

THE PRACTICAL GUIDE TO STARTING A BUSINESS (WITH FORMS)

BY
ALLBUSINESS.COM



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- Employee issues
- Legal
- Incorporation
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THE
PRACTICAL GUIDE TO
STARTING A BUSINESS
(WITH FORMS)

By
AllBusiness.com

The Practical Guide to Starting a Business (with Forms)

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Chapter 1

Choosing Your Form of Business

-
- Sole Proprietorship
 - General Partnership
 - Limited Partnership
 - C Corporation
 - S Corporation
 - Limited Liability Company
-

When starting out, it is important to determine what form of business will work best for your specific situation. Based on potential liabilities, tax status, ease of starting up and attracting investors, you can elect to do business as a sole proprietorship, form a general partnership, form a limited partnership, incorporate or form a limited liability company. The type of business you are starting and your future goals and aspirations for the company will be factored into your decision along with your need to raise capital.

Here, we outline the possible ways in which you can elect to structure your business, including some of the advantages and disadvantages of each form. Since every business venture is unique unto itself there is no blueprint formula that every owner of any one specific type of business to follow. Tax and liability issues, for example, will be determined in part by your own personal assets.

Sole Proprietorships

The most common and simplest form of business is a sole proprietorship. Many small businesses operating in the United States are sole proprietorships. An individual proprietor owns and manages the business and is responsible for all business transactions. The owner is also personally responsible for all debts and liabilities incurred by the business. A sole proprietor can own the business for any duration of time and sell it when he or she sees fit. As owner, a sole proprietor can even pass a business down to his or her heirs.

In this type of business, there are no specific business taxes paid by the company. The owner pays taxes on income from the business as part of his or her personal income tax payments.

Sole proprietors need to comply with licensing requirements in the states in which they are doing business as well as local regulations and zoning ordinances. The paperwork and formalities, however, are substantially less than that of corporations, allowing sole proprietors to open a business quickly and with relative ease (from a bureaucratic standpoint). It can also be less costly to start a business as a sole proprietor, which is attractive to many new business owners who often find it difficult to attract investors.

Advantages of a Sole Proprietorship:

- A sole proprietor has complete control and decision-making power over the business.
- Sale or transfer can take place at the discretion of the sole proprietor.
- No corporate tax payments
- Minimal legal costs to forming a sole proprietorship
- Few formal business requirements

Disadvantages of a Sole Proprietorship:

- The sole proprietor of the business can be held personally liable for the debts and obligations of the business. Additionally, this risk extends to any liabilities incurred as a result of acts committed by employees of the company.
- All responsibilities and business decisions fall on the shoulders of the sole proprietor.
- Investors typically won't invest in sole proprietorships.

Note: If the business is conducted under a fictitious name it is up to the sole proprietor to file all applicable forms under the fictitious name or under "doing business as" (DBA). This, however, does not mean that the business is a separate entity from a legal standpoint. The sole proprietor remains liable even if he or she is doing business under a fictitious name.

Most sole proprietors rely on loans and personal assets to initially finance their business. Some will elect to incorporate once the business has started to grow while other business owners maintain their sole proprietorship for many years.

General Partnerships

General partnerships consist of two or more partners who are both responsible for the business. They share assets, profits, liabilities and management responsibilities for running the business.

General partnerships are typically formed by individuals. They are taxed in the same manner as a sole proprietorship, meaning each partner includes business income on his

or her personal income tax return. Each partner can also deduct pro rata losses from the business on his or her own individual tax return.

While general partnerships provide a means of raising capital more quickly and allow several people to combine resources and expertise several problems commonly occur including:

- Partners having different visions or goals for the business
- An unequal commitment in terms of time and finances
- Personal disputes

For these, and other reasons, general partnership agreements should be drawn up carefully with legal counsel and signed by all partners. Additionally, there should be a means of dissolving the partnership in the case of death, disability or if one partner wants out of the business for any other reason.

General partnerships can be less expensive and require less paperwork and formalities than forming a corporation, but the partnership agreement is a key element and should be drawn up with due diligence on the part of all parties.

Advantages of a General Partnership

- Shared financial commitment
- Ability to pool resources, expertise and utilize strengths
- Limited start up costs
- Few formalities (mostly applicable licenses)

Disadvantages of a General Partnership

- Partners are generally personally liable for business debts and liabilities
- Each partner may also be liable for debts incurred by decisions made by, and actions taken by, the other partner or partners
- Disagreements in management plans, operational procedures and future vision for the business
- Difficult to attract investors

General partnerships can thrive when each partner brings a specific strength to the business. If each partner takes on a defined role and there is general agreement on the business plan, goals and visions from the onset, a partnership can be advantageous. Work can get done more quickly and having several partners involved will increase the potential for acquiring resources and attracting backers. The success of such an endeavor depends largely on the personalities of the parties involved.

Limited Partnership

A limited partnership differs from a general partnership in the role and responsibilities of the partners. The limited partners typically provide capital and help arrange financing while not taking an active role in running the business.

They do, however, receive a share of the profits for their involvement as limited partners. The general partner in a limited partnership runs the operations of the business.

Most states have statutes that regulate and define the obligations and responsibilities of partners in this type of business arrangement. You are required to file with your secretary of state and must also file various reports.

The key to this partnership agreement is found in the area of liability, which falls on the general partners, and typically not on the limited partners. For this reason individuals are reluctant to be general partners. The general partner of a limited partnership can itself be a corporation or LLC to mitigate liability issues to the promoters of the limited partnership. This, however, does not mean that a limited partner cannot be part of, or have a vote in, major decisions that affect the partnership.

A limited partnership can be attractive for a limited partner who can provide funding but not expertise and does not have the time to devote to being a hands-on part of the business. Taking on the financial risk of his or her investment but not the liability risk, is also more attractive to a limited partner.

For tax purposes, a limited partnership typically works like a general partnership in that it is a pass through operation with profits passing through to the partners who then include their allocated income on their personal tax returns. Limited partnerships are often formed to acquire, operate and hold real estate.

Advantages of a Limited Partnership

- Much easier to attract investors as limited partners
- Allows for general partners to use their expertise, make key decisions and manage the business
- Limited partners can leave the business or be replaced without the need for the limited partnership to be dissolved.

Disadvantages of a Limited Partnership

- Filings, formalities and state requirements
- General partners assume personal liability

An interesting aspect of the limited partnership is that partners are able to allocate profits, losses and gains as they see fit, regardless of the equity interest of a specific partner, subject to compliance with tax laws. This too can be attractive to prospective investors.

C Corporation

The most commonly found type of corporation is the C Corporation, which is a for-profit, state incorporated business. Articles of incorporation are filed and appropriate fees are paid to set up a corporation.

The corporation is established as a unique business entity, which takes on a distinctly separate business and tax identity from that of the owners (the shareholders). Separate income taxes are filed (IRS form 1120) and corporate taxes are paid regularly for the business. In return, the business owners are typically removed from personal liability for debt incurred by the corporation. Should the business go bankrupt, or be faced with a lawsuit, the owner's personal assets are protected. This is the most significant reason why many business owners choose to incorporate. Additionally, as a separate entity, a corporation can own property, make business dealings or even sue another business independently of the shareholders.

To establish a corporation, there are several requirements and formalities that need to be addressed. For example, a corporation needs to issue shares to stockholders. In addition, state requirements usually include minutes be taken at shareholder and Board of Director meetings, appointment of officers and maintaining specific records as outlined by the state in which the incorporation documents are filed. The shareholders have ownership in the corporation, the Board of Directors governs the business and elected officers manage the day-to-day activities. Corporations must adhere to corporate tax laws and file corporate taxes regularly. While corporate taxes can be higher, initially they may be lower than that of a sole proprietor who is paying a 28% rate on his or her personal income tax.

Advantages of a C Corporation

- The corporation is a separate legal entity, and if it is adequately capitalized and proper corporate formalities are followed, the shareholders should generally have liability protection from the debts and obligations of the corporation.
- Corporations can utilize corporate benefit health plans, which often offer better retirement options and benefits than those offered by non-corporate plans.
- 100% deductible health insurance for all employees as well as group term life insurance up to a specified amount per employee
- If a stockholder dies or wishes to sell out, the corporation continues
- Easier to raise capital as a corporation than as a sole proprietorship or partnership
- Can offer employee incentive stock plans

Disadvantages of a C Corporation

- “Double taxation”. This means that besides paying corporate income taxes, any dividends to shareholders are taxed again at the applicable tax rate.
- Formalities and regulations must be followed very closely in conjunction with the laws regarding incorporating in a specific state. Failure to do so can create a situation where shareholders may be held liable.
- Costlier to start than a sole proprietorship or partnership
- More time and effort to maintain

While the idea of “double taxation” is very troublesome to many new business owners, it is not usually significant for small businesses, where it is unlikely that there will be large dividend payouts. Rather, the money is paid out in the form of salaries and benefits. As the owner, you can pay yourself a reasonable salary and handle any number of duties in the corporation. By incorporating, you have the luxury of leaving some of the money in the corporation if you foresee significant personal income from other sources. This way you can reduce your own personal income tax payments.

Taking the time, making the effort and paying the additional expenses to incorporate are usually considered worthwhile by a business that foresees potential liabilities and/or seeks investors.

S Corporations

An S Corporation is initially formed in the same manner as a C Corporation, by filing incorporation documents with the state of incorporation. Once the business has incorporated, the owners may decide to file as an S corporation, within approximately 75 days of incorporating. To do so, they need to file an IRS form 2553. This does not create a separate type of corporation, but changes the tax structure of the corporation.

The S Corporation has shareholders and is taxed like a sole proprietorship or a partnership rather than a C Corporation, which is taxed as a separate business entity. Income is passed through to the shareholders who report their pro rata income, or losses, on their individual tax returns. The corporation still files a federal return (form 1120S) and possibly a state return as well, if required by individual state law. The S Corporation shows profits and losses as they pass through to the shareholders and the corporation generally does not pay federal income tax as a separate entity. Some states, however, do tax S Corporations in the same manner as C Corporations. Check your state tax laws before electing S Corporation status.

Advantages of an S Corporation

- Corporate losses can be passed through to the shareholders and as the owner (and shareholder) you may be able to take the loss against income that appears on your personal return.
- You can have the protection of limited personal liability without having to pay corporate taxes.
- You can minimize self-employment tax and FICA tax. Profits, as a shareholder, are not taxed in this manner.
- It is easier to raise capital as a corporation than as a sole proprietorship or partnership.

Disadvantages of an S Corporation

- Numerous regulations and requirements that must be upheld by an S Corporation including a limit on the number of shareholders (see list below).
- Like a C Corporation, it can be costly to set up and follow formalities.
- Close scrutiny by the IRS of shareholder-employees, who must receive reasonable compensation (subject to employment taxes) before any non-wage distributions may be made to that shareholder-employee.

Other regulations imposed on S Corporations include:

- All shareholders must be U.S. citizens.
- All shareholders must vote in favor of the S Corporation.
- Benefits such as health or accident insurance for employee shareholders (with at least 2% ownership) may not be deducted by the corporation.

A corporation that plans to pass through dividends regularly to shareholders, may want to elect S Corporation tax status. Also, a business owner who may want to take business losses on his or her own personal tax return, possibly to offset income earned by his or her spouse, may opt for this type of corporation. It is worth noting that if you do set up an S corporation and later decide that there is a better alternative for your business, you can vote to drop S corporation status.

Like other corporations, the S Corporation can limit the personal liability of the owners. Creditors can go after the assets of the corporation and not the owners if there are outstanding debts. It is important, however, that the owner keeps his or her personal financial records and those of the S Corporation completely separate to avoid legal entanglements.

Limited Liability Company (LLC)

The hybrid answer to choosing the form of business for your company may be to go with a Limited Liability Company (LLC), which combines the pass-through taxation of a sole proprietorship, or general partnership, with the limited liability of a corporation. A relatively new form of business, LLCs have become popular over the past ten years. An LLC operates as a separate legal entity, but without being a corporation. Therefore, there are no federal corporate taxes imposed on the LLC as a separate entity. To start an LLC, a member, or members, must file the specific forms with the secretary of state. Information that is required will include the latest date at which the LLC is to dissolve and a statement explaining whether the LLC will be managed by one manager, several managers, or the members.

What makes the LLC unique is that it is formed by members, not shareholders, who draw up an operating agreement to run the business without the structural guidelines imposed on a corporation. This allows for greater flexibility without formalities, such as Board of Director meetings, which are imposed on a corporation. While most LLCs have two or more members, in many states, a single member can now form an LLC as a legitimate business structure.

Advantages of a Limited Liability Company

- Personal liability protection for members
- No need to meet the requirements and formalities of a corporation to maintain the business status
- Members can draw up their own contract, allowing for flexibility in management and responsibilities
- Greater flexible in allocating income to members than in a corporation. For example, an LLC can have various classes of interest while an S Corporation can issue only one type of stock.

Making The Right Choice

<i>Comparisons at a glance:</i>			
<u>Form of Business</u>	<u>Tax Structure</u>	<u>Liability</u>	
Sole Proprietorship	Pass through	Personally liable	
General Partnership	Pass through	Personally liable	
Limited Partnership	Pass through	Liability protection for limited partners	
Limited Liability Company	Pass through	Personal liability protection	
S Corporation	Pass through	Personal liability protection	
C Corporation	Corporate taxes	Personal liability protection	
<u>Form of Business</u>	<u>Ease of Start Up (Based on paperwork & restrictions)</u>	<u>Ease of Attracting Investors</u>	<u>Ongoing Government Regulations & Formalities</u>
Sole Proprietorship	Easy	Difficult	Few
General Partnership	Easy	Difficult	Few
Limited Partnership	Medium	Medium	Some
Limited Liability Company	Difficult	Medium	Some
S Corporation	Medium	Easier	Many
C Corporation	Medium	Easiest	Many

Checklist

When deciding on which form of business will best serve your purposes you should take into account:

- Your own personal assets and liabilities
- Your existing capital and need for outside investors
- Your ability to attract outside investors
- State licensing, statutes and tax requirements
- The time commitment necessary to handle regulations and formalities
- The size, scope and type of business you are opening

Start up costs including licensing and other fees

The Need For Funding

The need for funding is one of the first concerns for any new business and unless you have the personal assets or can tap into friends, family or your bank, you will be seeking investors. Investors will look at:

- Returns on their investment
- Protection from personal liability
- Tax situation (their personal situation and that of your business)

While most businesses can only anticipate future returns, the business structure that protects personal assets and provides a favorable tax environment will be most attractive to investors. If, however, you do not need investors or are not seeking shareholders when starting up a business, you may do what many business owners have done and start small as a sole proprietor and incorporate later as the business grows.

Other Determining Factors

Determining not only the type of business you are starting, but the type of customers you will attract and the manner in which you will attract them should also be factored into your decision making process.

The potential for liability from customer relationships or interaction impacts heavily on your liability risk. For example, someone who is opening a business that will sell goods to customers via the Internet or through mail order is less likely to garner lawsuits than someone who owns physical store locations, where customer foot traffic (and potential injuries) could result in such a lawsuit. However, some small business owners opt for coverage from insurance policies rather than going through the time and expense of incorporating.

Attorneys, brokers or financial consultants offering advice and personal services may run a greater risk of a lawsuit from someone claiming they received “bad advice”. It will also be assumed that a professional business such as a law firm or accounting practice will have greater assets, making them greater “targets” in a litigious society. Therefore, such a business would more likely choose a form of business that protects their personal assets. Likewise, someone who has already had previous business success and has significant assets from a previous business venture would also want to protect those assets closely.

How fast you anticipate the business will grow is also of concern when selecting your form of business. If you expect it to take several years before you see a profit, you might select an S corporation so that shareholders can offset some of their personal income with losses from the business.

While a sole proprietorship is the optimal choice for many people starting small businesses, some people select this method primarily because it provides the easiest manner in which to start and open a business quickly. Others become sole proprietors simply because they do not believe they can incorporate. Apathy can come back to haunt a successful entrepreneur. Therefore, it is wise to sit down with both an attorney and an accountant and discuss the details of the business that you are planning to start where you see it going in five or ten years. Cover all the bases including liabilities,

taxes, employee benefits and the need for investors before making your decision. Then make the decision that is best for your new business from all aspects.

Alter Ego Liability: The courts may hold the shareholders in a corporation liable if they believe the corporation is not adhering to following the formal regulations a corporation needs to follow. This is called “alter ego liability” and emphasizes the need for any business that has incorporated, no matter how small, to abide by the guidelines in the state in which it is incorporated.

The Answer

So, what is the answer for the right business entity for an entrepreneur? In a nutshell:

- Stay away from sole proprietorships and general partnerships. The risk of personal liability for the debts and obligations of business are too great.
- LLCs and limited partnerships can be good for certain businesses (such as real estate), but can be complicated and expensive from a legal perspective.
- S corporations make a lot of sense if you can qualify. You can always convert to a C corporation later.

C corporations make sense if you plan to have sophisticated angel or venture capital investors.

Chapter 2

Business Plans

-
- Why a Business Plan?
 - Key Sections of the Business Plan
 - Do's & Dont's
 - A Mini Business Plan
 - Confidentiality
-

Why A Business Plan?

Commonly compared to a blueprint used by builders and architects, a business plan is a guide to putting together your business. It helps you put all the pieces in place and clearly envision the possibilities for the future of your endeavor. You should be able to look at your business plan and see what resources and capital you will need to get started.

Typically, the process of studying the market and putting your business plan together will allow you to clearly see where your business will fit in the marketplace, where your profits should come from and how long it should take to see such profits. Most significantly, your business plan can help you attract investors, who can clearly see on paper, how your vision will translate into a practical business venture and compete within the industry.

Within the plan, you will include a financial section with a breakdown of your start up costs, a break-even analysis and a projection of your profits and losses. By carefully working your way through the details of your financial plans and projections, you will be able to determine:

- If starting the business is a good idea
- Whether or not you can expand or need to minimize the scope of your business
- How much time and money it will take to realistically make your plan work

Often, a business plan provides the owner(s) with the first and most detailed breakdown of their ideas in black and white. It is useful to see, on paper; how all of the details come together to formulate the overall plan and ultimately should help you determine

how to proceed. You will likely be able to pinpoint potential problems and make necessary adjustments in advance or even abort the plan completely if the financial picture does not look promising.

And finally, unlike a blueprint, which usually remains somewhere buried in the archives, the business plan should be a viable tool once the business is “up and running”.

During the life of the business, your business plan can:

- Help you maintain your original vision
- Help you manage your ongoing business operations
- Provide the basis for a tracking system, which will enable you to evaluate the progress of your business

While the size and complexity of a business plan will vary greatly between a small one-person business venture and the formation of a new multi-million dollar enterprise, the principle remains the same... putting something on paper to guide you through the process of creating, evaluating, establishing and running the business and to show potential investors why they should back your business venture.

Key Sections of a Business Plan

Some business plans will run four or five pages, while others will be forty pages. The complexity of the business and details necessary to present a thorough picture of the business will define the appropriate length of your business plan. Regardless of the length of the plan, the same key elements need to be included. In addition, all business plans should be proofread, carefully reviewed for clarity and presented in a professional manner with a cover page, table of contents and all appropriate contact information. Appendices can be included to provide additional data and supporting information.

The Executive Summary

Although it appears at the start of a business plan, typically the executive summary is written last, after other sections have been written, evaluated and reworked to make sure the overall plan is sound. The executive summary provides a short (usually one or two page) overview of the rest of the business plan. It is often considered the most crucial part of the plan because it is the first section your readers see and is designed to capture their attention and draw them into reading further about the business endeavor.

The executive summary will touch on all of the areas of the plan that follows, including:

- The overall objective of the business
- What makes the business unique or distinctive
- The experience of the management team
- The target audience
- Future aspirations
- How the business will operate
- The current competition in the market

- Costs and financial projections

This last section is written primarily for funding purposes, although it also provides you, as the owner, with a capsule summary of all that needs to be addressed. Subsequently it can also help when marketing and promoting the business.

A strong executive summary should be concise and engaging. It should invite the prospective investor to read the rest of the business plan.

Company Description or Business Overview

Unlike the executive summary, which needs to be concise, this is where you can elaborate on the details of the business. Typically, for a new business, this section is used to explain your vision and goals for the business venture in practical terms. The who, what, where, when, and why of the business should fall into place and readers should have a clear understanding of how the company will function. Existing businesses looking to procure further capital use this section as an overview of the company, explaining how it is run, how it makes money and what plans are in place for the future.

Details that prospective investors will likely want to see in this section include:

- The legal structure of the business (Sole proprietorship, corporation, etc)
- Formation of the business (New venture, buying an existing business, franchise, etc.)
- Type of business (Manufacturing, retail or sales, service or a combination)
- Potential for profitability (How you will make money)
- Location (Where you will be based)
- Means of doing business (Internet, storefront operation, mail order)
- Time of business operations (Open daily, seasonal, specific hours, etc.)
- Resources (What you will need to get started and operate, from machinery to computers to manpower)

By the end of this section, the reader should understand why you believe this business will work. There are many varieties on a theme, and this section can include other details such as how this business idea initially came to fruition or opportunities you see for growth and expansion.

Products & Services

This section describes the products manufactured or sold, or the services offered. Classify the different types of products or services and provide a brief description of each. Indicate why you have selected to market such products or services and the need you fulfill for your prospective customers. If you are manufacturing products, you will also need to describe a cross section of products and the materials you will use to make such products. Service providers need to include the full range of services that

will be provided, their benefits to the target market and then include any products that they sell in conjunction with their services.

The key to writing the products and services section is explaining the significant benefits of your products or services and how they provide something other than that which is currently available from competing companies. You want to provide sound reasoning for manufacturing or selling a product or service.

Market Information

Market information describes the larger picture of the industry in which your business will compete. This sets a framework so that investors will see what piece of this market you will be able to capture and from where you will build your customer base. It also provides you, as a business owner with an opportunity to carefully research and evaluate the industry to better determine how you can make an impact.

Market information must be:

- Timely
- Accurate
- Easy to read and understand

Furthermore, you should present:

- An overview of the market
- Trends and changes in the market
- Niche markets or segments within the larger market
- Your target audience
- The needs of your target audience
- How you will impact on those needs
- How you anticipate the market will change over the next two, three or five years

Your market information should correlate with the products and, or services you have presented above.

Typically, in this section you will take an overall look at the industry and include broad based industry information. Then you will follow it up with specific geographic and demographic data. For example, the owner of a new health club can provide information and statistics about the health industry on a national level but should then discuss the industry and demographics specific to the geographic area in which he or she is planning to open the new health club or clubs. Charts and graphs can be advantageous in illustrating trends and growth patterns in the market.

Do's & Dont's For Business Plans

Do:

- ✓ Provide a compelling, concise executive summary
- ✓ Highlight the experience of the management team
- ✓ Differentiate your products from competitors
- ✓ Provide an explanation of a large market opportunity

Don't

- ✓ Use superlatives
- ✓ Make unsubstantiated claims
- ✓ Over-estimate financial projections
- ✓ Use hearsay or rumors about competitors (use fact-based information only)
- ✓ Provide an inaccurate portrayal of the market or industry
- ✓ Make sweeping generalizations

Competitive Analysis

Business is competitive by nature and to succeed it is vital that you research, understand and evaluate your competition. This will provide investors with a clear understanding of what market share you can realistically gain. In addition, it will allow you to best determine what you will need to do to gain a competitive edge. Using available data and even visiting competitors in person, you will learn how they conduct business, price their merchandise or services and manage their businesses.

The strengths, weaknesses and details of the most direct and indirect competition should be included in this section of your business plan. Without being disparaging toward any other business, you will then want to describe exactly how your business will differ and present alternatives to that which your competition is currently offering.

While putting together the competitive analysis, you want to ask yourself:

- What are my competitors doing that I can learn from?
- What are their strengths and weaknesses?
- What could I do better?
- How can I present similar products or services in a distinctive manner?
- What section of the market (if any) are they not capturing?
- How are they marketing themselves?

The reader should see a clear distinction between the competition and what you hope to achieve from your business. Naturally, the more crowded the marketplace the more creativity will be required on your part. You may need to find a niche market that will

allow you to compete against a more established business. For example, several privately owned bookstores have succeeded against competition from larger “superstores” by appealing to niche markets, such as targeting a store, along with special services and activities, to science fiction and occult readers.

How you can gain a competitive edge is very significant to prospective investors.

Operational Plan or Operational Strategies

This section describes how the business will operate. It will include how items will be ordered, stored, sold and/or, produced. A service company will describe how the service is offered and performed. Essentially, the objective is to walk the reader through the process of how business will be conducted.

The operations plan should include:

- Who will handle specific tasks
- How the business will be physically set up
- Inventory details
- Manufacturing details
- Pricing details
- Safety precautions
- The need for subcontractors or freelancers

The key to the operations section of your business plan, however, is not only to explain how you will do business, but to explain your strategies and how they best facilitate the type of business you plan to do. The reasoning behind your operations plan is as important, if not more so, than the actual description of how business will be conducted. You can highlight how your method of doing business will:

- Benefit your customers
- Expedite transactions
- Ensure quality customer service
- Give you a competitive advantage

Almost every business has a need to interact with other companies. You will want to include the other companies, vendors and distributors that your business will rely on to complete transactions. If, for example, you are taking sales orders online and using a fulfillment house, you will include a mention of the fulfillment house that you are working with and how they benefit your operation. Again, the listing of vendors or outside services with which you will do business is less significant than why you have made specific choices.

Additionally, a contingency plan of action may also be necessary if your business is highly sensitive to weather conditions or factors that are out of your control. For example, the owner of a vendor driven weekly flea market/carnival might include, in his business plan, contingency arrangements in the event of inclement weather.

Over the life of the business, the manner in which you do business will change significantly, as you will need to keep up with competitors and address changes in technology, the economy and in marketing trends. In addition, your business may grow from a small one or two person operation into a larger scale business with the need for a larger space and additional staffers. A business plan written ten to fifteen years ago, for example, typically did not include sales done via the Internet or the need for computer savvy employees to handle such sales. For this reason, you should include some general projections of how you expect the operational plans of your business to change and grow over time to meet the demand for increased sales.

Management & Ownership

This section features short (one to three paragraph) biographies of the key personnel involved in forming and running the business. You will also include key staff members and members of your Board of Directors. What each member of the team brings to this business, including pertinent past experience and significant attributes, should be included. His or her key responsibilities in the company should also be noted.

The organizational structure of the business should be included so that readers will have a clear understanding of how day-to-day operations will be managed.

Generally, this is one of the easier, less time consuming sections of the business plan to put together. There is, however, a need to be careful when writing this section to avoid some common mistakes.

For example:

- Be selective and use past experience that is specifically applicable to the new business.
- Do not use superlatives.
- Focus on a person's work background and not on his or her business philosophy.
- Be concise.
- Make clear distinctions between what individual's roles are. (i.e. don't simply list 11 Vice Presidents).

Explaining who is behind the company and what each person brings to the table is of great interest to any potential investor.

Funding Tip

Many venture capitalists view the makeup and experience of the management team to be the most important element of a business in determining what companies to invest in. If you have a skimpy or inexperienced management team, the likelihood of getting venture funding decreases dramatically.

Sales & Marketing

This section will address sales tactics, pricing, advertising and an overall marketing plan. Your sales and marketing strategies will need to coincide with your overall company goals and vision. External influences, including changes in the marketplace, competition and the overall economic climate will play a role in how you plan to market your business.

Manufacturing companies will want to include their methods of sales and distribution, which may include:

- On-premise selling by your field representatives
- Direct selling using the Internet and/or telephone
- Direct on site selling through your own facility or factory outlet
- Wholesale selling, using distributors or commissioned sales representatives
- Other means of sales

Retailers will include an overview of their anticipated product sales. This should include all means of selling such as:

- In store sales
- Internet sales
- Catalog sales

Specific sales strategies including anticipated promotions, should also be included. In addition, you can use charts and, or, graphs to represent potential sales growth patterns. Be conservative in your sales estimates and back up your projections with reasoning that supports your sales plan.

Service providers need to detail how the services will be offered to the public. If, as is now the case with many businesses, hard goods and services are both sales options, indicate how both will be sold and how they will be tied together.

Pricing

Pricing needs to be carefully determined to be in line with the market you are trying to reach. Various factors will influence your pricing strategies including:

- Your costs of purchasing or manufacturing goods
- Time involved in performing a service or making a sale
- Economic factors
- Location
- Competition
- Market conditions
- Consumer needs
- Seasonal activities

- Availability or exclusivity of an item or service
- Manpower or labor involved

Your pricing strategy should be explained to reflect the applicable factors listed above along with your overall market strategy. For example, you may be setting your prices low to penetrate a crowded market. Conversely, you may have an offering that is unique to your demographic region and can therefore set higher prices. Or you may be pricing in line with market competition and using customer service and other means in which to set your business apart from the nearest competitors.

Marketing

Marketing will play a significant part in the success of any new business. To create a successful marketing plan, you need to first do market research and learn as much as possible about your potential customer base. By learning the preferences and buying habits of your projected target audience you can create a marketing plan that will peak their interest and meet their needs.

Your marketing plan, outlined in the business plan, should include:

- An overview of your current market
- Description of your target audience
- New markets you plan to tap into
- Methods of reaching your target audience.

You will also need to outline your positioning strategy, which is how you plan to portray your product or service in the marketplace. This will include promotional and advertising campaigns. Typically, the types of media you plan to use for advertising such as print, television, radio, online banner ads, Internet paid listings or search engines, etc. will also be included. Explain how your choice of marketing vehicles will allow you to best reach the demographic audience that you are targeting.

In building your advertising and promotional campaign you will need to define the image that you are seeking. For example, are you trying to establish your business as a high-end company or a cost saving alternative to established brands? The corporate image of the company will be part of your plan.

Targeting Your Audience

When forming a new business it is usually advantageous to focus on capturing a specific narrow market. Typically, this will allow the new business to establish itself. Trying to mass market a new business (in most industries) can be difficult because the business is competing against larger, established, well-known companies. It is also more cost effective for start-up companies to go after a smaller target audiences to establish themselves.

You may also want to include your plans for:

- Promotional activities or sponsoring events
- Contests, coupons and free giveaways
- Special incentives and discounts
- Trade show representation
- Search engine optimization and search engine marketing
- Social media marketing

The marketing plan should provide a cross section of carefully selected methods designed to reach your target audience with the features and benefits of your product or service. It should be outlined in the business plan in a manner that shows diversity and fits within the scope and means of your overall budget.

Financial Plan

From start up costs to the day-to-day operational budget, a solid financial plan should be outlined within the overall business plan. It's advisable to sit down with your accountant, financial advisor or CFO to outline the financial structure of the business before including it in the business plan.

The financial section should outline:

- How much money is necessary to start the business
- How much money will be needed over the next two, three and even five years
- How funds will be utilized
- A timeline of when you will need funding

All of these elements of your initial financing should coincide with the goals and visions of the business as stated earlier in the business plan. The financing necessary to cover operations, marketing and promotion (discussed earlier)

Financial documents will include:

- Break-Even Analysis

- Balance Sheet
- Projected Profit and Loss Statement
- Projected Cash Flow Statement

You should include month-by-month details for your cash flow projections and income statement for the first year of business. Then follow up with quarterly information for two more years.

The financial plan will also include the start-up budget and operations budget, indicating what you need to launch the business and how much you will need to keep the business going on an ongoing basis. Include: salaries, wages, insurance costs, accounting costs, equipment costs, legal fees, taxes, cost of goods sold, advertising and promotional expenses and all other pertinent costs in each of your two budgets.

Review Your Business Plan

Once you have completed your business plan, go back and review your work. Make sure that you:

- Include all major sections
- Include a Table of Contents listing where each section can be found
- Cover all key points in clear and concise language
- Proofread carefully for spelling and grammar
- Fact check to make sure all data is accurate and all claims are substantiated
- Eliminate any extraneous information
- Have clearly visible contact information on a cover page and at the end of the document
- Present all graphs or charts in a clear and easy to read manner
- Have not over-estimated your financial projections or underestimated your time frame for launching the business

Remember, this document is typically designed to attract investors and also to provide a blueprint for the business. It should illustrate the goals, objectives, strategies and means of operations for the new business. It should, therefore, be presented in a professional manner. Neatness and attention to detail indicate that you are serious about this business endeavor.

A Mini Plan

A condensed, or mini version of the business plan can prove beneficial. Such a plan can be used to introduce the company to prospective investors in a concise manner, which can then be followed by sending the detailed plan to those parties who are most interested.

Such a mini plan should contain two or three paragraphs on most of the sections that would be found in a larger business plan. This would include:

- A short description of the business
- An overview of the market or industry analysis
- A review of the products or services the company offers
- An overview of the marketing plan
- A chart outlining financial projections over one, two and three years
- A short biography of each of the key members of the management team

If this shortened version of the business plan is intended to raise funding, you should add how much money will be needed to start the company and where existing capital has come from to date.

The key to making such a mini-plan effective is to strip down the details into the “TV Guide” version, highlighting the most important elements of each section and presenting them clearly.

Just as with a longer, detailed business plan, you will need to review the mini business plan carefully to make sure that what you have stated is accurate and that you are not over-estimating your financial projections. Proofreading is also a must.

Often, condensing the market or industry analysis and the marketing plan into a few short paragraphs are the most difficult tasks. If you include some broad numbers to illustrate the state of the industry and then follow that up with a paragraph that highlights the three or four leading players, you can provide a general overview of the market in which you will be doing business. Conclude the section with a third paragraph highlighting how you foresee the business fitting into the market and capturing a share of the existing market. Condensing the marketing plan means you will have to outline, on a broad level, which methods you will use to attract attention to the product or service. Mention packaging, promotional materials and, or, advertising that will be key to your overall marketing plan.

You can find a sample of a mini business plan in Appendix A: Forms & Agreements.

Web Resources

For a wealth of practical help and guidance in writing a business plan you may want to look at www.bplans.com, which features a business, plan outline, expert advice and sample business plans.

Also www.Businessplans.org has a wide range of sample plans to serve as models and provide ideas and a sense of structure when working on your business plan.

Confidentiality

On the front page of the business plan, indicate the confidential and proprietary nature of the plan. For example, you can have a legend at the bottom that states “Confidential and Proprietary. Copyright © 2012 by ABC, Inc.”

You also want to be careful about putting overly sensitive information in the business plan. If you intend to send the plan to venture capitalists or other investors, most of them will not agree to sign a Non-Disclosure Agreement or Confidentiality Agreement.

Chapter 3

Starting a Corporation

-
- Choosing a Name
 - Picking the State of Incorporation
 - Costs of Incorporation
 - Board of Directors
 - Officers
 - Drafting Bylaws
 - Issuing Stock
 - Stock Ledgers
-

In order to start a corporation, there are several necessary steps that need to be taken including filing Articles of Incorporation (called “Certificate of Incorporation” in some states) and paying appropriate fees. Incorporation papers can be easily obtained from your state government, from business software packages, online or in corporate kits. Beyond filing the forms, several choices need to be made and corporate formalities and responsibilities need to be handled. Having an attorney work with you on the process of incorporation is strongly advised.

First, prior to filing any papers, you will need to select the state in which you want to incorporate. A name for the corporation needs to be selected and researched to make sure it is available in your state of choice. You will also need to pay the appropriate fees in the state in which you are incorporating.

Your corporation will need to establish bylaws, appoint a Board of Directors (or a single director) issue stock certificates and hold Board of Directors meetings at which minutes will be recorded (or provide for written consents in lieu of meetings). Shareholder meetings are also typically required, however, in most cases a document signed by all, or a majority of, shareholders (called a consent action) can be submitted instead of having to hold a shareholder meeting. Each of the above-mentioned steps takes some effort, but is worthwhile for personal liability protection and other benefits of incorporating, as discussed in Chapter 1 of this book.

Choosing A Name

There are four primary concerns when selecting the name of a new corporation.

- The name needs to comply with the rules of incorporation in your state.
- A name search needs to be conducted to make sure you can legally use the name.
- The name needs to serve the company by being distinctive or highlighting the benefits of the company in order to draw attention from prospective customers or clients.
- The name should be researched to see if there is any conflict with outstanding trademarks, trade names, service marks, service names or domain names.

States will vary in their regulations regarding corporate names, but typically you will need to use either "Corporation", "Incorporated" or an abbreviation of one of these corporate designations in your corporate name. Certain words or phrases are also generally not permitted in most states, such as "bank" unless the company is actually a bank and properly registered as such.

It is important to conduct a name search prior to registering Articles of Incorporation. While doing such a search, you can typically reserve a name for 30 to 120 days – in most states. To do a name search you can begin by simply going on the Internet and looking for similar business names. You will also be able to find out from the state office in which you are incorporating whether or not the name you have selected is already being used by another corporation.

In addition, you will also want to do a trademark search and an overall name search of businesses in the region in which you will be doing business. Often a business that is not incorporated is using a name that may be either the same or similar to yours. Trademark law provides that if your business name is too similar to that of a competitor, you can be accused of trademark infringement. This can result in your having to change your name at a later date, which can be a costly process. Therefore, researching business directories and databases is advantageous.

You can do a state trademark search through the state trademark database, which is often found in conjunction with the Secretary of State's office. It is also possible to search for a federally issued trademark through the Patent & Trademark Office (www.uspto.gov).

Once you incorporate, your corporate name will be registered with the state. If, however, you are then going to use other "fictitious" names under which to sell products or services, those names need to be registered in accordance with state law and regulation regarding fictitious names or "doing business as". Once again, do a name search, using business listings, the Internet and the local Chamber of Commerce.

It is possible for two businesses operating independently of one and other to have the same names. If, for example a local house cleaning service in Columbus, Ohio and a pet store in San Diego, California both happen to have the same fictitious name, there will generally be no problem with using the name since the businesses are neither competitive in their type of business or in the market or region they serve.

It is also important that if you plan to do business over the Internet, or have a web presence for promotional purposes, that you also do a domain name search to make sure the name that you would like to use is available for Internet use. Most often a company will want to have a similar online name to that of their corporate or fictitious name.

Besides the need to do a name search and the need to comply with state requirements, selecting the right name can be significant for business purposes. You want a name that:

- People will easily remember
- Can be spelled and pronounced easily
- Fits your type of business
- Appeals to your projected target audience
- Defines what it is your company does

The type of business will often dictate how “clever” the name should be. For example a law firm or accounting firm may simply use the last names of the owners, while retailers may need shorter, more creative names to capture customers’ attention. Service providers try hard to include the benefit of their service in a quick title, such as Federal Express, which indicates that you can get your package anywhere in the nation in short amount of time. It also lends itself to a short catchy phrase, FedEx. It is best to think of several variations of a name that you would like to use so that you have options available in case your first choice of business name is already taken. Doing market research within selected demographic groups can also be very helpful when determining what a name means to your target audience and how they will react.

Picking The State of Incorporation

Although it is often assumed that you must incorporate in the state where your business resides, that is not the case. You can select any of the 50 states or the District of Columbia in which to incorporate. Your decision as to where to incorporate depends heavily on:

- A) The cost factors involved in incorporating in the state where your business is physically located compared to those involved in doing business as a foreign corporation in another state
- B) The tax structure and corporate laws of the individual states

It is typically less expensive and involves less paperwork to incorporate in the state where your company is physically located than it is to incorporate in another state and do business as a foreign corporation in your own state. Typically, small corporations that will be doing business on a local or regional basis incorporate in the state where they are physically located and conducting business.

To incorporate in another state with the intent of doing business in that state, your business will need to qualify as a foreign corporation in that state. Qualification is not difficult and includes a company name search and the filing of a certificate of authority in that state. Additionally, if you are incorporated in another state or doing business as a qualified foreign corporation in other states, the corporation is also typically subject to taxation and annual report fees in each of those states. A drawback about doing business as a foreign corporation in another state is the possibility of having to deal with legal claims or lawsuits in that state.

Publication Requirement

A few states, including New York, Pennsylvania and Arizona require that a new corporation be listed in the newspaper. Inquire in your state as to whether there is such a publication requirement.

Costs of Incorporation

The actual cost of incorporating is usually rather minimal. Each state has its own fee structure in place for corporations. Typically, costs include:

- Filing fees
- Annual report fees
- Attorney fees
- First Year Franchise Taxes

Filing fees, including administration fees, vary from state to state but will usually fall anywhere from \$50 to \$350. Some states will also require every business to obtain a business license, which can typically be obtained for a nominal fee. Annual report fees will generally run in the \$25 to \$200 range, depending on the state. Arizona, Georgia, Nebraska and Pennsylvania also require a new corporation to pay a publication fee, which ranges from \$150 to \$300.

The size and scope of your business and will dictate your legal fees. A law firm specializing in start-up business will generally charge in the \$500 to \$5,000 range for assisting you, as a small business owner, with the incorporation process. They can help you fill out the documents necessary for incorporating, explain the process and review the paperwork you have filled out prior to filing. Legal costs will increase if you have multiple shareholders or complicated shareholder arrangements.

The other “cost” of incorporating, is that of paying first year franchise taxes. The tax rates vary from state to state but will usually land somewhere between \$800 to \$1,000.

Incorporation services such as LegalZoom.com will also charge various fees.

Board of Directors

A corporation must have a Board of Directors. The Board of Directors is charged with the overall responsibilities for the corporation. The state in which you incorporate will determine how many directors must be on the Board. In many states this may be only one person if you only have one shareholder. In some states there is a minimum of three directors unless the company has fewer than three shareholders.

The shareholders appoint the Board of Directors, which can, and often will, include some of the shareholders. In small businesses the owner may be the sole director. Sometimes, however, as a corporation grows, it becomes advantageous to bring in an additional director, or directors, to present other opinions and expertise on business matters.

The role of the Board of Directors is to manage the corporation. This will likely include establishing policies which the business will follow, and making major business decisions such as:

- Establishing and amending Bylaws
- Issuing dividends
- Approving major contracts or mergers
- Making key decisions regarding budgets for the company
- Electing or appointing officers

Most often the Board does not handle the day-to-day activities of the business, but leaves that responsibility to the officers of the corporation.

The Bylaws in each state, set the parameters, which must be followed by the Board of Directors. Generally, this will include:

- Board of Director meetings held quarterly or monthly
- Recorded minutes from each meeting

It is important that minutes be accurate and reflect the work done by the Board, which is expected to act responsibly and make decisions that are in the best interest of the corporation. While each state will mandate that an annual board meeting be held, this does not preclude the Board from holding additional, special meetings as deemed necessary.

The first Board of Directors meeting should typically include:

- Approving the corporate Bylaws
- Establishing procedures including record keeping
- Deciding on the corporation's fiscal year
- Selecting or appointing the corporate officers
- Electing S Corporation status if appropriate

- Authorizing the sale of stock

Additionally, a stock certificate should be drawn up in advance to be accepted as the official corporate certificate at this first meeting. Stock certificates should then be issued.

Board members are required to act in a prudent manner on behalf of the corporation's best interests. The Board must also act cautiously in managing the affairs of the corporation and no Board member should put his or her personal interests ahead of those of the corporation. All Board actions should be documented to show that corporate business was conducted responsibly. Even if the Board consists of only one director, it is important that all activities be carefully and accurately documented.

Officers

Corporate officers are typically responsible for the day-to-day operations of the company. Most states stipulate that a corporation must have a President (or CEO), Secretary and Treasurer. In a small corporation this can usually be one person for all of the roles. Larger corporations can have Vice Presidents and other corporate officers.

Even though most states allow one person to wear many corporate hats, the individual or individuals holding positions as officers may be held accountable for not properly fulfilling their responsibilities.

The President is responsible for managing the corporation, following the directions of the Board of Directors and can typically enter into contracts and agreements on behalf of the business. The Treasurer (or CFO) is responsible for corporate funds, maintaining all financial records and issuing all financial reports. The Secretary is responsible for maintaining corporate records, following corporate formalities and, typically, for taking the minutes from all corporate meetings.

Vice Presidents are then generally appointed to handle specific areas of business as deemed necessary or as the business grows. Examples include Vice President of Marketing or Vice President of Sales.

Bylaws

Bylaws are, by definition, the laws or rules governing the internal affairs of an organization. The first corporate Board meeting is usually the time when the bylaws are first adopted. There may be revisions made, but the initial Bylaws are necessary as a provision of incorporation. In a corporation, the Bylaws will:

- Guide the day-to-day activities
- Establish corporate policies
- Establish a schedule for holding Board of Directors and shareholder meetings

- Provide rules of order for running meetings
- Provide the structure used for selecting officers
- Provide guidelines by which stock certificates will be issued
- Provide for indemnification for officers and directors

Books and software programs are available that provide a draft of corporate Bylaws and most corporate lawyers have a set of corporate Bylaws that they start from. It is worthwhile to get a hold of a template before drafting Bylaws. This will indicate how Bylaws should be broken down into individual sections which will cover all applicable rules and regulations pertaining to shareholders, the Board of Directors, officers, committees, the use of outside contractors, policy making, corporate actions, etc. The powers granted to Board members and officers as well as the procedures used in selecting, electing or removing board members or officers from appointed positions would also be included.

The Bylaws should include details explaining how amendments can be proposed and added in the future. It is advisable to work with an attorney when drafting Bylaws.

Once Bylaws have been drafted and approved, copies should be printed and be readily available in the corporate headquarters.

Issuing Stock

A corporation is responsible for filing a notice of stock issuance, preparing stock documentation and certificates, and then issuing the stock certificates to shareholders.

The Articles of Incorporation will state how many shares the company is authorized to issue. All issued shares will represent ownership of the company. Therefore, if a company is authorized to issue 5,000 shares, but only issues 2,000 of those shares, the individual with the highest percentage of those 2000 shares is the majority shareholder, despite the fact that there are 3,000 remaining shares of unissued stock.

Typically, incorporation rules and regulations do not stipulate how many shareholders a corporation must have. Therefore, in small companies, the shareholders are most often the original owners who started the company. However, as a business expands, so may the number of stockholders, each owning a share of the corporation. While shares of stock are initially purchased directly from the company and typically held onto by people closely associated with the company, shares may be purchased from other investors in the open market. Ultimately, for larger corporations, this leads to trading shares on a stock exchange, such as the NASDAQ, New York Stock Exchange or the American Stock Exchange.

When issuing stock in a small corporation, you can determine who will receive shares of stock, what percentage of the corporation each shareholder will own and how much shareholders will pay for each share of stock. A Stock Subscription Agreement will spell out the details of the transaction including the price per share and number of

shares purchased. A sample Stock Subscription Agreement can be found in Appendix A: Forms & Agreements.

Typically, a new business will not issue all of the authorized shares at the onset. Some percentage of shares will be held (or remain unissued shares) to be issued at a future date to new investors or employees. The most important factor for new business owners to remember is that when issuing stocks, the percentage of shares a person owns gives that individual a larger share of ownership in the company. Regardless of the price per share, if one person holds 51% of shares issued, he or she has largest percentage of ownership (assuming all of the shares are one class).

Stock Certificates

The act of actually issuing stock certificates is relatively simple. On the front, of face of the certificate, you will include the name of the corporation, the date, name of the shareholder and state in which the company is incorporated. In addition, the number of shares issued to the shareholder, number of authorized shares and the value at which the shares are being issued are also included. Certificates are numbered sequentially and are stamped with the corporate seal. The certificates are then signed by the corporate President and Secretary. The number of shares issued should be carefully recorded in a stock transfer ledger.

A corporation needs to not only be established in conjunction with the rules of incorporation under the laws of the individual state, but must be maintained as such by following ongoing requirements and formalities. Numerous corporate improprieties in recent years have created a climate in which corporate regulations and formalities are now being more closely scrutinized.

The issuance of stock must be in compliance with federal and state securities laws. This is a topic where you definitely need help from an experienced corporate attorney.

A small corporation, issuing stock only to family members and those individuals who have been active in forming and running the company, is typically exempt from having to register such securities offerings with state or federal agencies. (However you have to jump through some hoops and make appropriate filings to take advantage of the exemption.) If the stock is issued to a limited number of people and not made available to the general public, you may not need to register the stock. Registration is generally necessary if the stock will be sold to a large number of outside investors, by brokers or on the open market.

For a Checklist on Issuing Stock, see Appendix A: Forms & Agreements.

Incorporation Kits

It is possible to purchase what are called incorporation kits. These kits, available online and from legal supply companies provide a do-it-yourself approach to incorporating – although it is still advisable to consult a lawyer. Kits, which are state-specific, typically include:

- ✓ Articles of Incorporation form for the state
- ✓ Corporate Bylaws or samples thereof
- ✓ Forms for keeping minutes at shareholders or Board of Directors meetings
- ✓ Forms for meeting notification and waiver of notice
- ✓ Travel expense and medical reimbursement vouchers
- ✓ Seal and stock certificates
- ✓ Additional forms and templates

Kits are usually in leather bound volumes and run from \$45 to \$100.

The Stock Ledger

The purpose of a stock ledger (also called a stock transfer ledger) is to keep accurate records of all stock transactions made by your company. It is an essential part of your corporate records book. The stock ledger should include each shareholder's name and address along with the number of shares he or she owns plus the certificate number, class of stock, date of purchase or issuance and consideration paid.

Whether the corporation redeems shares or a shareholder sells his or her shares to someone else, all transactions should be recorded to keep the ledger current. If stock options have been granted and are exercisable, they also need to be recorded.

Many start-up companies neglect to maintain their stock ledger. In time, they may be faced with the slow process of trying to research and record such information. Not having such records can impinge upon new offerings of securities, future rounds of funding, new investors, mergers or acquisitions.

Corporate stock ledgers can typically be found in corporate kits at business stationary stores or in software packages.

Chapter 4

Raising Financing for Your Business

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- Loans
 - Stock Sales
 - Angel Financing
 - Lease Financing
 - Venture Capital
 - Bank Financing
-

Raising financing may be the most intimidating, and often most difficult, aspect of starting a business. Funding does not come quickly and it is generally harder to obtain than most business owners believe it will be. However, in today's business climate, there are a wide variety of options available besides borrowing money from a bank. Your success at securing the financing that you need will depend largely on:

- The strength and marketability of your business idea
- How you present your business idea
- Your business plan
- Your credit history
- Your level of preparation
- Your level of experience and training to operate and manage the business

There are a multitude of business ideas. The key to securing financing for yours is to do your homework and make sure that you present a business idea that sounds profitable to potential investors, without major risks, and on reasonable terms.

Loans

Gone are the days where business owners were dependent almost entirely on banks or loans from friends/relatives. Today, there are many different sources available for business loans.

Loans typically come in three primary forms.

- Short-term business loans provide capital for a business in need of cash to start operations. These loans are generally for one year or less.

- Intermediate term loans can help start-up businesses pay for equipment and cover large initial expenses. Such loans are usually for anywhere from one to three years.
- Long-term loans are often used to assist start-up businesses with initial costs such as equipment, furniture fixtures and commercial mortgages. Such loans are generally from three to seven years and repayment is typically made in installments.

Before approaching a lender it is important that you have a clear understanding of what the loan will be used for and how you can best present such information. It is equally important that you have a realistic plan for repaying the loan.

When working on a loan request, you want to include the following, some of which will likely be included in your business plan.

- The purpose of the loan
- Specifically how much money will be needed
- A management profile
- An overview of the market including your projected customer base and competition
- Personal and business financial statements and if possible, collateral that can secure the loan

Typically, if a small business owner is requesting a loan, the lender will want to see that he or she is investing a proportionate amount of his or her own money into the venture. In addition, for a larger business venture, the lender may want to see other sources of financing.

You will also need for a significant amount of supporting documentation when applying for a loan. Such documentation may include, but not be limited to:

- Incorporation or LLC organizational documents
- Proof of ownership or sale, if you purchased the business
- Material contracts
- Letters of reference
- Financial statements including personal tax returns for the last three to five years, a list of assets and liabilities and even credit references
- Tax returns

Receiving a loan will depend in part on the criteria and expectations of the lender. While one lender may say no, the next may say yes after reviewing the same loan request, business plan and documentation. If turned down for a loan, you can benefit from learning why you were rejected. If several lenders turn down a loan request for the same reason, you will know which area or areas you need to work on, whether it is improving your credit rating or rethinking your plans to purchase real estate for the business.

Once you have been approved for a loan, you need to work with the lender to obtain terms with which you feel comfortable. The due date and manner of payment will need to be determined. Will you pay the loan back in one lump sum or in various payments on a set schedule? Most often loans are made in several payments. Make sure such a payment schedule will work for your business in conjunction with your projected cash flow. Also of significant importance is the interest rate. You should get an idea of the going rate for similar loans and be ready to negotiate. Some state laws mandate the maximum amount of interest that can be charged on a loan. Below that, there is flexibility.

You will also want to look at other fees associated with the loan and what is considered a default of the terms of the loan. Read the loan agreement carefully and have a lawyer review it as well. Some of the terms are more common than others and some can be negotiated or even waived.

There are several organizations (see Appendix B) that work closely to help secure loans for minority business owners. They recognize that minority based businesses sometimes need greater assistance when getting started.

SBA loans

The Small Business Administration (SBA) is a service of the U.S. government designed to help small businesses in numerous ways through a variety of programs. Created in 1953, the SBA now has offices in all 50 states, plus the District of Columbia, Puerto Rico, the Virgin Islands and Guam. The SBA does not make direct loans but works in conjunction with lenders. The loans are made by the lenders and guaranteed by the SBA for as much as 85% on loans of less than \$150,000 and 75% on loans of more than \$150,000. This means that if the borrower cannot repay the loan, the government will reimburse the lender for a percentage of the loan. Lending partners that work with the SBA review the loan application and may accept the application without the need of the SBA guarantee. Loans can be provided for almost any aspect of business including the purchase of equipment and machinery, inventory, real estate or construction needs. SBA loans typically have a maximum term of 25-years. There are numerous SBA programs offered and widely utilized

The SBA has their main headquarters at 409 Third Street Southwest in Washington, D.C. You can, however, call 1-800-U-ASK-SBA or go to their website at www.sba.gov to find the closest regional office.

Stock Sales

A proven way to raise capital is to sell shares of stock. While selling stock to the public is generally not an option for a small business, selling stock in a private placement is a way of procuring cash from investors and maintaining control over who become shareholders in your company. Prior to selling shares of stock you will need to receive Board approval and possible shareholder approval. In addition you will need to set a stock price and have the stock sales agreements in final shape.

Of course, to even consider selling shares of stock, you need to have a company that shows signs of potential growth and profitability. Your business plan, financial projections and marketing plan will serve as key factors in convincing someone to purchase stock in your company. You need to show potential shareholders how their money will be spent and what you foresee as the growth pattern of the business.

To issue private stock, you can make a private placement offering that does not necessarily need to be registered with the Securities & Exchange Commission (SEC). A number of exceptions are in place to allow the small business owner to issue stock without having to go through the lengthy and somewhat difficult process of registration with the SEC. However, the offering still needs to comply with state and federal laws. This will typically require filings with state securities administrators.

While selling shares of stock can provide you with much needed capital, it also means that you will be relinquishing some degree of control. Shareholders will have a say in electing directors of the corporation. They can also review corporate books and records and vote on key corporate decisions. Review the stock sale agreement terms carefully with your attorney and make sure you understand all of the company's rights and obligations. It is imperative that you understand exactly what the stock offering will include and that it adheres to securities laws. A benefit of relinquishing some control through selling stock is that you may be able to utilize the knowledge and business experience key stockholders may bring to the company.

When selling private stock to start a small company, it is likely that you will know most of your shareholders. Maintaining a good relationship with shareholders is important. They will be more willing to assist you and buy more shares if and when offered if you keep them informed as to the operations and prospects of the business.

A Private Placement Memorandum

When a business is looking to raise funds by selling securities, a document providing full disclosure is typically required. A Private Placement Memorandum (PPM) is used to disclose such information about the company. Also known as an Offering Memorandum, this is an important document for small businesses and should be drawn up with the help of an experienced securities attorney.

Angel Financing

Angel investors are individuals who personally invest directly in a business. Often, they invest in early stage business. The term "angels" comes from investors who used to provide money to salvage a theatrical production that otherwise might not have had the backing to open. Traditionally, angels have been successful high net worth individuals, looking to get involved on the ground floor of a growing business for any of several reasons, from an opportunity to use their years of expertise to tax benefits to shrewd investment opportunities. As more wealth has been accumulated by a younger

segment of the population over the past decade, angels are now also young investors looking for the next innovative idea to get behind.

It is estimated that over twenty billion dollars are invested in start up or young growing companies by angel investors.

The typical angel investor:

- Is well educated
- Invests in an area of personal interest or industry with which they have been associated
- Does not get involved in the daily routine and operations of the business
- Makes an average investment of anywhere from \$10,000 to \$250,000
- Look for companies that have large growth potential

Angel investors, once thought to invest more often on a whim or based on their personal impression of a business or the individual behind it, are now exercising greater due diligence. They look for a sound business plan that clearly demonstrates how the business will work. Additionally, they want to be convinced that the management will be able to implement the plan. While angels are typically more patient than lenders, they want to know how soon the business will be able to see a profit or have an exit. Generally, they do not want to be the only source of funding and want to know where future investment capital is likely to come from.

A meeting with an angel investor should be set up in person. You should be ready with written material (business plan, projections, etc) and prepared to answer the tough questions. Angel investors want to see that you:

- Have done your homework and researched the industry thoroughly
- Stand firmly behind your business plan and goals
- Have thought through all aspects of the business from a practical aspect
- Have an experienced management team

Being prepared for meeting with an angel investor requires more than just knowing what is inside of your business plan. Due diligence on your part is necessary concerning the angel. Find out what you can about this investor's background, interests and past investments. You should know something about the person from whom you are requesting money. A personal rapport can be a key part of the success of the relationship.

Although you want an angel to invest money, you also need to establish what the business arrangement will include. Traditionally angel investors were often silent backers putting money into a project that they believed in but having little to do with the business beyond making their investment. Today, however, you will find angels who want to be involved in all key decisions and those who will provide guidance and expertise from afar. You need to establish from the onset the amount of involvement the angel investor wants in the management decisions and operations of the business.

Finding Angels

For years it was typically through friends and business associates that one would need to network in order to find the name of angel investors. Such investors kept a particularly low profile. Today, however, angels have, in some cases joined together to form groups and are also listed with business and investment organizations.

Individually, angel investors still fly below the radar, but in newly formed groups they are more accessible than in the past... many now having a web presence including posted guidelines telling entrepreneurs what types of businesses they are interested in backing and how to best go about reaching them. Unlike venture capitalists, who invest money from a variety of other sources, the angels in an investor group invest their own money. Angel investors may be inclined to fund very early stage companies and take greater risks.

The Internet has been particularly helpful in linking new business owners up with such groups. Websites, such as AngelList.com feature links to a variety of angels located throughout the country. Angel investors are often more likely to invest in business ventures in their state or region of the country. In many cases they focus on specific areas, such as the angels at angelmoney.com, who focus on investing in emerging technology businesses.

Tips For Finding Angel Investors

- ✓ Use your personal and business network and follow all prospective leads to investors.
- ✓ Look for seminars, forums, conferences or other gatherings that focus on raising capital, such as those by New York City's Angel Society.
- ✓ Surf the Internet for matching services or angel groups or bands. - - in particular, check out AngelList.com
- ✓ Affiliate with other entrepreneurs in local associations and alliances. While many business owners are secretive about such key investors, others may know investors who are looking for other new ventures.
- ✓ Focus on establishing one good angel-entrepreneur relationship because from one such relationship others often emerge as angel investors contact friends who may also be looking for a sound investment.

Lease Financing

It has become increasingly more common in recent years for companies to lease equipment. Each leasing agreement needs to be read through carefully to understand the terms and conditions within.

Typically a lease can run anywhere from one to five years. Most equipment necessary in commercial businesses today, including technical equipment, can be leased. Some

leases provide an option to then purchase the equipment at substantially less money when at the end of the term of the lease.

By leasing equipment, if structured properly, you can maintain your credit availability, as the lease debt does not have to be considered a direct liability on your financial statements. This is advantageous, as it does not limit your ability to borrow from lending sources.

Advantages of lease financing:

- It offers fixed rate financing. You pay at the same rate monthly.
- Leasing is inflation friendly. As the costs go up over five years, you still pay the same rate as when you began the lease, therefore making your dollar stretch farther. (In addition, the lease is not connected to the success of the business. Therefore, no matter how well the business does, the lease rate does not change.)
- There is less upfront cash outlay. You do not need to make large cash payments for the purchase of needed equipment.
- Leasing better utilizes equipment. You lease and pay for equipment only for the time you need it.
- You typically have an option to buy equipment at end of lease term.
- You can keep upgrading. As new equipment becomes available you can upgrade to the latest models each time your lease ends.
- Typically, it is easier to obtain lease financing than loans from commercial lenders.
- It offers potential tax benefits depending on how the lease is structured.

One of the reasons for the popularity of leasing is the steady stream of new and improved technology. By the end of a calendar year, much of your technology will be deemed “dinosaurs”. The cost of continually buying new equipment to meet changing and growing business needs can be difficult for most small businesses. For this reason leasing is very advantageous. Leasing can also help you enhance your status to the lending community by improving your debt-to-equity and earnings-to-fixed assets ratios.

There are a variety of ways in which a lease can be structured. This provides greater flexibility so that the lease is structured to best accommodate the individual cash flow requirements of a specific business. For example, you may have balloon payments, step up or step down payments, deferred payments or even seasonal payments.

Disadvantages of Leasing

Leasing is a preferred means of financing for certain businesses. However it is not for everyone. The type of industry and type of equipment required also need to be considered. Tax implications also need to be compared between leasing and purchasing equipment.

- You have an obligation to continue making payments. Typically, leases may not be terminated before the original term is completed. Therefore, the lessee is responsible for paying off the lease. This can pose a major financial problem for the owners of a business experiences a downturn.
- You have no equity, until you decide to purchase the equipment at the end of the lease term at which point the equipment has depreciated significantly.
- Although you are not the owner, you are still responsible for maintaining the equipment as specified by the terms of the lease. Failure to do so can prove costly.

Venture Capital

Venture capitalists raise money from various institutional and pension fund investors to back start-up and growing companies that show strong potential to develop and become big. Venture capital firms go through a process of raising funds from foundations, endowment funds, retirement funds, corporations and foreign investors. Similar to a mutual fund, a venture capitalist firm pools investment dollars and then looks for solid investments.

Most often, venture capitalists look for very big returns, making them more selective than angels who may invest in smaller businesses. They are devoted to raising money for new and emerging business ventures so they want to maintain a strong track record in raising fund for successful companies. Therefore, they are most often seeking to invest in companies that will grow quickly and see large profit margins.

Venture capitalists generally invest in several businesses at a time to limit their risk. Typically, they will also become involved in the business, providing their experience and expertise in the industry. This is, in part, because unlike angels who are investing their own money, the venture capitalist firm is investing the money of other people or institutions.

Like most other types of financing, venture capital is usually part of the equation. A venture capital firm may want to know that there are other sources of funding. In many cases, venture capitalists look at the long-term picture and if the business grows according to the plan, it may receive several rounds of funding. However, the business must account for how all funding has been used and follow the goals and plans set forth in accordance with the previous round(s) of financing.

There are also various types of venture capitalists. Some will focus on providing seed money for a new business venture, while others will come in only later on in the development of the business. Venture capitalists may specialize by investing in specific industries or types of businesses. They may only serve a specific geographic region or only provide funds for expansion purposes of an existing business. It is important that you research the investing criteria of a venture capital firm before approaching them.

It is also imperative that you be well prepared before meeting with such a venture capitalist. This means you will need to present a well-honed business plan and, as is the case with most potential investors, be able to answer all the hard questions about the business. This includes:

- Having a clear vision of the business and being able to articulate that vision.
- Understanding potential obstacles that you may encounter and having plans for dealing with such obstacles or setbacks
- Having a clear idea of how long it should take to show a profit
- Presenting a strong, experienced management team
- Providing a well-planned marketing strategy that defines your target market and how you plan to reach them
- Demonstrating enthusiasm and confidence that your business can meet any challenges and succeed
- Presenting a large market opportunity
- Showing proprietary technology or rights

If a venture capital firm is interested in your business, it will do its own due diligence and evaluate the background and history of the management team, the financial projections and the market in which the business is involved. A venture capital firm might be interested in providing seed money to a new business but may hesitate if, for example, they become aware of potentially steep competition in the marketplace. All potential investors will do research to determine the validity of their investment. Venture capitalists may go farther and dig deeper since they are usually dealing in larger amounts of money and are responsible to many investors. Therefore, be ready to hand over all documentation requested, ranging from your Bylaws to recently executed contracts so that they can evaluate your business thoroughly.

If all goes well and a venture capitalist is interested in working with you, a term sheet will be issued. This is a proposed contract of sorts, which includes how much the venture capitalist is willing to invest, the conditions of the investment and how the money is expected to be used. A lawyer should be present who is familiar with reviewing such term sheets and negotiating this type of deal.

Bank Financing

Traditionally, banks are more conservative with their investment dollars. Unlike many venture capitalists or angel investors, they are far more likely to approve a loan for an established business over a start-up or emerging company. This is largely due to the fact that they are investing the money of their depositors.

However, thanks to government agencies such as the SBA (mentioned above), which work with many banks, small business owners can get business loans from banks with a strong business plan and well prepared business loan request. And, banks are more

likely to give modest sized loans, whereas venture capitalists are looking for much larger deals.

First and foremost, prior to approaching a bank, you should have all of your key documents in order, starting with a solid business plan. You will also need to have the most recent financial statements available, projections for the business (this is typically in the business plan) and a repayment plan, plus collateral.

Collateral may include:

- Hard goods such as equipment
- Real estate
- Stocks or bonds
- Other personal assets
- Personal guarantees

Banks also want to know that you are making your own investment in the business. A bank is more likely to approve a loan if (pending a solid business plan) they see that the owners are investing a good percentage of the necessary start up capital into the business.

In order to maximize your chances of receiving approval on a business loan from a bank it is wise to look at the situation from the standpoint of the lender. A lender wants to know:

- Exactly how this business will operate and why it is anticipated that it will make money
- Exactly how the money will be used
- How you plan to repay the loan and over what time frame
- That you are willing to take a significant financial risk in the business
- That you are responsible and can manage this business
- Who else is involved in management or operations and that they will also be responsible for the proper use of the money from the loan

The smaller the business, the more closely the individual behind it will be evaluated. Most small businesses, in the forms of sole proprietorships or partnerships, are closely tied to the experience, know-how and overall character of the owner(s). Therefore, you need to make sure that you get your own financial records in order before asking for a bank (or any lender) for money to start a business. A solid personal credit rating is also very important since the small business is typically an extension of the individual starting it.

Chapter 5

Bookkeeping & Accounting

-
- Income Statements
 - Balance sheets
 - Record Keeping
 - Budgets & Projections
 - Using Accountants & Bookkeepers
-

While accounting and bookkeeping will probably not be the most interesting aspects of your new company, these are necessary elements for running a successful business. By having accurate and current financial information available, you can make important decisions concerning the business, monitor your ongoing financial status and comply with legal and government requirements.

It is typically to your advantage to have an accountant and/or bookkeeper working on maintaining your finances and keeping you abreast of your financial situation. Later in this chapter we will discuss hiring such professionals. Meanwhile, it is important that you have a working knowledge of the accounting and record keeping process that is vital to nearly all businesses. This will allow you to always keep a watchful eye on your financial situation and make sound business decisions.

Income Statements

One of the most common and important documents will be your income statement. Also called a profit and loss statement, this document provides you with a periodic summation of the profits and losses of the business during a specific time period, which may be one month, three months, six months or a year. The income statement, appropriately named, will provide you with an overall statement of your net income during the selected time period. It will prove advantageous for:

- Paying taxes
- Evaluating your current financial position
- Making financial projections
- Attracting potential investors

The manner in which an income statement works is relatively simple. By listing both revenues and expenses, you can determine how much money you have earned. It is a

simple formula in which you add up your revenues, add up your expenses and subtract the expenses from the revenues. (Revenues – Expenses = Net Income)

The Income Statement answers the question; “How is the business doing?” during a given time period. It allows you to see if you are spending too much money and if so, in which areas you could cut back. It also allows you to compare time frames such as the first quarter of 2012 versus the first quarter of 2011. This way you can compare your profits or losses and determine where you need to make adjustments. Your Income Statement should also help you determine your tax liability.

Typically, an Income Statement lists all revenue and expenses. The degree to which you breakdown each expense category will depend on the size and nature of the business along with the types of categories with which your business is most closely involved. For example, one business may have a general category for computer costs but a company in the technology industry, which relies heavily on the purchasing and maintenance of their computer system, might list specific items including; hardware costs, software costs, maintenance and repairs, and so on.

The Income Statement will typically include:

- Total or gross sales. This sales figure shows the amount of revenue generated by the business from sales.
- Net sales. This is the total sales, less returns or refunds.
- Cost of goods sold. This includes all costs associated with manufacturing or acquiring the products you sell. In the service industry it is the cost of performing a specific service.
- Gross profit. This is the net sales, less the cost of goods sold.
- Operating expenses. This includes individual categories for employee salaries, payroll taxes, advertising, rent, office supplies, utilities, depreciation and all else necessary to operate the business.
- Operating profit. This shows you the difference between your gross profit and your operating expenses.
- Net income before taxes.
- Income taxes. Here you list the amount owed to the federal government. If you pay state or city taxes, include them here as well.
- Net income (after taxes).

The net income after taxes is your profit (or loss). By looking at your net income on periodic Income Statements, you can determine how the business is doing. If you are seeing steady losses you will need to make changes in operations or cut the costs of goods or services sold.

The Balance Sheet

Along with the Income Statement, the Balance Sheet will provide you with the data necessary to make sound financial decisions. The Balance Sheet lists the assets and

the liabilities of the company. The difference between your assets and liabilities will be the net worth of the business at the end of a specific period ($\text{Assets} - \text{Liabilities} = \text{Net Worth}$). The net worth of your business at a given time is of particular interest to prospective investors and lenders.

The assets of the business are that which have a cash value including:

- Investments held by the company
- Equipment
- Machinery
- Display cases
- Inventory
- Cash and cash equivalents
- Accounts Receivable

Capital assets, or fixed assets, are the long-term assets, such as any building the company owns or the machinery used to produce goods. These are assets that are expected to be around for several years. They are also assets that can depreciate over the years, such as the new computer you purchased last year. Accumulated depreciations are deducted from your list of fixed assets. On the other hand, a building that you own might appreciate in value. This, however, is not reflected on the balance sheet until the building is actually sold.

The liabilities are all of the debts that the business owes. This may include:

- Money owed on equipment
- The mortgage on your building
- Accounts payable
- Accrued wages (which are wages owed to employees)
- Insurance and health benefit payments

Once you get a total of your liabilities you will add the Owner's Equity in the business, which consists of how much he or she has invested into the business and how much of the profits are still in the business. This is essentially the net worth of the business. Therefore, you would list on the balance sheet:

- Invested Capital
- Retained Earnings

Added together you will get the owner's equity. This total, together with the total liabilities should balance with your total assets. Hence the name "Balance" Sheet.

In addition to a Balance Sheet and Income Statement, you will want to keep a Statement of Cash Flows, which allows you to track the cash in and out of your company throughout the year. All manners in which the company uses cash can be recorded, including operating, financing and investing activities. By listing both the

previous and current cash amount on the Statement of Cash Flows you will be able to determine the increase or decrease in each activity for a specified time period.

For sample financial statements, including a Balance Sheet, Income statement and Statement of Cash Flows, see Appendix A: Forms & Agreements.

Record Keeping

Good record keeping can indicate, on paper, how your business is doing and whether or not you are making a profit. You can get a good idea of which items are selling, which services are being utilized or both. Typically, business owners look at their records to analyze the current situation and determine what changes or improvements can be made. Essentially, good record keeping can be the difference between business success and failure.

In addition to monitoring the progress of your business, good records will help you when preparing financial statements and preparing your tax returns.

Inventory, expense tracking, payroll and salary records, employee information, client information, receipts, bank statements, accounts receivable, billing and accounts payable are among the many records you will typically need to maintain while in business. Record keeping should be done in a diligent, consistent and timely manner, regardless of the type of system you choose to use.

As business operates, you will create an ongoing “paper trail” which will provide the source of all business transactions through purchase orders, receipts, deposit slips, and so on. Gross receipts will help you indicate how much income your business is generating. Likewise, keeping records of all purchases will tell you how much you are spending on materials used for the business or items for resale. You need to maintain records of all of your income sources and expenses. Also, employee related records including all employment taxes need to be maintained.

While many small businesses are using computer software to handle bookkeeping and record keeping, it is not imperative. Maintaining ledgers and using proper forms, available in most business stationary stores, can serve your purposes as well. For those business owners looking to set up their record keeping procedures on the computer, you’ll need to keep things in mind:

- You want to purchase the software package that fits your specific needs and not be lured by one that simply has the most features.
- The goal is to save time by using a software program. If it takes you more time to set up the computer record keeping system then you need to complete the tasks, then you’re better off using ledgers and paper.
- If bookkeeping tasks – on computer or manually - are cutting into time better spent in other areas of the business, then you should consider hiring someone with bookkeeping skills for a few hours a week to handle

the task and free up your time. More on hiring a bookkeeper later in this chapter.

Inventory Records

Another set of records you may need to maintain (depending on the type of business) are inventory records. Keeping good inventory records will allow you to better manage your inventory holdings. Such record keeping will also help you keep track of buying trends, seasonal activity and pilferage. You'll want to know how much stock is on hand versus the amount that you purchased and can do so by keeping records of the purchase date of the items in stock, purchase price, sale price and dates of items sold. You can use inventory software packages or a ledger or notebook.

To track money coming and going, most small businesses typically use a revenue and expense journal. This is a single entry method of accounting where receipts and expenditures are recorded. The other method used, a double entry system, is more time consuming, but records both a debit and a credit for each entry, marking the item sold as a credit and the money taken in as a debit. If you choose to use a computer software program to record revenues and expenses, you might consider:

- Quicken by Intuit (Single entry accounting)
- Microsoft Money (Single entry accounting)
- Quickbooks from Intuit (Double entry accounting)
- Peachtree Accounting from Peachtree Software (Double entry accounting)

Break Even Analysis

It helps any business, particularly a start-up, to determine at what point you will break even. By projecting how much revenue in sales you will need to take in versus your ongoing expenses, you will be able to determine approximately when you should break even and subsequently show a profit. Such an analysis can help you monitor your progress so you can see if your projections are on track. If not, you can make adjustments. Many established companies also look closely at the Break Even Analysis to determine where to make cutbacks.

Budgets & Projections

Your budget will assist you when tracking the flow and progress of your business by providing you with a picture of how much you are spending and in which areas you are exceeding your projected spending limits. A budget can be prepared for a specific area such as promotion and marketing or a special project or as an overall guideline for your small business.

To formulate your budget, you will come up with a reasonable projection of your sales. The budget will set forth the cash available to the business. For a new business you will include the funding you have obtained through personal financing, loans, investments, selling shares of stock and other sources. Once you have a realistic forecast of the money you anticipate having available, you can look at the potential categories of expenses and determine a realistic amount to spend in each category. Most budgets are works in progress with several revisions.

You need to establish several numbers, including the total you anticipate spending in each category and a finite ceiling, or maximum on spending that you do not plan to exceed. Create your numbers based on specific research. For example, you should have a good idea of the types of advertising that will best benefit your business and get realistic costs for such advertising options. Then determine an amount that will benefit you in the advertising category. Can you, for example, reach your target market for \$10,000 per month? If you are budgeting for this category in a major market, the answer is probably no. In a small market, however, this might serve as a workable number. For a small locally based business you might start with a much smaller amount.

You will also need to evaluate exactly how many employees you need to operate your business. Therefore, you should research the going rate of pay for such services and look into the cost of benefits packages. Study the workforce statistics in your area or region and see if you can offer a comparable package to attract quality employees. Then budget the proper amount for salaries.

Remember to include rent, taxes, insurances and all other necessary expenses. You will then have to prioritize and make adjustments as you go. Obviously, you won't be able to change the amount you pay in rent, but you can change the amount you put toward marketing if there is not a sufficient amount left in your budget. It's always better to be conservative than to make unrealistic assumptions and base your numbers on pie-in-the-sky hopeful thinking. It's also advantageous to give yourself some room when budgeting for purchases.

Using a previous budget as a guideline is always advisable. From year to year a business will typically need to make various adjustments, but the basic categories of expenses typically remain the same. If you are starting a new business, look for similar business models to your company. Keep in mind that such a similar business should be serving a similar market.

Timing also needs to be factored into your budget. Many businesses have peak seasons where revenue is higher and times of the year where they have additional expenses. For example, a seasonal business might not budget for advertising costs in its quiet time of year but budget more money toward advertising just prior to its busy season.

Budget tips:

- Set maximum spending limits that you won't exceed and monitor your budget closely so that you'll know when your spending is approaching such category limits.
- Don't juggle unless you absolutely have to. Try not to take from one pocket and move to another too often. It becomes increasingly harder to balance the budget if you keep moving money around.
- Be realistic with your projections.
- Make sure everything is clearly explained. While different businesses may categorize items in their own various ways, what matters for your business is that you can look at the budget and understand which items fall under which categories. Note: Go over each category carefully with your accountant, bookkeeper or anyone else who is working on your financial statements.
- Over-budget for areas in which you are more likely to have unexpected expenditures.

Using Accountants & Bookkeepers***Accountants***

When looking for an accountant for your business, the emphasis is on finding someone who will not only help you file tax returns, but can also provide ongoing financial advice and guidance. Typically, to find an accountant whom you can place your trust in and the future of your business, it's advisable to ask other business owners for recommendations. Discuss the type of business that you are starting and see if he or she has experience working with that type of business. Some accountants specialize in working with specific types of businesses and others are particularly familiar with the needs of small businesses.

Use a similar hiring process as you would when hiring any other key employee. Set up interviews and get to know the strengths of each individual. It's also very important that you have a good rapport and a strong sense of trust in this person who may hold your financial future in his or her hands. Remember that you should be working with an accountant and not relying on him or her to make key financial decisions for you. Therefore, keeping up on the activities of your accountant, or anyone working with your finances, is a must.

A good accountant is someone you can:

- Trust implicitly
- Expect to be up on the latest changes in tax laws and guidelines
- Rely on for specific advice as it pertains to your business
- Expect to maintain the confidentiality of your financial information

Bookkeepers

Most people who start out in business are fairly convinced that they will be able to keep their own books. With the proliferation of software products on the market it would seem that the process should be fairly simple. The belief is that you will:

- Save money by not hiring a bookkeeper
- Keep a closer eye on the financial aspect of the business
- Maintain privacy

While a small start-up business may allow for such self-management, as a business grows it is typically in the best interest of the owner(s) to hire bookkeeping help. Someone who specializes in the field can, in the long run, save you time and money. The details involved in maintaining accurate books can be lost when combined with the many other tasks and responsibilities of running a business. A business owner's time is too valuable to spend on journal entries. For this reason, there are individuals who specialize in the field.

Prior to hiring a bookkeeper, estimate the amount of hours he or she will need to prepare your books on a monthly basis. Small start-up companies generally do not need a fulltime bookkeeper. Use word of mouth and ask another business owner who handles his or her books and whether or not he or she would recommend their bookkeeper. The local Chamber of Commerce, industry associations, Internet job sites, or even your accountant can also prove to be worthwhile sources for finding a qualified bookkeeper.

Do's & Dont's About Hiring Bookkeepers & Accountants

While the vast majority of employees are basically trustworthy, you can inadvertently hire someone who will steal from you in some manner, whether they are padding the payroll, making deposits into a personal account or flat out embezzling funds. Employee theft has been steadily on the rise in recent years. It is, therefore, worthwhile to be cautious and follow some basic do's and don't when it comes to putting your financials in the hands of others.

Do:

- ✓ Establish clear and specific guidelines from the start
- ✓ Review the books periodically, but not at any "regularly scheduled" time
- ✓ Review all financial statements
- ✓ Read your own mail

Don't

- ✓ Put too much financial responsibility in any one person's hands
- ✓ Let your accountant/bookkeeper use software that you are not familiar with
- ✓ Give check-signing authority to anyone until they are proven to be reliable and trustworthy
- ✓ Hire someone who is unfamiliar with your type of business

Chapter 6

Small Business Tax Basics

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- Income Taxes
 - Pass Through Taxes
 - Sales Taxes
 - Payroll Taxes
 - Employment Taxes
 - Tax Software
 - Tax Planning
-

If you are starting a business, it is essential that you familiarize yourself with all of the necessary tax forms that you will need to file with the IRS and the various taxes you will be required to pay.

Every business is required to file a federal tax or information return. The type of business entity you have selected (as discussed in Chapter 1) will determine the manner in which you will file and subsequently pay taxes. A “C” Corporation, for example, will be responsible for paying corporate taxes, while the owner of a sole proprietorship will report the income or losses from his or her business on his or her personal income tax return. Payment will then be based on the sole proprietor’s personal income tax rate.

In this section we take a broad overview of the various types of taxes that you will encounter when going into business. It is highly advisable that you seek professional guidance from an accountant before filing your tax return. Look for someone who is familiar with your type of business.

It is also important to remember that as soon as you form a business you will need to obtain an employer identification number (EIN) from the IRS by filing Form SS-4. Your EIN, combined with the individual social security numbers of your employees, will provide the tax identification data needed by the IRS.

Income Taxes

A business is typically expected to pay estimated taxes quarterly throughout the fiscal year. Such estimated taxes are due for businesses that will anticipate having a tax bill of at least \$500 at the point of filing an annual return. Form 1040-ES from the IRS will help you determine how much in estimated taxes you should pay. Payments are made

to the Federal Government, and in most cases (depending on the state tax laws) to the state as well.

With the potential of facing IRS penalties, it is important to pay such quarterly estimated taxes on time or request an extension in advance of the due date. To calculate your tax bill you need to consider the following options.

You will be expected to pay:

- 90% of the overall tax that you will owe
- or 100% of last year's tax figure (110% if the total income is over \$150,000)
- or annualize based on the previous quarters, minus expenses, and then pay at your personal income tax or corporate tax rate.

Your accountant should help you make the decision as to which method of calculation is best for you based on your business entity.

“Ordinary & Necessary” Business Expense

Typically, all “ordinary and necessary” business expenses can be deducted from your business income when filing your business tax return. Such deductions may include business travel, office and/or computer equipment, attorney and accounting fees, delivery costs, utilities and rent. These are items that are necessary to properly conduct your business. Mileage accrued for business related travel can also be deducted at the current rate allowed by the IRS (see www.irs.gov).

Keep a careful record of your expenses and have backup material on hand for documentation whenever possible. If you have incurred expenses that are both business and personal in nature, such as a trip that was for business and personal reasons, you can deduct a portion of those expenses. Use discretion when determining what portion of the total expense was business related. Make sure to document all such expenses.

The steady rise in home-based businesses has created some gray area regarding business deductions. As is typically the case, you need to be able to justify each deduction in the event a tax auditor should question it. If you conduct business from a home-based office, for example, you can claim a deduction for the portion of your home that is being used for business purposes. Accordingly, you can also claim a percentage of your utilities, phone bill and other related costs such as Internet service used for business purposes. Save your bills and show the percentage you used as a business expense.

For all deductions you will want to maintain a paper trail including receipts listing the date, name of the person or the business that received the payment, the total amount paid and the category of the business expense.

Pass Through Taxes

The business entity you select will determine whether or not there will be pass through taxation. Partnerships, LLCs and S Corporations are examples of businesses that have pass through taxes. In each of these forms of business, taxes are passed through to the owners who then report the income or loss on their own personal income tax returns.

Unlike a C Corporation where there may be double taxation, since the corporation pays taxes as a separate entity, and any shareholder receiving dividends is also subject to tax, an LLC or S Corporation can pass through profits or losses without paying any additional corporate taxes.

According to the IRS, in the case of a pass-through entity classified as a partnership, tax returns must be filed by the 30th day of the 4th month following the end of a pass-through entity's taxable year. In the case of a pass-through entity classified as an S corporation, tax returns must be filed by the 30th day of the 3rd month following the end of such a pass-through entity's taxable year.

Tax Deferred Retirement Plans

If your business is structured in such a manner that you are paying tax on your profits from the business as part of your personal income tax bill (such as a sole proprietorship), you should consider having a tax deferred retirement plan. While such a plan is always advantageous for saving money toward reaching your retirement goals, a SEP, Keogh or SIMPLE plan will defer some of your personal income from the business and lower your tax bite. Your financial advisor should be able to help you in making this decision.

Sales Taxes

Although congress has toyed several times over the years, there is still no federal sales tax. Most states, however, charge sales tax on retail products sold. Sales tax rates vary from state to state and may also be imposed by a city or local government. The amount is determined as a percentage of the gross receipts for the items sold, not the net profit the seller makes on the items. Some states allow for specific goods, such as food, clothing or footwear, to be exempt from carrying sales tax. Make sure you know which, if any, retail items are exempt from sales tax in your state. Sales tax may also be imposed on rentals, leases and certain services depending on statewide regulations. If you are doing business in any state that has a sales tax, as a business owner, you will be responsible for charging, collecting and recording the tax.

The manner in which sales taxes are imposed also varies. The sales tax is typically imposed on the purchaser of the item, but in some states, the tax is imposed on the seller who usually passes the tax liability along to the customer.

Prior to filing sales tax, you will need to apply for, and secure permits or licenses for your various business locations. Such permits or licenses should be displayed at each of your business locations.

Having what is considered a “presence” in a state is the criteria used by the IRS to determine whether or not you are liable for paying state sales tax.

If you do not have a physical presence in another state, but sell items via the Internet or by catalog in that state, you can be subject to a state’s “use tax”, but typically not to their state sales tax (although the law is evolving in this area). A “presence” in another state does not necessarily mean that you have a retail outlet in that state. If you have an office, warehouse or have employees working for you in that state, the IRS may consider you to have a presence in that state. Make sure you are aware of your sales tax responsibilities in all states in which you are doing business.

Sales tax must then be reported and paid in a timely manner to the appropriate state collection office. This is usually done on a monthly basis. You need to check the requirement carefully for your state. Failure to pay sales tax or making late payments might cause you to incur a tax audit and/or potentially heavy penalties.

Payroll Taxes

Payroll taxes are due either semi-weekly or monthly depending on the size of your payroll. The IRS will dictate the schedule. If your total payroll won’t come to \$2,500 for the quarter, you can file quarterly.

You may consider using a payroll software program to handle your payroll needs. If your company is growing and you have an increasing number of employees, you might opt for an outside payroll service. The largest such services are Automatic Data Processing (ADP) and Ceridian. Both specialize in handling your payroll needs. ADP alone provides paychecks to over 30 million workers.

Social Security & Medicare (FICA)

The Social Security Program, created in 1935, by an act of Congress (the Federal Insurance Contributions Act or FICA) has relied primarily on withheld payroll taxes from employee paychecks to generate retirement savings. The goal was to provide American citizens with retirement income or financial assistance in the event of disability or death of the primary wage earner. Today, more than 90% of retired Americans receive Social Security. Unfortunately, because the rate of inflation has outpaced Social Security, the impact of the program on retiree’s income is less significant than in the past.

Medicare, meanwhile, is designed to help people over the age of 65 pay for medical costs. While it does not pay for many types of medications, it does help nearly 98% of Americans over the age of 65 with some portion of their medical bills.

In addition to the money that, by law, is withheld from each employee's paycheck for FICA, the employer is also required to match the amount. The amount for FICA is currently 7.65%, which is comprised of 6.2% for Social Security and 1.45% for Medicare. To determine how much Social Security and Medicare tax to pay, see IRS Publication 15.

The time frame in which you are required to pay FICA will depend on the size of the payroll. The larger the payroll, the faster you need to send in the payments. For example, a very small business with one employee might file quarterly, while a large company with a \$100,000 weekly payroll, will need to file within three days after payroll is completed. Again, this schedule will be provided for you.

Some Common IRS Tax Forms You Should Know About

SS-4	Application For Your Employer Identification Number (EIN)
W-2	Employer's Wage and Tax Statement
W-4	Employee's Withholding Allowance Certificate
940	Employer's Federal Unemployment Tax Return
941	Employer's Federal Quarterly Tax Return
1040	Estimated Tax
1099	Miscellaneous Income: Used to report compensation for non-employees
1120	US Corporate Income Tax Return
8109	Federal Tax Deposit Coupon: Used to deposit taxes.

Employment Taxes

Each business is required by law to withhold federal income taxes from the wages of its employees.

Federal Withholding Taxes

Withholding taxes are filed in accordance with the W-4 Employee's Withholding Allowance Certificate, which is filled out by each employee. The W-4, in conjunction with IRS Publication 15, is used to determine how much federal income tax you are required to withhold. Amounts will vary depending on:

- The number of withholding allowances claimed by the employee
- The marital status of the employee
- Any exemptions from withholding taxes claimed by the employee

Employees can change the amount withheld by submitting a new W-4 Withholding Certificate and changing the number of withholding allowances (dependents) and their tax status.

If you do not withhold the proper amount, fail to pay federal withholding taxes or pay late, you are subject to penalties by the IRS.

Note: All businesses that employ other people on the books must have an individual EIN, or Employment Identification Number. Therefore, if you are partners in more than one company, or you purchase a new business in addition to your own, you will need a separate EIN for each business entity or company. By filing an SS-4, Application for Employer Identification Number, you can obtain additional EIN's from the IRS service center in your state for each business.

Unemployment Taxes

To insure that unemployment pay is available to employees who have lost their jobs, the Federal Unemployment Tax Act of 1939 was passed by a vote in Congress.

According to the Department of Labor, "The Federal-State Unemployment Insurance Program provides unemployment benefits to eligible workers who are unemployed through no fault of their own (as determined under state law), and meet other eligibility requirements of state law."

Businesses are required to report federal unemployment tax on IRS form 940 and pay both federal and state unemployment tax. Unlike FICA and federal withholding taxes, unemployment taxes are not withheld from the employee's wages, but are paid entirely by the business. The state unemployment tax rate is a percentage based on the total number of employees you have and the number of former employees that are collecting unemployment at any given time.

If you pay the full amount to the state, the federal government only requires you to pay .8% for up to \$7,000 in income, for each employee on your payroll, which is a minimal amount (\$56). However, the federal unemployment tax is 6.2% if you do not receive the maximum state credit.

Who Qualifies As An Employee?

The proliferation of contractors, freelancers and consultants can blur the definition of who qualifies as a company employee. For tax purposes it is important that you understand which individuals are considered your employees by the IRS, regardless of common terms such as "consultants" or "contractors". Typically, an individual is considered an employee if he or she meets several requirements including, but not exclusive to:

- Receiving his or her primary income through working for your business
- Receiving direction from you on a regular basis
- Having his or her pay rate controlled by your decisions

- Being specifically trained to perform tasks or jobs for your company
- Working on your schedule, in your facilities and not having a business location of their own
- Receiving benefits from your company

Together these criteria can indicate, by IRS definition, that someone is considered your employee.

Non-employees, doing work for your company, including all independent contractors, freelancers and consultants, who earn over \$600 in a given year from your business, are required to receive an IRS Form 1099. The form will state the amount of money earned from your business during the calendar year. You are not required to withhold any money, and the independent contractor is, therefore, responsible for reporting the income on his or her own personal tax return.

Tax Software

There are a number of software products on the market designed to handle your tax related needs including payroll taxes, sales taxes and tax planning. While in the market for tax software products you should:

- Compare prices
- Make sure the program meets your system requirements
- Carefully evaluate the various features
- Make sure the program interfaces with software programs that you may currently be using and can import tax data
- Look for a program that is “user friendly” for your staff and offers a demo

Tax software programs are typically updated annually to take into account new tax laws and changes on tax forms. Be careful that you are not using a system that has become outdated.

Among the many popular software programs you'll find are:

Turbo Tax Business: One among several popular business software programs from Intuit, Turbo Tax is designed to help various types of businesses prepare tax documents. Included are: tax saving tips, deduction finding capabilities, IRS approved forms and a tax reference library. It is also designed to interface smoothly with Intuit's QuickBooks bookkeeping software programs. See www.intuit.com

Tax Pro: Designed to make tax filing easier, separate versions of Tax Pro are geared for either small businesses or large corporations. You can preview on-screen reports and enter data directly onto graphic representations of IRS forms. Preprinted forms are then easy to prepare, print and file on paper or electronically. Single user and multi user versions are available, enabling you to enter up to 5,000 transactions. See www.1099pro.com

After-the-Fact Payroll (AFP): This program, from Accountantsoffice.com, allows you to generate W-2, W-3, 1099, 1096 and other payroll tax forms. The program can also produce vendor reports, earnings reports, unemployment reports and allows for easy entry of payroll checks into the payroll register. Also available from Accountantsoffice.com is the **Tax Relief** program. See www.accountantsoffice.com.

Master Tax: Four versions of the Master Tax software programs are available to assist you in filing payroll taxes. You can import payroll data or enter it manually. A wide range of features are offered to produce reports and file federal, state and local payroll taxes. See www.mastertax.com.

Websites, such as www.taxsites.com and popular retail sites including Amazon.com or PC Mall.com provide listings of the various tax related software programs. In some cases, you can try a demo version of a program to see if it fits your comfort level.

Helpful Tax Websites

- ✓ The Internal Revenue Service - www.irs.gov
- ✓ Small Business Tax & Management - www.smbiz.com
- ✓ Business Town - www.businesstown.com/taxes
- ✓ Social Security Administration www.ssa.gov

Tax Planning

Tax planning should be done in conjunction with the guidance and expertise of your accountant. One of your first priorities will be to make an informed decision regarding the structure of your business, as discussed in Chapter 1. That decision, with help from your accountant, will make a significant impact on your tax status and subsequent planning.

Typically, a good tax professional will consider all aspects of your current business and personal financial situation. The size and nature of the business, number of employees, along with the most recent federal, state and local tax laws, will all play a significant role in such planning.

The bottom line will be to have a plan that limits your tax bite, while not hindering your ability to have the capital or resources you need on hand to conduct business. In addition, you want to make sure that any tax loopholes you decide to slip through, as part of your tax strategy, are legal and won't lead to a tax audit or to IRS penalties.

Chapter 7

Hiring Employees

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- Employment Interviews
 - Employee Applications
 - Offer Letters
 - Employment Agreements
 - Confidentiality and Invention Assignment Agreements with Employees
 - Employee Paperwork
-

Having the right employees is critical to the success of any business. Good employees can follow instruction, present new ideas and motivate other employees to work hard. They are dedicated, conscientious, trustworthy and do not need to be micromanaged. Conversely, the wrong employees can not only slow down or impede the progress of your business, but can cause you to lose money through wasted training time, improperly performed tasks and even stealing. Furthermore, any incompetence or improper activities by your employees can reflect poorly upon you and your business.

Before hiring anyone, you should familiarize yourself with the laws and regulations imposed regarding soliciting and interviewing employees. Protecting employee rights, physical safety and maintaining fair treatment are at the heart of most laws created to safeguard the hiring process. Laws protect against discrimination on the grounds of race, religion, national origin, age, sex or disability. They also protect against sexual harassment and unfair treatment of employees. You not only need to be aware of such employment laws, but you can protect your business by establishing appropriate policies.

Labor Laws

The United States Department of Labor (www.dol.gov) administers and enforces nearly 200 federal laws covering workplace activities. The laws fall under various congressional acts and are enforced by various divisions of the DOL. Included are laws pertaining to:

- ✓ Wages & Hours: Under the Fair Labor Standards Act, administered by the Wage & Hours Division of the Employment Standards Administration (ESA)
- ✓ Workplace Safety & Health: Under the Occupational Safety & Health Act, administered by the Occupational & Safety Administration (OSHA)
- ✓ Pension & Welfare Benefits: Under the Employee Retirement Income Security Act, administered by the Employee Benefits Security Administration (EBSA)
- ✓ Unions & Members: Under the Labor-Management Reporting & Disclosure Act, administered by the Office of Labor-Management Standards (OLMS)

The DOL enforces other laws pertaining to drug testing, polygraph use, garnishing wages and family & medical leave.

Depending on the types of positions you are looking to fill and the immediacy of your needs, you will determine the best manner in which to find employees. Newspaper classified ads, employment agencies, executive placement services, job postings on employment Internet sites, job postings on your own company Web site and word of mouth are all popular manners of finding candidates to fill available positions. The wider you extend your search, the more time you will need to go through resumes and narrow down the field. In some cases the cover letter accompanying the resume will tell you more about the individual than the resume itself.

When reviewing resumes, look for:

- Length of employment at previous jobs
- Previous job titles
- Responsibilities at each position
- Special skills
- Education

Once you have decided which applicants you would like to interview, you need to prepare in advance before they come in and sit down before you. It is helpful to prepare a list of questions that you would like to ask and then review it with your legal counsel. Keep in mind that you need not stick to the script but can follow up on comments made by the interviewee with additional questions.

Pre-interview To Do List

- ✓ Prepare the questions you will be asking in advance and review them carefully.
- ✓ Set up specific time periods on your schedule for interviews. Try to avoid scheduling too many interviews in one day or your recollection of individual applicants may become clouded.
- ✓ Select a comfortable, well-lit, quiet location to conduct interviews.
- ✓ Have a legal pad or paper available on which to take notes during the interview.

Review each applicant's resume just prior to the interview (and file along with your notes following the interview).

Employment Interviews

There are several different philosophies when it comes to the interview process. Depending on the position being filled, some employers will look more closely at specific technical skills, others will be concerned primarily with how this individual will fit in with the team, and some will focus on an applicant's enthusiasm and desire for the position. The need to handle specific tasks, supervise others, meet with clients and/or work independently will factor into how you approach the interview process and make your assessment of the candidates.

Although you can get the answers to many questions from looking at a resume, it is important to hear each prospective employee respond so that he or she can provide greater insight into his or her previous employment and education.

Among the questions you will want to ask include:

- What did you do at your last position?
- What did you like about your last position?
- Why did you leave your last position? Or why do you wish to leave your current position?
- How would you describe your relationship with your co-workers? Supervisors? Clients or customers?
- What accomplishments are you most proud of?
- In which areas would you most like to improve?
- What were your strengths and weaknesses?

You also want to find out about the applicant's reasons for starting in the field and their future plans or goals. Questions you might ask include:

- What made you pursue this field?

- What courses in college and/or graduate school do you feel were most applicable to your work in the field?
- What are your long-term goals or where do you see yourself in five or ten years from now?

When talking about the job in question, you will want to get a feel for how the individual will fit in and handle different situations. After explaining some of the basic tasks involved, you might ask questions such as:

- Which past experiences do you feel will help you most in this position?
- Would you be comfortable supervising x number of employees?
- We use x computer software. Are you familiar with that system?
- What other skills do you feel you can bring to this position?
- This position may require you to put in x number of hours per week or some travel out of town, would that be a problem for you?

Look at other specifics aspects of the position you are looking to fill, such as phone calls, client contact, sales or marketing skills and ask candidates how comfortable they are in handling such specific tasks.

You may also want to ask questions about the applicant's education, particularly with younger candidates who are more recently out of school and have less work experience. Internships have become more common in recent years and you should ask the applicant what she did and what she learned from any internships.

If the prospective employee has had large gaps in his or her employment history, you will want to inquire about what he or she was doing during those time periods.

Typically, you will ask what compensation the individual was receiving at the previous job and what he is seeking at this job. Sometimes this is saved for the second interview. In other situations, where you are limited to a certain salary or hourly wage, you might state that this job pays x or you might provide a salary range. This way you can determine early on in the process whether or not the applicant is interested at all.

Along with the questions and answers, you will want to get a feeling for the comfort and character of the person sitting across from you. However, try not to read too much into body language, since typically most people are nervous on a job interview. It is more important that you get a feeling for what this person brings to the position from his or her past experience and his or her manner of presentation. Candidates should dress accordingly for an interview, depending on the formality of the position.

Interview Red Flags!

You may find certain red flags during the interview process that will indicate that this is not the ideal person for the job. These might include:

- ✓ Inconsistency in the applicant's story
- ✓ Inconsistency between what is on the résumé and the applicant's answers to your questions
- ✓ Unexplained tardiness or improper behavior on the part of an applicant during the interview
- ✓ Avoiding or talking around specific questions but not providing an adequate answer
- ✓ Lack of knowledge concerning your company (showing lack of preparation)

Your Responsibilities

You should explain the position and mention any benefits package that will be included. It is also helpful, although not essential, to give each applicant a little background information about the company.

You should end the interview by asking the applicant if he has any questions. Make sure you know the answers before responding or make it clear that you can find out the answers and let them know. You do not want to misrepresent yourself or your company by answering incorrectly. It is important that any statements you make about the company or about the position are accurate.

And finally, you should thank each applicant for coming in to the interview and shake his hand. You need to be polite and professional throughout the interview process.

Along with the interview questions you should ask, there are several questions you should not ask, including:

- How old are you?
- What is your religion?
- What ethnicity are you?
- What is your sexual preference?
- Are you married?
- Do you have children?
- Are you planning to start a family?
- Have you ever done drugs?
- Have you ever been arrested?

Or any other questions that relate to personal information and are not pertinent to the job. In addition you should not touch an applicant, other than a handshake.

Typically, if an interview goes well, you will want to schedule a second interview with a strong candidate. It is at this time that you should get into describing the job more thoroughly and discussing salary. It is also at this point that you might introduce the candidate to the person who will be his or her immediate supervisor, should that be someone other than yourself. In many cases, the supervisor will conduct the follow up interview.

No matter how much you may feel that someone is right for a job, it is in your best interest to ask for, and contact, references. You also want to ask the prospective employee to sign a form allowing you to do a background check. You should then take the time to do it. Check out past employers to make sure the applicant worked where they claim they did and, if possible, talk to a former supervisor. Also check that the applicant did attend the schools he listed on his resume or on your application.

Employee Applications

Having prospective employees fill out Employment Applications will typically save you time gathering background information. While a resume will include some of their work history, you can obtain more information from presenting your own application.

Applications should provide spaces for basic information such as name, address, phone number and social security number. While you cannot ask a person's age, you can ask if he or she is over the age of 18. You may also want to ask where the applicant heard about the position or who referred them to your business.

Past job history, including job title, key responsibilities, salary history and reasons for leaving the previous positions should be included for at least the applicant's last three jobs.

Education should include high school, college, post graduate work plus special schooling the applicant may have had that would be applicable to the position.

Finally, you need to have a paragraph (review this with your attorney) proclaiming that all statements made by the individual are true and that this application does not signify that any hiring agreement has been entered into. Also, have the applicant answer whether or not it is okay to contact his or her current or previous employer. The Employment Application should then be signed by the applicant and dated.

As is the case with the interview, you cannot ask a variety of personal questions on the Employment Application. Once you have hired someone for the position, you should hold onto the application and the employee's resume. This is the information on which you based your hiring decision, should it ever be questioned in the future.

For a sample Employment Application, see Appendix A: forms & Agreements.

Offer Letters

Yes, you can always call candidates on the phone and hire them, making it clear when you would like them to start work or come in for training. However, you can also present them with a job offer letter which can protect you should the employee someday decide to take legal action against you, a practice that has become increasingly popular and has tied up the legal system with an abundance of lawsuits.

A job offer letter simply puts in writing the terms of the job offer so that ambiguities do not arise later. This also makes it clear that either party can terminate employment when they so choose. In addition, changes made to the terms of employment later on can also be written into the agreement and signed by both parties.

Do's & Dont's of Job Offers	
Do:	<ul style="list-style-type: none"> ✓ State clearly the salary and how often payment is made (weekly, bi-weekly, monthly). ✓ Give the prospective employee time to think about the offer and respond. ✓ If there is a qualifying period before the employee is entitled to benefits, include how long that time period will be. ✓ Include the date of hire and title of the position. ✓ Make it clear that employment is "at will" and that the employee can be terminated at any time by the employer.
Don't:	<ul style="list-style-type: none"> ✓ Promise raises, bonuses, vacations or perks that may not be forthcoming ✓ Make any guarantees that the employee will be employed for any length of time ✓ In short, don't promise anything that you cannot follow up by providing.

Typically the terms of employment are spelled out in the offer letter. However, for executives and other high level employees, you might want to compose a more formal agreement.

Appendix A contains a sample form of an employee offer letter.

Employment Agreements

Employment Agreements are generally designed to spell out and define the terms of employment.

A well-drafted Employment Agreement addresses the following key issues:

- The job description: title, role, and responsibilities

- Whether the employer can change the position
- The length of the agreement
- The salary, bonus, and benefits
- Whether the employee gets stock or stock options in the company (the employee should typically earn these over time)
- When the employee can be terminated
- Severance payments, if any
- The employee's job responsibilities
- The employee's confidentiality obligations
- Where and how disputes will be handled (arbitration is sometimes best)

Confidentiality and Invention Assignment Agreements with Employees

While employed by your a company, an employee may be privy to confidential material. If such materials fell into the hands of competitors it could potentially cost your business its competitive edge. For this, among other reasons, Confidentiality and Invention Assignment Agreements can be drawn up to be signed by employees in order protect such proprietary information.

Such an agreement will also state that inventions that your employees create while working for the company, or new ideas, also belong to the company rather than the employee. This insures that work created by an employee, while under your employ, is owned by company.

A good Employee Confidentiality and Invention Assignment Agreement typically covers the following:

- Disclosure of inventions
- Ownership of inventions, patents & copyrights
- Definition of material deemed "confidential"
- Situations in which material may be divulged or discovered
- What is considered a breach of the confidentiality obligation
- Obligations of employee both during and after employment
- Timeframe of obligation after employment
- Employment at will

Employee Paperwork

Prior to welcoming new employees into the business and before you show them around the office, plant or sales floor, you should be prepared with all of the proper paperwork.

New Employee Paperwork

Consider the following paperwork for the employee to sign on the first day:

- ✓ Employee handbook:: Have employees sign a receipt indicating that they have received and read the handbook.
- ✓ Form W-4: It is mandatory that an employee completes the IRS W-4 Form used to determine the appropriate level of tax withholding
- ✓ Employee benefit elections: Employees should sign up for any such benefit programs, providing all necessary information. This would include company health or pension plans.
- ✓ Confidentiality and Invention Assignment Agreement: This agreement stipulates that all proprietary information will remain confidential and that the company owns all inventions created by the employee, relevant to the company business, while under the employ of the company.
- ✓ Emergency notification: This form lists phone numbers to contact should there be an emergency

An employee handbook should include all practical information on:

- 401k or retirement accounts
- Pension Plans
- Stock Options Plans
- Medical & dental benefits
- Disability Insurance
- Vacation days
- Sick & personal days
- Leave of absence
- Maternity/paternity and family leave
- Adoption benefits
- Legal holiday schedule
- Performance reviews
- Operational policies & procedures
- Safety & security policies
- Codes of conduct
- Sexual harassment policies
- Dress codes
- Email and internet use policies

Short of such a handbook for each employee, there should be a central location such as an Intranet site or a handbook in the office of the person who handles human resources for your company with all of this information spelled out in writing. It's to your advantage

to take the time to carefully think through and list all matters pertaining to employees prior to the hiring process. This can prevent future lawsuits. (More on employment policies in Chapter 8).

You will also need to fill out forms for Worker's Compensation (discussed later in Chapter 13 on Insurance). This protects your business in the event someone gets injured or sick from a job related accident or occurrence.

Keeping Employee Records

While it does take up space in your files and/or on your hard drive, it is important to maintain employee records after the employee has been terminated or leaves your business for any reason. The IRS recommends keeping tax records, including W-2 forms, amounts and dates of wages paid, dates of employment, benefits paid, plus contact information about each employee for at least four years after they have completed their employment with your business.

Whether it is necessary for future legal action, a tax audit or your own statistical data, you may need to refer to past employee records at a later date.

You also need to make every effort to maintain the confidentiality of all employment records. This information should not be available to more than a few select, trusted, employees. Personnel files in the wrong hands can spell legal trouble.

Employee Drug Testing

Some thirty years ago it would have been unheard of, and probably sparked a lawsuit for invasion of privacy, but today it has become a fairly routine business practice to conduct a drug test prior to hiring an employee. As an employer you do not want to be liable for the actions of someone in your employ who is under the influence of illegal narcotics.

While drug and alcohol testing has become more widely accepted in business, you do need to consider the rights of the employee who can file a lawsuit if he feels that his personal rights have been intruded upon. Courts, seeking reasonable cause for such testing, have become increasingly more lenient in allowing employers to conduct the tests providing they respect the privacy of the individual.

If you do decide that you want to screen employees for drug and alcohol use, run it past your attorney to make sure you proceed in a manner that will not infringe upon the personal rights of any employee. Keep a written record of any drug testing that you administer.

Note: Keep in mind that you are, by law, not supposed to request a drug test from a candidate for a job until you have made an offer of employment

Chapter 8

Managing Employees

-
- Motivating Employees
 - Employee Incentive Arrangements
 - Personnel Policies
 - Avoiding Employee Lawsuits
-

While it's not easy to find good employees that you can rely on, it's even more difficult keeping them motivated and inspired to work hard. Many jobs become routine for employees who eventually seek greener pastures elsewhere.

The growth and success of a business is very much contingent on having a solid, motivated staff of individuals. It is, therefore, up to you as the business owner to not only attract, but to retain such valuable employees.

Motivating Employees

To motivate means to use available methods or resources to persuade someone to work harder or excel at what he or she does. If successfully done, it is a means of enhancing the success of your overall business.

Accentuate The Positive

One of the simplest and least costly methods of motivating employees is to show them recognition for a job well done. This can range from a pat on the back to an Employee of The Month Award to a token gift. Small gestures that recognize the positive accomplishments of an individual can often go a long way. It increases the employee's sense of self-esteem and he or she feels better about his or her job. The result is usually better productivity.

The accomplishments of a team or a group should also be rewarded, whether it is for their ongoing work or for a special project. Employee certificates, small bonuses or even giving the team Friday off, can show them that you have recognized their efforts.

The Happy Employee

Typically, studies and surveys have shown that the more satisfied the employee is with his or her job, the better he or she will perform. Therefore, to motivate on an ongoing basis, you need to create an environment in which an employee feels involved and enjoys working.

There are various ways of increasing job satisfaction, which include:

- Providing flexible schedules. Many businesses are allowing employees to work alternative schedules that do not adhere to the traditional 9 to 5 workday. This might include part time schedules or even job sharing, where two people share one full-time position.
- Telecommuting. Some jobs can be performed by employees who telecommute from their home computers a few days a week
- Regularly scheduled performance reviews, which include positive feedback and let employees know what is expected of them
- Encouraging employees to do various tasks so that their jobs do not become routine and boring
- Allowing employees to enhance, improve and decorate their own workspace
- Providing a means of socialization through lunch time or after hour activities
- Stressing that employees can move up and advance within the organization
- An open-door policy, which encourages employees to ask questions or make recommendations
- Making donations to charities selected by the employees on behalf of the company

Strong communication is also a key to having satisfied employees. Make sure that employees know what is expected of them and also let them know that they will be heard if they voice problems or have questions.

Five Common Reasons Why Employees Become Disenchanted

- ✓ They feel nobody in a management position will listen to them when they have concerns, problems, suggestions or complaints.
- ✓ They feel that they are stuck in positions with no potential for advancement.
- ✓ They are bored because the tasks are routine and they are not encouraged to take on new projects or new responsibilities.
- ✓ They only receive negative feedback.
- ✓ The office environment is sterile and impersonal. There is no social aspect to the work environment.

While highly paid motivational speakers may be brought in for “pep talks”, you will more likely receive better results from sitting down periodically with your employees and asking for feedback. Find out what they like about their jobs, what they dislike and what they would like to see changed or improved. You might start with anonymous employee satisfaction surveys, which may allow employees greater latitude in communicating how they honestly feel about company policies, management and their jobs. Do employees feel that they need more training to do their jobs efficiently? Do they feel they need better equipment? Would they like more or less supervision? Would flexible hours help employees who have long commutes or family responsibilities? These are among the questions you may want to include on such a survey.

Do's & Dont's Of Management / Employee Interactions

Do:

- ✓ Compliment employees on a job well done
- ✓ If there are problems/issues, discuss them in one-on-one or team meetings
- ✓ Maintain an open line of communication
- ✓ Provide clear and direct instructions and field questions to make sure all employees are on the same page regarding their responsibilities
- ✓ Provide regular reviews and constructive feedback on employee's work

Don't:

- ✓ Gossip or discuss the work of an employee with other employees
- ✓ Label employees or categorize them
- ✓ Communicate strictly by emails or memos
- ✓ Dangle incentives or promises that you cannot keep
- ✓ Micromanage
- ✓ Stereotype employees
- ✓ Create an impersonal/sterile environment

Employee Incentive Arrangements

What better way to motivate employees than to provide an incentive package? There are a variety of possible arrangements that can be made including: stock options, bonuses and profit sharing plans. Smaller businesses that are not yet seeing significant profits can provide incentives that might include: flexible schedules, telecommuting or additional vacation days.

The type of incentives you offer will depend largely on:

- The size of your business and number of employees
- The structure of your business
- The profitability of your business
- The level of experience and base salaries of the employees
- The economic climate

Stock Option Plans

Stock Option Plans are typically structured so that an employee must be employed by the company for a certain amount of time before he is able to exercise the option (often referred to as “vesting”). For example, a company may offer a stock option of 10,000 shares, vesting equally each year over four years. This means that the employee can, after one year, exercise options for 2,500 shares at the option price set forth on the initial date of grant. If the stock has doubled or tripled in the course of the year, the employee can exercise his option to take ownership of the shares and then sell them for a profit. If, however, the stock has remained the same or the per share price has dropped, the employee can decide not to exercise his option at that time.

In recent years, employees have met Stock Option Plans with less enthusiasm than in the late 1990's. As the stock market took a downturn, the incentive of receiving options became less of a motivating factor. Nonetheless, since the stock market has traditionally rebounded over time, Stock Option Plans still remain a valuable part of a long-term incentive package for employees who are expected to remain with the company for many years. When the economy is strong, Stock Option Plans can make employees very wealthy as they share in the success of the company.

All of the terms, including the time frame, vesting, the exercise price (typically the market price at which the employee can purchase shares of the stock) and the total number of shares of the stock to be issued, should all be clearly detailed in the Stock Option Plan.

Bonuses

A monetary bonus can certainly serve as an incentive. However, it can also set a standard that can be hard to follow. Once word spreads that an employee received a monetary bonus, others will anticipate the same for their good work. Therefore, unless

the bonus is part of an Employment Agreement, you need to establish a policy that details the expectations of an employee before he or she will be eligible to receive such a bonus.

Any plan to offer monetary bonuses should be made prior to the annual budget so it can be included as a budget item. Bonuses are typically determined based on a percentage of the employee's salary in conjunction with his or her position and/or standing in the company and the value of the work he or she has performed.

Besides cash bonuses, other types of incentive bonuses include:

- Gifts
- Extra vacation time
- Extra personal days

The sluggish economy in recent years has caused many companies to become more creative in their incentive plans. Cash value life insurance, flex schedules and other forms of non-monetary perks have been used in lieu of more traditional cash bonuses.

Profit Sharing Plan

If a company is doing well, sharing profits with employees serves as a very strong incentive.

Such plans will need to be carefully designed and spelled out. Typically, the company will set a starting point for determining when profits will be shared, such as once the company earns profits of at least \$250,000 for the fiscal year. What percentage will be shared and who is eligible to benefit from the Profit Sharing Plan must also be determined in advance. For example, a company might decide that 15% of all profits over \$250,000 will be distributed to all senior employees who have been with the company for at least three years. Each employee will receive an amount based on his or her salary at the end of the previous calendar year. All of these parameters should be decided upon with the help of your financial advisor and/or attorney.

Retirement Plans

Many companies offer 401(k) plans, which are retirement plans for long-term employee savings. Employees may contribute up to a certain amount of their salaries into the retirement plan on a regular basis. The money is not considered taxable income upon contribution and it is generally deducted automatically from each paycheck. It is then typically invested in stocks, bonds or mutual funds. The employee can select from several choices of investment options. The employer can also contribute money, or in some cases stock, to the employee's 401(k) plan.

The money invested must remain in a 401(k) plan until the employee reaches age 59 ½, at which time he or she can start withdrawing from the plan without penalties. At this point, however, he or she will pay income taxes. Should an employee change jobs, the

plan can be rolled over into a new 401(k) plan within a certain time frame. Some plans also allow a participant to take out a loan against the plan. The loan must then be repaid before the employee takes any money from the plan in order for the funds to remain tax deferred.

Before setting up such a plan you should review the particulars with your accountant who will help you abide by the IRS rules and regulations concerning 401k plans. Retirement plans are generally an attractive benefit for employees.

Personnel Policies

Policies can help you protect your business from liabilities, while also setting basic ground rules for employees and protecting their rights. All employees should be encouraged to familiarize themselves with all personnel policies, which may be distributed in an employee handbook or posted on an Intranet Web site.

Below, you'll find some of the more common policies. Such written policies can:

- Prevent miscommunication or misunderstandings
- Prevent injuries and help maintain a safe work environment
- Justify actions taken regarding employees
- Minimize employee lawsuits
- Promote team building
- Help maintain structure and order

Hours

One of the basic policies you will need to establish will focus on work hours. From standardized time cards or time sheets to a more casual atmosphere in which employees are simply expected to complete their workload in a defined amount of time, there are numerous variations on the popular 9 to 5 workday. Among the guidelines you will need to establish are:

- What constitutes a "full time" work week
- How you will keep track of employee hours
- What constitutes lateness and how it will be handled
- Flex hours
- Overtime pay

State and federal employment laws will impact upon your policies, particularly regarding overtime pay for certain employees, so be aware of them and know which employees qualify for overtime pay under such laws. If you are employing members of a union you will also have to abide by union rules and regulations.

Security & Employee Safety

An area of growing concern in recent years has been that of security. Your policies concerning the security of your business and of your employees needs to be carefully thought out so that you do not infringe upon anyone's personal liberties, while at the same time you do provide a safe work environment. Such policies should include your safety evacuation program and outline how fire and evacuation drills will be conducted in conjunction with state and local laws and ordinances.

The personal security of all employees should be of primary concern. Many companies issue security photo I.D. cards and computer passwords are commonly used at all levels. Sign-in/out sheets for employees working on weekends or after regular business hours and policies regarding visitors also need to be considered.

In many small companies, only certain employees are allowed to have keys, while in retail businesses there are specific policies regarding the handling of cash or working cash registers. You should also clearly state in your security policies which employees are entitled access to confidential information.

Make sure all security policies are clearly explained to employees and any security personnel you may hire to help enforce such regulations. Your security personnel, or that which handles security in the building in which your company resides, needs to combine a knowledge of your security policies with good common sense and awareness.

Firearms & Weapons

Unfortunately there has been a growing need for companies to include policies regarding having firearms or weapons on the premises. This should be included in your safety and security policy. Depending on the nature of the business, there may even be a need for metal detectors. State clearly what disciplinary actions will be taken should someone be carrying a concealed weapon. As is always the case, review your policy with your attorney. Employees can claim that they have the legal right to carry an item that might otherwise be considered a weapon.

Drug Use

There is no place for illegal drug use in your business. Your policies need to be strong and very clear.

As an employer, your options to minimize illegal drug use include drug testing, which has become quite common today in many businesses. According to the United State Supreme Court, your right to require a drug test depends on the reasonableness of the test. The definition of "reasonableness" has evolved and broadened over the past

twenty years and drug testing is typically found to be within the rights of most employers.

Short of drug testing, or in addition to a drug test, you may require all new employees to sign a Drug-Free Workplace Policy. Such a policy should make it clear that:

- It is unlawful to possess, distribute or manufacture any controlled substance while on company property or while conducting company business
- It is unlawful to be engaged in company business while under the influence of an illegal drug
- Violations of the above policies will result in disciplinary actions that can include termination and even legal action

Understanding that drug, as well as alcohol, abuse can be the results of a physical illness and/or an emotional dependency, some companies are now offering programs to help treat such employees. Unfortunately, many smaller businesses simply do not have the resources or funds to take part in such programs.

Communications & Computer Use

Nearly every business in America has someone who spends too much time on the telephone making personal phone calls. Coupled with personal emails, the amount of non-business related communications taking place during standard “work hours” today is staggering.

While it would be impractical to completely forbid personal calls, such calls should be limited to those that are deemed necessary and important. This policy should include the use of an individual’s cell phone during business hours.

Policies regarding e-mail (and computer use/Internet access in general) should state that:

- The use of email is for business purposes only
- E-mail that includes jokes or content that could be deemed offensive is prohibited
- The use of e-mail to send confidential or other such materials that might be sensitive to the company is prohibited
- The company has the right to monitor and review all e-mail sent and received by company employees
- Visiting Web sites that are deemed inappropriate, including sites featuring pornography, online games or potentially offensive material is prohibited
- No personal shopping or personal business transactions are permitted via the Internet
- Computer use is for authorized employees only
- No one other than the specific employee is permitted to use his or her own personal password

- Any computer virus or malfunction must be reported immediately
- Disciplinary actions will result from the breach of any of the rules or regulations stated in this policy

Vacations, Sick & Personal Days

Typically, companies allow employees one-week vacation after six months and/or two weeks vacation after a year of employment. Vacation policies need to be set up in a manner that allows your employees to get some much needed time off while not stifling your company's productivity. In some cases this will mean not allowing more than a certain number of employees (particularly in one department) to use their vacation days at the same time. For seasonal businesses it may mean limiting the time of year in which employees can use their vacation days. You should also limit the number of vacation days that can be taken at one time, thus prohibiting a senior employee from taking his or her six-weeks worth of vacation days consecutively.

You can also define the manner in which vacation days are accrued. Typically, companies add vacation days based on how many months or years a person has been employed. Many companies give higher-level employees more vacation days, which serves as an incentive to newer employees to work their way up to executive positions.

Extra vacation days can also serve as part of an Incentive Package. Many sales oriented companies use a specific vacation package as an incentive for their top salesperson or persons.

Also, make it clear whether or not vacation days can be carried over into the following year if they are not used (in compliance with applicable state law).

Sick and personal days can also be handled in a variety of ways. By setting up a specific limit on such days, you provide a framework for what is and is not acceptable. Due to situations such as personal emergencies or religious holidays, companies have typically become more flexible in granting extra paid personal and sick days to employees who have proved their worth. This is one policy where a little flexibility can serve to bolster the company's image and motivate employees.

Maternity, Paternity, Adoption, Disability & Family Leave

State and federal laws govern the amount of disability time you are required to provide for your employees. However, specific policies for time away from work for maternity, paternity or adoption are at the discretion of the employer.

According to the 1993 Family Leave act, any industry employing 50 or more employees for each working day during 20 or more calendar work weeks in the current or preceding calendar year must provide up to twelve weeks of unpaid leave during a twelve month period to each eligible employee for any of the following reasons:

- Birth and or child care of the newborn child of the employee

- Placement through foster care or adoption of a child with the employee
- To care for an immediate family member with a serious health condition
- If the employee is unable to work because of a serious medical condition

Eligible employees are defined as those who have worked for the company for 12 months; have worked for a minimum of 1,250 hours during the 12-month period immediately preceding the leave; and are employed by a business where 50 or more employees are employed within 75 miles of the worksite.

Sexual Harassment

Having a policy regarding sexual harassment can prevent many unnecessary headaches including legal hassles caused by the actions of your employees.

A policy regarding sexual harassment should state emphatically that your company will not tolerate such activities, including:

- Unwelcome sexual advances, sexual requests, suggestions or overtures
- Specific behavior or statements implicating that someone is expected to perform sex acts in exchange for a job, to keep a job, receive a raise, promotion or any other form of compensation
- Lewd or crude comments, jokes, e-mails, phone messages, cartoons or photographs
- Improper and unwelcome physical contact

If an employee claims to have been sexually harassed, within your company – and such a harassment complaint can also come from (or be levied against) an outside contractor, consultant, vendor or client - you need to investigate the situation very carefully. You need to establish, in your policy, how such activities will be reported and what specific steps will be taken to determine exactly what has transpired. It is very important that you remain neutral while investigating any such claim and make sure to gather facts before accusing anyone or dismissing such an allegation.

If it is determined that sexual harassment has taken place, you then need to take disciplinary action, which should also be outlined in your Sexual Harassment Policy.

Avoiding Employee Lawsuits

Over the past ten years many court cases have demonstrated greater sensitivity toward employees and their rights. This has resulting in an increase of lawsuits by disgruntled former employees. Lawsuits can be time consuming, costly and present a public relations nightmare. Therefore, it is essential to make every effort to avoid such employee lawsuits.

The most frequent causes of these lawsuits are:

- Wrongful termination

- Discrimination
- Harassment

By carefully drafting clearly worded policies and reviewing them with your attorney, you will have more solid ground to stand on should a former employee initiate such legal action. If, for example, you have all employees read and then sign that they have read Confidentiality and Sexual Harassment policies when they are first employed, you will have such documents available to you. Signed policies will usually stand up in court if the employee was terminated for clearly violating company policies.

Taking Precautions

Before you fire someone, you should make sure you have a legitimate reason that is based on fact and documented. If, for example you have proof that the employee showed up late or was absent from work on a regular basis, then you can use time sheets or time cards as documentation should you need to substantiate your decision to fire the employee on the grounds of tardiness or absenteeism. Illegal acts, including embezzlement, stealing or drug use are also valid grounds on which to terminate an employee. Again, you must make sure that you have proof of such activities before doing so.

An employee who is not adequately doing his or her job can also be fired. In some instances it might be appropriate to give the employee an opportunity to improve his or her work. It is also important that you provide clear (and documented) instructions as to exactly what task or tasks the employee is expected to do. Then, if he or she has failed to do so, you have documentation stating that the specific tasks or job requests were not carried out. Consistently poor job evaluations will also indicate that the employee is not performing at the level expected of him or her. However, since such evaluations can be subjective, you may wish to substantiate them further by attaching copies of a time sheet showing lateness or work done incorrectly before terminating an employee based on job evaluations.

Employees are also let go because the company can no longer afford to keep them on the payroll. In some cases such layoffs are widespread and may include entire departments while in other circumstances only a few employees may be dismissed. Be careful. Make sure you can fairly justify why each employee is no longer necessary to the company or why a department has been singled out to be eliminated. You do not want to show any pattern of discrimination, either willfully or unintentionally.

Discrimination laws protect against firing someone because of race, sex, religion, disability, ethnic background or because an individual is over 40 years of age. If, for example, all of the layoffs in the company were of individuals of the same ethnicity, they could file a discrimination suit against your business and potentially win.

Parting Ways

The manner in which you terminate an employee is very important. It is to your advantage to make provisions prior to firing or laying off an employee. An employment termination policy is sometimes desirable to put in place that outlines what the employee is entitled to when his or her employment ends. Such a policy will typically include:

- The terms of a severance package, which is usually commensurate with the length of time the individual has been employed and his or her position in the company
- Payment to the employee for unused vacation days
- Provisions for continuing health benefits after termination
- Whether a letter of recommendation is given for potential future employers

In some cases employers will also help by providing outplacement services.

Do's & Dont's of Firing Employees	
Do:	<ul style="list-style-type: none"> ✓ Try to make the situation as amicable as possible ✓ Have a reasonable, legitimate and documented reason for the termination ✓ Collect all keys, I.D.'s and other company related materials in the employee's possession ✓ Make sure you know his or her computer password ✓ Terminate employees in person, or have the employee's immediate supervisor handle the task in person ✓ If you are going to pay severance pay, get a release from the employee
Don't:	<ul style="list-style-type: none"> ✓ Discuss an impending termination with other employees (except his or her immediate supervisor) ✓ Fire someone based on rumor, innuendo, unsubstantiated claims or for personal or discriminatory reasons ✓ Make any statements that could be deemed personal, disparaging or defamatory.

Settlement Agreements

If there is a dispute with the employee upon termination, a Settlement Agreement can prove less costly than litigation. Such an agreement should state that both the company and the employee agree to settle the dispute. The terms of such an agreement should provide for a severance package for the employee. Other terms can be negotiated such as the payment of unused sick or vacation days. In exchange the employee will agree

to release the company from any liability and from all claims he or she may have against any employees of the company.

In addition, a Settlement Agreement should also stipulate that the former employee will keep all proprietary information about the company confidential.

Your attorney should carefully draft all Settlement Agreements.

Chapter 9

Key Contracts

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- Understanding Contracts
 - Sales Contracts
 - License Agreements
 - Stock Purchase Agreements
 - Office Leases
 - Right of First Refusal Agreements
 - Boilerplate
-

Understanding Contracts

Business contracts are legally binding written agreements between two or more parties. They are an important part of business and such agreements need to be created and/or reviewed carefully.

While smaller businesses will often conduct business based on informal handshake agreements or unspoken understandings, the more that is at stake, the more essential it is to have a signed contract. A contract serves as a guide to the agreement that must be followed by both parties. It presents each party with the opportunity to:

- Describe all obligations they are expected to fulfill
- Describe all obligations they expect the other party, or parties, to fulfill
- Limit any liabilities
- Set parameters, such as a time frame, in which the terms of the contract will be met
- Set terms of a sale, lease or rental
- Establish payment terms
- Clearly establish all of the risks and responsibilities of the parties

A contract is, in essence, a written meeting of the minds. While it is typically drawn up by one party and favors the needs and requirements of that party, protecting them from most (if not all) liabilities, it should be thought of, initially, as a work in progress that changes and grows as each party contributes prior to signing, when it becomes an official document. Consideration, whether it is monetary or a promise to do work or provide a service by a specified date, is at the root of a contract. Obviously, both sides should benefit in some manner before entering into any such agreement. The term “standard contract” is more myth than reality and too often people simply sign on the dotted line without reading or negotiating the terms of a contract.

Consideration, compensation, ownership rights, liability and risk are all areas that need to be worded carefully and you should seek out help from a qualified attorney, experienced in contract, in an effort to make sure you have covered each of these areas in a clear manner.

Within a contract it should stipulate how the contract shall be enforced and what actions can be taken if one party fails to meet their obligations. Some contracts will also include “out clauses” whereby one party can opt to get out of the contract at a certain date. Typically, this is done by informing the other party of their wish to terminate the contract in writing.

There may also be a need to arbitrate disputes that may arise under the life of the contract. How such disputes will be handled (i.e. by a neutral third party arbitrator) can also be included within the contract.

In situations where you do not generate the form of the contract, but are entering into an agreement with another business or individual you should typically:

- Read the contract over very carefully
- Highlight anything that is ambiguous or vaguely worded for further clarification and/or possible deletion
- List any additions you feel are necessary
- Discuss all changes to the contract with the other party or parties
- Make sure any requested changes have been added prior to signing (oral agreements can be very tricky and are not always binding)
- Review the contract again, prior to signing
- Keep a signed copy of every contract that you sign

Sales Contracts

Many companies sell a product and therefore need a good *Sales Contract*. The Sales Contract lays out the price, terms, and conditions for the sale of goods, equipment, or other products. The actual Sales Contract can take the form of fine print on the other side of an order form or an invoice, or it can be tailor-made for a particular sale. From your company’s perspective, you always want to start with your own form. Having your form preprinted helps it look “standard” and nonnegotiable. (*Note: No “standard” form of Sales Contract actually exists.*) As the drafter of the Sales Contract, you can make the contract more favorable to you as the seller. Here are some important terms to potentially address in your Sales Contract:

- **Price:** Make sure that the Sales Contract correctly states the price (often by filling in a blank space provided on the form). The Sales Contract also needs to spell out any discounts, installation charges, and delivery charges.
- **Price adjustments:** Consider how you may increase the price from time to time if you are entering into a long-term contract.

- **Taxes:** Try to ensure that the purchaser is responsible for all sales taxes.
- **Payment and credit terms:** Make sure to state when payment is due. If you don't require immediate payment, consider a small discount to the purchaser if payment is made within 10 days and a finance charge if payment is late (such as 30 days past due).
- **Warranties:** Decide what warranties you want to give. Ideally, you want to limit warranties, but the competitive marketplace may require you to grant extensive warranties. Typical warranties state that for a designated period, the goods sold will be free from defects of workmanship and will conform to designated specifications. Any necessary repairs will be under warranty for that designated time period.
- **Disclaimers:** State clearly in your Sales Contract (after you have set forth what your warranties are) that no other warranties exist, express or implied, including merchantability or fitness for a particular purpose. This disclaimer is usually in all capital letters or boldfaced to stand out and comply with certain provisions of the Uniform Commercial Code.
- **Liability limitations:** Use the Sales Contract to attempt to limit your liability under the contract. A typical clause for liability states that the seller's maximum amount of liability is equal to the purchase price. Make sure, too, that you include a sentence that says you are not responsible for consequential, punitive or speculative damages or lost profits (although some laws may limit successful enforcement of this clause).

License Agreements

A license gives you the right to use someone else's assets. A *License Agreement* spells out the precise terms of those rights and the corresponding obligations.

The party that gives someone the use of a right or license is the *licensor* and the party that receives the use of that asset is the *licensee*.

A common example of a License Agreement concerns the use of software. When you buy a software product, you only buy the right to use the software in limited ways—you don't buy "ownership" of the software. The License Agreement that comes along with the software sets forth these limits. Some other typical License Agreements include Trade Name License, Patent License, Software License, and Copyright License.

If you are negotiating to obtain a license or if you find yourself in the situation of providing a license to someone else, the License Agreement can address the following key points:

- **Exclusivity / Nonexclusively:** The license can be exclusive or nonexclusive. Licensors typically resist giving exclusive licenses. If the license grants exclusivity, over what areas is the license exclusive? If the license is exclusive, under what circumstances does the license convert to a nonexclusive one?

- **Term:** The License Agreement needs to spell out the length of the license, plus any renewal rights.
- **Payment:** The License Agreement needs to clearly state any upfront payments and any periodic payments required to maintain the license. A particular use of the license may also require an increase in payments. (For example, Software Licenses often require greater payment as the number of users increases.) Non-monetary payments may also apply.
- **Restrictions on use of the license:** Licensors often place a number of restrictions on use of the license, such as in certain geographic areas, or for designated purposes. (For example, a trade name licensor may grant the right to use a name, but only in a certain city.)
- **Infringement:** The licensee may desire a statement that the licensor actually owns the licensed item and it does not infringe on the rights of third parties. Licensors will resist giving such statements.
- **Termination:** The licensor typically defines various circumstances that allow him or her to terminate the License Agreement early, especially if the licensee breaches the License Agreement.
- **Assignment and sublicense:** Depending on the agreement, the licensee may be able to assign or sublicense the license. An *assignment* typically means a transfer of all of your rights in the license, whereas a *sublicense* involves giving someone the right to use a portion of your rights in the license. Most License Agreements prohibit assignment or sublicensing without the licensor's approval. Licensees may want to negotiate for broader rights if their business necessitates sublicensing the product.

Stock Purchase Agreements

If the company is selling stock, a Stock Purchase Agreement can be advisable. The key ingredients of these agreements are as follows:

- **Type of security:** The type of security (for example, common stock or preferred stock) is set forth
- **Price and number of shares:** The price per share and the number of shares being sold is identified
- **Representations and warranties of the company:** A list of representations and warranties made to the investors by the company is included. The agreement's representations and warranties are important. Here, the company must present a truthful picture of the financial and operational state of the business. A breach of the company's representations and warranties (a false or misleading statement) can lead to a real problem for the company, giving the investors various remedies.
- **Representations and warranties of the investor:** The agreement can have the investor represent and warrant that he or she:
 - Has the knowledge and experience necessary to evaluate the investment adequately.
 - Has had an opportunity to review and documents he or she requested

- Has had prior personal or business relationships with the company, its officers, or directors; or has the business sense to protect his or her own interest in the transaction.
- Realizes that the stock is sold pursuant to an exemption from the securities laws and is not freely transferable.
- **Covenants:** Any promises by the company to do various things are often set forth.
- **Conditions:** Any conditions to closing of the deal are set forth (for example, various certificates or opinion letters to be delivered).
- **Closing date:** The date and place where the closing is to occur are set forth, together with how the money or other consideration will be delivered to the company.

Office Leases

Most businesses require leased space. And as your business grows, you may need to add additional space for more people or increased operations. A lease agreement can constitute a significant financial commitment for a business. Yet many people blindly sign leases that bind their business for many years without any meaningful attempt to negotiate the terms of the lease.

When you find a great space for the business and are ready to lease, the landlord typically hands you a preprinted agreement that looks (for all the world) just the way leases were meant to look. The landlord is likely to call this the *standard lease*, as if the perfect form of a lease agreement had been chiseled in stone eons ago.

Pay attention here. This form is undoubtedly totally one-sided in favor of the landlord. No “standard” lease exists. And regardless of whether the form looks standard or preprinted, don’t be afraid to carefully review and negotiate the lease.

Your ability to negotiate changes to an office lease depends on how much leverage you have. Are other companies vying for the space? Has the space been vacant a long time? Are you willing to pay a good rent? Let’s face it: if Microsoft and General Motors are about to engage in a bidding war for the same prime space you’re interested in, all your negotiating skills mean zilch (zero, in technical legal terms).

Here are the key issues to negotiating leases:

- The amount of the rent, including any free rent granted to the tenant
- The permitted use of the premises
- The particular space leased
- Operating costs charged to the tenant
- Any tenant improvements to be paid by the landlord
- Responsibility for repairs and maintenance
- Rights to assignment and subletting by the tenant
- Right to renew the lease

- Right to cancel or leave
- Insurance requirements
- Whether any personal guarantees or security deposit is required
- Option for additional space if needed by the tenant

Lease Gotchas

Landlords often hand you a form lease that contains gotchas. *Gotchas* is a highly technical term for provisions that may cost you a lot of money or headaches in ways that you didn't plan. Your best bet is to negotiate them out of the lease. Here are some classic gotchas:

- ☒ The landlord's right to pass increased operating costs in the building on to the tenant without limitation
- ☒ The tenant's obligation to pay any increased taxes as a result of the landlord's sale of the building
- ☒ The landlord's right to terminate your lease early for his or her convenience
- ☒ A disclaimer about the building and the services provided to tenants
- ☒ Severe limitations or prohibitions on subletting your space (you may need to sublet space if your business shrinks)
- ☒ Personal guarantees of payment of the rent required from the company's owners

More on leases can be found in Chapter 14.

Right of First Refusal Agreements

Your company may want the investors who buy stock in the company to execute a Right of First Refusal Agreement. This agreement typically requires the shareholders to grant the company a right to match any offers for their stock, and thus to preempt any other buyers. Such an agreement may help keep your company's stock in friendly hands.

The Right of First Refusal Agreement can also be expanded to provide the option or the obligation for the company to buy back shares of a shareholder who has died or left the employment of the company.

Sometimes, investors may insist on a Right of First Offer Agreement in lieu of a Right of First Refusal Agreement. This agreement provides that the shareholder can first come to the company with a proposed price and terms for the shares to be sold. If the company turns down the offer, then the shareholder is free to sell the stock to any third party, as long as the price is the same or greater than that offered to the company. This type of agreement may be somewhat more appealing to an investor than a Right of First Refusal Agreement.

Boilerplate

Boilerplate is the term used to describe the section that appears at the end of a contract, which includes legal provisions. Since there is no “standard” boilerplate, a company can phrase this section as it sees fit. It is, therefore, imperative that before signing a contract that you read the boilerplate very carefully. Even attorneys sometimes neglect to review this section closely and their clients fall victim to important legal issues that are written into this section.

From your perspective, when drafting contracts, you need to word the language in the boilerplate section very carefully while making sure to cover all key legal issues.

Provisions within the boilerplate will typically include:

- **Merger Clause:** This clause indicates that the contract is the final and complete agreement between all parties. The clause is used to state clearly that any other agreements such as oral statements or other promises made are not valid unless clearly included in the signed agreement. Only the agreements in the executed and signed document are binding in this contractual agreement.
- **Governance & Jurisdiction:** This clause indicates under which state laws the agreement is governed and where any disputes will be resolved. In drafting the contract, you should list your own area of jurisdiction as the place where such disputes will be settled.
- **Arbitration in settling disputes:** This section will spell out how such disputes will be settled. A section on arbitration can help you avoid costly litigation fees.
- **Force Majeure:** This clause basically states that neither party can be held liable for not meeting the obligations of the contract if prevented by cause that is reasonably beyond it’s control, the effects of which could not be avoided. For example, if you cannot meet your obligations because of an act of God, such as a hurricane or tornado, the clause is intended to relieve you from liability for failure to perform.
- **Attorneys Fees:** This clause sets forth that in any legal action brought about by either party to enforce the terms of the contract, the prevailing party shall be entitled to collect fees to cover all reasonable and applicable legal expenses.
- **Modification of Agreement:** This clause will typically state that any modifications to this agreement will not be valid unless made in writing and signed by both parties.
- **Assignment:** This clause typically prevents either party from assigning the contract, and obligations within the contract, to another party. You may make special allowances under which a contract can be assigned.

You should include appropriate boilerplate language on all types of agreements including proposals, purchase orders, sales invoices, leases and licenses. The basic language can be repeated from contract to contract, but be careful to change specific

clauses to fit each contract. Review the boilerplate with your attorney to make sure the wording is carefully crafted. Ambiguity can cause you headaches.

Web Resources

To find some good sample contracts, check out the following websites:

- ✓ **www.E-PersonalFinance.com:** Contains a comprehensive library of small business forms and agreements, allowing you to preview a form before purchasing it. Forms include letters of intent, employment agreements, confidentiality agreements, purchase agreements, check lists and more.
- ✓ **www.sec.gov:** This is the official Web site of the Securities & Exchange Commission where you can access material agreements from public companies. Thus, if you want to see an important agreement that Microsoft, GM or Apple has entered into, you can find it for free.
- ✓ **www.lexisnexis.com:** One of the premier legal research sites available, contains sample contracts and litigation related forms.

Chapter 10

Legal Issues

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- Avoiding Personal Liability
 - Laws To Worry About
 - Business Licenses
 - Mediation & Arbitration
-

It is the responsibility of every business owner to do his or her best to follow the letter of the law. This will require some homework on the part of the business owner who not only needs to be on top of the all applicable laws, but also be aware of proposed changes to local, state or national laws. You need to be particularly knowledgeable about the laws that directly affect your business and be prepared to make any necessary corrections should you be made aware that you are not complying with a specific law.

Avoiding Personal Liability

Every business is subject to liabilities. Essentially, you want any such liabilities to be the responsibility of the company and not result in a personal liability. The type of business structure you choose will determine how vulnerable you are to personal liabilities. For example, if you are a sole proprietorship, you are liable for all debts and claims against the business. A lawsuit could be financially devastating. However, if you have taken the time and effort to incorporate or to form a Limited Liability Company, then you will likely be protected to a significant degree from such personal liabilities.

Many business owners, however, are under the mistaken impression that they are completely protected from personal liability by filing Articles of Incorporation, for a corporation. This is not true. The mere process of incorporating does not completely protect the business owners or shareholders. To lessen the likelihood of such personal or shareholder liability you should make sure to adhere to certain procedures. You should:

Always use the corporate name. The name of the corporation should be used in full, including “Inc.” or “Corp.” on all contracts, invoices or documents used by the corporation. This clearly indicates the existence of the corporation as a separate entity.

Always use proper signatures. This means that you will sign on behalf of the corporation, using the name of the corporation and your title. You should typically use the following format when signed contracts on behalf of the corporation:

CORPORATION NAME

*By: _____
Your name – authorized signing officer and corporate title*

Follow all corporate formalities. This includes following Bylaws, proper issuance of stock, holding meetings of the Board of Directors and recording of the minutes - plus other corporate formalities.

Make sure to keep funds separate. Corporate funds and the funds of individual shareholders should not be in the same accounts or combined for any reason.

Make sure to keep taxation separate. The corporate taxes should be paid entirely from corporate accounts and separate tax returns filed for the corporation.

Keep all transactions separate. All transactions made by the corporation should be clearly separate from any individual transactions.

Essentially, by never blurring the line between individual shareholders, owners or the Board of Directors and the corporation, which stands as a separate entity, you run less risk of any personal liabilities.

Laws To Worry About

Suffice to say it would take several volumes to include all of the laws that pertain to business, particularly if you start including state, city and county laws. There are thousands of business laws on the books, some of which are relevant to your business and others that are antiquated and have not been enforced since the 1920's. No one, including your local law enforcement agencies, department knows all of them. However, it is important that you know the laws most likely to affect your business. Here are some of the categories of laws with which you should familiarize yourself. (Most of these laws are discussed in more detail in other sections of this book.)

- Employment Laws, includes laws regarding: hiring and firing of employees, overtime pay, child-labor, disability, worker's compensation, unemployment, employee rights, employee safety and discrimination
- Tax laws including laws pertaining to the filing of tax returns and payment of: sales tax, withholding taxes, corporate taxes, pass through taxes and both state and local taxes

- Business formation laws including those pertaining to the specific business structure you have selected
- Environmental laws, including recycling laws and the discharge of hazardous waste materials
- Trademark and patent laws, plus all other such laws pertaining to ownership, inventions and/or intellectual property rights
- Consumer protection laws against fraud or unfair business or advertising practices
- Zoning laws, which typically include local ordinances that regulate: parking, advertising and signage, use of the land surrounding the business and even the type of business that is allowed to be conducted in a specific area.

These are just some of the significant legal categories under which you will find laws that affect most businesses. In addition, laws may pertain to the type of activity involved. If, for example, you are selling shares of stock you will need to adhere to securities laws and if you are operating a business that sells liquor you will need to adhere to the state alcohol laws. State laws may also dictate how contracts and legal documents will be written and enforced.

Just as you put together a business plan, you need to approach the legal aspect of a business in a systematic manner. Begin with the laws pertaining to the basics of starting a business. Do you need a business license? A permit? (Both of these are discussed later in this chapter). What laws pertain to opening a business in your state, city or county? Are you planning to hire employees? Will you be selling goods and therefore charging sales tax? Analyze each aspect of your business.

If you are in business for yourself, for example, you won't need to familiarize yourself with employee laws until you are ready to hire additional staffers. Likewise, if you are in a service business, you typically won't need to familiarize yourself with removal of hazardous waste. Review applicable laws in advance for each aspect of your business as you see it unfolding. Also, review all potential significant legal matters with your attorney. Ask questions and do not assume something is legal because it is common practice among other business owners.

If you should find yourself in violation of a law, take immediate steps to rectify the situation. Depending on the severity of the law, you may only receive a warning or a small fine from the local authorities. Typically, you will be given a time frame in which to make the appropriate corrections.

Zoning laws can often frustrate a new business owner. While you may be legally allowed to open a specific type of business in the zoned area, you will often discover that these laws affect how you may conduct your business.

It is important to take some time to familiarize yourself with all municipal, commercial and/or industrial zoning laws that could pertain to your business and ask questions of

the local Chamber of Commerce and/or other business owners to make sure you are adhering to the details.

Zoning Laws

Common zoning law questions that may arise include:

- ✓ Where can you build a loading dock?
- ✓ How high can you build?
- ✓ What are the rules regarding waste removal?
- ✓ Are there specifications about trucks or large vehicles?
- ✓ Can you build a parking lot? How much of your land can you use?
- ✓ Can you use part of a sales or retail facility as a warehouse?
- ✓ Can you use the sidewalk in front of your business for selling, advertising or expansion?
- ✓ Can you use part of a commercial retail site for manufacturing purposes?
- ✓ What are the laws regarding noise?

Zoning laws cover everything from storing and serving food to having drive-up facilities. Review them carefully.

Note: Zoning laws can, and do, change. Keep up with meetings of the local municipal boards and/or Chamber of Commerce.

In addition, if you operate a home-based business, make sure to review local zoning ordinances. Most home based businesses fail to do so. Many never encounter any problems until a neighbor files a complaint. The more obvious it is that you are running a home-based business (such as having numerous deliveries of large items to your front door) the more diligent you need to be about making sure you comply with local zoning ordinances.

A Good Filing System

Along with trying to stay abreast of all of the laws that pertain to your business, you can benefit yourself greatly by maintaining accurate and up to date files. Such record keeping will prove beneficial, should you:

- Need to comply with any change in the current laws
- Have a lawsuit filed against your business
- Be audited
- Be looking to make changes or additions to your business
- Be looking to sell or merge your business with another company

Bank records, employee records, contracts, business forms, permits and licenses, zoning ordinances, copyright filings, patents, leases, bookkeeping records and tax

documents are among the many records you will want in categorized files that you can find easily should you need to. Make sure all documents include the date. Although they may take up space, it is usually advantageous to save copies of such records for several years.

Business Licenses

State laws generally require that you obtain and typically display, a business license for most forms of business. The steps and paperwork necessary for obtaining a license will vary from state to state. The State and/or local Chamber of Commerce, local Small Business Administration office or city government office will typically be the place to turn for information on obtaining such licenses.

In addition to licenses for operating a business, many professions require licensing. Along with physician and attorneys, licenses are typically required for:

- Accountants
- Architects
- Auctioneers
- Chiropractors
- Cosmologists
- Dentists and dental technicians
- Dieticians
- Engineers
- Health care providers including nurses and EMS professionals
- Insurance agents
- Judges
- Land Surveyors
- Pharmacists
- Plumbers
- Psychologists
- Real estates brokers
- Therapists, including family, marital and physical
- Technicians
- Veterinarians

Other professional licenses may be necessary depending on the state requirements. If your business centers around such professionals, it is not only imperative that the individuals meets all licensing requirements, including ongoing education, but also that they renew their licenses accordingly.

In addition, many businesses require specific licenses for the sale or manufacturing of certain products. For example, businesses making, selling or storing food products will be required to have specific licenses or permits typically issued by the health department. Most often, there are licensing requirements for the manufacturing and/or sale of:

- Alcohol
- Chemicals
- Firearms
- Gasoline or petroleum products
- Lottery tickets or other games of chance
- Stocks or investment vehicles including bonds and/or mutual funds
- Tobacco products

Services, which you provide, may also require licensing. For example, if you are providing financial advice, operating a daycare center or serving as a masseuse you are typically required to have a license.

Operating or housing certain equipment or machinery on your premises may be subject to permits. For example, operations involving gambling or explosives will require a license. Having vending, arcade or video games on the premises may also generally require that you obtain a permit or license.

Certain types of businesses fall under the jurisdiction of government agencies. For example, if you want to open a radio station, you will need to comply with FCC laws and regulations.

Your Start-Up Business Legal & Licensing To Do List

While adhering to the many laws and ordinances may seem daunting at first, you will have to start somewhere. Here is a basic "To Do" List for getting started on your way to having a legal business.

- ✓ Set up a filing system for all documents.
- ✓ Get letterhead stationary, business cards and all necessary printed matter including standard contracts, invoices and receipts printed with the company or corporate name.
- ✓ Set a policy that all contracts and business agreements of any type will be in writing and that there will be a written record of each and every transaction.
- ✓ Obtain all necessary local business licenses and permits, then display as required.
- ✓ Make sure that all personal licenses necessary for your business have been obtained by the individuals and are displayed as required by state law.
- ✓ Review local zoning ordinances and file any specific documents that are deemed necessary.
- ✓ Obtain your Employee Identification Number, Federal Employer ID Number & State Employer ID Number before hiring employees.
- ✓ Make sure to have all necessary employment documentation, including IRS forms W-2 and I-9, available for new employees.
- ✓ Establish all personnel policies prior to hiring employees.
- ✓ Have all necessary tax documents on hand and review them.

Since obtaining some licenses and permits may take several weeks, it is to your advantage to start well in advance of your projected grand opening, or launch date.

Arbitration & Mediation

In the course of business you will inevitably have disputes with customers, vendors, landlords, employees and/or other individuals or companies with which you do business. Litigation to resolve such disputes is both costly and time consuming. Your top executives, sales people and other employees have better things to do than spend time waiting in court for the typically slow litigation process to unfold. More significantly, you cannot afford the time either.

Therefore, many businesses are seeking alternatives to litigation. The term alternative dispute resolution has been used to define the new means of settling disputes through arbitration and mediation. Either option can prove to be less expensive, less time consuming and can result in fair terms that both parties can accept. Many contracts now state that such arbitration will be used to settle such disputes should they arise while carrying out the terms of the contract.

Arbitration

Arbitration is a process in which both sides present arguments in front of a neutral third party, the arbitrator. This person, or organization (such as the American Arbitration Association) needs to be agreed upon in advance by both parties, who typically agree to abide by his or her decisions. Much like a judge in a courtroom, the arbitrator reviews the arguments of both sides and renders a decision. There is generally no appeal process and the decision is then considered binding. Non-binding arbitration is where an arbitrator suggests a course of action but the parties are not bound by his or her decision. The decision whether arbitration will be binding or not must be agreed upon in advance – typically binding arbitration is part of a contractual agreement.

Mediation

Mediation is a process where a neutral third party tries to find common ground on which to bring two sides of a dispute to the table to talk. Often used in labor disputes, mediation helps open the lines of communication between the parties. The mediator can establish guidelines by which the two parties will meet and oversee settlement discussions. He or she may take an active role in facilitating discussions and encouraging the parties to stay focused on settling the dispute. However, unlike arbitration, he or she does not make a ruling and unlike binding arbitration no legal decision results from mediation.

Sometimes, however, parties will come to an agreement having communicated through the mediation process and a contract may then be drawn up and ratified. Often in these situations, the mediator serves as the middle person, bringing various proposals to each side and seeking compromises.

The final decision to enter into arbitration or mediation is largely dependent on the nature of the dispute and the parties involved. In either case, both are often advised by lawyers for small business owners as a means of avoiding litigation.

Chapter 11

Protecting Your Inventions & Ideas

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- Patents
 - Copyrights
 - Trademarks
 - Confidentiality and Invention Assignment Agreements
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An original idea, creation or invention is often the cornerstone to a successful business. Known collectively as intellectual property, these may be what distinctively separate you and your business from another business. It is important that you closely guard the rights to such intellectual property through copyrights, patents and trademarks to prevent others from profiting off of your original ideas and creations. Trade secrets, such as the ingredients behind a popular soft drink or the formula for making the farthest flying golf balls also need to be protected through confidentiality and invention assignment agreements signed by all employees who work on creating the product. Such agreements will be discussed later on in this chapter.

Patents

A patent is a property right, which gives the holder the exclusive right to exclude others from the manufacture, use, or sale of the product or invention. The subject matter being patented is described in the patent's claims and protected if a patent is issued. Therefore, if for example, you were the inventor of the remote control copy machine and you had a patent on the invention, no one else could manufacture or sell such a product.

To obtain a U.S. Patent, you must file an application with the United States Patent & Trademark Office (USPTO). You can apply for one of three types of patents. According to the USPTO:

- “Utility Patents may be granted to anyone who invents or discovers any new and useful process, machine, article of manufacture, or composition of matters, or any new useful improvement thereof.”
- “Design patents may be granted to anyone who invents a new, original, and ornamental design for an article of manufacture.”

- “Plant patents may be granted to anyone who invents or discovers and asexually reproduces any distinct and new variety of plant.”

For information on the USPTO and filing a patent, you can call 1-800-703-308-4357, go to the USPTO Web site at www.uspto.gov or visit a Patent and Trademark Library in your area.

The application for a patent is a complex document and typically requires that you file through a patent lawyer or patent agent. They are licensed to appear before the USPTO. There are over 21,000 licensed patent attorneys and nearly 7,000 licensed patent agents and the USPTO website can help you in your search for one.

Once you have filed your patent application, you can expect a long wait, which may be several years. According to the USPTO, they receive over 300,000 applications each year, primarily for non-provisional utility patents. Applications are given an application number, which includes a six-digit serial number and a two-digit series code. The application is reviewed and a patent is then either granted or denied.

The time frame for patenting an item is limited. If the inventor uses the invention publicly, puts it up for sale or describes the invention in a printed publication, the inventor then has one year to apply for a patent or the right to patent the item will be lost. Once patent applications are granted, the patent is public information and the patent term begins – it generally lasts for twenty years.

While you await the acceptance or rejection of your patent application, you (or preferably your patent attorney or agent) can inquire on the status of such an application. You can also use the words “patent pending” while marketing and selling your invention. This does not protect you legally but it might ward off others who are looking to create a similar product. Conversely, it might encourage a competitor to create a product that serves a similar function but is unique enough not to be construed as a copy of your product.

If two people team up to invent something that they want patented, they can file one claim together and they will receive a joint patent for the invention if it is accepted.

Before Embarking On Your Patent Quest

A few things you need to consider before applying for a patent.

- ✓ Patents are only issued for actual, concrete, new and novel inventions or creations and not for ideas or plans.
- ✓ Patents are only issued for previously unpatented items. Therefore, you should go online and do a search for any similar item. Additionally, a description of the invention cannot generally appear in a publication anywhere in the world.
- ✓ Patent attorneys can be costly, so be as sure as possible that you are trying to patent an original invention.
- ✓ Make sure the invention serves a useful purpose. The USPTO will not issue a patent if they do not feel that the object serves some practical purpose. In addition, a machine that will not operate to perform the intended purpose will not be deemed useful by the USPTO and a patent will not be granted.

Do not expect to make a fortune off of your patented invention. For starters, it will take a long time before you receive a patent. In addition, having a patent, and having a strong, marketable product that the public needs are two very different things. Many wonderful inventions have gone the way of 8-Track tapes, most not even seeing the light of day. A patent is just a preliminary precautionary step in the life of a new invention or product.

Copyrights

A copyright protects the author or authors of published or unpublished original works including literary or artistic works plus certain other types of intellectual property.

Copyrights can be registered at the Library of Congress in the Copyright Office.

According to the Copyright Act, the owner of the work has the rights to distribute copies of the work, prepare derivative works, sell copies of the work and/or perform the work publicly. A copyright protects the specific work of expression and not the subject matter described. In business, the employer typically owns the copyright for any works that the employees create pursuant to their employment with the company.

A copyright can be used to protect:

- Articles
- Books
- Written reports
- Photographs
- Movies
- Scripts
- Artwork
- Architecture

A copyright generally cannot be used to protect:

- Ideas
- Subject matter
- Concepts
- Schemes or plans
- Names

The protection afforded by a copyright guards against the use of the material without the consent of the author. Use can be defined as selling, copying, distributing, recording, performing or displaying the work, depending on the nature of the material. Unauthorized use of copyrighted works can make the author or creator eligible to receive damages against the person infringing on the copyright.

Use of Copyrighted Materials

In the course of business, you may wish to use third party copyrighted materials for a project, in a book or perhaps in advertising or marketing materials being created by your company. You can request the use of the material for your purposes by writing to the owner of the copyright.

If you are lucky, the copyright lists the owner's name. However, it is not required that the owner of a copyright be listed. Therefore, you will need to seek out the owner through research. Typically, contacting the publisher, producer or distributor of the material will be your starting point. Reference librarians and the Internet can be helpful when embarking on such a search

Once you have contacted the owner of the copyrighted work, you can find out what, if any, compensation the owner wants in return for allowing you to use the material. This can run the gamut, from a mere mention by name to large sums of money. The owner has the right to name the price or not, and you have the right to negotiate. Ultimately, whatever you both determine to be fair will be included in a contract, which should be drawn up by a qualified attorney

Ownership of a copyrighted work can also be transferred in part, or in whole through a copyright assignment, which transfers the rights to another party.

Conversely, you can field requests to use works that you own the copyright to and can stipulate the guidelines under which you will grant such permission.

As owner of a copyright, the owner has the right to authorize (or not) any of the following:

- Reproduction of the copyrighted work
- A derivative work based on the copyrighted work

- Distribution of the copyrighted work by sale, rental, lease or lending
- Performance or display of the copyrighted work publicly

The owner does not have to provide any explanation if he or she chooses not to allow the copyrighted work to be used.

Infringement On Your Copyrighted Work

If you discover that someone has infringed upon your copyrighted work by using it without your permission, you should immediately draft a letter regarding the infringement of your copyrighted materials. In the letter, explain exactly what copyrighted material was used and in what manner. Demand that the party cease and desist from using the work or allowing anyone else to use the work in any manner.

Send the letter by certified mail with return receipt requested and close the letter by letting it be known very clearly that any failure to comply with the letter immediately will result in further legal action.

Infringement of the Copyrighted Works of Others

To prevent any infringement on the copyrighted works of others, remind your employees that they must seek permission before using copyrighted work.

Of course, there are quotes, lines and photocopies that are typically part of the everyday business process and “fair use” of materials should not violate copyright laws. But what constitutes such “fair use” of this material?

Fair use of copyrighted work, which includes reproduction or performance of the work is not an infringement of copyright if the work is used for the purposes of:

- Criticism
- Comment
- News reporting
- Teaching
- Research Purposes

Factors that will be considered in deeming the fair use of the work in question include:

- How the work is being used
- Whether such use is of a commercial nature or for nonprofit educational purposes
- The amount of the work being use in relation to the work as a whole
- How such use of the work will affect the value and potential commercial market for the copyrighted work
- Whether proper attribution is given to the copyrighted work

Trademarks

The idea of marking an item for ownership can be traced back in history to the finding of marks on pottery created many thousands of years ago. The economic use of such marks shows up in 500 B.C. during the Roman Empire.

Today, according to the USPTO, a trademark is defined, as “a word, phrase, symbol or design, or a combination of words, phrases, symbols or designs, that identifies and distinguishes the source of the goods of one party from those of others.”

Service marks are the same as trademarks, except they refer to the source of a service and not a product. The term “marks” is typically used to define the proper usage of both.

The benefit of such a mark is that it will legally prevent others from using a similar name or likeness that identifies your product or business. Familiar commercial companies such as Federal Express use trademarks to protect their company name, slogans, logos and other identifiable symbols. This protects a company in the event that someone tries to confuse the public by presenting a very similar name, logo or slogan.

Technically speaking, it is not necessary to register a trademark with the USPTO. By legitimately using the TM symbol next to your mark, it is possible to establish rights. However, it is beneficial to register the mark with the USPTO for several reasons, which include:

- Legal recognition of the USPTO registration symbol ® by United States courts
- Ability to bring a legal action in a Federal Court
- Listing on the Principal Register, which provides public notice of legal ownership of the mark
- Greater ease in obtaining registration in other countries
- Recognition by U.S. Customs, which can prevent infringement by the importation of foreign goods

Like a copyright, you should use the mark whenever using the product, symbol or slogan publicly. FedEx® is an example of how the trademark is used in all packaging, advertising and promotion of a brand name. You should take the time to remind all of your employees, particularly in the advertising, promotion, graphics and design departments, to use the mark properly.

A trademark search can save you time and money. You can find companies such as Thomson and Thomson in North Quincy, Massachusetts (800-629-8833, www.thomson-thomson.com) or Allmark Trademark in San Jose, California (866-ALLMARK, www.allmarktrademark.com) that will conduct a search for you to make sure another company is not already using a trademark that you are looking to register. Doing a web search on Google is also advisable.

Note: Many words cannot be registered as a trademark. If a word simply describes an invention, a function or is a widely used generic term, it will not qualify as a mark and the USPTO can refuse to register it. For example, the word “printer” cannot be registered for the invention of a new type of computer printer.

Filing Your Trademark Application

The USPTO encourages applicants to file electronically. However, applications are also accepted by mail or phone. Applications cannot be faxed to the USPTO.

- ✓ Trademark Electronic Application Service (TEAS) is available 24/7 at <http://www.uspto.gov/teas/index.html>
- ✓ TEAS can be accessed at any Patent & Trademark Library
- ✓ The USPTO automated phone line is 703-308-9000 or you can call 800-786-9199 and order a form
- ✓ The USPTO mailing address for new applications is:

United States Patent & Trademark Office
Commissioner for Trademarks
2900 Crystal Drive
Arlington, Va. 22202-3514

It is advantageous to review the guidelines regarding the filing of an application at the USPTO Web site, www.uspto.gov, under “Basis For” or get the pamphlet called “Basic Facts about Trademarks”. While you do not need an attorney to file a trademark or service mark application, it may be worthwhile to have one look over your application before you send it. The current filing fee, which accompanies the application is \$335.

Outside of The United States

A federal trademark is not valid outside of the United States. Each country has its own laws regarding trademarks. Many countries, however, will recognize a United States trademark and grant registration in that country.

Confidentiality and Non-Disclosure Agreements

Yes, there is a way of protecting your great business ideas. A Confidentiality Agreement, sometimes known as a Non-Disclosure Agreement is, as the name would indicate, an agreement that any confidential plans or ideas that you may have will be held by the other party in the strictest of confidence. Such an agreement, naturally, will only be effective if it is signed by the receiving party prior to disclosure of your ideas.

There are numerous instances where you may want to share confidential information with another party. Here are some typical situations where you may want to use a Confidentiality Agreement:

- Presenting an invention or business idea to a potential partner, investor, or distributor
- Sharing financial, marketing, and other information with a prospective buyer of your business
- Showing a new product or technology to a prospective buyer or licensee
- Receiving services from a company or individual who may have access to some sensitive information in providing those services
- Allowing employees access to confidential and proprietary information of your business in the course of their job

Confidentiality Agreements may be presented to new employees or used when companies are working on a joint business deal or a merger in which one company will be privy to the process or procedures used by the other. From software programs to “secret” recipes, most businesses will typically have some confidential material that needs to be protected.

Such an agreement, drawn up with help from your attorney, will include:

- Specifically what material needs to be kept confidential
- Under what circumstances and in what manner any confidential information may be used
- Your right to seek an injunction should the other party violate the agreement
- How any such dispute regarding the agreement will be settled
- A specific time frame including when the agreement begins and how long after your business interaction ends the recipient is obligated to keep all information confidential

The party receiving the confidential information then signs the agreement, and is therefore bound by the contractual obligation not to disclose your information.

Many new businesses, particularly in the planning and development stages are very diligent about making everyone associated with the company as an employee or independent contractor signs such an agreement.

Confidentiality Agreements can play a key role in your ability to maintain valuable intellectual property rights. Too often, inventors have been burned by disclosing an idea to a potential business partner or investor without taking the time to draw up such an agreement.

There is an unlimited range of material that can be deemed confidential. It is your decision, as the business owner to determine what information, in the hands of another business or individual, could prove detrimental to your business or to you personally in

any manner. You can also determine, in which situations the material is confidential and where it may be used. It is then equally important to determine which individuals could, intentionally or unintentionally, use such confidential information for self gain or to secure an edge in competing with your business. These are the people you most want to sign and date the agreements. You will then keep them on file.

See Appendix A for a sample Confidentiality Agreement.

Chapter 12

Sales & Marketing

-
- Market Research
 - Advertising
 - Promotion
 - Press Releases
 - Email Marketing
 - Direct Mail
 - Web Sites
-

The frequently used term, “Sales & Marketing”, typically works in reverse order, as marketing generates sales. If done successfully, the marketing process will help you evaluate your potential target audience and place your product in front of this target group in a manner that will increase sales. There are many ways in which you can market your goods or services. However, before you start putting together your marketing plan, you need to do market research.

Market Research

Before selling a product or service, it's important to know the market that you will be entering into. Research includes finding out what potential customers need, want/don't want and why. Your goal is to build a demographic profile of your customers. A research or business library can prove helpful for studying the manners in which other small businesses have approached their target audiences. You can then take a similar approach, adding your own creativity and the particular benefits of your products or services.

Surveys, questionnaires and focus groups are three among the many ways to obtain original data on potential customers. You can also get basic information when a customer calls for your services, visits your facility or browses your web site. When customers make a purchase, or any kind of inquiry, you can find out where they heard about your business. In this manner you can better plan, and track, your marketing efforts.

Your marketing plan should be the result of your market research. You can then proceed to use the most viable means to promote and advertise your products or services.

There are many factors that will impact on your marketing plan including:

- Your budget
- The type of products or services you are selling
- Your geographic region. (Are you selling locally? Nationally? Globally?)
- The amount of sales volume you can handle
- Your methods of distribution
- The amount of personal service you can or cannot provide
- Your personnel

From market research you can also learn about pricing, trends and competition. Typically, you will want to structure your pricing to be competitive. Depending on your position in the market, you may opt to undersell the competition and offer discounted items or you may price items on the higher end, and offer personalized attention and strong customer service. Pricing strategies are important and you'll adjust as your business grows.

Market research will also help you gain a greater understanding of the actual value of your product or service in the marketplace. By continuing to do market research as your business evolves, you will see what changes occur in the market for your service or product.

Means of researching the market include:

- Trade magazines
- Trade associations or organizations specific to your type of business
- Industry web sites & email newsletters
- Visiting competing businesses and/or reading annual reports of competitors
- The local Chamber of Commerce

When gathering market data you can use either primary or secondary research. Primary research means gathering your own data based on surveys, focus groups and through other means. Secondary research means using other sources such as the United States Census Report, books or trade magazines. Many businesses use a combination of both primary and secondary research.

Your Target Audience

The goal of your market research is to determine your sales demographics and establish a target audience. This is to whom you will gear your advertising and marketing campaign. Just as children's games and toys clearly state on the box, for ages 7 through 12, nearly every product or service has a specific demographic group

that will be most interested in spending money to buy the product or utilize the services offered. The number of businesses that have failed because the owners have not taken the time to determine their target audience is staggering.

Some products and services, such as selling soda or providing haircuts, will span a wide range of potential customers. Therefore, it is important to create various marketing campaigns to reach the different segments of this vast market that you are most likely to attract. Conversely, other products and services have a narrow audience and need to be targeted in a more specific manner, such as a new service for dermatologists. Niche marketing can be very beneficial and cost effective if done properly.

Some questions to ask yourself when outlining your target market or demographic group include:

- What is the age range of the customer who wants my product or service?
- Which sex would be more interested in this product or service?
- What is the income level of my potential customers?
- What level of education do they have?
- What is their marital or family status?
- Is this a product or service they need or a luxury item?
- How will they use this product or service?
- What will draw them to this product or service? (Easy availability? Low price? Personalized attention? Special features?)
- Which, if any, special features are most appealing?
- What do they like or dislike about the product or service in general?
- Is this an impulse buy or something they are saving up for?
- What is the common method of payment for this product or service? (Cash? Credit Cards? Installment Plans?)
- Where do they gather their decision-making information? (The Internet? Newspapers? Magazines? Books? Television?)

These are just a few of numerous categories in which you can breakdown your target market.

Advertising

Typically, advertising and promotion are vital to the success of a business. To successfully advertise you will need to allocate a portion of your budget for such purposes. This will depend on the size of your business and the scope of the market you are trying to reach. Proportionally, a small business and a multi million-dollar corporation may spend the same percentage of their budget on advertising. If the advertising campaign is carefully planned to reach the target audience, the resulting increase in business may also be a similar percentage. For example a few well-placed billboards in a small town might generate a 10% increase in sales for a small business while a national commercial might produce the same 10% increase for a major retail chain.

Your focus, when advertising needs to be on:

- The type of media that will best reach your target audience
- The type of advertising campaign you will run (i.e. promote a new product; place a familiar product or company name in front of the audience; promote a special service or activity)
- What style of advertising will best suit your products and/or services
- How can you reach the most people (within your defined market) for your advertising dollar

When you advertise, you are investing in your own business and like any type of investment there are risks involved. The major risk is that the advertisements will not generate enough sales to justify the costs of the advertising campaign. As is the case with any investment, through due diligence you will determine the best means of advertising before taking such risks.

Print Advertising

Newspapers continue to provide a means of reaching a large audience in a city, town or region. You can reach a specific audience by selecting the best location within a newspaper to advertise your product or service.

Advertising rates vary significantly by geographic region and market size. Deals can be made through negotiating. Buying an ad that will run for weeks will always be cheaper in the long run than buying on a day-to-day basis.

Advantages to newspaper advertising:

- Ads are inexpensive to create
- Most papers offer various rates and sizes of ads
- Changes can be made to an ad rather easily
- It is relatively inexpensive in comparison to other forms of advertising
- You can offer coupons or immediate savings (Request an “outside position” on the page if you are placing coupons in an ad)

Disadvantages to newspaper advertising:

- Photographs typically do not print well
- Placement - The ad is only as good as the page it's on
- Readership may be limited depending on the news of the day, the circulation of the paper and the day of the week
- Competitor's ads are usually found in the same section(s)

Do's & Dont's of Print Advertising

Do:

- ✓ Plan an advertising campaign in advance: coordinate ads so that there is a theme or hook that ties them together and builds an image for your business
- ✓ Get price quotes in advance from a sales representative at the newspaper and prepare to bargain
- ✓ Consider advertising in Sunday papers since they typically have the largest circulation and are often saved for several days
- ✓ Get copies of each ad you place (before paying the bill) to make sure it ran in the right section and the typeface was legible

Don't:

- ✓ Overwrite, or try to place too much copy in your ad
- ✓ Get into very long-term agreements unless the ad has proven to draw more business
- ✓ Use a complicated layout or multiple visual images

Magazine advertising allows you to place ads in periodicals read specifically by your target audience. Photographs can, and typically do, enhance magazine advertisements. Unlike newspapers, where ads feature the basic details of the products or services and the price, magazine ads are more often focused on creating and building an image. The immediacy of newspapers is advantageous for special promotions, sales and one-time offers. Magazine ads, however, are typically designed to have a longer life. Often a reader will pick up the magazine two or three weeks after it was initially published and the ad should still be of value to the reader. Take time to look at ads in the magazines your research has determined are read by your target audience. Also consider regional magazines if your business is regionally based or trade magazines if you are doing business-to-business sales and marketing.

You may opt for an advertising agency or copywriter to handle magazine print ads if your budget allows for such specialists.

Advantages to magazine advertising:

- You can more easily create an image
- You can use photos, color and a more elaborate layout than with newspaper advertising
- You can target a very specific audience (more so than with a newspaper, where a reader may be buying the paper for any of ten very different sections)

Disadvantages of magazine advertising:

- More costly than newspapers
- There is a long lead time (ads may need to be ready six months in advance)
- Typically, the ad will run only once per month since most magazines are monthly publications

Whether you choose to advertise in a newspaper or a magazine, prepare print ads that have some lasting power. Typically, a print ad will run several times before you'll want to start working on a new one, especially a magazine ad.

Radio

Radio is often a far underutilized medium. Typically, it costs much less money to produce a radio commercial and buy airtime than to buy television airtime or to do a photo shoot for a magazine print ad. For a radio commercial to be effective, it needs to grab the listener's attention quickly and cover all the key points in a concise, informative and entertaining manner.

Your ad can be in the form of radio copy read by on-air personalities or you can have a pre-produced spot of 5, 30 or 60 seconds. Remember copyright usage (Chapter 11) before using recorded music. If you write advertising copy, make sure you write in a conversational style and repeat important information during the ad. Don't try to pack too much into the copy.

Placement is the other key to radio advertising. An ad during morning or evening "drive time" will be far more effective than an ad at 2 a.m. In addition, you will want to select the type of station(s) most listened to by your buying demographics. Once you've chosen a station and requested the time slots during which you wish to advertise, you'll be quoted rates. Typically radio ads are bought in chunks since a high frequency of commercials during a short period of time has been proven to be most effective. You may also opt for summer placement, since radio listenership usually increases during June through August.

Advantages of radio advertising:

- Inexpensive to produce commercial spots
- Easy to make last minute changes and/or update radio scripts or spots
- Can buy in blocks and reach your target market consistently for a period of time

Disadvantages of radio advertising:

- Very dependent on placement
- Limited time in which to include all pertinent information
- Scripts are typically only as good as the talent reading them

Before advertising on the radio, get the listener demographics and the ratings for each station in your market.

Television

If you can afford television, you can typically benefit in a greater manner than using any other form of media. Your ad, however, needs to be carefully written and produced to be effective. For that reason, it is often advisable to hire an advertising agency to work with you while creating a suitable television commercial campaign.

Advantages of advertising on television:

- Reach a large demographic audience
- Lends a degree of credibility
- You can establish a specific image more easily
- It allows for much more creativity
- You can establish your presence or introduce a new product very quickly

Disadvantages of television advertising

- High production costs for a quality commercial
- Very dependent on placement
- Very costly to buy time in medium to large markets: make sure your budget allows for television advertising
- Difficult and costly to make changes

Television advertising can be very draining on your budget. The cost of producing a commercial is only a small portion of the overall expense. Buying time on local or national networks will be the bulk of your cost factor, and like radio, you need to buy in blocks and repeat a commercial many times to the same target audience to be effective. You also need to carefully study demographics and ratings for various programs and time slots before committing to television advertising.

Establishing an image and accentuating the key selling points or benefits of your product or service through your script are the keys to a successful commercial. Entertainment and creativity are important factors, provided they do not detract from the product. Many advertisements are fun to watch, but moments later viewers cannot recall what product was being advertised.

Yellow Page Advertising

A common source of new business is from advertisements in the Yellow Pages. Typically, such advertising is sold by the size of the page. Like all print advertising, you want to have an ad that is eye-catching and presents your key information in a concise manner. Since you buy the ad once for a year, you need to keep your Yellow Pages ad generic. It cannot be changed once it's in the book. You should also consider that (unlike most other forms of advertising), you will be pitted against your competition by virtue of placement in a specific section. Therefore, you should spend less ad space explaining the need for your product (since they have already opened to that section)

and more space featuring the unique qualities and benefits of your product or service over the surrounding competitors on the page.

Billboards, Signage & Posters

Billboards, signage and well-placed posters can be inexpensive ways of reaching a large audience. Advertisements on city busses are seen by thousands of people daily. A strong visual image coupled with concise copy and a catch phrase or logo can catch the attention of many potential customers. An advantage of outdoor signs, posters or billboards is that the viewer cannot shut it off or turn the page. Therefore, if you can grab those two or three seconds of attention you build a presence in the market. Of course, to be most effective, you will need to think visually and plan your campaign carefully. Test marketing is recommended.

Money Saving Ways To Advertise or Market Your Wares

- ✓ Look into co-op ads with vendors, retailers, service providers or manufacturers, depending on the nature of your business.
- ✓ You can often barter or trade your product or services for advertisements.
- ✓ Consider guerilla marketing, which has become a popular means of using unorthodox methods to get your product or services in front of an audience.

Web Ads & Paid Listings

Consider advertising on specific web sites with banner ads or rich media ads. A new powerful advertising vehicle is through “paid listings”, which are mini-ads that can be placed on search sites (such as Google, Yahoo, Bing, etc.). Paid listings typically are structured so that you are only paying if someone actually clicks on your ad to be transported to your web site.

Promotion

Advertising and promotion typically go hand in hand. However, unlike advertising, promotion can be a less costly means of putting the name of your business in front of the public. Promotional campaigns can include:

- Contests
- Giveaway Items
- Parties, activities or events
- Sponsorship

Building strategic alliances with other businesses that also attract a similar demographic audience is also a strong manner of promoting your business. For example, a car wash and nearby auto parts store might run a combined discount special. Also ingratiating

yourself within the community and/or having a visible presence at everything from street fairs to local sporting events can help promote your business, depending on the type of goods or services you sell. Service providers can benefit from speaking engagements and other public appearances in which they can demonstrate their expertise in the field while promoting their business.

Any opportunity to further the growth of your business is a form of promotion and should be investigated. Promotion builds a need for your goods or services. From t-shirt giveaways to publicity stunts, the objective is to get your name out in a manner that appeals to your prospective audience.

Good promotion for a new business or a home based business might mean giving out business cards, sending out an e-mail newsletter and providing good customer service that leads to referrals. Word of mouth is very significant to a start-up business, so customer satisfaction needs to be high.

Before embarking on a promotional (or an advertising) campaign you should:

- See what your competitors are doing to promote themselves
- Look closely at the cost factor
- Test out your idea(s) with a small sample or focus group
- Seek feedback

There are plenty of creative means of promoting your business. Within the bounds of the law and good taste, you can certainly think of several.

Press Releases

All newsworthy events concerning your business should be written up in a press release. The release will then be sent via email, fax or regular mail to a list of media outlets and key contacts that can potentially spread the word about your business through articles in the print media or stories/reports in the broadcast media.

An effective press release should provide the who, what, where, why and when of the story in a concise manner. The release should spark reader's attention with a strong headline and immediately feature the prominent details of the story in the opening lines. People in the media have little time to read the numerous press releases they receive, so yours needs to be media friendly, meaning the writer or reporter can practically lift the information from the page and use it in their story.

Below the important news, you should provide basic information on your business. Also make sure to include:

- Contact information
- The release date
- A headline
- A dateline – where the story is originating from

- End with # or –30-, centered on the page, which mean “the end”

#

You need to be discerning in determining what information is worthy of a press release. Too many non-descript press releases are tossed in the trash everyday. You also need to be accurate and up to date with your information, so double check your facts and figures carefully before sending. Press releases should be one or two pages, tops.

Typically businesses, especially new businesses, will have a press kit, which will include several recent press releases, a backgrounder (one-page history of the company), newspaper clips (if there have been stories written about the business or individuals behind the business) and possibly some photos. A well-designed press kit will provide potential clients, vendors, investors and media representatives with a brief overview of the activities of your company.

For a sample of a press release, see Appendix A: Forms & Agreements.

Email Marketing

It has become increasingly harder to promote a business using email. SPAM clogs up in-boxes and most people are quick to delete the deluge of mail they receive without even reading it.

Nonetheless, email marketing, if done correctly, can be an inexpensive and quick way of reaching a very large audience. The key is to get people to WANT to receive your mailings. To do this, you need to do permission mailing, which means having people either sign up on your web site for such mailings or provide their email addresses when they purchase something from your company. In this way, you can collect email addresses without buying a list that may be created and/or sold illegally.

Emailing advertisements (with permission to have the recipients email address) can still become redundant and the recipient will likely ask to be taken off the mailing list unless you:

- Offer new discounted products or services regularly
- Provide very targeted mailings
- Offer some content

Even two or three sentences of original content can provide a reason to read your email. It can also support the advertising that otherwise may be deleted. Short bits of information, such as five tips for a healthy lawn from a lawn care company or dressing for success from a clothing retailer are ways to keep your audience reading your emails. Establishing your own newsletter (which may only be a few paragraphs) can draw the attention of your readers.

When emailing customers, you also need:

- A catchy headline
- A recognizable company name in the “from” box so they’ll know it’s from your business
- A simple one-click manner in which they can get more information on specific products or services
- A means of reaching customer service

Since you may only have one second to capture the reader before he or she hits delete, it’s to your benefit to make sure something interesting shows up in the window that displays part of the email prior to the reader actually opening it. This window can literally provide you a “window of opportunity” to grab their attention. Make this about “them”. Unlike a press release, which tells the media what your business is up to, email marketing needs to focus on benefits to the customer. Once you’ve got them reading, you can put as much as you’d like about your company farther down the page. They can elect to read it or not. Nonetheless, the farther down the reader scrolls, the more advertising and marketing information he or she will have absorbed.

A few email marketing rules of thumb:

- Make sure everyone on the list has agreed to be there...don’t add names
- Reassure readers that their information will not generally be shared
- Give readers an opportunity to opt off of the list
- Keep information concise, to the point and focused on their needs
- Don’t blitz – emailing more than once or perhaps twice a week can be annoying
- Provide a choice of HTML or TEXT version

Landing pages are also important. Readers should be able to get more information by clicking on various places on the initial marketing email or newsletter. Don’t send them to a home page and make them search for the specific information that brought them there. For example, on Amazon.com if you click on a specific book you’ll get a page with details and reviews of that book and suggestions of similar books. That landing page provides information including pricing or purchasing and then leads to a sales page or shopping cart. Your promotional emails should do the same thing and also give the reader an opportunity to go to your home page.

A new company that is not conducting business directly over the Internet may want to take advantage of the interactivity of the Internet by providing readers with something to do, such as a quiz, questionnaire, survey or short article. This puts your name in front of the reader while giving them a chance to interact. It is also a way of monitoring how many people are visiting your site and staying for a few minutes.

Direct Mail

Despite the glut of junk mail, direct mail marketing continues because it is still successful for many businesses. The key to a successful direct mail campaign is the

mailing list. If you have a well-honed, targeted mailing list, you can get a better rate of investment (ROI) than if you are mailing randomly. You can purchase a list through a good list broker. However, it is essential that you make sure the list is targeted, current and legally sold. Get references and check on the list broker. There are too many people passing off stolen or old lists. In addition, it is not wise to buy a list blindly off of a web site or a CD Rom. Often such lists are randomly generated from various other lists and not frequently updated.

Buy updated lists when necessary to keep your list current. Every three to six months your list should be updated. Some local businesses or niche companies opt to do their own due diligence and create their own lists. This is only effective if you have the time and manpower to put into creating a strong list.

To do a direct mail campaign you need to:

- Have a targeted (current) mailing list that suits your demographic needs
- Determine what you want to send (i.e. flier, brochure, postcard, sales letter)
- Find a mailing house
- Find a good printer – shop around and get quotes
- Have a means of tracking the success of your mailing

Tricks of the Direct Mail Trade

There are numerous tricks to the trade and direct mailing experts spend ample amounts of time honing and testing direct mail pieces. Color, texture, print, tone, wording, phrasing, size of the piece and numerous other issues are all debated by the experts. Direct mail is unique in that it is a tangible item that your recipient can hold, read, save or toss, depending on his or her need for the product or service and the interest created by the piece. In the end, a 5% return on investment (“ROI”) is considered extremely good when embarking on a direct mail campaign. Therefore, once you’ve put together the piece you want to mail, you should start with a test run before mailing to your entire list. This will give you an idea of the impact of the piece.

Direct mail pointers include:

- Use all the elements: Paper quality, size, color and texture are all part of the presentation, not just what you have to say.
- Don’t over-design. Graphic designers often get carried away with the overall look and forget that someone has to be able to pick up the piece and actually read it.
- Don’t try to fool readers with “come ons” on the envelope such as “Sweepstakes Winner”.
- Send a separate mailing to steady customers with special offers, promotions or advance notice of upcoming sales. Make them feel important, since, in actuality, they are vital to your business.

- If you are mailing to a business, try to find the best name to send to. Sending to a title or a company name is usually an exercise in futility.
- Use a postage meter, it looks more professional than using stamps.
- Write conversational copy that focuses on what your product or service can do for the reader.
- Avoid technical jargon and hyperbolae.
- Make valid claims and promises that you can keep.
- If you are requesting a return by mail, make the process simple and the instructions very clear.
- Reply cards are often more effective than 800 numbers unless you have competent round the clock operators on hand. Even then, offer both options since some people would prefer not call.
- If you have a web site, include it on all direct mail pieces.
- Add a personalized touch – no “dear occupant” letters. Include a signature that appears personalized.
- Watch your costs closely. A successful direct marketing campaign is contingent upon generating a profit, so track your spending versus your ROI.
- If you find an income-generating piece, use it as a template for future mailings.

Web Sites

Many businesses today are on the World Wide Web. From major e-tailers to small mom and pop businesses, it's almost essential to have a presence on the web.

Domain Names

The first step in building a web site is purchasing a domain name that is not already being used. This can take some creativity on your part. Typically, .com or occasionally .net will be used for a commercial business. Toying around with your product, services or company name may produce an original domain name. Often it's easier than you think to find a close match. For example, if you manufacture and sell teddy bears, teddybears.com will likely be taken. However, if you are based in New Jersey and try teddybearsnj.com you may likely find a domain name. Start with the name you'd most like to use and branch out.

Web Hosting Services

A web hosting service is in the business of keeping your site up on the web, maintaining it for you and allowing you to select from many of the features that are found on successful sites.

Depending on the services and features provided, costs for such a web hosting service typically start at around \$25 per month. Obviously the more web space you need,

additional features and the more traffic your site is generating, the more the cost will increase.

A Web Hosting Service typically allows you to:

- Register your own domain name for a modest fee
- Pay for more space as your site grows
- Get email at your site and usually have several email addresses
- Receive viewer statistics, such as how many visitors there are to your site per week or month

When selecting a web hosting service, look at the fee structures carefully. Typically, companies will charge an initial set up fee, monthly fees plus additional charges for various options. Make sure you know what all the fees will be and how often they will be charged. While most companies charge for updating the site, some offer deals that allow for some free updates. Evaluate and compare services offered. Get recommendations.

Web Site Developers

There are many individuals out there who will offer to develop your web site for you. The trick is finding someone who will do what you want.

To find a good web site developer, look at other web sites. Contact the names of developers listed at the bottom of the sites that you like. You can also ask for referrals from other businesses, providing you like what you see on their sites. Shop around and find someone who is easy to work with and comes highly recommended.

Depending on the complexity of the site and the need for business transactions, detailed graphics, etc., the costs will vary greatly. Keep in mind that no matter what you pay, the web site developer is working for you, which means:

- You call the shots
- All content, graphics and everything else on the site should be owned by you (and your contract should spell that out)
- The developer (as stated in the contract) is responsible for all functions on the site and making sure that they are in working order
- You should draw up a contract with the developer which is a “work for hire agreement”, specifying the start and completion date of the site’s creation and the costs

What Makes A Good Web Site?

The best web sites are those that serve the purpose of their owners. For some businesses, a web site provides the backbone of the company’s retail operation. For many other companies, the site offers an adjunct source of sales revenue along with

their brick and mortar operations. Some businesses use a web site primarily for promoting their products or services and keeping their name in front of the public.

No matter what the use will be, it is generally a good idea to look at other web sites to get an idea what you feel would work best for your business. Look at each site with a critical eye.

Ask yourself:

- Do I like the layout?
- Is there a logic to the sequence and the information?
- Is the site easy to navigate or are you clicking repeatedly to find what you're looking for?
- Is the site current?
- Are products and/or services clearly displayed?
- Is the sales checkout process simple and quick?

The best web sites are user-friendly, easy on the eyes (visually appealing), entertaining, informative and current.

Some site planning and web page design tips include:

- Less can be more, so don't overcrowd a web page.
- If you are selling items, make sure your product photos are large enough to see clearly. Try to illustrate the key features.
- Title each page so that they are easily located by the user and by search engines.
- Make each page easy to navigate.
- Try to be concise with text. You can always have readers click to get more information.
- Make the home page the center of activity. Make sure it is always easy to return to. Clearly define the purpose of the site, and create an image on your home page.
- Provide customer service, phone numbers and contact information that clearly illustrates an accessible business behind the site.
- Make sure the color of your text is easy to read against the background you've selected. Experiment with different colors to see which creates the best presentation.
- Double-check all links often to make sure they work.
- Don't get caught up in "bells and whistles." Just because the software, web designer or web hosting service allows you to include a myriad of features doesn't mean you need them.
- Make sure the site loads quickly. Don't let graphics slow it down.
- Be diligent about copyright usage and make sure you have the rights to all information you are posting.

Besides dotting the i's and crossing the t's, so to speak, you not only want to make sure your site looks good and works properly, but that it best represents your business. Also, keep in mind that you need to promote the web site. Unlike the line in the movie *Field of Dreams*, "If you built it they will come", a web site will not attract visitors unless you register with several search engines and promote the site.

Chapter 13

Insurance

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- Liability Insurance
 - Property Insurance
 - Business Interruption Insurance
 - Deductibles
 - Making A Claim
 - Other Types of Insurance
-

If you are going to go through the time and effort to start a business, you need to consider proper protective steps. Therefore, you want to purchase the right insurance coverage.

Your first order of business is to determine your specific insurance needs based on the nature of your business. What risks must be covered? How much coverage will be sufficient? You will then want to find and evaluate insurance providers or insurance brokers to determine which companies handle the types of coverage that suits your needs.

While shopping for insurance, you will want answers to several key questions such as:

- What are the deductibles?
- Are the coverage limits high enough?
- What items or occurrences are excluded from coverage?
- Are there any gaps in my coverage?

As you read farther and determine your own insurance needs, your list of key questions will grow depending on the nature of your business and the types of insurance coverage you are purchasing.

Liability Insurance

In today's litigious society, liability insurance is more essential than ever. This type of insurance can protect you from lawsuits resulting from:

- Any bodily injuries that occur on your premises to customers, employees, vendors or visitors

- Injuries sustained as a result of the actions or negligence of one of your employees
- Property damage caused by your employees

There are typically four types of liability insurance. General Liability Insurance is the more common form. In many instances it is part of a larger insurance package. Typically, it provides coverage for the above-mentioned occurrences. Some liability coverage will also include libel, slander and/or infringement on intellectual property. Read the fine print very carefully to determine what is and is not covered in such a policy.

A second type of liability coverage is called Professional Liability Insurance, which is essential in the service industry. This type of coverage protects professionals from claims made against them personally for errors made while they are performing their services. Examples of such insurance would include Malpractice Insurance carried by doctors or Errors & Omissions Insurance carried by financial advisors, attorneys, accountants, building contractors and other professionals.

third type of coverage, which you would strongly consider if you own a manufacturing business, is Product Liability Insurance. This coverage protects you in the event that an item manufactured or developed by your company is responsible for an accident, injury or death. From toy manufacturers to car manufacturers, there can be a significant risk of injury from the produced product. Naturally, the type of product being manufactured would indicate how much coverage you would need to purchase. Safety measures and precautions taken are factored in when determining your premium.

And finally, the fourth and newest type of liability coverage insures a business against the actions of the employer. The increase in lawsuits filed for wrongful termination, sexual harassment and/or discrimination has fueled the need for Employment Practices Liability Insurance (EPLI). This type of insurance typically protects you as the employer against such claims made by employees, former employees or business associates.

Occurrence or Claims-Made Policies

When buying liability insurance you can typically purchase either an “occurrence policy” or a “claims-made policy.” An occurrence policy can cover claims made months or even years after the incident occurred. The insurance company is obligated to review and, if warranted, pay for any claims made resulting from an incident that took place during the coverage period even if the claim is reported at a later date. The more commonly used “claims-made policy” provides protection only while the policy is in force and claims are made during that time frame. Prior act coverage may also be included, indicating that acts occurring within a specific time period (prior act coverage period) will also be covered. Claims-made premiums are typically lower than occurrence policies.

Many umbrella, or “business” liability insurance packages offered will cover your basic insurance needs. However, it is strongly advised that you read the fine print carefully to make sure there are no gaps where you specifically need to be covered.

Property Insurance

You can protect the assets of your business, including your equipment and the building or buildings in which you operate by having Property Insurance. Property Insurance typically covers your property in the event of theft or damage caused by fire, explosions, accidents or acts of nature. Additional office equipment can be protected by having Contents Insurance. If you are running a business from your home, you should also have such protection to cover your work related equipment, which may not be covered under a standard homeowner's policy.

The amount of stock or equipment you maintain for your business operations will determine how much coverage you will need to purchase. By taking a detailed inventory of all property, equipment and stock you can determine the amount of coverage you will need. Include real estate such as buildings or garages you own.

It's important to take your time in assessing and determining a value for your property. You will want to receive a fair amount of compensation for any goods lost or destroyed. Keep in mind that the higher the dollar amount of coverage, the higher the insurance premium will be. Therefore, you may elect not to cover certain items that may not be worth the cost of coverage.

Additional Property Coverage

There are other coverage areas you may choose to inquire about when shopping for Property Insurance. Depending on the insurer, some of these will be included and others may be purchased at an added cost. Nonetheless, they may be worth considering.

- ✓ **Undamaged stock protection**, which covers undamaged items that can no longer be marketed because of damage to related goods.
- ✓ **Data or records protection**, which covers loss of data or company records that were destroyed and will take time, and cost money, to reproduce.
- ✓ **Computer virus protection**, which covers the loss of data and business through computer viruses.
- ✓ **Off premises property protection**, which extends your property coverage to include protection at other locations such as trade shows, fairs, installations, exhibits or any place where your company is doing business with company-owned equipment.
- ✓ **Intangible coverage**, which includes patents, copyrights and trademarks.

Property Insurance is sometimes offered by specific risks. For example, you may purchase Fire and Theft Insurance. Other companies will offer broad based policies that cover a variety of risks and potential hazards. The type of business you run, your physical location and the region in which you are doing business should all be factored

into determining which risks are more likely to occur and potentially destroy your property and subsequently hurt or destroy your business.

How well you are protecting your business against such potential risks can determine how much you will pay for Property Insurance. For example, if you have excellent security measures, working sprinklers and adhere strictly to fire and building codes, you will pay less for Fire and Theft Insurance.

Property and liability coverage can be purchased together under a general business owner's policy. However, the coverage is usually not as great as if you purchase them separately. Again, this will depend on your specific needs.

Business Interruption Insurance

Many small business owners do not realize the value of Business Interruption Insurance. If a business is forced to close because of a fire or due to disaster related damages of any kind, the business can suffer significantly, losing revenue during the time the business is closed and also losing customers to competitors. For any number of reasons, a business may also be forced to close, such as a power failure, a fire to a neighboring business or even nearby brush or wild fires such as those found in Arizona or Colorado. Having Business Interruption Insurance can save a business.

Typically, this type of insurance is part of a package or added when purchasing Property Insurance. A business will be covered for income they would have earned during the time they are unable to conduct business. This is generally based on the financial records of the company. The policy will also typically cover expenses the business still has to pay even though they cannot resume normal operations, such as the phone or electric bill.

As is the case with most types of insurance, there is a catch. Not unlike a deductible, there may be a waiting period of 48-hours before Business Interruption Insurance begins payment. It is still, however, worth inquiring about unless you can move your operations to another location entirely. In such a case you might consider Added Expense Insurance, mentioned below.

Deductibles

While your insurance company will pay most of the costs if you should suffer a loss covered under your policy, there is typically a deductible, which is the amount that they will not pay. Therefore, if your policy has a \$1,000 deductible and you have \$5,000 worth of damages, the first \$1,000 will come from your pocket and the remaining \$4,000 from the insurance company.

Typically, a policy with a low premium will have a higher deductible and visa versa. Depending on the risk involved, you can determine which option is better for your business. Sometimes it's better to pay a higher premium and have a lower deductible to pay at the time of an incident, or accident, when you may need to watch your money

closely as business operations may be slowed down or halted temporarily. Conversely, it may be better for your monthly cash flow to pay a lower premium, although you then carry a greater risk and will have a higher deductible. Work with an insurance professional to determine which is best for your needs.

Property Insurance deductibles can be on an individual claims basis or an aggregate basis. Depending on how many claims you anticipate making, you will determine which is best for you. Smaller companies that have few claims might find paying per claim to be advantageous, where a large company that may file many claims in the course of a year might be better with the cumulative payments made on an aggregate basis.

There are also several ways in which you will recoup money for property damages. A “cash value” basis is an assessment of the actual cost to replace the lost or destroyed item (less depreciation). A replacement cost will replace or repair an item at the current cost. Therefore, if the item stolen was a specialty piece of equipment, at the time cost \$2,000, but today would cost \$3,000, you would receive \$3,000 to replace it at today’s cost. Replacement cost coverage is less common and will typically have you paying higher premiums than a cash value basis of payment.

Making A Claim

Buying insurance is typically the easy part, once you understand the language and find an insurance agent with whom you feel comfortable. Often the more difficult aspect of being insured is filing a claim and getting the insurance company to pay on the claim.

To make a claim you need to:

- Notify your insurance company immediately when you experience a loss, damages or have a lawsuit filed against you or your business. You should also notify the police of a burglary, theft or accident immediately.
- Read your insurance policy, which will explain your responsibilities to the insurance company
- Assess the damages and/or list the items lost, stolen or destroyed
- Find receipts or proof of ownership for as many lost, stolen or destroyed items as possible
- In a lawsuit from a third party, gather any information you may have on the incident or reason for the lawsuit

Although you may elect to phone your insurance company, you should also send a written notice by registered mail to have verifiable proof of the date that you notified your insurance provider regarding a claim.

Keep in mind that some insurance companies will not cover any legal fees that you incur prior to notifying them about the claim. Therefore, if you run out and hire a lawyer prior to reporting the claim, you may pay out of pocket until you involve the insurance company.

The process of filing a claim will usually require that you have your paperwork in order. For example, if you have Business Interruption Insurance, you will need to show, on paper, how much business you are losing during the interruption period. As mentioned earlier in the book, it is essential to keep good records of your typical business activity. They will be used to determine how much income you are losing.

Once you file a claim, be prepared in case you need to do battle with your insurance company. If you feel you are not receiving a fair settlement, schedule a time to talk with your insurance agent, the claims adjustor and/or contact the customer service division of the insurance provider. Working with your insurance company, you may be able to reach a better settlement. If you are completely dissatisfied, you may hire an attorney familiar with insurance claims to help you with the settlement.

Ways To Lower Insurance Premiums

In an effort to pay lower insurance premiums, you can safeguard your business in many practical ways. Below are some suggestions:

- ✓ Install sprinkler systems and make sure they are maintained
- ✓ Have all electrical wiring properly installed by a professional and insulated
- ✓ Maintain adequate and updated files of business transactions and personnel information including all signed agreements
- ✓ Adhere to proper industry specific safety precautions
- ✓ Have all employees trained in the proper use of equipment – keep manuals readily available
- ✓ Make sure there is adequate lighting
- ✓ Have all vehicles maintained, registered and inspected on a regular basis
- ✓ Only allow employees with good driving records to operate a company vehicle
- ✓ Have clearly marked emergency exits and hold safety drills
- ✓ Limit access and the number of keys distributed to your primary facility and/or vehicles, warehouses or other facilities
- ✓ Have an arbitration provision in all of your contracts for settling disputes and to reduce the costs and hassles associated with disputes.
- ✓ Repair any damages, unsafe conditions or broken equipment

If you can make every effort to keep your employees (and yourself) safe from physical injury and you have employees read and sign policies covering conduct and behavior while employed, then you can typically lower your risks of accidents or lawsuits and in turn, lower your insurance premiums.

Other Types of Insurance

Along with purchasing Property Insurance and Liability Insurance (including E & O, Employment Practices, Product Liability and/or other forms of liability insurance), you will pay Unemployment Insurance as mandated by law. In addition you will typically pay

Disability Insurance in accordance with state regulations. Other types of insurance you may elect to purchase include:

- **Health & Medical Insurance:** The larger the business grows the more you will want to consider some type of health insurance to cover your employees' medical costs and/or work related injuries. Having a health plan in place will typically attract better, more qualified applicants. Generally you pay for part of the total health insurance plan and your employees contribute a portion as well.
- **D & O Insurance:** D & O Insurance is shorthand for a directors' and officers' insurance policy. The goal of this policy is to protect the officers and directors of a corporation from personal liability in the event of a claim or lawsuit against them claiming wrongdoing in connection with the company's business.
- **Vehicle Insurance:** This insurance covers liability for injuries caused by use of the vehicles owned and operated by your company as well as providing additional coverage for the vehicles beyond that of Property Insurance. The more your business relies on vehicles for deliveries or for transporting goods, the more you can benefit from such insurance.
- **Web Site Insurance:** In today's web conscious world, this insurance is growing in popularity and significance. Web Site Insurance covers claims made against the company's web site or as a result of actions taken or items purchased through the company web site. You should first check your policies to make sure you are not covered elsewhere. Web Site Insurance can protect you against lawsuits made in conjunction with activities on your site. This may include personal privacy matters or even computer viruses that have resulted from visiting your site.
- **Key Man Life Insurance:** This is a life insurance policy taken out on the owner of the business or the key person behind the business, in the event this individual dies. In a small business, which is closely run by one person, or a few key people, this type of insurance may be very worthwhile.

Choosing an Insurance Company

Before you sign with an insurance company, shop around. You will find that companies differ significantly. Below are several factors that you will want to weigh when choosing an insurance company.

- ✓ **Price:** The same amount of coverage can cost \$15,000 or \$50,000 depending which company you choose. Get quotes from three or four companies for the same type of policies.
- ✓ **Stability:** Insurance companies are evaluated and rated by various rating services. Among the most common are: A.M. Best Company in Oldwick, New Jersey, www.ambest.com; Moody's Investor Services in New York City, www.moody.com; Standard & Poor's Insurance Rating Services in New York City, www.standardandpoor.com; and Weiss Research in Palm Beach Gardens, Florida, www.weissratings.com
- ✓ **Service:** You will want to deal with an insurance company that provides fast and sufficient answers to your questions; reviews and responds to claims in a fair and timely manner; and provides both accessibility and a degree of comfort.

You can get more information on an insurance company by contacting your state insurance department, The Insurance Regulatory Information Network at www.irin.org, or the Better Business Bureau. You want to find out if there are many complaints registered and the validity of such complaints.

Word of mouth is one good way of finding an insurance company with which other businesses have had positive experiences. Also, try running a Google Web search on the particular type of coverage you need

Chapter 14

Office Leases

- Key Lease Terms
 - Options
 - Types of Leases
 - Getting Out of a Lease
-

Signing an office lease is a major step for anyone starting a business. It is a commitment to a location in which to do business. It is typically among the first milestones.

Prior to signing a lease it is imperative that you understand, and agree with, all of the key terms. Reading a lease can be difficult and intimidating. A lease is typically slanted in favor of the landlord, so it is important to determine which terms you can accept and which you need to negotiate. It is advantageous to have an attorney look over the lease with you to help evaluate all of the terms and clarify any unfamiliar wording.

Key Lease Terms

The first and most critical terms are typically the amount of rent you will pay and the length of the lease. Depending on the situation, they may be open for negotiation, particularly the length of the term.

Leases will often have rent escalation clauses. You should carefully review such clauses and match them with the projected cash flow of your business.

A shorter-term lease allows you the flexibility to pack up and leave sooner if you are not pleased with the location. A long-term lease can give you long term stability and keep rent increases down, but may tie you to a location that may not be profitable or one, which your business may outgrow. There are generally ways to break any lease, but it's not your intent going into such an agreement to seek ways to get out.

Among the other key terms you will want to focus on when evaluating a lease include:

- What type of lease are you signing? (Various lease types are discussed below.)
- What charges, taxes or fees are or are not included in the rent?

- Which improvements, modifications or repairs are you responsible for and which ones are your landlord responsible for?
- Exactly what are the physical boundaries included in the lease? (Are you paying for any common areas such as hallways, stairways or a shared loading dock?)
- Can the space be assigned or sublet to another party?
- How much is the security deposit (if there is one) and what are the conditions for its return?
- How can the lease be terminated early and what penalties will you have to pay?
- Specifically, what business activities can the premises be used for? Not used for?
- How are disputes resolved, should they arise between lessor and lessee?

Since there is no such thing as a “standard lease” it may be possible to negotiate the terms, depending on your position. If the space you are looking to rent is highly sought out by other businesses, your bargaining power will diminish greatly. Depending on how valuable the space is to your needs (such as a prime location) you will need to determine whether or not you can accept the terms of the lease with few or minimal changes.

If you have some leverage in negotiating the terms of the lease, look at several areas in which you can work a better deal. Most often the initial amount of rent will be the most difficult to negotiate. Therefore, you may look at other terms such as:

- Rent Escalations: If the landlord insists on rent escalations, try to negotiate that there is no escalation for the first two years and then agree upon a ceiling for increases after that. Such provisions may allow you to sign a longer-term lease. If the landlord has had trouble renting the space, he or she may also want to sign you for a longer term provided there are rent escalations.
- Repairs & Services: If the rental price is set, you may be able to make some agreement on repairs and services that will be provided by the landlord, such as a paint job.
- Returning the Premises to Their Original Condition: Typically most construction and alterations need to be approved by the landlord. Many businesses improve upon the structure of the original location by adding additional wiring for computers and additional telephone lines as well as enhancing the capacity for other technology. You may be able to negotiate that such upgrades can remain and that you do not have to return the premises to their original condition. In addition, you may be able to use the fact that your technological improvements will increase the value of the property as a bargaining chip.

Before negotiating terms of a lease, make a list of terms that would benefit your business. For example, if you are opening a jewelry store in a mall, the lease should

stipulate that no other, or only one other jewelry store, can open in the mall during the term of your lease. If you are expecting to generate walk-in business, you will need terms that allow you to put up necessary signage.

Whatever type of business you are opening, there are specific needs that will have to be discussed prior to signing a lease. In addition, make sure that zoning ordinances do not prohibit you from opening up the type of business you chose to run.

As is the case with any negotiation, the side with the greater need will have less bargaining power. A building owner or landlord who has had an empty storefront or office space for an extended period of time will be more agreeable to your terms including options. He or she may have a greater need to rent the space.

Options

When you negotiate your lease there are several options you can have included. The most common is the option to renew. Since landlords will want to raise the rent at the end of the initial agreed period, this will need to be addressed in advance. If you can get an option to renew at a predetermined fixed price, as opposed to renewing at the fair market price, you will likely save money when the initial term of the lease ends, especially if office rents have escalated.

A short lease with one or more options to renew gives you some flexibility. Typically, you have a certain time period before the end of the initial lease term in which you can notify the landlord in writing that you want to renew the lease at the predetermined amount. There may be an additional fee, also agreed upon in the initial lease for exercising your right to stay. Generally, with the exception of the increase in rent, other terms of the initial lease will carry over into the renewal period.

Another option you might include is the option for additional space. Being able to expand is key for a growing business. A landlord who sees the potential of having an important tenant that may attract other businesses, especially in a mall or similar retail situation, may be more inclined to grant you an option for additional space. You will need to examine and negotiate the terms for renting such extra space and make sure the space is suitable to your business needs.

The option for additional space may state that you will expand at the same per square foot rate that you are currently paying, at a fixed rate of increase or at the fair market rate at the time of the expansion. This will need to be determined when working out the initial option agreement. Such an option can only be included if the landlord can reserve or make such space available. A landlord may counter by offering you a right of first refusal, meaning you have first choice on any empty space at the same rental rate that any other tenant will pay. Again, it is a matter of which one of you is in the stronger position.

Also, becoming more common in commercial leases is the option to terminate the lease early. Landlords may offer such clauses to higher profile businesses to entice them to

sign longer-term leases and help draw other established tenants into the facility. The landlord will receive some form of compensation if the tenant exercises the option to leave early. In the case of retail leases, particularly at malls, landlords may guarantee a level of occupancy among surrounding storefronts. If that level, for example 75% occupancy, is not met by a certain date, the tenant then has the option to terminate the lease.

Types of Leases

A wide range of commercial leasing possibilities exist. Typically, an office lease in a major city and a retail lease in a suburban shopping center will be considerably different.

From a broad perspective, there are a few types of leases commonly found. Within these categories, leases may vary considerably.

- **Gross Lease**: The tenant pays a set amount of rent and the landlord is responsible for payment of taxes, insurance and other costs associated with owning the property.
- **Net Lease**: The tenant pays the rent plus a portion of the maintenance fees, insurance premiums and other operating expenses.
- **Triple-Net Lease**: Typically, for a freestanding facility, this type of lease has the tenant paying for all fees and operating expenses associated with the space.
- **Shopping Center Leases**: The tenant pays a base rate in conjunction with the square footage of the retail facility. Typically, the tenant will also pay some common charges and frequently a certain percentage of the gross sales. The tenant may also be assessed part of the property taxes. A shopping mall lease will often include terms about signage, hours of operations, common areas and deliveries. The landlord may also have the right to relocate the tenant.
- **Land or Ground Lease**: The tenant leases the grounds and builds on the property. Typically, with a land or ground lease, all improvements on the property, including any building or buildings revert back to the landowner at the end of the lease period.

There are numerous variations on common lease forms. For example a lease may cover both office and warehouse space in one facility with separate rental amounts and separate options.

Additional Costs

Leases typically address who pays for electricity, water and heat. Some terms you should know include:

- ✓ **Operating Costs:** An overall term for additional building related expenses such as janitorial, electrical and maintenance costs.
- ✓ **Overages:** The increase in the cost to operate the property from one year to the next. If, for example the cost for electricity was \$2 per foot one year and \$2.30 per foot the next, the overage of \$.30 would be passed on to the tenant.
- ✓ **Pass Through Costs:** All expenses that are passed through from landlord to tenant.

Getting Out Of A Lease

Your reason for wanting to get out of the lease will factor into the method you choose. A tenant generally wants out of a lease because:

- Business is growing and the facility is too small
- Business is bad and the rent payment is too high or you simply want to close up shop
- You are dissatisfied with the service of the landlord or how the terms of the lease are being handled

If you need to move to a larger space or a better location, one option is to sublease the space to someone else. You must first make sure subletting is allowed in the terms of the lease. Most often a sublet is allowed with the approval of the landlord. You will still be obligated to the landlord if the subtenant defaults on payment.

Another option, if business is going well, is to buy out the remaining portion of the lease with a lump sum payment. If the landlord will be able to rent the space without much difficulty, your buyout price will be far less than the amount remaining on the lease. This payment may be worthwhile if you are moving to a bigger space or better location.

If business is going poorly, you can also look to sublet, or find a new tenant with whom the landlord can negotiate a new lease for more money. Talk to your landlord about the situation. Landlords usually do not benefit from having a tenant who might be headed toward bankruptcy, so they may allow you to rent out the space, or a portion thereof, while actively looking to find a new tenant.

If you are dissatisfied with the manner in which the landlord is meeting the terms as outlined in the initial lease, re-read your lease carefully and see if any terms have been violated that allow you to break the lease. Read the section on how all disputes will be handled. Do you have sufficient grounds to get out of the lease? If, for example, the lease states that you will have the only jewelry store in the mall, but a department store

opens directly across from you, selling jewelry in one of their many departments, does that violate the lease? Your business is being affected. If you are paying a percentage of your business to the landlord, then this drop in business is also affecting his or her share of your rent. Therefore, the landlord may try to work out a compromise solution, which might mean relocating your shop or talking with the department store about moving their jewelry department farther away from your store.

You should first make an effort to work out the situation with your landlord rather than having to resort to legal action.

Legal counsel can advise on situations whereby you are looking to get out of a lease because you are dissatisfied with how the terms are being handled.

Lease Review

Below are some common lease terms that you will want to put on your list of key areas to discuss.

- ✓ Lease term
- ✓ Manner of payment and when payment is due
- ✓ Type of lease
- ✓ Escalations and manner of calculation
- ✓ Responsibility for repairs and maintenance
- ✓ Responsibility for common areas (if any)
- ✓ Subleasing or Assignment of lease
- ✓ Security deposit
- ✓ Terms for early termination
- ✓ Options to renew
- ✓ Manner of settling disputes
- ✓ Permitted use of space

A checklist for office leases can be found in Appendix A: Forms & Agreements.

Appendix A

Forms & Agreements

- A1: **Checklist for Contracts**
- A2: **Checklist for Formation of a California Corporation**
- A3: **Employee Offer Letter**
- A4: **Stock Subscription Agreement**
- A5: **Sample Short Form Business Plan**
- A6: **Checklist for Office Leases**
- A7: **Sample Press Release**
- A8: **Sample Financial Statements**
- A9: **Sample Confidentiality Agreement**
- A10: **Checklist for Issuing Stock**

Form A1**Contract Checklist****(1) Identity of Parties**

- Name
- Type of entity of each party (corporation, LLC, etc.)
- Addresses

(2) Recitals

- Background of agreement
- Purpose for entering into the contract
- Key assumptions for the contract

(3) Obligations of the Parties

- What is each side required to do?
- By what date?
- If something has to be delivered, whose obligation is it and at who's cost?

(4) Terms of the Contract

- Is the contract a one-shot situation or will it last for some designated time period?
- How can the term be renewed or extended?

(5) Price

- What is the price for the product or service?
- Is it a fixed price, determined by a formula, by a project fee, or some other manner?
- Who pays any tax?

(6) Payment Terms

- When is payment due?
- Will there be installment payments?
- Will interest be charged?
- Is there a penalty for late payment?

(7) Representations and Warranties

- What representations and warranties are to be made by the parties?
- Are certain warranties disclaimed (e.g., merchantability or fitness for a particular purpose)?
- How long are any warranties good for?

(8) Liability

- What limitations of liability exist (e.g., no liability in excess of payment received, or no liability for consequential damage or lost profits)?
- Under what circumstances is one party liable (e.g., material breach of agreement or grossly negligent in performing services)?

(9) Termination of Contract

- When can one party terminate the contract early?
- What are the consequences of termination?
- What post-termination obligations are there?

(10) Confidentiality

- What confidentiality obligations are there?
- What are the exclusions from confidentiality?

(11) Default

- What are the events of default?
- Does a party have a period to cure a default?
- What are the consequences of a default?

(12) Disputes

- How are disputes to be handled – litigation, mediation or arbitration?
- If arbitration, what rules will govern? (e.g., JAMS/Endispute or the American Arbitration Association)
- If arbitration, how many arbitrators and how will they be picked?
- If arbitration, will there be procedures for discovery and what the arbitrator can and can't do?
- If litigation, where can or must the litigation be brought?

(13) Indemnification

- Is there indemnification for certain breaches or problems?
- What is the procedure required to obtain indemnification?
- Is there a cap on or exclusions from indemnification?

(14) Miscellaneous

- Governing law
- Attorneys fees
- Modification of Agreement
- Notice
- Entire Agreement
- Severability
- Time of the Essence
- Survival
- Ambiguities
- Waiver
- Headings

- Necessary Acts and Further Assurances
- Execution
- Jury Trial Waivers
- Specific Performances
- Representation on Authority of Parties
- Force Majuere
- Assignment

(15) Signatures

- What authority is required for one party to sign the contract (e.g., Board of Directors approval)?
- How many signatures are required?
- Are the signature blocks correct? For corporations, this is a typical appropriate signature block:

ABC, Inc.

By: _____
John Smith, President

Form A2**CHECKLIST FOR FORMATION OF A CALIFORNIA CORPORATION**A. Information for Articles of Incorporation

1. Preferred name(s) of corporation (in order of preference)
2. Trademark and trade name search for articles?
3. Name and street address of the initial agent for service of process (P.O. Box not acceptable)

4. Total number of authorized shares of Common Stock
5. Blank Check Preferred Stock provision desired?
6. Name of incorporator

B. Bylaws

1. The street address of principal office of the corporation

2. Date and time of annual meeting of shareholders

3. Authorized number of directors:
 - (a) Fixed # _____
 - (b) Variable: From _____ to _____
(see Cal. Corp. Code § 212)
Fixed initially at _____
4. Accounting Year End:
5. Optional provisions desired:
(see Cal. Corp. Code § 212)

C. Action by Incorporator

1. The names and addresses of the initial directors

D. Unanimous Written Consent In Lieu of Meeting of Board of Directors

1. Names and Titles of Officers and Driver's License numbers (*indicates a required officer; all others are optional)

<u>Name</u>	<u>Title</u>	<u>LicenseNo. for DE-1 Form</u>
_____	President and Chief	_____
_____	Executive Officer*	_____
_____	Secretary*	_____
_____	Chief Financial Officer*	_____
_____	Vice President	_____
_____	Assistant Secretary	_____
_____	Chairman	_____

2. Initial Issuance of Shares

- (a) Aggregate shares to be issued:

<u>Name</u>	<u>Address</u>	<u>Number of Shares</u>	<u>Consideration (and Valuation if Non-Cash)</u>
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____

- (b) Specify if issuance of shares is to be under:

California:

- (1) _____ Section 25102(f)
- (2) _____ Section 25102(h) of the Corporate Securities Law of 1968
- (3) _____ Other exemption: _____
- (4) _____ Qualification with the Department of Corporations

Federal

- (1) _____ Rule 504, 505, or 506 of SEC Regulation D [Note - Form D must be filed no later than 15 days after first receipt of subscriptions or money]
- (2) _____ Section 4(2)
- (3) _____ Other exemption: _____

Other State Blue Sky Laws:

- (1) _____
- (2) _____

3. Principal Executive Office Address

4. Authorization of bank account(s)

(a) Name and branch of bank(s) _____

(b) Number of signatures required _____

Authorized signatories:

(c) Dollar limitations, if any, on authority of signatories _____

5. Borrowing Resolutions

(a) Maximum amount of borrowing _____

(b) Lender's Name _____

E. S Corporation Election and Form SS-4 Information

1. Is S Corporation election to be made?

_____ Yes _____ No

2. Social Security numbers of Shareholders and Spouses:

<u>Name</u>	<u>Spouse</u>	<u>Shareholder's Social Security No.</u>	<u>Spouse's Social Security No.</u>
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____
_____	_____	_____	_____

3. S Corporation election to be effective for taxable year beginning

4. Date corporation first had shareholders

5. Date corporation will first have assets

6. Date corporation will begin doing business

7. Taxable year ending

8. Description of principal business activity

9. County of business location

10. Estimated number of employees in first year

11. First date wages (will be) paid:

12. Products or services to be sold:

☐ Wholesale ☐ Retail ☐ N/A ☐ Other: _____

F. Fictitious Business Name, Tradename, Trademark search issues?

G. Where will the company be doing business, for purposes of qualifying to do business in those states?

Offer Letter to Prospective Employee

[Date]

Re: Terms of Employment

Dear _____:

We are pleased to inform you that after careful consideration, _____ (the “Company”) has decided to make you this offer of employment. This letter sets forth the terms of the offer which, if you accept, will govern your employment.

Position; Duties. Your position will be _____, reporting to the _____ of the Company. Your duties and responsibilities, will be as designated by the Company, with an initial focus on (i) _____ and (ii) _____.

Full Time Employment. The employment term will begin on _____, ____.

Compensation. Your compensation will be \$_____ a year, paid twice monthly consistent with the Company’s payroll practices. Your package will include participation in the health and other benefit plans of the Company pursuant to their terms as may be amended by the Company from time to time[; until the Company’s health plan is adopted, your reasonable COBRA payments will be reimbursed (subject to a maximum of \$200 per month)]. You will be entitled to _____ week’s paid vacation (equivalent of ____ business days) for each year of full employment.

Stock Options. You will be granted options to acquire _____ shares of the Company’s Common Stock, vesting over a [four (4)] year term with one (1) year cliff vesting for 1/4th of the options. The options will be granted at a strike price of \$_____ per share. The terms and conditions of your stock options are contained in a Stock Option Agreement of even date herewith and must be executed by you and returned to us immediately to be effective.

Employment at Will. Our employment relationship is terminable at will, which means that either you or the Company may terminate your employment at any time, and for any reason or for no reason.

Confidentiality and Invention Assignment Agreement. You will be subject to the Company's Confidentiality and Invention Assignment Agreement, which is enclosed with this letter and must be signed and returned by you before any employment relationship will be effective.

Certain Acts. During employment with the Company, you will not do anything to compete with the Company's present or contemplated business, nor will you plan or organize any competitive business activity. You will not enter into any agreement, which conflicts with your duties or obligations to the Company. You will not during your employment or within one (1) year after it ends, without the Company's express written consent, directly or indirectly solicit or encourage any employee, agent, independent contractor, supplier, customer, consultant or any other person or company to terminate or alter a relationship with the Company.

No Inconsistent Obligations. You represent that you are aware of no obligations legal or otherwise, inconsistent with the terms of this Agreement or with your undertaking employment with the Company. You will not disclose to the Company, or use, or induce the Company to use, any proprietary information or trade secrets of others. You represent and warrant that you have returned all proprietary and confidential information belonging to all prior employers.

Miscellaneous. Upon your acceptance, this letter will contain the entire agreement and understanding between you and the Company and supersedes any prior or contemporaneous agreements, understandings, term sheets, communications, offers, representations, warranties, or commitments by or on behalf of the Company (oral or written). The terms of your employment may in the future be amended, but only by writing and which is signed by both you and, on behalf of the Company, by a duly authorized executive officer. In making this offer, we are relying on the information you have provided us about your background and experience, including any information provided us in any Employment Application that you may have submitted to us. The language in this letter will be construed as to its fair meaning and not strictly for or against either of us. In the event a dispute does arise, this letter, including the validity, interpretation, construction and performance of this letter, shall be governed by and construed in accordance with the substantive laws of the State of [California or other State]. Jurisdiction for resolution of any disputes shall be solely in [City] [State].

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If these terms are acceptable, please sign in the space provided below and return this letter to us. Again, we're very excited to have you join the Company.

Yours truly,

[Name]

[Title]

Agreed and Accepted:

[Name]

Form A4**Stock Subscription Agreement**

The undersigned hereby offers to subscribe for the number of shares of Common Stock (the "Shares") of _____ (the "Company") set forth on the signature page of this Subscription Agreement at a price of \$_____ per Share.

By execution of this Subscription Agreement, the undersigned hereby acknowledges that the undersigned understands that the Company is relying upon the accuracy and completeness hereof in complying with its obligations under applicable federal and state securities laws. The undersigned further acknowledges and certifies that the undersigned received and read the Private Placement Memorandum of the Company dated _____ and any supplements thereto (the "Private Placement Memorandum"), and the undersigned is familiar with the terms and provisions thereof.

The undersigned agrees and represents as follows:

1. Representations, Warranties and Agreements.

The undersigned hereby represents and warrants to, and agrees with, the Company, as follows:

(a) That the undersigned is aware of the following:

- (1) The Shares are speculative investments which involve a substantial degree of risk of loss by the undersigned of the undersigned's entire investment in the Company and that the undersigned understands and takes full cognizance of the risk factors related to the purchase of the Shares, including, but not limited to those set forth in the Private Placement Memorandum;
- (2) The Company is newly formed and has been operating at a loss and may do so for the foreseeable future.
- (3) There are significant restrictions on the transferability of the Shares; the Shares will not be, and the investors will have no rights to require that the Shares be registered under the Securities Act of 1933 (the "Act") or any state securities laws; there is no public market for the Shares and none is expected to develop; and, accordingly, it may not be possible for the undersigned to liquidate the undersigned's investment in the Company;
- (4) No federal or state agency has made any findings as to the fairness of the terms of the offering; and

- (5) Any projections or predictions that may have been made available to investors are based on estimates, assumptions and forecasts which may prove to be incorrect; and no assurance is given that actual results will correspond with the results contemplated by the various projections;
- (b) That at no time has it been explicitly or implicitly represented, guaranteed or warranted to the undersigned by the Company, the agents and employees of the Company, or any other person: (1) That the undersigned will or will not have to remain as owner of the Shares an exact or approximate length of time; (2) That a percentage of profit and/or amount or type of consideration will be realized as a result of this investment; (3) That any cash dividends from Company operations or otherwise will be made to shareholders by any specific date or will be made at all; or (4) That any specific tax benefits will accrue as a result of an investment in the Company;
- (c) That the undersigned is financially responsible, able to meet all obligations hereunder, and acknowledges that this investment will be long-term and is by nature speculative;
- (d) That the undersigned has received and carefully read and is familiar with the Private Placement Memorandum, this Subscription Agreement, and all other documents in connection therewith, and the undersigned confirms that all documents, records and books pertaining to the investment in the Company have been made available to the undersigned and/or to the undersigned's personal investment, tax and legal advisers, if such advisers were utilized by the undersigned;
- (e) That the undersigned has relied only on the information contained in the Private Placement Memorandum and that no written or oral representation or information that is in any way inconsistent with the Private Placement Memorandum and has been made or furnished to the undersigned or to the undersigned's purchaser representative in connection with the offering of the Shares, and if so made, has not been relied upon;
- (f) That the undersigned is capable of bearing the high degree of economic risks and burdens of this venture including, but not limited to, the possibility of complete loss of investment and the lack of a public market which may make it impossible to readily liquidate the investment whenever desired;
- (g) That the undersigned is an "accredited investor" as that term is defined in Regulation D under the Act or is otherwise a sophisticated, knowledgeable investor (either alone or with the aid of a purchaser representative) with adequate net worth and income for this investment;

- (h) That the undersigned has knowledge and experience in financial and business matters (either alone or with the aid of a purchaser representative), is capable of evaluating the merits and risks of an investment in the Company and its proposed activities and has carefully considered the suitability of an investment in the Company for the undersigned's particular financial situation, and has determined that the Shares are a suitable investment;
- (i) That the offer to sell Shares was communicated to the undersigned by the Company in such a manner that the undersigned was able to ask questions of and receive answers from the Company concerning the terms and conditions of this transaction and that at no time was the undersigned presented with or solicited by any leaflet, public promotional meeting, newspaper or magazine article, radio or television advertisement or any other form of advertising or general solicitation;
- (j) That the Shares for which the undersigned hereby subscribes are being acquired solely for the undersigned's own account, for investment, and are not being purchased with a view to or for the resale, distribution, subdivision or fractionalization thereof; and the undersigned agrees that such Shares will not be sold without registration under the Act or an exemption therefrom. In furtherance thereof, the undersigned will not sell, hypothecate or otherwise transfer the undersigned's Shares unless the Shares are registered under the Act and qualified under applicable state securities laws or unless, in the opinion of the Company, an exemption from the registration requirements of the Act and such laws is available;
- (k) That the undersigned has had prior personal or business relationships with the Company or its affiliates, or by reason of the undersigned's business or financial experience (either alone or with the aid of a purchaser representative), the undersigned has the capacity to protect the undersigned's own interest in connection with this transaction;
- (l) That the undersigned has been advised to consult with the undersigned's own attorney regarding legal matters concerning an investment in the Company and has done so to the extent the undersigned considers necessary;
- (m) That the undersigned certifies, under penalty of perjury, (i) that the social security or Tax Identification Number set forth herein is true, correct and complete, and (ii) that the undersigned is not subject to backup withholding either because the undersigned has not been notified that the undersigned is subject to backup withholding as a result of a failure to report all interest or dividends, or the Internal Revenue Service has notified the undersigned that the undersigned is no longer subject to backup withholding; and

- (n) That the undersigned acknowledges that the Private Placement Memorandum reflects the Company's current intentions and estimates at the current time, and as with any developing company, the precise elements of the Company's plans can be expected to change from time to time.

2. Indemnification. The undersigned shall indemnify, defend and hold harmless the Company, and any officers, employees, shareholders, partners, agents, directors or controlling persons of the Company (collectively the "Indemnified Parties" and individually an "Indemnified Party") who was or is a party or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative, against losses, liabilities and expenses of each Indemnified Party (including attorneys' fees, judgments, fines and amounts paid in settlement, payable as incurred) incurred by such person or entity in connection with such action, arbitration, suit or proceeding, by reason of or arising from (i) any misrepresentation or misstatement of facts or omission to represent or state facts made by the undersigned, including, without limitation, the information in this Subscription Agreement, or (ii) litigation or other proceeding brought by the undersigned against one or more Indemnified Party wherein the Indemnified Party is the prevailing party.

3. Entity Investors. If the undersigned is an entity, trust, pension fund or IRA account (an "Entity"), the Entity and the person signing on its behalf represent and warrant that: (i) such Entity is an existing entity, and has not been organized or reorganized for the purpose of making this investment (or if not true, such fact shall be disclosed to the Company in writing along with information concerning the beneficial owners of the Entity), (ii) the undersigned has the authority to execute this Subscription Agreement, and any other documents in connection with an investment in the Shares, on the Entity's behalf, (iii) the Entity has the power, right and authority to invest in the Shares and enter into the transactions contemplated thereby, and that the investment is suitable and appropriate for the Entity and its beneficiaries (given the risks and illiquid nature of the investment) and (iv) all documents executed by the entity in connection with the Company are valid and binding documents or agreements of the Entity enforceable in accordance with their terms.

4. Revocation. The undersigned agrees that the undersigned may not cancel, terminate or revoke the offer to subscribe for shares for a period of 120 days or any agreement hereunder at any time and that this Agreement shall survive the death or disability of the undersigned and shall be binding upon the undersigned's heirs, executors, administrators, beneficiaries, successors and assigns.

5. Certain Securities Law Matters.

- (a) The Shares shall not be sold, assigned, transferred or pledged except upon satisfaction of the conditions specified in this Section 5, which conditions are intended to ensure compliance with the provisions of the Act. The undersigned will cause any proposed purchaser, assignee,

transferee or pledgee of the Shares held by the undersigned to agree to take and hold such securities subject to the provisions and conditions of this Section 5.

- (b) Each certificate representing (i) the Shares and (ii) any other securities issued in respect of the Shares upon any stock split, stock dividend, recapitalization, merger, consolidation or similar event, shall (unless otherwise permitted by the provisions of Section 5(c) below) be stamped or otherwise imprinted with a legend substantially in the following form (in addition to any legend required under applicable state securities laws):

THE SHARES REPRESENTED BY THIS CERTIFICATE
HAVE BEEN ACQUIRED FOR INVESTMENT AND HAVE
NOT BEEN REGISTERED UNDER THE SECURITIES ACT
OF 1933. SUCH SHARES MAY NOT BE SOLD OR
TRANSFERRED IN THE ABSENCE OF SUCH
REGISTRATION OR UNLESS THE COMPANY RECEIVES
AN OPINION OF COUNSEL OR OTHER EVIDENCE
REASONABLY ACCEPTABLE TO IT STATING THAT
SUCH SALE OR TRANSFER IS EXEMPT FROM THE
REGISTRATION AND PROSPECTUS DELIVERY
REQUIREMENTS OF SAID ACT. COPIES OF THE
AGREEMENT COVERING THE PURCHASE OF THESE
SHARES AND RESTRICTING THEIR TRANSFER MAY BE
OBTAINED AT NO COST BY WRITTEN REQUEST MADE
BY THE HOLDER OF RECORD OF THIS CERTIFICATE
TO THE SECRETARY OF THE CORPORATION AT THE
PRINCIPAL EXECUTIVE OFFICES OF THE
CORPORATION.

The undersigned consents to the Company making a notation on its records and giving instructions to any transfer agent of the Shares in order to implement the restrictions on transfer established in this Section 5.

- (c) The undersigned agrees to comply in all respects with the provisions of this Section 5. Prior to any proposed sale, assignment, transfer or pledge of any Shares, unless there is in effect a registration statement under the Act covering the proposed transfer, the undersigned thereof shall give written notice to the Company of the undersigned's intention to effect such transfer, sale, assignment or pledge. Each such notice shall describe the manner and circumstances of the proposed transfer, sale, assignment or pledge in sufficient detail, and shall be accompanied, at the undersigned's expense evidence satisfactory to the Company the effect that the proposed transfer of the Shares may be effected without registration under the Act or applicable state securities law.

6. Investor Information

The Company may only accept subscriptions from persons who meet certain suitability standards. Therefore, certain information is requested below.

(a) Name: _____

Age: _____

Social Security Number: _____

(b) Home Address: _____

Home Telephone Number: _____

(c) Firm Name: _____

Nature of Business: _____

Position/Title: _____

Length of Time in Position: _____

Business Address: _____

_____ Zip Code: _____

Business Telephone Number: _____

(d) Send Correspondence to: Home _____ Business _____

(e) List each prior employment position or occupation during the last five years, giving dates: _____

(f) List any business or professional education, indicating degrees received, if any: _____

(g) (1) My net worth (together with my spouse's net worth), is in excess of \$ _____

(2) In order for the Company to determine if I qualify as an “accredited investor” under Regulation D of the Securities Act of 1933, the reasonable fair market value of my personal home, home furnishings, and automobile is in excess of \$_____.

(3) My estimated annual gross income was or is (do not include your spouse’s income):

<u>Current Year</u>	<u>Last Year</u>	<u>Year Before</u>
\$_____	\$_____	\$_____

(4) My spouse’s actual gross income and estimated gross income was or is:

<u>Current Year</u>	<u>Last Year</u>	<u>Year Before</u>
\$_____	\$_____	\$_____

(h) Previous Investment Experience in Other Private Offerings of Securities or Other Relevant Experience:

Name of Program Or Company	1. _____
	2. _____
	3. _____
Amount Invested	1. _____
	2. _____
	3. _____

(i) In which state do you currently

- (a) Maintain your primary residence? _____
- (b) Maintain your secondary residence? _____
- (c) Vote? _____
- (d) File income tax returns? _____
- (e) Maintain a driver’s license? _____

(j) List any other information you believe is relevant in showing that you are able to adequately evaluate the risks and merits of this investment:

In furnishing the above information, I acknowledge that the Company will be relying thereon in determining, among other things, whether there are reasonable grounds to believe that I qualify as a purchaser under applicable securities laws for the purposes of

the proposed investment.

7. Miscellaneous.

- (a) All notices or other communications given or made hereunder shall be in writing and shall be delivered or mailed by registered or certified mail, return receipt requested, postage prepaid, to the Company at the address set forth on the instructions page hereof and to the undersigned at the address set forth on the signature page hereof.
- (b) This Agreement shall be governed by and construed in accordance with the laws of the State of California, without reference to conflict of law principles.
- (c) This Agreement constitutes the entire agreement among the parties hereto with respect to the subject matter hereof and supersedes any prior or contemporaneous understandings, representations, warranties or agreements (whether oral or written) and may be amended only by a writing executed by all parties.
- (d) The undersigned acknowledges that the Company may, in its sole and absolute discretion, accept or reject this subscription offer in whole or in part.

8. Certification.

The undersigned represents to you that (i) the information contained herein is complete and accurate on the date hereof and may be relied upon by you and (ii) the undersigned will notify you immediately of any change in any of such information occurring prior to the acceptance of the subscription and will promptly send you written confirmation of such change. The undersigned hereby certifies that he has read and understands the Private Placement Memorandum and this Subscription Agreement.

IN WITNESS WHEREOF, the undersigned has executed this Subscription Agreement
this _____ day of _____.

Number of Shares Subscribed for
at \$_____ per share
\$_____
Total Purchase Price

NAME OF PURCHASER

Signature

Title of Authorized Signatory if Purchaser
Is a corporation, partnership or other entity

Signature of Spouse or Co-owner

THE SECURITIES HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE "ACT") AND MAY NOT BE OFFERED, SOLD OR OTHERWISE TRANSFERRED UNLESS THE SECURITIES ARE REGISTERED UNDER THE ACT OR AN EXEMPTION THEREFROM IS AVAILABLE.

Accepted by Company,
[NAME OF COMPANY]

By: _____

Title: _____

Date: _____

Form A5**Sample Short Form Business Plan*****Picture Perfect, Inc.***

900 Remington Road

Philadelphia, PA

Phone: (215) 976-4000 Fax: (215) 976-4001

E-mail: mpeterson@aol.com Web Site: www.ppi.com

Business Description:

Picture Perfect, Inc. (the “Company”) was founded by an experienced management team to develop and market new types of consumer products in the picture frame, photography products and photo album markets. The Company has applied for patents on several of its new innovative products.

Industry and Market Description:

The picture frame, photography products and photo album markets have annual sales in excess of \$15 billion, expected to grow to \$20 billion by 2015. The picture frame industry is dominated by three large players (Burnes, Fetco and Carr) and smaller niche players (Malden, Advent). Photo albums are made and distributed by many of the same companies. Large retail chains as well as specialty boutique stores are the primary purchasers of picture frame and photo albums.

The photography products industry consists of numerous companies large and small (Kodak, Fuji, Arrelle). The Company, however, will be focusing on photography products for general consumer orientation (as opposed to professional photographers).

The Company plans to develop and market comprehensive innovative product lines to intelligently compete in all three areas, with the goal of obtaining significant and profitable market share.

Company History:

The Company was formed in August 2011 by four individuals with significant experience and contacts in the various relevant industries. Since that time, the Company has (1) designed four new picture frame products, (2) designed two new photo album products, (3) lined up several distributors, (4) made product demonstrations to Macy’s, Nordstrom’s, Wal-Mart, JC Penney, and other major retailers, and (5) implemented manufacturing contracts.

The Company’s Products:

The Company’s products are intended to be innovative and interesting. The Company has designed a new series of frames, the DateFrame™ picture frames, which incorporate a feature that displays the date when the picture was taken on a built-in mechanism in the frame. The Company has a patent pending on this product line. The Company has also designed picture

frames and photo albums, samples of which are available on request. The Company plans to develop a broad based product line to penetrate the market.

Marketing:

The Company intends to use a combination of employees and distributors for marketing its products. The Company founders have extensive relationships with major prospective chain stores and distributors, which should facilitate marketing. The Company has also been developing distinctive packaging and logos to achieve brand recognition for its products.

Projections:

The Company projects that sales and profits will be as follows, all as further detailed in more extensive projections and underlying assumptions available upon request:

	<u>2012</u>	<u>2013</u>	<u>2014</u>
Revenues	\$450,000	\$1,625,000	\$3,000,000
Cost of Sales	225,000	700,000	1,100,000
Gross Profit	225,000	925,000	1,900,000
Operating Expenses	452,000	707,000	1,210,000
New Income (loss) Before Taxes	(277,000)	218,000	690,000

Management Team:

<u>President:</u>	<u>Barry Sanders:</u> Previously Head of Product Development at Burnes of Boston (the largest picture frame company in the United States); formerly Marketing Manager at Eastman Kodak. 20 years of industry experience.
<u>Vice President of Operations:</u>	<u>Terry Davis:</u> Previously Office Manager at PhotoExpress, Inc.; 10 years of operations experience with Carr Frames, Inc. and Fetco International. 15 years of industry experience.
<u>Vice President of Development:</u>	<u>Joe Bledsoe:</u> Previously Chief Product Designer of Arrelle (consumer photography products) and Product Manager at Macy's; 10 years of industry experience.
<u>Chief Financial Officer:</u>	<u>Confidential Candidate:</u> CPA, Big 4 Accounting experience; Controller and CFO for consumer products companies; 15 years of industry experience.

Vice President of
Marketing:

Jill Buckley: MBA from Penn State; Marketing Manager at Digital Albums, Inc. and Burnes of Boston. 12 years of industry experience.

Funding:

Amount Needed:

\$3-\$5 million of funding is needed over the next two years for development, marketing, manufacture, sales and personnel.

Funding History:

Over \$400,000 has been raised from the founders of the company and angel investors.

* * * *

Form A6**CHECKLIST FOR OFFICE LEASES**

1. Space
 - (a) What is the rentable square footage?
 - (b) What is the usable square footage?
 - (c) Is rent based on usable or rentable square footage?
 - (d) Verify square footage number provided by the landlord.

2. Permitted Uses of the Premises
 - (a) What uses of the premises are permitted?
 - (b) Is the permitted use clause broad enough for possible changes in the business?
 - (c) Is the permitted use clause broad enough for potential assignments or subleases?
 - (d) Can the use clause be drafted to include “any lawful purposes”?
 - (e) Can uses be changed with landlord’s consent, which consent can’t be unreasonably withheld or delayed?

3. Primary lease term
 - (a) What is the commencement date of the lease?
 - (b) What happens if the space is not ready on the commencement date? Is there rent abatement, monetary damages, right to cancel the lease, or other remedies specified?
 - (c) What is the termination date?
 - (d) Does the landlord have the right to terminate early without cause?
 - (e) Does the tenant have the right to terminate early by payment of a fee?

4. Rentals
 - (a) What is the base rent for the primary term?
 - (b) Are there escalation clauses?
 - (c) Are there cost of living increases?
 - (d) Is there a cap on any rent increases?
 - (e) Is there a reasonable grace period and written notice before a late charge is imposed?

5. Common area maintenance, HVAC, and Operating costs
 - (a) What does the tenant have to contribute for common area maintenance, ventilating, heating, air conditioning, and other building operation costs?
 - (b) Is there a cap?
 - (c) Can the amount be increased each year?
 - (d) Real estate taxes and other impositions:
 - (i) Does the tenant have to pay a portion of the real estate taxes?
 - (ii) What increases over base year are allowed?
 - (iii) Is there a cap on tax increases?

- (iv) Does the tenant have to pay increased taxes that may occur on sale of the building?
- (e) Are there any special provisions or exceptions on the payment of these expenses?
- (f) When is payment due?
- (g) What detailed reports does the landlord have to provide the tenant showing the actual expenses?
- (h) What audit rights does the tenant have to review the landlord's books and records?
- (i) Are there provisions made for weekend and holiday service? What are the charges?
- (j) Does the tenant have a remedy for service interruption?

6. Tenant Improvements

- (a) What tenant improvements will be necessary?
- (b) What is the cost?
- (c) How much time will it take to complete the tenant improvements?
- (d) Will the landlord contribute to the cost for the tenant improvements?
- (e) What approvals will be necessary?
- (f) What permits will be necessary?
- (g) Does the landlord or the tenant own any improvements?

7. Repairs and replacements:

- (a) What responsibility does the tenant have for repairs or replacements?
- (b) What responsibility does the landlord have for repairs or replacements?
- (c) At the end of the tenancy, is tenant's obligation to return the premises in same condition at the beginning of tenancy, excluding (1) ordinary wear and tear, (2) damage by fire and other unavoidable casualty, and (3) alterations previously approved by landlord?

8. Utilities:

- (a) Direct supply or individually metered?
- (b) Method of computing payment?

9. Assignment and subletting:

- (a) Is the landlord's written approval required?
- (b) What standard is there for approval? absolute discretion? reasonable approval?
- (c) Does the landlord have the right to cancel the lease if notified of a proposed assignment of sublease?
- (d) If the assignment or sublet is at a higher price than the base rent, who keeps the excess? or what split is there?
- (e) Can the lease be assigned to affiliates of the tenant without landlord approval?
- (f) Can the landlord terminate the lease if the stock ownership of the tenant changes?

10. Subordination and attornment:
 - (a) All present or future mortgages?
 - (b) Execution of estoppel certificates required?
 - (c) Tenant agrees to attorn to landlord's successor in interest?
11. Destruction:
 - (a) Is there a right of cancellation for the tenant in the event of destruction?
 - (b) What obligation does the landlord have to rebuild?
 - (c) Does the tenant share in any proceeds from insurance?
12. Indemnity and Disclaimer:
 - (a) Indemnity mutual or tenant only?
 - (b) Waiver of claims mutual or tenant only?
 - (c) Waiver of subrogation?
 - (d) Landlord liability limited to interest in property?
13. Default:
 - (a) Does the tenant have a cure period after notice of a breach?
 - (b) What remedies are available for breach?
14. Landlord's warranties:
 - (a) Quiet enjoyment of premises by the tenant?
 - (b) First class services?
 - (c) Security building?
 - (d) Ownership of building?
15. Option to renew
 - (a) Does the tenant have the option to renew the lease?
 - (b) How long is the renewal option?
 - (c) How far in advance must the option be exercised?
 - (d) How is rent determined for the renewal period?
16. Right of first refusal or first offer for additional space
 - (a) What is the scope of any right of first offer or first refusal?
 - (b) How is rent determined?
 - (c) How long does the tenant have before exercising the right?
17. Security deposit:
 - (a) What is the amount?
 - (b) Can it be a letter of credit?
 - (c) Is there interest on the security deposit?
 - (d) Does the lease provide for the return of the tenant's security deposit within a set number of days after termination of the lease?

18. Guaranty:

- (a) Is a personal guarantee required?
- (b) When does the guarantee terminate?

19. Mortgages:

- (a) Can any mortgages adversely affect the tenant's rights if foreclosed upon?

20. Free rent:

- (a) Will the landlord grant a free rent period?
- (b) When does it have to be returned (e.g., on breach of lease)?

21. Are there any peculiar landlord obligations that should be included?22. Compliance With Law:

- (a) Does landlord warrant that the premises are in compliance with applicable law?
- (b) If tenant is obligated to comply with applicable law, does it exclude matters that should more properly be the responsibility of the landlord (e.g., asbestos problems, disability access)?
- (c) Is landlord obligated to comply with all laws applicable to its control of the building?

23. Insurance:

- (a) What insurance is the tenant required to maintain?
- (b) What insurance is the landlord required to maintain?
- (c) Has the tenant's insurance agent reviewed the insurance requirements in the lease?

24. Rules and Regulations for the Building:

- (a) Are there specific rules and regulations in existence?
- (b) Can the rules be changed without approval of tenant?
- (c) Is the landlord required to enforce the rules and regulations against other tenants?
- (d) Are there any rules that interfere with the expected operations of the tenant?

25. Rights of Entry:

- (a) Exclusive of emergencies, what notice must the landlord give in advance for entry into the tenant's premises?
- (b) Are there any restrictions on landlord interfering with tenant's business in showing the premises to buyers, lenders or prospective tenants?

26. Signage:

- (a) What signage is the tenant allowed to put in or about the building and premises?

27. Parking:

- (a) How many parking spaces will be available to the tenant?
- (b) At what cost?

Form A7**Press Release – New Product****For Immediate Release**

Contact: Richard Anderson
Catchy Software Inc.
Phone: (415)771-8000
Fax: (415) 771-8001
Email: randerson@catchysoftware.com

New Software for Small Businesses

San Francisco, California (November 30, 2012) -- Catchy Software Inc., the makers of the Biz Success™ suite of software products, today introduced Biz LegalAdvisor™, a new software product aimed at giving start-up and emerging businesses high quality forms and legal advice.

Biz LegalAdvisor™ combines a comprehensive package of forms, checklists and agreements with explanations and guides. The product will be of tremendous value to entrepreneurs, business professionals and small businesses.

“This is a cutting edge product far superior to anything in the marketplace,” said Richard Anderson, the President of Catchy Software Inc. “We expect tremendous sales of this product.”

The software provides guidelines and forms for almost any legal matter encountered by small businesses -- from issues relating to employment to stock sales to intellectual property.

More than 900,000 new businesses are started each year. “With Biz LegalAdvisor™, many business owners and entrepreneurs will now be able to avoid legal pitfalls and save thousands of dollars in legal fees,” said Richard Anderson.

Catchy Software Inc. is a San Francisco based software company whose mission is to provide software products to start-up and emerging businesses that are comprehensive, useful

and of high quality. The company has 35 employees and has successfully developed other business software. More information can be obtained by visiting the company's Web site at www.catchysoftware.com.

####

Form A8**SAMPLE FINANCIAL STATEMENTS****Balance Sheet**

As of: _____

Assets	\$	
Current Assets:		
Cash		_____
Marketable Securities		_____
Accounts Receivable (Net)		_____
Total Current Assets		_____
Fixed Assets:		
Property and Equipment		_____
Buildings		_____
Land		_____
Less: Accumulated Dep.		_____
Total Fixed Assets		_____
Other Assets		_____
Total Assets		=====
Liability and Equity		
Liabilities		
Current Liabilities:		
Accounts Payable		_____
Notes Payable		_____
Taxes Payable		_____
Other: _____		_____
Total Current Liabilities		_____
Non-Current Liabilities:		
Long-Term Debt		_____
Other: _____		_____
Total Non-Current Liabilities		_____
Total Liabilities		_____
Equity:		
Stock (Capital)		_____
Retained Earnings		_____
Total Equity		_____
Total Liabilities and Equity		=====

Income Statement

Period of _____ to _____

	\$ _____
Revenues	_____
Sales – Cash	_____
Sales – Credit	_____
Less Returns and Allowances	_____
Net Sales	_____
 Cost of Merchandise Sold	
Beginning Inventory	_____
Purchases (Net)	_____
Direct Labor	_____
Outside Services	_____
Other: _____	_____
Less Ending Inventory	_____
Total Cost of Merchandise	_____
 Gross Profit	_____
 Operating Expenses	_____
Selling Expenses	_____
Advertising	_____
Commissions	_____
Other: _____	_____
Total Selling Expenses	_____
General Expenses	_____
Salary	_____
Insurance	_____
Depreciation	_____
Repairs and Maintenance	_____
Interest	_____
Taxes	_____
Utilities	_____
Other: _____	_____
Total General Expenses	_____
Total Operating Expenses	_____
 Income From Operations	_____
 Other Income	_____
Other Expenses	_____
Income (Loss) Before Income Taxes	_____
Income Taxes (Credits)	_____
 Net Income (Loss)	=====
EBITDA	=====

Statement of Cash Flows

	Current Period	Prior Period	Increase/ (Decrease)	Percent Change
Period Ending:	_____	_____	_____	_____
<u>Cash Flows from Operating Activities</u>	\$ _____	\$ _____		% _____
Net Income	_____	_____	_____	_____
Non-Cash Expenses Included in Net Income	_____	_____	_____	_____
Gain / Loss on Sale of Assets	_____	_____	_____	_____
Depreciation	_____	_____	_____	_____
Net Change in Receivables	_____	_____	_____	_____
Net Change in Payables	_____	_____	_____	_____
Net Change in Inventory	_____	_____	_____	_____
Net Change in Accrued Items	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
_____	_____	_____	_____	_____
<u>Net Cash</u>				
<u>Provided by Operating Activities</u>	\$ _____	\$ _____	\$ _____	\$ _____
<u>Cash Flows from Investing Activities</u>	_____	_____	_____	_____
Purchases of Capital Assets	_____	_____	_____	_____
Sales of Capital Assets	_____	_____	_____	_____
Loans Given	_____	_____	_____	_____
Loan Repayments	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
<u>Net Cash</u>				
<u>Used by Investing Activities</u>	_____	_____	_____	_____
<u>Cash Flows from Financing Activities</u>	_____	_____	_____	_____
Debt Reduction	_____	_____	_____	_____
Short-Term	_____	_____	_____	_____
Non-Current	_____	_____	_____	_____
Dividends	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
<u>Net Cash</u>				
<u>Used by Financing Activities</u>	\$ _____	\$ _____	\$ _____	\$ _____
<u>Net Increase / Decrease in Cash</u>	\$ _____	\$ _____	\$ _____	\$ _____
Schedule of Non-Cash Investing and Financing	_____	_____	_____	_____
Purchases of Capital Assets	_____	_____	_____	_____
Loans on Capital Assets	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
Other: _____	_____	_____	_____	_____
Total Net Change	_____	_____	_____	_____

Form A9**CONFIDENTIALITY AGREEMENT**

This CONFIDENTIALITY AGREEMENT (the "Agreement") is by and between _____, a _____ corporation (hereinafter "Disclosing Party"), and the undersigned (hereinafter "Recipient").

WHEREAS, Recipient has requested information from Disclosing Party in connection with consideration of a possible transaction or relationship between Recipient and Disclosing Party.

WHEREAS, in the course of consideration of the possible transaction or relationship, Disclosing Party may disclose to Recipient confidential, important, and/or proprietary trade secret information concerning Disclosing Party and his/its activities.

THEREFORE, the parties agree to enter into a confidential relationship with respect to the disclosure by Disclosing Party to Recipient of certain information.

1. Definitions. For purposes of this Agreement, "Confidential Information" shall include all information or material that has or could have commercial value or other utility in the business or prospective business of Disclosing Party. Confidential Information also includes all information of which unauthorized disclosure could be detrimental to the interests of Disclosing Party whether or not such information is identified as Confidential Information by Disclosing Party. By example and without limitation, Confidential Information includes, but is not limited to, the Company's Business Plan and plan of operations.

For purposes of this Agreement, the term "Recipient" shall include Recipient, the company he or she represents, and all affiliates, subsidiaries, and related companies of Recipient. For purposes of this Agreement, the term "Representative" shall include Recipient's directors, officers, employees, agents, and financial, legal, and other advisors.

2. Exclusions. Confidential Information does not include information that Recipient can demonstrate: (a) was in Recipient's possession prior to its being furnished to Recipient under the terms of this Agreement, provided the source of that information was not known by Recipient to be bound by a confidentiality agreement with or other continual, legal or fiduciary obligation of confidentiality to Disclosing Party; (b) is now, or hereafter becomes, through no act or failure to act on the part of Recipient, generally known to the public; (c) is rightfully obtained by Recipient from a third party, without breach of any obligation to Disclosing Party; or (d) is independently developed by Recipient without use of or reference to the Confidential Information.

3. Confidentiality. Recipient and its Representatives shall not disclose any of the Confidential Information in any manner whatsoever, except as provided in paragraphs 4 and 5 of this Agreement, and shall hold and maintain the Confidential Information in strictest confidence. Recipient hereby agrees to indemnify Disclosing Party against any and all losses, damages, claims, expenses, and attorneys' fees incurred or suffered by Disclosing Party as a result of a

breach of this Agreement by Recipient or its Representatives.

4. Permitted Disclosures. Recipient may disclose Disclosing Party's Confidential Information to Recipient's responsible Representatives with a bona fide need to know such Confidential Information, but only to the extent necessary to evaluate or carry out a proposed transaction or relationship with Disclosing Party and only if such employees are advised of the confidential nature of such Confidential Information and the terms of this Agreement and are bound by a written agreement or by a legally enforceable code of professional responsibility to protect the confidentiality of such Confidential Information.

5. Required Disclosures. Recipient may disclose Disclosing Party's Confidential Information if and to the extent that such disclosure is required by court order, provided that Recipient provides Disclosing Party a reasonable opportunity to review the disclosure before it is made and to interpose its own objection to the disclosure.

6. Use. Recipient and its Representatives shall use the Confidential Information solely for the purpose of evaluating a possible transaction or relationship with Disclosing Party and shall not in any way use the Confidential Information to the detriment of Disclosing Party. Nothing in this Agreement shall be construed as granting any rights to Recipient, by license or otherwise, to any of Disclosing Party's Confidential Information.

7. Return of Documents. If Recipient does not proceed with the possible transaction with Disclosing Party, Recipient shall notify Disclosing Party of that decision and shall, at that time or at any time upon the request of Disclosing Party for any reason, return to Disclosing Party any and all records, notes, and other written, printed or other tangible materials in its possession pertaining to the Confidential Information immediately on the written request of Disclosing Party. The returning of materials shall not relieve Recipient from compliance with other terms and conditions of this Agreement.

8. No Additional Agreements. Neither the holding of discussions nor the exchange of material or information shall be construed as an obligation of Disclosing Party to enter into any other agreement with Recipient or prohibit Disclosing Party from providing the same or similar information to other parties and entering into agreements with other parties. Disclosing Party reserves the right, in its sole discretion, to reject any and all proposals made by Recipient or its Representatives with regard to a transaction between Recipient and Disclosing Party and to terminate discussions and negotiations with Recipient at any time. Additional agreements of the parties, if any, shall be in writing signed by Disclosing Party and Recipient.

9. Irreparable Harm. Recipient understands and acknowledges that any disclosure or misappropriation of any of the Confidential Information in violation of this Agreement may cause Disclosing Party irreparable harm, the amount of which may be difficult to ascertain, and therefore agrees that

Disclosing Party shall have the right to apply to a court of competent jurisdiction for specific performance and/or an order restraining and enjoining any such further disclosure or breach and for such other relief as Disclosing Party shall deem appropriate. Such right of Disclosing Party is to be in addition to the remedies otherwise available to Disclosing Party at law or in equity. Such right of Disclosing Party is to be in addition to the remedies otherwise available to Disclosing Party at law or in equity. Recipient expressly waives the defense that a remedy in damages will be adequate and any requirement in an action for specific performance or injunction for the posting of a bond by Disclosing Party.

10. Survival. This Agreement shall continue in full force and effect at all times.

11. Successors and Assigns. This Agreement and each party's obligations hereunder shall be binding on the representatives, assigns, and successors of such party and shall inure to the benefit of the assigns and successors of such party; provided, however, that the rights and obligations of Recipient hereunder are not assignable.

12. Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of California, without regard to conflict of law principles.

13. Attorney's Fees. If any action at law or in equity is brought to enforce or interpret the provisions of this Agreement, the prevailing party in such action shall be awarded its reasonable attorneys' fees and costs incurred.

14. Counterparts and Right. This Agreement may be signed in counterparts, which together shall constitute one agreement. The person signing on behalf of Recipient represents that he or she has the right and power to execute this Agreement.

15. Entire Agreement. This Agreement expresses the full and complete understanding of the parties with respect to the subject matter hereof and supersedes all prior or contemporaneous proposals, agreements, representations and understandings, whether written or oral, with respect to the subject matter. This Agreement is not, however, to limit any rights that Disclosing Party may have under trade secret, copyright, patent or other laws that may be available to Disclosing Party. This Agreement may not be amended or modified except in writing signed by each of the parties to the Agreement. This Agreement shall be construed as to its fair meaning and not strictly for or against either party. The headings hereof are descriptive only and not to be construed in interpreting the provisions hereof.

Date: _____

_____. ("Disclosing Party")

By: _____
Title: _____

_____. ("Recipient")

By: _____
Title: _____

Checklist for Issuing Stock

If you are planning to issue stock, there are a number of important steps that should be undertaken, including the following:

1. Board Approval. The Board of Directors of the company should approve the offer and sale of the stock, any agreements for the sale, and the filing of any needed governmental documents. This can be accomplished through resolutions adopted at a Board meeting or by written unanimous consent.
2. Shareholder Approval. Approval of the shareholders may also be necessary, especially if the Articles of Incorporation of the company are being amended. Amendment of the Articles will typically require approval by the holders of the majority of the outstanding shares, either by resolutions adopted at a meeting or by written consent.
3. Review the Company Charter. The company's charter (Articles of Incorporation or Certificate of Incorporation) should be reviewed to ensure that you have enough shares authorized to allow the new issuance.
4. Review Compliance With Securities Laws. Before an offer or sale of stock can be made, you need to ensure that the proper steps have been taken to comply with the federal securities laws and the securities laws of the states where the offers or sales of stock are made. Typically, you will want to find a private placement type of exemption to avoid the costly procedures of conducting a registered offering.
5. Prepare Appropriate Agreements. The sale of the stock should be documented by appropriate agreements. When the transaction is not really negotiated, such as the sale of Common Stock to friends and family, a Subscription Agreement may be appropriate. If the transaction involves venture capitalists or strategic investors, then a more detailed negotiated Stock Purchase Agreement will be necessary.
6. Review How the Sale Will Affect Future Action. The company should review how this stock offering might affect future financings. Ideally, the stock issuance should not unduly restrict the ability of the company to issue additional stock in the future.
7. Price and Number of Shares. The appropriate price for the shares and the number of shares to be issued need to be established. The dilution to the existing shareholders resulting from the new issuance must be reviewed and determined acceptable.

8. Make Securities Law Filings. Make sure to make the required filings with the SEC and any state securities administrators, generally within 15 days of the stock sale.
9. Stock Certificate. After the sale, the company should issue a stock certificate, signed by the appropriately authorized officers of the company. It will be useful to keep a copy of the stock certificate in the company records. Each stock certificate should be dated and numbered. The certificate should include any appropriate legends.
10. Stock Ledger. The issuance of stock should be recorded on the company's Stock Ledger, showing the date issued, consideration paid, name and address of each shareholder, certificate number and other relevant information.