



SPI 231

Attorney Roundtable: Money and Legal Considerations for Starting Out

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- Pat: This is the Smart Passive Income podcast with Pat Flynn, session number 231. Let's go.
- Announcer Welcome to the Smart Passive Income podcast, where it's all about working hard now so you can sit back and reap the benefits later. Now your host. He teaches business to his kids during bath time. Pat Flynn.
- Pat: What's up, everybody? Thank you so much for joining me today. This is a very, very important episode because it has to do with legal things related to your business. I know a lot of this is very scary, and a lot of it is very overwhelming, and I know because I've spoken to a lot of people who because of the legal things that are required or that are out there related to business, they don't get started at all. That's not good because we all have a lot to contribute to this world. We can reward ourselves and others through the businesses that we create. We shouldn't let things like legal things stop us sometimes. Now, of course, we have to play by the rules, which is why I'm very excited because I invited two people on who have helped me with legal things. Of course, I'm not a lawyer, so I just want to get that out of the way, but these two people are, Richard Chapo from socalinternetlawyer.com, and then also Alena Herranen from herranenlaw.com. All the links and resources mentioned in this episode, including links to their websites, will be available at smartpassiveincome.com/session231, which you can check out at the end of the show.
- I actually polled the audience. I sent an email out and asked a lot of you, "Well, what legal things do you have questions about?" so that we can answer as many of them as possible. We didn't get to a lot of them, and there were a lot of people that actually asked a lot of the same questions, so my plan was to initially feature some of your voicemails because some of you did leave voicemail questions about these things and mention your names and stuff, but so many people asked about the same things, we're going to touch on a lot of those things, so I just wanted to credit everybody out there who had asked questions. I was told after the show that Richard and Alena were more than happy to come on on guest posts later on

answering specific questions that you might have. If we don't get to questions that you have about legal things today, you can leave questions at smartpassiveincome.com/session231 or also at askpat.com, and we'll compile those and I'll have them answer those and put them into a round-up blog post of some kind that comes out every few months because this is really important stuff.

I've gotten into legal trouble in the past myself with trademark issues, specifically, but there's a lot of other things out there that can happen, but again, I don't want the legal stuff to stop you and make you feel overwhelmed. That's why I invited Richard and Alena here on the show today. We're going to get right into it, and you'll hear me discuss what these questions are, and I have them answer one by one. Some of the stuff may or may not be relevant to you. I encourage you to, as for some of you this might be boring because it's legal and it's stuff that really isn't as exciting as building products and advertising and building relationships with your audience, but of course, like I said, it's really important. Listen all the way through because at the end, they have some really great advice for those of you who may be feeling overwhelmed with all this stuff. I felt it was really important to compile this information. Here are my US-based, actually California-based, lawyers that have helped me out in certain situations. They're going to talk about their roles right here at the very beginning. Let's get right into it.

Alena: I've been practicing since 1992 as well, so I practice in the areas of for-profit and non-profit businesses. I do contracts, trademarks, and copyrights. Well, I guess that's about it. I don't know what else you want to know about that.

Pat: Well, we'll get into a lot of the stuff that the audience has actually asked about. You know, I've had a lot of questions in the past about legal stuff that I was always a little bit afraid to talk about because I just know that I'm not really qualified to talk about all of this stuff, and there's sort of legal ramifications that can happen when I share things like that. That's why I wanted to bring the experts on, so Richard and Alena, thank you again for coming on. First, let's start with you, Richard. For those just starting out, legal can be

something that can be very scary. Often it stops people from getting started because there just is a lot to think about. What are some good basic sort of getting started things that entrepreneurs should just at least focus on, worry about, in order to get started in the proper way?

Richard:

Sure. I think if you're starting out, you know, obviously the legal issues can be complex. The other factor, quite frankly is the cost. In a perfect world, you know, you'd really want to form a business entity, typically an LLC, that's going to create a hurdle should somebody come after you from a liability perspective, and in addition, buy liability insurance, which is something we can discuss in greater detail later. Those are really the two foundational steps that you want to take. When you have a website and an app, you know, the biggest things that you want are terms and conditions and the privacy policy.

Unfortunately, there are free sets out there floating around on the web. There's all sort of generators, and they're really horrible. You know, I would try to budget in the cost of doing terms and conditions and privacy policies as part of your start-up. The problem is that if you get them wrong, you can really run into serious problems. For example, with privacy policies, most privacy policies that you'll find for free online will contain a statement that says, "We do not share, rent, or sell your personal information to third parties." It sounds like a noble idea. Unfortunately, it absolutely kills your business. One case can really tell us why. This case involved a dating site called true.com. It was a large dating site and it was doing very well. Unfortunately, its parent company had all kinds of problems, and the parent company went bankrupt. True.com was dragged into the bankruptcy estate.

Another dating site called Plenty of Fish tried to buy true.com. They offered \$700,000 for the membership list and for the site. The attorney general of a variety states objected to the sale, and the reason was the privacy policy had that statement that, "We will not sell, share, or rent your personal information." Well, the sale of a website is the sale of personal information. When you have those

types of clauses in your privacy policies, you know, you're really killing your exit strategy from your business.

With terms and conditions, you know, I think at this point everybody know who Zappos is. A very large retailer, sold for a huge amount of money to amazon.com. A few years back, they had a data issue where they were hacked, basically, and the customer information was collected. The terms and conditions contained a clause saying, "We reserve the right to update these terms and conditions whenever we want, and if you continue to use the site, you agree to this update." As Alena and any other lawyer would tell you, the problem with that is it's an unconscionable clause. It's just completely one-sided. It doesn't require any notice or acceptance by the user of the site. It's an invalid contract, and that's what the court ruled. The terms and conditions for Zappos were thrown out.

Those terms and conditions would have saved them a significant amount of money. They probably would have settled the dispute for \$100,000, which seconds like a lot, but for a company of that size, is nothing. Instead, they're facing upwards of, oh, I don't know, \$30 or \$40 million in settlements. Spending money on those two documents is something you really want to do if possible.

Pat: Terms and conditions and privacy policy were those two things.

Richard: Yeah.

Pat: Okay.

Richard: Right. They're legalese. If you think of your health insurance or your car insurance, you know, I'm an attorney. I buy car insurance. I never read the contract. That contract is written as in favor of the insurance company as possible. That's really the way your terms and your privacy policy should be written as well. They're there to protect you. Everybody, you know, most business owners look at them as an annoyance, but they're ammunition in your boat; they help you. Plan on spending money there.

Another area where we see big problems that should be part of any website is if you allow visitors to your site to upload anything, images, music, text, comply with the digital millennium copyright act, better known as the visitors. It's a controversial law, but for website owners and app owners, it is a beautiful law because it does this. If you comply with it, you cannot be found liable for copyright infringement based on content uploaded by your users. If you think about Facebook, somebody uploads a cartoon or a video or a song or anything of that sort that is copyrighted, Facebook cannot be found liable for that copyright infringement; only the user can. It really protects you. Complying with the visitors costs a couple hundred bucks. It's definitely something that anybody starting out wants to do.

In this day and age, you know, most sites are going to have some kind of interactivity, so do it, please do it.

Pat: How would one-

Richard: Think how many people-

Pat: How would one comply with the visitors? What does that mean exactly?

Richard: Well, you can contact an attorney to go through it, or frankly, there's a book on Amazon for sale called "The visitors Handbook," and most people can read that. It's written by an attorney in Arizona. She went through and detailed the whole process. It makes sense to me as an attorney. If it's a bit confusing to me, you can consult with any attorney. It would take less than an hour. Frankly, the biggest expense is really designating an agent. You have to register and designate an agent with the copyright office. The United States Copyright Office. It costs \$140. They have one clerk that handles all the designations for filings from around the world, so it's a little annoying. It's a fairly simple process. Basically, if a complaint comes in, you have to take down the content in question. Then the person who posted the content has the right to counter-notice, basically saying, "No, it's not infringement." Then at that point, you alert the

person who made the original complaint.

Then those two parties go have at it in court, but you are not dragged into court. This is how Twitter, Facebook, Instagram, all of these sites and services avoid being pushed into bankruptcy by millions of copyright infringement lawsuits.

Pat: Okay. The visitors, that sounds familiar to me because I know that that's something that you have to deal with if you see some of your own content that you've written or maybe one of your own books or an image that you created yourself on somebody else's site. Alena, before we get to you, Richard, can you speak on that a little bit? If you see some of your own content on somebody else's site, I know DMCA has something to do with that. What steps should you take to hopefully get that taken down?

Richard: Right, so typically, if you put it up on the web, it's going to be stolen at some point, whether it's scraped by a bot or some other source. You will find them in other places. Typically, at that point, the DMCA ... What the DMCA's purpose was essentially to avoid flooding the courts across the US with endless copyright infringement lawsuits, so it creates an informal process for getting content taken down.

The way to do it is you use something called a visitors takedown notice. What you would do is, let's say that I run a copy scrape search and I find somebody's copied one of my blog posts to another blog. I would contact that blog probably informally first and just say, "What's going on? Take this down." If I don't get any response, which typically I wouldn't, I would then identify who the host is. You would do that by going to the WHOIS record and look at their host. Then you would go to the host's website, and they will have a copyright or abuse or DMCA link somewhere in the bottom of the site.

Then you click that, and then you would submit the form. There are various elements that you have to declare, so you would have to provide the domain for the original content on your blog, the domain for the blog that's stealing your content, and then a

statement under penalty of perjury basically that you created the work and that you own it. At that point, the host will take down the content in question. It's not a situation where they review it and think about it or try to evaluate whether it's infringement. They automatically take it down. In 99% of cases, that's the end of it. The other side can file a counter-notice, but if they copied your content, they're never going to.

Pat: Right. I've run across that on YouTube before. Somebody swiped my YouTube video and uploaded it onto their own channel. YouTube has a really good method of reporting that. They're typically pretty fast at taking those things down. That's good. That's actually going to be really helpful for a lot of people because I know that's one of the biggest complaints that people have, is all this hard work.

Richard: One other things I would just mention, so business model, a black hat business model ... Black hat is doing things that are unethical or violates regulations for various sites. One black hat strategy is you send bots out to copy content off of various sites, and then you publish them on a new site, and that site is hosted offshore. Well, the DMCA is only a law in the United States. If you start trying to serve notices to somebody in Amsterdam or someplace of that sort, they're often going to ignore it.

In that situation, what you want to do is go to Google, Bing, and Yahoo and anywhere where you can see traffic being sourced. It's typically going to be the search engines. You can file a DMCA takedown notices with them as well. They will de-list the site. In that situation, obviously, you get rid of most of the traffic. You also get rid of duplicate content penalties, things of that sort. If affiliate programs are being promoted with your content, you can contact those programs as well. They'll often terminate the person.

Pat: Great. Thank you, Richard. Alena, let's move onto you. Let's talk a little bit about business structure. Richard mentioned a little bit about LLC versus S-corp and all that stuff. Can you help us define which one is best for who? Even going further, I know there are some companies including my own that have sort of an umbrella

company and then use either DBAs or doing business as or other elements to kind of have different businesses under one umbrella business. Can you speak a little bit about where does one start even with how to determine what business structure is right? We know that we should create a business for protection and so it's separate from ourselves, of course, but where do you even start with that, Alena?

Alena:

Well, the simplest and cheapest possible business structure would be the sole proprietorship, of course, where you basically just get a business license, and you can start operating. That's nice because it is cheap and it's easy. It doesn't give you the liability protection at all. Likewise with a partnership. A partnership is worse than a full proprietorship because then you're liable not only for the errors that you make but also for those of your partner. To get the liability protection, you want to set up a formal corporation or LLC which gives you limited liability. Basically, they're pretty similar except that corporations ... Well, corporations are owned by shareholders just for terminology purposes. Corporations are owned by shareholders, and they're managed by officers. Then they have a board of directors who control the officers. Then LLCs are owned by members, which is basically the equivalent of shareholders, and they're managed by either the members or by managers. Just the organizational structure is a little bit different.

Liability wise, they both give you limited liability. Tax wise, the corporation, if you don't make the S election, you will be subject to double tax. That means that the corporation pays tax on its profit, and then when it distributes dividends to its shareholders, the shareholders pay tax on the dividends, so that's called a double tax. If you make the S election, then you can be treated for tax purposes as a pass-through entity, which means you don't pay the tax at the corporate level; you're just paying tax at the shareholder level. You do, with all 3, the corporation, S corporation, and LLC, you do have to pay an \$800 minimum franchise tax, but you can avoid some of the other taxes.

One of the things that you can do, so with a corporation, some

people find it helpful tax wise to pay themselves sort of a slightly lower than normal salary and not have to pay employment taxes on the rest of the profit of the corporation. You can do that with an S corporation because like I said, the S corporation has pass-through tax treatment. Anything that you pay yourself as a salary, you are subject to self-employment taxes, but whatever you pay yourself as a dividend is not. Now, this isn't something that should be abused, of course, because the IRS does look to see if you're paying yourself a reasonable wage, and they can go back and deem some of your dividends as wages and charge you back taxes and penalties, so you do have to be careful. Some people have found that to be a way to save on employment taxes as well.

Pat: Would you recommend even before selecting sort of a business structure to connect with a financial person to help walk you through which one might be the best for you depending on what kind of business you have?

Alena: You should always have a conversation with your accountant, that's for sure. It's not really a terribly complicated decision. If you call an attorney, they're going to be able to suggest to you which form of the entity might work best for you, whether it's a corporation or S corporation or an LLC.

Pat: Okay. Now let's say you have a business, an LLC, that you've created, and then under that LLC, you have sort of another idea for something that could be ... You know, another sort of kind of business, I guess you could say, or a sub-business, if you will. What would you recommend in terms of dealing with that? Would you recommend creating a whole completely different entity for that second thing? Because us entrepreneurs, we have a ton of different ideas. I think a lot of people know this from watching what I do and all of the different projects that I have a hand in. Would you recommend having an umbrella company to manage all that, or separate companies, or does it kind of depend?

Alena: It depends for sure. Again, if you wanted to go the most economical route, what you could do is just have one LLC and then own several

DBAs or fictitious business names as they're called. Then you can set up separate accounting for each of those different DBAs on your own record so that you can track which one is making profit and which one's not. They really are just part of the same LLC. Now, the disadvantage with that is that each business unit is a risk and also suffers exposure from the other business units. If one of your business units has a potential for higher liability, then you might want to protect the other ones from that one. The way you can do that is set up separate LLCs for each one because then they're protected from each other.

When I'm saying "limited liability," that means that if the entity were sued, the assets that would be subject to that lawsuit would be only the assets of the LLC and not those of the owner's or the other sister companies. You can definitely reduce your liability to each of the business units by setting up separate entities. Now, you do have to take into consideration the cost because there is a cost with setting up the entity and maintaining it. You have to have separate tax returns. You pay your \$800 minimum franchise tax, even if you're not making a profit, for each of those. You know, of course you have a little bit of legal expenses as well with each of the entities on an annual basis.

Pat: The \$800 franchise tax you were talking about, that's-

Richard: Sorry to step in.

Pat: Oh, go ahead.

Richard: That \$800 expense is really only California.

Alena: That's California, yeah, sorry.

Pat: Which actually brings up a great question. Richard or Alena, I don't know who wants to speak to this. It just came up. A lot of people when they're starting businesses, they hear that, "Oh, Delaware is where you should start a business because they are more favorable towards businesses, and there's no taxes," or Oregon or

Washington, not California even though you might live in California. How do you determine where you should be starting a business, or is that strategy of setting up an LLC in a different state even worthwhile considering? Maybe Richard, you can speak to that?

Richard: Oh, I don't know if Alena and I would have the same opinion about this. I'm not in favor of it typically.

Alena: I can help you with this. I'd be happy to comment on that ...

Pat: Oh, thanks.

Alena: ... if you would like. Yeah, because I get that question a lot. People want to set up a Nevada corporation because there's no corporate or income taxes in Nevada, but the problem is when you are located in California, you're subject to all of the California laws anyway. If you are living here, you're working here, maybe you have employees here and you don't live or work or have employees or office in Nevada, then it doesn't work. It doesn't really work for you. What happens is if you're a foreign corporation, say you're incorporated in Nevada, you have to qualify ... It's called "qualifying" in California. It's basically the same steps as you would have to take if you were to incorporate in California. You're subject to all the same filings, all the same disclosures, and basically what happens is you're just duplicating your expenses because not only have you paid to set up your entity in Nevada, but now you're also having to pay for all the standard California fees. None of the fees are less, either, just because you're a foreign corporation.

Pat: I see.

Alena: That part doesn't really help you. Now, the way it can help you is if you actually moved to Nevada and set up your business there and work there and have your employees there.

Pat: Ah, which I don't think I'll ever do.

Alena: I have several clients that have done that. They were California

entities, they moved to Nevada, they're happily working there, and they're not paying their corporate or income taxes because there aren't any, but they're no longer California residents.

Richard: Yeah, but all the savings are burnt up by running the air conditioner 24/7.

Alena: Yeah.

Richard: I would just throw in a couple things on that. You know, one of the things about Delaware is popular, there is one instance where I would think forming in Delaware makes sense. That is if your intent is to become a publicly-traded company or to attract venture capital. In that situation, you're really restricted to a corporation, and they want to see a Delaware formation because the classification of shares can be done and situated; it's very favorable to the investor. If that's your goal, and realistic, not something you just came up with, but something you have a business plan, you have an idea, you've really laid it out, then Delaware is somewhere that you want to incorporate for that purpose because I think that it's ...

If you form in California, you can probably still get funding, but there's going to be less interest. If you're an LLC, there's going to be no interest. Well, not no, but very little interest. They want to see that Delaware corp. They're comfortable with it. When I say "them," I'm talking about venture capitalists. They're comfortable with it, and so that's really your only choice. Of course, you really don't care because if you get venture capital, you know, you have money; you can develop a business in San Juan.

Pat: Right, right.

Richard: The second thing about states is although Alena and I are both in California, the states have really taken the revolutionary view as to where you incorporate. What caused it was the sales tax on the internet. There's been an effort to come up with a national sales tax since about, I don't know, 2000, and it's failed miserably because you'd just have to look to Washington, DC to see how many

conflicts we have in our politics. States can't get their act together. They can't agree on one form of sales tax. They can't even agree on the form. It's never really happened.

What has occurred is it's triggered the attention if you will of the tax agencies in the states. Before, in 1980, people had formed Nevada LLCs or Nevada corporations all the time. Let's say people in California would do that. Then they would run their business through Nevada corporations. The tax agency in California, the Franchise Tax Board, wasn't all that aggressive about going after them. With the internet and the changes in tax revenues that are earned from purchases, I mean, just consider I myself am a slave to Amazon. I buy practically everything on Amazon. California doesn't ... Well, now it does get some sales tax from that, but until recently, California lost all of that sales tax revenue because they don't go down to the local store, they don't go down to Home Depot or whatever to buy those purchases. The tax agencies now are much more awake to the idea of this national business and people putting businesses in states that have favorable taxes, and they will now aggressively hunt those areas.

California has, you know, the Franchise Tax Board is known to have investigators. All they do is go down the corporate rolls and try to figure out if these are really California businesses and challenge them. Other states do it as well, New York, Illinois, and you're seeing this kind of development. If you are going to form an entity in a tax-favorable area such as Nevada, I agree completely with Alena, you definitely want to talk to your CPA, and you want to talk to an attorney to make sure it makes sense because in most situations, you're going to have to qualify in your own state, which means you're just paying more fees for no particular reason.

Some of the taxes that Nevada and Delaware these people will tell you is they'll tell you your information is confidential and that you'll never know ... Nobody will ever be able to discover who's a shareholder. I can go pay a private investigator 500 bucks, and I can find the shareholder of every Nevada corporation in a day. You know, most of that stuff is marketing. Unless there's a really viable

reason to look at these other areas, you know, I'd be very careful about incurring an expense.

Pat: Okay, cool. Thanks, guys, I appreciate that. Alena, let's move onto you. I have a question now that we're talking about setting up a business. Let's talk about trademarks, and so we set up a business. We have a name. When should we even start thinking about that, or should we already start thinking about that right away, you know, in terms of trademarking our business name and then even down the road when we create products of our own? Should we be trademarking those as well? Can you speak to that, please?

Alena: In the ideal world, it would be nice to have your trademark application filed before you make the public aware of it, but that's not always realistic. I know that with internet businesses, it's an important, it's really important, your domain name if you're using it as a trademark, registered as a trademark early on because that's probably the main source of your value. I mean, obviously, if someone's going to use a similar name, they could divert traffic away from yours, and so forth, and so that's really important.

There are ways to save, though. Trademarks can be expensive. I mean, just the filing fees with the United States Patent and Trademark office are \$225, but you can imagine that when you have several, and a lot of businesses do, that that can add up. When you're starting a business, that can be a bit of a cash crunch for people.

Pat: Totally.

Alena: There are ways to minimize how much you're spending up-front but still getting some protection. For example, say you have a trademark, a wordmark, and a logo and a slogan ... Or actually, just go with the wordmark and the logo. What you could do is save the logo for later if that's not the most important part of your trademark, which it probably wouldn't be if it's an internet-based business. Then use just the words. Register just the words for now. Then later as cash flows better, you can add on other features that you want to protect.

Pat: Now, I know most people don't actually even do the trademark, and I have heard a lot of people rely on this thing called the fair use or first use, and it's, I believe, if you're the first one to actually come up with that name and use it, then you have some legal stance on it and ownership. Is that even true? Obviously, trademarking would be the best thing, but is there a first use kind of thing that exists?

Alena: There is some truth to that. Okay, from the person who's registered the trademark, from this person's perspective, we don't like that because you can go and register your trademark, but then you find out somebody else has started using it before you. You don't get to stop them from using it, even if it's for a similar class of goods and services, but you can stop them from expanding their usage.

From the person who's trying to economize and doesn't want to register a trademark, that's what you have to keep in mind is that you get your first use, and then someone who comes later with a registered trademark can't necessarily stop you, but you can't really grow your business or expand it to other products or other services or other states when someone else has a registered trademark. Really, what you want to do is go ahead and get that registered trademark, and then you know going forward you're protected.

Pat: I see. How long does it take for a trademark to usually get finished after you start the process?

Alena: Once you file, it can take 9-12 months, but I actually have been seeing them come through a lot quicker lately. I had one that just came through after only 5 months, so that was really impressive. The trademark office is actually probably one of the best-functioning government offices that we have in this country because they're just always improving their procedures, and they're getting faster, and the prices have even come down.

Pat: Well, that's good. I mean, that's great, but 5 months, 6 months, a year is a lot of time. Would you recommend for people who have like a business idea right now, it's better to get started right away, right? To go out there and put content into the world, to build

authority, to build your brand, get that domain name and all that sort of stuff. You're not saying to delay 6 months to get the trademark first, right?

Alena: No, no. No, not at all. When I say to take action right away, what I'm really saying is you file your application. The first one to file has priority.

Pat: Okay.

Alena: Even if it hasn't yet registered.

Pat: Got it, okay. Awesome.

Alena: You know, you're on the road to getting protection by the time you've filed the application, which can be done that day. It does take about 5 ... Like I said, a minimum of 5 months at this time, for the mark to actually register and for you to get a certificate of registration, but you're good to go for initially at least once you file.

Pat: Great, okay, that's good to know. Then for products that we create, should we be trademarking them, or like how do we protect the name of our online course, for example, and book even? Can you even do that with a book?

Alena: Books, you would generally want to get a copyright on them, but if you have, say, like I think Richard mentioned the Dummy series earlier ... Or that may be before we had ... before this call.

Pat: Yeah, that was pre-recording.

Alena: Anyway, so the Dummy series, they have a trademark because it's a whole series of books all under the name the dummy, the Dummies, whatever, book for algebra or something. That's a trademark and it's also copyrighted, but copyright protects the content, and then the trademark protects the brand name.

Pat: Got it. Okay. Then your products and all those kinds of things, I mean, is it ... Generally, I guess, it's a rule if you really wanted it to

be protected, you'd go ahead and trademark or copyright it, right?

Alena: Yes. Then you don't want to go overboard because there are expenses associated with trademark maintenance. Between the fifth and sixth year after you register a trademark, you have to do another statement showing that you're continuing to use the mark. Then at the 10-year point, you have to file another statement. Then after that, it's every 10 years. That can be burdensome. I've seen that happen with clients where they would get 5 or 10 trademarks, and then they get to the 5- to 6-year point. Maybe things aren't looking so good business-wise and they say, "Well, maybe we don't need all these trademarks." They start whittling them down. You do have to be careful, but yes, you can register a trademark on, say, like a menu item or any specific service that you might have or product that you might have. Generally, the business name isn't necessarily a trademark, but usually it turns out to be.

You know, domain names, again, they're not necessarily a trademark, but they can be if you're using it as a trademark. I can explain that further to anyone who's interested in talking about that. It's a little bit of an art on defining when it's being used as a trademark. Not everybody understands that right off.

Pat: Yeah, we could save that for further conversation, Alena.

Alena: Yeah.

Pat: Thank you for that. Now, Richard, let's talk a little bit about using content that other people have used. I know it's okay to, for example, use certain images or quotes or certain blocks of text that other people have shared or even music on your own site. What protections should we have, or how do we know that we're doing this in the right way that's not going to, you know, have somebody coming after us?

Richard: Well, if you're talking about copyright, copyright is probably the most common legal dispute that you see online. Copyright, generally, is simply the right to copy, perform, something that

you create. When you talk about it in a vacuum, it can be difficult to understand, but I think if you're talking about when using an example, you know, it can be helpful. Let's consider a Stephen King book. You know, it's 300 pages of text.

There, that text, is copyrighted automatically when you creates it, for purposes of this discussion. When you're looking at content online, be it pictures, songs, text, or whatever, you should assume that it is copyrighted and that you can only use it, then, if you have the permission of the person who owns that copyright, typically the person who created it. In the instance of a Stephen King book, he's created it, he owns the copyright, he signs an agreement with the publisher. The publisher is then given the right to copy and distribute and sell, obviously, that book in exchange for royalties paid to King. That's the basic concept of copyright.

Now, there are situations where you can use it without consent or where consent is given to you either automatically or semi-automatically. When you're looking for images and songs and things of that sort online, one of the best places to look is Creative Commons. Creative Commons has a licensing system set up. The web is a unique business environment because in brick and mortar business, most businesses would not share their intellectual property freely. They would charge for it.

On the web, people share things right and left, open source software being a perfect example. With the Creative Commons situation, you can go in there and you can find content. Maybe it's images, maybe it's songs, whatever it is, that already have licenses attached. As long as you read and comply with the license, you're fine. Now, that compliance may involve listing who, you know, the person who's created it and what have you. That's probably the best free way to do it.

Just going out and finding something that you like and copying it and republishing it is almost always going to be infringement because you don't have permission because there's no consent there. If you go to Google. You know, Google's the famous case.

Google's a search engine. They have an image search engine. If you just go in there and start copying things and republishing them, you're infringing. If you're really lucky, you'll get something that Getty Images is in control of, and they'll send you a nasty letter demanding \$5,000 to settle the infringement case.

You don't want to do that. You don't want to copy off of Facebook or copy off of news sites or anything of that sort. You really want to just think it through. You know, the best option and the safest option is either Creative Commons or to actually purchase the content. You know, I have a blog. I have a couple sites. I post images on them. I get them all from Fotolia, which is F-O-T-O-L-I-A.com. They're really cheap. They have images. There are a number of stock image sites out there that you can use. If you use those, you never have a concern.

Then there are practical legal defenses to it. One would be public domain. If something's in the public domain ... Just because it's published on the internet does not mean it's in the public domain. Public domain refers to something where the copyright has expired. That's typically after 70 years after it's created, or 70 years after the person that created it died. It depends on the exact measurement. Basically, if you were trying to use anything that was created after the 1930s, public domain doesn't really count.

The other issue that you get into is fair use. Fair use is a difficult legal concept to explain because it's decided on a case-by-case basis. There isn't really ... There are some general standards you can lean on, but there are 4 factors that a court will look at. They'll weigh those factors differently. In 1985, there was a Supreme Court case that said basically, "We have these 4 factors, but really the biggest, most important thing is your use of that copyrighted content going to cost the original copyright owner money." For instance, if I took the Stephen King book and I made exact copies, I made my own fake cover, and I started selling it on Amazon, that would be costing him money because people would buy the alternative book. In that case, fair use would not apply.

Then the argument was that if you had a situation where you weren't going to cost that person money, then you were much more likely to be found to have a fair use defense. Unfortunately, the Supreme Court has kind of changed that in the last 10 years. Now they look at the 4 different elements, which are basically the purpose and character of the use, are you using it commercially, are you using it for educational purposes or non-profit, you know, the nature of the copyrighted work, a whole bunch of legal standards that people really aren't all that interested in. As a default, I would buy stuff. I wouldn't really rely on fair use unless it's an obvious situation such as criticism, like a movie review. If you're using it for news. Something of that sort. In most situations, you're probably okay. As a default, I just, I myself, I either grab it from Creative Commons, or I just purchase it. It's pretty cheap to do these days. That way, you're never really worried about anything coming back to haunt you.

If you do use a copyrighted image or content of some sort, the good news is, again, we return to the DMCA. Well, you might get a cease and desist letter from an attorney. The typical first thing that you're going to get is actually a DMCA takedown notice. Your host or somebody is going to contact you saying, "We received this notice that you're infringing on somebody," and if you take that content down, often you're fine. I wouldn't rely on that completely, but in the practical real world situation, that's typically what's going to happen.

Pat: What about images that you take yourself of things that you might be reviewing? Maybe you're shooting a video of something that you're doing a review on that you're going to put on YouTube, or you have a blog post that has images of a particular product that you're showcasing? Is that okay to do, or do you still need permission from that product owner to use those images?

Richard: My view is if it's a review, then it's okay as long as you're using ... you're being brief about it. I mean, if you're taking a picture of the product's cover, then you're probably okay. I wouldn't worry about that too much. If you're copying huge swaths of whatever it is, it

becomes much more questionable. If it's a review, if it's criticism or commentary on it where you're not doing it for the purpose of reselling it, essentially, or using it to make a profit, then you're probably going to be fine. If you think of any news story, if a news story reports on some element of a corporate report or something of that sort, they're fine. We've all seen the millions of movie reviews on YouTube; those are all fine because they're commentary. The question is really what's your motivation.

It comes down to the fair use defense, and there are two problems with the fair use defense. The first is it's a defense, which means it's really only resolved, typically, at a trial. Even if you win on the fair use defense, you've spent 50 grand in legal fees or more defending the case. Have you really won? Perhaps. Then the second problem is the more you read about fair use and the more you see the decisions come down, the more courts are kind of all over the place. They literally look at it on a case by case basis. One legal commentator I read recently in a fair use case I was looking at even suggested the judge should just decide if it's fair use or not and then come up with a theory as to why he thinks that. It's difficult.

For instance, there are 4 factors. Well, what if the judge finds 2 of the factors are violated and 2 of the factors are in your favor? Then you essentially have a tie, so how do you decide the case? Unless it's an obvious situation where it's commentary ... The other obvious situation is parody. For instance, if you really want to read an abomination or you're having problems sleeping, go read the Apple iTunes terms and conditions. It's 56 pages. I'm currently creating an article for one of my sites where I go through it and I do the plain English interpretation of the various clauses with hopefully a humorous twist to them. That'll be a parody.

Now, I can guarantee you Apple's attorneys will probably send me a cease and desist letter, and I'll send them back a thing saying it's parody; go pound sand. Off we'll go. In that situation, it's making fun of it. If you see College Humor's videos on YouTube and they cite something that would otherwise be copyrighted, it's a parody. Any of the late night shows, Stephen Colbert doing the takeoff of the

Hunger Games, it's a parody. In those situations, you're fine as well.

There are other classifications, the education exemptions and things of that sort, but they're really rarely invoked. I can't imagine most of your listeners would actually use those.

Pat: Now, what if you are doing something like a review but it's with an affiliate link? Can you talk a little bit about the affiliate relationships and kind of the things that we have to worry about?

Richard: The affiliate relationship, in that sense, you need to disclose basically is the biggest issue right now. This is kind of a hot topic with the FTC. The FTC is looking at ... They want to make sure that people, when they go to a site or they go to a video or whatever, and they see a review or there see something that's ... they know if there's any bias. You know, PewDiePie, the gamer on YouTube, he recently ran into this ... Not so much him, but he and other gamers that are popular on YouTube were being paid money by one of the gaming companies. It was disclosed, but it was disclosed far down in the description under the videos where people might or might not have seen it. The FTC went after the gaming company and forced them to change those kinds of situations. You're going to see a lot of that kind of approach.

In fact, if you go to Smart Passive Income and you look at the resource page, if I remember correctly, there's a big paragraph explaining that these are affiliate links and what have you.

Pat: Yeah.

Richard: In relation to the copyright issue, the affiliate links, you know, depend. If the review is of the product and it's generally positive, your affiliate agreement with that company typically is going to have a clause that allows you to use that content. There's a license there that will allow you to do it. If you're negative, it kind of depends on what the terms say. Non-disparagement clauses can be included in the terms, and what a non-disparagement clause is is basically you can't criticize us or our products, and those are generally not found

to be particularly binding because otherwise people will use them ... There's a case called ClearGear. ClearGear, it was a website that sold various products, and their terms and conditions contained a non-disparagement clause that said you cannot leave a negative Yelp review regarding the company, and if you did, you agreed to pay a penalty of \$3,500.

Pat: What?

Richard: A couple had a bad experience with the company, and actually, if you look at their Yelp reviews, a lot of people did. They complained, and they published something actually on ripoffreport.com saying this is a ripoff. The company sent them a notice for the \$3,500 penalty. They didn't pay it. The company reported it to the credit agency damaging their credit rating. They sued in court. The judge found it was an unconscionable clause and adhesion contract and awarded \$300,000 to the couple against the company. Disparagement clauses aren't great, but you're rarely going to see those anymore.

Typically, if you have an affiliate link, as long as you're being clear that it is an affiliate link and that you're being compensated, typically you're going to be fine.

Pat: Okay. Cool. Alena, I have a question that comes from a listener here. On a similarly related note, you know, when it comes to employees and a lot of people who are expanding their businesses, they're hiring people and sometimes those people are coming on as employees, and sometimes they're coming on as contractors. Which one is better? How do we know what actually makes sense for our business?

Alena: Well, companies generally like to have independent contractors because they don't have to pay employment taxes and provide benefits, but there's a balancing test to determine if it really is an independent contractor or an employee. Basically, it's an employee if you control what will be done and how it will be done, and it's an independent contractor if you control only the result of the work,

not what will be done and how it will be done. It's a little bit of a control test.

Pat: Interesting.

Alena: You know, some clues are, does the person, the independent contractor or employee, have other customers or clients too, or do they only work for your company? Do they use their own supplies and materials and tools to perform the work? Do they work when they want to, or do they have to work during certain hours? Do they have to work at your business location, or can they work wherever they want? Does the person have their own business license? Does the person have their own corporation or LLC through which they're working?

Basically, it's really kind of a control test, and you should talk to an accountant to go over the details with them and just be careful because if you classify them as an independent contractor and you don't withhold payroll taxes and then they're later deemed to be an employee, you'll have a big problem.

Pat: Awesome. Thanks, Alena.

Alena: Mm-hmm (affirmative).

Pat: Richard, when we are ... This is a big question I get. When we interview somebody for a podcast, do we need a release form from them in order to use their audio files for our podcast?

Richard: Yes.

Pat: Now, does that form need to be a hand-written PDF or whatever that's sent back, or can that just simply be an agreement over an email?

Richard: Hmm, well, as an attorney, I would definitely prefer it be an actual written agreement.

Pat: So better safe than sorry you're saying for that?

Richard: Yeah, the concern is really this. You need to lay down the specifics regarding the usage of the files. For instance, let's say that you do podcasts over a number of years and you identify 10 really great podcasts that went well and you want to create a collective, it sounds strange, but a CD or something of that sort to sell it on Amazon. Well, when that person agreed to be on the podcast, did they agree to also let you use their information on that CD? What about payment? What about copyright issues or right of publicity? Publicity is an antiquated idea, but it's gaining new life in law.

Right publicity basically says is that you have the right to control your image, your name, things of that sort. It's kind of being hacked out on social media right now where you have people's images being used when they don't consent, couples breaking up, things of that sort. It gets nasty. The law's not really settled in that area, but it is becoming a bigger issue. Generally, yeah, you do want that, and that's the best way to go.

As far as email, it's better than nothing. In some cases, it's fine, but the problem is the email message typically ... Well, the email message would typically be used in court to show a party admission by the other side that they allowed this to happen. The question is whether that goes far enough, so again, if you were to compile a, let's take blog posts. Say you do a bunch of interviews. I know you do interviews with different people and you were posting them on Smart Passive Income for a while. I don't know if you still do it, but when you were doing those and you wanted to create a compilation, an ebook, with all these different interviews, it's unlikely in an email exchange that you would have addressed that issue. Now, you could come back later and address that with the guests. Most of the guests would probably agree.

A far better way to do it so you can keep everything organized is just to have a template form that covers these issues. You know, when the podcasts or blog posts or interviews or whatever it is is first addressed, and then you have a record of all that stuff and

you are in good shape. Even then sometimes I tell clients, “Well, go back and make sure that the person understands,” because if you interviewed them 5 years and then suddenly there’s a book out and they’re interview number one in the book, you know, they may not recall, and so they get unhappy and what have you. Yeah, generally, releases are a definite.

Pat: Okay. Do you know of a good place where one could get a release like that, or are there any templates available?

Richard: Let me tell you about the law, so Richard Chapo. Attorney lawyer should be able to put one together for you in a half hour. Some of them will already have them. I do. I haven’t really thought about what I would charge for them. I just use them with my current clients. I would definitely have somebody actually draft it for you. This wouldn’t be a LegalZoom or that kind of a thing. They’re not going to cover the various issues, but it should be a minimum cost, maybe 100 bucks.

Pat: Okay. Then here is a question that is actually a really good question. Let’s say you are a person who’s talking about health and fitness, or maybe someone who is creating recipes for people who are in paleo or crossfit or whatever. Can a disclaimer, just a written disclaimer, that says, “Hey, I’m not a health professional. These suggestions are based on my own opinions, research, and personal experiences. They are not designed to diagnose, treat, or cure any health conditions. Please consult your doctor before drastically changing your diet,” like that sort of stuff. Does that have any legal ... Like, can that hold up in court? Does that form any sort of protection for you, or no?

Richard: It helps. The internet is a little bit different than the warning you see on your mattress when you buy a new mattress. The problem with the web is that they want to see acceptance. When internet law first developed, most of the judges were 60 or 70 years old and couldn’t set up their own email. They weren’t familiar with the workings of the web. Now they are. The problem is that unless you can show

some kind of an affirmative acceptance by the people who are viewing that disclaimer, it's not going to be an absolute defense. If you go to certain websites and you want to purchase something or you want to rent something, you want to become a member, they force you to check a box that says, "I agree to the terms and conditions and the privacy policy." What you also see now is people adding disclaimer to that, "... and the disclaimer of the site."

At that point, that's an affirmative evidence that somebody has accepted the disclaimer; they've recognized that, and they're essentially agreeing to it. In that situation, it's really going to help you, and it can be an absolute defense depending on the judge's attitude. It also depends on the nature of the disclaimer. If you're doing a weight loss product or a weight loss site and you put up an image of a woman who weighs 300 pounds and then the next image is she's super thin, looks like a super model and you say she lost 72 pounds in 1 week, no disclaimer is going to save you. That's just a lie. The FTC is going to come after you for what they call deceptive marketing practices, and in court, you're going to get fraud claims and things of that sort. Disclaimer isn't worth anything.

In most cases, I would say absolutely include a disclaimer. It doesn't hurt. It's something that you can leverage in court, and if nothing else, you can put it up on an exhibit board in front of the jury and say, "We had this disclaimer," and it should be enforced and what have you. The problem is the FTC is really hot and bothered in this area, and they've started issuing what are called dot-com disclosure documents. I believe I sent you one. You probably fell asleep after the second page. They want disclaimers to actually be placed directly next to whatever product or service the disclaimer applies to.

Say you're an affiliate and you're selling a bottle of weight loss pills, they would want the disclaimer placed right next to it before they'll consider it binding. Courts are going to look at that, and that's going to be very persuasive to a lot of judges because most people are going to have the disclaimer down on a link in the footer of the site, or in the terms and conditions. In those situations, the chance of the

disclaimer getting you out of trouble is not going to be great. It's kind of an evolving area of the law.

The problem with the FTC is the FTC has never run a business. Those people have never run a business, and so they require things that are just absurd. You and I have had this discussion. Social media, if you have Kim Kardashian ... Or what was it? Selena Gomez, I think. She gets \$500,000 per Instagram post, sponsored post?

Pat: Yeah.

Richard: If she does a tweet or something of that sort and she's being paid for it, the FTC wants her to put a disclaimer in the tweet. Well, the tweet's only 140 characters long, so how are you going to do that? They come up with these bureaucratic rules about, "Well, you can link to a page that would have the disclaimer," which nobody is going to do. Nobody does. The disclaimer area is a bit confused right now.

Should you have a disclaimer, should you use them? Yes. The disclaimer has to be reasonable. If you have a check the box, which is called a clickwrap agreement ... If you have a check the box function on your site, add the disclaimer to that so it would read, "I agree to the terms and conditions, the privacy policy, and the disclaimer," and keep a log of that. That's going to be much more effective in trying to enforce the disclaimer.

Pat: Richard and Alena, thank you again for your time. There's obviously a lot more we could talk about, but I think for a lot of people who lasted to the end here, at least, they're going to be happy that they got a lot of this information. I think a lot of people will also be quite overwhelmed, and especially for those who are just starting out, it's a lot to think about. The last thing I want to do is scare people away from starting a business that could change their lives and change the lives of many others. Can each of you say one thing to help these people through a lot of these legal things and when they're just starting out? Even for people who have already started, how do

we just make sense of all this in the best way possible? Obviously, one of the best things you could do is find an attorney that you trust and work with them through all these different things because each business is different, obviously, but any words of wisdom before we finish off today? Richard, we'll start with you.

Richard:

Yeah, the legal issues can be a little overwhelming. I think that a lot of these things are issues if you're pushing the envelope. I think that if you do things ... even if you just sit down with an attorney, consult with them for an hour kind of on an outline, have a website review. As part of this, I told you I would do free website reviews for anyone that's listening if they have questions. You know, just contact me at socialinternetlawyer.com, and I'll take a look at your site and let you know if there are any issues for free, no cost. As long as you can isolate the potential problem areas of your site and take care of those, you're fine.

I mean, we're talking about copyright and a lot of these issues are somewhat esoteric. Once you get up and rolling, they're really not issues that you deal with too much. The key is just to have a good foundation in place and make sure that, you know, for instance, if you allow people to post to your site or something, you're going to be DMCA compliant and those kinds of things. It sounds like it's a big hurdle, but it's actually very simple. Once you learn the 3-step process, you never really have to worry about it again. None of this should be considered something that's going to be a hurdle for you getting into business. Most of these things will actually help you, your terms and conditions, your privacy policy, disclaimers. Although they're annoying and there can be legal minutiae involved in them, they're there to help you and they will protect you.

With most of my clients, knock on wood, by putting everything together properly and organizing things properly, they have almost no legal issues that come up. You know, if you do that and the listeners take the step to set it up right, they're ahead of 95% of the internet.

Pat:

Yeah, yeah.

- Richard: The potential risk is almost nothing. It's just you have to do the annoying little things, and then you can get on and start working on growing your business.
- Pat: Yeah, well, thank you, Richard. I appreciate that. You had, again, one more I want to reiterate your offer there, which was just a free quick consult. If you email Richard, you can find his email over at socialinternetlawyer.com. Is that correct, Richard?
- Richard: Yeah, just drop me a note and I'll be happy to either look at your site or answer any questions you have.
- Pat: Cool. Thank you. Alena, any final words of wisdom from you?
- Alena: Yeah, I mean, having your own business is rewarding, and I think as long as you go in prepared and you manage your own expectations and you're ready to work hard and then you're willing to take the steps to prevent a lot of the problems that can arise, then you'll be fine. A lot of the problems people have is when they come in maybe under-funded. You got to plan for not only the purchase price of a business or starting of the business, the operating expenses, but also unanticipated expenses, which always seem to arise. You can minimize that by doing due diligence ahead of time and just being careful, taking appropriate steps.
- Being prepared with adequate funding is important, managing your expectations. Don't think that you're going to make a profit that first year. Some businesses don't make profit for several years. If you're prepared to live with that, then you won't be disappointed when you're not making a profit right away. Then also be ready to work hard. You have to make sure your heart's in it for the long haul. Sometimes you'll come upon challenges and then you might feel like giving up because it's just too hard, but if you push through, you'll get the rewards.
- Pat: Love it. Thank you. Yeah, Richard?
- Richard: Pat, there was one other thing I was going to mention. I know a lot

of people have common questions about finding insurance.

Pat: Yeah, let's talk about that really quick. Thanks for that.

Richard: Okay. The insurance industry is about 20 years behind normal business, so it can be difficult to find some insurance companies that will insure your business. You should have insurance if you can afford it. The reason why is the insurance will actually pay any settlements or any judgment against your business, but equally importantly, your insurance will pay your attorney fees to defend the lawsuit. If you just form a corporation or an LLC and you get sued, the problem is you're going to need 20 grand, 30 grand, whatever it is to pay your defense counsel to defend the case. Most companies aren't going to have that, so insurance is really important. Finding it can be difficult.

There are two companies that I know that at least act as brokers for it. I don't know anything about these companies, if they're good or not or anything of that sort, so you need to take a look at them yourself. One is the unfortunately named hiscox.com. It's H-I-S-C-O-X.com. The second one is techinsurance.com. Then, Pat, I don't know if you want to mention the company that you're with, but getting insurance is definitely something that a business, you know, you want to do as a small business as soon as you can afford it. Again, there are a lot of different costs that you have when you start a business, but insurance is definitely one worth paying.

Pat: Yeah, and you know, knock on wood, I haven't had the need for insurance for that particular reason, but I still have insurance. I think it's important. I'll put in the show notes who I use and links and all that stuff of everything we mentioned today, but the insurance was actually really important for a DDOS attack that I had in 2013. I was able to recoup some costs from a week and a few days of downtime as a result of a hacker attack on SPI. It was helpful for that reason, too. Yeah, thank you, guys. Alena, did you want to give a shout-out to where people can find out more about you, like what website and if you had anything to offer?

Alena: Sure, my website is herranenlaw.com. That's H-E-R-R-A-N-E-N-L-A-W.com. If you have any business law questions or trademark/copyright questions, feel free to send me an email or give me a call. I'd be happy to talk to you and see if I can help.

Pat: Awesome. You guys are great. Thank you so much for what you do for me and what you've just done for the SPI community. Thanks. We'll talk soon, I'm sure. Cheers, guys, thank you.

Alena: Thank you.

Richard: Great. Thanks, Pat.

Pat: All right, thank you for listening in. I appreciate you listening all the way through, and I hope that wasn't too much for you. You can always obviously download the transcript or relisten to this if you'd like. You can also visit Richard at socalinternetlawyer.com. Alena is available at herranenlaw.com. As she mentioned, that's H-E-R-R-A-N-E-N law.com. The very generous offers they have to help you out with any questions that you might have. Feel free to reach out to them, and they're going to do their best to help you.

Now, of course, you might be in a different state, so there might be different laws. You might be in a different country, so of course these US laws do not apply, but I wish you all the best, and I don't want these legal things to stop you from doing what it is that you want to do so that you can provide value to another person and be rewarded at the same time or provide value to a large number of other persons.

I also want to thank 99designs.com today, who is the sponsor of this particular episode. I was actually very happy with their service recently when I ran a contest to take an old blog post of mine and repurpose it into an infographic. Just recently, I actually launched that infographic in its own blog post, and several people have shared it. Definitely worth the time and effort that I put into that. I just want to thank 99designs.com because they made it really easy. It was actually really fun because I posted that job description up

there, and several really great designers from around the world came in and designed their own version of what they thought I was looking for, and I got to pick the favorite one that I loved. That's the one I shared. It was really cool to have all these different options because they all had different styles. I think that's a really cool thing. If you can't yet afraid that one designer who's going to work with you full-time on your projects, I would highly recommend checking out 99designs.com for these little one-off projects that you might have, anything from logos to website design to tee shirts, to infographics, anything you can think of that is related to design.

If you want to get \$99 that you can apply for free towards your next design project there, you can go to 99designs.com/spi. That's where you go, 99designs.com/spi. Thank you all so much for listening in. I appreciate it, and I look forward to serving you in next week's episode. We got a number of success stories coming up and a lot of great content coming your way. Keep listening in. Subscribe if you haven't already. Again, one more time, the show notes for this episode are available at smartpassiveincome.com/session231. I appreciate you. Thanks so much. All the best, bye.

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