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OF COUNSEL
PAUL R. KENNERSON

December 5, 2002

Mr. Gene Magre
P.O. Box 551
Rancho Santa Fe, CA 92067

Re: Magre — General Business
Our File No. 2500.1

Dear Mr. Magre:

As we have been discussing for some time, you have engaged the services of this firm to assist you in a specific aspect of a new venture you are undertaking. As you have explained it to me, you believe that the cost of doing business in California, particularly as it concerns costs related to employees, is excessive. This includes, but is not limited to, the cost of workers' compensation insurance. It is your belief that these costs have given rise to a large segment of the business community (particularly in the construction and related industries) skirting the law, either through the use of undocumented workers or wrongfully categorizing employees as independent contractors.

The question you have asked us is whether a business entity can be created in accordance with California law that will allow the business entity to operate with a lower employment cost and, at the same time, offer a bundle of benefits (disability, life and health insurance, etc.) that is superior to that which they would otherwise receive. In answer to your question, California Labor Code Section 3351(c) reads as follows:

3351. "Employee" means every person in the service of an employer under any appointment or contract of hire or apprenticeship, express or implied, oral or written, whether lawfully or unlawfully employed, and includes:

... (c) All officers and members of the board of directors of a quasi-public or private corporations while rendering actual services for the corporations for pay; *provided that, where the officers and directors of the private corporation are the sole shareholders thereof, the corporation and*

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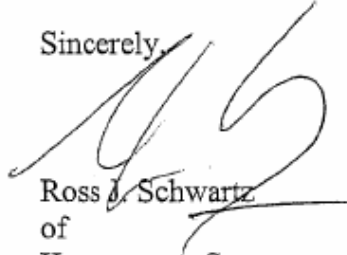
Mr. Gene Magre
December 5, 2002
Page 2

*the officers and directors shall come under the compensation provisions of this division **only** by election as provided in subdivision (a) of Section 4151. (Emphasis added.)*

Stating it another way, if they are the *sole* shareholders of the corporation, then the officers and directors who perform services for the corporation are *not* employees under the act unless they elect to be. Since, by law, these individuals are not employees, then the goal would be to establish the business entity as a corporation in which all (or virtually all) of the employees are shareholders, officers and/or directors.

I hope this letter provides you with the information you desired. To the extent you have any questions or require any additional information, please let me know.

Sincerely,



Ross J. Schwartz
of

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