Legal Thought Leadership

2023

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Table of Contents

FTC Proposes Rule to Bar Non-Competes for Employees .... P. 3

What You Need to Know About Disclosure Schedules .... P. 4

Is Phantom Equity a Security Under North Carolina Law? .... P. 6

Dissolution of a North Carolina Corporation .... P. 8

The Power and Perils of Spousal Privilege .... P. 10

The Difference Between Private Equity and Venture Capital .... P. 13

What is a Letter of Intent? .... P. 15

The Corporate Transparency Act: A Brief Primer .... P. 17

Federal Rules of Evidence (FRE) 702 Update .... P. 19

Clickwrap Agreements and Why Your Website Needs Them .... P. 22

January 10, 2023 | By: Alex Nibert & Jessica Shoop

FEDERAL TRADE COMMISSION PROPOSES NEW RULE TO BAR NON-COMPETES FOR EMPLOYEES

On January 5, 2023, the Federal Trade Commission (FTC) issued a notice of proposed rulemaking that, if adopted, would prohibit non-competes in most circumstances.

The FTC's rule proposes to ban non-competition clauses in employment agreements as "an unfair method of competition," rendering such clauses unlawful under Sections 5 and 6(g) of the Federal Trade Commission Act. The proposed rule would apply with equal force to traditional employees, independent contractors, and unpaid workers including volunteers and interns. The proposed ban would also apply retroactively, requiring employers to rescind any non-compete agreements previously entered into before the final rule's effective date, and mandating that employers issue a notice that any non-competition agreement between the employer and employee would not be enforced against the employee.

While this is an aggressive move by the FTC, Employers need not panic. The notice of proposed rule-making is only the first stage in a multi-step process required before any rule will go into effect. The FTC will accept comments on the proposed rule for 60 days after it has been published in the Federal Register. At the conclusion of this notice-and-comment period, the FTC will then publish a final version of the rule. Employers will be given 180 days after the implementation of a final rule to comply.

In addition to this lengthy rule-making process, we anticipate significant legal challenges to the rule, which could also delay any final implementation and enforcement.

JAH Can Help

Our **Labor and Employment Practice Group** is closely monitoring these developments. For questions about the FTC's proposed rulemaking or non-competition agreements, please contact any member of **JAH's employment attorneys** or complete our **General Contact Form**.

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February 03, 2023 | By: Bill Zwicharowski

WHAT YOU NEED TO KNOW ABOUT DISCLOSURE SCHEDULES

Disclosure schedules are more than just a helpful medium for parties to provide and receive information regarding details of a seller's business. Disclosures made or omitted by a seller in disclosure schedules have legal and practical consequences for both the seller and the buyer. From a seller's perspective, failure to disclose material information to the buyer could result in money damages or worse, and from a buyer's perspective, these schedules can alert buyers to potential red flags about the business and give the buyer an opportunity to negotiate additional protections and concessions.

What Are Disclosure Schedules?

Disclosure schedules are critical to a purchase agreement in an M&A transaction. Disclosure schedules are attached to the purchase agreement to supplement, qualify, and disclose exceptions to representations and warranties made in the purchase agreement. Although it is the due diligence process that largely acts as the opportunity for the buyer to obtain information about the inner workings of the seller's business, the disclosure schedules officially memorialize key aspects of the business in a legally binding way. For example, a disclosure schedule could be used to supplement a representation addressing material contracts of the seller by listing all material contracts and providing key details regarding those contracts. Alternatively, a disclosure schedule could be used to qualify a warranty. For example, a purchase agreement might warrant that, except as provided by a certain disclosure schedule, the seller does not have any outstanding tax liability. The seller discloses any known outstanding tax liabilities on that schedule to memorialize the disclosure and assure all parties are aware of the warranty exception. Thus, disclosure schedules give buyers vital details about the operations, assets, and liabilities of the entity it seeks to acquire and gives the seller the space to disclose those details in order to protect itself.

Why Are Disclosure Schedules Important?

Disclosure Schedules matter because they supplement and provide exceptions to the representations and warranties which themselves are linked to potential liability to the parties. Revisiting the example above, the seller could warrant in the purchase agreement that it did not have any outstanding tax liability, except as provided on a certain disclosure schedule. If the seller then properly listed any outstanding tax liabilities on the disclosure schedule, the seller would not be in breach of the warranty. If, however, the seller did not include that caveat to the warranty or included the caveat but failed to properly list all outstanding tax liabilities, the seller could be in breach of the warranty. Disclosure schedules are thus a powerful tool to protect a seller but only if properly

utilized. From a buyer's perspective, disclosure schedules give the buyer a level of detail about the seller's business that cannot practically be included the purchase agreement. Moreover, as discussed above, disclosure schedules give buyers grounds for recourse in the event that a seller omits or misrepresents information in connection with representations and warranties.

Common Pitfalls and Helpful Considerations

Many clients have the understandable misapprehension that information disclosed during due diligence does not need to also be included in the disclosure schedules. This is not the case—these schedules provide the crucial and final written record of key disclosed information. Accordingly, preparing these schedules can be time consuming and detail intensive, but it is vitally important. Common mistakes include providing incomplete or outdated information, failing to coordinate with appropriate employees or others that could have relevant information, failing to understand the full scope of the representation or warranty, or simply overlooking responsive information. To avoid these pitfalls, it is helpful to work with experienced counsel in order to understand the purpose, scope, and implications of disclosure schedules and properly prepare them.

JAH Can Help

The **attorneys at JAH** are available to counsel you on all aspects of your merger, acquisition, sale, or disposition, including the preparation of disclosure schedules. **Our corporate attorneys** specialize in navigating the details with precision and tackling other complications surrounding M&A deals so that you don't have to. **Click here to contact a member of our Corporate Group if you are in need of assistance.**

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March 06, 2023 | By: Corporate & Nonprofit Practice Group

IS PHANTOM EQUITY A SECURITY UNDER NORTH CAROLINA LAW?

Phantom equity (also referred to interchangeably as “phantom units” or “phantom stock”) has been utilized in recent years by companies who wish to motivate their employees by issuing them contractual rights to a share of company profits (often upon a triggering event such as the sale of the company). Phantom equity provides some of the **benefits** to the employee of owning real equity, while the employer avoids granting actual equity to the employees. Granting “real equity” can potentially require owners to give up voting power, require sharing of company financials with the investing employees, create fiduciary duties to the employee, and/or provide other rights and responsibilities to the employee. Phantom equity has arisen as a mechanism to avoid some of the negatives of issuing real equity for employers while still providing employees with owner-like economic benefits. What is not always certain, however, is whether phantom equity is a security under federal and state securities laws. If phantom equity is a security, employers may be subject to registration requirements upon the issuance of phantom equity and employees may have access to causes of action against their employer under federal and state securities laws. The North Carolina courts recently in *Higgins v. Synergy Coverage Sols., LLC, 2020 NCBC 4 (North Carolina Business Court, 2020)* ruled as a case of first impression that phantom equity is generally not a security under North Carolina law.

Higgins v. Synergy

In *Higgins*, **litigation** arose from the termination of plaintiff Arlene B. Higgins from her **employment** with Synergy Coverage Solutions, LLC. *Id.* at *4. One of the plaintiff’s numerous claims against her former employer was a claim under the North Carolina Securities Act (“NCSA”). *Id.* at *79. The defendant moved to dismiss this claim under the theory that the phantom stock the plaintiff had purchased from the defendant was not a security under the NCSA. *Id.* The court noted that phantom stock is not listed as a security in the North Carolina statutes and that no North Carolina court had addressed whether a phantom stock is a security under the NCSA. *Id.* at *80. Turning to federal guidance, the court noted that “several federal courts have persuasively reasoned that phantom stock is not ‘stock’ under federal securities laws because it does not grant the holder equity.” *Id.* at *85. Utilizing this reasoning, the North Carolina court concluded that “the Phantom Units [do not] represent ‘real equity’ in Synergy Holdings. Rather, the Phantom Units are instruments that are assigned value under a formula provided in the Plan upon the sale of Synergy Holdings at or above a certain price . . . . As such, the Phantom Units are not ‘stock’ within the NCSA.” *Id.* at *86. The court concluded, “Higgins has failed to plead that the Phantom Units constitute a ‘security’ under the NCSA. Plaintiff’s NCSA claim must therefore be dismissed for failure to allege an offer or sale of a

security under the statute." *Id.* at *91. It is important to note that the facts and circumstances of each particular case, as the court references in *Higgins*, can play a large role in determining whether phantom equity is considered a security. Moreover, although *Higgins* speaks to the North Carolina treatment of phantom equity, the court did not ultimately address the also looming question of how a federal court would treat the phantom equity under federal securities laws. Accordingly, this article does not in any way address this question of federal law.

JAH Can Help

The **attorneys** at JAH are available to counsel you on your phantom equity plans, including assisting you with drafting your plan in a manner intended to avoid treatment of your company's phantom equity as a security. Our corporate attorneys will navigate these and other complicated legal concepts so that you don't have to. Click here to contact a member of our **Corporate Group** if you are in need of assistance.

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April 19, 2023 | By: Iyanu Lipede

DISSOLUTION OF A NORTH CAROLINA CORPORATION

At times, entities and shareholders are faced with the decision to terminate the existence of a corporation. Voluntary dissolution is the process by which shareholders and directors may do so, and while the complexity of closing down a business may depend on the complexity of the business, North Carolina statutes set out specific procedures to voluntarily dissolve and terminate a corporation's existence with the North Carolina Secretary of State. It is important to understand the proper steps for corporation dissolution to properly protect shareholders from potential claims related to the corporation.

What Steps Must I Take to Dissolve my Corporation

To effectively dissolve a corporation under North Carolina law, a corporation must file Articles of Dissolution with the North Carolina Secretary of State. If the corporation has not yet issued any shares, the board of directors or a majority of the incorporators of the corporation deliver these Articles to the Secretary of State. N.C.G.S. § 55A-14-01. If the corporation has issued shares, the board of directors must recommend the dissolution to the shareholders, and the shareholders must approve the dissolution with a written resolution. N.C.G.S. § 55A-14-02. After shareholder approval, the Articles of Dissolution may be delivered to the Secretary of State. The Articles of Dissolution contain information, such as the name of the corporation and the date the dissolution was authorized. N.C.G.S. § 55A-14-04. Usually, the dissolution is effective upon filing; however, an entity can prescribe a later date of dissolution in the articles of dissolution.

What Happens After Dissolution

A dissolved corporation continues its corporate existence but may not carry on any business except actions appropriate to wind up and liquidate its business and affairs, including paying its creditors, distributing property to its shareholders, filing final tax returns, and other necessary business incidental to winding up and liquidating. N.C.G.S. § 55A-14-06. Some may be surprised to learn that even after liquidation, the formalities of the corporation such as quorum or voting requirements for board of directors or shareholders continue. *Id.* Additionally, a dissolved corporation can continue to operate its bank account and contract with professionals such as CPAs and attorneys for the purpose of winding up its affairs. As part of this process, it is also recommended that a dissolved corporation file Form 966 with the IRS, notifying them of the dissolution. After dissolution, a corporation is generally expected to pay all its existing debts and then liquidate its remaining assets to its shareholders. This sometimes becomes difficult, however, where there are unknown claims that may exist against the corporation. If a corporation distributes its assets to its shareholders and is later

subject to such a claim, the shareholders could be responsible for paying the claim of the corporation despite the limited liability nature of corporate ownership. However, North Carolina law limits such potential liability where a corporation publishes notice of its dissolution in a public newspaper and a claim is not made within five years of such publication date. N.C.G.S. § 55A-14-08.

JAH Can Help

Dissolution of a business may not be an easy decision, and the procedures can be complicated. The **corporate attorneys at JAH** are available to assist you with the procedures and filings needed to effectively dissolve your corporation in a manner that best protects you. **Click here to contact a member of our Corporate Group** if you are in need of assistance.

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May 04, 2023 | By: Grace Ketron and Kim Kirk

THE POWER AND PERILS OF SPOUSAL PRIVILEGE

Privilege is a powerful litigation tool. Documents, conversations, and communications can all be protected by privilege under the right circumstances. Privilege, however, comes in many shapes and sizes, so understanding the basics of privilege is crucial for determining whether a specific document, conversation, and/or communication is covered. Without a proper understanding of when privilege does or does not apply, certain documents, conversations, and communications may ultimately be admissible in court. A recent North Carolina Business Court decision highlights both the powers and perils of attempting to claim spousal privilege.

In *Futures Group, Inc. et al. v. Brosnan*, 2023 NCBC LEXIS 25, 2023 NCBC Order 9 (N.C. Super. Ct. Feb. 10, 2023), the North Carolina Business Court considered whether spousal privilege applies to "two recorded conversations" from November 9, 2017, and March 1, 2020, that a wife "had privately with" her husband during their marriage. Unbeknownst to the now ex-wife, the conversations were "record[ed] surreptitiously." The ex-wife, a non-party to the lawsuit, argued that the conversations were "confidential marital communications protected by North Carolina's spousal privilege." In contrast, the plaintiff suggested the conversations were "not privileged and that [the ex-wife], as a non-party, lacks standing to contend otherwise." The Court, therefore, analyzed whether surreptitiously recorded private conversations between a husband and wife are covered by North Carolina's doctrine of spousal privilege.

Spousal Privilege in North Carolina is Sacred

The Court first emphasized the sacredness of spousal privilege in North Carolina. Spousal "privilege is 'premised upon the belief that the marital union is sacred and that its intimacy and confidences deserve legal protection.'" Spousal privilege is also intended to foster trust between spouses, so spouses need not fear that private conversations had during the marriage will be weaponized in later court proceedings. Spousal privilege even goes so far as to protect "communications that occur during the marriage even after the marriage ends." N. C. Gen. Stat. § 8-56 further solidifies North Carolina's commitment to protecting spousal privilege by codifying that "[n]o husband or wife shall be compellable to disclose any confidential communication made by one to the other during their marriage."

What is Spousal Privilege?

North Carolina's doctrine of spousal privilege relates to: "(1) communications between spouses during marriage, (2) that are intended to be kept confidential, and (3) are 'induced by the marital relationship

and prompted by the affection, confidence, and loyalty engendered by such relationship.'" It is important to note that this privilege does not cover any and all communications had between spouses during a marriage, but it does cover a significant amount of communications, so long as the communications (1) occur between the spouses (2) during the course of the marriage and are (3) expected to be confidential based on (4) the spouses' marital relationship and affection, confidence, and loyalty to each other. It is important to note that spousal "privilege may not be waived by one spouse alone. Both spouses hold the privilege, and one may prevent the other from revealing protected communications."

Who Can Claim Spousal Privilege and When?

The Court subsequently made three determinations regarding the applicability of spousal privilege in this case. First, the Court found that the ex-wife had standing to argue against the use of the recordings in open court. The Court explained, "Even though she [i.e., the ex-wife] is not a party to the action, Aimee's assertion that the communications she had with her husband were private, reflected in her objection on grounds of the spousal privilege, gives her a personal stake in a justiciable controversy." The ex-wife, therefore, had the standing, or authority, to contest the use of the recordings.

Second, the Court analyzed whether the November 9, 2017 recording was privileged. During the conversation, the ex-wife clearly indicated that she wanted her ex-husband "to tell her father about her concerns." Essentially, the ex-wife wanted to loop others into the details of this specific conversation. Because the ex-wife herself was not planning to keep the communication private, such communication was not protected by spousal privilege.

Third, the Court analyzed whether the March 1, 2020 conversation was covered by privilege. During this conversation, the ex-wife did not suggest that she wished for others to know about the conversation or that she had previously discussed the same with anyone else. In fact, it was not apparent whether her father later knew anything about the contents of this conversation. The ex-wife also made statements during the conversation which emphasized her belief that the conversation was and should remain confidential. As such, the recording was inadmissible because the ex-wife's own statements indicated that, at the time of the conversation, she thought the conversation, "was, in its entirety, a confidential marital communication."

JAH Can Help

Navigating the powers and perils of privilege, whether spousal or otherwise, can be a complicated endeavor. If you have questions about what does or does not constitute privilege, please reach out to our **litigation team** or complete our **general contact form**.

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May 18, 2023 | By: Bill Zwicharowski

WHAT IS THE DIFFERENCE BETWEEN PRIVATE EQUITY AND VENTURE CAPITAL?

The terms private equity and venture capital are often used interchangeably, but if your company is looking for investors, whether you should pursue private equity or venture capital investors can differ depending on the type of company and your long-term goals.

What is Private Equity?

Private equity refers to ownership of, or an interest in, a company that is not publicly traded or owned. Private equity investors generally seek out mature, established companies and acquire a majority, controlling interest. Private equity investors may seek out businesses in distress or businesses that are successful but that could benefit from increased efficiency or further resources. Because private equity investors usually acquire a controlling interest, they tend to be more hands on in the management of the business, seeking to spearhead changes to increase profitability, often including streamlining the business and making leadership changes. The goal for most private equity investors is to sell the business, with its improved operations, for a profit. Thus, private equity investors tend to focus on short-term value maximization to ensure a return on their investment.

What is Venture Capital?

Venture capital refers to financing invested in startups or smaller companies, generally closer to their infancy, that show significant growth potential. In this sense, venture capital is actually a subset of private equity. Venture capitalists tend to acquire less than a majority interest in the business. As such they can still lend their expertise, but have less control and may have less of a hand in the day-to-day business. Further, because venture capitalists seek out young, growing companies, they tend to be more interested in the long-term value of the company. An “angel investor” is also a specific type of venture capital investor. Typically, this term refers to an individual who invests their own money in startups, rather than through a capital company owned by a group of investors. Angel investors may invest earlier than other venture capital in a startup and may exit earlier as well, as they focus on the early-stage funding for startups.

What Are the Key Similarities and Differences?

- Because venture capital is a type of private equity, both are forms of investments in privately held companies with the goal of increasing the value of the company and making a profit.

- Private equity investors tend to invest in older, more established companies that have the potential to increase profitability with the help of investors. On the other hand, venture capitalists tend to invest in young, growing startups with unproven, yet promising, value.
- Private equity investors generally seek to acquire a controlling interest in a company, while venture capitalists generally acquire a minority share of a company.
- Private equity investors are more likely to be involved in the decision making of the company and to be more hands on. Venture capitalists, by contrast, may be more hands off, especially with day-to-day matters.
- The goal for private equity investors tends to be more focused on maximizing the value of the company in the short-term with the intent to sell the company once it has done so. On the other hand, the goal for venture capital investors tends to thinking about value in the long-term with the intent to maintain equity until the company reaches a good cash-out event such as going public. As such, venture capitalists are long-term investors who aim to get in early on company with long-term potential.
- While both types of investments are riskier than investing in established publicly traded companies, venture capital investments tend to be riskier for investors than general private equity given the volatile nature of startups. About 90% of startups fail, so venture capital investors expect that the majority of their investments may not pan out. In contrast, private equity targets more mature companies that they hope to purchase on a discount, providing for more opportunity to turn a profit.

JAH Can Help

Working with private equity or venture capital investors can be a challenging but exciting prospect. The experienced **corporate attorneys** at JAH are available to counsel you throughout the investment process, ensuring that your business is protected and its value is maximized. **Click here to contact** a member of our **Corporate Group** if you are in need of assistance.

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July 11, 2023 | By: Benjamin Hopkins

WHAT IS A LETTER OF INTENT?

A Letter of Intent (sometimes called a Memorandum of Understanding or an "LOI") is generally a non-binding agreement between a seller of a business and a prospective buyer. It commonly includes a proposed price, the structure of payment (cash up-front, promissory note, etc.), the nature of the sale (asset sale, stock sale, or merger), closing conditions, and expected timelines. While most terms are non-binding, LOIs do include a few important binding terms, such as confidentiality, exclusive negotiation rights for the buyer, and terms governing buyer's rights to information to conduct due diligence. LOIs set the groundwork for more substantive negotiations to come. Although they are mostly non-binding, sellers should not make the mistake of agreeing to the buyer's initially proposed terms without engaging an **attorney** to help negotiate.

Why Do I Need a Letter of Intent?

In most cases, buyers will not engage in negotiations to purchase a business without first executing an LOI. Buyers send sellers an LOI as a way to express interest in purchasing the business but also to protect themselves by locking the seller into negotiations with the prospective buyer. Although the LOI's terms are generally non-binding, they do set the tone for future negotiations, so the buyer has an interest in keeping the key terms short and vague so that they can easily update them as the deal develops. In contrast, a seller who has signed an LOI, generally have little motivation to deviate from the initial terms. Accordingly, if the seller can negotiate reasonable terms in the LOI, it can provide for smoother sailing for the seller down the road as the deal falls into a final form.

An important part of negotiating an LOI is to address any potential deal-breakers before substantive talks begin. For example, if a buyer will only consider an asset sale, and a seller will only consider a stock sale, it would be best to discuss the structure of sale in the LOI phase and, if need be, part ways before both sides pour considerable time and money into negotiating a sale that is doomed from the start.

Additionally, buyers want an LOI because of the exclusivity provisions they often contain. These provisions bar the seller from negotiating with other prospective buyers for a period of time. Buyers will push for a long exclusivity period to increase their bargaining power, while sellers prefer a shorter exclusivity period.

Buyers will also want to include provisions giving them an "out" if certain conditions cannot be met. For example, in a cash up-front sale, buyers will often need to obtain financing to have the requisite funds to close the sale. However, banks typically require detailed financial information about the seller that the buyer can only obtain during its due diligence process. Thus, LOIs often contain a provision

that the sale is contingent on the buyer obtaining the necessary financing. If buyer cannot obtain financing, it has the right to pull out from negotiations.

JAH Can Help

LOIs are an important and often necessary first step in the sale of a business. However, if a seller is not careful in negotiating an LOI, it could find itself in a less advantageous position. Furthermore, an LOI is just the beginning of the complicated and involved process that is a business sale. The experienced **corporate attorneys** at JAH are here to counsel you through every step, from negotiating an LOI to closing the deal itself. **Click here to contact a member of our Corporate Group if you are in need of assistance.**

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September 13, 2023 | By: David Rugani

THE CORPORATE TRANSPARENCY ACT | A BRIEF PRIMER

The Corporate Transparency Act ("CTA") comes into effect on January 1, 2024. It is the most sweeping corporate transparency law in decades and will have a major impact on how most businesses in the U.S. operate. The purpose of the law is to crack down on "shell companies" used in illegal operations like terrorism financing, money laundering, tax evasion, and sanctions violations. To do this, and for the first time in U.S. history, the CTA will create a federal database of the ultimate owners (termed "beneficial owners") of many businesses and other organizations in the U.S. This database will be maintained by the Financial Crimes Enforcement Network ("FinCEN") which is a part of the Department of Treasury.

Required Reporting Information for Beneficial Owners

Each entity that is subject to the CTA is deemed a "reporting company." The definition of a reporting company will generally encompass any entity that is formed by making a filing with a Secretary of State's (or similar organization's) office. Corporations, limited liability companies, limited partnerships, and limited liability partnerships, are all examples of reporting companies. Each reporting company the does not qualify for an exemption will be required to provide FinCEN with the following information for the beneficial owners that either: (i) exercise "substantial control" over the entity, or (ii) own or control 25% or more of its ownership interests

1. Full legal name of the individual
2. Date of birth
3. Current residential street address
4. Unique identifying number from a passport, state identification, or driver's license
5. Image of the individual's passport, state identification, or driver's license

In addition, reporting companies will need to provide information about the company itself and the individual(s) who formed the company. Individuals will also have the option to obtain a unique FinCEN identifier (which requires a one-time disclosure of the above information), which they can use in lieu of providing their personal information to FinCEN every time they are listed in a report.

The database maintained by FinCEN is *not* publicly accessible, but it will be available to U.S. and international law enforcement agencies, among others.

New entities formed after January 1, 2024 will have 90 days from the date of formation to provide this information to FinCEN. Note that this decreases to 30 days starting in 2025. Entities that existed prior to January 1, 2024, will have until **January 1, 2025**, to comply with the CTA. If any report a company has filed with FinCEN becomes inaccurate – for example, due to a change in the beneficial owners – the reporting company is required to provide an updated report with FinCEN within 30 days.

Exemptions to the Reporting Requirements

Importantly, the CTA provides a list of more than 20 exemptions to the reporting requirements. These are entities that are excluded from the definition of a "reporting company". Exemptions include: publicly-traded companies, companies that operate in highly-regulated industries (e.g. broker-dealers, banks, and insurance companies), certain tax-exempt entities, certain inactive entities, and "large reporting companies". The large reporting company exemption will be particularly important for many businesses. A large reporting company is a company that meets **ALL** of the following criteria:

1. Employs 20 or more employees on a full-time basis in the U.S.
2. Files an income tax return in the previous year demonstrating more than $5 million in gross receipts, and
3. Has an operating presence at a physical office within the U.S.

Penalties

The CTA is not optional, and noncompliance is not to be taken lightly. Failure to comply can result in a fine of $500 per day (up to a maximum of $10,000 *per violation*) and up to two years imprisonment.

JAH Can Help

The Corporate Transparency Act will have a major impact on many companies. The experienced **corporate attorneys** at JAH are available to counsel you throughout the new guidelines, ensuring that your business is protected. **Click here to contact** a member of our **Corporate Group** if you are in need of assistance.

This update is a short primer on the CTA. A more thorough analysis of the CTA will follow in the coming weeks.

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November 14, 2023 | By: Austin Walsh

FEDERAL RULES OF EVIDENCE (FRE) 702 UPDATE: CLARIFYING EXPERT TESTIMONY ADMISSIBILITY

On December 1, 2023, changes to the Federal Rules of Evidence (FRE) 702 take effect clarifying a trial court's role in determining expert testimony admissibility. These revisions, announced by the U.S. Supreme Court and sent to Congress on April 24, 2023, are the culmination of work by the Advisory Committee on Evidence Rules that began in 2017.[1]

The Supreme Court last substantively amended Rule 702 23 years ago, following the Court's opinions beginning with *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993) and proceeding through *Kumho Tire Co. v. Carmichael*, 526 U.S. 137 (1999). The *Daubert* line of cases, and the 2000 amendment to Rule 702, established trial judges as gatekeepers to exclude unreliable expert testimony.[2] Over time, the Advisory Committee found that some trial courts were not fulfilling the gatekeeper role, and it sought to clarify application of Rule 702 to "empower the court to pass judgment" on an expert's conclusions and reject the view that expert testimony is presumed to be admissible.[3]

After a public notice and comment period that drew over 500 comments, the Advisory Committee unanimously adopted the proposed changes to Rule 702 set forth below (with new language underlined and deleted language struck through):

A witness who is qualified as an expert by knowledge, skill, experience, training, or education may testify in the form of an opinion or otherwise if the proponent demonstrates to the court that it is more likely than not that:

(a) ***the expert's scientific, technical, or other specialized knowledge will help the trier of fact to understand the evidence or to determine a fact in issue;***

(b) ***the testimony is based on sufficient facts or data;***

(c) ***the testimony is the product of reliable principles and methods; and***

(d) ***the ~~expert has reliably applied~~ expert's opinion reflects a reliable application of the principles and methods to the facts of the case.***

What Changed?

Despite the significance of a rare amendment to the FRE, the Advisory Committee clearly states that the changes are only intended to resolve conflicts in the Rule's application.[4] Specifically, the Rules of Evidence require that all admissibility requirements, such as the Rule 702 elements, are to be determined by a court under a preponderance standard (more likely than not). For example, a court must find that an expert's testimony, more likely than not, is based on sufficient facts or data. The Advisory Committee found that some trial courts applied the preponderance standard inconsistently or did not apply it at all. By explicitly adding the burden of proof to Rule 702, the Advisory Committee sought to address this important conflict.[5]

Experts Must Stay In Their Lane

Similarly, the amendment to Rule 702(d) clarifies and emphasizes the court's power to pass judgment on an expert's conclusion – an expert's opinion must actually proceed from a reliable application of a reliable methodology.[6] This gatekeeper function is consistent with the Supreme Court's holding in *General Electric Co. v. Joiner*, 522 U.S. 136 (1997) and is especially important where jurors may be unable to meaningfully evaluate the reliability or boundaries of an expert's basis and methodology.[7]

Effective Date

The revised Rule 702 applies to all federal proceedings commenced after December 1, 2023. However, **litigators** should take note that the Supreme Court's Order opens the door for the Rule's application to *all* proceedings pending on December 1, 2023, "insofar as just and practicable."[8]

Does This Apply To North Carolina State Court Matters?

In 2011, eleven years after the post-*Daubert* changes to Federal Rules of Evidence 702, the North Carolina General Assembly added language to North Carolina's Rule 702(a) that was nearly identical to the federal rule. In 2016, the N.C. Supreme Court held for the first time in *State v. McGrady* that North Carolina's Rule 702(a) "incorporates the standard from the *Daubert* line of cases" and that "North Carolina is now a *Daubert* state."[9]

Once again, North Carolina is lagging behind federal changes to Rule 702. However, the Advisory Committee's Note clearly states that the federal changes are meant to clarify how Rule 702 should have been applied all along. Therefore, even if North Carolina is slow to codify similar changes to Rule 702, the Advisory Committee's Note and Report is instructive to state courts' application of a preponderance standard to each reliability element of N.C. Rules of Evidence 702. [10] **Litigators** should keep this in mind for motions to exclude opposing experts filed after December 1, 2023.

[1] United States Courts, *Report of the Judicial Conference Committee on Rules of Practice and Procedure* – September 22 at Rules Appendix E-19, available at, **https://www.uscourts.gov/sites/default/files/sept_2022_jcus_rules_report_final_for_website.pdf**. (hereafter "Report")

[2] FED. R. EVID. 702 advisory committee's notes on 2000 amendments.

[3] Report at p. 23.

[4] Report at Rules Appendix E-20.

[5] Id.

[6] Report at Rules Appendix E-19. (citing General Electric Co., v. Joiner, 522 U.S. 136 (1997)).

[7] Report at Rules Appendix E-13, E-20.

[8] Supreme Court Order frev23_5468 (April 24, 2023), available at, **https://www.supremecourt.gov/orders/courtorders/frev23_5468.pdf**

[9] State v. McGrady, 368 N.C. 880, 888, 787 S.E.2d 1, 8 (2016).

[10] See id. at 892-93, 787 S.E.2d at 10-11.

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December 01, 2023 | By: Jessica Shoop

CLICKWRAP AGREEMENTS AND WHY YOUR WEBSITE NEEDS THEM

Your company's terms and policies are important to you. So what is the best way to share them with your website's users, and how can you make sure they're enforceable? In our current digital age, the use of clickwrap agreements is becoming widespread, and courts are increasingly upholding them as the most effective way to bind website users to a company's terms.

What is a Clickwrap Agreement?

A "clickwrap" agreement is a prompt that requires a website user to affirmatively "accept" a company's policies and terms. This prompt often appears when a user first opens the website, registers for an account, or makes a purchase at checkout, providing a link to each policy and term and requiring that the user check an "accept" box before they can proceed.

But clickwrap agreements are not the only way companies try to bind their customers and website users: (i) "browsewrap" agreements are posted generally on a website, either requiring a user to simply browse through the agreement or simply making it available for review and (ii) "shrinkwrap" agreements require no customer action at all, accompanying a product (and presented to a customer for the first time) only after a purchase has been made.

Why Should I Use Clickwrap Agreements?

Courts have repeatedly upheld clickwrap agreements as effective in binding users to companies' terms. This is because, unlike both browsewrap and shrinkwrap agreements, a clickwrap agreement presents website users with the clear opportunity to read each term and knowingly and affirmatively accept them. In contrast, browsewrap and shrinkwrap agreements provide no evidence that a user knows what he is agreeing to. The customer's click of the "accept" button functions the same as an electronic signature, and provides evidence that the customer not only read the terms but chose to proceed according to them.

Clickwrap agreements are also the easiest way to support the enforceability of your company's terms without impairing the customer's website experience. They can be used on apps, software licenses, and other digital platforms, as well as websites. And because customers show their assent through the click of a mouse, you can keep an electronic record of each customer who has agreed to the terms.

But clickwrap agreements are not foolproof: courts have repeatedly held that clickwrap agreements must be conspicuous, easy to access, and reasonably easy for the average customer to

understand. If your clickwrap agreements fail to meet these standards, you may not be able to enforce them against your customers.

JAH Can Help

Your company's terms and conditions serve an important part of your company's business. However, if you are not careful in how you share these terms with your customers, they may not be enforceable. The experienced **corporate attorneys** at JAH are here to counsel you through every step.

Please note that the above JAH article does not constitute legal advice nor does it create an attorney-client relationship. Should you be in need of legal services regarding a particular matter, please reach out directly to one of our attorneys. ***Click here for our full website disclaimer****.*

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