

# **Legal Guide to Small Business**

Written and Presented by

**The Masters of Business Administration Graduate Students**

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**with the support and encouragement of the**

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and

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# Table of Contents

## Introduction

1. Legal Concerns at Startup.....	3
Legal Forms of Doing Business	
Permits and Licensing	
Taxes	
Insurance	
Leases	
2. Buying an Existing Business.....	11
Finding a Business for Sale	
Gathering Information about a Business	
Valuing the Business	
Bulk Transfer	
Covenant Not to Compete	
Assessing the Business' External Environment	
The Sales Agreement	
3. Hiring Employees.....	18
Job Descriptions, Advertisements, and Applications	
Interviews	
Background Checks	
Wages and Overtime	
4. Employee Termination.....	25
Wrongful Termination	
Contract Employment Issues	
The Firing Process	
Layoffs versus Firing	
References	
Post-Termination Issues	
5. The Regulatory Environment.....	32
Worker's Compensation	
OSHA	
ADA	

## Introduction

The [Masters of Business Administration](#) graduate students at Humboldt State University, School of Business, for the Spring 2003 semester created this manual to provide local small business owners a guide to legal topics relevant to their business formation and operation. The topics selected are a compilation from the knowledge acquired in our class with the guidance of Professor Ben Allen and from previous curricula learned in the graduate program.

Our desire is to benefit your business and to help you understand basic business legal issues. Please note that this manual is designed as a general overview of many legal issues that should be considered. Therefore, this manual should not be used in lieu of legal advice; thus, professional consultation is recommended when you deem necessary.

We, the following MBA students at Humboldt State University, wish to you and your employees a healthy, happy and balanced business environment that generates fruitful income and assets for your local community business.

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# 1. Legal Concerns at Startup

## **Legal Forms of Doing Business**

When you start or operate a small business, you will likely be doing so as either a sole proprietor, partner, member in a limited liability company (LLC), or as a shareholder of a corporation. If you fail to comply with appropriate laws regarding formation, you will be either a sole proprietor (if one owner) or a partner (if more than one owner). Following appropriate legal requirements means that you can change that status to a corporation or to an LLC. Many factors drive the decision on which form of business is best for you including limiting liability of your personal assets for business losses, costs of formation, and, very importantly, income taxation of net revenues.

Small businesses should use caution when operating as a sole proprietorship or a partnership because of a concept known as “unlimited liability” which allows the creditors of the business to seize personal as well as business assets. Additionally, you can be liable personally for all of the actions of your partners within the scope of a business.

Formation of an LLC or a corporation is more complex and potentially more costly than a sole proprietorship or partnership. However, the small businessperson should balance the risk of not adopting one of these forms of doing business with the costs of formation. It is reasonably possible for you to comply with the legal requirements without the assistance of an attorney. We recommend that you review publications such as Legal Guide for Starting and Running a Small Business, (Steingold, 6<sup>th</sup> Edition; NOLO Press) to assist you in making a decision on which form of business is best for you and whether or not to retain the services of an attorney.

## **Permits and Licensing**

The following section outlines several licensing and permit requirements that small businesses can incur.

### **Federal Permits and Licensing**

- ❑ **Employer Identification Number:** Every business, except a sole proprietorship, is required to apply for this identification number. Sole proprietors may use their social security number but it is highly recommended to obtain this identification number. Form SS-4 is used to do this and can be found at [www.irs.gov/](http://www.irs.gov/).
- ❑ **Incorporation:** This filing is only if you are intending to incorporate your small business. Check the IRS website for the correct form: [www.irs.gov/](http://www.irs.gov/).

### **State Permits and Licensing**

- ❑ **Occupations and Professions:** Some of the occupations that require licensing are the lawyers, doctors, psychiatrists, building contractors, nurses’, etc. Depending on the state where business is conducted, other occupations such as private investigators, barbers, cosmetologists, etc. may require licensing. [www.ss.ca.gov/business.com](http://www.ss.ca.gov/business.com).
- ❑ **Product Licensing:** Businesses that sell alcohol, tobacco, firearms, food, gasoline and lottery tickets require special permits to do so. [www.calgold.ca.gov](http://www.calgold.ca.gov)

### Local Permits and Licensing

- ❑ **Business License:** Most businesses will require a business license. Applications for a license may be obtained from the local City Hall for incorporated areas or from the County Tax Collector's office for unincorporated areas. For help with specific cities in the Humboldt/Del Norte area, contact NCSBDC's BizNet at <http://www.northcoastsbdc.org/biz>
- ❑ **Crowd Control:** The fire department and the building and safety department must be consulted to meet all requirements regarding crowds, safety features and permits.
- ❑ **Building Codes:** Permits are required to alter, modify or remodel buildings and shops. Consult the building and safety department for laws and permits and consult a licensed contractor for advice. Also obtain a copy of the uniform building code.
- ❑ **Zoning:** Zoning regulations may involve the type of business, environmental issues, construction issues, and local political issues. Compliance with all zoning laws, including parking requirements, is essential. These laws apply to home-based businesses and can be explored in more depth in the book, Legal Guide for Starting and Running a Small Business. Steingold, F., 6<sup>th</sup> edition. 2001. Nolo Press, Berkeley, California or at [www.nolo.com](http://www.nolo.com).
- ❑ **Health:** Health permits can be obtained at the county level and are essential for operating a food-oriented business. An outline of all the permits one needs for starting a restaurant can be obtained at [www.cagold.ca.gov](http://www.cagold.ca.gov)

### Fictitious Business Name Statement

If a business name does not contain the owner's surname or includes words additional to the owner's name, a fictitious business name statement must be filed with the County Clerk. After filing, the statement must be published in a court-approved newspaper 4 times and Proof of Publication provided to the County Clerk. A business owner needs to refile and publish the statement every 5 years. <http://www.northcoastsbdc.org/biz>

### Environmental Issues

There are environmental laws, permits, and licenses that often must be addressed before starting a small business.

- ❑ **Federal:** Chemical production and waste companies must contact the federal government to obtain permitting. Other businesses may require federal permits. [www.cagold.ca.gov](http://www.cagold.ca.gov)
- ❑ **State:** You may need permits for any the following activities: air emissions (ex. dry-cleaners), discharge of wastewater, and hazardous waste such as chemical storage and disposal. [www.cagold.ca.gov](http://www.cagold.ca.gov)
- ❑ **Regional and Local:** Locally, licenses and permits are required to operate a business that involves the preparation and or the sale of food. Receiving water from sources other than public water supply will require purity testing and possible permitting. These issues and numerous other possible health issues can be addressed through the health department. [www.cagold.ca.gov](http://www.cagold.ca.gov)

**Taxes**

The five basic types of taxes that the small business owner is subject to are: payroll, sales, property, personal business property, and income tax.

**Initial Filings: Tax Account Numbers**

As noted previously, taxpayer identification numbers should be acquired before the payment of taxes. The following forms should be filed to obtain these numbers:

- SS-4                      Federal: Application for Employer Identification Number  
[www.irs.gov/](http://www.irs.gov/)
- DE 1                      State: Registration Form for Employers [www.edd.ca.gov/](http://www.edd.ca.gov/)
- BOE 400-MIP            State Board of Equalization: Application for Seller’s Permit & Registration as a Retailer (Individuals/Partnerships)  
[www.boe.ca.gov/](http://www.boe.ca.gov/)
- W-9                      Federal: Request for Taxpayer Identification Number: to be completed by all hired independent contractors prior to the start of work and kept on file. [www.irs.gov/](http://www.irs.gov/)

**Payroll Taxes: Employees**

All employees are required to complete these forms:

- W-4                      Federal: Employee Withholding Allowance Certificate
- I-9                      Federal: Employee Eligibility Verification (Citizenship)
- DE 34                  State: Report of New Employees

**Payroll Tax Liability Payments**

These taxes must be paid if you have employees. The employer pays both their tax liability and the employee tax liability (deducted from the paycheck) to the government.

Form	Type	Tax	% Paid	Payer	Wage Limit	Frequency
941:	Federal	FICA	6.2	employer	\$87,000	quarterly
		FICA	6.2	employee	87,000	
		Medicare	1.45	employer	none	
		Medicare	1.45	employee	none	
		Withholding	varies	employee	none	
940	Federal	FUTA	0.008	employer	7,000	quarterly
DE6	State	PIT	varies	employee	none	quarterly (report only)
DE88:	State	UI	2-8%	employer	7,000	monthly
		ETT	0.001	employer	7,000	
		SDI	0.009	employee	56,916	
		PIT	varies	employee	none	
DE7	State					annual reconciliation

### **Federal Payroll Tax Deposits**

The amount of the company's annual tax liability determines if and how often deposits must be made for the Federal Form 941 taxes.

Form 8109 Federal Tax Deposit Coupon:  
annual tax > \$50,000 → semiweekly deposits  
annual tax < \$50,000 → monthly deposits  
quarterly ≤ \$ 2,500 → no deposits required

### **Annual Federal Reporting of Wages**

W-2 Wage & Tax Statement: to employee by 1/31  
W-3 Transmittal of Wage & Tax Statements: to federal gov't by 2/28 with W2 copies  
1099 Report of Independent Contractor Income: file if payment to contractor is \$600 or more (may be < \$600 for certain services) 1099-MISC most common form (14 types), to contractor by 1/31  
1096 Annual Summary & Transmittal of US Information: to federal government with 1099 copies by 2/28

To obtain more information:

Federal (IRS) (800) 829-4933 [www.irs.gov/](http://www.irs.gov/)  
State (EDD) (888) 745-3886 [www.edd.ca.gov/](http://www.edd.ca.gov/)

### **Sales & Use Tax (Resale tax)**

BOE-401-A2 Sales & Use Tax Return (7.25% tax)

Frequency of payments is dependent on the amount of the monthly tax liability:

\$0 – 100 → file annual  
\$101-300 → quarterly  
\$301-1200 → monthly  
\$1201+ → quarterly prepayments  
\$20,000+ → quarterly prepayments/EFT

Check the instruction booklet for tax exemptions (transactions not subject to resale tax).

Taxes are payable to the State Board of Equalization: (800) 400-7115. Information is available at [www.boe.ca.gov/](http://www.boe.ca.gov/).

### **Property Taxes**

Property taxes apply for any building or land you own (business or residence). The first installment must be paid by 12/10, and the second installment by 4/10. It is the property owner's responsibility to pay property taxes, even if they do not receive a bill. Contact the County Assessor's Office to obtain this information (445-7663).

### **Personal Business Property Taxes**

Form 571-L Business Property Statement is due 4/1.

Taxes paid on personal business property (all property excluding land, buildings, vehicles, inventory), includes all equipment and fixed items (shelves, etc). Tax rate is approximately 1% of assessed value. Value is depreciated (based on a system similar to

the federal depreciation system) down to a holding value (taxes paid as long as equipment is in use).

No application exists. Contact the County Assessor's Office (telephone 445-7564) if you do not receive the form.

### **Income Tax**

It can be beneficial to hire an accountant to compute your taxes if you do not have knowledge of income tax laws and preparation. Quarterly tax deposits (Form 1040ES) are required for most businesses. Sole Proprietorships and Partnerships are also subject to a 15.9% self-employment tax. Numerous Schedules must also be filed with the federal and state tax forms. For information contact:

Federal (Internal Revenue Service) (800) 829-4933

[www.irs.gov/](http://www.irs.gov/)

State (Franchise Tax Board) (800) 852-5711

[www.ftb.ca.gov/](http://www.ftb.ca.gov/)

### **Insurance**

A small business owner should carefully examine his or her business with an insurance agent to identify needs. When seeking an agent it is important to find one who listens to your needs and asks many questions. Furthermore it may behoove you to locate an agent who represents many different companies and is capable of giving you quotes from several insuring organizations. Insurance agents recommend reviewing your policies frequently and knowing exactly what is covered and what is not so you can align your business practices and policies with your insurance policies or visa versa.

### **Qualifying for a Policy**

Insurers typically rate businesses on the services they perform or products they sell, the riskier either of these are the less likely they will be to insure you and the more expensive the premiums will be. Furthermore, most insurance companies require experience in the field, sometimes upwards of three years. Often you can modify your business practices and discuss options with your agent to qualify for policies for which you may not otherwise qualify.

### **Property Coverage for the Property Owner**

- ❑ **Property:** Business owners can obtain Building and Personal Property Coverage. Make sure the building is listed in addition to anything you have added, such as fixtures (machinery, equipment, light poles), and any important surrounding property. Be specific.
- ❑ **Perils Covered:** Perils are essentially specific types of coverage and come in three forms: Basic, Broad, and Special. Basic gives a list of things that are covered (smoke, lightening, aircraft...). Broad simply expands on those in Basic. Special perils are different. They are constructed oppositely in that they cover everything except what is written in as exceptions, thus offer a wider coverage.
- ❑ **Amount of Coverage:** Insure only what you need: the buildings, fixtures etc. Yet insure these things with at least 80% coverage otherwise you become a co-insurer, at which you are financially liable for 50% of losses.

- ❑ **Replacement Cost vs. Current Value:** The replacement cost is how much it costs to replace what is insured; the current value is essentially how much it is worth as is. It is important to know which one you are insured for.
- ❑ **Ordinance or Law Coverage:** This applies when dealing with an older structure that does not meet the current building and/or health and safety codes. If insured with this coverage the insurance company will pay for the costs to meet the contemporary statutes in the event of a disaster.

### **Property Coverage for the Tenant**

Often commercial leases have provisions stating that you will insure the building and the landlord against liability suits based upon your actions. Even if there are no such provisions you may wish for coverage on any improvements you made to the premises. When signing a lease make sure there is a “mutual waiver of subrogation” in it. This will remove you personally from the disputes of your insurance company and your landlords in the event of ambiguous damage.

### **Liability Insurance**

This type of insurance covers your business in the event that you or your employees negligently failed to act reasonably and someone was injured or something was damaged. This insurance generally will not protect you from punitive damages (judgments given to you for intentionally engaging in malicious practices), nor will it cover the intentional assaults of employees to customers.

- ❑ **Products Liability:** This type of insurance covers you for any “product” you design, install, manufacture, and/or sell in the event that your “product” injures someone because of its design, safety, durability, or in adequate warning. Products refer to tangible things.
- ❑ **Vehicle Liability:** It is important to insure any vehicles your company uses, including rented, owned, or employee vehicles if used in the scope of employment.
- ❑ **Workers’ Compensation:** This insurance is mandatory if you have employees and is available through either a state run fund or private insuring companies and covers you if an employee is injured in the scope of employment. This subject is covered more thoroughly in section 5 page 32 of this booklet.

### **Other Insurance to Consider**

These types of coverage are called endorsements, and cover specific aspects of business typically exempt:

- ❑ **Employee dishonesty or theft:** This insurance covers you if your employees are stealing from you. This insurance is void if you or your partners are engaging in the thefts.
- ❑ **Crime insurance:** This insurance covers you from many forms of crime not associated with you or your employees such as theft or missing property.
- ❑ **Industry specific insurance:** This type of insurance usually comes in packages for specific types of businesses: manufacturing, retail, restaurant, service, etc, and usually is associated with discounts.

- ❑ **Valuable papers and records:** Covers any important business documents that are essential to business such as, clients accounting records if you are an accountant.
- ❑ **Property of others:** As the title implies, this insurance covers the property of others while in your care.

### **Tips for Reducing the Financial Burden of Insurance**

- ❑ Cover only what the state requires. Then look at your business practices to discover other likely and reasonable points of liability and insure accordingly.
- ❑ You can raise the deductibles on your insurance, which often provides significant cost reductions.
- ❑ Have excellent safety and risk reduction policies. The simple things often work the best. These can include: staging fire drills, installing smoke detectors and alarms, giving supplemental and annual training to employees.
- ❑ Quite possibly the best way to save money is to shop around.

### **The Commercial Lease**

When you begin the process of finding a space to lease, the first step you should take is analyzing your needs. For example:

- ❑ How great of a concern is location?
- ❑ How much space are you going to need?
- ❑ Do you want your own space?
- ❑ How much can you spend on rent?

Two common choices people make when looking for a space to rent are doing it themselves and hiring a real estate agent. It's possible to go out on your own and find a space that's going to fit your needs, but consider the amount of time and money that you are willing to spend on this course of action.

The job of a rental agent is to find you a space to rent, and they don't get paid until that happens. The best thing about hiring an agent is that you don't pay them, your new landlord does. Rental agents are linked to updated listings, which you can methodically search.

Before you sign the lease, it is important that you understand that you have the right to negotiate any and all of the following terms:

#### **Rent**

The following is a short explanation of the many different ways that rent is computed. Gross or Base rent is simply a flat fee. Net rent is when the tenant pays a monthly base rent plus some or all of the real estate taxes, depending on the proportion of the building the tenant is renting. Net-net rent goes further and requires the tenant to pay the base rent plus real estate taxes, plus the landlord's insurance on the space being occupied. Net-net-net (Triple Net) rent includes the base rent plus the landlords operating costs, including taxes, insurance, repairs and maintenance. Percentage rent is often when a business is located inside a shopping mall. In this situation, rent calculation involves base rent plus a percentage of gross income.

### **Usage**

This term binds you to a very specific use of your space, so pay careful attention.

### **Maintenance, Repairs & Alterations**

Leases usually absolve the landlord of all liability for any adverse impact on your business due to defective conditions. You can negotiate special provisions into this section that: (1) permit you to repair and deduct after reasonable advance oral or written notice, (2) make the landlord liable for any adverse impact on your business, and (3) expressly reduce rent for the period of time that the defective conditions remain, so the landlord is not encouraged to delay repairs. Also make sure you clearly state, within the lease, that you have the right to remove anything you install.

### **Assigning and Subletting**

Most leases read: "Tenant agrees not to assign or transfer this lease or sublet the premises or any part of the premises without the written consent of landlord". It's important that you fully understand what the terms of this part of the lease mean. In the future, you might realize that you don't need all of the space you have, and you decide to supplement your rent by subletting the extra space. In this case, you're still responsible for paying the entire rent to the landlord and honoring all of the provisions of the lease.

Another possibility is that you will want to move out of the space during the term of the lease, because you have found a better space or decided to go out of business. Assigning the lease to someone else allows you to do so. The new tenant pays the landlord directly and you have no further liability under the lease.

### **Landlord's Access**

Most leases grant the landlord a broad right to enter the premises. This has the potential to create a somewhat awkward relationship. If the landlord shows up whenever he or she deems it necessary, it will most likely feel like an intrusion into your privacy and more importantly it can disrupt business.

### **Lease Renewability**

This is one of the more critical points of the lease. The rent increase will most likely be more favorable to you, if you opt to renew the lease. Take into account the fact that you cannot predict what business will be like in the future. If business is good and you negotiated an option to renew, the option operates successfully for you. If you believe that there is something better out there, then you might want to let it ride and see what develops

You can obtain legal information in dealing with your commercial lease at the following websites:

- ❑ [www.nolo.com](http://www.nolo.com) Nolo Press puts out legal guides for just about everything.
- ❑ [www.tenantslegalcenter.com](http://www.tenantslegalcenter.com)
- ❑ [www.silver-freedman.com](http://www.silver-freedman.com) Professional Law Corporation

## 2. Buying an Existing Business

There are many reasons why purchasing an existing business may be appropriate. You are able to buy an established customer base and a viable product or service, and you can reduce the start-up costs with a possible immediate cash flow.

However, you will probably have to pay a price premium for a successful business and you may find it difficult to find a business that specifically suits your individual personality.

For more comprehensive information on purchasing a business, check [www.findlaw.com](http://www.findlaw.com), [www.businesslaw.gov](http://www.businesslaw.gov), or Nolo Press' authority on small business ownership, including purchasing or selling a small business, Legal Guide for Starting & Running a Small Business.

### **Finding a Business for Sale**

The following section outlines some pertinent issues to consider when looking for a business to buy.

#### **Narrowing down your search**

- ❑ Types of business: Analyzing what part of the supply chain you want to be in increases the efficiency of the buying process. Ask yourself: Do I want to work in retail, wholesale, or the service industry? Remember when you are deciding what type of business to buy that running a small business requires an immense amount of dedication and skill. As such, it is extremely advantageous to take your personal and professional strengths into consideration.

#### **Where to find businesses for sale**

- ❑ Buying from someone you already work for: this approach allows you to start up your business in an environment you are already comfortable and familiar with.
- ❑ Newspapers: regularly run advertisements on businesses for sale, though often times the best opportunities are absent.
- ❑ Small Business Network: Individuals and organizations that service small businesses (Bankers, Accountants, Lawyers, Insurance Agents, Trade Associations etc.) have an inherent knowledge of who is in the market to sell and may alert you to potential businesses early on.
- ❑ Broker: Most experts suggest avoiding brokers because they are paid commission on sale. As a result, often times your interests may not be among their highest priorities.

### **Gathering Information about a Business**

- ❑ **Why is the owner selling the business?** Ask the owner questions that may lead to underlying issues as to why he/she is selling the business. Check with business associates and people involved in the business to see if they know any reason the owner might be selling the business.

- ❑ **Who owns the business?** If there are multiple owners be sure that they are all selling their stake in the business, and that by the end of the sale everyone agrees to the terms established.
- ❑ **Physical conditions of the business.** The owner of the business should permit you entrance on to the property to inspect all assets. These assets combined with the goodwill of the business will determine your price for the business, so look carefully.
- ❑ **Financial condition of the business.** The financial condition of the business can be found in the bank records, tax returns, sales records, and certification by state and/or federal agencies from the last three to five years. It is important to look three to five years back to get a realistic picture of what the business really takes in. It is relatively easy to inflate sales and decrease cost for one or two years. You might also have a reputable CPA firm do an audit of the financial condition of the business.
- ❑ **A confidentiality agreement** will likely be needed at this time. This document indicates that you won't use the information about the seller's business for any purpose other than making the decision to buy.
- ❑ **Employee contracts and benefits.** Be certain to examine and determine liability on their existing contracts.
- ❑ **Retaining the previous owner.** Although it is not a requirement for the previous owner to continue employment for a specified amount of time when changing owners, it maybe a good idea to ensure that the process goes smoothly. To ensure that the previous owner upholds this part of the agreement the payment should be held in escrow until the services have been completed.

### **Other important documents that should be looked into include:**

- ❑ **Customer lists:** Depending on the nature of the business, it may be questionable as to whether the previous customers will transfer when you buy the business. Try to determine this.
- ❑ **Supplier/ purchaser contracts, warranties and guarantees:** Try to be sure that all contracts, warranties and guarantees have been completed. When buying a sole proprietorship, it is not usually a requirement for you to uphold these contracts. However, to keep the goodwill of the business it is a good idea to honor them. Be sure that all suppliers and purchasers are willing to negotiate new contracts with you.
- ❑ **Organization and list of employees:** Check with the employees to see if they are willing to stay on when you take over the business.
- ❑ **Payroll, benefits and employee pension/profit sharing info:** Again, these are contracts that the employees will probably expect you to uphold. If you are going to retain existing employees, be sure that you are willing to continue these contracts.

### **Valuing the Business**

The determination of value is pivotal to a successful purchase. When valuing a business it is helpful to break the value into its component parts.

### **Tangible Assets**

- ❑ **Fixed Assets:** Furniture, fixtures, and equipment. Establish what type of return each asset will provide the purchaser. Additionally, determining the life expectancy of equipment then depreciating from original price will assist in gaining an appropriate value.
- ❑ **Non-fixed tangible assets:** It is entirely likely, and probably desirable, that during the transfer of the business the seller will still have a substantial inventory. It is important to determine whether inventory will be purchased at retail, wholesale, or some discounted cost.

### **Intangible Assets**

- ❑ **Goodwill:** Generally considered the reputation or loyalty of customers to the business. Essential questions to ask yourself should be: "Will goodwill remain when I take over or is goodwill associated with the present owner rather than the business?" One approach used for assigning value to goodwill is through the use of a multiplier (the number by which earnings must be multiplied to determine the value of the business). Many industries (construction, accounting, for example) have standard multipliers that appraisers use. However, you should be especially critical of multipliers since last years earnings may not be accurate indicators of future earnings.
- ❑ **Trade Name:** The name of the business to be purchased. It is likely that you will want to purchase the trade name if you are paying for goodwill.
- ❑ **Customer Lists:** You need to establish whether or not the esteem, if any, will be transferable to you and your new business in determining what degree of value you want to assign to customer lists.

### **Outstanding Liabilities**

- ❑ **Liabilities to the government:** Generally taking the form of taxes owed to municipal, state, or federal agencies back taxes should always be considered when valuing a business as they can, if not handled correctly, end up being the responsibility of the new owner. (Handling government and creditor liabilities in the "Bulk Transfer" section is discussed later.)
- ❑ **Liabilities to creditors:** Accounts payable for services can result on liens on the business during the sale. Similar to taxes liabilities, creditors liabilities can become the responsibility of the new owner if the transfer is not done correctly.

### **Bulk Transfer**

Generally, the bulk transfer is done with the sale of a major part of materials, supplies, merchandise, or inventory beyond the normal course of the seller's business. The purpose of the bulk transfer is to protect creditors. The bulk transfer is important for the buyer because he/she is liable to creditors the process is not done correctly.

### **Bulk Transfer Process**

**Seller's responsibility:** To initiate the process have the seller sign an affidavit revealing all creditors and tax liabilities and then contact creditors. This will provide legal shelter in the future if some liabilities are intentionally or unintentionally omitted.

**Notice of Intention:** Notifies all creditors that a sale of the business is about to occur and that any claims against the business need to be filed. The notice generally should follow the following form:

- ❑ Names of the buyer and seller (including business names used by seller in past 3 yrs.)
- ❑ Addresses of buyer and seller.
- ❑ Location and general description of business to be transferred.
- ❑ Place and anticipated date of bulk sale.
- ❑ Whether or not bulk sale is subject to Commercial Code 6106.2, requiring payment of purchase price to creditors who file timely claims.
- ❑ If so, name and address of person with whom claims should be filed.
- ❑ Last date for filing claims.

In regard to tax liabilities, within 12 business days before the date of the bulk sale the buyer should do the following to notify tax authorities and any other creditors that have been left out of the initial notification:

- ❑ Record notice with the county recorder in the county or counties where the property to be transferred is located, and if different, where seller is located.
- ❑ Publish a notice in a newspaper within the area of property to be transferred and, if different, in the judicial district where seller is located.
- ❑ Deliver notice to county tax collector where property to be transferred is located.

### **Covenant Not to Compete**

Covenants not to compete are commonly used to protect the buyer of a business from competition from the seller. Although the enforceability of non-compete agreements are uncertain, they are usually recommended. There are a few guidelines to follow:

- ❑ Be specific and reasonable about the areas in which the seller is not to compete.
- ❑ State a reasonable time period during which the seller is not to engage in competition with the sold business.
- ❑ Covenants not to compete may not completely restrict the seller's ability to make a living.

In addition to covenants not to compete, there are some other types of agreements such as “non-solicitation agreements” and “non-disclosure agreements”. Non-solicitation agreements prohibit the seller of a business from soliciting past clients, while non-disclosure agreements prevent the seller from disclosing trade secrets or other sensitive information about the business.

For examples of language to use, see the 6<sup>th</sup> edition of Nolo Press’ book, Legal Guide for starting and Running a Small Business, page 10/17.

## **Assessing the Business' External Environment**

Among the things in the external environment that deserve some investigation are:

### **Licenses and Permits**

Many necessary licenses, such as liquor licenses, will not transfer with the sale of a business. Before purchasing the business, figure out what licenses the business needs for operation and then contact the issuing agency to ensure that you will be able to transfer the license or apply for a new one.

### **Patents, Trademarks, Copyrights and Logos**

If the business that you are considering purchasing has pending patents, trademarks, copyrights or logos, find out what entity owns these proprietary items to ensure that they will be transferred as part of the sale. Check the expiration date on patents or copyrights to make sure that the value you assigned to them is consistent with their remaining life span. Usually a registered trademark or service mark is assignable as part of the goodwill of the business as part of the transfer. Make sure to include patents or copyrights among the list of items to be transferred when drafting the sales agreement.

### **Questions about the Lease**

Part of your interest in the business may result from its location. If the property is occupied under a lease, you'll want to see a copy of the lease agreement and note the following (in addition to matters discussed in the previous section on leases):

- Will you be able to assume the lease?
- How much time is left on the lease?
- Will you have an option to renew the lease?
- Is the tenant required to pay anything other than rent? For example, a set percentage of sales or maintenance fees?
- Who is responsible for building repairs and maintenance?
- Is there a clause stating when rent will go up?

### **Title to Assets**

If the business owns vehicles or real estate, you will want to ensure that it will transfer as part of the sale. You'll first want to know who legally owns the asset and whether or not there are any outstanding liens or encumbrances against the asset. For automobiles, you'll want to see a copy of the vehicles title or loan documents. For real estate, you'll want to see a copy of the title insurance policy or request a title search from a local title company; there is usually a fee for this service. As a part of the escrow process, funds for the purchase of the business can be designated to repay creditors, or the purchase price can be adjusted to reflect the lien amounts.

### **Zoning Limitations**

Check with the city and county in which the business operates to see what the zoning is in the area where the business is located. Look for "zoning variances" and "conditional use permits" or other language indicating that the business is in an area not designated solely for that type of activity. (Please refer to prior information in section 1 on required licenses and permits.)

It is possible that with the transfer of ownership, you may find that you need comply with zoning standards (such as number of parking spaces) or other regulations that were not applicable to the previous owner because their business predated these clauses. If you find this is the case, you may be able to receive a variance from the city or county for a fee.

### **Pending Legal Matters or Contingent Liabilities**

Investigate pending lawsuits and other legal issues affecting a business before you purchase it. Ask the seller to see copies of legal papers and letters from anyone who is threatening lawsuits. The county clerk in the counties where the organization conducts business is a good place to check. They can tell you if any lawsuits have been filed against the business or sellers in question.

Ask to be held “free and harmless” of liability by the seller. By using such language in your sales contract, the seller agrees to be financially responsible for any suits resulting from behavior or product sales before the transfer date.

### **The Sales Agreement**

The sales agreement should define all details of the sale as specifically as possible.

- ❑ **What’s being sold:** Often it is intangibles that get forgotten (Ex: customer lists, logos, trademarks, business name, etc). Develop an outline, then work with a lawyer to draw up the sales agreement. By initiating the process, you can better insure that you get those assets you want and leave the assets you don’t want or need.
- ❑ **Identify the parties involved:** Identify the buyer(s) and seller(s) and their addresses. This should include any partners of the seller if the buyer is purchasing the business in its entirety. The name of the business should also be included in the sales agreement if it is different from the seller’s name.
- ❑ **Allocation of purchase price:** Define how much value is assigned to what part(s) of the business. Allocations will typically be under categories such as goodwill, fixed assets, merchandise, etc. The allocation of the sales price to the different parts of the business is an important process because it will affect your future taxes. Buyers want the majority of value assigned to those assets that provide the fastest recovery on your investment. Value assigned to fixtures, equipment, and furniture provides the best tax shelter since they can be written off as a depreciation expense. Allocation of value to goodwill or intangible assets should be avoided if possible because they provide little or no tax shelter. If seller is going to work with you for a while get a larger portion of price allocated to his/her salary since you can write it off as a business expense.
- ❑ **Payment of business:** Often sellers “carry” the financing of the purchase. If you are the seller of the business, this may be dangerous because of loss of assets on buyer's default. Essentially this means that a buyer gives the seller a down payment and then pays the remainder of the purchase price over an agreed upon period of time (usually every month for an agreed upon number of months). This is beneficial to the buyer even if they have the ability to purchase the business

outright because it reduces the money up front as well as increasing the seller's interest in your success.

- ❑ **Covenant not to compete:** A covenant not to compete legally restricts seller from opening a business that could reasonably be considered threatening to your own. Be as specific as possible. The covenant should specify geographic (within 20 miles of your business) and time period (until 2010) restrictions.
- ❑ **Contingencies:** In the event that some unforeseen event precludes your ability to open or purchase the business you should include contingencies in the sales agreement upon which you will be released from any contractual obligation to purchase. If, for example, inspection of assets does not meet claims you should stipulate that the sales agreement is no longer binding. The possibility that you will not be able to get a license, permit, or loan should all be put into the sales agreement to insure that you are not obligated to buy if unanticipated events make the purchase less attractive.

### **Letter of Intent to Purchase**

This information can be found in the [California Legal Forms: Transaction Guide](#) and the Summary of [California Law 9<sup>th</sup> edition](#).

- ❑ **Non-binding:** A letter of intent usually creates a non-binding offer to purchase the business, and is usually needed in order for the seller to provide sensitive information about the business. It should spell out the proposed price, terms, and conditions for the sale of the business. The letter should also state that either side may revise or quit for any reason. A lawyer's supervision is always a good idea when drafting such a letter to be sure that the language is appropriate and non-binding. [www.businesslaw.gov/](http://www.businesslaw.gov/)
- ❑ **Binding:** The letter of intent may also be a binding agreement with contingencies built into it. These contingencies allow for the buyer to have a way out of the contract if anything is found that is unsatisfactory. The reason for binding letters of intent is the sellers' security. The seller may feel uncomfortable allowing a prospective buyer to look at sensitive financial documents without anything binding them to a contract with the seller. This contract should provide the buyer and the seller with the security to continue negotiations.

For a checklist on the items that should be completed by the close of the sale refer to [www.business.gov](http://www.business.gov). If you are still unclear about these items, seek legal assistance to direct you.

### **3. Hiring Employees**

Making the decision to hire employees is a big step for a small business. It involves legal and personal responsibility for others. Federal and state laws govern how you can search for potential employees, interview, investigate, and compensate them.

#### **Job Descriptions, Advertisements, and Applications**

##### **Job Descriptions**

Law prohibits intentional and non-intentional job discrimination against applicants on the basis of race, color, national origin, religion, gender, age, marital status, pregnancy, childbirth related medical conditions, sexual orientation, physical and mental disability, AIDS/HIV, and political activities or affiliation. With this in mind, write a job description that focuses on essential job functions and qualifications, such as necessary skills, education, experience, and licensure. Avoid language that could be evidence of discrimination (i.e. salesman vs. salesperson, married couple vs. two-person job, waiter vs. wait staff, young vs. energetic).

Do note that it's acceptable to list non-essential job functions as desirable but not required. For example, someone whose hearing is impaired may have trouble handling phone calls but be perfectly able to file and retrieve papers; therefore, handling phone calls would not be an essential job function. The Equal Employment Opportunity Commission at [www.eecoc.gov](http://www.eecoc.gov) has information on employer responsibilities under the American Disabilities Act (ADA) or the ADA section of this manual.

##### **Education as a Requirement**

Requiring a high school diploma or college degree could create an unnecessary barrier for a group population that can perform the job but are not likely to have the education requested. If the job requires more than basic skills, education or licensure is legitimate. For example: a high school diploma is not necessary to prepare meals at a fast food restaurant; however, an AA degree could be required for bookkeeper.

##### **Bona Fide Occupational Qualifications**

Anti-discriminatory laws recognize that in certain circumstances, an employer may have legal and essential reasons to seek an employee of a particular gender, age, religion or special qualification. For example, a women's clothing boutique might legitimately hire only female attendants if part of an attendant's job involves assisting clients in the boutique's dressing rooms.

##### **Job Advertisements**

In any ad, stick to the essential job functions and make reasonable accommodations for disabled applicants. A job advertisement that has only phone number would discriminate against potential job applicants with hearing impairments; thus, the job announcement must also provide an address. Please refer to the ADA section of this manual for more information on reasonable accommodations.

To gather a diverse applicant pool, it's recommended to place ads in various locations such as career centers at high schools, colleges, agencies, churches, senior citizen centers, newspaper, radio, television, and magazines.

## Hiring Employees

### Job Applications

Develop a standard application form that allows non-discriminatory comparison among applicants. Limit the form to the job-related information that will help you decide the best candidates to interview. At this stage, consent to have you conduct a background investigation and reference check can be obtained.

Americans Disabilities Act (ADA) prohibits pre-employment questions about disabilities. Refer to the ADA section of this manual for more information.

Consider requesting the following information:

- Name, address and phone number
- Are you legally entitled to work in the United States?
- What position or you applying for?
- What other positions would you like to be considered for?
- Can you work overtime?
- If you are hired, when can you start work?
- Education – high school, college, graduate and other (including school names, addresses, number of years attended, degree and major)
- Employment history – including name, address and phone number of each employer, supervisor’s name, date of employment, job title and responsibilities and reason for leaving
- Special training or achievements

Samples of job applications are found in Everyday Employment Law, The Basics ,Guerin and DelPo, Nolo Press, 2002.

### Interviews

Asking illegal questions can result in an applicant having sufficient grounds for filing a discrimination suit against your company. An interviewing process is much more cost effective when you account for the possibility of a long and costly court battle. The following information will help lead you through the process that is important for an employer who wants to reduce risk.

#### Examples of Lawful and Unlawful Questions

<b>Age</b>	<u>Unlawful</u> Lawful	How old are you? Are you 18 years of age or older? To determine if the applicant is old enough to perform the job.
<b>Marital Status</b>	<u>Unlawful</u> Lawful	Are you married? Is your spouse employed by this employer? If your company has a nepotism policy.
<b>Citizenship</b>	<u>Unlawful</u> Lawful	Are you a native-born citizen of the US? Where are you from? Are you legally authorized to work in the US?
<b>Disability</b>	<u>Unlawful</u> Lawful	Do you have any physical disabilities that would prevent you from doing this job? These are the essential functions of the job... How would you perform them?
<b>Drug &amp; Alcohol Use</b>	<u>Unlawful</u> Lawful	Have you ever been addicted to drugs? Do you currently use illegal drugs?

### **Tips for creating an interviewing system:**

- ❑ **Create guides for your interviewers.** Many sources suggest making two lists, one of the tasks that the employee will need to perform on the job and another of the experience or education necessary to perform the listed tasks. This way your interviewer has a guide to focus them on the critical points that need to be addressed and at the same time alerting them to topics that do not need to be discussed. Basically if it's not on the guide don't bring it up! This does not mean that the applicant cannot bring up a topic.
- ❑ **Create a method or criteria for judging responses.** Some companies even use a numbered rating scale for each question. This way each applicant is judged objectively and on a uniform measure.
- ❑ **Document all correspondence with applicants.** Save all resumes, cover letters, emails, interview notes and anything else you have documented about the applicant. Keep in mind that all this information is private! The applicant may not have ever become an employee, but this documentation should be protected just like an employee file.
- ❑ **Train your interviewers to be aware** of the risks associated with the interview and tactics to reduce this risk. Some companies reduce risk further by using a committee to interview applicants so that there are many people to judge the applicant.
- ❑ **Don't make promises in an interview.** Promises of promotions, or pay increases can be construed as implied contracts to applicants. You basically must make good on this promise/implied contract and if this is broken the applicant can file suit against you for breach of this contract.
- ❑ **Treat prospective employees with honesty and respect.** They deserve to know the truth. For example, if you don't tell an employee critical information such as informing them that the company may go bankrupt in the next 30 days, or layoffs are planned you could be held liable for this. If you don't tell them about something that could affect their security and could cause them damages then something along these lines better not happen. The employee could hold you liable for the damages associated with the fact that you did not disclose this information.
- ❑ **Always create a "Conditional Offer of Employment"** for any employee that you offer to hire. This is a contract of sorts simply stating that you intent to hire this person given all reference and background checks come out to your satisfaction. This formalized document is needed before you start any background checks.

### **Testing Employees**

The testing of employees is becoming more common in today's workplace. Here is a list of common tests and the legal issues associated with them.

- ❑ **Skills Tests:** generally acceptable to do as long as the skills tested are related to the job and the skills listed in the job description.
- ❑ **Aptitude Tests:** risky, come very close to laws regarding invasion of privacy, hard to relate to the job skills.
- ❑ **Honesty Tests:** polygraphs or lie detector tests are generally outlawed by the Federal Employee Polygraph Protection Act

### **Background Checks**

Once the interview process has been completed you may want to run a background to gain insight into a person's experiences that could affect their ability to work well in the specific job.

## Hiring Employees

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Background checks can also be used to decide whether to promote a current employee or transfer them to another job. Only run a background check on someone who is very likely to be hired or promoted. You do not want a rejected applicant or employee accusing you of using background check information as an excuse for not hiring them even though they are qualified. It is always safer to make decisions on job qualifications. If you wish to read the actual laws concerning background checks, they are the California Investigative Consumer Reporting Agencies Act (ICRA) and the Federal Fair Crediting Reporting Act (FCRA). These can be found on the web at [www.privacy.ca.gov/icraapv.htm](http://www.privacy.ca.gov/icraapv.htm) and [www.ftc.gov/os/statutes/fcra.htm](http://www.ftc.gov/os/statutes/fcra.htm). These laws refer to “background checks” as “consumer reports”. Consumer reports refers to checks that provide information on the individuals “character, general reputation, personal characteristics, or mode of living.”

<p><b>What can be checked and used to make a decision?</b></p> <ul style="list-style-type: none"> <li><input type="checkbox"/> What is relevant to the job and can be found on public record, excluding things that are prohibited.             <ul style="list-style-type: none"> <li><input type="checkbox"/> Court records</li> <li><input type="checkbox"/> Credit reports</li> <li><input type="checkbox"/> Driving record</li> </ul> </li> <li><input type="checkbox"/> Work history from former employers</li> <li><input type="checkbox"/> Neighbors and other acquaintances</li> </ul>	<p><b>What cannot be checked and used to make a decision?</b></p> <ul style="list-style-type: none"> <li><input type="checkbox"/> Anything that is confidential.             <ul style="list-style-type: none"> <li><input type="checkbox"/> Education Records. (Always must get specific written permission to get school transcripts)</li> <li><input type="checkbox"/> Military service record</li> <li><input type="checkbox"/> Medical Record</li> <li><input type="checkbox"/> Workers Compensation</li> <li><input type="checkbox"/> Bankruptcy</li> <li><input type="checkbox"/> Arrest information</li> </ul> </li> </ul>
<p><b>What can be divulged by a former employer?</b></p> <ul style="list-style-type: none"> <li><input type="checkbox"/> Anything that is true, excluding things that are confidential.</li> <li><input type="checkbox"/> Public information</li> </ul>	<p><b>What cannot be divulged by a former employer?</b></p> <ul style="list-style-type: none"> <li><input type="checkbox"/> Anything False</li> <li><input type="checkbox"/> Anything that is confidential</li> <li><input type="checkbox"/> Anything irrelevant</li> </ul>

**Where can you go to have a background check run?**

- Look under "Investigators" in the Yellow Pages.
- Consumer reporting agencies (CRA).
- Online CRAs such as
  - <http://www.knowx.com/>
  - <http://www.informus.com/>
  - <http://www.conf-chek.com/>

Shop around for a CRA. Ask about their reputation and where they get their information. If they say that they cannot tell you where they get their information, look for another. A consumer report will cost roughly \$50.

**Getting permission to run a background check.**

- Get prior written consent, separate from the application, before checks are conducted, whether performed “in house” or through a third party.
- Within three days of requesting or compiling the report, provide written notice to the applicant or employee that a check is being done, or has been requested. The name and address of the agency, and the nature and scope of the background check must be included.

## Hiring Employees

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- ❑ Provide a copy of the report to the applicant or employee if they have requested one, either at a meeting with the individual or within seven days of the employer receiving the report, whichever comes first.

### **Adverse Action**

After a background check has been performed and reviewed, you may find something that you will use as a basis for denying the job. Denying the job or promotion because of information uncovered in the background check is referred to as *adverse action*.

*If adverse action is going to be taken...*

- ❑ Before you take adverse action, you must give the individual a Pre-adverse Action Disclosure that includes a copy of the individual's consumer report and a copy of "A Summary of Your Rights Under the Fair Credit Reporting Act". The credit-reporting agency that furnishes the individual's report will give you the summary.
- ❑ After you have taken an adverse action, you must give the individual notice orally, in writing, or electronically that the action has been taken in an Adverse Action Notice.

*An Adverse action Notice must include...*

- ❑ The name, address, and phone number of the CRA that supplied the report.
- ❑ A statement that the CRA that supplied the report did not make the decision to take the adverse action and cannot give specific reasons for it,
- ❑ A notice of the individual's right to dispute the accuracy or completeness of the information the agency furnished, and his or her right to an additional free consumer report from the agency upon request within 60 days.

### **Wages and Overtime**

#### **FLSA and Minimum Wage**

Both federal and state statutes regulate wages and working hours of employees, mainly the federal Fair Labor Standards Act. The FLSA sets a federal minimum wage which workers must be paid. Earnings may be in the form of piece-rate, commission, salary, or hourly, but these must be averaged out to equal at least minimum wage. This law also requires pay for overtime, and covers child labor law and "equal pay for equal work" rights.

Most employees of small businesses are hourly wage earners. The FLSA provides for a minimum wage and overtime provisions for these employees. Currently, the federal minimum wage for covered nonexempt employees is \$5.15 an hour with overtime of 1 1/2 times due for more than 40 hours a week in most cases. However, where state law requires a higher minimum wage, the higher standard applies. In California, minimum wage is \$6.75 per hour, and overtime is required for work in excess of 8 hours a day. This is what will apply to small businesses in California.

#### **Exemptions**

Exempt classifications are generally narrowed down to five categories:

- ❑ Executives
- ❑ Administrators
- ❑ Professional employees
- ❑ Outside salespeople
- ❑ Employees in certain computer-related occupations

Exempt employees are usually salaried at a higher pay rate and work for a fixed amount per week or month. A certain percentage of their work time must be devoted to specific type of duties. These employees are usually in positions such as manager, finance officer, and other department heads. An outside salesperson must regularly engage in sales work away from the office and no more than 20% of their time should involve duties other than sales. These employees are exempt from overtime and certain other provisions of the FLSA.

### **Exceptions**

Exceptions to the federal minimum wage laws may apply to tipped employees. An employer may credit a certain amount of the tips against the employer's minimum wage obligation. According to federal law, this sets the employer's cash obligation to the employee at not less than \$2.13 per hour. However, this wage added to the employee's tips must equal at least minimum wage. If not, the employer must make up the difference. Higher standards set forth by state codes must be followed, though. Under California law, tipped employees must be paid the prevailing minimum wage.

The FLSA also covers child labor law. Federal law allows child labor for certain types of work. 14 and 15 year olds cannot work in hazardous industries, and their hours are limited to 3 hours on a school day and 8 on a non-school day. (18 hours a week total). There is also a federal youth sub-minimum wage of \$4.25 an hour established for employees under 20 years old during their first consecutive 90 days of employment. After this initial period, minimum wage will apply. Employers may not displace current workers to hire a sub-minimum waged worker.

### **Compensable Time and Duties**

An employer must pay covered employees for all of their time they control and that benefits the employer. It's important for an employer to know what kinds of time and work are considered compensable. Fines of up to \$1000.00 per violation may be assessed against employers for violation of minimum wage and overtime provisions. Some examples of normally compensable time are:

- ❑ Breaks
- ❑ Meal periods if employee is not relieved of duty
- ❑ Meetings sponsored by the employer
- ❑ Travel to outlying job site.

If an employee is not actually working, but is required to remain on the premises while awaiting an assignment, they must be paid. An on-call employee must be paid for their time while on-call if the employee has little or no control over their time and can't use it for their own benefit or enjoyment. For example, a repairperson that must remain on call is not necessarily at liberty to use his time for their benefit and enjoyment, and that employee must be paid for the on-call time. An employer does *not* have to provide pay for absence due to illness, holiday or vacation, lunch hours, or due to shutdown for regular maintenance.

### **Overtime**

In addition to minimum wage, federal and state laws regulate the amount of overtime an employee must be paid. Historically, overtime has been paid at a rate of 1 ½ times the regular wage for time worked in excess of 40 hours a week. In January 2000, the "Eight-Hour Day

## Hiring Employees

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Restoration and Workplace Flexibility Act” took effect in California. This Act mandates that nonexempt employees be paid overtime for any work performed in excess of 8 hours in a workday, regardless of how many hours worked in the week. Currently, California employers are obligated to pay:

- Up to 8 hrs a day = \$6.75
- 8-12 hrs = "time and a half"
- Over 12 hrs a day = "double time"
- 1<sup>st</sup> 8 hrs of 7<sup>th</sup> consecutive workday = "time and a half"
- Over 8 hrs on the 7<sup>th</sup> day = "double time"

*Overtime pay cannot be waived by the employee.*

### **"Comp Time"**

Employers may be inclined to offer employee compensation time in place of overtime pay: one hour off for every hour of overtime worked. However, according to federal law this is illegal for small businesses. Employees do not receive their fair time and a half pay, and the federal government doesn't collect the taxes on that income. Under federal law, if an employee does not work over 40 hours a week, there is no overtime earned and "comp time" may be used. In California, there is a daily overtime standard making this impossible. The only circumstances under which comp time can be used in California is if the employee is given 1 ½ hours off for every hour of overtime worked, *and* the time off is taken within the same pay period.

### **Future Changes**

Proposed changes to both the overtime and comp time regulations are currently under consideration. The U.S. Department of Labor is proposing to strengthen overtime protection for employees and possibly institute the use of compensation time for small businesses. Make sure to check for the new law.

## 4. Employee Termination

### Employment At-Will

Any employee who is employed “at-will” can be terminated for any reason or no reason at all, except for “wrongful reasons”. At-will employment serves as a safety shield for both the employee and the employer. Not only can the employer terminate the employee freely, but the employee can also terminate his/her own employment at any time, for any reason, and without notice. (Two-week notice may be a common practice, but it is not the law.)

### Wrongful Termination

The employment at-will doctrine allows you to fire an employee for any *legal* reason. Here are a few illegal reasons that an employer must avoid.

- ❑ **Discrimination:** Federal law makes it illegal in most cases to fire an employee based on race, gender, national origin, disability, religion, or age (if over 40). It is also illegal to terminate an employee if she is pregnant or has a pregnancy-related medical condition. Most states include their own anti-discrimination laws as well.
- ❑ **Retaliation:** Employers may not terminate an employee for asserting any of their legal rights protecting them against discrimination or harassment. Employees cannot be terminated for complaining, filing a lawsuit, or testifying on behalf of a co-worker, with regards to discrimination.
- ❑ **Refusal to participate in a lie detector test:** The federal Employee Polygraph Protection Act prohibits most employers from firing employees for refusing to submit a lie detector test (agencies such as the sheriff’s department are exempt).
- ❑ **Status of citizenship:** The federal Immigration Reform and Control Act prohibits the termination of an employee based on the fact that she/he is not a US citizen. This act protects any legally eligible employee of alien or legal resident status.
- ❑ **OSHA violations:** It is illegal for employers to terminate an employee for making complaints about unsafe working conditions, under the federal Occupational Safety and Health Act.

### Contract Employment

It is unlawful to terminate a contract employee if the termination was in breach of the terms of the contract. Employers may make a contract in two different ways. First, there are written, expressed contracts. This makes it easy to judge whether or not you have a contract and the specific terms that allow a termination of the contract employee.

As explained previously, it is also possible to create an implied contract with an employee, whether the employer intended it or even knows it. An employment contract is implied (and valid) by the actions and statements made by the employer. The best suggestion for prevention is to state at the time of hire that the employee is considered “at-will”. The best way to make this statement is in writing, with a signature of the employee, proving his/her acknowledgement.

Here are a few tips to follow that can help prevent you from unintentionally forming an implied employment contract:

- ❑ Never tell an employee that the only way he can get fired is if he or she messes up. This may prevent you from firing him or her for any other legal reason, but also it will prevent the employee from taking necessary risks that can really put you ahead of your competition.
- ❑ Never use the term “90-day probationary period”. An employee can easily infer that after this 90-day period, he is considered a “for cause” employee.
- ❑ No matter how well an employee does, never tell them that you see "a long future ahead for them at the company". You are implying that they have job security at the company, regardless of what events might occur.

### **Firing a Contract Employee**

It is possible to fire an employee, even with a contract. Therefore, it is critical to include in the contract all reasons for which the employee can be fired. The more detailed the terms are, the easier it will be to terminate the employee. Once these terms are written, read, and signed, they must be followed carefully.

### **Good Cause**

Almost all written and implied contracts allow employers to fire contract employees for a good cause. Good cause means that there must be a legitimate, business-related reason. A few examples are:

- ❑ Sexual harassment
- ❑ Violence or violent threats
- ❑ Drug/alcohol abuse within the scope of employment
- ❑ Committing crimes
- ❑ Poor job performance. To use this as a cause, it is always best to have a practice that measures and standardizes good performance, in order to prove that an employee was not performing up to these standards.

### **Good Faith and Fair Dealing**

With respect to contract employees, an employer has the obligation to treat the employee fairly and honestly. For example, an employer is not allowed to fire the employee to prevent him/her from collecting retirement benefits. Likewise, it is not legal to fire an employee only to replace him/her with an employee who requires less pay.

### **The Firing Process**

Sometimes, it is your duty to fire an employee. For example, if an employee is sexually harassing other employees, it is your duty to fire that employee in order to put the harassment to a stop.

Other times, it is not so clear as to whether or not you should fire someone. Here are a few tips to think about before dropping the axe.

- ❑ Know whether or not you are dealing with a contract employee. Written contracts are clearer, but implied contracts are often unclear.
- ❑ Follow your company’s policies. If you have a policy regarding the termination of employment, follow it. Policies are set as guidelines to follow for this exact reason. You need to protect yourself from anybody who may have been fired for the same reason in

the past, and you want to set an example for the future. It is very critical to be consistent with your policies.

- ❑ **Be Fair and Impartial.** Your decisions will not only affect the employee being fired, but also the employees who are still with you. If they see that you are treating a fellow employee unfairly, they will realize that you would treat any of them the same way. This will also keep you out of legal trouble.
- ❑ **Talk to a Lawyer.** If you are unsure about whether or not your reasoning is legal, talk to a lawyer. It is better to be safe than sorry. The lawyer's fees may be less than your former employees damages.

### **How to Fire an Employee**

The manager has to break the news to the employee, but he or she also must be very careful in the manner in which the termination takes place. This section will take a closer look at the specific event of firing an employee, and the “do’s and don’ts” related to the fateful occasion.

#### **Some suggestions:**

- ❑ **Be respectful of your employee.** The firing process can be traumatic for everyone involved; however, the employee who is getting terminated certainly deserves dignity and respect. Not only is this the decent thing to do, but it may also help your business avoid future lawsuits or employee sabotage.
- ❑ **Document everything.** Many businesses get themselves in trouble by not carefully documenting the firing process. It is critical to write down everything that happened during the process. This process is both for the company to learn from experience how it can improve its processes, and have evidence if the employee makes claims against it in court.
- ❑ **Choose the proper time and place to fire an employee.** There is much debate about the topic of when to fire an employee. Research indicates that there are two choices that may be advantageous for both the worker, and the organization: Monday or Friday. The advantages of firing a worker on Monday are that the worker may be able to commence his or her job search earlier, and the organization can “tidy up” the worker’s final exit paperwork. The advantage of Friday may be that it allows the worker an opportunity to “cool off” over the weekend and let things settle before beginning his or her job search on Monday. Either way, both Monday and Friday seem to be the most commonly recommended days. As for “where the meeting should take place,” a manager should pay very close attention to the dignity of the individual and use a private room to break the news. Places to be avoided in the firing process: cubicles, hallways, break rooms, etc... It is very important to not make the employee feel like an outsider or criminal.
- ❑ **Be careful about what you say.** Make sure to keep the conversation focused and to the point, and avoid any “small talk” at the risk of being misconstrued as uncaring or cruel. Essentially, keep your focus on the details – tell the employee why he or she is being terminated, and detail the steps in the process. For example, after breaking the bad news, make sure that the employee knows what to expect with regard to severance pay, holiday or sick pay, health insurance, personal property, business property, etc...
- ❑ **Reclaim business property in a respectful manner.** Many employees will have company property (such as cell phones, laptops, etc...) that must be returned before the worker permanently leaves the premises. There are many stories about businesses that go

through a fired employee's desk and take everything...while the employee stands there under the scornful eyes of his or her former workmates. This may not be a good idea. For one, you are not showing your former employee the respect that he or she deserves.... and two, you may be setting yourself up for a legal battle.

- ❑ **Have a neutral person perform the task.** It makes sense that a direct supervisor may not be the best person to fire a worker who has worked for him or her. Accordingly, it is recommended that a neutral figure meet with the worker during the termination process. One example of such a worker may be the human resource manager of the organization.

### **Layoffs versus Firing**

All of the previous ideas apply to the layoff process. Layoffs are, in many respects different than firing. First, layoffs may be required by a business that is ailing financially, and the decision to lay off workers may be due to business weakness rather than individual weakness. Second, a layoff often will occur en masse...meaning that a business will lay off many workers at once.

- ❑ **Involve the top management in the process.** When the decision is made to layoff workers, often a business will have to let go of workers that it would otherwise like to keep. In this respect, the workers may feel let down by the management, and may seek retribution for receiving a pink slip. To avoid the perception that the management does not care about the workers' well being, it is recommended that the top management meet with each worker to discuss the core reasons for the layoff. This step in the process is also designed to soothe the workers that are remaining in the company.
- ❑ **Make sure to give advance notice.** Under the Workers Adjustment and Retraining Act (WARN), specific large businesses must give workers 60 days' notice before conducting lay offs.
- ❑ **Be careful about security.** A worker who is fired or laid off will feel many emotions. It is possible to assume that some workers' may take out that anger or resentment on the company or its staff. Several key areas of concern to be considered:
  - Employee access to computer servers or IT operations
  - Employee access to trade secrets or classified business information
  - Employee access to security codes or keys to the business

It may seem paranoid to think about employees that may return to harm your business. But, don't allow yourself to be fooled. The potential that a former worker will lash out at the business that fired him or her is fairly great. In fact, the FBI estimates that disgruntled former employees cause over \$378 million dollars in damages per year. One such story that will send shivers up any businessperson's back is of a former employee of a chemical firm in New Jersey who was laid off in 2001. The individual happened to be the Information Management Systems Director, and he was escorted off the premises by security guards after working for the company for 30 years. In return, the employee tapped into the company's computer and caused over \$20 million in damages.

### **Giving and Requesting References**

Giving references for past employees might seem like a casual event, but it ought to be an area of great caution for any owner/operator of a small business. When speaking in regards to a past employee it is essential that you only relay true, verifiable facts. Never meander into the realms of speculation, opinions, or exaggerations regarding the person or their conduct.

- ❑ **Blacklisting Laws:** Many states have passed blacklisting laws that allow for civil and criminal legal action against anyone who attempts to sabotage a worker's prospective job situation. Answering direct questions or making truthful, good intentioned statements probably will not get you in any trouble. The laws were established to eliminate former employers actively going out of their way to keep a person from getting a job.
- ❑ **Defamation:** If a former employee believes that you have made hurtful or damaging statements about them, you could potentially be sued for defamation. This typically takes place when there is a request for a reference, but can also result if you release negative or embarrassing facts about their termination to a co-worker. Under law in every state, you can defeat a defamation suit if you can prove that the statements were true.
- ❑ **Public Disclosure of Private Facts:** When providing references or answering questions regarding a former employee's termination reveal only that which is relevant to the circumstances. Keep to topics that are relevant to the business world and never cross over into the private sector of a former employee's life. You may know plenty about this person having worked with them for sometime, but if they have a reasonable expectation of privacy regarding that information, you are bound to honor their privacy.
- ❑ **Misrepresentation:** Making untrue statements, or failing to disclose relevant information regarding a former employee's experience with your business can also open the door for a lawsuit. For example, you fail to disclose that your employee was stealing a company asset. When the employee is hired by a subsequent employer, they begin to steal from them. By not providing this relevant information you could be held liable.

### Guidelines for References

There are a few actions you can take to help minimize the potential for reference related lawsuits. The number one rule is to only give written references. This gives you the opportunity to think through your responses regarding an employee while properly documenting everything that you say. It also minimizes the negative impact that emotions, lack of preparation, or timing of a phone call can play into your reference. Here are some other policies and procedures to help you in these situations.

- ❑ **One person:** Designate a specific person, usually in human resources, who knows the ins and outs of the state and federal laws and your specific company policy on requests for references.
- ❑ **Documentation:** Keep extensive documentation of everything that is directly or indirectly connected to referencing. This includes, but is not limited to, requests, responses, correspondence, and notes from conversations.
- ❑ **Consultation:** Eliminate any surprise that the ex-employee might have by addressing and discussing the reference you will give them if requested. It is important to establish this before the employee departs.
- ❑ **Get a release:** You can request that the former employee first sign a release giving up their right to sue before you will address their time with your business. It becomes the prospective employer's responsibility to get the employee's signature if they truly want the reference.
- ❑ **Review personnel file:** Don't speak from your memory. Consult the personnel file to re-acquaint yourself with the former employee and the circumstances regarding their leaving your business.

- ❑ **Speak fully:** If you do decide to give a reference, do not withhold information that could be detrimental to the future employee especially in regards to violence, drugs, dangerous actions, or sexual misbehavior. If the individual is hired and commits similar acts, you could be held liable for not disclosing this information.

### **Post Termination Issues**

**Health Insurance: C.O.B.R.A. (Consolidated Omnibus Reconciliation Act):** This federal law states that any company with 20 or more employees, which offers group health care, must continue to extend an opportunity for those benefits to employees after they quit or are terminated. The benefits are offered to the employee, their spouse, and dependents for 18 months, at the employee's cost. The former employee must now pay both portions of the premium in order to receive these benefits. The employer can offer these benefits for 102% of their past premium cost in order to recoup the administrative expenses that might occur. This applies to HMO, PPO, and traditional plans. Dental and vision coverage must also be offered if they were previous part of the employee's package. More information regarding C.O.B.R.A. consult the Department of Labor website at [www.dol.gov/](http://www.dol.gov/).

**Severance Packages:** Severance packages are typically extended to long-term employees as a gesture of appreciation for their time and efforts. They are not required by law and are generally used as an attempt to minimize potential litigation. Severance is only required if you led an individual to believe that they would be receiving this type of package upon termination of your work relationship. This includes:

- ❑ Written contracts promising a severance package.
- ❑ Statements in an employee handbook or policy manual.
- ❑ A historical precedent of severance for people in that position.
- ❑ Verbally stating that severance will be provided.

**Releases:** One way to possibly eliminate the risk of dealing with litigation regarding an employee's termination is to get them to sign a release. A release is a contract that states that they are giving up the right to sue your company for reasons regarding their termination. The following are some items that you ought to keep in mind regarding releases.

- ❑ **Exchange:** Often times a severance package will be offered on condition of signing a release. Considering that you are asking them to give up their right to sue, it is much more appealing for the employee if you are also willing to give up something in return.
- ❑ **Clarity:** It is important, for your sake and for the employee, that you provide clarity within this document of the rights that are being given up. This can be essential in avoiding future litigation coming back to haunt you if they claim that they didn't know what the release meant.
- ❑ **Time:** You must give the employee adequate time to make their decision regarding giving up their right to sue. It may be reasonable that they might ponder it for a week or two.
- ❑ **Coercion:** The signing of a release must be completely voluntary and without coercion on your part. If it is found that you coerced the individual into signing the release, it could be thrown out in future litigation hearings.
- ❑ **Special cases:** For individual who are forty years or older, there are some special clauses regarding releases. You must offer them longer period of time to think about signing the

release, you must allow a revoke period, and you must recommend (in writing) that they consult an attorney.

### **Unemployment Eligibility**

An individual is only eligible for unemployment if they are out of work through no fault of their own.

- ❑ **If the employee quits:** An employee must have a reasonable and compelling reason to leave in order to receive unemployment benefits after quitting their job. The terms “good cause” are used to determine whether or not they had a valid reason. Intolerable work conditions, threats to health and safety, or being laid off are all considered to be compelling reasons and allow for eligibility of unemployment benefits.
- ❑ **If the employee is fired:** An employee who is fired can be eligible for unemployment benefits under certain specific conditions. If a company makes financial cutbacks, the employee was not a good fit for their position, or they were fired due to a minor infraction then they could still be eligible. If the individual was fired for “misconduct” then they are not eligible for unemployment benefits.

## **5. The Regulatory Environment**

If you think your business is so safe you don't need workers' compensation coverage, think again. Each year, thousands of workers are injured on the job, and workers compensation insurance may be the only way to avoid liability. In addition, workers compensation is an important topic of concern, because of its extreme cost to small businesses. Therefore, understanding the complexities of the workers compensation system is a must for small business owners.

In addition, according to statistics provided by the U.S. Department of Labor, each year approximately 6% of workers suffer a work-related injury or illness, and over 6,000 workers lose their lives as a result of injury or illness. What are the ramifications for failing to comply with health and safety standards? Simply stated, the answer is stiff fines & penalties, which may amount to more than you are able to pay. Don't lose your business because you failed to understand the regulations set forth by the Occupational Safety and Health Act (OSHA) of 1970.

Finally, discrimination on the basis of disability is illegal according to Federal regulations. The Americans with Disabilities Act (ADA) of 1990 is another aspect of the regulatory environment governing small businesses. Understanding how to avoid unwittingly discriminating against potential or current employees is essential to limiting the liability of a business.

These three bodies of law contain significant regulating impacts on small businesses. Of course, there are numerous other regulations (e.g. public health) that also impact businesses.

### **Workers' Compensation**

#### **What is workers' compensation?**

It is a required insurance, which protects an employer against losses due to work-related accidents and illnesses. This insurance provides the injured employee with benefits to compensate for lost wages or decreased ability to work. The California workers' compensation system is a no-fault system, which means benefits are provided without regard to negligence or fault. It provides benefits to employees who are injured or become ill during the course of, or due, to employment.

#### **Who is required to have workers compensation?**

- ❑ In California, every employer is required to carry insurance to cover the cost of occupational injuries. It does not matter if a company employs full or part-time employees.
- ❑ Companies whose headquarters are located outside of California are required to have workers' compensation insurance if they have employees in California.

### **Exceptions**

- ❑ Self-insured companies: Companies that can prove to the California Department of Insurance that they can cover the cost of injuries incurred by their employees do not need workers' compensation coverage. These companies normally purchase catastrophic insurance for injuries that go beyond the required amount.
- ❑ Partners and owners are not required to have workers' compensation insurance for themselves. However, they can elect to have workers' compensation insurance if the insurance company and the California Department of Insurance approves.

### **Benefits for injured workers**

- ❑ Medical care: An injured employee is entitled to all necessary medical care to cure or relieve the effects of the injury.
- ❑ Temporary benefits: The employee receives a payment every two weeks to replace a portion of the wages lost while recovering from the injury. They will receive 2/3 of their weekly earnings, within a minimum and maximum benefits as determined by law.
- ❑ Permanent disability: This is additional money that compensates the employee for any permanent disability suffered as a result of the injury.
- ❑ Vocational rehabilitation: If the injury permanently prevents a return to his or her usual occupation, the employee is entitled to "vocational rehabilitation" (for example: job counseling, job modification, training, or placement assistance).
- ❑ Death benefits: If the injury causes death, a benefit is payable to qualified surviving dependents. Death benefits will be paid until the youngest minor child reaches age 18 and will continue if the aggregated total exceeds the statutory maximum amount.

### **Cost to Employers**

- ❑ All employers are required to contribute 2% of each dollar earned to the California Guarantee Association. The California Guarantee Association covers workers' compensation benefits for employers who purchase comp insurance from insolvent comp carriers.
- ❑ Experience modification: The cost of workers compensation insurance varies. It is determined by a formula that takes into consideration the following: size of company, type of company, past work related injuries, etc. Companies may pay a discount or premium based on their experience modification. Positive experience modification would allow a discount rate, whereas a negative score would mean the company must pay a surcharge for comp insurance.

### **Responsibilities of Employers**

- ❑ Post the name of your insurer and information about workers' compensation. The sign should be posted in a visible area.
- ❑ Notify all new employees of their right to workers' compensation benefits. When employees are hired, they should be given a handout regarding their rights.
- ❑ Complete and send an "employee report of occupational injury or illness" *within 5 days of injury*.

- ❑ Provide the employee a “dwc-1” form (requiring the employees to explain how their injury occurred) within one day of learning of an injury.
- ❑ Provide a safe and healthy environment. If you know something is wrong, fix it.
- ❑ Comply with occupational safety and health standards. (see "OSHA" section.)
- ❑ Do not discriminate or retaliate in any manner against any employee because s/he has filed a claim. Such action is a misdemeanor and, if found guilty, can result in a fine, increase in injured employee's benefits by one-half or both.

### **Fraud**

Workers’ compensation fraud laws make it a felony for employers or employees to file a false or fraudulent statement or to submit a false report or any other document for the purpose of obtaining workers compensation benefits.

### **Preventive Steps (reducing costs and headaches)**

- ❑ Have an “early return to work” program in place. When employees suffer job-related injuries or illness, you will want to do everything to help them recover and return to work. The program should consist of a lead person who has a basic understanding of the workers’ compensation process. Return to work programs help ensure smooth, expedient transition from injury and illness to productivity. When injured workers feel wanted, there is a good chance they will return to work sooner.
- ❑ Discuss the elements of the claim with carrier. This allows the workers compensation carrier to understand how the accident occurred. The insurance carrier should be able to provide measures to prevent a recurrence.
- ❑ Notify insurer in writing whenever you have actual knowledge of any facts that would tend to disprove the claim. By doing so, you will allow a better opportunity to investigate the claim thoroughly, possibly reducing the cost.
- ❑ Reclassify employees when possible and legal. Workers compensation cost is partially based on an employee’s classification. For example, if you have five people in a warehouse assembling and packing products, consider assigning two as assemblers and three as warehouse workers. The cost of workers compensation for the assemblers should be lower since they do not need to lift heavy loads or work with equipment.
- ❑ File claims in a timely manner. If the employer has knowledge of an industrial injury but fails to notify its carrier, the claim could be accepted at a later date. There are statutory laws that require claims be given to the workers compensation carrier within certain dates.
- ❑ Have an employer-designated provider for employees on file. If the employee has not pre-designated a personal physician/chiropractor, prior to a work-related injury, the employer can select the treating physician for the first 30 days after the report of injury. With new legislation, the treating physician or chiropractor’s opinion is presumed correct. The employer’s designated physician's opinion is assumed correct. This allows the employer to refer injured employees to a physician that the employer is comfortable with.

## **The U.S. Occupational Safety and Health Act (OSHA)**

### **The Occupational Safety & Health Act**

The United States Congress passed the [Occupational Safety and Health Act of 1970](#) (OSHA), (29 U.S.C. §651 to 678), requiring employers to provide workplaces free from serious recognized hazards. OSHA is operated under the direction of the U.S. Department of Labor, and its purpose is as stated in the Act itself: “To assure safe and healthful working conditions for working men and women.”

- ❑ OSHA encourages, authorizes, approves, and monitors states in their efforts to establish their own safety and health programs.
- ❑ Twenty-three states have established their own OSHA approved standards, and provide their own publications and trainings available for employers and workers. The following states have approved plans: Alaska, Arizona, California, Connecticut, Hawaii, Indiana, Iowa, Kentucky, Maryland, Michigan, Minnesota, Nevada, New Jersey, New Mexico, New York, North Carolina, Oregon, Puerto Rico, South Carolina, Tennessee, Utah, Vermont, Virgin Islands, Virginia, Washington, and Wyoming.

### **Effected Employers**

Employers in the 50 states, the District of Columbia, Puerto Rico, and all other territories under Federal Government jurisdiction are required to comply with OSHA standards, with a few narrow exceptions.

### **Employer Requirements**

- ❑ Provide a safe work environment, and a place of employment free from recognized hazards that are causing or likely to cause death or serious physical harm, and, further, to comply with occupational safety and health standards.
- ❑ Display the federal or state OSHA poster in your workplace.
- ❑ Have a copy of the federal or state OSHA standards that apply to your industry.
- ❑ Almost every business is required to have an Emergency Action Plan. It should include procedures and course of action to be taken during an emergency.
- ❑ You are required to post copies of all citations for violations and standards at or near the alleged violations for 3 days or until they are corrected.
- ❑ If your company employs more than ten (10) employees<sup>1</sup> at any time during the year, you must keep OSHA injury and illness records unless your establishment is classified as a partially exempt industry. However, all employers covered by the Act must report to OSHA, within 8 hours, any workplace incident that results in a fatality or the hospitalization of three or more employees. Report any injury requiring medical attention to your reporting OSHA office within 8 days of discovering the injury or receive an automatic \$5,000 penalty.
- ❑ According to the Act, you shall promptly notify any employee who has been or is being exposed to toxic materials or harmful physical agents in concentrations or at

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<sup>1</sup> (Workers are considered employees under OSHA if you: A) Control the actions of the employee, B) have the power to control the employee's actions, and C) Are able to fire the employee or modify employment conditions)

levels that exceed those prescribed by an applicable occupational safety and health standard.

- ❑ Records are to be maintained for five years and must be made available for inspection.
- ❑ You must comply with the your state OSHA as well as the Federal OSHA regulations. Contact your state agency for specific regulations.

### **Employee Rights**

- ❑ An employee has the right to report any hazards and unsafe conditions without retaliation or other consequence from an employer.
- ❑ Records regarding employees exposure to potentially harmful substance may be examined.
- ❑ May request an OSHA inspection at their worksite.

### **Inspections**

Under the Act, “OSHA representatives are authorized to inspect your workplace at reasonable times any factory, plant, establishment, construction site, or other area, workplace or environment where work is performed by an employee of an employer; to inspect and investigate during regular working hours and at other reasonable times, and within reasonable limits and in a reasonable manner, any such place of employment.”

Keep in mind inspections are conducted without advance notice unless there is one or more of the following:

- ❑ Imminent danger.
- ❑ Inspections that require special preparation or need to be held after regular business hours.
- ❑ Cases where an employer and/or employee must be present.
- ❑ Situations where an OSHA official deems it is important to inform the employer.

Due to the tremendous amount of worksites, OSHA inspectors can’t possibly inspect each of them on a regular basis. OSHA administrators have established a priority system for conducting inspections. They are listed according to priorities.

- I. Imminent Danger where there is certainty that a danger exists and serious harm, meaning “permanent or prolonged damage” or fatality are of concern.
- II. Fatalities and Catastrophes resulting in hospitalization of three or more employees.
- III. Employee Complaints: Each employee has the right to request an OSHA inspection when the employee feels that there is a violation of the standards.

### **Suggestions for Handling an Inspection**

- ❑ Verify OSHA inspector's credentials.
- ❑ Consider calling your legal counsel to determine if s/he needs to be present during the inspection.
- ❑ You have the right to protect your trade secrets.
- ❑ Ask questions and take notes during the inspection.

- ❑ Ask for a copy of all of the pictures, field-testing charts and other documents generated during an inspection.
- ❑ Focus the inspector to the area in question and the purpose of the inspection.
- ❑ If you are cited for violations of the OSHA regulations and standards, you have an allotted time to take corrective measures. You may receive a reduction in penalties if your effort is diligent and speedy.
- ❑ You may appeal a decision.

### **Preventative Steps**

- ❑ Have a safety policy, created with your employees input.
- ❑ Keep up-to-date on all of the regulations that apply to your business.
- ❑ Provide safety training for your employees.
- ❑ Self-inspect your facility on a regular basis.
- ❑ Document all training, inspections, and injuries.
- ❑ Develop a plan for an inspection. Make sure that you have someone on the premises who is informed and ready to implement the plan.

## **The Americans with Disabilities Act (ADA)**

### **Americans with Disabilities Act (ADA) of 1990**

The ADA is "designed to eliminate discriminatory employment practices that prevent otherwise qualified workers with disabilities from fully participating in the national labor force."

- ❑ The ADA only applies to private employers with 15 or more employees, local governments and their agencies, employment agencies and labor unions
- ❑ The act does not apply to the federal government.
- ❑ If an employee is disabled, then the employer must "reasonably accommodate" the needs of the disabled unless to do so would be an "undue hardship".
- ❑ To prevail in a lawsuit based in disability discrimination under the ADA, a plaintiff must be able to show that they:
  - have a disability,
  - are otherwise qualified for the employment in question, and
  - were excluded from employment solely because of the disability.

### **Defining Disability**

The ADA defines disability as:

- ❑ a physical or mental impairment that substantially limits one or more of the major life activities of such individuals
- ❑ a record of such impairment
- ❑ being regarded as having such impairment.

However, defining whether a person has a disability is done on a case-by-case basis by the courts, but a plaintiff must prove that they have the disability to be able to sue under the ADA. ADA does not have specific criteria for classification.

Some of the “Federally Recognized Disabilities”:

- Heart disease
- Blindness
- Muscular dystrophy
- Paraplegia
- AIDS, and since 1998 HIV
- Kleptomania is *excluded* by the ADA
- Cancer
- Alcoholism
- Cerebral palsy
- Diabetes
- Morbid obesity (weighing twice that of a normal person)

### **Reasonable Accommodation**

"If a job applicant or an employee with a disability can perform essential job functions with reasonable accommodation, the employer must make the accommodation."

Reasonable accommodation for the disabled may include, but is not limited to, such things as the following:

- installing wheelchair ramps,
- establishing flexible working hours,
- creating or modifying job assignments, and
- creating or improving training materials and procedures

*Exception:* "If an applicant fails to let the employer know how his or her disability can be accommodated, the employer may avoid liability for failing to hire or retain the individual on the ground that the individual failed to meet the 'otherwise qualified' requirement."

Employers must accommodate the disabled unless to do so would be an undue hardship. An “undue hardship” is defined as "significant difficulty or expense" to the employer. No uniform standards of what undue hardship means exist, so the courts decide what is "undue" on a case-by-case basis. Employers should carefully balance potential for liability with costs of accommodation.

### **Job Applicants & Pre-employment Physical Exams**

- Employers must reasonably modify their application processes so that those with disabilities can compete for jobs. (Example: Job postings that list only a phone number can discriminate against the hearing impaired because the deaf have no way of applying for the position.)
- As discussed previously, application/interview questions must be limited to assessing the applicant's ability to perform job functions in order to avoid potential liability.
- Employers cannot require a physical unless all applicants are required to provide one, employers may give a conditional offer of employment on the employee's successfully passing of an examination related to bona fide occupational qualification.

### **Health Insurance Plans**

- The disabled must have equal access to insurance, but employers can exclude from coverage preexisting health conditions and certain types of diagnostic or surgical procedures.

- ❑ Employers can also put a limit on health-care payments in its policy, as long as all employees have the same limitations.

### **Dangerous Workers**

- ❑ Employers are not required to hire/retain those who, because of their disabilities, pose a "direct threat to the health or safety" of their co-workers.
- ❑ The ADA requires that employers hire/retain otherwise qualified individuals but it does not require employers to hire/retain *unqualified* disabled applicants.

### **Substance Abusers**

- ❑ The ADA does not cover current drug users, only persons with prior alcohol/drug addictions –those who have completed a supervised drug– rehabilitation program or are currently in a supervised rehabilitation program.
- ❑ Casual drug users are not protected by the ADA because their drug use is not a disability.

## **Resources**

### **Workers Compensation**

- ❑ [www.scif.com/](http://www.scif.com/)
- ❑ [www.insurance.ca.gov/](http://www.insurance.ca.gov/)
- ❑ [www.dol.gov/](http://www.dol.gov/)

### **U.S. Occupational Safety and Health Act (OSHA)**

- ❑ The Federal Register is the best resource for updates on standards. OSHA regulations are listed under Title 29 of the Code of Federal Regulations (CFR), Part 1900-1999. It is available at public libraries. An annual subscription is available from the Superintendent of Documents, U.S. Government Printing Office, Washington D.C. 20402.
- ❑ The U.S. Department of Labor provides a website, which contains a full copy of the Act and provides useful information for business owners. There site is located at [www.osha.gov](http://www.osha.gov).
- ❑ A useful handbook for small business owners is OSHA Handbook for Small Businesses, it is available by writing to the U.S. Government Printing Office, Superintendent of Documents, Washington, DC 20402, or calling (202) 512-1800
- ❑ Small Business Development Centers provide training, counseling, and information to assist you in developing your safety policies and keeping up-to-date on standards.
- ❑ OSHA provides consultants who will visit your worksite and inspect without issuing citations. The consultants will provide you with a complete report and suggestions for improving the safety conditions of your workplace. They will also make a recommendation that your site be exempt from inspection for 1 year
- ❑ Contact your insurance agent. Due to the nature of such coverage, the company will assist you in being in compliance.

### **The Americans with Disabilities Act**

The ADA has a website where users can ascertain specific aspects of the Americans with Disabilities Act. The ADA homepage is located at: [www.usdoj.gov/crt/ada/adahom1.htm](http://www.usdoj.gov/crt/ada/adahom1.htm).