

5 Common Mistakes Every Entrepreneur Should Avoid in 2015

Partner Gary Schall and Counsel John Demeter, WilmerHale:

Making mistakes is part of the learning curve of launching a startup. Most errors can be fixed without any major impact on your business, but some that seem like no big deal can have serious implications.

Seemingly innocent gaffes can be a red flag to potential investors. In the worst-case scenario, they can cost you so much time and money to fix that they can drag your whole company under.

Are you at risk of making any of these mistakes?

Blowing off payroll. Before you bring employees on board, you need a payroll system that can handle required employer withholdings and make quarterly payments and contributions for Medicare and Social Security. You need signed I-9 forms on file affirming that all workers are cleared for U.S. employment. And you need to comply with state and local laws, too. Those in New York should note that the state is particularly aggressive when it comes to workers' comp insurance and has been known to levy fines and penalties in the five figures for failing to purchase mandated coverage. And did you know that the city of San Francisco requires employers to provide health insurance?

Consult a CPA or accounting advisor to avoid payroll problems and an unwelcome letter from the IRS or state or local tax or regulatory authority.

Unpaid interns. Wouldn't it be great if eager college students provided free labor in exchange for the amazing experience of seeing your dynamic startup in action? It's tempting, but don't go there.

Qualifying college students as unpaid interns can be difficult to do. They must meet several criteria based on applicable law, like working in an educational environment and receiving college credit. Even if they sign a document affirming that they agree to work without pay and are not claiming to be employees, you're not off the hook.

Wage claims cannot be waived, so these unpaid interns can later sue you for back pay. If they pursue unemployment benefits or a worker's comp claim, your business's employment records and tax payments can be scrutinized by state and



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federal agents. The IRS can hit you up for unpaid taxes and impose penalties and unpaid taxes steep enough to shutter a cash-poor business.

Pay your interns minimum wage. Then you'll have a clean conscience when you send them on a latte run.

Selling unregistered securities. Before you can sell securities (such as stock or convertible notes) to anyone, you must do one of two things: file a registration statement with the U.S. Securities and Exchange Commission with the mandatory disclosures that protect investors, or find an exemption from those requirements. And that's just at the federal level. You must also comply with laws governing the sale of securities in every state where your investors are based, not just where your startup is.

Fail to do this and investors can legally demand a refund of their investment — money you might have already spent. You could also face fraud charges for failing to disclose adequate information about the sale of unregistered securities.

Before you offer to sell your securities to your business school buddies, consult a trusted legal advisor to be sure you're complying with state and federal securities laws.

Paying employees "later". Founders sometimes tell us they have a handful of employees who will be "paid" with stock options or who will receive a salary when some funding comes through. Whoa. All workers by law must receive at least minimum wage or a minimum salary if they are exempt employees.

If at all possible, bring on these early workers as consultants or contractors — and treat them as such by not defining their workday or how they do their job, for example. It's fine to "pay" those consultants with stock.

"Borrowing" material. You need a privacy policy and terms of use for your website. Instead of paying a lawyer to draft these documents, founders sometimes just lift the boilerplate text from their competitor's website.

We know an entrepreneur who tried this. He came to see us after he received a nasty letter from his competitor's attorney threatening legal action if he didn't take down the pirated text. He learned that copyright law protects even dull legal jargon when it's published in most media. We drafted a unique privacy policy and terms of use for his site and responded to the letter.

Bite the bullet and pay for legal advice before you get into trouble. Or prepare to pay more to dig yourself out later.

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