Be proactive

Four common mistakes in business that won't cost you much to avoid

INTERVIEWED BY MARK SCOTT

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Realizing it'd be a setback if a key employee who drives a lot of revenue to your business walked out the door, you offer a minority share in the company to show how much you value what this person does.

Six months later, a great opportunity arises with a competitor and the employee decides to take it. You must come up with an amicable solution to the ownership issue, but that's not your only concern. It turns out you didn't have the employee sign a non-compete agreement, so he is free to immediately take his talents and client connections to one of your biggest competitors.

The decision to sell shares in your business or to not get a non-compete agreement on file are two mistakes that Todd C. Baumgartner, a partner at Brouse McDowell, sees business owners make over and over again.

"For a few thousand dollars or less of legal work, these mistakes, which can cost a company hundreds of thousands of dollars, can usually be avoided," says Baumgartner.

Smart Business spoke with Baumgartner about four of the most common mistakes businesses make and what you can do to avoid them.

Mistake No. 1: Not having non-compete agreements for key employees.

Star performers bring revenue to your business. Depending on the depth of your sales team, they can be responsible for a sizable percentage of the overall money that your company brings in each year. A non-compete agreement protects you by formalizing what happens if the employee decides to leave.

The process is not expensive and requires just a few hours with your legal team to make sure you've covered all the bases. You may get some grumbling from an employee who has a strong position from which to negotiate. But even if it's only for six months or a year, it's worth it to get the agreement.

Mistake No. 2: Not separating key assets in a corporate structure.

Let's say you have a manufacturing company sitting on a piece of land worth $500,000. You find out the Environmental Protection Agency has issued a $2 million finding on the land. If you have the real estate and the operating company separated, the environmental liability won't impact the business. You may lose the real estate, but you can keep all your equipment and keep the business operating.

Conversely, if you have a separate operating company and there is an accident in your manufacturing facility, a creditor won't be able to go after the real estate because it's a separate company. The limited liability company (LLC) is a useful tool to split out your real estate and it's something that can be done fairly seamlessly.

Mistake No. 3: Bringing in key employees as minority shareholders.

Once you take this step, you can no longer terminate the employee without a legitimate business reason, even if their contract says they are employed on an at-will basis. Complications also arise if you want to reorganize the company.

If this employee works in one part of the company that you want to split off, there is potential liability if you move money between the divisions because you're moving it away from a minority shareholder.

If the employee decides to leave and you're not publicly traded, there could also be a dispute about how much the individual share is worth.

A profit sharing program, a stock appreciation rights plan or phantom stock are few options that help you avoid these problems.

Mistake No. 4: Not protecting intellectual property.

Companies will develop software and not get any type of patents on it. There are patent trolls out there just looking for ideas that don't have intellectual property (IP) protection. Talk to an IP attorney to go through your inventory.

People don't value IP the way that they should. For some companies, IP is their whole business.

It's advisable to protect everything, especially for companies looking to make a liquidity event or exit strategy. A potential buyer is going to come in and look to see what is and what is not protected. ●