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SettlePou Newsletter

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SETTLEPOU
ATTORNEYS ▪ COUNSELORS

3333 LEE PARKWAY, EIGHTH FLOOR, DALLAS, TEXAS 75219
TEL: (214) 520-3300, FAX: (214) 526-4145
WWW.SETTLEPOU.COM

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Doing Business with Terrorists: Executive Order 13224

By Jeff Mosteller

In response to the events of September 11, 2001, President Bush issued Executive Order 13224, which was intended to help in the fight against terrorism. The Executive Order provides for, among other things, a ban upon "United States Persons" (essentially, any individual, entity, charity or other type of organization) doing business with any Specially Designated Nationals and Blocked Persons (SDNs) as designated by the U.S. Treasury Department's Office of Foreign Assets Control (OFAC). The SDN list, which includes the names of terrorists, terrorist entities, drug dealers and money launderers can be viewed at the OFAC website in either .pdf or database-ready format at http://www.treas.gov/offices/enforcement/ofac/sdn/index.html.

Note that this ban on doing business with SDNs is broad and without exceptions. This would include, without limitation, entering into any type of contract, lease or agreement, or loan transactions, or utilizing any services with SDNs, as well as the employment of any SDNs. A violation of the Executive Order is a "strict liability" offense; that is, a party cannot claim as a defense to the crime that it was unaware or did not intend to do business with an SDN.

> WHEN THE OFAC DETERMINES THAT A PARTY HAS CONDUCTED BUSINESS WITH SDNS, THE PENALTY IS STEEP REGARDLESS OF WHETHER OR NOT THE PARTY HAD KNOWLEDGE OF THE VIOLATION.

When the OFAC determines that a party has conducted business with an SDN, the penalty is steep regardless of whether or not the party had knowledge of the violation. Civil penalties range from $11,000 to $1 million per violation. Furthermore, if the violation occurred knowingly or with a "willful blindness," criminal penalties are imposed.

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Attorneys:

- BRADFORD E. ADATTO
- SAYURI BELTRAN
- MICHAEL S. BYRD
- SCOTT J. CONRAD
- MARSHA L. DEKAN
- BRIAN P. DEVOSS
- J. GARTH FENNEGAN
- DON GWIN
- BARRY D. JOHNSON
- KATHERINE L. KILLINGSWORTH
- NORMAN H. KINZY
- OLIVER B. KREJS
- BRADLEY E. MCLAIN
- MICHAEL P. MENTON
- KELLY J. MIDDLETON
- CARL W. MORGAN
- JEFF MOSTELLER
- DAVID M. O'DENS
- JEFFREY J. PORTER
- ROBERT L. POU III
- SHARON REULER
- JOHN D. "JAY" SETTLE
- J. ALLEN SMITH
- JAMES M. STANFORD
- MICHAEL R. STEINMARK
- STEVEN M. THOMAS
- CLIFF A. WADE
- C. RUSSELL WOODY

Doing Business with Terrorists... *Continued from page 1*

Corporate criminal penalties can include fines from $50,000 to $10 million, and individuals can be imprisoned from 10 to 30 years. In addition to the formal penalties, a business may also suffer negative publicity when its customers learn it has laundered money for terrorists.

Unfortunately, there have been no definitive compliance procedures or clarifications of the broad restrictions noted above by the OFAC. Even strict compliance with the procedures to be discussed below will, at most, serve as mitigating factors if a party violates the Executive Order. While evidence of thorough, strictly-enforced policies may be beneficial if a party is required to demonstrate its commitment to OFAC compliance, it will not absolve it of liability.

Given the foregoing, all businesses and individuals should establish policies with respect to OFAC compliance. As part of standard procedure in any potential transaction, dealing, contract or business relationship, two proactive steps should be considered: (1) *Screening* – you must ascertain if the other party is on the SDN list and (2) *Certification* – you must require that the other party certify to you that they are not on, affiliated with, or working for a party identified on the SDN list.

SCREENING

(1) *Obtain and screen the names of all parties to the transaction.* The SDN list originally contained fewer than 50 names. Today it includes thousands, and it is updated frequently. In order to facilitate compliance, the OFAC now provides the list in a database-ready format that can be incorporated into an in-house compliance software program. There are also web-based services specializing in terrorist screening, and a few credit reporting agencies have added the SDN list to their screening services. It may be difficult with large companies or entities to determine how deeply one should probe. For example, when dealing with a corporation, must one also identify and screen the directors, officers, major shareholders, etc. Unfortunately, no guidance has been given from the OFAC as to the scope and extent to which one must screen.

(2) *Conduct a periodic recheck of all (new and existing) business partners.* Because of the frequent updates to the SDN list, it is important to confirm that all continuing business relationships (not just new relationships) are not in violation of the Executive Order. However, there is no standard that decrees how often one must screen these parties, employees, agents, business partners, etc. All parties must determine for themselves the vigilance required to ensure that they are not engaging in business activities with SDNs.

(3) *Verify and report any matches.* Because of the large number of spelling variations in certain names, it is necessary to cross-check positive matches to ensure their validity. Addresses, gender, marital status, identification numbers, birth dates, and other criteria should be examined. When a match is verified, the OFAC and the FBI should be notified immediately for further discussion and instructions. The OFAC will require a "blocking report" which must include the name and description of the person, information regarding the transaction, including the address of the property, the name of the property owner, and the phone number of a contact person with additional information regarding the transaction.

(4) *Keep thorough records.* Keep all screening records and investigation reports in order to show due diligence in case of a violation.

CERTIFICATION

A provision should be added to all transaction documents (e.g., leases, contracts, service or supply contracts, loan documents, purchase or sale agreements, etc.) whereby each party certifies, represents and warrants that they are not an SDN or working on the behalf of or affiliated with an SDN. Such certification should also provide indemnification if a party is found to be in violation. Of course, without performing the screening noted above, a party which relies only on such a certification leaves itself vulnerable to an SDN providing it with a false certification and potential liability under the Executive Order.

If you would like to discuss these procedures further, or if you have other questions related to the Executive Order, please feel free contact Jeff Mosteller or Jeff Porter at (214) 520-3300.

Meet Your Lawyers:

Scott J. Conrad

Hometown:
Des Moines, Iowa

College:
Southern Methodist University

Law School:
Texas Tech

Family:
Wife, Julie; daughter, Allie; and son, Jack

Personal Favorites

Food:
Tex-Mex

Drink:
Margarita

Hobby:
Golf

TV Show:
History Channel

Old Movie:
Hoosiers

Recent Movie:
Inside Job

Book:
The Five Dysfunctions of a Team

Music:
Anything by U2 or George Strait

Vacation:
Grand Cayman

Sport:
Any competition

Sports Team:
Dallas Cowboys

What do you consider as the most important qualities of a good lawyer?
Communication, integrity and how these assist you in developing strong working relationships with your clients and fellow attorneys.

Scott J. Conrad

Areas of Practice:

Financial Institution Litigation, Commercial Lending Law, Business Litigation and Condemnation Law

The New Texas Business Organizations Code's Impact on Lenders

By Don Gwin

As discussed in our Spring Newsletter, the new Texas Business Organizations Code (TBOC) became effective on January 1, 2006. The TBOC represents a codification of eleven separate statutes governing non-profit and for-profit entities. Among the statutes codified and replaced by the TBOC are the Texas Business Corporation Act, the Texas Limited Liability Company Act, Texas Revised Partnership Act, and Texas Revised Limited Partnership Act. The TBOC impacts banks and other lending institutions that loan money to commercial borrowers by changing the landscape of the due diligence checklists so closely relied upon by closing officers in making final approvals. For the most part, the purpose of the Code is not to substantively change the laws governing the various types of business entities, but to rearrange those statutes, harmonize various provisions, and eliminate duplicative and ineffective provisions.

Going forward, lenders should recognize that any domestic entity (e.g., a Texas corporation or a Texas limited liability company) formed in Texas on or after January 1, 2006 must be formed under, and governed by, the TBOC. Domestic entities existing prior to January 1, 2006 will not become subject to the TBOC until January 1, 2010, unless they affirmatively elect to opt in to the TBOC before such date. Further, any foreign "filing entity" (e.g., a Delaware corporation or Delaware limited liability company) that registers with the Texas Secretary of State on or after January 1, 2006 to transact business in Texas will be subject to the TBOC. Similar to domestic entities, foreign filing entities registered with the Texas Secretary of State prior to January 1, 2006 to transact business in Texas will not be governed by the TBOC until January 1, 2010, unless they elect to be governed by the TBOC before such date.

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Texas Business Organizations Code...*Continued from page 3*

So what does the TBOC mean to those of you who are on the "front line" preparing due diligence checklists and reviewing entity formation documents? Most significantly, you should now be seeing entity-formation documents that are more uniform, and differ slightly from documents reviewed prior to the enactment of the TBOC.

The most notable difference between the old statutes and the new TBOC is the replacement of familiar terminology used in titling entity formation documents. One of the new terms that lenders will begin to see regularly is the *Certificate of Formation*, which now applies to nearly every entity to which a bank might loan money. For those entities to which the TBOC applies, the Certificate of Formation will replace all of the following: Articles of Incorporation, Articles of Organization, Articles of Association, Certificate of Limited Partnership, Declarations of Trust and Charters. Another new term used in the TBOC is the *Company Agreement*, which replaces what the old statutes identify as "Regulations" for a limited liability company.

The last fairly significant change in terminology is that you will no longer be seeing a "Certificate of Incorporation", Certificate of Organization", or "Certificate of Association" for entities being formed under the TBOC. Instead, you should look for a *Certificate of Filing*. In order to verify a company's legal formation under the TBOC, we recommend that you obtain a copy of the Certificate of Filing, along with a file-stamped copy of the entity's Certificate of Formation.

You may be relieved to know that there is at least one important organizational document that the legislature did not feel compelled to rename: Corporate *Bylaws* will continue to be referred to as "Bylaws" under the new TBOC.

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Meet Your Legal Support Team:

Pete Elfrink

Pete Elfrink

Position:
Legal Assistant, Transactional/ Real Estate Section

Hometown:
Big "D"

Education:
Droughn's Business School

Family:
Husband, Bert; four brothers and two sisters

<u>Personal Favorites</u>

Food:
Trout Almondine

Drink:
Arnold Palmer Tea

Hobby:
Gardening

TV Show:
24 and Grey's Anatomy

Old Movie:
Gone with the Wind

Recent Movie:
Titanic

Book:
Let's Roll by Lisa Beamer

Music:
All types

Vacation:
Williamsburg, Virginia

Sport:
Football

Sports Team:
Dallas Cowboys

Pete Elfrink joined SettlePou in 1996 as Jeff Porter's legal assistant and says she has had the pleasure of being part of the growth of the firm. In her spare time, she enjoys entertaining family and friends, as well as her aging neighbors.

Texas Business Organizations Code... Continued from page 4

Finally, when revising due diligence checklists to conform to the new terminology under the TBOC, you should remember that the old terminology will still apply to entities that were formed prior to January 1, 2006. Therefore, you will need to keep that terminology on your checklists for the time being. To make matters even more confusing, there may be some entities formed under the TBOC which may incorrectly file documents containing the "old" terminology. For example, someone might file "Articles of Incorporation" for a corporation formed after January 1, 2006, instead of a Certificate of Formation. We have been informed that the Texas Secretary of State may still accept documents entitled under the old regime for a limited amount of time. That is another reason why your new due diligence checklists should contemplate both the "old" and "new" documents.

Bear in mind that this discussion is only a very broad overview of some of the changes that might affect our lender clients, and is not intended to be a comprehensive analysis of the TBOC. If you have any questions, please feel free to contact Don Gwin at (214) 520-3300 or dgwin@settlepou.com.

Don Gwin

Areas of Practice:

SBA and USDA Lending, Financial Institutions, Loan Workouts and Restructuring, Asset Recovery, Commercial Bankruptcy, Lender Liability and SBA Liquidation

Trademarks: Is Your Company Ignoring a Valuable Asset?

By Michael S. Byrd

Trademarks are a source of value. They create brand recognition and increase the growth potential of a business. Moreover, the trademark itself, or a portfolio of trademarks, can be a significant and valuable asset to a business. This asset enables a business to define its position in the market and evidences its good will to prospective buyers. Unfortunately, the importance of selecting, developing, and protecting trademarks is often overlooked by businesses. The following is a primer to assist in identifying whether a business has a potentially viable trademark.

Essentially, a trademark is a brand name. The term trademark may be broadly applied to encompass brand names used for both goods and services. A service mark, however, identifies and distinguishes only services provided by one party from the services provided by others. Some commonly known examples of trademarks and services marks are Coke, identifying soft drinks; Nike, identifying athletic apparel; and Citibank, identifying banking and financial services.

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Michael S. Byrd

Areas of Practice:

Health Law, Private Business, Private Business/Technology, Private Business/Mergers and Acquisitions, Business Litigation and Condemnation Law

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In assessing the potential value of a trademark, there are three general categories that gauge the strength of a mark: (1) arbitrary or fanciful marks; (2) suggestive marks; and (3) descriptive marks. Arbitrary and fanciful marks are the strongest and most distinctive class of marks. Arbitrary and fanciful marks are marks that cannot be labeled as being descriptive or even suggestive of the goods or services with which they are associated. Accordingly, they are afforded trademark protection upon use and provide their owners the greatest degree of protections. Consequently, they are the most valuable kind of mark. An example of an arbitrary or fanciful mark is Exxon or Google, which neither suggest nor describe petroleum or an Internet search engine.

Suggestive marks are the second strongest class of marks and also obtain trademark protection upon use. A suggestive mark is a mark that is suggestive of the goods and services with which it is associated. An example of a suggestive mark is Microsoft, which is suggestive of microcomputer software. These can also be valuable marks, but a higher degree of brand recognition is needed before these marks become valuable.

The least distinctive class of marks is descriptive. Unfortunately, many marks fall into this category due to the mark owner's or marketing department's desire to create a mark that describes the good or service to their clientele. Descriptive marks do not immediately obtain protection upon use, but must acquire a secondary meaning through extensive and continued use. Examples of descriptive marks are NFL Network, which is descriptive of the broadcasting network services of the National Football League, or Holiday Inn, which is descriptive of motel services.

In addition to nationwide protection, a federally registered mark has several important advantages. Federal registration gives the owner access to the federal courts. It removes the burden of the owner to prove the mark is valid and protectable, and that the owner has the exclusive right to use the mark. Federal registration provides the public with notice of the owner's claim to the mark. Federal registration can also be used as a basis for obtaining trademark registration in foreign countries and may be filed with U.S. Customs Service to prevent importation of infringing foreign goods. Without federal registration, a mark is protected only in the geographic region in which it is used, or if registered with a state, only in the state in which it is used. To obtain nationwide protection of a trademark, the owner must obtain registration with the United States Patent and Trademark Office ("USPTO").

Proper identification and use of the mark prior to, during, and after registration is very important. The mark owner should use the symbols "TM" for trademark, or "SM" for service mark, prior to federal or state registration. The ® symbol, however, cannot be used until the mark is federally registered with the USPTO. Affixing the ® symbol is highly advisable once registered. To recover damages or profits under federal statutory law without having to prove the defendant had actual knowledge of the mark's registration, a mark owner must affix the ® symbol or provide other adequate notice of registration.

Even after a mark has been registered, however, it may lose protection in a number of ways, including failure of the mark owner to police its mark. If another business uses the same or even a similar mark and is not challenged, this will dilute the value of the mark. Another area where mark owners commonly make mistakes is the manner in which they actually use their marks. To maintain the strength of the mark, it should be used as an adjective when describing its associated goods or services and not as a noun.

It is important to obtain counsel on selection of your trademark, assistance in applying for registration with the USPTO, and assistance with maintaining proper use and protection of your mark. For additional information regarding trademark planning and registration, please contact Michael S. Byrd, Chair of the Business Counsel Services Section at (214) 520-3300 or by email at mbyrd@settlepou.com.

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