Top Ten Ways to Get Sued – Guaranteed!
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Over 80 million lawsuits are filed every year in the United States. If you are in business, you should be thinking about the risks involved. The following are some of the most common pitfalls that lead to liability and lawsuits for small business owners and how to avoid them.

Pitfall #1: Doing Business as a Sole Proprietor

Most people who go into business do so as a "sole proprietor." This means that they are doing business as an individual or a "d.b.a." (doing business as). This scenario offers absolutely no asset protection, not to mention poor tax benefits. If the business is sued, all of the personal assets of the individual are at risk. For less than $100 in most states, you can form a corporation to do your business or trade. If properly maintained, a corporation will shield your personal assets if the business is sued or goes bankrupt.

Pitfall #2: Doing Business as a General Partnership

Doing business with a partner is even worse than doing business as a sole proprietor. A "partnership" is formed when two or more people decide to do business together for profit. It does not require a formal partnership agreement or the filing of any official documents, although it is often done that way. A partnership can be created even if the parties did not intend it!

Here is the problem with a general partnership: if your partner does something foolish, you are liable. That right! If you allow your partner to commit the partnership to a contract, the partnership and its partners can be held liable for that debt. If your partner is negligent or incurs a debt on behalf of the partnership, you are on the hook - even if your partner files bankruptcy!

If you intend to business with partners, consider a corporation or other limited liability entity. It is just as easy to set up for two people as it is for one.

Pitfall #3: Using a Corporation Improperly

A corporation is good, but only if you use it properly. Many people pay an attorney up to $1,000 to setup a corporation, then they take the corporation's minute book and stick it in the closet. A corporation will not shield you from personal liability if you do not follow corporate formalities! Even worse, if the IRS audits you, they can set aside the corporation and hold you personally liable for the taxes!

At least once a year, have your attorney and/or tax advisor review your corporate records and practices.

Pitfall #4: Personal Guarantees

In some situations, such as a bank loan or line of credit, it is inevitable that you must sign personally. However, it is not necessary to give a personal guarantee in every situation, simply because they request it. Often, vendors of your business will request that you sign a personal guarantee of a corporate liability. If they are not extending you credit, you should simply refuse. For example, if a landlord requests a personal guarantee on a lease, offer a larger security deposit instead. Or, you can negotiate so that after two years of prompt payment, your personal guarantee is not necessary.

If you choose to sign personally on an obligation, do not make the mistake of allowing your spouse to co-sign with you. Unless your spouse is involved in your business, there is no reason for a vendor or bank to require your spouse's personal guarantee.

Pitfall #5: Failure to Maintain Adequate Insurance

Don't be cheap. Insurance will protect you in most circumstances. If you keep the minimum insurance, increase the liability limits. You can usually double your liability insurance for a relatively small amount. Keep in mind that if your insurance is not adequate to cover the claim, the injured party can go after your personal or unincorporated business assets for the difference.

Insurance also gives you an attorney in an event you are sued, even if the claim is settled before trial. The duty of an insurer to defend (pay for your lawyer) is much broader than its duty to indemnify (pay for claims against you). Even if the lawsuit is completely bogus, the insurance company will provide you with a lawyer, saving you thousands of dollars.

Pitfall #6: Sexual Harassment in the Workplace

Sexual harassment is another hot issue for the 90's. If you own a company with employees, be aware of what goes on. Even if you don't personally engage in any conduct which is harassing in nature, you can be sued if your company permits a "hostile" environment. Make certain you have written company policies that are given to all of your employees that specifically state that sexual harassment will not be tolerated. Set up an internal complaint and investigation procedure within your company. Immediately investigate and resolve any issues within your company, especially those that involve people of the opposite sex. Be especially aware of these events if you have a company picnic or office party.

Pitfall #7: Using "Independent" Contractors

If you regularly pay "contract" employees, you may be treading thin ice. If your "independent contractor" commits a negligent act and a third party is injured, you can be held liable. The problem with this area of law is that it does not matter whether you thought the individual was an independent contractor or an employee. The law presumes an individual to be an employee by balancing some of the following factors:

- Did the individual work your hours or his?
- Did he use your tools or does he have his own?
- Does he do work for other people, or just for you?
- Did you personally supervise the work?
- Did you pay him daily, weekly or upon completion?
- Was there a written contract?

These are only some of the factors, but you can get a general idea of what factors are relevant. If the court considers the individual to be your employee, you are responsible for his actions.

Pitfall #8: Failure to "Get it in Writing"

Always leave a paper trail. Whenever you speak with someone at a company, the IRS or any governmental organization, get it in writing. If they won't give it to you in writing, send them a "self-serving" follow-up letter summarizing your conversation. Their failure to object to its contents may be deemed an admission of what the letter states. Keep a copy in your file in case to have to prove the oral conversation in court.

Remember, it's not what happens, it's what you can prove in court (also known as the "O.J. Rule")! The written word is your most powerful weapon in Court - use it.

Pitfall #9: Opening Your Mouth too Wide

If you are involved in what could potentially be a lawsuit, think before you act. Do not write offensive letters to your adversary stating your legal positions. Successful litigation involves some element of surprise. State firmly, but vaguely, that you intend to pursue your legal remedies . . . that's all!

Pitfall #10: Owning All of Your Assets in One Business Entity

Don't place all of your eggs in one basket. While a corporation or limited liability company may shield your personal assets from business liabilities, it will not shield the business's own assets. If your business entity has a substantial amount of debt-free equipment or real estate, consider spreading out the risk. Create one or more corporations or limited partnerships to hold title to the assets, then have your business lease the assets back.

John D. Rockefeller once said, "Own nothing, but control everything." The more assets your business owns, the more likely it will be sued.

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