

Getting Down to Business: Things to Consider



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Introduction

There are many issues to consider when setting up a business. This article provides an overview of some of the legal requirements and issues that should be dealt with prior to starting your business venture. This list of issues is not exhaustive; however, it will provide enough information to help a potential business operator ask the right questions.

Corporate Structure

There are three common types of business structures: sole proprietorship, partnership, and corporation. People often ask which business model is the best, but the answer will vary depending on your needs, resources, and intentions.

Sole Proprietorship

Setting up a sole proprietorship has both advantages and disadvantages. It is the simplest way to set up a business, and the start-up costs are low. However, the sole proprietor is personally responsible for all debts and obligations related to the business. In other words, the sole proprietor bears unlimited liability.

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Partnership

A partnership is the relationship that exists between two or more persons carrying on a business in common with a view to profit. As with any relationship, partners should consider putting together some form of partnership agreement in the event of a disagreement or dissolution of a partnership. The partnership model has its advantages, such as the relative ease in putting it together, low start-up costs, and limited regulations. The disadvantages of a partnership include, but are not limited to, the fact that partners have unlimited liability and a partner may bind the other partners to a legal agreement, for example, without their approval or knowledge.

Corporation

A corporation, also known as a limited company, is a legal body which is separate and distinct from its shareholders. The relevant provincial legislation for corporations incorporated in Alberta is the *Business Corporations Act*. Some corporations are incorporated at the federal level; however, this article will focus on Alberta incorporated corporations.

Incorporating has many advantages, such as limiting the shareholders' personal liability in any legal dispute. For example, if a creditor had a claim against the company, the creditor would normally have no rights against the shareholders. As well, incorporating allows for income splitting and other possible tax advantages.

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However, as with any business model, there are disadvantages. Incorporating is costly to pursue, it has extensive record requirements such as the preparation of a minute book and corporate resolutions, and in some limited instances, shareholders may still be held personally liable.

Most lawyers are asked to assist an owner-operated company where all the shareholders are actively involved in the day-to-day operations. The corporation must decide how many shareholders will be in the business, determine the various classes of shares, and decide how involved the shareholders will be in the business' day-to-day operations. Consideration must be given to setting up the management of the business such as the election of directors and the appointment of officers. Who will be the directors, the president, and the secretary? Will there be an opportunity for new shareholders to buy into the business?

If a business operator chooses to incorporate, it is essential that the shareholders develop a method by which to define their relationship and determine how to resolve disputes. The agreement between the shareholders is usually called the Unanimous Shareholders' Agreement (USA). Spending time drafting a USA and anticipating contentious issues will enable the corporation to focus on its day-to-day operations

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as opposed to spending time and expense resolving disputes and other issues between shareholders. Notwithstanding a USA, issues will undoubtedly crop up and litigation may ensue. However, an agreement between the shareholders will reduce the likelihood of costly litigation

for a business. A dispute resolution mechanism is an important component of any USA and should identify a forum for resolving disputes such as mediation, arbitration, or court process.

A well-drafted agreement will greatly help to ensure the long term success of the shareholder relationship, thereby contributing to the long-term success of the business.

Any agreement should also address the issue of how to buy one shareholder out from the company through the use of some form of buy/sell provision or “shotgun clause”. Under a shotgun clause, a shareholder (*offeror*) would be permitted to offer his/her shares for sale (*offer price*) to the other shareholders (*offerees*) and those shareholders (*offerees*) would have the opportunity to purchase the shares at the offer price or to sell their shares to the shareholder (*offeror*) at the same offer price. The benefit is that the parties would be forced to accept a fair price for the shares because the person offering to sell the shares to the other shareholders does not know whether or not his/her offer would be accepted.

In addition, shareholders should consider including non-competition and confidentiality provisions in the USA to restrict any departing shareholder from getting involved in the same type of business with a competitor or starting a similar type of business.

Finally, as with all agreements, the parties should include a provision that sets out the manner in which the agreement may be terminated.

Employment

Any business operator must recognize the importance of minimizing claims from current and former employees. The most common issue relating to employment matters is the wrongful dismissal action.

In the absence of a written employment contract, every employment relationship is governed by an unwritten employment contract with terms that are implied by law. Those implied terms include all minimum standards as set out in the *Employment Standards Code* of Alberta, as well as reasonable notice provisions found at common law. Employers are free to draft their own employment contracts provided the terms meet or exceed the minimum requirements set out in the *Employment Standards Code* of Alberta. Business operators may want to consider entering into written agreements with their

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management employees and taking the time to ensure that all employees understand their responsibilities.

The law allows an employer to terminate any employee at any time – with or without cause. Any employee terminated without cause must be given reasonable notice or payment in lieu of notice. It is important that business operators consider the reasonable notice periods and understand that if they fail to provide reasonable notice, the business may expose itself to a legal action. What is reasonable notice depends on the particular facts relating to the employee's history of employment.

If an employee is terminated with cause, there is no need to provide reasonable notice or make any payment in lieu of notice. However, keep in mind that the threshold for terminating an employee with cause is high. A business operator must have written documentation to establish that the employee was properly terminated.

All small business operators must recognize that there are a number of employment law issues that will arise from time to time. It is important to manage their employees' performance and to seek legal assistance when issues arise.

Contracts

Regardless of what type of business is being operated, there will be the need to enter into contracts with third parties. Generally, a contract is formed when there is an offer and acceptance, consideration, an intention on the part of the parties to form an agreement, and an understanding of the terms such as price and subject matter of the agreement. It

is important to identify the names of the parties on the written contract so that there is no doubt as to who the contracting parties are. Any contract should also address remedies upon breach, and if the business is based in

Alberta, the contract should indicate that Alberta laws govern.

Business operators should take the time to review any contract before signing it and ask for assistance where necessary. Once they have signed an agreement, they are deemed to have read the agreement even though they may later claim that they did not read or understand it. Although there are exceptions to the rule, it would be prudent on the part of business operators to read every paragraph in any contract before signing it. If they do not understand a particular clause, they should ask their lawyer or ask the other party to make changes to the wording so that it is clearer to both parties. The signing of contracts ought not to be taken lightly.

Prior to entering into any binding offer to lease or other lease commitment, it is essential to take the time to review the zoning of the property to ensure that the intended type of business can in fact operate on that property.

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Leases

With the exception of home-based businesses, most businesses need to have a place to operate. Often, these places of business are located in buildings owned by a third party. A signed lease agreement between the owner of the building (landlord) and the business operator (tenant) will be required.

Commercial leases generally favour the landlord. There are several types of leases that a landlord may present to a business operator. Most leases provide a landlord with a net return. A landlord may attempt to shift other costs, such as utilities, common area costs, and HVAC (heating, ventilation, air-conditioning), to the tenant. A business operator should seek legal assistance prior to signing the lease agreement.

Some of the things to consider when reviewing a commercial lease are:

- the net rent;
- the duration of the agreement;
- any additional rent or costs;
- the tenant's responsibilities under the lease agreement such as hours of operation and repairs;
- the landlord's responsibilities under the lease agreement;
- whether there are any competition restrictions in the building;
- parking and access issues;
- how to deal with a default under the lease agreement (i.e., arbitration, mediation, or court process);
- a renewal option clause; and
- the ability of the tenant to assign or sublease, and whether or not consultation and approval of the landlord is required.

Some landlords may provide a tenant with free rent for a certain period to allow the tenant to set up its business operations. If the lease agreement does not provide for this, a tenant may request this opportunity.

It is also useful to consider and review the provisions in the lease agreement that deal with the sale, demolition, or redevelopment of the building by the landlord. Some lease agreements allow a landlord to terminate a long-term lease with six months' notice if the landlord decides to demolish or redevelop the building. This may put a business operator's investment at risk.

Business operators should consult a lawyer prior to signing any commercial lease agreement to avoid expensive roadblocks in the future.

Municipal Regulations

Most municipalities in Alberta have established business regulations and fees for businesses. Accordingly, most businesses will require a business licence in order to operate legally within the municipality. If a business operates without a business licence, most municipalities have the authority to impose fines. An owner may also be required to pay a fee ranging from \$150 to as much as \$3000 to the municipality depending upon the nature of the business. Business licence fees can range from about \$150 to as much as \$3000.

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In addition to a business licence, a development permit may be required from the municipality. Prior to entering into any lease commitment, it is essential to take the time to review the zoning of the property to ensure that the intended type of business can operate on that property. Even if the proposed use is permitted, it may require additional parking spaces, costly building code compliance, and safety upgrades. As part of the due diligence process, it is important to take the time to review the applicable zoning provisions and building code requirements for the proposed leased premises.

An offer to lease should be conditional, not only on the proposed use being permitted, but also on the proposed plans receiving at least tentative, preferably final, approval from municipal officials. Without the appropriate prior due diligence, a tenant could find its proposed use prohibited under applicable zoning bylaws, or find the cost of complying with applicable codes and other requirements extremely costly. Again, retaining a lawyer to assist in securing the appropriate zoning at this stage can reduce costs, uncertainties, and headaches later on.

Conclusion

Although the concept of starting a business sounds simple at first, it can be challenging in many ways. It requires a great deal of time, effort, and planning on the part of the business operator. To move forward with your business idea, take the time to retain the services of a lawyer, accountant, and other professionals to assist you with your business venture.

Corporate lawyers are trained to look at business plans, anticipate potential problem areas, and help business operators to successfully navigate around them. The money spent on legal counsel early on will go a long way in ensuring the long-term success of a business.

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