

This tipsheet is intended to provide general information and is not a substitute for legal advice.

Tipsheet contents	Page
• What is a business opportunity? ...	1
• What is a franchise? .....	1
• How investing in a business opportunity or franchise differs from investing in the stock market.	1
• What business-opportunity and franchise frauds are.....	2
• What protection you have.....	2
• What warning signs to look for....	3
• What precautions to take before you invest in a business opportunity or franchise.....	3
• How to get more information.....	4

### What is a business opportunity?

A business opportunity is a chance to invest money in a business. It's an arrangement in which a seller sells goods or services to a buyer. The seller generally offers to do one or more of the following:

- refund the initial payment if the buyer is dissatisfied
- reimburse the buyer for goods that the buyer has produced or has bought from the seller
- help the buyer find a location at which to sell the product or service on premises that the buyer doesn't own or lease (for example, on racks, in vending machines, or in display cases).

The cost to invest in a business opportunity is usually relatively small, between \$100 and \$1000. A business opportunity often provides part-time work for one individual who functions independently. The stocking of vending machines is an example of a business opportunity.

### What is a franchise?

A franchise is also a chance to invest in a business, but it differs from a business opportunity. A franchise is an arrangement in which a seller (a parent company, or a franchisor) sells to a buyer (a franchisee, or sub-franchisor) the rights to do the following:

- sell or distribute a continuous supply of the franchisor's goods and services
- use the franchisor's marketing plan and trademark
- recruit additional franchisees or sub-franchisors

The fee for buying these rights can be \$10,000 to \$250,000. The total cost of the investment can be substantial - as much as hundreds of thousands of dollars.

Franchisees usually buy entire systems - buildings, equipment, supplies, training assistance, uniforms, and so on. Their total investment, in time and money, is generally greater than for business opportunities.

A franchise often provides full-time work for many people. One outlet in a chain of fast-food restaurants is an example of a franchise.

### Is investing in a business opportunity or franchise like investing in the stock market?

Investing in a business opportunity or franchise isn't the same as investing in stocks and bonds. In general, investors who place their money in the markets are passive, but business-opportunity and franchise investors take a much more active role. They "sink or swim" on the basis of how hard they work and how well the supplying companies honour their end of the bargain.

## What are business-opportunity and franchise frauds?

Fraud is the intent to deceive. Business-opportunity and franchise frauds are attempts to deceive people into investing their money in unreliable businesses. Con artists strip thousands of investors each year of millions of dollars. Swindlers overwhelm victims with high-pressure sales tactics and promises of quick profits and a life of independence and ease. Retired and unemployed people are often the targets of swindlers.

### *Classic business-opportunity swindles unfold this way:*

Con operators place ads that are filled with glowing promises in local newspapers. They may also rent booths at business-opportunity shows. Potential investors are invited to call a toll-free number for more information and for application forms. Once unwary investors express interest, the swindlers arrange a meeting at which they promise prompt delivery, high-quality merchandise, low costs, untapped markets, and minimal risk of loss. The swindlers also insist that it's a "now or never" opportunity and that investors must buy immediately.

The investors turn over their money to the promoters and are left with slick catalogues and order forms. The swindlers leave town and, if they're ever heard from again, supply the investors with a small amount of over-priced, shoddy merchandise and none of the promised "100-percent sure-fire, can't miss" advice and assistance.

Examples of other vehicles for business-opportunity frauds are:

- programs for breeding chinchillas, rabbits, beavers, or worms
- home mail-order business
- dealerships for auto parts, vending machines, or energy-related products

Franchise frauds sometimes involve grandiose guarantees of high profit and low risk. The promoters overstate the protective, supportive role of the franchisor. Frequently, the parent

company is either non-existent or much smaller and less helpful than the promoters suggest.

### *Here's a real-life example:*

Prospective investors responded to a newspaper ad and attended a hotel-room meeting with a promoter. The promoter's company had a limited number of hot-dog franchises available for sale. The company would provide the product, equipment, training, and operating assistance. A deposit of \$15,000 was required to obtain one of these fast-selling franchises. Numerous people paid deposits. After a few months of contact, the promoter disappeared. Police issued a warrant for the arrest of the promoter.

## What protection do I have?

The *Franchises Act* no longer requires filing with the Alberta Government. It requires franchisors to give disclosure documents to franchisees. Disclosure documents contain important information about franchises that investors can read to make informed decisions. The Act also specifies that every franchise agreement imposes on each party a duty of fair dealing in its performance and enforcement.

**Prospective franchisees must receive disclosure statements 14 days before they sign any agreement relating to the franchise, or the payment of any consideration relating to the franchise, whichever is earlier. If the franchisor fails to give out the disclosure statements within 14 days, the prospective franchisee may rescind all the franchise agreements.**

If a franchisee suffers a loss because of a misrepresentation contained in a disclosure statement, the franchisee has a right of action for damages against the franchisor and every person who signed the disclosure statement.

Be aware that the government can't become involved in disputes between franchisees and franchisors. If you have a dispute with a franchisor, speak directly with the company to

try and resolve the problem. If the matter is not resolved you may have to get legal advice.

The Alberta government doesn't regulate business opportunities, but Alberta Government Services requires some businesses to be licensed. Examples are door to door sales, home renovators who require prepayment, collection agencies, and so on.

### **What warning signs should I look for?**

The following signs should alert you to a possible business-opportunity or franchise fraud.

#### **High pressure sales tactics**

Shady promoters demand quick decisions. They don't allow investors to investigate profit claims or consult with lawyers or accountants. Don't be impressed with ads in national or local publications. Publications often don't screen ads that they print.

#### **Promises of sky-high profits**

Honest promoters don't guarantee clients a return on their investments, much less astronomical profits of 100 percent or more. Legitimate operators qualify their success stories by stating the percentage of participants who have earned big money.

#### **Unjustified start-up fees**

Examine the inventory, training course, and sales kits that promoters insist that you buy. Are the promoters asking for more than the fair market value of these start-up items?

#### **Evasive answers and failure to reveal information**

If the promoters don't answer you questions directly or if they refuse to provide details, don't go any further. Remember that your chance to succeed depends on the sellers' full cooperation and assistance. What do the promoters have to hide?

### **What should I do before I invest in a business opportunity or franchise?**

If you're considering a business-opportunity or franchise offer, take these precautions before you invest:

#### **Check out the product**

Are the goods or services of high quality? Get all the details about patents, warranties, frequency of repairs, consumer ratings, and provincial or federal restrictions on use.

#### **Size up the market**

Will anyone buy this product? (You don't want to get stuck trying to install tennis courts in an economically depressed area.) Are existing businesses already meeting demand? Ask for market studies.

#### **Analyze profit claims**

Get all the promoters' promises in writing. Check the profit claims with an accountant. Compare the claimed returns with those earned by similar products in your market. Find out what percentage of investors have received large profits.

#### **Question large start-up fees**

Make sure that you're getting something for every dollar that you turn over to the promoters. Are they offering you the product at such a price that you can retail it at a profit?

#### **Find out all restrictions**

As a prospective investor, you want to know all of the limitations that'll be imposed on your business operation, including what and where you must buy and sell. For example, franchises often impose rigid rules about sales, marketing, and quality control.

#### **Find out how much help you'll get**

Get a detailed written description of any help that the business will provide, including training, site selection and financial assistance.

**Get the names of investors and customers**

Check the operation yourself. Take the time to get the information from people who have experience dealing with the seller.

**Check whether the business has a record of lawsuits against it**

Ask for information about lawsuits and bankruptcy proceedings that involve the business's owners and staff. Look, too, for charges of embezzlement, fraud, and unfair or deceptive practices. Review the disclosure document carefully as details of those incidences are required to be disclosed on the disclosure document.

**Demand detailed financial information**

The most recent financial statements must be included in the disclosure document, unless the franchisor has been exempted. If necessary, ask the promoters for financial statements of the business for the previous years. Have your accountant review the financial information and explain it to you if you don't understand it.

**Read and understand the business contract**

Have your lawyer review it and explain any clauses that you don't understand.

**Read the tip sheet**

The tipsheet *Buying a Franchise* provides more details on the questions you should ask if you are considering a franchise.

One final point: if you suspect that an offer is a swindle, tell your suspicions to the authorities, even if you decide not to invest. Your warning can help protect other investors. Contact the police and the Better Business Bureau if you suspect any fraudulent business activity.

**For more information****Alberta Government Services**

Edmonton: (780) 427-4088

Toll free in Alberta: 1-877-427-4088

**Better Business Bureau**

Calgary and Southern Alberta

350, 7330 Fischer Street SE

Calgary, Alberta T2H 2H8

Phone: (403) 531-8780

**Central and Northern Alberta**

514, 9707-110 Street

Edmonton, Alberta T5K 2L9

Phone: (780) 482-2341

Toll free in Alberta: 1-800-232-7298

---

A current version of this tipsheet and other tipsheets are available at the Alberta Government Services web site at [www.gov.ab.ca/gs](http://www.gov.ab.ca/gs) Most public libraries have Internet access available if you don't have access at home.

If you need more copies of this tipsheet you have permission to photocopy. Please call our office to make sure you have the most up-to-date version.