reason of Reseller's material breach of this Agreement, either (a) Reseller's appointment to sell Products on Amazon shall become nonexclusive and Reseller shall continue to have the right to continue selling Products on Amazon and elsewhere, or (b) at your option upon written notice to Reseller, Reseller's authorization to sell Products shall terminate. In the event you terminate Reseller's authorization to sell Products, you will repurchase Reseller's existing inventory of Products for 125% of the purchase price paid by Reseller, and will pay a one-time branding fee to Reseller equal to ten percent (10%) of Reseller's gross sales of Products during the twelve (12) month period immediately preceding the effective date of termination.

3. Pricing. Reseller's prices for Products will be determined F.O.B. your warehouse based on your current distributor pricing list attached to this Agreement as Exhibit "B", subject to change upon thirty (30) days' prior written notice to Reseller. Reseller shall be entitled to purchase Products at a price or prices to be mutually agreed in writing from time to time. You will provide Reseller with suggested resale prices for the Products which shall be fair and reasonable having regard

to the marketing of each Product and Reseller's cost of doing business. Reseller in marketing the Products shall do its reasonable best to adhere to your resale pricing schedule. In the event you offer another distributor or reseller a lower price for any Product than that charged to Reseller, you will promptly notify Reseller of such lower price and Reseller thereafter shall have the right to purchase such Product at the lower price.

4. Payment and Returns. Purchase orders from Reseller for Products will be fulfilled within two (2) business days of receipt unless we mutually agree otherwise in writing. You will invoice Reseller for each shipment of Products and such invoices will be paid within thirty (30) days of receipt. You will honor returns of defective or damaged Products by providing replacement Products within two (2) business days of return, and will maintain a sufficient inventory of Products to honor all orders placed by Reseller on Amazon.

5. Product Warranties; Insurance. If you are the manufacturer of the Products, you warrant all Products according to your standard printed warranty. If you are not the manufacturer of the Products, you agree to pass on to Reseller the manufacturer's warranty for each Product to the fullest extent you are entitled to do so. Reseller will not make any warranties for any Product other than the manufacturer's printed warranty. If requested by Reseller at any time, you will provide Reseller with evidence of products liability insurance coverage for any Product in such amount and with such insurance carrier as shall be reasonably acceptable to Reseller, and will name Reseller as an additional insured under any such policy.

6. Trademarks and Logos. Reseller is permitted to use your trademarks, service marks, logos and trade names for each Product as long as this Agreement is in effect, subject to your reasonable trademark usage and advertising policies. You will make such changes to a Product's packaging, labeling and appearance (for example, the affixing of a Universal Product Code or UPC to same) as Reseller may reasonably request to facilitate resale on Amazon or comply with Amazon's rules, regulations and seller policies.

7. Disclaimer. Reseller will use commercially reasonable efforts to resell the Products in strict accordance with this Agreement and with a high degree of care, skill, diligence, professional knowledge, judgment, and expertise according to sound work practices and accepted professional and industry standards, in a well-managed, organized, and efficient manner. There can be no guarantee that you will be satisfied with the results of Reseller's performance, or that any particular results will be achieved by you, even if communicated to Reseller. If you are dissatisfied with Reseller's performance under this Agreement, your sole remedy is to terminate this Agreement in accordance with the provisions hereof. The warranty provided above is the exclusive warranty given by Reseller and supersedes any prior, contrary or additional representations, whether oral or written. THIS WARRANTY IS IN LIEU OF ALL OTHER WARRANTIES, EXPRESS OR IMPLIED, INCLUDING WITHOUT LIMITATION, THE IMPLIED WARRANTIES OF MERCHANTABILITY AND FITNESS FOR A PARTICULAR PURPOSE.

8. Limitation of Liability. Neither party shall be liable to the other party for any special, indirect, incidental or consequential damages including, with out limitation, damages for lost profits, or costs of procurement of substitute goods or services, arising out of his Agreement. Except as otherwise specifically set forth herein, Reseller's total liability to you under or in connection to this Agreement shall not exceed the amounts paid or payable to Reseller hereunder during the three (3) immediately preceding calendar months or $100, whichever is greater; provided however, that the foregoing limitation of liability shall not apply to the willful misconduct of Reseller. Any action against Reseller arising out of, resulting from, or related to the performance or breach of this Agreement shall be filed not later than three (3) months after the cause of action has accrued.

9. Assignment. Reseller may not assign, in any manner, its right, obligation, or interest in or under this Agreement without your prior written consent, except for assignments by operation of law due to corporate reorganization.

10. Governing Law. The validity, interpretation, and performance of this Agreement shall be controlled by and construed under the laws of the State of [state where reseller is located], as if performed wholly within that state and without giving effect to its conflict of laws principles, if any term, provision, covenant or condition of this Agreement is held invalid or unenforceable for any reason, the remaining provisions shall continue in full force and effect as if the Agreement had been executed with the invalid portion eliminated, so long as the Agreement continues to express, without material change, the original intentions of the parties. The parties further agree that any action, claim or proceeding under this Agreement shall be commenced exclusively in the federal courts of the United States of America or the courts of the State of [state where reseller is located] located in the City of [city where reseller is located]. The parties expressly waive any objection they may have to the exclusive jurisdiction and venue of such courts.

11. Relationship of Parties. Reseller is an independent contractor under this Agreement. Nothing contained in this Agreement is intended or is to be construed so as to constitute the parties as partners or joint venturers, nor is either party the employee or agent of the other, nor are the employees or agents of either party employees or agents of the other party. Neither party hereto shall have any express or implied right or authority to assume or create any obligations on behalf of or in the name of the other party or to bind the other party to any other contract, agreement or undertaking with any third party.

12. General. This instrument contains the entire agreement between the parties hereto and supersedes all prior oral or written agreements with respect to the subject matter hereof. This Agreement may not be amended, modified or changed verbally but only by a written instrument signed by the authorized representatives of both parties. The waiver by either party of a breach of any provision contained herein shall be in writing and shall in no way be construed as a waiver of any succeeding breach of such provision or the waiver of the provision itself. This Agreement may be executed in several counterparts, each of which shall constitute a separate original but all of which together shall constitute one and the same instrument. Section headings in this Agreement are solely for convenience and shall not be considered in its interpretation.

Please indicate your agreement to the foregoing terms and conditions by signing this Agreement in the space provided below.

[Name of Reseller]

By: _____

Print Name and Title:

ACCEPTED AND AGREED TO:

[Name of Manufacturer]

By: _____

Print Name and Title:

EXHIBIT “A”

PRODUCTS REPRESENTED BY RESELLER

The following products manufactured and sold by [name of manufacturer], including but not limited to any line extensions thereof released by [name of manufacturer] during the term of this Agreement, together with any other products mutually agreed by the parties in writing or by e-mail exchange during the term of this Agreement:

[list of manufacturer’s products to be represented by reseller]

EXHIBIT “B”

PRICING LIST

[attach manufacturer’s current distributor pricing list]

1. SALE OF ASSETS.

(a) The Buyer agrees to purchase and the Seller agrees to sell, transfer, convey and assign to Buyer, free of all liabilities and obligations except as otherwise agreed herein, all of the business assets used in the conduct of the Business and the Websites (the "Assets"), including but not limited to (i) such right, title and interest Seller may have to the Websites' domain names and URLs listed on Schedule 1(a) attached hereto (the "URLs"), (ii) any and all content on the Websites (including the images posted thereon except for certain images licensed from Google Images as listed on Schedule 1(c), any and all accounts and contracts between Seller and third parties (including but not limited to accounts and contracts with vendors, advertisers and content providers) relating to the Business or the Websites more particularly described in Schedule 1(a) attached hereto (the "Assumed Contracts"), (iii) the use of the trade name "_____", (iv) the goodwill of the Business as a going concern, (v) the Websites' advertiser, customer and vendor lists, (vi) any and all business records relating to the Business, and all other business assets of any kind or nature whatsoever, whether tangible or intangible, as the Seller or any of his affiliates owns and used by the Seller in the Business. The Assets do not include, and the Buyer shall not purchase the "Excluded Items" set forth in Section 1(b) hereof. The Assets shall include, but shall not be limited to:

(i) any and all equipment, merchandise, inventory, supplies, and proprietary software used in the Business;

(ii) the Website URLs, telephone and fax numbers, hosting accounts for all of the Website URLs, addresses and password information for all hosting accounts, servers and e-mail accounts directly tied to the Websites, all Website content, text, artwork, graphics and computer code (or, in the case of "Third Party Software" described in Section 5(b) of this Agreement, such right and license as the Seller has to use the same) comprising the Websites, all of Seller's rights under hosting and domain name registration agreements for the Website URLs and any other Assumed Contracts, any and all social media accounts for the Websites on Facebook, Twitter, Pinterest, Instagram, and any other social media platforms, all newsletters and blogs pertaining to the Websites or the Business, all vendor and customer lists and databases relating to the present and former suppliers, clients and customers of the Business, employee lists, files, papers, books, records, sales and advertising materials and records, and sales and purchase correspondence, affecting or pertaining to the Business, the Websites, or the Website URLs;

(iii) any and all prepaid expenses of the Business, customer advances and deposits existing on the Closing Date; and

(iv) any and all permits, licenses, consents or other authorizations for the conduct of the Business, to the extent the same may be assigned under applicable law.

The Website URLs shall be placed into escrow in the manner and for such period of time as is set forth in Section 3(d)(vi) of this Agreement.

(b) Buyer acknowledges that the Assets do not include cash on hand, bank deposits, accounts receivable, any real property, such items of personal property (if any) as shall be set forth in a list and mutually agreed to by Seller and Buyer in writing on or prior to the Closing, and any and all debts, liabilities and obligations of any nature whatsoever, or any assets of any business or website owned or operated by the Seller other than the Business, the Websites and the Website URLs (collectively, "Excluded Items"). Seller shall be solely responsible for collecting any and all accounts receivable accruing prior to the Closing Date (as hereinafter defined).

(c) Except for the Assumed Contracts, Buyer shall assume no liabilities or other obligations, commercial or otherwise, of the Seller, known or unknown, fixed or contingent, choate or inchoate, liquidated or unliquidated, secured or unsecured, or otherwise, regardless of when the same may arise or may have arisen, including but not limited to all of Seller's accounts payable accruing on or before the Closing Date (the "Retained Liabilities").

CALIFORNIA PROVISIONS FOR WEBSITE PRIVACY POLICY

For California Users

- The California Civil Code requires a business with whom a California resident has an established business relationship to disclose to such residents, upon their request: (1) the types of personal information the business shares with third parties for the third party's marketing purposes, and (2) the identities of the third parties with whom the business has shared this information during the immediately preceding calendar year.
- If you are a California resident, and would like to make such a request, please submit your request via email to PRIVACY@_____.COM.

Faculty Biographies

In Alphabetical Order

Maureen Crush, Esq.
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Maureen Crush heads the corporate and commercial practice group of the firm and practices primarily general corporate and business transaction law, and trusts and estates. She also has extensive not-for-profit corporate law experience providing advice to her clients throughout the Hudson Valley on governance, compliance, formation, mergers and affiliations.

Ms. Crush worked for four years at the accounting firm of KPMG. She then began her legal practice at a boutique New York City Wall Street firm where for seven years she concentrated on corporate law, commercial transactions, commercial and institutional financing and trusts & estates law. Maureen's clients cover a wide variety of businesses including technology companies, manufacturers (large and small), professional practices (physicians, nurse practitioners, physical therapists and accountants), minority and women owned businesses (MWBE), not-for-profit social service agencies, charities, museums, and religious and social benefit organizations. She counsels her clients on negotiation and drafting of complex mergers and acquisitions, transaction structuring, due diligence and corporate governance, employment issues, contracts, leases, loans and financings, shareholder and member operating agreements, business succession planning and the admission/termination of partners. She also frequently provides estate and succession planning services for the key employees and owners of her business clients.

Ms. Crush is a frequent lecturer on corporate and not-for-profit law issues for the New York State Bar Association, National Business Institute and many local bar associations and organizations.

Areas of Practice:
Business and Corporate Law
Not-for-profit and Tax Exempt Organization Law
Partnership Law (including LLCs and LPs)
Health Care/Medical Services Delivery Law
Banking, Finance & Secured Transactions

Wills, Trusts & Estates, Business Succession Planning

Bar Admissions:
New York State
Supreme Court of the United States

Education:
J.D. Fordham University School of Law
B.S. Accounting New York University

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John has over 26 years of CPA, CFO, CEO and entrepreneur experience serving early stage and fast growth companies under 30 million dollars. He is a graduate of Binghamton University and an alumnus of the Entrepreneurial Services Group of the New York office of Ernst and Young, LLP. He is the founder of a national on-line and three state retail wine businesses which he sold in 2006. He has CFO and CEO experience in fast growth private and public companies including Comstock Images, MCY.com, Select Wines, Small Business Television Network and others. John has authored numerous business plans, raised several million in growth capital and is the trusted financial and CPA advisor to successful entrepreneurs in several states and three countries.

John is an active Certified Public Accountant licensed in New York and Florida and has passed Series 6, 63 and 65 Securities license exams

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Since 1996, Cliff Ennico has worked as a "general counsel" or "Wall Street lawyer" to hundreds of small businesses, entrepreneurs, franchise owners, self-employed professionals, not-for-profit entities, and other business clients throughout the northeastern United States. He graduated magna cum laude from Dartmouth College in 1975, and got his law degree from Vanderbilt University School of Law in 1980, where he was Articles Editor of the Vanderbilt Law Review.

During the 1980s, Cliff worked for a succession of law firms in New York City, where he specialized in corporate finance, venture capital and securities law. After a brief stint during the early 1990s as in-house counsel for General Electric Capital Corp., Cliff worked as a corporate/business lawyer for two Connecticut law firms before launching my own practice in 1996.

Cliff is admitted to practice law in New York and Connecticut, and am in good standing in both states. Cliff focuses on representing entrepreneurs, small business owners and self-employed professionals.

In addition to being a lawyer, Cliff also is:

- The author of several law books for West Group, a leading U.S. legal publisher, including a best-selling collection of legal forms called Forms for Small Business Entities.
- The author of Succeeding in Your Business™, a weekly business advice column that appears in dozens of newspapers nationwide as well as www.entrepreneur.com and other business-oriented Web sites.
- The former host of MoneyHunt, the popular PBS television show about entrepreneurs;
- An instructor for eBay University, where I advise entrepreneurs nationwide on legal and tax implications of buying and selling goods on eBay, the nation's leading internet auction site.

- The author of Small Business Survival Guide, a collection of useful tricks for dealing with the 12 biggest enemies you will face when you run your own business.
- The author of The eBay Seller's Tax and Legal Answer Book, the best - and ONLY - comprehensive guide to the legal and tax rules that apply when you're selling on eBay, the world's leading auction marketplace.
- A frequent contributor to Entrepreneur and other small business magazines, websites and blogs.
- A leading authority on entrepreneurship and small business management, giving talks to business groups nationwide.

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Teige P. Sheehan is a patent attorney with particular expertise in biotechnology, neuroscience, and pharmaceuticals, and experience in related areas such as medical devices and nanotechnology. His work includes drafting and prosecuting patent applications and managing global patent portfolios, providing patentability, validity, and freedom-to-operate opinions, and performing due diligence analyses, as well as litigation, post-grant proceedings, and appeals. He also provides analogous services related to trademark protection.

Teige received a Presidential Scholarship from Boston College, where he received his Bachelor's degree, was named Scholar of the College, and was awarded membership in Phi Beta Kappa, and continued his studies there to receive his doctoral degree. As a postdoctoral fellow at the Yale University School of Medicine, he subsequently studied intracellular signaling mechanisms, regulation of genome expression, and morphological aspects of neural plasticity responsible for the adaptations seen following chronic exposure to stress, antidepressant drugs, and drugs of abuse. Thereafter, Teige was an assistant professor at Brown University, directing a research laboratory where he continued such work. He authored numerous peer-reviewed research papers, review articles, and book chapters throughout his career as a research scientist, a rich background that enables him to combine scientific awareness with considerable legal expertise in advancing clients' interests.

Teige enjoys Irish folk music and plays the saxophone. His favorite movie would be the Big Lebowski.