Disclosure Requirements and Prohibitions Concerning Business Opportunities
Staff Report to the Federal Trade Commission and
Proposed Revised Trade Regulation Rule
(16 CFR Part 437)

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This Report, as required by Section 1.13(f) of the Commission's Rules of Practice, contains the staff's analysis of the rule amendment record and its recommendations as to the form of the proposed final Business Opportunity Rule. The Report has not been endorsed or adopted by the Commission. The Commission's final determination in this matter will be based upon the record taken as a whole, including the Report and comments on the Report received during the 75-day period after the Report is placed on the public record.

Key to Terms and Abbreviations Used Throughout This Report

"Amended Franchise Rule" refers to the amended Franchise Rule published at 72 Fed. Reg. 15,444 (Mar. 30, 2007) and codified at 16 CFR 436.

"Initial Proposed Disclosure Document" refers to the version of the Disclosure Document that was proposed in the INPR.

"INPR" refers to the Initial Notice of Proposed Rulemaking, 71 Fed. Reg. 19,054 (Apr. 12, 2006).

"Interim Business Opportunity Rule" refers to the current Business Opportunity Rule, codified at 16 CFR 437.

"IPBOR" refers to Initial Proposed Business Opportunity Rule, which was proposed in the INPR.

"Macro Report" refers to Macro International, Inc.'s report to the FTC on the Disclosure Form, available at http://www.ftc.gov/bcp/workshops/bizopps/disclosure-form-report.pdf.

"Original Franchise Rule" refers to the original Franchise Rule published at 43 Fed. Reg. 59,614 (Dec. 21, 1978).

"Proposed Final Disclosure Document" refers to the proposed Disclosure Document incorporating the staff's recommendations and attached as Attachment D.

"Proposed Final Rule" refers to the proposed Business Opportunity Rule incorporating the staff's recommendations and attached as Attachment B.

"Revised Proposed Disclosure Document" refers to the version of the Disclosure Form that was published in the Workshop Notice.

"RNPR" refers to the Revised Notice of Proposed Rulemaking, 73 Fed. Reg. 16,110 (Mar. 26, 2008).

"RPBOR" refers to the Revised Proposed Business Opportunity Rule, which was proposed in the RNPR.

"Workshop" refers to the June 1, 2009 public workshop held in Washington, D.C. to discuss the proposed Disclosure Document and other aspects of the Business Opportunity Rule.

"Workshop Notice" refers to the Federal Register Notice announcing the Workshop, 74 Fed. Reg. at 18,712 (Apr. 24, 2009).

The staff recommends that the Interim Business Opportunity Rule, 16 CFR Part 437, be amended to, among other things, broaden its scope to cover sellers not currently covered by the Interim Business Opportunity Rule, such as sellers of work-at-home opportunities, and to streamline and simplify the disclosures that sellers must provide to prospective purchasers ("Disclosure Document"). The Commission has gathered and analyzed comments on an Initial Proposed Business Opportunity Rule ("IPBOR"),[1] proposed significanworeanges to the scope and substance of the IPBOR in a Revised Proposed Business Opportunity Rule ("RPBOR"),[2] engaged a contractor to improve the clarity of the proposed Disclosure Document, and conducted a public workshop on this matter. In addition, the staff has reviewed public comments on the RPBOR and the workshop.[3]

The RPBOR would have required that business opportunity sellers disclose to potential purchasers four categories of material information, including: litigation history of the business opportunity and certain key personnel; the terms of any cancellation or refund policy, if offered; documentation and substantiation for any claims sellers make about potential earnings; and contact information for previous purchasers of the business opportunity. It also would have prohibited sellers from making certain misrepresentations and impose recordkeeping

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[1] Business Opportunity Rule Notice of Proposed Rulemaking, 71 Fed. Reg. 19,054 (Apr. 12, 2006) ("INPR"). Comments responding to the INPR are available at http://www.ftc.gov/os/comments/businessopprule/index.shtm.

[2] Business Opportunity Rule Revised Notice of Proposed Rulemaking, 73 Fed. Reg. 16,110 (Mar. 26, 2008) ("RNPR"). Comments responding to the RNPR are available at http://www.ftc.gov/os/comments/bizoprevised/index.shtm.

[3] See An FTC Workshop Analyzing Business Opportunity Disclosure Form and Other Proposed Changes to the Business Opportunity Rule, 74 Fed. Reg. at 18,712 (Apr. 24, 2009). Workshop comments are available at http://www.ftc.gov/os/comments/bizoprulerevwrkshp/index.shtm.

- To allow sellers to provide as part of a supplemental disclosure pertaining to any prior legal actions a 100-word description of any such action;
- To add a definition of "material" and to clarify that sellers must disclose to purchasers the "material" terms of any cancellation or refund policy;
- To omit from the required disclosure of prior purchasers information, the city where the prior purchaser is located;
- To add a requirement that if a business opportunity is marketed in Spanish to a potential purchaser, then the Spanish-language version of the Disclosure Document must be furnished, and any disclosures required by the Rule must be provided in Spanish, and if a business opportunity is marketed to a potential purchaser in a language other than English or Spanish, the business opportunity seller must furnish all required disclosures, including an accurate translation of the Disclosure Document, in the same language that the opportunity is marketed;
- To allow sellers to use industry statistics, when they have written substantiation demonstrating that purchasers of their business opportunity have earnings equal to or greater than the industry statistics; and
- To add a definition of "signature" or "signed" to include electronic signatures.

This Report analyzes the rulemaking record to date, describes each provision of the proposed Final Rule, and sets forth the staff's recommendation on each provision.[6]

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[6] Within this Staff Report references to the comments responding to the Business Opportunity Rule INPR are cited as: Name of the commenter-INPR (e.g., Avon-INPR); references to the comments responding to the Business Opportunity Rule RNPR are cited as: Name of the commenter-RNPR (e.g., Primerica-RNPR). A list of the INPR and RNPR commenters and the abbreviations used to identify each are attached as Attachment A.

I. Background

On December 21, 1978, the Commission promulgated the Original Franchise Rule to address deceptive and unfair practices in the sale of franchises and business opportunity ventures.[7] Based upon the original rulemaking record, the Commission found that franchise and business opportunity fraud was widespread, causing serious economic harm to consumers, and the Original Franchise Rule covered, in a single Code of Federal Regulations part, both franchises and business opportunity ventures.

The Commission adopted the Franchise Rule to prevent fraudulent practices in the sale of franchises and business opportunities through pre-sale disclosure of specified items of material information. The purpose of the Franchise Rule was not to regulate the substantive terms of a franchise or business opportunity agreement but to ensure that sellers disclose material information to prospective buyers. The Franchise Rule was posited on the notion that a fully informed consumer can determine whether a particular offering is in his or her best interest.

As part of the Commission's overall policy of periodic review of its trade regulation rules, the Commission commenced a regulatory review of the Original Franchise Rule in 1995. Much of the information revealed by the regulatory review focused on the differences between franchises and business opportunity ventures, and the distinct regulatory challenges presented by these two types of offerings – that franchises typically are expensive and involve complex contractual licensing relationships, while business opportunity sales are often less costly, involving simple purchase agreements that pose less of a financial risk to purchasers. Based on the record amassed during the review proceeding, the Commission concluded that the Franchise

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[7] Promulgation of Trade Regulation Rule and Statement of Basis and Purpose ("SBP"), 43 Fed. Reg. 59,614 (Dec. 21, 1978).

[8] Since 1995, the Commission has conducted more than eighteen law enforcement sweeps, many with other law enforcement partners to combat business opportunity fraud. E.g., Operation Bottom Dollar (2010); Operation Short Change (2009); Project Fal$e Hope$ (2006); Project Biz Opp Flop (2005); Project Busted Opportunity (2002); Project Telesweep (1995); Project Bizillion$ (1999); Operation Money Pit (1998); Project Vend Up Broke (1998); Project Trade Name Games (1997); and Operation Missed Fortune (1996). In addition to joint law enforcement sweeps, the Commission also targeted specific business opportunity ventures such as envelope stuffing (Operation Pushing the Envelope 2003); medical billing (Operation Dialing for Deception 2002 and Project Housecall 1997); seminars (Operation Showtime 1998); Internet-related services (Net Opportunities 1998); vending machines (Operation Yankee Trader 1997); and 900 numbers (Project Buylines 1996).

[9] Trade Regulation Rule on Franchising and Business Opportunity Ventures: Advanced Notice of Proposed Rulemaking, 62 Fed. Reg. 9,115 (Feb. 28, 1997).

[10] 71 Fed. Reg. at 19,054. Later, on March 30, 2007, the Commission published the

the sale of business opportunities, the INPR proposed an expansive definition of "business opportunity" aimed at covering business opportunities that had been covered by the Franchise Rule, but also work-at home schemes, such as envelope stuffing and product assembly, medical billing schemes, and pyramid schemes.[11] While expanding the scope of the Original Franchise Rule's coverage of business opportunities, the IPBOR greatly reduced the compliance burden that the Original Franchise Rule imposed on business opportunity sellers. The Commission recognized that the extensive disclosures of the Original Franchise Rule would entail disproportionate compliance costs for comparatively low-cost transactions involving the sale of business opportunities.[12] Therefore, in an attempt to strike the proper balance, the Commission

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deleted. As noted above, Part 437 continues to govern sales of non-franchise business opportunities, pending completion of these Business Opportunity rulemaking proceedings. 73 Fed. Reg. at 16,111.

[11] Promoters of these kinds of schemes were often able to evade coverage under the disclosure requirements of the Franchise Rule by pricing their opportunities below $500, the monetary threshold of Franchise Rule coverage.

[12] 71 Fed. Reg. at 19,057.

[13] Id.

before execution of a contract in connection with a business opportunity sale, or prior to payment of any consideration to the seller. The initial proposed Disclosure Document was intended to provide prospective purchasers with material information with which to make an informed decision about the potential business opportunity. The seller would have been required to use the exact form and language proposed by the Commission and to include identifying information about the seller and information about four substantive areas: earnings claims, legal actions involving the offered business and its key personnel, existence of cancellation or refund policies and the number of cancellation or refund requests, and references.[14]

In response to the INPR, the Commission received more than 17,000 comments, the overwhelming majority of which came from the multi-level marketing ("MLM") industry. MLM companies, their representatives and trade associations,[15] as well as individual participants in various MLM plans, expressed grave concern about the burdens the IPBOR would impose on them, and urged the Commission to narrow the scope of the IPBOR, to implement various safe harbor provisions, and/or to reduce the required disclosures.[16] The Commission also received approximately 187 comments, primarily from individual consumers or consumer groups, in

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[14] Id. at 19,068.

[15] Multi-level marketing is one form of direct selling, and refers to a business model in which a company distributes products through a network of distributors who earn income from their own retail sales of the product and from retail sales made by the distributors' direct and indirect recruits. Because they earn a commission from the sales their recruits make, each member in the MLM network has an incentive to continue recruiting additional sales representatives into their "down lines." See Peter J. Vander Nat & William W. Keep, Marketing Fraud: An Approach to Differentiating Multilevel Marketing from Pyramid Schemes, 21 J. Pub. Pol'y & Marketing 140 (Spring 2002).

[16] Thousands of comments were form letters submitted by participants in various MLM operations such as Quixtar, Shaklee, PartyLite, and Xango, among others. 73 Fed. Reg. at 16,113.

[17] Numerous letters came from individuals having negative experiences with various MLMs like Quixtar, 4Life, Mary Kay, Arbonne, Liberty League International, Financial Freedom Society, Herbalife, Xango, Melaleuca, EcoQuest, Pre-Paid Legal, PartyLite, Shaklee, Vartec/Excel, and Vemma. 73 Fed. Reg. at 16,113 n.37.

[18] Id. at 16,113.

[19] Id. As one commenter described it, the IPBOR would have swept in traditional arrangements for distribution of "food and beverages, construction equipment, manufactured homes, electronic components, computer systems, medical supplies and equipment, automotive parts, automotive tools and other tools, petroleum products, industrial chemicals, office supplies and equipment, and magazines." IBA-INPR at 5; see also Timberland-INPR (noting that numerous manufacturers structure their retail distribution in this manner).

[20] In the RNPR, the Commission acknowledged that some MLMs do engage in unfair or deceptive acts or practices, including the operation of pyramid schemes or unsubstantiated earnings claims that cause consumer harm, but concluded, based upon an

On March 26, 2008, the Commission issued the RNPR that proposed a revised Business Opportunity Rule, the RPBOR, which would have modified the IPBOR in several significant ways, primarily by narrowing the scope of the proposed Rule to avoid broadly sweeping in all sellers of MLM opportunities,[21] while retaining coverage of those business opportunities sellers historically covered by the FTC's Original Franchise Rule (and by the FTC's Interim Business Opportunity Rule), as well as coverage of sellers of work-at-home schemes, including envelope stuffing, medical billing, and product assembly. The RPBOR also would have cured a potential overbreadth problem that may have inadvertently swept in companies using traditional product distribution arrangements.[22]

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[21] The RPBOR would not have exempted MLMs from coverage under the RPBOR. Instead, it would have narrowed the scope of the IPBOR by redefining the term "business opportunity." Under the RPBOR, the three definitional elements of a business opportunity would have been: (1) a solicitation to enter into a new business; (2) a "required payment" made to the seller; and (3) a representation that the seller will provide "business assistance" to the buyer. The RPBOR would have eliminated two types of "business assistance" that formerly would have triggered the Rule's strictures and disclosure obligations, namely tracking payments and providing generalized training or advising. See infra Section V.C. (discussion of the term "business opportunity"); 73 Fed. Reg. at 16,121.

[22] The RPBOR also would have included several other substantive modifications to the IPBOR. See 73 Fed. Reg. at 16,110.

[23] 73 Fed. Reg. at 16,125. The initial proposed Disclosure Document was revised to eliminate these disclosures. See 73 Fed. Reg. at 19,091.

stated purpose, and if it did not, what alternatives the Commission could consider.[24] In contrast to the INPR, which generated more than 17,000 comments, the Commission received fewer than 125 comments and rebuttal comments in response to the RNPR. The vast majority of commenters were from the MLM industry, and supported the Commission's proposal to narrow the scope of the Business Opportunity Rule, albeit with suggestions for fine tuning.[25] Only one comment came from a business opportunity seller.[26] The Commission also received comments

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[24] 73 Fed. Reg. at 16,133.

[25] Some commenters suggested changes to the language of certain definitions proposed in the RNPR to ensure that the multi-level marketing industry was not inadvertently swept into the ambit of the rule.

[26] Planet Antares-RNPR.

[27] Some letters came from individuals having negative experiences with MLMs such as Quixtar, Herbalife, and USANA Health Science.

[28] 73 Fed. Reg. at 16,133.

Following publication of the RNPR, Macro International, Inc. ("Macro"), the expert engaged by the FTC, conducted extensive consumer testing of the initial proposed Disclosure Document that resulted in substantial improvement to both the layout and the wording of the form.[29]

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[29] A copy of the expert's report to the FTC, "Design and Testing of Business Opportunity Disclosures," ("Macro Report") is available at http://www.ftc.gov/bcp/workshops/bizopps/disclosure-form-report.pdf.

[30] The version of the revised proposed Disclosure Document that was tested by Macro inadvertently omitted the phrase "or pay any money" from the conclusion of the penultimate sentence of the revised proposed Disclosure Document. Macro determined that this omission had no effect on the results of its testing. See Macro Report at 2.

[31] See 74 Fed. Reg. at 18,712.

[32] Commission staff selected individuals as panelists based upon their comments, backgrounds, and interest in the subject matter. See infra Section VII.B. for more information about the Workshop.

conclusion of the discussion of the revised proposed Disclosure Document, panelists and audience members were invited to express their views about other issues related to the RPBOR.[33] Following robust discussion on various topics, the Commission received written comment from six individuals and entities.[34]

Following the Workshop, the staff has considered the utility of the Disclosure Document for business opportunities marketed in Spanish – specifically, whether the Disclosure Document could be made more effective by translating it into Spanish and requiring that when a business opportunity is marketed in Spanish, the Disclosure Document and any disclosures required by the Rule be provided in Spanish. The Commission's law enforcement history demonstrates that some fraudulent business opportunities are marketed primarily to Spanish speaking consumers.[35]

II. Organization of the Report

This Staff Report analyzes the rulemaking record to date, including the comments on the RNPR and the Workshop Notice, examines the continuing need for the Rule, and sets forth the staff's recommendations to the Commission regarding the specific provisions of the proposed final Business Opportunity Rule ("proposed Final Rule"). The sections that follow discuss the specific Rule provisions that the staff recommends the Commission issue, along the way, noting areas of disagreement and attempts to harmonize the Commission's law enforcement experience

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[33] A copy of the transcript of the June 1, 2009 workshop is available at http://www.ftc.gov/bcp/workshops/bizopps/index.shtml. References to the transcript from the June 2009 Business Opportunity Rule public workshop are cited as: Name of commenter, June 09 Tr at page no. (e.g., Jost, June 09 Tr at 12).

[34] References to comments received in response to the Workshop Notice are cited as: Name of commenter-Workshop comment.

[35] See infra Section IX.

with legitimate concerns articulated by commenters.

Annexed to the Report are seven attachments. Attachment A is a list of commenters cited within the body of the Report. The proposed Final Rule that incorporates the staff's various recommendations is Attachment B. To assist the reader in reviewing the staff's analysis and recommendations, Attachment C is a redline that shows additions, deletions, and revisions to the RPBOR made by the proposed Final Rule. The Disclosure Document that incorporates the staff's various recommendations ("proposed final Disclosure Document") in English is Attachment D. To assist the reader in reviewing the staff's analysis and recommendations, Attachment E is a redline that shows additions, deletions, and revisions to the revised proposed Disclosure Document as compared to the proposed final Disclosure Document. The Spanish version of the proposed final Disclosure Document is Attachment F.

III. Summary of Comments to the Revised Notice of Proposed Rulemaking

The Commission invited members of the public to comment on any issues they believed were appropriate to the Commission's consideration of the RPBOR. The Commission also solicited comment in specific areas, including: (1) whether the proposed categories of "business assistance" that would trigger coverage by the Rule were adequate to cover the field of business opportunity promoters that were most likely to engage in fraud, and to exclude from coverage traditional distributor relationships; (2) whether the presentation of information in the one-page disclosure document could be improved to make it more useful and understandable; (3) whether mm" tfu4nl DpJ1of

[36] 73 Fed. Reg. at 16,133.

[37] Planet Antares-RNPR.

[38] Id.; see infra Sections IV.A. and IV.B for a discussion of the commenter's first three contentions, and Section VII.C.4. for a discussion of the fourth.

[39] See, e.g., DSA-RNPR; Avon-RNPR; Bates-RNPR; IBA-RNPR; MMS-RNPR; Mary Kay-RNPR; Melaleuca-RNPR; Primerica-RNPR; Pre-Paid Legal-RNPR; IDS-RNPR; Tupperware-RNPR; Venable-RNPR.

[40] See, e.g., Tupperware-RNPR; Primerica-RNPR; Mary Kay-RNPR.

[41] See, e.g., DSA-RNPR; Babener-RNPR; MarketWave-RNPR; NBCC-RNPR; Whittle-RNPR.

[42] DSA-RNPR. Although the RNPR indicates the Commission's intent to narrow

[45] See Credit Practices Rule, 49 Fed. Reg. 7,740, 7,742 (Mar. 1, 1984); see also 15

consumers the information they need to protect themselves from fraudulent sales claims, while minimizing the compliance costs and burdens on sellers of business opportunities.[47]

A. The FTC's Law Enforcement History Demonstrates the Continued Need for the Rule

The staff strongly disagrees with commenters who urge abandonment of the Business Opportunity Rule. The FTC's law enforcement history demonstrates that the sale of fraudulent business opportunities has been a widespread and persistent problem since the Franchise Rule was first promulgated in 1978, and many consumer complaints received by the FTC have also sounded this theme.[48] The continued necessity of an anti-fraud regulation that provides consumers with material information on a pre-sale basis is, therefore, well supported by the Commission's law enforcement experience. Since 1995, the Commission has brought more than 245 cases against business opportunity sellers, and conducted more than eighteen law enforcement sweeps,[49] many with other federal and state law enforcement partners, to combat persistent business opportunity frauds violating the Original Franchise Rule, such as those

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[47] See id.

[48] In 2009, the Commission logged over 13,000 complaints against franchises, business opportunities, and work-at-home schemes, and that figure has increased each year since 2007. See Consumer Sentinel Databook, available at http://www.ftc.gov/sentinel/reports/sentinel-annual-reports/sentinel-cy2009.pdf.

[49] E.g., Operation Bottom Dollar (2010); Operation Short Change (2009); Project Fal$e Hope$ (2006); Project Biz Opp Flop (2005); Project Busted Opportunity (2002); Project Telesweep (1995); Project Bizillion$ (1999); Operation Money Pit (1998); Project Vend Up Broke (1998); Project Trade Name Games (1997); and Operation Missed Fortune (1996). In addition to joint law enforcement sweeps, the Commission has also targeted specific business opportunity ventures such as envelope stuffing (Operation Pushing the Envelope 2003); medical billing (Operation Dialing for Deception 2002 and Project Housecall 1997); seminars (Operation Showtime 1998); Internet-related services (Net Opportunities 1998); vending machines (Operation Yankee Trader 1997); and 900 numbers (Project Buylines 1996).

[50] E.g.

that will allow them to make informed purchasing decisions. At the same time, the streamlined form eases the compliance burden currently imposed on business opportunity sellers. The staff recommends that the Commission retain a pre-sale disclosure requirement for the sale of business opportunities. Like the Franchise Rule and the Interim Business Opportunity Rule, the RPBOR was posited on the notion that a fully informed consumer is in a better position to determine whether a particular offering is in his or her best interest. The proposed disclosure document would have provided prospective purchasers with information that is critical to making an informed purchasing decision. The RPBOR would not have regulated, nor was it intended to, the substantive terms of a business opportunity contract. Rather, it was designed to prevent fraud by prohibiting sellers from failing to disclose material information to prospective buyers. It is beyond dispute that consumers should be protected against receiving inaccurate information and self-serving unsubstantiated claims from business opportunity sellers.

C. The Rule Avoids Broadly Sweeping in MLMs

We agree with the Commission's decision articulated in the RNPR to narrow the scope of the IPBOR, to avoid broadly sweeping all MLMs into the ambit of the Rule. The Commission reasoned that the IPBOR would have imposed greater burdens on the MLM industry than on other types of business opportunity offerings without providing sufficient countervailing benefits to consumers.[58] At the same time, the Commission acknowledged that some MLMs engage in unfair or deceptive acts and practices, including the operation of pyramid schemes and the making of false and unsubstantiated earnings claims. However, the Commission concluded, and we agree, that neither the earnings disclosure provided by the proposed Rule, nor alternatives

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[58] See 73 Fed. Reg. at 16,133.

proposed by commenters, would enable potential recruits to differentiate between a legitimate MLM and a pyramid scheme, or to inform consumers adequately about likely earnings.[59] Consequently, the Commission concluded that because Section 5 continues to provide an effective tool to challenge unfair and deceptive acts or practices in the MLM industry, the burden of applying the Rule to MLMs generally appeared to outweigh any potential benefits.

We agree with the Commission's conclusions. While we take very seriously the commenters' concerns about pyramid schemes posing as legitimate MLMs, we are not persuaded that subjecting all MLMs to the Rule would allow consumers to differentiate between unlawful pyramid schemes and legitimate companies using an MLM business model.[60] Identifying a pyramid scheme masquerading as an MLM requires a fact-intensive inquiry, making it particularly well-suited to Section 5 enforcement, which proceeds on a case-by-case basis. We also believe that the Commission has taken the correct approach in narrowing key definitions –

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[59] The Commission determined that in view of the differences in the structure of MLM programs, it might not be possible to prescribe a feasible, uniform, industry-wide standard for providing earnings information. 73 Fed. Reg. at 16,120. Furthermore, identification of the true earnings of participants is undermined by the incentives in many MLMs for participants to report manufactured sales in order to retain a favorable commission level. Id. It further determined that other disclosures required by the proposed Rule, such as prior recruits, are not likely to help potential recruits evaluate the risk of participating, because all participants in the MLM have a financial incentive to enlist new recruits. Id.

[60] None of the comments received provided an industry-wide analysis of pyramid schemes masquarading as MLMs. They ask the Commission to assume widespread fraud in the multi-level marketing industry, but offer no evidence. Instead, the comments that purported to present evidence that legitimate MLMs were in fact unlawful pyramid schemes provided only anecdotal evidence. CAI-RNPR; Pyramid Watch-RNPR; Aird-RNPR; Durand-RNPR; Johnson-RNPR. As the Commission noted in the RNPR, identifying a pyramid scheme (or, at least, one that attempts to disguise itself as a legitimate business opportunity) entails a complex economic analysis including an in-depth examination of the compensation structure and the actual manner in which compensation flows within an organization. See Vander Nat & Keep, supra note 15, at 149. There is no bright line disclosure that would help consumers identify a fraudulent pyramid from a legitimate MLM.

namely, the IPBOR's definition of "business assistance" and "required payment" – that would necessarily have extended the Rule's coverage to all MLMs.

As discussed in more detail in infra Section V.C., some commenters argued that further refinement of the definition of the term "business opportunity" is necessary, either to address particular business practices common in the MLM industry or to ensure that MLMs are entirely excluded from the final Rule.[61] Many commenters rehashed arguments the Commission previously rejected in the RNPR.

As to the concern that certain non-harmful business practices may be covered by the RPBOR, commenters proposed a number of revisions to the definitions section of the RPBOR.[62] We believe the following clarifications to the RPBOR will address those concerns. First, a small change in section 437.1(a)(3)(i) to the definition of "business opportunity" will clarify that a seller's offer to provide, at no cost to its purchasers, office space or the use of business equipment (such as computers and printers) for the operation of the purchaser's business, does not trigger coverage by the Rule.[63] Second, a slight clarification in section 437.1(m) to the "otherwise assisting" clause of the "providing locations, outlets, accounts, or customers" will make clear that

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[61] Mary Kay-RNPR; Primerica-RNPR; Tupperware-RNPR; Pre-Paid Legal- RNPR.

[62] See, e.g., Mary Kay-RNPR (revise definition of "business opportunity" to ensure that sellers' offers to buy back unused inventory or equipment would not trigger coverage of the Rule); DSA-RNPR (same); Primerica-RNPR (definition of "equipment" in 437.1(c)(3)(i) should clarify that it is not intended to cover no-cost office space or equipment that an upstream seller offers); Pre-Paid Legal-RNPR (clarify that general advice and training about starting a new business would not trigger coverage of the Rule); Tupperware-RNPR (same); Avon-RNPR (clarify that the definition of required payment does not include payments for materials, supplies and equipment sold on a not-for-profit basis); Venable-RNPR (eliminate the word "customer" from the definitions of "business opportunity" and "provides locations, outlets, accounts, and customers"); DSA-RNPR (same); Primerica-RNPR (same).

[63] See infra Section V.C.

a business opportunity seller that provides advertising and general business advice to purchasers is not "providing locations, outlets, accounts, or customers"[64] within the meaning of the Rule.[65]

We are not persuaded by a second set of commenters who advocate creating an exemption for all MLMs by crafting a definition of multi-level marketing opportunity.[66] In the RNPR, the Commission rejected a similar suggestion that the Rule include a definition of "pyramid scheme" that would exclude legitimate MLMs from coverage while ensuring pyramid schemes remained covered.[67] The Commission reasoned that any definition of "pyramid scheme" would provide bad actors with a road map for restructuring their businesses to skirt the definition, at least facially, and thereby provide them with a safe harbor that could undercut law enforcement efforts. Similarly, we believe that any definition of "multi-level marketing opportunity" would allow fraudulent business opportunity sellers to manipulate their corporate structure to evade coverage by the Rule.

MLM industry commenters also suggest limitations on the Rule by granting a safe harbor to exempt firms that require very low registration fees;[68] firms that offer refunds on inventory purchases;[69] firms that are publicly-traded;[70] firms that have a high net worth;[71] or firms that are

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64 See proposed section 437.1(m).

65 See infra Section V.M.

66 DSA-RNPR; Babener-RNPR; Tupperware-RNPR.

67 73 Fed. Reg. at 16,119.

68 See, e.g., Babener-RNPR; Pre-Paid Legal-RNPR.

69 See, e.g., Pre-Paid Legal-RNPR; Tupperware-RNPR; IBA-RNPR.

70 Id.

71 See, e.g., IBA-RNPR.

members of a self-regulatory body, such as the Direct Selling Association ("DSA").[72] These are not novel suggestions; each was also made in response to the INPR. In the RNPR, the Commission concluded that none of these factors is determinative of whether a company is, in fact, a pyramid scheme or otherwise engaged in deceptive conduct, and that the effort to craft a

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[72] See, e.g., DSA-RNPR.

[73] 73 Fed. Reg. at 16,119.

[74] See, e.g., Telemarketing Sales Rule ("TSR"), 16 CFR 310; Franchise Rule, 16 CFR 436.

any relevant comments received in response to the RNPR, as well as the staff's analysis and recommendation, is summarized below.

A. Proposed Section 437.1(a): Action

1. Background

Proposed section 437.3(a)(3) would require the disclosure of material information about certain civil or criminal actions[75] involving the business opportunity seller, its directors, and

[75] Proposed section 437.3(a)(3) would require disclosure of "any civil or criminal action for misrepresentation, fraud, securities law violations, or unfair or deceptive practices, including violations of any FTC Rule."

[76] The proposed Rule would capture "any sales managers, or any individual who occupies a position or performs a function similar to an officer, director, or sales manager of the seller." See proposed section 437.3(a)(3)(i)(c).

risk investment."[77] Disclosure of litigation history is also required under the Amended Franchise Rule and the Interim Business Opportunity Rule.[78]

During the Business Opportunity Workshop, a panelist representing the U.S. Department of Justice suggested that bankruptcy is another type of legal action that should be disclosed to potential purchasers because a bankruptcy filing could be a red flag warning of potential risk associated with the business opportunity.[79] A panelist from the Maryland Attorney General's Office disagreed, arguing that this additional disclosure would not benefit potential business opportunity purchasers because, in his experience, fraudulent business opportunities do not typically file for bankruptcy protection.[80] Instead, in the panelist's experience, they shutter the business and reopen as an entirely new fraudulent entity. Another panelist posited that disclosure of the existence of a bankruptcy by the business opportunity or its key personnel was not likely to identify fraudulent or problematic business opportunities that would not already be identified through the existing proposed categories of legal actions.[81]

The staff is not persuaded that disclosure of information concerning bankruptcy would significantly aid potential buyers in identifying a fraudulent offering. Based on a review of the FTC's law enforcement history, we agree that fraudulent business opportunity sellers who run

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[77] 73 Fed. Reg. at 16,125.

[78] 16 CFR 436.5(c); 16 CFR 437.1(a)(4).

[79] Jost, June 09 Tr at 32. A second panelist (Taylor, June 09 Tr at 35), and a commenter (Brooks-Workshop comment) agreed that existence of a bankruptcy might be relevant to a potential purchaser.

[80] Cantone, June 09 Tr at 37.

[81] MacLeod, June 09 Tr at 33.

into law enforcement or other trouble tend to reopen under new company names.[82] The disclosure of a prior bankruptcy could, therefore, lead potential purchasers to avoid the honest seller that fell upon hard times, but invest with the dishonest seller that never filed for bankruptcy, but instead continued to operate under a new name. We also agree that disclosing the existence of a bankruptcy filing is not likely to identify additional fraudulent business opportunities that would not otherwise be identified through the disclosure of actions in the proposed definition. Finally, in the INPR, the Commission specifically requested comment on whether the proposed categories of legal actions should be expanded to include bankruptcy,[83] but this request generated no substantive comment. We agree with the Commission's conclusion that the categories of legal action proposed in the RPBOR will aid consumers in identifying risks associated with the business opportunity, and therefore, do not recommend expanding the scope of 437.3(c)(3)(i) to require the disclosure of bankruptcy filings. We note, however, that some state administrative proceedings result in parties entering into assurances of voluntary compliance, while other states refer to such orders as assurances of discontinuance. Accordingly, the staff recommends adding "assurance of discontinuance" to the categories of legal actions enumerated in the proposed definition.

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[82] See, e.g., FTC v. Nat'l Vending Consultants, Inc., CV-S-05-0160-RCJ-PAL (D. Nev. complaint filed Feb. 7, 2005) (business under federal order began operating under new company name).

[83] 71 Fed. Reg. at 19,085 (Question 14).

B. Proposed Section 437.1(b): Affiliate

1. Background

Proposed section 437.3(a)(3) would require a business opportunity seller to disclose not only litigation in which it was named as a party, but any litigation naming any of the seller's affiliates or prior businesses. Proposed section 437.1(b) would define the term "affiliate" to mean: "an entity controlled by, controlling, or under common control with a business opportunity seller." This definition would also cover litigation involving a parent or subsidiary of the business opportunity seller.

2. The record and recommendation

Apart from comments pertaining specifically to the MLM industry, which were discussed in the RNPR,[84] the Commission's proposed definition of "affiliate" received no comment. The staff recommends, therefore, that the definition of "affiliate" be adopted in the form proposed in the RPBOR.

C. Proposed Section 437.1(c): Business Opportunity

1. Background

The RNPR proposed a definition of "business opportunity" that significantly narrowed the definition originally proposed in the INPR. As explained in Section I.A., the IPBOR was designed to be broad enough to cover the sale of virtually any type of business opportunity, including two types in particular that had traditionally fallen outside the scope of the Original Franchise Rule – work-at-home and pyramid marketing schemes. As explained more fully in the INPR, these two schemes have been shown by the Commission's law enforcement experience and

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[84] 73 Fed. Reg. at 16,125 n.197.

consumer complaints to be sources of prevalent and persistent problems.[85] The Commission has traditionally used Section 5 of the FTC Act to challenge these schemes.[86]

In order to reach these schemes, the INPR proposed a broad definition of "business opportunity" that comprised three elements: (1) a solicitation to enter into a new business; (2) payment of consideration, directly or indirectly through a third party; and (3) the making of either an "earnings claim" or an offer to provide "business assistance."[87] The Commission incorporated the broad definition of "earnings claims" from the Original Franchise Rule,[88] recognizing that the most frequent allegation in its law enforcement actions against business opportunity frauds has been that the seller made false and unsubstantiated earnings claims. Furthermore, the IPBOR's definition of "business assistance" would have included assistance in the form of "tracking or paying, or purporting to track or pay, commissions or other compensation based upon the purchaser's sale of goods or services or recruitment of other persons to sell goods or services."[89] The Commission noted that many pyramid schemes offer this type of assistance, purporting to compensate participants not only for their own product sales but also for sales made by their

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[85] In 2009, pyramid schemes generated nearly 2,500 consumer complaints, while work-at-home schemes generated nearly 8,000 complaints.

[86] Many of these schemes fell outside the ambit of the Franchise Rule because: (1) the purchase price was less than $500, the minimum payment necessary to trigger coverage under the Original Franchise Rule; (2) required payments were primarily for inventory, which did not count toward the $500 monetary threshold; (3) the scheme did not offer location or account assistance; or (4) the scheme involved the sale of products to the business opportunity seller rather than to end-users, a further limitation on coverage under the Original Franchise Rule. See 71 Fed. Reg. at 19,055, 19,059.

[87] See IPBOR, 437.1(d)(3).

[88] IPBOR, 437.1(h).

[89] IPBOR, 437.1(c)(iv).

would have imposed greater burdens on the MLM industry than other types of business opportunity sellers without sufficient countervailing benefits to consumers.[97]

To cure these problems, the Commission proposed a tailored definition of "business opportunity" intended to reach those business opportunities that have, in the Commission's law enforcement experience, persistently caused substantial consumer injury.[98] The changes to the IPBOR's definition of "business opportunity" were three-fold. First, the RPBOR definition of "business opportunity" would have included those opportunities for which "the prospective purchaser makes a required payment." The term "required payment" was defined to exclude payments for inventory at bona fide wholesale prices. Second, the RPBOR definition would have eliminated two types of "business assistance" that formerly would have triggered the Rule's strictures and disclosure obligations, namely tracking payments and providing training. Third, unlike the IPBOR, the RPBOR would not have linked the definition of "business opportunity" to the making of an earnings claim.

The RPBOR incorporated and expanded the definition of "business opportunity" used in the Original Franchise Rule and the Interim Business Opportunity Rule to cover the types of

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[97] See 73 Fed. Reg. at 16,120. For instance, in the RNPR, the Commission acknowledged one characteristic of the MLM model that could undermine the utility of requiring MLMs to disclose a list of prior purchasers. Specifically, prior purchasers on the reference list likely would stand to receive a financial benefit if they could convince a prospect to enroll into their downline. Under these circumstances, information provided by such a reference might not be a reliable indicator of the potential risk and rewards of enrollment. The Commission further acknowledged that the varied and complex structure of MLMs would make it exceedingly difficult to make an accurate earnings disclosure and likely would require different disclosures for different levels of participation in the company.

[98] These include business opportunities promoting vending machine, rack-display, work-at-home, medical billing, and 900-number schemes, among others. 73 Fed. Reg. at 16,121.

schemes that had evaded coverage by those rules.[99] Accordingly, section 437.1(c) of the RPBOR would have defined the term "business opportunity" as follows:

(c) Business opportunity means:

(1) A commercial arrangement in which the seller solicits a prospective purchaser to enter into a new business; and

[99] See supra note 85.

coverage are sufficient to exclude from the rule traditional distributor relationships[100] that had been inadvertently swept in.[101]

2. The record and recommendation

The majority of comments in response to the RNPR focus on whether the revisions to the proposed Rule would capture MLMs,[102] and as noted above, the staff recommends against creating a blanket exemption for MLMs. The remaining comments focus on two issues. First, some commenters expressed concern that the buy-back provision, set forth in section 437.1(c)(3)(iii), would sweep in MLM companies that offer to buy back their distributors' unused inventory.[103] These commenters suggested amending this provision to strike the word "provides" from section 437.1(c)(iii), so that the definition of "business opportunity" would clearly not

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[100] For example, commenters to the INPR noted that the IPBOR would cover "manufacturers, suppliers and other traditional distribution firms that have relied on the bona fide wholesale price exclusion to avoid coverage" under the Rule. Sonnenschein-INPR. The Cosmetic, Toiletry and Fragrance Association posited that the IPBOR would cover the relationship between a manufacturer and an independent contractor who sells the product to beauty supply companies, salons, and others. CTFA-INPR; see also LHD&L-INPR at 2 (noting that the IPBOR could cover the relationship between a manufacturer and a regional distributor of products).

[101] 73 Fed. Reg. at 16,133.

[102] DSA-RNPR. In addition, the Commission received more than 40 comments from various MLMs that expressed support and concurrence with DSA's comments. See, e.g., Big Ear-RNPR; Jafra Cosmetics-RNPR; Lia Sophia-RNPR; Longaberger-RNPR; Princess House-RNPR; Shaklee-RNPR. Some commenters expressed disappointment that the Commission proposed to exclude MLMs from coverage by the Rule. See, e.g., CAI-RNPR; Durand-RNPR; PSA-RNPR; Aird-RNPR (Rebuttal); Parrington-RNPR. For the reasons identified in supra Section IV.C., we agree with the Commission's decision to narrow the scope of the Rule to avoid broadly sweeping in MLMs.

[103] DSA requires that its members offer to buy back, at 90% of the salesperson's cost, all resalable inventory and other sales materials. DSA-INPR at 35.

encompass a return of unused materials or merchandise.[104] We are not persuaded that this change is necessary. The Commission made clear in the RNPR that proposed 437.1(c)(iii) was intended to capture work-at-home business opportunities in which the seller provides the purchaser with some supplies and the purchaser converts those supplies into a product or other "good" for repurchase by the seller or other person.[105] We believe it would require a labored reading of this section to suggest that the word "provides" means "to return unused inventory the purchaser bought from the seller but was not able to sell." Moreover, the Commission has explicitly stated that this provision "would not include the offer to buy back inventory or equipment needed to start a business."[106]

Second, some commenters argued that section 437.1(c)(i) would inadvertently cover entities that offer, at no cost to purchasers, the use of office space and equipment for the operation of the purchasers' business.[107] These commenters were concerned that such offers could be construed under proposed section 437.1(c)(3)(i) to be providing "locations for the use or operation of equipment . . . on premises neither owned nor leased by the purchaser." In the

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[104] DSA-RNPR at 6 n.14 (noting that "the buy-back provision is the cornerstone of the DSA's self regulatory regime and a valuable protection for individual direct sellers"); Mary Kay-RNPR at 6; Babener-RNPR; Melaleuca-RNPR.

[105] See 73 Fed. Reg. at 16,123.

[106] See 71 Fed. Reg. at 19,062.

[107] For example, Primerica, an MLM that sells insurance products and services, requires that its regional managers provide at no cost to "downline" sales agents the use of office space, supplies, and equipment (such as computers and printers) for the operation of his or her business. Primerica noted that as a practical matter, it must require this assistance, as the regulatory structure in which Primerica operates necessitates that regional managers exercise compliance oversight functions with respect to the agents in their downlines. Primerica-RNPR; see also Avon-RNPR; Tupperware-RNPR.

RNPR, the Commission stated that this provision was intended to capture fraudulent vending machine and rack display schemes,[108]

[108] 73 Fed. Reg. at 16,123 (citing FTC v. Am. Entm't Distribs., No. 04-22431-CIV-Martinez (S.D. Fla. 2004); FTC v. Advanced Pub. Commc'ns Corp., No. 00-00515-CIV-Ungaro-Benages (S.D. Fla. 2000); FTC v. Ameritel Payphone Distribs., Inc., No. 00-0514-CIV-Gold (S.D. Fla. 2000); FTC v. Mktg. and Vending Concepts, No. 00-1131 (S.D.N.Y. 2000)).

[109] FTC v. Equinox, Int'l, No. CV-S-99-0969-JAR-RLH (D. Nev. 1999).

[110] The staff additionally recommends that the Commission strike the final clause of this provision of the RPBOR – "on premises neither owned or leased by the purchaser." The clause is superfluous, as a buyer would never need a seller's assistance in identifying locations that the buyer already owns or leases.

D. Proposed Section 437.1(d): Designated Person

1. Background

The term "designated person" appears in the definition of "business opportunity" in section 437.1(c)(3), which refers to representations made by the seller or by "one or more designated persons." It is used to ensure coverage of those transactions in which a seller refers a purchaser to a third party for the provision of locations, accounts, buy-back services, etc., as specified in sections 437.1(c)(3)(i)-(iii).[111] Proposed section 437.1(d) would define the term "designated person" to mean "any person, other than the seller, whose goods or services the seller suggests, recommends, or requires that the purchaser use in establishing or operating a new business, including, but not limited to, any person who finds or purports to find locations for equipment."[112]

2. The record and recommendation

In response to the RNPR, one commenter argued that the current proposed definition of "designated person" is overbroad and that its application would result in many multi-level marketing opportunities being swept into the Rule.[113] For instance, if an MLM company requires its managers to provide the use of office space, equipment and supplies, and general business

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[111] In other words, the definition and use of "designated person" is designed to close a potential loophole. For example, a fraudulent vending machine route seller would not be able to circumvent the Rule by representing to a prospective purchaser that a specific locator will place machines for the purchaser. The referral to a third party would be sufficient to bring the transaction within the ambit of the Rule. See 71 Fed. Reg. at 19,064.

[112] This approach is consistent with the Amended Franchise Rule's analogous definitional elements, extending the scope of that rule's coverage to reach transactions in which the franchisor provides to the franchisee the services of a person able to secure the retail outlets, accounts, sites, or locations. 16 CFR 436.1(j).

[113] Primerica-RNPR at 11.

advice to new agents (and presumably to describe these types of assistance to prospective purchasers as part of a sales pitch),[114] it could be argued that the company would be covered by the Rule.[115] The commenter offered several suggested revisions to resolve this problem, one of which was to specify that "designated person" does not include entities that receive no payment from the purchaser in order to receive the services provided.[116] The staff determined that an alternate resolution is more appropriate – namely the modification to the definitions of "business opportunity"

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[114] The MLM company compensates managers for this service; there is no cost to down-line agents. Primerica-RNPR at 11.

[115] Id.

[116] Id. at 13.

[117] See supra Section V.C.

[118] See infra Section V.M.

[119] The Franchise Rule contains a comparable provision. See 16 CFR 436.1(a).

"clear." Similarly, required information such as the number and percentage of prior purchasers obtaining a represented level of earnings would not be "conspicuous" if set in small type, printed in a low-contrast ink, or buried amid extraneous information.

2. The record and recommendation

The Commission's proposed definition of "disclose or state" received no comment. The staff agrees that this definition will ensure that potential purchasers are provided with information that will assist them in making an informed purchasing decision. The staff recommends, therefore, that the definition of "disclose or state" be adopted in the form proposed in the RPBOR.

F. Proposed Section 437.1(f): Earnings Claim

1. Background

As noted above, the Rule's key feature is the disclosure document, which provides potential purchasers of a business opportunity with four items of material information before they pay any money or other consideration or execute a contract. The RPBOR would have required written disclosure of all "earnings claims" made by the seller. This would allow a potential purchase to compare a seller's written representations with any oral representations made. Proposed section 437.1(f) would have defined the term "earnings claim" as "any oral, written, or visual representation to a prospective purchaser that conveys, expressly or by implication, a specific level or range of actual or potential sales, or gross or net income or profits." It was intended to cover all variations of earnings representations that the Commission's law enforcement experience shows are associated with business opportunity fraud.[120]

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[120] 71 Fed. Reg. at 19,065.

The definition would also provide two examples of communications that constitute earnings claims. The first of these examples would describe common types of potentially fraudulent earnings claims: "a chart, table, or mathematical calculation that demonstrates possible results based upon a combination of variables." This example was intended to clarify that sales matrices that purport to show income from an array of "vends" per day from a vending machine, for example, would constitute an "earnings claim" under the proposed Rule.[121]

The second example would incorporate the principle, as expressed in the Interpretive Guides to the Original Franchise Rule, that "any statements from which a prospective purchaser can reasonably infer that he or she will earn a minimum level of income" would constitute an

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[121] Id.

[122] Final Interpretive Guides Accompanying the Franchise Rule ("Interpretive Guides"), 44 Fed. Reg. 49,966 (Aug. 24, 1978).

[123] See infra Section VIII.

[124] Planet Antares stated that the earnings claim definition was so broad that "it would be difficult to imagine how a business opportunity seller could avoid making an earnings claim." It offered no suggestions about how to narrow the definition, however.

[125] 71 Fed. Reg. at 19,065.

[126] Id.

[127] E.g.

Accordingly, proposed section 437.1(g) would define the term "exclusive territory" as "a specified geographic or other actual or implied marketing area in which the seller promises not to locate additional purchasers or offer the same or similar goods or services as the purchaser through alternative channels of distribution." According to the Commission, this definition reflects the common industry practice of establishing geographically delimited territories – such as a city, county, or state borders – as well as other marketing areas, such as those delineated by population.[128] It would include both representations that other business opportunity purchasers will not be allowed to compete with a new purchaser within the territory, as well as representations that the business opportunity seller itself or other purchasers will not compete with the new purchaser through alternative means of distribution, such as through Internet sales.

The definition would also cover implied marketing areas, such as representations that the seller or other operators will not compete with the purchaser, without delineating a specific territory, or stating a vague or undefined territory, such as "in the metropolitan area" or "in this region." The Commission concluded that if untrue, any of these kinds of representations can mislead a prospect about the likelihood of his or her success.[129]

2. The record and recommendation

The Commission's proposed definition of "exclusive territory" received no comment. The staff agrees with the Commission's analysis, and recommends, therefore, that the definition of "exclusive territory" be adopted in the form proposed in the RPBOR.

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[128] 71 Fed. Reg. at 19,065.

[129] Id.

H. Proposed Section 437.1(h): General Media

1. Background

The term "general media" would appear in proposed section 437.4(b), which would prohibit business opportunity sellers from making unsubstantiated earnings claims in the "general media."[130] Proposed section 437.1(h) would define "general media" to mean: "any instrumentality through which a person may communicate with the public, including, but not limited to, television, radio, print, Internet, billboard, website, and commercial bulk email."[131] .

2. The record and recommendation

The Commission's proposed definition of "general media" received no comment. The Commission intended that this definition be broad enough to include traditional advertising, as well as new and emerging technologies.[132] Due to the explosive growth of advertising through mobile devices, the staff recommends adding the phrase "mobile communications" to the list of

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[130] This proposed provision was based on an analogous provision in the Franchise Rule, 16 CFR 436.1(e). The Commission has alleged unsubstantiated earnings claims through the general media in numerous cases, e.g., FTC v. Wealth Sys., Inc., No. CV 05 0394 PHX JAT (D. Ariz. 2005); United States v. Am. Coin-Op Servs., Inc., No. 00-0125 (N.D.N.Y. 2000); United States v. Cigar Factory Outlet, Inc., No. 00-6209-CIV-Graham-Turnoff (S.D. Fla. 2000); United States v. Emily Water & Beverage Co., Inc., No. 4-00-00131 (W.D. Mo. 2000); and United States v. Greeting Card Depot, Inc., No. 00-6212-CIV-Gold (S.D. Fla. 2000).

[131] See Interpretative Guides, 44 Fed. Reg. at 49,984-84 (earnings claims made "for general dissemination" include "claims made in advertising (radio, television, magazines, newspapers, billboards, etc.) as well as those contained in speeches or press releases"). We also note that the Interpretive Guides recognize several exemptions to the general media claim, such as claims made to the press in connection with bona fide news stories, as well as claims made directly to lending institutions. Id. The Commission proposed that future Compliance Guides to the new Business Opportunity Rule retain these standard general media claims exemptions. See 71 Fed. Reg. at 19,065. The staff agrees with the Commission's proposal.

[132] 71 Fed. Reg. at 19,065.

J. Proposed Section 437.1(j): New Business

1. Background

The term "new business" would appear in proposed section 437.1(c), which would set forth the definition of the term "business opportunity." As discussed in supra Section V.C., the first of three elements comprising a "business opportunity" is a "solicitation to enter into a new business." This prong would distinguish the sale of a business opportunity from the ordinary sale of products and services.[137] "New business" was defined in section 437.1(i) of the RPBOR[138] as "a business in which the prospective purchaser is not currently engaged, or a new line or type of business." Thus, the definition covers not only the establishment of a new business, but also entry into a new "line or type of business."[139] The Commission's intent was to cover sales of business opportunities to persons who may already be in a business, because it is reasonable to assume that an existing businessperson could be defrauded like any other consumer when expanding his or her business to include new products or services not currently offered for sale.[140] The Commission concluded that in such instances, the veteran businessperson may need the proposed Rule's protections as much as a novice.[141]

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137 71 Fed. Reg. at 19,066.

138 Because of the addition of two proposed new definitions – "material" at 437.1(i), and "signature or signed" at 437.1(r) – the numbering designation of section 437.1 of the proposed Final Rule does not match that in the RPBOR. See Attachment C for a redline of the proposed Final Rule and the RPBOR.

139 71 Fed. Reg. at 19,066.

140 For example, an existing tire business could purchase a vending machine route, or a beverage vending machine route owner could purchase an envelope stuffing opportunity.

141 71 Fed. Reg. at 19,066.

2. The record and recommendation

The Commission's proposed definition of "new business" received no comment. The staff agrees with the Commission's analysis and recommends, therefore, that the definition of "new business" be adopted in the form proposed in the RPBOR.

K. Proposed Section 437.1(k): Person

1. Background

Proposed section 437.1(k) would define the term "person," a term used in many of the proposed Rule's definitional or substantive provisions.[142] As in the Amended Franchise Rule and Interim Business Opportunity Rule, the term means "an individual, group, association, limited or general partnership, corporation, or any other entity."[143] The term "person" is to be read broadly to refer to both natural persons, businesses, associations, and other entities. Where the Rule refers to a natural person only, it uses the term "individual."[144]

2. The record and recommendation

The Commission received no comments in response to the RNPR related to the proposed definition of person. The staff recommends, therefore, that the definition of "person" be adopted in the form proposed in the RPBOR.

L. Proposed Section 437.1(l): Prior Business

1. Background

As discussed in infra Section VII.C., section 437.3(a)(3) of the proposed Final Rule would

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142 E.g., proposed sections 437.1(n); 437.6(q).

143 See 16 CFR 436.1(n); 437.2(b).

144 71 Fed. Reg. at 19,066.

require business opportunity sellers to disclose litigation in which they have been involved, including through their affiliates or any prior businesses. Proposed section 437.1(k) of the RPBOR would have defined "prior business" to mean:

(1) a business from which the seller acquired, directly or indirectly, the major portion of the business' assets, or

(2) any business previously owned or operated by the seller, in whole or in part, by any of the seller's officers, directors, sales managers, or by any other individual who occupies a position or performs a function similar to that of an officer, director, or sales manager of the seller.

This definition was intended to include not only an entity from which a seller acquired the major portion of the seller's assets, but also businesses that the seller previously owned or operated, but that had ceased operations.[145] This coverage is necessary because it is the Commission's law enforcement experience that sellers of fraudulent business opportunities frequently ply their trade through multiple companies simultaneously or sequentially, disappearing in order to avoid detection, and then reemerging in some new form or in a different part of the country under new names.[146] Accordingly, a broad definition of "prior business" is necessary to capture all of a seller's prior operations.[147]

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[145] The proposed definition of "prior business" is broader than the definition of "predecessor" found in the Amended Franchise Rule, which covers only an entity from which a seller acquired the major portion of the seller's assets. See 16 CFR 436.1(p).

[146] E.g., FTC v. Nat'l Vending Consultants, Inc., No. 05-0160 (D. Nev. 2005); FTC v. Joseph Hayes, No. 4:96CV06126 SNL (E.D. Mo. 1996); FTC v. O'Rourke, No. 93-6511-CIV-Ferguson (S.D. Fla. 1993); FTC v. Inv. Dev. Inc., No. 89-0642 (E.D. La. 1989).

[147] 71 Fed. Reg. at 19,066.

2. The record and recommendation

The Commission's proposed definition of "prior business" received no comment. The term is used to identify the legal actions that a seller must disclose, including any legal actions pertaining to a "prior business of the seller."[148] On its own initiative, the staff notes that the second prong of the "prior business" definition contains a redundancy that renders the rule unclear. Namely, the second prong of the definition of "prior business" refers not only to the seller but to the seller's key personnel. It thus repeats the language in proposed section 437.3(a)(3)(i)(C), which requires the disclosure of legal actions of certain key personnel of the seller. To eliminate any potential confusion, the staff recommends that the second prong of the "prior business" definition eliminate reference to "any of the seller's officers, directors, sales managers, or by any other individual who occupies a position or performs a function similar to that of an officer, director, or sales manager of the seller."

M. Proposed Section 437.1(m): Providing Locations, Outlets, Accounts, or Customers

1. Background

The proposed definition of "providing locations, outlets, accounts, or customers" relates to the third prong of the "business opportunity" definition, which requires a representation that the seller will provide assistance in the form of securing locations or accounts, or by buying back goods produced by the purchasers.[149] The Commission's law enforcement history shows that fraudulent sellers will often falsely promise to assist the purchaser in obtaining the key

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[148] Proposed section 437.3(a)(3)(i)(B).

[149] See supra Section V.C.

ingredients necessary for the success of the proposed business: a source of customers, locations, outlets, or accounts. Location assistance is the hallmark of fraudulent vending machine and rack display route opportunities,[150] while the provision of accounts or customers is typical of medical billing schemes.[151] In such schemes, the seller itself may purport to secure locations or accounts, or may represent that third parties will do so. Proposed section 437.1(l) of the RPBOR defined "providing locations, outlets, accounts, or customers" as:

> furnishing the prospective purchaser with existing or potential locations, outlets, accounts, or customers; requiring, recommending, or suggesting one or more locators or lead generating companies; providing a list of locator or lead generating companies; collecting a fee on behalf of one or more locators or lead generating companies; offering to furnish a list of locations; or otherwise assisting the prospective purchaser in obtaining his or her own locations, outlets, accounts, or customers.[152]

The IPBOR had included two additional categories of assistance that would have triggered coverage by the Rule – advice or training in the promotion, operation or management of a new

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[150] E.g., FTC v. Am. Entm't Distribs., No. 04-22431-CIV-Martinez (S.D. Fla. 2004); FTC v. Advanced Pub. Commc'ns Corp., No. 00-00515-CIV-Ungaro-Benages (S.D. Fla. 2000); FTC v. Ameritel Payphone Distribs., Inc., No. 00-0514-CIV-Gold (S.D. Fla. 2000); FTC v. Mktg. and Vending Concepts, No. 00-1131 (S.D.N.Y. 2000).

[151] E.g., FTC v. Mediworks, Inc., No. 00-01079 (C.D. Cal. 2000); FTC v. Home Professions, Inc., No. 00-111 (C.D. Cal. 2000); FTC v. Data Med. Capital, Inc., No. SACV-99-1266 (C.D. Cal. 1999); see also FTC v. AMP Publ'n, Inc., No. SACV-00-112-AHS-ANx (C.D. Cal. 2000).

[152] The Commission has noted that the proposed definition is intended to capture offers to provide locations that have already been found, as well as offers to furnish a list of potential locations; and includes not only directly furnishing locations, but also "recommending to a prospective purchaser specific locators, providing lists of locators who will furnish the locations, and training or otherwise assisting prospects in finding their own locations." 71 Fed. Reg. at 19,066.

[153] 71 Fed. Reg. at 19,087.

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[162] E.g., Avon-RNPR at 3 (noting that this practice is designed to help potential

create an exception when the assistance offered by the seller is limited to advice or training.[168] Some commenters suggested eliminating the concept of "potential customers" from the scope of the "otherwise assisting" language.[169]

[168] Pre-Paid Legal-RNPR.

[169] Mary Kay-RNPR at 7 (as an alternative Mary Kay suggests that in the commentary to the Final Rule, the Commission make clear that passing on ad hoc referrals of customers who contact the company directly would not trigger this provision).

[170] Melaleuca-RNPR.

[171] See, e.g., FTC v. Medical Billers Network, Inc., No. 05-CV-2014 (S.D.N.Y. 2005); FTC v. Medical-Billing.com, Inc., No. 3-02CV0702CP (N.D. Tex. 2002); FTC v. Electronic Medical Billing, Inc., No. SACV02-368 AHS (C.D. Cal. 2002). See also FTC v. Star Publishing Group, Inc., No. 00cv-023D (D. Wyo. 2000) (offering everything necessary to earn money processing HUD refunds); FTC v. AMP Publications, Inc., SACV-00-112-AHS (C.D. Cal. 2000) (offering to provide list of companies in need of consumer's home-based computer services).

recommend that the Commission continue its long-standing policy of analyzing the significance of assistance in the context of the specific business opportunity, focusing on whether the seller's offer is "reasonably likely to have the effect of inducing reliance on [the seller] to provide a prepackaged business."[172]

Although the staff does not recommend eliminating the word "customers" from the definition of "providing locations, outlets, accounts, or customers," the staff recommends adding language to address the concern that the definition could be read more broadly than the Commission intends. The RNPR makes it clear that the "otherwise assisting" provision of the definition was not intended to apply to advertising and no-cost offers of general business advice and training described by the various commenters.[173] A short proviso to the "otherwise assisting" clause would add clarity, and therefore, we recommend adding to the final clause of this definition the phrase "provided, however, that advertising and general advice about business development and training shall not be considered as 'providing locations, outlets, accounts, or customers.'"[174]

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[172] Staff Advisory Opinion 95-10, Business Franchise Guide, (CC) ¶ 6475 (1995) (citing Original Franchise Rule, Statement of Basis and Purpose, 43 Fed. Reg at 59,705).

[173] 73 Fed. Reg. at 16,123.

[174] For example, this new proviso makes even clearer that giving advice about how to demonstrate products, complete product order forms and process payments, and how to process returns (Tupperware-RNPR); or providing brand advertising and generalized training in customer and business development (Primerica-RNPR), would not be considered as "providing locations, outlets, accounts, and customers."

N. Proposed Section 437.1(n): Purchaser

1. Background

Proposed section 437.1(m) of the RPBOR would have defined the term "purchaser" to mean "a person who buys a business opportunity." By operation of the definition of "person,"[175] a natural person, as well as any of various entities, would qualify as a business opportunity purchaser.

2. The record and recommendation

The Commission's proposed definition of "purchaser" received no comment. The staff recommends, therefore, that the definition of "purchaser" be adopted in the form proposed in the RPBOR.

O. Proposed Section 437.1(o): Quarterly

1. Background

To ensure accuracy and reliability of disclosures, proposed section 437.3 (instructions for completing the disclosure document) requires sellers to revise their disclosures at least "quarterly."[176] The definition of "quarterly" proposed in the RPBOR would have set forth a bright line rule that is easy to follow and that would ensure uniformity of disclosures: "quarterly" means "as of January 1, April 1, July 1, and October 1." Thus, the proposed Rule would require sellers to update their disclosure by those specific dates each year.

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[175] Supra Section V.K.

[176] Proposed section 437.3(b) requires that until a seller has at least 10 purchasers, the list of references must be updated monthly.

2. The record and recommendation

The Commission's proposed definition of "quarterly" received no comment. The staff recommends, therefore, that the definition of "quarterly" be adopted in the form proposed in the RPBOR.

P. Proposed Section 437.1(p): Required Payment

1. Background

The RPBOR would have reached only business opportunities in which the prospective purchaser makes a "required payment." The RPBOR would have defined "required payment" to mean:

> all consideration that the purchaser must pay to the seller or an affiliate, either by contract or by practical necessity, as a condition of obtaining or commencing operation of the business opportunity. Such payment may be made directly or indirectly through a third-party. A required payment does not include payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices for resale or lease.

The definition of "required payment" is substantially similar to that employed in the Franchise Rule, but it also includes language that reaches situations where a payment is made directly to a seller or indirectly through a third party. The Commission reasoned that without such a provision, fraudulent business opportunity sellers could circumvent the Rule by requiring payment to a third party with which the seller has a formal or informal business relationship.[177]

The last sentence of the definition excludes payments for reasonable amounts of inventory at bona fide wholesale prices. This effectuates the Commission's determination that traditional

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[177] 73 Fed. Reg. at 16,122.

product distribution arrangements should not be covered by the Business Opportunity Rule.[178] Manufacturers, suppliers, and other traditional distribution firms "have relied solely on the bona fide wholesale price exclusion to avoid coverage as a franchise."[179] The IPBOR had eliminated the inventory exemption in an attempt to bring pyramid schemes that engaged in "inventory loading" within the ambit of the Rule.[180] However, as discussed in Section IV.C., the Commission has determined that challenging such practices in targeted law enforcement actions brought under Section 5 of the FTC Act is a more cost-effective approach than attempting to address pyramid schemes as proposed in the IPBOR.[181]

2. The record and recommendation

In response to the RNPR, MLM industry commenters urged the Commission to expand the inventory exemption to additionally exempt sales of business materials, supplies, and equipment to purchasers on a not-for-profit basis.[182] Commenters stated that the MLM business

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178 Id.

179 Id.

180 71 Fed. Reg. at 19,055.

181 73 Fed. Reg. at 16,122.

182 Commenters suggested various ways to expand the exemption. See DSA-RNPR at 4 (recommending that the exemption include "business materials, supplies, and equipment sold on a not-for-profit basis"); Mary Kay-RNPR at 2 (same); Avon-RNPR at 2 (exemption should extend to "sales aid or kits at cost"); Tupperware-RNPR at 4 (required payment should not include payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices, which may be used for resale, lease or display, or payments for products for personal use). Also, one commenter expressed concern that under the proposed definition, voluntary payments made to third parties unaffiliated with the seller for items or equipment to be used in a purchaser's business could be considered a "required payment." See IBA-RNPR at 4. We do not agree. By its very words, the definition is not intended to capture payments of the type described by the commenter, as such payments are not made directly or indirectly to the seller.

[183] DSA-RNPR at 4; Tupperware-RNPR at 2 (explaining that it requires purchase of a starter Business Kit that contains a selection of Tupperware products sold below retail value for demonstration at parties); Mary Kay-RNPR at 4 (initial sales kit, sold to consultant at below cost, is used to demonstrate products to customers); Avon-RNPR (sales kits, which explain business fundamentals and provide necessary equipment such as sales brochures, sales receipts, a tote bag, and product samples, are sold to independent sales representatives without a profit).

[184] Tupperware-RNPR (products in starter Business Kit sold to sales consultants for $79 or $129 have retail value of $350 and $550 respectively).5o0M0 or $72.32 108 211.9801 Tm0 5c0 Tw(184)

[187] See supra

[191] The proposed definition would effectively permit business opportunity sellers to comply with the proposed Rule electronically, consistent with the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7001. See 71 Fed. Reg. at 19,067 n.142; see also TSR, 16 CFR 310.3(a)(3)(i); Franchise Rule, 16 CFR 436.3(u) (containing similar

S. Proposed Section 437.1(s): Written or In Writing

1. Background

The RPBOR defined the terms "written" or "in writing," which are used throughout the proposed Rule[193] to mean "any document or information in printed form or in any form capable of being downloaded, printed, or otherwise preserved in tangible form and read. It includes: type-set, word processed, or handwritten documents; information on computer disk or CD-ROM; information sent via email; or information posted on the Internet. It does not include mere oral statements." This definition was designed to capture information stored on computer disks, CD-ROMs, or through new or emerging technologies, as well as information sent via email or posted on the Internet. Nevertheless, the definition seeks a balance, attempting to minimize compliance costs while at the same time preventing fraud. To that end, the definition would make clear that all electronic media must (being downloaded, printed, or otherwice)]TJT*0008 Tc-.0008 Twble of

193 E.g., RPBOR sections 437.2, 437.3(a), 437.4(a).

194 71 Fed. Reg. at 19,067.

[196] See 71 Fed. Reg. at 19,067.

[197] See 16 CFR 437.2(g).

[198] See

sufficient time to review the disclosure information and conduct due diligence, and recommends, therefore, that section 437.2 be adopted in the form proposed in the RPBOR.

VII. Proposed Section 437.3: Disclosure Document

Section 437.3(a) of the RPBOR instructed how to prepare the basic disclosure document, identified the categories of required disclosure, and specified what information must be included in each of these categories. Section 437.3(a) would require that sellers present to a prospective purchaser information about the seller's litigation history, cancellation and refund policy, earnings claims, and references[201] in "a single written document in the form and using the language set forth in Appendix A" to the Rule.[202] The Commission concluded that the single written document requirement was necessary to ensure that disclosures were not furnished in piecemeal fashion that easily could be overlooked or lost.[203] In addition, the Commission noted

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[201] Each of these substantive disclosures is discussed infra in Section VII.C.

[202] The staff recommends adding a clause to proposed section 437.3(a) requiring that if the offer for sale, sale, or promotion of a business opportunity is conducted in Spanish, the seller must provide a Spanish-language versions of the Disclosure Document and any required disclosures must also be provided in Spanish. Thus, proposed section 437.3(a) would make it an unfair or deceptive practice in violation of Section 5 of the FTC Act for any seller to "[f]ail to disclose to a prospective purchaser . . . material information in a single written document in the form and using the language set forth in Appendix A to this part; or if the offer for sale, sale, or promotion of a business opportunity is conducted in Spanish, Appendix B to this part." See infra Section IX.

[203] 71 Fed. Reg. at 19,067.

[204] Id.

follow Appendix A's form and language would constitute a violation of Section 5 of the FTC Act.[205]

Proposed section 437.3(a)(6) would require that a seller provide the potential purchaser with two copies of the disclosure document, one of which is to be signed and dated by the prospective purchaser and returned to and maintained by the seller in accordance with proposed section 437.6.[206] Proposed section 437.3(b) would make it an unfair or deceptive practice and a violation of Section 5 of the FTC Act for a seller to fail to update the required disclosures at least quarterly to reflect changes in the four require

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[205] Proposed section 437.3(a).

[206] One commenter noted that the requirement that a purchaser be provided with a second copy of the disclosure document appears inconsistent with the proposed Rule's recognition that the disclosure document can be provided to potential purchasers through electronic media. Quixtar-INPR at 27. As the definition of "written" or "in writing" makes clear, the disclosure document can be provided via electronic media. See supra Section V.C.

purchasers.[207] The Commission recognized that requiring sellers to make these extensive disclosures would likely impose significant compliance costs on covered businesses, and that many of the disclosures, which are more relevant in the context of franchise sales, are not well-suited to business opportunity sales. The Commission sought to strike the proper balance, therefore, between prospective purchasers' need for pre-sale disclosure and the burden imposed on those selling business arrangements.[208]

Thus, the Commission proposed a single-page Disclosure Document in the INPR and the RNPR. The Commission invited public comment about the form, including whether the overall presentation of information could be improved to make it more useful and understandable, and whether the four substantive sections capture the information that would most benefit potential purchasers.[209] The Commission received no comments in response to this request.

As explained in supra Section I.C., the Commission engaged a consultant with expertise in document design and comprehension to evaluate the proposed Disclosure Document to ensure that it adequately conveyed to consumers information material to the prospective business opportunity, and to determine whether the overall presentation of the information in the proposed Disclosure Document could be improved to make it more useful and understandable.[210]

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[207] These include but are not limited to information about the seller; the business background of its principals and their litigation and bankruptcy histories; the terms and conditions of the offer; statistical analyses of existing franchised and company-owned outlets; prior purchasers, including the names and addresses of at least 10 purchasers nearest the prospective buyer; and audited financial statements. Additional disclosure and substantiation provisions apply if the seller chooses to make any financial performance representations.

[208] 73 Fed. Reg. at 16,013.

[209] 73 Fed. Reg. at 16,133.

[210] See generally Macro Report.

[214] The staff received requests to serve as panelists from eight persons. We extended offers to serve as panelists to each of these individuals, three of whom declined.

[215] Kenneth Jost ("Jost"), DOJ, Office of Consumer Litigation.

[216] Dale Cantone ("Cantone"), Maryland Attorney General's Office.

[217] Jon Taylor ("Taylor"), Consumer Awareness Institute.

[218] Maureen Morrissey ("Morrissey"), Tupperware.

[219] William MacLeod ("MacLeod"). Although at the Workshop Mr. MacLeod represented only his own views, he had previously filed comment to the INPR and RNPR on behalf of Planet Antares, which markets vending machine businesses.

[220] See, e.g., Jost, June 09 Tr at 12-15 (noting that the simplicity of the form is the key to it being successful: "Having a one page document that focuses on the key issues such as legal actions, earnings claims, and references will put the most important information in the hands of the prospective purchaser"); MacLeod, June 09 Tr at 18 (same, and commending the

nearest to the prospective purchaser's location. A discussion of the record pertaining to each of the required substantive disclosures follows, along with the staff's recommendations that the Commission adopt minor changes to the proposed Rule and conforming amendments to the Disclosure Document. A copy of this proposed final Disclosure Document is included as Attachment D to this Report.

1. Proposed section 437.3(a)(2): Earnings claims

As discussed in Section VIII, the Rule would permit sellers to make an earnings claim, provided there is a reasonable basis for the claim and the seller can substantiate the claim at the time it is made.[224] If the seller makes no earnings claim, then section 437.3(a)(2) would direct the seller simply to check the "no" box on the on the disclosure document.[225] If the seller does make an earnings claim, then the Rule would require the seller to check the "yes" box and attach to the basic disclosure document a second document, the earnings claim statement. The Disclosure

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from offering refunds. Because companies with liberal refund policies are more likely to have refund requests than those offering no refunds, disclosure of refund requests could mislead consumers into thinking that a company offering liberal refunds is less reputable than the company offering no refunds. The Commission was persuaded by these commenters and omitted this required disclosure from the RPBOR. See 73 Fed. Reg. at 16,126. We agree with the Commission's decision.

[224] This is consistent with analogous provisions in the Franchise Rule, 16 CFR 436.9, and the Interim Business Opportunity Rule, 16 CFR 437.1(c).

[225] One panelist commented that an earnings claim is the most important selling feature of any business opportunity, and for that reason, sellers should not be permitted to state they make no earnings claim. Taylor, June 09 Tr at 68. The staff agrees that the earnings claim is important to purchasers' investment decisions. However, there is an important distinction between forcing sellers to make an earnings claims and requiring them to substantiate any claims they choose to make.

Document would advise the prospective purchaser of this requirement: "If the statement is yes, [the seller] must attach an Earnings Claim Statement to this form."[226]

At the June 1, 2009 workshop, the DOJ representative approved of the form and language of this disclosure, noting that if a seller had checked the "no" box, but had, in fact, made an earnings claim, the claim that the seller had not made an earnings claim would be a misrepresentation in violation of Section 5 of the FTC Act, and the seller would be subject to civil penalties.[227] Two Workshop panelists, however, found the language confusing and believed that a potential purchaser reading this disclosure might not know who should be completing this section of the form – him or herself, or the seller.[228] The panelists had some suggestions for improving the language of the disclosure.[229]

The staff is not convinced that any revision to the proposed language of the earnings disclosure is necessary. The initial proposed Disclosure Document, including the earnings disclosure, underwent substantial revision based upon consumer testing.

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[226] See Section VIII. Business opportunity sellers must also make the following prescribed cautionary statement in close proximity to the "yes" or "no" check boxes: "Read this statement carefully. You may wish to show this information to an advisor or accountant."

[227] Jost, June 09 Tr at 56.

[228] Cantone, June 09 Tr at 55; Taylor, June 09 Tr at 56.

[229] E.g., Cantone, June 09 Tr at 57 ("Does Acme products discuss, or allow its salespersons to discuss how much money purchasers of the business opportunity earn or have earned?"); Taylor, June 09 Tr at 57 ("Acme products or I as its representative have discussed how much money purchasers of the business opportunity earn or have earned? 'Yes' or 'No'").

[230] See supra Section I.C.

the seller."[234] Proposed 437.3(c)(ii) would require that if the seller has litigation to disclose pursuant to 437.3(c)(i), it must provide an attachment to the disclosure document with the full caption of each legal matter (names of the principal parties, case number, full name of court, and filing date).[235] Under the RPBOR, it would have been a violation of the Rule to include any additional information.

b. The record and recommendation

The Workshop discussion on this section centered on two main issues.[236] First, the panel addressed the concern that the legal action disclosure might unfairly tarnish the image of a seller who had meritless lawsuits filed against it. Second, the DOJ panelist recommended revising the form of the disclosure to enhance the government's ability to prosecute violations of the Rule.

i. Additional information regarding legal actions disclosed

Workshop panelists discussed whether the required disclosure of legal actions may unfairly tarnish a seller if the Rule also prohibits the seller from providing a short truthful statement about the nature of the litigation or its ultimate settlement. One commenter stated that in some instances, litigation may be meritless and disposed of short of formal adjudication – for example, through dismissal or settlement of nuisance lawsuits – and sellers should have the opportunity to provide an explanation of any disclosed legal actions.[237] A panelist agreed and

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[234] In the RNPR, the Commission solicited comment on whether this provision adequately captures the types of individuals whose litigation history should be disclosed. It received no comments responsive to that request.

[235] 71 Fed. Reg. at 19,069.

[236] See also supra Section V.A. (addressing the Workshop discussion on whether a seller's bankruptcy history should be considered a legal action).

[237] Gary Hailey ("Hailey"), Venable LLP, June 09 Tr at 122.

also noted that the FTC's expert report of consumer testing revealed that consumers involved in the testing of the disclosure document had very negative reactions to the existence of legal actions against the seller.[238] The DOJ panelist, on the other hand, expressed concern that if allowed to provide a description of disclosed legal actions, sellers might craft misleading descriptions.[239] He stated that he has seen such abuse in the context of the Franchise Rule,[240] although he did acknowledge that it might be unfair to prohibit sellers from providing an explanation when they have been sued.

The Commission's stated intent in identifying information to be disclosed pursuant to 437.3(c)(ii) was to minimize compliance costs to sellers – the proposed Rule would not require sellers to detail the nature of each legal action, as in the Franchise Rule."[241] The Commission reasoned that if "armed with the full caption, a prospective purchaser can seek additional information if he or she so chooses," as "the public's ability to review complaints in legal

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[238] MacLeod, June 09 Tr at 124. The panelist also argued that lawsuits are often overpled and that there may be instances where some claims (such as constitutional claims) are not really of particular materiality to a prospective purchaser.

[239] Jost, June 09 Tr at 125.

[240] The Franchise Rule requires that legal actions against franchise sellers be disclosed to potential purchasers. 16 CFR 436.5(c)(3) requires that franchisors summarize, "the legal and factual nature of each claim in the action, the relief sought or obtained, and any conclusion of law and fact," and provide information about damages or settlement terms, terms of injunctive orders, dates of any convictions or pleas, and the sentence or penalty imposed. The Interim Business Opportunity Rule requires that sellers disclose only: the identity and location of the court or agency; the date of conviction, judgment, or decision; the penalty imposed; the damages assessed; the terms of the settlement or the terms of the order; and the date, nature, and issuer of each such ruling. A seller may also include a summary opinion of counsel as to any pending litigation, but only if counsel's consent to the use of such opinion is included in the disclosure statement. 16 CFR 437.1(a)(4)(ii).

[241] 71 Fed. Reg. at 19,069.

proceedings has become significantly easier since the advent of the Internet. Many legal documents are now routinely posted on court or related websites."[242] It further noted that since the disclosure document itself instructs potential purchasers that the legal matters disclosed pertain to misrepresentation, fraud, securities law violation, or unfair or deceptive practices, potential purchasers would have a basic understanding of the subject matter of the action.[243]

The staff acknowledges that the existence of legal actions against the seller is not conclusive proof of fraud and that some legal actions may be meritless. We believe, however, that existence of the actions of the type enumerated – misrepresentation, fraud, securities law violations, or unfair or deceptive practices – against the business opportunity or its key personnel is critical to assessing the financial risk of the proposed investment. Indeed, discovering that a seller has a history of violating laws and regulations is perhaps the best indication that a particular business opportunity is a high-risk investment. In fact, in the Commission's law enforcement experience, business opportunity promoters have failed to disclose such material information to prospective purchasers, to the detriment of those purchasers.[244]

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[242] 71 Fed. Reg. at 19,069 & n.165.

[243] 71 Fed. Reg. at 19,067.

[244] E.g., FTC v. Success Vending Group, Inc., No. CV-S-05-0160-RCJ-PAL (D. Nev. 2005) (failure to disclose guilty plea for mail fraud of de facto corporate officer); FTC v. Netfran Development Corp., No. 1:05-cv-22223-UU (S.D. Fla. 2005) (failure to disclose FTC injunction against principal); FTC v. Am. Entm't Distribs., Inc., No. 04-22431-Civ-Martinez (S.D. Fla. 2004) (failure to disclose prior FTC injunction); United States v. We The People Forms and Serv. Ctrs. USA, Inc., No. CV 04 10075 GHK FMOx (C.D. Cal. 2004) (failure to disclose prior lawsuits); FTC v. Joseph Hayes, No. Civ. 4:96CV02162SNL (E.D. Mo 1996) (failure to disclose prior state fines and injunctive actions); FTC v. WhiteHead, Ltd, Bus. Franchise Guide (CCH) ¶ 10062 (D. Conn. 1992) (failure to disclose fraud action); FTC v. Inv. Dev. Inc., Bus Franchise Guide (CCH) ¶ 9326 (E.D. La. 1989) (failure to disclose insurance fraud convictions).

Like the DOJ panelist, the staff is concerned that allowing sellers to provide a description of any disclosed legal action provides the opportunity for dishonest sellers to misrepresent or mischaracterize such actions, including their ultimate outcomes. Nevertheless, we acknowledge that legitimate sellers could potentially be harmed if not afforded the opportunity to address in writing the legal action they are required to disclose.[245] We recommend, therefore, that proposed section 437.3(c)(ii) be revised to add the following sentence: "For each action, the seller may also provide a brief accurate statement not to exceed 100 words that describes the action." Non-compliance with the restriction of this proposed provision (i.e., statements that exceed the word limitation or that mischaracterize the action or outcome) would be a violation of the Rule and a violation of Section 5 of the FTC Act.

ii. Amendments to the form of disclosure

During the Workshop, the DOJ panelist advocated amending the proposed language of the legal action disclosure to enhance the ability of DOJ to prove knowledge in cases against Rule violators. The revised proposed Disclosure Document published prior to the Workshop would require the seller to answer the following question: "Has [the seller] or any of its key personnel been the subject of a civil or criminal action involving misrepresentation, fraud, securities violation, or unfair or deceptive practices within the past 10 years?" The DOJ panelist recommended that the Commission modify slightly the language of this section of the Disclosure Document by adding the phrase "including violation of an FTC Rule" after "or unfair or

[245] As the Commission noted in the RNPR, however, nothing in the RPBOR prevents the seller from speaking with the consumer to explain the nature or outcome of any legal action disclosed on the form. 73 Fed. Reg. at 16,125.

deceptive act or practice . . . ."[246] The panelist noted that DOJ has the authority to seek civil penalties for violations of trade regulation rules issued pursuant to the FTC Act,[247] but to obtain civil penalties for infractions of an FTC rule, the government must prove "actual knowledge or knowledge fairly implied on the basis of objective circumstances that such act is unfair or deceptive and is prohibited by such rule."[248] The DOJ's law enforcement experience shows that individuals who market business opportunities sometimes claim that they simply copied their required disclosure documents from a previous employer or another business opportunity marketer.[249] Including the suggested language would prevent such a seller from arguing that he or she was unaware that violations of an FTC Rule are unfair and deceptive acts or practices that must be disclosed to potential purchasers.

The staff agrees that the proposed addition to the "Legal Actions" section of the disclosure document will assist enforcement efforts by eliminating any significant question as to whether the defendant had actual or implied knowledge that violation of an FTC rule constitutes an unfair and deceptive practice. The staff recommends, therefore, that the proposed final Disclosure Document include this language.[250]

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246 Jost, June 09 Tr at 36.

247 See 15 U.S.C. § 56(a)(1); § 45(m)(1)(A) .

248 15 U.S.C. § 45(m)(1)(A).

249 Jost, June 09 Tr at 16.

250 To make the proposed Final Rule consistent with the proposed final Disclosure Document, proposed Section 437.3 would also include the language "including violations of any FTC Rule."

3. Proposed section 437.3(a)(4): Cancellation or refund policy

a. Background

Proposed section 437.3(a)(4) pertains to a common practice among business opportunity sellers, namely, offering prospective purchasers the right to cancel or to seek a whole or partial refund.[251] The RPBOR would not have required any seller to offer cancellation or a refund. However, if the seller does offer a refund or right to cancel the purchase, it must "state the terms of the refund or cancellation policy in an attachment to the disclose document."[252] Specifically, a seller that offers a cancellation or refund policy must check the "yes" box on the disclosure document and also must attach to the disclosure document a written description of its policy. To minimize compliance costs, the seller may comply with this disclosure by attaching to the disclosure document a copy of a pre-existing document that details the seller's cancellation or refund policy. For example, a seller may detail its refund policy in a company brochure. If so, the seller need only attach to the disclosure document the particular page setting forth the refund policy. As in the other examples above, if no cancellation or refund is offered, then the seller need only check the "no" box.

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[251] See, e.g., FTC v. AMP Publ'n, Inc., No. SACV-00-112-AHS-ANx (C.D. Cal. 2001); FTC v. Home Professions, Inc., No. SACV 00-111 AHS (Eex) (C.D. Cal. 2001); FTC Innovative Prods., No. 3:00-CV-0312-D (N.D. Tex. 2000); FTC v. Encore Networking Servs., No. 00-1083 WJR (AIJx) (C.D. Cal. 2000); FTC v. Mediworks, Inc., No. 00-01079 (C.D. Cal. 2000). Indeed, allegations that business opportunity sellers misrepresented their refund policies rank among the top 10 complaint allegations in Commission business opportunity cases brought under Section 5. See 71 Fed. Reg. 19,069.

[252] The Commission adopted a similar approach in the TSR. 16 CFR 310.3(a)(1)(iii) (if a seller makes a representation about a refund policy, it must disclose "a statement of all material terms and conditions of such policy").

b. The record and recommendation

Workshop panelists raised two issues related to disclosure of refund and cancellation policies. First, panelists questioned whether information about the percentage of purchasers requesting and obtaining refunds should be part of the disclosure, and second, whether proposed section 437.3(a)(4) should specify particular terms of a refund policy that must be disclosed to potential purchasers. The sections that follow address each of these concerns.

i. Percentage of purchasers requesting and obtaining refunds

One panelist stated that information concerning the percentage of purchasers requesting and obtaining refunds would be relevant information to potential purchasers.[253] Another panelist disagreed, arguing that requiring disclosure of this information might have the unintended consequence of harming purchasers by discouraging sellers from offering refunds.[254] This issue was previously considered by the Commission. The IPBOR would have required a seller that had a cancellation or refund policy to disclose the number of purchasers who had asked to cancel or who had sought a refund in the two previous years.[255] In the INPR, the Commission specifically sought comment on the proposed disclosure of the seller's refund history, particularly on the likely effect this disclosure might have on the willingness of sellers to offer refunds.[256] Based upon arguments articulated in the comments to the INPR, the Commission concluded that this

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253 Taylor, June 09 Tr at 48. One commenter agreed. Brooks-Workshop comment.

254 MacLeod, June 09 Tr at 50.

255 IPBOR, 437.3(a)(5).

256 71 Fed. Reg. at 19,070.

disclosure would not be useful to consumers, and that disclosure of refund history could be unduly prejudicial to business opportunities that offer and liberally provide refunds to prior purchasers.[257] Indeed, a prospective purchaser might compare the refund requests of a fraudulent seller with no refund policy against a legitimate seller with a liberal refund policy and inappropriately conclude that the legitimate seller offers a riskier business venture. The Commission concluded that disclosure of refund history would not reliably remedy deception on this issue, and it was eliminated in the RPBOR.[258]

Panelists in favor of requiring disclosure of seller's refund histories presented no arguments other than those previously considered by the Commission. The staff is persuaded by the Commission's reasoning in concluding that this disclosure would not benefit potential

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[257] 73 Fed. Reg. at 16,126.

[258] Id.

[259] Lois Greisman ("Greisman"), FTC, Associate Director, Division of Marketing Practices, June 09 Tr at 42.

Attorney General's Office thought the Rule should specify that all material terms of a refund policy must be disclosed, because in the context of business opportunity sales, it has been his experience that the requirements to obtain a refund are often so onerous that as a practical matter, no one is ever eligible.[260] Some panelists felt the Rule should identify specific information to be disclosed. For example, one commenter noted that the period of time a seller has to exercise a right to cancellation or refund, or any conditions on return of unsold goods are material and should be required to be disclosed to potential purchasers.[261] One panelist suggested that the DSA Code of Ethics' refund requirements could be looked at to identify types of information that should be disclosed to potential purchasers.[262] We agree that sellers should be provided with additional guidance and recommend clarifying that sellers must disclose all material terms of refund and repayment policies to prospective purchasers. The commentary to the IPBOR reveals that this was the Commission's intent.[263]

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[260] Cantone, June 09 Tr at 47 (providing as an example a company offering a 100% buy-back for vending machines and noting the company's failure to disclose that the cost of sending back the vending machine would be borne by the purchaser, and would often exceed any refund due, thereby rendering any potential refund worthless).

[261] Taylor, June 09 Tr at 43.

[262] Morrissey, June 09 Tr at 45. We have reviewed applicable provisions of the DSA Code of Ethics, but do not find them instructive. DSA dictates the specific terms of its members' refund policies. The RPBOR, in contrast, would not have specified the requirements of a seller's refund or cancellation policy, or even whether the seller has such policies. Instead, it attempted to ensure that if such policies exist, potential purchasers are aware of how they can exercise their rights under those policies.

[263] See 71 Fed. Reg. 19,069 n.166.

The staff recommend, therefore, modifying proposed 437.3(a)(4), to track closely a similar disclosure requirement in the TSR.[264] The TSR requires that if the seller or telemarketer makes a representation about a refund, cancellation, exchange or repurchase, it must provide the purchaser with a statement of all material terms and conditions of such statement. Requiring disclosure of all material terms of a refund or cancellation policy would most effectively accomplish the Commission's stated purpose of ensuring that potential purchasers are provided with information that would assist them in assessing the financial risk associated with the offer. We recommend, therefore, that the penultimate sentence of 437.3(a)(4), which would require disclosure of any refund policies, be clarified to read: "If so, state all material terms and conditions of the refund or cancellation policy in an attachment to the disclosure document." As discussed earlier, the staff recommends that the proposed Final Rule include a definition of "material" similar to the definition in section 310.2(q) of the TSR. Proposed section 437.1(i) would define "material" as "likely to affect a person's choice of, or conduct regarding, goods or services."[265] Examples of material terms and conditions may include, for example, the period of time the purchaser has to cancel a purchase or request a refund; the specific steps necessary to cancel a purchase or request a refund; any fees or penalties incurred for cancellation; where unused inventory must be returned and by what method, etc. At this time, however, the staff

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[264] Indeed, that was the Commission's intent. In describing its approach regarding refund and cancellation policy disclosures, the Commission noted that it "adopted the same approach in the TSR." 71 Fed. Reg. at 19,069 n.166 (citing 16 CFR 310.3(a)(1)(iii) (if a seller makes a representation about a refund policy, it must disclose "a statement of all material terms and conditions of such policy").

[265] Section 310.2(q) of the TSR defines "material" to mean "likely to affect a person's choice of, or conduct regarding, goods or services or a charitable contribution." The definition we proposed for the Business Opportunity Rule would exclude the phrase "or a charitable contribution."

declines to recommend that the Rule enumerate what terms are material, as materiality is likely to vary depending on the circumstances of the opportunity and the refund or cancellation policy.

4. Proposed section 437.3(a)(5): References

a. Background

Section 437.(a)(5)(i) of the RPBOR would have required that sellers of business opportunities disclose to potential purchasers the name, city, state, and telephone number of a limited number of prior purchasers as references.[266] The proposed Final Rule would require the seller to provide this reference disclosure by listing each prior purchaser (if fewer than 10), or listing at least the 10 prior purchasers nearest to the prospective purchaser's location. The proposed Rule would limit the disclosure of references to those who have purchased the business opportunity within the last three years. In order to minimize compliance costs, the proposed Rule also provides sellers with an alternative disclosure option – in lieu of a list of the 10 prior purchasers nearest the prospect, a seller may furnish a prospect with a national list of all purchasers. In the INPR, the Commission noted that this option would allow the seller to maintain a master list of purchasers on its website that could be updated periodically, which would allow the seller to avoid having to tailor the disclosure to each prospective purchaser.[267]

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[266] Unlike the Interim Business Opportunity Rule, the proposed Rule does not require the disclosure of prior purchasers' street addresses. The Commission concluded that prospects could readily contact a prior purchaser if provided with the prior purchaser's name, city and state, and telephone number, and that this approach enables prospects to contact references while minimizing the intrusion into prior purchasers' privacy. 71 Fed. Reg. at 19,071 n.180.

[267] 71 Fed. Reg. at 19,071.

The proposed Rule would specify that sellers selecting the national option must insert the words "See Attached List" and attach a list of the references to the disclosure document.[268]

Notwithstanding the fact that the type of information required by the reference disclosure is often readily available and in the public domain, in crafting this section of the proposed Rule, the Commission considered potential privacy concerns raised by the use of prior purchaser information.[269] To address these concerns, proposed section 437.3(a)(5)(ii) would require that the disclosure document state the following language clearly and in immediate conjunction with the list of references: "If you buy a business opportunity from the seller, your contact information can be disclosed in the future to other buyers."

b. The record and recommendation

In response to the INPR, a number of commenters, primarily from the MLM industry, expressed concern that the reference disclosure requirement raised privacy and security concerns.[270] The Commission, however, was not persuaded by the commenters. The Commission reasoned that disclosure of prior purchasers is important to prevent fraud because it enables prospects to evaluate the seller's claims based on information from an independent source with relevant experience.[271] Further, it concluded that the very limited proposed reference disclosure did not raise security concerns because the required disclosures include no sensitive

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[268] In the RNPR, the Commission solicited comment on whether giving sellers the ability to provide prospective purchasers with a national list was a viable option. It received no comments responsive to that request.

[269] See id.

[270] See 73 Fed. Reg. at 16,126.

[271] See id.

personal information whatsoever – no social security numbers, birth dates, or financial account numbers.[272]

Following publication of the RNPR, one commenter continued to argue that the disclosures enumerated in proposed section 437.3(a)(5) would raise privacy and data security concerns.[273] The commenter articulated three main concerns: (1) that requiring the seller to "store purchasers' personal information in a single location or document creates a target ripe for theft and improper disclosure;" (2) that requiring disclosure of information of prior purchasers conflicts with the FTC's Privacy of Consumer Information Rule ("Privacy Rule" or "GLB Privacy Rule"),[274] promulgated under the Gramm-Leach-Bliley Act ("GLB")[275] because it does not allow those prior purchasers of the business opportunity the right to opt out of having their contact information disclosed to potential purchasers;[276] and (3) that the mandatory disclosure of

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[272] See id.

[273] Planet Antares-RNPR at 18.

[274] 16 CFR Part 313.

[275] 15 U.S.C. § 6801 et seq.

[276] The Commission received a few comments in response to the INPR in support of allowing individual business opportunity purchasers to opt out of having their contact information disclosed. DOJ, however, urged the Commission to reject any opt-out believing it would be an easy matter for sellers to talk purchasers into opting out, describing to them what a hassle it becomes for those who do not opt out because of all the demand that arises for their time and attention. The Commission agreed with DOJ and after analyzing all of the commentary to Section 437.3(a)(5), declined to make any changes to that section. See 73 Fed. Reg. at 16,126.

references violates privacy obligations under the California Constitution.[277] The staff disagrees with each of these contentions.[278]

[277] Planet-Antares- RNPR at 20.

[278] This same commenter contends that the required reference information constitutes trade secrets that should be afforded special protections, but offers no support for this contention. Id. at 14.

[279] 16 CFR 437.1(a)(16)(iii).

customers of its privacy policies and practices,[280] including the consumers' right to opt out of having their personal information shared with third parties.[281] For purposes of the Privacy Rule, a consumer is an individual who obtains financial products or services for personal, family or household purposes.[282] We need not consider the limited circumstances where a business opportunity seller might be considered a financial institution, because the Privacy Rule is aimed at protecting the non-public personal financial information of consumers, not businesses.[283]

The commenter argues that business opportunity operators should be considered consumers for purposes of the Privacy Rule, and thus should have the right to opt out of having their contact information disclosed to potential purchasers.[284] The staff believes that the commenter's interpretation is contrary to both prior Commission policy, and the plain meaning of the words of the Privacy Rule. As the Commission has previously stated, by investing in a business opportunity, purchasers are entering the world of commerce and embarking upon the

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[280] 73 Fed. Reg. at 16,127.

[281] 16 CFR 313.1(a)(3).

[282] 16 CFR 313.3(e). Similarly, a customer is a consumer with a continuing relationship with the financial institution. See 16 CFR 313.3(h).

[283] Congress enacted GLB to protect personal financial information of individual consumers but excluded from the ambit of the law the protection of information pertaining to businesses. See 16 CFR 313.1(b) (expressly stating that the Privacy Rule "does not apply to information about companies or about individuals who obtain financial products or services for business, commercial, or agricultural purposes"). Indeed, federal law often focuses on privacy concerns affecting individuals, not businesses. See, e.g., the Fair Credit Reporting Act ("FCRA") 15 U.S.C. § 1681(a)(4) (requiring various protections for consumer information, including provisions addressing identity theft). There is no comparable statute that protects business information.

[284] The commenter argues that the purchase of a business opportunity might be intended to "provide a revenue stream" to a purchaser and "not necessarily a source of employment." We find this distinction immaterial in the analysis.

[285] 73 Fed. Reg. at 16,127 & n.210.

[286] The Commission has not issued guidance about the meaning of "personal, family, or household purposes" because the plain meaning of the words seems abundantly clear. Courts' interpretation of this phrase when used in other consumer protection laws is instructive. See, e.g., In re Runski,102 F.3d 744, 747 (4th Cir. 1996) (noting in the bankruptcy context that courts have uniformly concluded that debt incurred for a business venture or with a profit motive does not fall into the category of debt incurred for "personal, family, or household purposes").

[287] See "Frequently Asked Questions for the Privacy Regulation," Question B-2 (Dec. 2001), http://www.ftc.gov/privacy/glbact/glb-faq.htm (Privacy Rule does not apply when a financial institution makes a business loan to a sole proprietor; although an individual, a sole proprietor is not a "consumer" for purposes of the Privacy Rule where the financing is not for personal, family, or household purposes).

[288] See, e.g., Preservation of Consumer's Claims and Defenses, 16 CFR 433.1(b); Credit Practices, 16 CFR 444.1(d).

[289] When personal information has been released without consent, a cause of action for invasion of privacy exists under the California Constitution only if: (1) the individual had a

action. First, the disclosure document plainly notifies potential purchasers that their reference information will be provided to subsequent purchasers, thus they have no reasonable expectation that their information will be kept private. Next, the reference disclosure includes no sensitive personal information whatsoever, and the value to prospects of information about prior purchasers outweighs any potential detriment to those prior purchasers.

[290] Morrissey, June 09 Tr at 87.

[291] Jost, June 09 Tr at 88.

[292] As described in supra

opportunity offers outweighs any costs of more frequent updating until the list of 10 is compiled.[299]

b. The record and recommendation

No comments were received about this proposed requirement. The staff recommends, therefore, that section 437.3(b) be adopted in the form proposed in the RPBOR.

VIII. Proposed Section 437.4: Earnings Claims

Section 437.4 of the proposed Rule would address earnings claims, and is similar to the parallel sections of the Franchise Rule and Interim Business Opportunity Rule. Like each of those rules, the proposed Rule would not require business opportunity sellers to make an earnings claim. Rather, the disclosure of earnings information is strictly voluntary. Also, like the analogous provisions of the Franchise Rule and Interim Business Opportunity Rule,[300] proposed section 437.4(a) would require a seller making an earnings claim to: (1) have a reasonable basis for the claim at the time the claim is made; (2) have in its possession written materials that substantiate the claim at the time the claim is made; (3) make the written material available to the prospect and the Commission upon request; and (4) furnish the prospect with an earnings claim statement. Also, similar to the Franchise Rule, proposed section 437.4(b) would set forth the requirements for making earnings claims in the general media,[301] and would require that sellers notify prospects in writing of any changes in earnings information before the prospect enters into a contract or provides any consideration to the seller, directly or indirectly through a third

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299 Id.

300 See 16 CFR 436.9 and 437.1(b), (c) and (e).

301 16 CFR 436.1(e).

material because a prospective purchaser cannot begin to evaluate an earnings representation without knowing how recently the supporting data was collected. For example, a seller may have conducted a survey of business opportunity purchasers in 2008. The Rule would not necessarily prohibit the use of that survey information in 2010, but the prospect should be made aware of the applicable time period in order to assess the relevance of the claim to current market conditions. Similarly, a prospect may reasonably give greater weight to a survey of purchasers over an extended period of time (for example, over a three-year period), than a more limited survey (for example, over a three-month period).[305]

Further, this section of the proposed Rule would require the disclosure of the number and percentage of all purchasers who purchased the business opportunity prior to the end of the represented time period who have achieved at least the claimed earnings during that period. This information is material because it enables the prospect to determine whether the claimed earnings of prior purchasers are typical.[306] For example, a seller may claim that purchasers have average earnings of $50,000 a year. Even if true, this statement may not reflect the experience of the typical purchaser because a few purchasers with unusually high earnings could skew the average. Thus, the number and percentage of purchasers earning $50,000 a year might actually be very low.[307]

In addition to the earnings claim and substantiation requirements, this section of the proposed Rule would require a seller making an earnings claim to disclose any characteristics that

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305 71 Fed. Reg. at 19,072.

306 Id.

307 Id.

distinguish purchasers who achieved at least the represented level of earnings from those characteristics of the prospective purchasers.[308] For example, a survey of ice cream vending route purchasers operating only in the South may not be readily applicable to other regions, such as the North. Similarly, a survey limited to large urban areas may not be applicable to smaller, rural areas. Distinguishing characteristics of opportunity purchasers who achieved a represented level of earnings is material information because it enables a prospect to assess the relevance of an earnings claim to his or her particular market.[309]

Finally, the proposed Rule would require a seller making an earnings claim to disclose to the prospective purchaser that written substantiation for the claim will be made available upon request.[310] Requiring that a prospective purchaser can

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[308] Proposed section 437.4(a)(4)(vi).

[309] 71 Fed. Reg. at 17,073.

[310] Proposed section 437.4(a)(4)(vii).

[311] See, e.g., 16 CFR 436.1(b)(2); 436.1(c)(2).

whether the requirement that sellers disclose any materially different characteristics of prior purchasers that attained at least the stated level of earnings adequately covered the relevant earnings information that should be disclosed.[312]

2. The record and recommendation

No comments were received in response to the Commission's specific questions, nor were any comments directed to this proposed provision. We agree with the Commission's conclusions regarding the necessity of provisions of 437.4(a). We recommend, therefore, that section

[312] 73 Fed. Reg. at 16,133.

[313] Section 437.4(b)(3) requires similar disclosures, calculated in the same way, in conjunction with any earnings claim made in the general media.

[314] E.g.

making informed decisions.[317] For example, the performance experience of prior purchasers of a business opportunity might contrast favorably against the industry average and, if so, that information would help a prospective purchaser assess the value of the investment against other proposed businesses. We agree that there may be a limited number of situations in which providing industry statistics may be beneficial to potential purchasers. However, we remain concerned that industry statistics can be, and have been, used to imply to potential purchasers that their likely earnings with the promoted business opportunity will match the industry averages.[318]

Staff recommends, therefore, a small change to proposed section 437.4(c) to state that it is an unfair or deceptive practice to "disseminate industry financial, earnings, or performance information unless the seller has written substantiation demonstrating that such information reflects, or does not exceed, the typical or ordinary financial, earnings, or performance experience of purchasers of the business opportunity being offered for sale."

Accordingly, a seller could use industry information only if it is able to measure the performance of existing purchasers and document that the existing purchasers' typical performance equals or exceeds the average performance of others in the industry. A start-up business opportunity with no or very limited prior sales, therefore, would probably not be able to use industry statistics because it would lack a sufficient basis to demonstrate that the industry statistics reflect the typical or ordinary experience of the start-up's prior purchasers.

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317 Planet Antares-RNPR.

318 See supra note 314.

D. Proposed Section 437.4(d): Material Changes

1. Background

Proposed section 437.4(d) addresses post-disclosure changes in earnings information. It would prohibit any seller making an earnings claim from failing to notify the prospective purchaser, before the prospect enters into a contract or pays any consideration, of any material change that has occurred and that calls into question the relevance or reliability of the information contained in its earnings claim statement. "Such material changes include the issuance of a new survey or other facts that would lead the seller to conclude that a prior survey is no longer valid."[319] In crafting proposed section 437.4(d) the Commission was cognizant of the high degree of materiality of earnings information for prospective purchasers, but attempted to minimize compliance costs.[320] "The proposal would not require a seller, for example, to prepare a revised earnings claim statement immediately, but would simply require written notification of the change."[321] The Commission stated that this approach strikes the right balance between accurate disclosure to prevent deception and compliance costs that would result from a more frequent updating requirement.

2. The record and recommendation

In response to the RNPR, the Commission received no comments about this provision. We agree with the Commission's analysis regarding the benefits and burdens of this provision. We recommend, therefore, that section 437.4(d) be adopted in the form proposed in the RPBOR.

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319 Id.

320 Id.

321 73 Fed. Reg. at 19,073.

IX. Proposed Section 437.5: Spanish and Other Non-English Language Sales (New Proposed Requirement)

On its own initiative, the staff recommends adding a new provision to the proposed Final Rule that would require sellers to provide the Disclosure Document and the disclosures required by sections 437.3(a) and 437.4(b) to potential purchasers in the same language the seller uses to market the business opportunity. The Commission has long recognized that "with increasing intensity, advertisers are making special efforts to reach foreign-language speaking consumers," and that disclosures required by orders, rules, or guides should be made in the predominant language of the advertisement or sales material.[322] Similarly, the staff believes that when a business opportunity seller purposefully reaches out to a particular population by marketing in the foreign-language spoken by members of that community, all of the disclosures required by the Rule should be accessible and comprehensible to each of those potential purchasers.

The Commission's law enforcement history demonstrates that fraudulent business opportunities have specifically targeted Spanish-speaking communities.[323] But the staff

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[322] FTC Enforcement Policy Statement Concerning Clear and Conspicuous Disclosures in Foreign Language Advertising and Sales Materials, 16 CFR 14.9.

[323] E.g., FTC v. Zoilo Cruz, No. 3:08-cv-01877-JP (D.P.R. 2008) (envelope stuffing scheme marketed in Spanish-language newspapers and on a website available in Spanish and English); FTC v. Integrity Mktg. Team, Inc., No. 07-cv-61152 (S.D. Fla. 2007) (envelope stuffing scheme marketed in Spanish-language classified advertisements); FTC v. Hispanexo, Inc., No. 1:06-cv-00424-JCC-TRJ (E.D. Va. 2006) (assistance in starting a construction, gardening, or cleaning business marketed through Spanish-language television and radio stations); FTC v. Juan Matos, No. 06-61429-CIV-Altonaga (S.D. Fla. 2006) (craft assembly business marketed through Spanish-language advertisements); FTC v. Nat'l Vending Consultants, Inc., CV-S-05-0160-RCJ (PAL) (D. Nev. 2005) (deceptively marketed vending machine business opportunities – with many marketing efforts specifically targeting Spanish-speaking consumers); FTC v. Amada Guerra, No. 6:04-CV-1395 (M.D. Fla. 2004) (product assembly scheme telemarketed to Spanish-speaking consumers); FTC v. USS Elder Enter., Inc., No. SACV-04-1039 AHS (Anx) (C.D. Cal. 2004) (work at home assembly scheme offered

recognizes that business opportunities may be marketed in dozens of languages besides English and Spanish. The staff recommends, therefore, that business opportunity sellers be required to provide the disclosure document to potential purchasers in the language the seller used to conduct the offer for sale, sale, or promotion of the business opportunity. Because the Commission's law enforcement history demonstrates the sale of business opportunities in Spanish, a translation of the basic Disclosure Document is attached as Appendix B to the Rule. Should a seller use a language other than English or Spanish, the seller would be responsible for obtaining an accurate transaction of the Disclosure Document.

A new section 437.5, entitled "Spanish and Other Non-English Language Sales" would require:

(a) If the seller conducts the offer for sale, sale, or promotion of a business opportunity in Spanish, the seller must provide the disclosure document required by § 437.3(a) in the form and language set forth in Appendix B to this part, and the disclosures required by §§ 437.3(a) and 437.4(a) must be made in Spanish; and

(b) If the seller conducts the offer for sale, sale, or promotion of a business opportunity in a language other than English or Spanish, the seller must provide the disclosure document required by § 437.3(a) using the form and an accurate translation of the language set forth in Appendix A to this part, and the disclosures required by §§ 437.3(a) and 437.4(a) must be made in that language.

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through Spanish-language newspapers and magazines); FTC v. Esteban Barrios Vega, No. H-04-1478 (S.D. Tex. 2004) (deceptive product assembly opportunity marketed through Spanish-language newspaper and magazine advertisements).

The staff further recommend revising section 437.3(a) to conform with this requirement.[324]

The staff seeks public comment about whether this new provision adequately promotes the Commission's goal of ensuring that potential purchasers be provided with information necessary to make an informed purchasing decision. Why or why not? What alternatives, if any, should the Commission consider? What would be the costs and benefits of each alternative?

The staff also seeks comment about whether the translation into Spanish of Appendix A is adequate to convey to Spanish-speaking potential purchasers the meaning of the required disclosures. Would different word choices make the disclosures more meaningful? Additionally, the staff seeks comment on its recommendation to require sellers that market business opportunities in languages other than English or Spanish to provide translations of the disclosure document and required disclosures.

X. Proposed Section 437.6: Other Prohibited Practices

Section 437.6 of the proposed Rule would prohibit sellers from engaging in a number of deceptive practices, whether directly or through a third party, that are common in the sale of fraudulent business opportunity ventures. Violation of any provision of this section would be a violation of the Rule and an unfair or deceptive act or practice in violation of Section 5 of the FTC Act. Each of the proposed prohibitions is discussed below.

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[324] See supra Section VII.C. Section 437.3 of the proposed Rule would make it an unfair or deceptive act or practice for any seller to fail to disclose to a prospective purchaser material information required by sections 437.3 and 437.4 in a single written document in the form and using the language set forth in Appendix A to this part; or if the offer for sale, sale, or promotion of a business opportunity is conducted in Spanish, in the form and using the language set forth in Appendix B to this part; or if the offer for sale, sale, or promotion of a business opportunity is conducted in a language other than English or Spanish, using the form and an accurate translation of the language set forth in Appendix A to this part.

A. Proposed Section 437.6(a): Disclaimers

1. Background

Proposed section 437.6(a) would prevent sellers from using disclaimers or waivers as a means of insulating themselves from the consequences of materially false or deceptive statements in their own disclosure documents. This provision would prohibit a business opportunity seller from disclaiming, or requiring "a prospective purchaser to waive reliance on, any statement made in any document or attachment that is required or permitted to be disclosed under this Rule."[325] The Commission has stated that the purpose of this provision is to preserve the reliability and integrity of pre-sale disclosures. "Otherwise, the Rule's very purpose would be undermined by signaling to prospects that they cannot trust or rely on the Rule's mandated disclosures."[326]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions and recommends, therefore, that section 437.6(a) be adopted in the form proposed in the RPBOR.

B. Proposed Section 437.6(b): Inconsistent or Contradictory Information

1. Background

Proposed section 437.6(b) would prohibit sellers from making any representation, whether

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[325] This provision is parallel to the anti-disclaimer prohibition in the Amended Franchise Rule. See 16 CFR 436.9(h).

[326] 71 Fed. Reg. at 19,073.

[327] This provision is similar to the Amended Franchise Rule prohibition against the making of statements that contradicts any required disclosure. See 16 CFR 436.9(a).

[328] 71 Fed. Reg. at 19,074.

[329] E.g., FTC v. Am. Entm't Distribs., Inc., No. 04-22431-CIV-Martinez (S.D. Fla. 2004); FTC v. Inspired Ventures, Inc., No. 02-21760-CIV-Jordan (S.D. Fla. 2002); FTC v. Mortgage Serv. Assocs., Inc., No. 395- CV-13362 (AVC) (D. Conn. 1995); FTC v. Tower Cleaning Sys., Inc.

[330] Indeed, in response to the INPR, DOJ urged the Commission to exclude state disclosures from the proposed form. In DOJ's experience, "[p]urveyors of fraudulent business opportunities will seek every opportunity to water down this document with extraneous information to hide any negative information it may contain." See 73 Fed. Reg. at 16,128. The Commission's experience supports DOJ's conclusions.

[331] This is the same approach used in the Amended Franchise Rule. See 16 CFR 436.6(d).

[332] See 16 CFR 436.10.

[333] See

disclosures into one document would be an invitation to sellers to present lengthy and confusing information to prospective purchasers.[334] Such a result would be contrary to the Commission's goal of providing a simple, clear, and concise disclosure document.

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions, and recommends, therefore, that section 437.6(c) be adopted in the form proposed in the RPBOR.

D. Proposed Section 437.6(d): False Earnings Claims

1. Background

As previously noted, the making of false earnings claims is the most prevalent problem in the offer and sale of business opportunities. Proposed section 437.6(d) would prohibit sellers from misrepresenting the amount of sales, gross or net income, or profits a prospective purchaser may earn or that prior purchasers have earned. This prohibition complements the Rule's proposed earnings substantiation requirements detailed in proposed section 437.4. Thus, both unsubstantiated and false earnings claims would be prohibited by the Rule.

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff recommends, therefore, that section 437.6(d) be adopted in the form proposed in the RPBOR.

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[334] 73 Fed. Reg. at 16,129.

E. Proposed Section 437.6(e): Misrepresentations Regarding the Law as to Earnings Claims and the Identity of Other Business Opportunity Purchasers

1. Background

The IPBOR section 437.6(e) would have prohibited sellers from stating that any law or regulation prohibits seller from furnishing earnings information. The Commission intended that this provision address a recurring problem identified in the rulemaking record – sellers misrepresenting that federal law or the FTC prohibits the making of earnings claims.[335] In effect, this prohibition would ensure that prospective purchasers are not misled into believing that earnings information is unavailable to them as a matter of law.[336] The RPBOR added a second prohibition to section 437.6(e) that would have prevented sellers from misrepresenting that any law or regulation prohibits a seller from disclosing to prospective purchasers the identity of other purchasers of the business opportunity. The Commission made this proposed change in response to DOJ's request because in its experience, fraudulent business opportunity sellers frequently deflect potential purchasers' requests for contact information of current distributors by falsely claiming that the law forbids disclosing those identities.[337] The Commission agreed that the

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[335] In the Amended Franchise Rule, the Commission addressed this problem through a new requirement that franchise sellers include a specific preamble in the financial performance section of their disclosures. Among other things, the preamble makes clear that franchisors can make financial performance information available, assuming they have a reasonable basis for their claims. See 16 CFR 436.5(s)(1). In an effort to streamline the business opportunity disclosure document and reduce compliance costs, the Commission proposed this different approach for the Business Opportunity Rule, believing it sufficient to address deceptive business opportunity sales. The Commission noted that "whereas the Franchise Rule seeks to encourage franchisors to make earnings claims, no such encouragement is needed in the business opportunity field, where such claims are all too common." 71 Fed. Reg. at 19,075 n.211.

[336] 73 Fed. Reg. at 16,127.

[337] Id.

prohibition is appropriate, because "it will help consumers understand that if the seller supplies no references, it is because none exist, or because the seller chooses not to make such information available, which would contravene the RPBOR."[338]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions and recommends, therefore, that section 437.6(e) be adopted in the form proposed in the RPBOR

F. Proposed Section 437.6(f): Written Substantiation for Earnings Claims

1. Background

Proposed section 437.6(f) would prohibit a seller who makes an earnings claim from failing to provide written substantiation to prospective purchasers and to the Commission upon request.[339] Rather than mandating that business opportunity sellers include documentation for earnings claims – which could be voluminous – in the earnings claim statement itself, the proposed Rule would reduce com003 Tc-e busonlyction 4rmke such 3(Bale no writtend.0004 Tc-.0006 Tw[(No

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[338] Id.

[339] The Amended Franchise Rule and Interim Business Opportunity Rule have similar requirements. See 16 CFR 436.5(r)(3)(v); 437.1(b)(2); and 437.1(c)(2).

[340] E.g., FTC v. Indep. Mktg. Exch., Inc., No. 10-CV-00568-NLH-KMW (D.N.J. 2010); FTC v. Preferred Platinum Servs. Network, Inc., No.10-CV-00538-MLC-LHG (D.N.J.

I. Proposed Section 437.6(i): Assistance

1. Background

Proposed section 437.6(i) would prohibit business opportunity sellers from misrepresenting any material aspect of assistance provided to purchasers.[344] The Commission's enforcement experience shows that misrepresentation of post-sale assistance offered to a prospective purchaser is an element common to many business opportunity frauds targeted in FTC cases.[345] Also, consumer complaints about misrepresentations concerning the type and amount of assistance promised but not received are among the top categories of reported deceptive business opportunity practices.[346] The Commission concluded that the best way to address this deceptive practice is through a direct prohibition.[347]

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344 71 Fed. Reg. at 19,075 n.216.

345 The Commission has recognized that promises of assistance made to induce prospects to purchase a franchise are material, especially to those prospects with "little or no experience at running a business." See, e.g., FTC v. Am. Entm't Distribs., Inc., No. 04-22431-CIV-Martinez (S.D. Fla. 2004); FTC v. USS Elder Enter., Inc., No. SA CV-04-1039 AHS (ANx) (C.D. Cal. 2004); FTC v. Kitco of Nevada, 612 F. Supp. 1282 (D. Minn. 1985); FTC v. Leading Edge Processing, Inc., No. 6:02-CV-681-ORL-19 DAB (M.D. Fla. 2003); FTC v. Darrell Richmond, No. 3:02-3972-22 (D.S.C. 2003); FTC v. Elec. Med. Billing, Inc., No. SA02-368 AHS (ANX) (C.D. Cal. 2003); FTC v. Transworld Enter., Inc., No. 00 8126-CIV-Graham (S.D. Fla. 2000); FTC v. Advanced Pub. Commc'ns Corp., No. 00-00515-CIV-Ungaro-Benages (S.D. Fla. 2000); FTC v. Hi Tech Mint Sys., Inc., No. 98 CIV 5881 (JES) (S.D.N.Y. 1998); United States v. QX Int'l,Inc., No. 398-CV-0453-D (N.D. Tex. 1998).

346 71 Fed. Reg. at 19,075 n.218.

347 71 Fed. Reg. at 19,075.

foster the expectation that a profitable market exists for the goods or services the purchaser will sell.[350]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff

[350] 71 Fed. Reg. at 19,076.

a purchaser.[351] These representations have lured prospective purchasers into believing that the investment is either low-risk or even risk-free.[352]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions and recommends, therefore, that section 437.6(k) be adopted in the form proposed in the RPBOR.

L. Proposed Section 437.6(l): Failure to Cancel or Make a Refund

1. Background

Proposed section 437.6(l) would prohibit a seller from failing to cancel a purchase or make a refund when the purchaser has qualified for such relief under the seller's cancellation or refund policy.[353] As noted above, proposed section 437.6(k) would prohibit a seller from misrepresenting, pre-sale, the seller's cancellation or refund policy. Proposed section 437.6(l) would complement that section and was intended to address sellers' post-sale conduct, prohibiting the seller from failing to honor cancellation or refund requests when purchasers have satisfied all the terms and conditions disclosed in the seller's Disclosure Document for obtaining such

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[351] E.g., FTC v. Med. Billers Network, No. 05 CV 2014 (RJH) (S.D.N.Y. 2005); FTC v. Castle Publ'g, Inc., No. AO3CA 905 SS (W.D. Tex. 2003); FTC v. America's Shopping Network, Inc., No. 02-80540-CIV-Hurley (S.D. Fla. 2002); FTC v. Home Professions, Inc., No. SACV 00-111 AHS (Eex) (C.D. Cal. 2001); FTC v. Encore Networking Servs., No. 00-1083 WJR (AIJx) (C.D. Cal. 2000).

[352] 71 Fed. Reg. at 19,076.

[353] This is consistent with the Interim Business Opportunity Rule approach. See 16 CFR 437.1(h).

relief.[354] In the Commission's experience, the failure of business opportunities sellers to make promised refunds or to honor cancellation policies ranks high among issues raised by business opportunity purchasers.[355]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions and recommends, therefore, that section 437.6(l) be adopted in the form proposed in the RPBOR.

M. Proposed Section 437.6(m): Employment Opportunity

1. Background

Proposed section 437.6(m) would prohibit business opportunity sellers from misrepresenting a business opportunity as an employment opportunity. The Commission's law enforcement experience demonstrates that some business opportunity sellers lure unsuspecting consumers by falsely representing that they are offering employment when, in fact, they are offering vending, work-at-home, or other business opportunities. For example, in some instances consumers have responded to advertisements seeking sales executives, only to discover that the "position" requires them to purchase equipment or products from the seller and, in turn, to sell those products.[356]

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[354] E.g., FTC v. AMP Publ'ns, Inc., No. SACV-00-112-AHS-ANx (C.D. Cal. 2001) (failure to honor 90-day money back guarantee); FTC v. Star Publ'g Group, Inc., No. 00-023 (D. Wyo. 2000) (failure to honor 90-day refund policy).

[355] 73 Fed. Reg. at 19,076.

[356] See, e.g., FTC v. Trek Alliance, Inc., No. 02-9270 SJL (AJWx) (C.D. Cal. 2002) (defendants placed ads in "Help Wanted" sections of newspaper offering salaried position); FTC v. Leading Edge Processing, Inc., No. 6:02-CV-681-ORL-19 DAB (M.D. Fla. 2003) (defendants sent emails to job seekers who posted their resumes on job websites, falsely representing the

or she will not be competing for customers with the seller or other purchasers, thereby increasing the purchaser's likelihood of success.[359]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions and recommends, therefore, that section 437.6(n) be adopted in the form proposed in the RPBOR.

O. Proposed Section 437.6(o): Assignment of Territories

1. Background

Proposed section 437.6(o) would prohibit a seller from assigning a single "exclusive" territory to more than one purchaser. This prohibition would complement section 437.6(n), which would prohibit sellers from misrepresenting territories. It is intended to address sellers' post-sale conduct, prohibiting the seller from failing to honor its promises regarding exclusive or protected territories. Consumer complaints indicate, and the Commission's law enforcement experience confirms, that fraudulent business opportunity sellers often sell the same purportedly exclusive territory to several unsuspecting purchasers.[360] In these circumstances, purchasers who have been lured to invest in an opportunity on the basis of promises of an exclusive territorial lock on their market find that their chances of success are materially reduced by competition from the other purchasers.

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[359] 71 Fed. Reg. at 19,075.

[360] E.g., FTC v. Am. Safe Mktg., No. 1:89-CV-462-RLV (N.D. Ga. 1989).

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees that this prohibition regarding post-sale conduct by the seller is necessary and recommends, therefore, that section 437.6(o) be adopted in the form proposed in the RPBOR.

P. Proposed Section 437.6(p): Third-Party Endorsements and Affiliation

1. Background

To prevent endorsement fraud, proposed section 437.6(p) would prohibit business opportunity sellers from misrepresenting that "any person, trademark or service mark holder, or governmental entity, directly or indirectly benefits from, sponsors, participates in, endorses, approves, authorizes, or is otherwise associated with the sale of the business opportunity or the goods or services sold through the business opportunity."[361] The Commission's enforcement experience reveals that business opportunity frauds often lure consumers by misrepresenting that their opportunities have been approved or endorsed by a government agency or well-known third party.[362] In other instances, business opportunity sellers falsely claim that their opportunities are sponsored by or associated with a charity, or that a charity will benefit from a percentage of sales.[363] The Commission concluded that such claims are material to a purchaser because an

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[361] Cf. TSR, 16 CFR 310.3(a)(vii) (prohibiting misrepresentations concerning "affiliation with, or endorsement or sponsorship by, any person or government entity").

[362] E.g., FTC v. Streamline Int'l, No. 01-6885-CIV-Ferguson (S.D. Fla. 2001) (misrepresented FDA approval); FTC v. Bus. Opportunity Ctr., Inc., No. 95 8429-CIV-Zloch (S.D. Fla. 1995) (misrepresented FDA approval); FTC v. Star Publ'g Group, Inc., No. 00-023 (D. Wyo. 2000) (misrepresented HUD approval); see also FTC v. Hawthorne Commc'ns, No. 93-7002 AAH (JGX) (C.D. Cal. 1993) (order restricting use of testimonials and endorsements in the sale of business opportunities).

[363] E.g., FTC v. Global Assistance Network for Charities, No. 96-2494 PHX RCB (D. Ariz. 1996).

alleged endorsement or shared-profit arrangement may create the impression that the opportunity is legitimate or that the affiliation will enhance sales and profits.[364]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions and recommends, therefore, that section 437.6(p) be adopted in the form proposed in the RPBOR.

Q. Proposed section 437.6(q): Shills

1. Background

Proposed section 437.6(q) addresses one of the most pernicious practices common in fraudulent business opportunity sales – the use of "shill" references to lure unsuspecting consumers to invest in a business opportunity.[365] The Commission has brought many actions against business opportunity sellers who provided prospects with the names of individuals they falsely claimed were independent prior purchasers or independent third parties, but who in fact were paid by the seller to give favorable false reports confirming the seller's claims, especially their earnings claims.[366] The use of paid shills to give false reports induces prospective purchasers into believing that the opportunity is a safe and lucrative investment.

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[364] 71 Fed. Reg. at 19,077.

[365] See id. ("After earnings claims, false testimonials and shill references are the most common Section 5 allegations in Commission business opportunities cases.").

[366] E.g., FTC v. Am. Entm't Distribs., Inc., No. 04-22431-CIV-Martinez (S.D. Fla. 2004); United States v. Vaughn, No. 01-20077-01-KHV (D. Kan. 2001); FTC v. Hart Mktg. Enter. Ltd., Inc., No. 98-222-CIV-T-23 E (M.D. Fla. 1998); FTC v. Inetintl.com, No. 98-2140 (C.D. Cal. 1998); FTC v. Infinity Multimedia, Inc., No. 96-6671-CIV-Gonzalez (S.D. Fla. 1996); FTC v. Allstate Bus. Consultants Group, Inc., No. 95-6634-CIV-Ryskamp (S.D. Fla. 1995).

To address this deceptive practice, proposed section 437.6(q) would contain two related prohibitions. First, it would prohibit any seller from misrepresenting that any person "has purchased a business opportunity from the seller." This would prevent a seller, for example, from claiming that a company employee, locator, or other third party is a prior purchaser of the opportunity, when that is not the case. Second, the provision would prohibit a seller from misrepresenting that any person – such as a locator, broker, or organization that purports to be an independent trade association – "can provide an independent or reliable report about the business opportunity or the experiences of any current or former purchaser." Providing a prospect with a list of brokers who are paid to give favorable reports, for example, would violate this provision because any statement a person on such a list makes would fail the "independence and reliability" prong of this provision.[367]

2. The record and recommendation

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions and recommends, therefore, that section 437.6(q) be adopted in the form proposed in the RPBOR.

R. Proposed Section 437.6(r): Paid Consideration or Prior Relationship

1. Background

Proposed section 437.6(r) was intended to complement the prohibition in section 437.6(q) regarding shills. Proposed section 437.6(r) would prohibit a seller from failing to disclose payments to individuals identified as references, as well as any personal relationships the seller

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[367] E.g., FTC v. Affiliated Vendors Ass'n, Inc., No. 02-CV-0679-D (N.D. Tex. 2002); FTC v. Raymond Urso, No. 97-2680-CIV-Ungaro-Benages (S.D. Fla. 1997); see also 71 Fed. Reg. at 19,077 & n.238.

[368] Indeed, the Commission has long held that the failure to disclose compensation paid to an endorser is a deceptive practice in violation of Section 5. See 71 Fed. Reg. at 19,077.

[369] 71 Fed. Reg. at 19,078.

[370] 73 Fed. Reg. at 16,136.

XI. Proposed Section 437.7: Record Retention

A. Background

Proposed section 437.7 would establish the minimal record retention requirements necessary to document compliance and permit effective Rule enforcement. This section would apply to both the business opportunity seller, as well as its principals, to ensure that records required by the Rule are not destroyed if the seller goes out of business or otherwise ceases operations.[371] As detailed below, sellers and their principals must keep, and make available to the Commission, the following five types of records for a period of three years:

Proposed section 437.7(a)	Each materially different version of all documents required by the Rule;
Proposed section 437.7(b)	Each purchaser's disclosure receipt;
Proposed section 437.7(c)	Each executed written contract with a purchaser;
Proposed section 437.7(d)	Each oral or written cancellation or refund request received from a purchaser; and
Proposed section 437.7(e)	All substantiation upon which the seller relies from the time an earnings claim is made.

The Commission concluded that these limited recordkeeping requirements strike the right balance, requiring no more than necessary for effective law enforcement, while reducing compliance costs.[372]

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[371] 71 Fed. Reg. at 19,078.

[372] Id.

[373] Id.

[374] For example, businesses exempt from Franchise Rule coverage pursuant to the exemption for fractional franchises would not be subjected to coverage by the proposed Business Opportunity Rule because such businesses would meet the criteria of proposed section 437.8. The Commission concluded that this is an appropriate result because the same rationale underlying exemption of these types of businesses from the Franchise Rule would also dictate that they not be covered by the proposed Business Opportunity Rule – i.e., the franchisor is not likely to deceive the prospective franchisee or to subject the prospective franchisee to significant investment risk. Therefore, imposing the requirements of either the Franchise Rule or the

opportunities that are exempt from the Franchise Rule but that should be regulated by the proposed Business Opportunity Rule.

On the other hand, certain businesses carved out of Franchise Rule coverage should not escape regulation by the proposed Business Opportunity Rule – specifically, those exempt from the Franchise Rule's coverage due to the minimum payment exemption[375] or the oral agreement exemption.[376] The Commission concluded that while these two exemptions are warranted in the franchise context to ensure that the significant disclosure costs imposed by the Franchise Rule are

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375 16 CFR 436.2(a)(3)(iii).

376 16 CFR 436.2(a)(3)(iv).

377 71 Fed. Reg. at 19,078.

378 73 Fed. Reg. at 16,133.

379 See, e.g., Babener-RNPR; Pre-Paid Legal-RNPR.

380 See, e.g., Pre-Paid Legal-RNPR; Tupperware-RNPR; IBA-RNPR.

For example, the proposed Business Opportunity Rule contemplates greatly streamlined disclosures, as compared to the Franchise Rule's extensive disclosures.

To enable business opportunity sellers to take advantage of the Business Opportunity Rule's reduced disclosure obligations, as well as to reduce any potential conflicts between existing orders and the proposed Business Opportunity Rule, proposed section 437.9(a) would permit persons under order to petition the Commission for relief consistent with the provisions of the new Rule. The RPBOR would have allowed business opportunities required by FTC or court order to follow the Franchise Rule, 16 CFR Part 436, to petition the Commission to amend the order so that the business opportunity could follow the provisions of the Business Opportunity Rule.

No comments received in response to the RNPR were directed to this provision. However, the staff notes that while the Commission could modify an FTC administrative order, it does not have the authority to modify any order entered by a court. In the case of a court order, the Commission could, however, stipulate to an amendment of the order by the court to allow the business opportunity to follow the provisions of the Business Opportunity Rule. The staff recommends, therefore, that section 437.9(a) be revised to add the phrase "or to stipulate to an amendment of the court order" as follows: "A business opportunity required by prior FTC or court order to follow the Franchise Rule, 16 CFR Part 436, may petition the Commission to amend the order or to stipulate to an amendment of the court order so that the business opportunity may follow the provisions of this part." In addition, the staff notes that the first sentence of section 437.9(a) proposed in the RPBOR is superfluous, and recommends deleting it. The staff agrees with the Commission's previous conclusion that all such determinations regarding the amendment of orders should be made on a case-by-case basis.

[386] 16 CFR 436.10. This approach is consistent with other Commission trade regulation rules. See, e.g., Appliance Labeling Rule, 16 CFR 305.17; Cooling-Off Rule, 16 CFR 429.2; Mail Order Rule, 16 CFR 435.3(b)(2).

[387] Although state laws offering equal or greater protections are not preempted, section 437.6(c) of the proposed Rule would prohibit providing the state and federal disclosures together. See supra

agrees with the Commission's conclusions, and recommends, therefore, that section 437.9(b) be adopted in the form proposed in the RPBOR.

XIV. Proposed Section 437.10: Severability

Finally, proposed section 437.10 would adopt the severability provision currently found in the Franchise Rule at 16 CFR 436.3. This provision would make clear that, if any part of the Rule is held invalid by a court, the remainder will still be in effect.[390]

No comments received in response to the RNPR were directed to this provision. The staff agrees with the Commission's conclusions, and recommends, therefore, that section 437.10 be adopted in the form proposed in the RPBOR.

XV. Conclusion

The Commission's law enforcement history and the record developed during the course of this rulemaking demonstrate the need to update the Business Opportunity Rule. This Report analyzes the entire record to date, and sets forth the staff's recommendation as to the form of the proposed Final Rule and the proposed final Disclosure Document. We welcome comment on this Report, the proposed Final Rule, and the proposed final Disclosure Document, during the next 75 days, as provided by the Commission's Rules of Practice, 16 CFR § 1.13(h).

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[390] This provision is comparable to the severability provisions in other Commission trade regulation rules. E.g., 900-Number Rule, 16 CFR 308.8; TSR, 16 CFR 310.9.

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Cited INPR, RNPR and Workshop Notice Commenters

Aird, Gail
Avon Products, Inc. (“Avon”)
Babener and Associates (‘‘Babener’’)
Bates, Kenneth
Brooks, Douglas
Big Ear, Inc. (“Big Ear”)
Consumer Awareness Institute (‘‘CAI’’)
The Cosmetic, Toiletry and Fragrance Association (‘‘CTFA’’)
Direct Selling Association (‘‘DSA’’)
Durand, Justin
Independent Bakers Association (‘‘IBA’’)
Integrative Health Concepts LLC (“Integrative”)
Jafra Cosmetics International, Inc. (“Jafra Cosmetics”)
Lia Sophia
The Longaberger Company (“Longaberger”)
Princess House
Shaklee Corporation (‘‘Shaklee’’)
Johnson, Scott
Lopez, Nicole
Larkin Hoffman Daly & Lindgren Ltd. (‘‘LHD&L’’)
Maclay Murray and Spens LLP (‘‘MMS’’)
MarketWave, Inc. (“MarketWave”)
Mary Kay, Inc. (‘‘Mary Kay’’)
Melaleuca, Inc. (‘‘Melaleuca’’)
National Black Chamber of Commerce (‘‘NBCC’’)
Parrington, Reid
Planet Antares, Inc. (“Planet Antares”)
Pre-Paid Legal Services, Inc. (‘‘Pre-Paid Legal’’)
Primerica Financial Services, Inc. (‘‘Primerica’’)
Pyramid Scheme Alert (‘‘PSA’’)
Pyramid Watch
Rotolante, Steven
Sonnenschein
The Timberland Co. (‘‘Timberland’’)
Tupperware Brands (“Tupperware”)
Venable, LLP (‘‘Venable’’)
Whittle, Bill

ATTACHMENT B

§ 437.1 Definitions.

The following definitions shall apply throughout this part:

(a) Action means a criminal information, indictment, or proceeding; a civil complaint, cross claim, counterclaim, or third-party complaint in a judicial action or proceeding; arbitration; or any governmental administrative proceeding, including, but not limited to, an action to obtain or issue a cease and desist order, an assurance of voluntary compliance, and an assurance of discontinuance.

(b) Affiliate means an entity controlled by, controlling, or under common control with a business opportunity seller.

(c) Business opportunity means:

(1) A commercial arrangement in which the seller solicits a prospective purchaser to enter into a new business; and

(2) The prospective purchaser makes a required payment; and

(3) The seller, expressly or by implication, orally or in writing, represents that the seller or one or more designated persons will:

(i) Provide locations for the use or operation of equipment, displays, vending machines, or similar devices, owned, leased, controlled or paid for by the purchaser; or

(ii) Provide outlets, accounts, or customers, including, but not limited to, Internet outlets, accounts, or customers, for the purchaser's goods or services; or

(iii) Buy back any or all of the goods or services that the purchaser makes, produces, fabricates, grows, breeds, modifies, or provides, including but

not limited to providing payment for such services as, for example, stuffing envelopes from the purchaser's home.

(d) Designated person means any person, other than the seller, whose goods or services the seller suggests, recommends, or requires that the purchaser use in establishing or operating a new business.

(e) Disclose or state means to give information in writing that is clear and conspicuous, accurate, concise, and legible.

(f) Earnings claim means any oral, written, or visual representation to a prospective purchaser that conveys, expressly or by implication, a specific level or range of actual or potential sales, or gross or net income or profits. Earnings claims include, but are not limited to:

(1) Any chart, table, or mathematical calculation that demonstrates possible results based upon a combination of variables; and

(2) Any statements from which a prospective purchaser can reasonably infer that he or she will earn a minimum level of income (e.g., "earn enough to buy a Porsche," "earn a six-figure income," or "earn your investment back within one year").

(g) Exclusive territory means a specified geographic or other actual or implied marketing area in which the seller promises not to locate additional purchasers or offer the same or similar goods or services as the purchaser through alternative channels of distribution.

(h) General media means any instrumentality through which a person may communicate with the public, including, but not limited to, television, radio, print, Internet, billboard, website, commercial bulk email, and mobile communications.

commencing operation of the business opportunity. Such payment may be made directly or indirectly through a third-party. A required payment does not include payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices for resale or lease.

(q) Seller

§ 437.3 The disclosure document.

In connection with the offer for sale, sale, or promotion of a business opportunity, it is a violation of this Rule and an unfair or deceptive act or practice in violation of Section 5 of the FTC Act, for any seller to:

(a) Fail to disclose to a prospective purchaser the following material information in a single written document in the form and using the language set forth in Appendix A to this part; or if the offer for sale, sale, or promotion of a business opportunity is conducted in Spanish, in the form and using the language set forth in Appendix B to this part; or if the offer for sale, sale, or promotion of a business opportunity is conducted in a language other than English or Spanish, using the form and an accurate translation of the language set forth in Appendix A to this part:

(1) Identifying information. State the name, business address, and telephone number of the seller, the name of the salesperson offering the opportunity, and the date when the disclosure document is furnished to the prospective purchaser.

(2) Earnings claims. If the seller makes an earnings claim, check the “yes” box and attach the earnings statement required by § 437.4. If not, check the “no” box.

(3) Legal actions.

(i) If any of the following persons has been the subject of any civil or

(B) Any affiliate or prior business of the seller; or

(C) Any of the seller's officers, directors, sales managers, or any individual who occupies a position or performs a function similar to an officer, director, or sales manager of the seller.

(ii) If the "yes" box is checked, disclose all such actions in an attachment to the disclosure document. State the full caption of each action (names of the principal parties, case number, full name of court, and filing date). For each action, the seller may also provide a brief accurate statement not to exceed 100 words that describes the action.

(iii) If there are no actions to disclose, check the "no" box.

(4) Cancellation or refund policy. If the seller offers a refund or the right to cancel the purchase, check the "yes" box. If so, state all material terms and conditions of the refund or cancellation policy in an attachment to the disclosure document. If no refund or cancellation is offered, check the "no" box.

(5) References.

(i) State the name, state, and telephone number of all purchasers who purchased the business opportunity within the last three years. If more than 10 purchasers purchased the business opportunity within the last three years, the seller may limit the disclosure by stating the name, state, and telephone number of at least the 10 purchasers within the past three years who are located nearest to the prospective purchaser's location. Alternatively, a seller may furnish a prospective buyer with a list disclosing all purchasers nationwide within the last three years. If

choosing this option, insert the words “See Attached List” without removing the list headings or the numbers 1 through 10, and attach a list of the references to the disclosure document.

(ii) Clearly and conspicuously, and in immediate conjunction with the list of references, state the following: “If you buy a business opportunity from the seller, your contact information can be disclosed in the future to other buyers.”

(6) Receipt. Attach a duplicate copy of the disclosure page to be signed and dated by the purchaser. The seller may inform the prospective purchaser how to return the signed receipt (for example, by sending to a street address, email address, or facsimile telephone number).

(b) Fail to update the disclosures required by paragraph (a) of this section at least quarterly to reflect any changes in the required information, including, but not limited to, any changes in the seller’s refund or cancellation policy, or the list of references; provided, however, that until a seller has 10 purchasers, the list of references must be updated monthly.

§ 437.4 Earnings claims.

In connection with the offer for sale, sale, or promotion of a business opportunity, it is a violation of this Rule and an unfair or deceptive act or practice in violation of Section 5 of the FTC Act, for the seller to:

(a) Make any earnings claim to a prospective purchaser, unless the seller:

(1) Has a reasonable basis for its claim at the time the claim is made;

(2) Has in its possession written materials that substantiate its claim at the time the claim is made;

(3) Makes the written substantiation available upon request to the prospective purchaser and to the Commission; and

(4) Furnishes to the prospective purchaser an earnings claim statement. The earnings claim statement shall be a single written document and shall state the following information:

(i) The title “EARNINGS CLAIM STATEMENT REQUIRED BY LAW” in capital, bold type letters;

(ii) The name of the person making the earnings claim and the date of the earnings claim;

(iii) The earnings claim;

(iv) The beginning and ending dates when the represented earnings were achieved;

(v) The number and percentage of all persons who purchased the business opportunity prior to the ending date in paragraph (a)(4)(iv) of this section who achieved at least the stated level of earnings;

(vi) Any characteristics of the purchasers who achieved at least the represented level of earnings, such as their location, that may differ materially from the characteristics of the prospective purchasers being offered the business opportunity; and

(vii) A statement that written substantiation for the earnings claim will be made available to the prospective purchaser upon request.

(b) Make any earnings claim in the general media, unless the seller:

(1) Has a reasonable basis for its claim at the time the claim is made;

(2) Has in its possession written material that substantiates its claim at the time the claim is made;

(3) States in immediate conjunction with the claim:

(i) The beginning and ending dates when the represented earnings were achieved; and

(ii) The number and percentage of all persons who purchased the business opportunity prior to the ending date in paragraph (b)(3)(i) of this section who achieved at least the stated level of earnings.

(c) Disseminate industry financial, earnings, or performance information unless the seller has written substantiation demonstrating that the information reflects, or does not exceed, the typical or ordinary financial, earnings, or performance experience of purchasers of the business opportunity being offered for sale.

(d) Fail to notify any prospective purchaser in writing of any material changes affecting the relevance or reliability of the information contained in an earnings claim statement before the prospective purchaser signs any contract or makes a payment or provides other consideration to the seller, directly or indirectly, through a third party.

§ 437.5 Spanish and non-English language sales.

(a) If the seller conducts the offer for sale, sale, or promotion of a business opportunity in Spanish, the seller must provide the disclosure document required by § 437.3(a) in the form and language set forth in Appendix B to this part, and the disclosures required by §§ 437.3(a) and 437.4(a) must be made in Spanish.

(b) If the seller conducts the offer for sale, sale, or promotion of a business opportunity in a language other than English or Spanish, the seller must provide the disclosure document

required by § 437.3(a) using the form and an accurate translation of the language set forth in Appendix A to this part, and the disclosures required by §§ 437.3(a) and 437.4(a) must be made in that language.

§ 437.6 Other prohibited practices.

In connection with the offer for sale, sale, or promotion of a business opportunity, it is a

business opportunity;

(f) Fail to make available to prospective purchasers, and to the Commission upon request, written substantiation for the seller's earnings claims;

(g) Misrepresent how or when commissions, bonuses, incentives, premiums, or other payments from the seller to the purchaser will be calculated or distributed;

(h) Misrepresent the cost, or the performance, efficacy, nature, or central characteristics of the business opportunity or the goods or services offered to a prospective purchaser;

(i) Misrepresent any material aspect of any assistance offered to a prospective purchaser;

(j) Misrepresent the likelihood that a seller, locator, or lead generator will find locations, outlets, accounts, or customers for the purchaser;

(k) Misrepresent any term or condition of the seller's refund or cancellation policies;

(l) Fail to provide a refund or cancellation when the purchaser has satisfied the terms and conditions disclosed pursuant to § 437.3(a)(4);

(m) Misrepresent a business opportunity as an employment opportunity;

(n) Misrepresent the terms of any territorial exclusivity or territorial protection offered to a prospective purchaser;

(o) Assign to any purchaser a purported exclusive territory that, in fact, encompasses the same or overlapping areas already assigned to another purchaser;

(p) Misrepresent that any person, trademark or service mark holder, or governmental entity, directly or indirectly benefits from, sponsors, participates in, endorses, approves, authorizes, or is otherwise associated with the sale of the business opportunity or the goods or services sold through the business opportunity;

(q) Misrepresent that any person:

(1) Has purchased a business opportunity from the seller or has operated a business opportunity of the type offered by the seller; or

(2) Can provide an independent or reliable report about the business opportunity or the experiences of any current or former purchaser.

(r) Fail to disclose, with respect to any person identified as a purchaser or operator of a business opportunity offered by the seller:

§ 437.7 Record retention.

ATTACHMENT B

§ 437.9 Outstanding orders; preemption.

(a) A business opportunity required by prior FTC or court order to follow the Franchise Rule, 16 CFR Part 436, may petition the Commission to amend the order or to stipulate to an amendment of the court order so that the business opportunity may follow the provisions of this part.

(b) The FTC does not intend to preempt the business opportunity sales practices laws of any state or local government, except to the extent of any conflict with this part. A law is not in conflict with this Rule if it affords prospective purchasers equal or greater protection, such as registration of disclosure documents or more extensive disclosures. All such disclosures, however, must be made in a separate state disclosure document.

§ 437.10 Severability.

The provisions of this part are separate and severable from one another. If any provision is stayed or determined to be invalid, it is the Commission's intention that the remaining provisions shall continue in effect.

ATTACHMENT C

§ 437.1 Definitions.

The following definitions shall apply throughout this part:

(a) Action means a criminal information, indictment, or proceeding; a civil complaint, cross claim, counterclaim, or third-party complaint in a judicial action or proceeding; arbitration; or any governmental administrative proceeding, including, but not limited to, an action to obtain or issue a cease and desist ~~order~~, and assurance of voluntary compliance. .

(b) Affiliate means an entity controlled by, controlling, or under common control with a business opportunity seller.

(c) Business opportunity means:

(1) A commercial arrangement in which the seller solicits a prospective purchaser to enter into a new business; and

(2) The prospective purchaser makes a required payment; and

(3) The seller, expressly or by implication, orally or in writing, represents that the seller or one or more designated persons will:

(i) Provide locations for the use or operation of equipment, displays, vending machines, or similar devices, ~~on premises neither owned nor~~ leased by the purchaser; or

(ii) Provide outlets, accounts, or customers, including, but not limited to, Internet outlets, accounts, or customers, for the purchaser's goods or services; or

(iii) Buy back any or all of the goods or services that the purchaser makes, produces, fabricates, grows, breeds, ~~modifies~~, or provides, including but

not limited to providing payment for such services as, for example, stuffing envelopes from the purchaser's home.

(d) Designated person means any person, other than the seller, whose goods or services the seller suggests, recommends, or requires that the purchaser use in establishing or operating a new business.

(e) Disclose or state means to give information in writing that is clear and conspicuous, accurate, concise, and legible.

(f) Earnings claim means any oral, written, or visual representation to a prospective purchaser that conveys, expressly or by implication, a specific level or range of actual or potential sales, or gross or net income or profits. Earnings claims include, but are not limited to:

(1) Any chart, table, or mathematical calculation that demonstrates possible results based upon a combination of variables; and

(2) Any statements from which a prospective purchaser can reasonably infer that he or she will earn a minimum level of income (e.g., "earn enough to buy a Porsche," "earn a six-figure income," or "earn your investment back within one year").

(g) Exclusive territory means a specified geographic or other actual or implied marketing area in which the seller promises not to locate additional purchasers or offer the same or similar goods or services as the purchaser through alternative channels of distribution.

(h) General media means any instrumentality through which a person may communicate with the public, including, but not limited to, television, radio, print, Internet, billboard, website, and commercial bulk email .

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(ħ) Quarterly means as of January 1, April 1, July 1, and October 1. |

(ѳ) Required payment means all consideration that the purchaser must pay to the seller or an affiliate, either by contract or by practical necessity, as a condition of obtaining or commencing operation of the business opportunity. Such payment may be made directly or indirectly through a third-party. A required payment does not include payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices for resale or lease. |

(þ) Seller means a person who offers for sale or sells a business opportunity. |

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(ꟈ) Written or in writing means any document or information in printed form or in any form capable of being downloaded, printed, or otherwise preserved in tangible form and read. It includes: type-set, word processed, or handwritten documents; information on computer disk or CD-ROM; information sent via email; or information posted on the Internet. It does not include mere oral statements. |

§ 437.2 The obligation to furnish written documents.

In connection with the offer for sale, sale, or promotion of a business opportunity, it is a violation of this Rule and an unfair or deceptive act or practice in violation of Section 5 of the Federal Trade Commission Act ("FTC Act") for any seller to fail to furnish a prospective purchaser with the material information required by §§ 437.3(a) and 437.4(a) of this part in writing at least seven calendar days before the earlier of the time that the prospective purchaser:

(a) Signs any contract in connection with the business opportunity sale; or

(b) Makes a payment or provides other consideration to the seller, directly or indirectly through a third party.

§ 437.3 The disclosure document.

In connection with the offer for sale, sale, or promotion of a business opportunity, it is a violation of this Rule and an unfair or deceptive act or practice in violation of Section 5 of the FTC Act, for any seller to:

(a) Fail to disclose to a prospective purchaser the following material information in a single written document in the form and using the language set forth in Appendix A to this part:

(1) Identifying information. State the name, business address, and telephone number of the seller, the name of the salesperson offering the opportunity, and the date when the disclosure document is furnished to the prospective purchaser.

(2) Earnings claims. If the seller makes an earnings claim, check the “yes” box and attach the earnings statement required by § 437.4. If not, check the “no” box.

(3) Legal actions.

the 10 years immediately preceding the date that the business opportunity is offered, check the “yes” box:

(A) The seller;

(B) Any affiliate or prior business of the seller; or

(C) Any of the seller’s officers, directors, sales managers, or any individual who occupies a position or performs a function similar to an officer, director, or sales manager of the seller.

(ii) If the “yes” box is checked, disclose all such actions in an attachment to the disclosure document. State the full caption of each action (names of the principal parties, case number, full name of court, and filing date).

(iii) If there are no actions to disclose, check the “no” box.

(4) Cancellation or refund policy. If the seller offers a refund or the right to cancel the purchase, check the “yes” box. If so, state the terms of the refund or cancellation policy in an attachment to the disclosure document. If no refund or cancellation is offered, check the “no” box.

(5) References.

(i) State the name, ~~city and~~ state, and telephone number of all purchasers who purchased the business opportunity within the last three years. If more than 10 purchasers purchased the business opportunity within the last three years, the seller may limit the disclosure by stating the name, ~~and~~ state, and telephone number of at least the 10 purchasers within the

past three years who are located nearest to the prospective purchaser's location. Alternatively, a seller may furnish a prospective buyer with a list disclosing all purchasers nationwide within the last three years. If choosing this option, insert the words "See Attached List" without removing the list headings or the numbers 1 through 10, and attach a list of the references to the disclosure document.

(ii) Clearly and conspicuously, and in immediate conjunction with the list of references, state the following: "If you buy a business opportunity from the seller, your contact information can be disclosed in the future to other buyers."

(6) Receipt. Attach a duplicate copy of the disclosure page to be signed and dated by the purchaser. The seller may inform the prospective purchaser how to return the signed receipt (for example, by sending to a street address, email address, or facsimile telephone number).

(b) Fail to update the disclosures required by paragraph (a) of this section at least quarterly to reflect any changes in the required information, including, but not limited to, any changes in the seller's refund or cancellation policy, or the list of references; provided, however, that until a seller has 10 purchasers, the list of references must be updated monthly.

§ 437.4 Earnings claims.

In connection with the offer for sale, sale, or promotion of a business opportunity, it is a violation of this Rule and an unfair or deceptive act or practice in violation of Section 5 of the FTC Act, for the seller to:

(a) Make any earnings claim to a prospective purchaser, unless the seller:

available to the prospective purchaser upon request.

(b) Make any earnings claim in the general media, unless the seller:

(1) Has a reasonable basis for its claim at the time the claim is made;

(2) Has in its possession written material that substantiates its claim at the time the claim is made;

(3) States in immediate conjunction with the claim:

(i) The beginning and ending dates when the represented earnings were achieved; and

(ii) The number and percentage of all persons who purchased the business opportunity prior to the ending date in paragraph (b)(3)(i) of this section who achieved at least the stated level of earnings.

(c) Disseminate industry financial, earnings, or performance information unless the seller has written substantiation demonstrating that the information reflects the typical or ordinary financial, earnings, or performance experience of purchasers of the business opportunity being offered for sale.

(d) Fail to notify any prospective purchaser in writing of any material changes affecting the relevance or reliability of the information contained in an earnings claim statement before the prospective purchaser signs any contract or makes a payment or provides other consideration to the seller, directly or indirectly, through a third party.

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§ 437.5

Other prohibited practices.

In connection with the offer for sale, sale, or promotion of a business opportunity, it is a violation of this part and an unfair or deceptive act or practice in violation of Section 5 of the FTC Act for any seller, directly or indirectly through a third party, to:

(a) Disclaim, or require a prospective purchaser to waive reliance on, any statement made in any document or attachment that is required or permitted to be disclosed under this Rule;

(b) Make any claim or representation, orally, visually, or in writing, that is inconsistent with or contradicts the information required to be disclosed by §§ 437.3 (basic disclosure document) and 437.4 (earnings claims document) of this Rule;

(c) Include in any disclosure document or earnings claim statement any materials or information other than what is explicitly required or permitted by this Rule. For the sole purpose of enhancing the prospective purchaser's ability to maneuver through an

electronic version of a disclosure document or earnings statement, the seller may include scroll bars and internal links. All other features (e.g., multimedia tools such as audio, video, animation, or pop-up screens) are prohibited;

(d) Misrepresent the amount of sales, or gross or net income or profits a prospective purchaser may earn or that prior purchasers have earned;

(e) Misrepresent that any governmental entity, law, or regulation prohibits a seller from:

(1) furnishing earnings information to a prospective purchaser; or

directly or indirectly benefits from, sponsors, participates in, endorses, approves, authorizes, or is otherwise associated with the sale of the business opportunity or the goods or services sold through the business opportunity;

(q) Misrepresent that any person: |

(1) Has purchased a business opportunity from the seller or has operated a business opportunity of the type offered by the seller; or

(2) Can provide an independent or reliable report about the business opportunity or the experiences of any current or former purchaser.

(r) Fail to disclose, with respect to any person identified as a purchaser or operator of a business opportunity offered by the seller:

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§ 437.~~6~~ Record retention. |

To prevent the unfair and deceptive acts or practices specified in this Rule, business opportunity sellers and their principals must prepare, retain, and make available for inspection by Commission officials copies of the following documents for a period of three years:

(a) Each materially different version of all documents required by this Rule;

(b) Each purchaser's disclosure receipt;

(c) Each executed written contract with a purchaser; and

(d) All substantiation upon which the seller relies for each earnings claim from the time each such claim is made.

§ 437.~~7~~ Franchise exemption. |

The provisions of this Rule shall not apply to any business opportunity that constitutes a "franchise," as defined in the Franchise Rule, 16 CFR Part 436, provided however, that the provisions of this Rule shall apply to any such franchise if it is exempted from the provisions of Part 436 because, either:

(a) under § 436.8(a)(1), the total of the required payments or commitments to make a required payment, to the franchisor or an affiliate that are made any time from before to within six months after commencing operation of the franchisee's business is less than $500, or

(b) Under § 436.8(a)(7), there is no written document describing any material term or aspect of the relationship or arrangement.

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§ 437.~~8~~ Outstanding orders; preemption. |

(a) ~~If an outstanding FTC or court order applies to a person, but imposes requirements that are inconsistent with any provision of this regulation, the person may petition the Commission to amend the order. In particular, business opportunities~~ |

required by FTC or court order to follow the Franchise Rule, 16 CFR Part 436, may |

petition the Commission to amend the order |

so that the business opportunity may follow the provisions of this part. |

(b) The FTC does not intend to preempt the business opportunity sales practices laws of any state or local government, except to the extent of any conflict with this part. A law is not in conflict with this Rule if it affords prospective purchasers equal or greater protection, such as registration of disclosure documents or more extensive disclosures. All such disclosures, however, must be made in a separate state disclosure document.

§ 437.~~9~~ Severability. |

The provisions of this part are separate and severable from one another. If any provision is stayed or determined to be invalid, it is the Commission's intention that the remaining provisions shall continue in effect.

DISCLOSURE OF IMPORTANT INFORMATION ABOUT BUSINESS OPPORTUNITY

Required by the Federal Trade Commission, Rule 16 C.F.R. Part 437

Name of Seller: Address:

Phone: Salesperson: Date:

[Name of Seller] has completed this form, which provides important information about the business opportunity it is offering you. The Federal Trade Commission, an agency of the federal government, requires that [Name of Seller] complete this form and give it to you. However, the Federal Trade Commission has not seen this completed form or checked that the information is true. Make sure that this information is the same as what the salesperson told you about this opportunity.

LEGAL ACTIONS: Has [Name of Seller] or any of its key personnel been the subject of a civil or criminal action involving misrepresentation, fraud, securities law violation, or unfair or deceptive practices, including violations of any FTC Rule, within the past 10 years?

† YES Æ If the answer is yes, [Name of Seller] must attach a list of all such legal actions to this form.

† NO

CANCELLATION OR REFUND POLICY: Does [Name of Seller] offer a cancellation or refund policy?

† YES Æ If the answer is yes, [Name of Seller] must attach a statement describing this policy to this form.

† NO

EARNINGS: Has [Name of Seller] or its salesperson discussed how much money purchasers of this business opportunity can earn or have earned? In other words, have they stated or implied that purchasers can earn a specific level of sales, income, or profit?

† YES Æ If the answer is yes, [Name of Seller] must attach an Earnings Claims Statement to this form. Read this statement carefully. You may wish to show this information to an advisor or accountant.

† NO

REFERENCES: In the section below, [Name of Seller] must provide you with contact information for at least 10 people who have purchased a business opportunity from it. If fewer than 10 are listed, this is the total list of all purchasers. You may wish to contact the people below to compare their experiences with what [Name of Seller] told you about the business opportunity.

Note: If you purchase a business opportunity from [Name of Seller], your contact information can be disclosed in the future to other potential buyers.

	Name	State	Telephone Number		Name	State	Telephone Number
1.				6.			
2.				7.			
3.				8.			
4.				9.			
5.				10			

Signature: _____ Date: _____

By signing above, you are acknowledging that you have received this form. This is not a purchase contract. To give you enough time to research this opportunity, the Federal Trade Commission requires that after you receive this form, [Name of Seller] must wait at least seven calendar days before asking you to sign a purchase contract or make any payments.

For more information about business opportunities in general: Visit the FTC's website at www.ftc.gov/bizopps or call 1-877-FTC-HELP (877-382-4357). You can also contact your state's Attorney General.

DIVULGACIÓN DE INFORMACIÓN IMPORTANTE SOBRE OPORTUNIDAD DE NEGOCIO

Formulario requerido por la Comisión Federal de Comercio (FTC)
Regla 16 de la Parte 437 del Código de Regulaciones Federales

Nombre del Vendedor: Domicilio:
Teléfono: Representante de Ventas: Fecha:

[Nombre del Vendedor] completó el presente formulario y en el mismo suministra información importante sobre la oportunidad de negocio que le está ofreciendo. La Comisión Federal de Comercio (Federal Trade Commission, FTC), una agencia del gobierno federal, le requiere a la compañía [Nombre del Vendedor] que complete el presente formulario y que se lo entregue a usted. Pero la FTC no ha visto este formulario completado por la compañía ni ha verificado que la información indicada sea veraz. Asegúrese de que la información contenida en el presente