



# Newsletter

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Our office will be closed for the following holidays:

May 31<sup>st</sup> Memorial Day

July 4<sup>th</sup> – Independence Day

Our next newsletter will be mailed out the beginning of August 2004.

Remember if you have an article that you would like to contribute to our newsletter just fax it to us for our review. We must receive the article no later than June 15<sup>th</sup> for our July newsletter.

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## FRANCHISING BASICS

By Christopher Gonzalez, Esq.

If you are considering starting your own business, you have a choice of either starting from scratch, buying an existing business, or looking at a business opportunity like a franchise. The Federal Trade Commission noted that although there is not complete agreement on precisely what elements are common to all franchises, it is clear "...that franchising is not an industry, a product or a service, but is instead a method of doing business or a method of distribution."



Franchising is an alternative to expand a company without having to incur the costs of building or staffing business locations. Through the years it has proven to be an effective way to build a "chain" or "distribution network" comprised of many small business owners all operating under a "common banner" or name. For example, the McDonalds Corporation relies on independent business owners to make sure their hamburgers and other products reach consumers in a consistent manner. Owning and operating a franchise can be as much work as other options, and it can also be quite profitable. The challenge is to decide on one that both interests you and is a good investment – so do your homework and comparison-shop by looking at multiple franchise opportunities before deciding on the one that is right for you.

**How does it work?** Typically, a company (franchisor) owns a trademark that it licenses others to use upon condition that the user (franchisee) conform its business operations to the franchisor's standards. A franchisor may provide extensive assistance to its franchisees in terms of their organization, promotional activities, management, marketing plan, methods of operation or other business affairs.

**Initial Considerations.** Whether approaching the franchise from the viewpoint of the franchisor or that of the franchisee, it is useful to keep in mind the three distinct conceptual characteristics which distinguish it from conventional commercial relationships: (1) it is assumed on both sides that the franchisor's association with the franchisee will significantly increase the latter's potential for success; (2) the quid pro quo for the first, is that the franchisee, although nominally independent, must rely to a large extent on public recognition of the franchisor's goods and services and must adhere to prescribed methods of operating the franchised business; and (3) the capital investment in the form of a payment to the franchisor is unique to franchising because it provides the Franchisor with low-cost capital for use in the rapid development of a distribution network.

### **Advantages**

- ☞ Reduced Risk (lower failure rate than other start-up businesses)
- ☞ Complete Package (may include trademarks, easy access to an established product; a proven marketing method; equipment; inventory; etc.)
- ☞ Strength in Numbers (buying power of the entire network)
- ☞ Business Processes (proven systems including financial and accounting systems; ongoing training and support; research and development; sales and marketing assistance; planning and forecasting; inventory management; etc.)
- ☞ Financial and Site selection Assistance
- ☞ Advertising and Promotion (benefit from any national or regional advertising and promotional campaigns from the franchiser)

### **Drawbacks**

- ☞ Lack of Flexibility and Control
- ☞ Cost
- ☞ You're Not Alone (franchisor's reputation can benefit your individual business, the franchisor's problems are also your problems)
- ☞ Commitment (franchise agreement is a binding contract, and can be quite restrictive)

**How much will it cost?** There are basically two types of fees you should expect to pay for your franchise -- upfront fees and ongoing fees. The first is the initial upfront fee, which is what you pay the franchisor for the rights open your franchise. Essentially, you are purchasing the rights to use the franchisor's trademarks, business methods, and distribution rights. This charge can be significant, especially for a well-known, established franchise -- it's not unusual for it to be in the tens of thousands of dollars. Often, it is also based on the value of the territory or trading area, so the larger your market, the more you could end up paying.

Be aware that this upfront fee may be in addition to any other start-up costs you will have to incur. You will also have to pay ongoing fees to maintain the rights to your franchise. Most franchisors charge a royalty fee, typically a percent of your gross sales, not your profits. This royalty fee can range from 1 percent to as much as 15 percent, although 5 percent is typical. Remember, you are paying this royalty on gross sales (your total receipts, less sales tax, returns and refunds), so it can potentially take a significant bite out of your profits.

**What about the laws?** There are two laws you should know about that cover the franchisor's disclosure of information. The first is the FTC Rule, which is the federal government's regulation covering franchisor disclosure. The FTC Rule requires that a franchise seller must give you a detailed disclosure document at least 10 business days before you pay any money or legally commit yourself to purchasing the opportunity (so you have enough time to make an intelligent decision). This document -- which is like a financial prospectus -- contains information you need to make a knowledgeable decision about purchasing a franchise. Also, you must receive all contracts necessary to purchase the franchise at least 5 business days prior to the date the contracts will be executed.

The FTC rule allows states to create their own stiffer regulations -- many of which are based on the Uniform Franchise Offering Circular (UFOC), which requires even more detailed disclosure than the FTC Rule. Most franchisors provide information based on UFOC regulations so as to comply with disclosure requirements across the nation. You should consider having an attorney, accountant or other advisor review the disclosure documents and proposed contracts before entering into any agreement.

**Disclosure documents?** The disclosure documents provided to you by the franchisor can serve as a window into the company's operations. It is important to review it completely to learn all you can about the franchisor. It is important to learn as much as you can before purchasing any kind of business so you can make an informed decision. There are a wide variety of sources you can approach to learn about a franchise opportunity.

Here are some general questions you may ask: What is the franchisor's track record of success? What will it cost me? Will my territory be exclusive? What products can I sell and how can I sell them? What services will the franchisor provide to me? Is there any bad news I should know about? How much can I expect to make from this business? Does the franchiser maintain effective financial management and other controls? What kind of image?

Here are some general things you may do: Interview the franchisor. Interview existing franchisees. Read the business and trade press. Check references. Conduct research with independent agencies. Get a credit report.

Contact Christopher Gonzalez at 818-550-7979

# Investing in Life Settlements

By: Michael Tompkins, CEPP, CSA

## 1. What exactly is a Life Settlement Investment:

It is simply the purchase of a life insurance policy at a discount to face value from a seller of that policy, typically a senior citizen with declining health and a limited life expectancy. The spread between the purchase price and the policy face value can represent the profit to the purchaser/investor. Life Settlement investments pay Fixed Total Returns of 42 to 72%, based on the maturities of 3 to 6 years, with no risk to principal.

## 2. Why would someone want to sell his/her life insurance policy?

Policies are sold for a variety of reasons. Most often the seller has major health problems with a short life expectancy. The money from the sale of the policy may be used for such things as mortgage payments, education expenses for the grandkids or simply to ease the financial stress brought on by a complicated illness. Often these policies are no longer needed by the sellers, or carry large annual premiums that the seller no longer wishes to pay. Other uses of life settlement proceeds are to liquefy an otherwise dormant asset, to fund new, more cost-effective life insurance coverage, to create funds to make other investments, to fund a charitable trust, or to make cash gifts to other family members. Corporations often sell unneeded key man policies if the CEO has retired, the company must sell assets to raise cash, or must buy back stock from a partner or shareholder. The secondary market for life insurance is huge. Warren Buffet recently invested over \$400 million dollars in Life Settlements through his Berkshire Hathaway Co.

## 3. As an investor in Life Settlements, how do I know my money is safe?

Your invested monies are deposited in an FDIC insured account at a major bank. You are credited money market interest until the closing of the policy funding. Once the insurance company has added you to the policy as irrevocable beneficiary, your money is then transferred as a part of the closing process, so that the seller can get paid. From that point forward, your principal and return is protected by all of the laws that govern life insurance death benefit payouts. All U. S. insurance companies, by law, must adhere to strict guidelines and reserve requirements, which insure that all death claims will be paid without undermining the strength of the insurance company. (These strict guidelines are not required of banks and other financial institutions.) In addition, only policies issued by U.S Life Insurance Companies and rated A or better by AM Best & Company are considered for purchase.

## 4. This seems too good to be true!

That's because investors have gotten used to getting lower and lower returns on their investments over the last few years. Because this investment is unaffected by day-to-day stock market volatility, the returns seem high during a down market. In the late 90's when high tech stocks were paying stellar returns, we were told that our Life too low! It's all a matter of perspective. For more information contact Michael Tompkins at 805.267.1127

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**Benevolence is one of the distinguishing characters of a man.**

Mencius

# FEDERAL TAXPAYER IDENTIFICATION NUMBERS

Important Changes. In the past if you didn't have a social security number you could fax a copy of your passport to the IRS in order to obtain a federal taxpayer identification number. As of January 1, 2004 faxing a copy of your passport does not work. If you do not have a social security number you must apply for an ITIN number before you can obtain a federal taxpayer identification number.

If you are a resident or nonresident alien applying for an ITIN to file a tax return, you must now attach your original, completed return to Form W-7 to get the ITIN.

# INTERNET SECURITY: FIREWALLS

By Nick Mancini

If you have a DSL line, cable modem or other Internet connection connecting one or more computers to the Internet, it is highly recommended that a firewall be installed between your computers and the Internet. As the name implies, a firewall insulates your *internal* network (*your* computers) from the *external* network (*everyone* else's computers). Without a firewall, it's very easy for **practically anyone else in the world** to have access to **all the information on your computers**. Before you say "*I have nothing of interest to anyone else...so who cares?*" think of this: Hackers all over the world spend their time looking for vulnerable systems to take advantage of. Just for fun, they may delete files from your systems, possibly wreaking havoc on your business. Or, your computers may be used to send out spam (junk email) or even used as a repository for files like music, movies or pornography to be shared with other hackers throughout the world. Because the Internet is truly world wide, legal recourse is almost impossible. If your business is affected by such actions, the consequences may be devastating.

Short of physically disconnecting your computers from the Internet, the only form of protection from such intrusions is to install a properly configured firewall. Another way of thinking about a firewall is to think of the way we protect our homes: We lock our doors and windows at night or when we are away. This makes it *harder* for an intruder to enter our homes. Additional measures some of us may take include installing a gate or alarm system, or even hiring armed guards in some extreme cases. Each of these measures makes it more difficult for an intruder to enter our property. A firewall does likewise: makes it more *difficult* for an intruder to have access to our data. Without one, you are leaving the "windows and doors" of your systems wide open for anyone to access. There are several brands of firewalls with many different options. With prices starting below \$100.00 for basic models, not having one could cost thousands of times more than the small expense of having one installed.

*Nick Mancini is a freelance business computer consultant with over 20 years of experience in helping small businesses with their computer needs. Contact Nick Mancini at 818-225-0949 or [nick@nickmancini.com](mailto:nick@nickmancini.com).*

In future columns we will discuss: spam, spyware, data backup, small business servers, file sharing, Internet domain names and more. Feel free to submit a request for a topic of a future column!

# Assets The IRS Targets First

An IRS collection officer has wide discretion when choosing property to seize for purposes of satisfying a tax claim. In making the decision, the IRS considers several factors:

- ?? The amount of the tax liability compared to the property needed to satisfy the claim.
- ?? The ease of seizure and disposal of your various assets.
- ?? How necessary each asset is to the taxpayer.

Assets the IRS targets-in descending order:

- ?? Bank and checking accounts,
- ?? Cars, boats, airplanes, and recreational vehicles with a high equity,
- ?? Accounts receivable,
- ?? Stocks, bonds, and other obligations due you,
- ?? Investment real estate,
- ?? Home,
- ?? IRA's, Keogh's, and other pension accounts,
- ?? Wages.

The IRS is most reluctant to seize a home, pension accounts or wages, and generally do so only when the taxpayer is uncooperative. Threatened seizure of the home may also be attempted when the agent believes it will spur the taxpayer to refinance the home to pay the taxes. The IRS will not hesitate to file a lien against all property.

The IRS has its own guidelines concerning the seizure of social security payments and retirement funds. According to the IRS collection manual, levy of these sources of income should be made only in flagrant and aggravated

cases, and then only with the prior approval of the authorized IRS supervisor who must sign the notice of levy. Contrary to popular belief-these two assets are not beyond the reach of the IRS.

# Assets the IRS Can't Touch

The IRS does not have to leave you with very much, but the IRS still cannot take everything you own. Exempt from IRS seizure is:

- ?? Fuel, food, furniture and personal effects up to a total of \$1,650,
- ?? Undelivered mail,
- ?? Tools and books needed for your job, business or profession-up to \$1,100,
- ?? Income needed to provide court-ordered child support,
- ?? Unemployment, worker's compensation, public assistance and job training benefits,
- ?? Clothing and school books,
- ?? Pension Payments of retired railroad employees, military disability benefits, or benefits from individuals on the Armed Forces Honor Roll.

Note that Social Security, IRA's, Keogh plans and 401K Qualified Pension Plans are not protected. That doesn't suggest the IRS will quickly seize these assets, and in fact they are seldom seized by the IRS. But if you have a large tax liability you should not keep IRA's, Keogh's or other pension accounts. Liquidate these tax deferred accounts to shelter the funds-even if it means incurring a tax penalty for early withdrawal. As a practical matter, the penalty may be treated much like the original tax liability, since it will be of little or no consequence if you do not intend to fully pay your tax liability.

Another caution: If you believe your home is protected from the IRS by your state homestead laws, you will be in for a rude surprise. The IRS is the one creditor that can totally disregard your homestead protection.

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ADDRESS CORRECTION REQUESTED

