

Small Business, Big Needs

During tough financial times, small firms look to their lawyers for wide-ranging expertise to pilot them through rough waters.

By Barry Rascovar
Illustration by Peter Ferguson

As the United States tries to claw its way out of the worst economic collapse since the 1930s—not with a V-shaped bounce-back as politicians had hoped but with an aching slow U-shaped recovery bordering on a double-dip recession—small businesses continue to feel the pain.

Firms with annual sales of less than \$10 million were hit the hardest during the Great Recession, losing a combined \$2 *trillion* in profits. These smaller companies accounted for almost 60 percent of the nation's layoffs, according to Barlow Research Associates' Quarterly Economic Pulse Survey.

While monthly unemployment figures are wavering up and down and big businesses are cautiously hiring, small-sized firms remain in the doldrums. It's what Steve King, a partner at the California consulting firm Emergent Research, calls a "trickle-down economic recovery" with large corporations "leading the way and small businesses lagging and mired in the downturn."





For those in the legal field, representing small firms requires broad legal skills even in boom years. It becomes even more of a test for these attorneys when the economy tanks. What can they offer small clients who are struggling to stay afloat?

Since small businesses lack in-house counsel or personnel offices, the attorney's job often covers a wide array of topics. "You have to hone your skills," says Michelle Harner, a professor at UM Carey Law and co-director of the Business Law Program, "so that you know what to be sensitive to in order to meet the client's needs."

"It's a more intimate scale for the attorney, who must quickly understand the client's story and anticipate the needs and potential problems."

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Aaron Ghais '96, a business transactions lawyer with Shulman, Rogers, Gandel, Pordy & Ecker in Potomac, Md., has found this to be true. "Small firms need the most hand-holding. You educate them to business realities," he says. One of his clients recently sought institutional financing from angel investors for the first time. Ghais coached the client on what was about to happen. "He had no idea of the financial process. He had no idea what he should agree to or how much control to give to the investor group."

"Lawyers are referred to as counselors for a reason," says Anirban Basu '03, chairman and CEO of Sage Policy Group, an economic and policy consulting firm in Baltimore. "Most attorneys who have small-business clients also work with larger clients. This gives them a very broad view of business and the economy and puts them in good position to counsel smaller companies."

In a recession, says Stephen A. Goldberg '76, a general business lawyer with Gallagher, Evelius & Jones in Baltimore, small owners are desperate for advice from a trusted source. "It's ironic that the more a company's business is off, the more the owners need your help. You have to work even more closely with the client—and know the company better than you ever have before."

"A recession is a squeeze on money," he notes. A small company loses customers; payments arrive late, if at all, and banks tighten their financing. Yet employees—and the government—must be paid and material purchased. "Do you advise the client to sue his best customers? Will that help or hurt in the long run?" Goldberg says he might suggest ways to keep financing in place through additional collateral or negotiations with the bank. Or he might offer ways the owner can lower expenses so the firm can tread water. "It's a case-by-case situation," he says. "If you have a collaborative relationship with the client, your suggestions will be welcomed."

It's particularly important during tough financial times for the small-business lawyer to play multiple roles, agrees Carolyn Jacobs '85, who practices health-care law with Rifkin, Livingston, Levitan and Silver in Towson, Md. Questions pop up on a wide range of topics, such as employment law, workers compensation, tax implications, state and federal regulations, contract law, insurance issues, corporate law, and—in the end—bankruptcy law. All of this makes it crucial for any attorney representing a small business "to have a generalist mentality."

If a medical practitioner, for instance, is setting up a practice, Jacobs says she will establish the doctor's corporate entity, review office and equipment leases, advise the doctor on malpractice insurance as well as "slip-and-fall" insurance, submit regulatory filings, and raise personnel and tax issues.

As the economic cycle heads south, Jacobs' tasks change. She may become "an old-style counselor"—suggesting ways for the physician to economize by outsourcing parts of the

business, trimming staff, reorganizing benefits, or taking on a partner.

If income continues to decline, she might raise unpleasant options like merging with a larger medical group or selling the practice to a hospital.

“Your job is to be the cynic,” she says. “You have got to look ahead for the client.”

Hands-on Experience for Students

At UM Carey Law, elements applicable to smaller firms are embedded in many courses, such as Business Associations, Tax Planning, Employment Law, the Intellectual Property Survey course, and the Intellectual Property Clinic, which works with entrepreneurs and technology start-ups.

“We see a lot of small biotech companies, computer software companies, Internet-based firms, companies in electronic and mechanical arts, and firms selling consumer products,” says School of Law Associate Professor Patricia Campbell, who is director of the UM Carey Law’s Intellectual Property Legal Resource Center in College Park. Twelve students participated in the School of Law’s IP Clinic this summer, where they worked on preliminary patent and trademark matters for small businesses seeking help.

During the most recent recession, “there’s been a marked increase in our number of clients,” says Campbell. “We have many more than we can assist. There are so many people out of work who are looking to start a new business. I could easily keep five to 10 more students busy this summer.”

On-the-ground legal training while at UM Carey Law has become much more important to students, as legal practices face their own recession-related constraints, according to Campbell.

“It used to be that law firms wouldn’t expect much in the way of practical skills from their new attorneys for a few years,” she says. “Now, they want attorneys who know what they are doing and can create value right away. They demand real, practical experience.”

Playing Outside the Box

Christopher Steer ’01, a business partner at PA & Associates of Timonium, Md., a company that helps negotiate lower shipping rates for large and small companies, says his legal training has given him ideal skills to help clients weather rough seas.

“In law school, you are taught to adapt, to think critically and strategically. You are taught to solve problems. Those are the same skills you need in business”—especially in a recession.

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“Lawyers underestimate themselves,” he says. “They are really powerful when they must be creative” for clients during difficult economic periods. “You crystallize your focus on how to improve the company. You focus your attention on the core business and develop ideas.”

Basu notes that lawyers often “invest their intellectual capital” analyzing basic aspects of how a business is being run, not only “to protect the organization from harmful litigation,” but also to provide strategic advice clients might overlook.

The key, notes Campbell, is for attorneys advising cash-strapped small companies “to make smart decisions and deliver value to the client.”

“Start-ups and small, family-run companies have very limited resources for attorney fees,” she says. This means the lawyer might file just one patent application right away rather than four separate ones, to save the company money. The attorney “must minimize the time spent on certain legal matters” and perhaps consider a reduced fee until the company is in better financial shape.

Entrepreneurial firms are thinly capitalized. In a recession, they can't afford big legal bills. “It's a bit of a challenge,”

Modernizing the Maryland LLC

In 1992, Maryland became the fifth state to create an unincorporated form of business known as a limited liability company. “People were skeptical of the LLC's value,” recalls Marshall Paul '72, a co-author of the statute.

Today, the LLC is ubiquitous, especially among small businesses. According to Paul, a partner at Saul, Ewing in Baltimore, the LLC “has become the most widely used form of business organization in this country.”

And why not? It fits the needs of smaller companies. The LLC Act is simple, practical, and straightforward. As Michelle Harner, UM Carey Law professor and co-director of the Business Law Program, notes, “It gives you the flexibility of a partnership, but the partners generally have limited liability absent wrongful conduct.”

To keep pace with business trends and court rulings, the original statute has undergone fine-tuning from time to time. Last year, the Maryland State Bar's Committee on Unincorporated Business Associations offered comprehensive revisions to the LLC Act that were approved in April by the Maryland General Assembly.

The changes remove “ambiguities and uncertainties that created some confusion,” says Harner, who served as vice-chair of the bar committee. “We wanted to make the LLC Act more user friendly.”

One of the revisions places added emphasis on the validity of an LLC member's operating agreement, regardless of the language of external contracts. “If the parties take the time to negotiate a contract, we should respect the results between those contracting parties even if it is not what we would have done,” says Harner.



Ghais admits. He says attorneys must make their own business decisions about a client's prospects and whether it is worthwhile to defer payment, not bill the full amount of hours worked, or write off the account.

Steve Goldberg sees a silver lining in economic hard times for smaller legal firms. "In prosperous years, there's a box everyone must play in." But during a recession, he says lawyers "can play outside the box because the normal rules of financing don't apply. You have to look for ideas that work, not simply what's typical." Lawyers can use their creativity and analytical skills to great advantage.

Ghais, for one, finds working with smaller companies and start-up entrepreneurs invigorating—and, in a recession, challenging. "One of the fun things is the variety of legal work you do for small companies. The owners involve you much more in the business end of things. They bounce ideas off you

and you can throw out suggestions, too. You're not confined to one narrow aspect of the law."

Steer concurs. "In a recession, you get to use that great adaptive quality of the legal mind," he says. "You can be strategic and help business owners solve their problems."

Adds Basu, "The best lawyers view their role as broader than legal matters. They help the client see the bigger picture and that there is light at the end of the tunnel—even when the client sees only darkness." ■

Two other key enhancements to the LLC Act are as follows:

- **The rights of creditors are refined.** They can obtain a charging order to collect a partner's distributions, but the creditors do not gain voting rights in the LLC. "We didn't want one member's creditors having the ability to affect other members' interests in the business," Harner says. Creditors obtaining a charging order against a single-member LLC, though, can take over the business and liquidate its assets.
- **A partner's voting rights are not automatically passed along, protected or retained.** When a partner assigns his economic interests in an LLC to a third party, the partner's voting rights are not included. That requires approval from the other LLC members. "If there is a change of business partners in

ownership, all have to agree to it," adds Harner. "Since the old partner no longer has any economic rights, why should he retain his voting rights?" explains Paul.

With these and other modest changes to Maryland's LLC Act, Paul and Harner believe the form of business entity most favored by smaller companies continues to make a great deal of sense.

—Barry Rascovar

