# CONTRACT ROULETTE: THE TOP FIVE AGREEMENTS THAT GET BUSINESSPEOPLE IN TROUBLE

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You can do a lot of damage with a signature. You can go broke.

It's scary how many entrepreneurs play contract roulette. They sign a terrible agreement. Nothing bad happens. So they just keep signing until something blows up—like their business.

Some agreements go boom more often than others. Ever since Eve and the serpent signed that infamous catering agreement, the following five contracts have caused the most disasters:

## 5. Leases

Most execs spend more time picking their carpet and paint than they do reading their lease. Who can blame them? Most leases are 60-page tomes with no pictures. So they think/hope, "It's all standard. Everybody signs these things." Careful, now. There are a lot of gotcha-clauses in all of that fine print. The landlord may be able to veto the sale of your business. Or, you may have to pony up a small fortune in additional rent when the landlord finally decides to fix all of the code violations in the building. Worse, plenty of landlords want the ability to "renovate" your building. You and I would call it "demolish and rebuild." They turn the property into a construction site—while you're still in it. In one case, the landlord ripped off the exterior walls of a posh office building and tacked up plywood boards for a year or so. All day, trucks beeped, compressors clanked and workers jackhammered (interrupted only by everyone's favorite heavy metal band during worker breaks). All the amenities of a door-less porta-potty, but the same high rent! The tenant's signature on the lease pretty much wiped out any ability to complain.

Here's the lesson of 1,000-plus lease negotiations squeezed into a simple winning formula: Read the entire, miserable, infuriating screed. Revise it so that it is acceptable to someone with a functioning brain. Get at least one backup location. Start early enough so you can credibly threaten to walk away from a bad deal and move on to a good one.

## 4. Loan Agreements

You think you're just borrowing money. But, if you hold the loan agreement up to the light, the watermark says "Hostile Takeover." Surprise! You sign and now the bank controls your business.

In good conscience, I can't even recommend that you read the loan documents. They weren't meant to be understood. Take a random page and give it a try. Then give that same page to your dog. Neither of you is going to get much out of it, unless your dog likes to chew on paper.

The average loan agreement is long, complicated and burdensome. You make promises about everything. You need the bank's approval to enter new markets, increase inventory, make key hires, and you can't borrow money from anyone else. It turns out the typical mega-lender is like that Tinder weirdo—possessive, insecure and intrusive.

Don't be intimidated because it's a bank. Negotiate! Consult with your advisors and have them help determine what is most important and achievable. Then bargain for changes. You may need to adjust the required financial ratios. Try to limit reserves—they're interest-free dead money held by the bank. Insist that the bank be reasonable with certain approval rights. Cap the bank's open-ended fees. Most of all, get the right to prepay the loan, unless you have a favorable fixed rate. Prepayment is a critical escape hatch.

## 3. Construction Contracts

In Contract Land, construction agreements are the ultimate game of tag. If you're "it," you're liable for everything: injuries at the project site, damage to the work, cost overruns, late work that causes lost rent, lawsuits that try to recover damages for defective work, compliance with building codes, hazmat discovered during excavation, interference with adjacent

buildings, fines imposed for late or loud construction, etc. The list is endless. You make one mistake and your profit is gone. You make a second mistake (a/k/a the "final mistake") and your business is gone.

Construction involves a lot of people with competing interests: the project owner, general contractor, subs, lenders, insurers and investors. Each wants protection and each has a big stake in the outcome. The insurance alone requires a Ph.D. The difference between "named insured and "additional insured" can mean survival or bankruptcy. Some folks just pick up a hammer—or a pen—and hope for the best. Successful businesses do their worrying before they sign, not after. They learn the risks and nail down who is responsible for what. Then they put an "A" team on every project.

**2. Partnership Agreements**

At some point in many partnerships, "partner" feels like "warden" and "partnership agreement" feels like "prison." Partnership agreements are usually prepared when businesses are just being formed. But startups don't have the money or battle scars to get it right. Some common failings:

- Amateur agreements have unrealistic buy-out clauses. But, no matter how you slice the pie, you can't make it bigger. If the business is broke, all the fancy formulas in the world won't generate the funds to buy out a retiring partner. Sometimes your only real option is to close the doors, sell off your assets and pay the bills. It's not a sign of weakness to admit things might not work out. Plan for the good—and the bad.

- Don't treat all partners as if they're equal when they're not. For example, an investor and famous chef become 50/50 partners in a new restaurant named after the chef. Their partnership agreement solves any deadlock by giving the business to whichever partner is willing to pay the most for the business. Like 97.3% of all restaurateurs, they have a falling out. The restaurant CANNOT survive without its namesake chef. So, the chef can lowball the investor and still win the business. Equal isn't always fair.

**1. Personal Guarantees**

When disaster strikes, only three things survive: rats, cockroaches and personal guarantees.

Most personal guarantees never die. That longevity makes them the number-one contract that gets businesspeople in trouble.

Owners sign personal guarantees in the early days of their business when they don't know any better or don't have any other choices. If they're lucky, the business grows. Time goes by and they get even luckier. They sell that business for a ton of money. But, often, they forget something—that old guarantee. Long after the sale, maybe they're sitting at the club, and they hear the business has taken a bad turn. Somebody else's problem, right? Not so fast. You're still liable on that guarantee. Even years later, most guarantees are just as dangerous as the day they were signed. Plenty of guarantors find out the hard way. They write big checks to make the mess go away.

There are solutions. Don't sign a personal guarantee in the first place. Instead, provide some collateral, such as escrowing cash with the lender. Whatever you do, insist on termination of your guarantee if you sell. Make the buyer put up a new guarantee or some other collateral, if required. Sure, plenty of businesspeople are nervous about rocking the boat when they sell. But, there is a lot to be gained by getting rid of an obligation that can—and regularly does—rear its head and bite you years later.

It's your signature, not an autograph. Be careful what you sign.

## ABOUT JACK GARSON

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Jack Garson's practice focuses on Real Estate, Construction and Business law. He serves as a legal advisor for numerous local, regional and national companies. In his role as legal counsel, Jack also serves as a strategic advisor and lead negotiator. Further, Jack provides guidance on the structure of complex transactions, the resolution of business disputes, the growth and sale of companies, and the management of issues such as liability and risk reduction, employment practices, and enhancing profitability.

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In the past two years, we've grown by 50% through expansions in New York City and, most recently, Charlotte, North Carolina. This growth has provided immense value to our clients and attorneys.

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