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FEDERAL TRADE COMMISSION

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FEDERAL TRADE COMMISSION

In the Matter of: )  
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FRANCHISE RULE ) Matter No. R-511003

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Thursday, August 21, 1997

Federal Trade Commission  
55 East Monroe Street, Suite 1860  
Chicago, Illinois 60671

The above-entitled matter came on for meeting pursuant to  
notice, at 9:05 a.m.

APPEARANCES:

ON BEHALF OF THE FEDERAL TRADE COMMISSION :

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1 open to the public as they see fit to come in and offer what  
2 comments they wish on the ANPR or the Franchise Rule or any  
3 other related issues. And that meeting will begin at 9:00 and  
4 we will go until 3:00 o'clock.

5 I also want to make sure that everybody is aware that  
6 the Commission has extended the comment period. The comment  
7 period now will close at the end of the year literally, December  
8 31st, so there's still plenty of opportunity for people to  
9 continue to make comments if they wish or to supplement their  
10 comments. And we would appreciate that.

11 I also want to mention that we're going to have future  
12 workshops. As I mentioned, this is the second in a series of  
13 six. The next workshop will be in New York City on September  
14 18th, and at that meeting we'll focus exclusively on franchise  
15 sales. And among other issues, we'll discuss revising the  
16 Franchise Rule based upon the UFOC model, Internet issues,  
17 programming, international sales and proposals to develop an  
18 industry compliance program. So anyone interested in attending  
19 the New York meeting or any of the other workshops, by all means  
20 you can let us know that today or call us at the Commission in  
21 the next weeks.

22 Before we begin, I also want to mention that I thank  
23 everybody for coming today and participating in this meeting.  
24 It is a small meeting, but I think that that's understandable  
25 given the nature of the subject matter and also the fact that we

1 are having a series of workshops. We believe it's important at  
2 the Commission to open up the process and allow as much public  
3 participation in helping the Commission staff understand the  
4 issues, understand the industry, so that when we go to the  
5 Commission to make recommendations on revising the rule, we have  
6 a full record of support as well as, again, the opportunity for  
7 input from the public. So even though today's meeting is small,  
8 it's not the quantity that counts. It's the quality. And hope  
9 that we have a great discussion today and really help us to  
10 better understand the nature of business opportunities.

11 So with that, what I would like to do is have  
12 introductions. We'll go around the table and please state your  
13 name for the record, what organization, if any, you are with,  
14 and any particular concerns that you may have. And I mean a  
15 real brief statement. And then we'll go into the substantive  
16 areas. So I'm going to ask Myra to open this up.

17 MS. HOWARD: I'm Myra Howard, an attorney at the  
18 Federal Trade Commission working with Steve on the Franchise  
19 Rule project. And I'll just leave it at that.

20 MR. D'ALESSANDRO: I'm John D'Alessandro. I'm on the  
21 board of the American Franchisee Association, which represents  
22 14,000, some 7,000 franchisees with some 14,000 outlets across  
23 the United States. I also am an independent distributor for  
24 Quaker State in the ten minute oil change business.

25 MR. FINNIGAN: Dave Finnigan. I'm an attorney with the

1 Illinois Secretary of State in the Illinois Securities  
2 Department. We just recently passed legislation regulating  
3 business opportunities in the State of Illinois. It went into  
4 effect in January of 1996. So I'm basically here to express  
5 some of the experiences that we've incurred under the law and  
6 find out and to learn more about how we can make our law a  
7 better law.

8 MR. WIECZOREK: Dennis Wieczorek. I'm a partner with  
9 Rudnick & Wolfe in Chicago. I'm here on behalf of the  
10 International Franchise Association and a number of franchisors.  
11 My primary concern here is that if a business opportunity rule  
12 is created, that it provide for appropriate exemptions that are  
13 applicable to franchisors and to other companies who would  
14 traditionally not be viewed as business opportunities.

15 MR. BENNETT: My name is Mike Bennett. I work for the  
16 Longaberger Company. We're a direct selling company based in  
17 Ohio but with independent sales associates in all 50 states.  
18 They market a line of home decorative products through in-home  
19 shows or parties, much like Tupperware parties, and we're  
20 members of the Direct Selling Association and are here in  
21 support of the comments filed by DSA.

22 MR. BROWN: My name is John Brown. I'm an attorney  
23 with Amway Corporation. Amway offers a direct selling  
24 opportunity throughout the United States. And our interest in  
25 these proceedings is that we continue not to be a business



1 opportunity for purposes of the FTC Trade Regulation Rule or to  
2 be deemed a franchise, for that matter.

3 MR. ELLMAN: Eric Ellman with the Direct Selling  
4 Association. And our trade association represents 150 direct  
5 selling companies and 7.2 million direct sellers nationwide.  
6 Several of those companies are represented here at the table  
7 today, and we appreciate their support and their interest in  
8 this rule-making process. Direct selling, as John Brown had  
9 just mentioned, has never been considered either a business  
10 opportunity or a franchise type of system. And we have some  
11 valuable comments which we have filed which I can see if we can  
12 get into toward the end of the day and leave it at that.

13 MR. GEU: My name is Rick Geu. I'm with the Pampered  
14 Chef with headquarters in Addison, Illinois. Pampered Chef is a  
15 direct selling company that markets high quality kitchen tools  
16 and utensils with a home party plan. We've been a member of the  
17 Direct Selling Association since 1986. And we currently have  
18 about 40,000 active sales consultants across all 50 states and  
19 also came here in support of the Direct Selling Association's  
20 proposal.

21 MR. TOPOROFF: And again, I'm Steve Toporoff in the  
22 Division of Marketing Practices at the Commission.

23 Okay. The first item on the agenda is an overview of  
24 the business opportunities issues and the ANPR proposals. And I  
25 will be real quick.

1           The Commission has an extensive law enforcement history  
2 targeting deceptive and fraudulent sale of some business  
3 opportunities. Since the Rule was promulgated, the Commission  
4 has pursued over 130 cases against over 450 corporations and  
5 individuals for various rule violations or deceptive practices.  
6 And the majority of those cases have been against business  
7 opportunities.

8           Since 1995 alone, the Commission has pursued  
9 approximately 44 business opportunity cases. I note that the  
10 comment from the National Consumers League also observes that  
11 business opportunity type complaints rank among the top ten  
12 consumer complaints that that organization receives each year.  
13 And indeed, with our work with state governments, we know that  
14 state securities offices and state attorney general's offices  
15 also bring a significant number of business opportunity  
16 disclosure registration and deceptive acts type cases each year.

17

18           At the same time, I want to note that numerous  
19 franchisors and their representatives have told us through our  
20 various comment periods that they would like to see the  
21 separation of regulation for business opportunities and  
22 franchises, in part, and these are more or less their words,  
23 they no longer want to suffer the stigma of being associated  
24 with business opportunities.

25           So today, we are beginning to take a hard look at the

1 Rule's disclosure requirements for business opportunities. Does  
2 our disclosure regime work, and how could it possibly be  
3 improved. We also want to explore other approaches that the  
4 Commission should consider regarding deceptive business  
5 opportunity sales. For example, one suggestion that was offered  
6 in the comments by John Baer, who unfortunately could not make  
7 it today, he cancelled, I believe yesterday, was to adopt some  
8 kind of cooling off period for business opportunity sales.  
9 Instead of just disclosure, which fraudulent companies probably  
10 aren't going to comply with anyway, perhaps there just should be  
11 some kind of cooling off period. So that's one idea of an  
12 alternative to a disclosure type of regime. And we can explore  
13 others.

14           So with that background, I'm going to turn it over to  
15 Myra. The first substantive item on the agenda is an overview  
16 of the business opportunity industry.

17           MS. HOWARD: Well, as Steve said, we are, at the  
18 Commission, are fairly familiar with fraudulent biz op's. What  
19 we're trying to do here is get an idea of the whole picture of  
20 the biz op industry to fill in the picture, because we really  
21 are unaware of a lot of what's going on. So, if we can start  
22 off with big picture, we will then start whittling it down. So,  
23 the first topic I would really like to find out about is just to  
24 know what types of biz ops are sold. What's popular these days.  
25 You know, what isn't. And I'll open that up if anyone cares to

1 say. David, you look like you were.

2 MR. D'ALESSANDRO: What do you mean sold, business  
3 opportunities. If somebody comes to me and says, I've got  
4 something for you to buy, what am I buying? I don't know.

5 MS. HOWARD: Well, what I'm referring to is what types  
6 of products or services are being sold as business  
7 opportunities.

8 MR. D'ALESSANDRO: Products sold. Not businesses  
9 sales you're talking about.

10 MR. TOPOROFF: Actually, it's a combination of the two.  
11 I think perhaps a better way to start off is, let's ask David,  
12 who, do you do registrations in Illinois?

13 MR. FINNIGAN: We do registrations. I'm on the  
14 enforcement side of it. So, I guess the caveats I should make  
15 is that, one, our law has been in effect since the 1st of  
16 January '96. We have not sat down and done any comprehensive  
17 review or statistical overview. So, my comments are basically  
18 going to be anecdotal based on my experience as to discussions  
19 with other persons. But it's been my experience, considering  
20 the number of cases that we have looked at, that it seemed that  
21 in the past the most popular type of ones that we went after  
22 and, again, my viewpoint tends to be towards the ones which we  
23 consider to be questionable or fraudulent. And so, perhaps some  
24 comments from the other persons who represent the industry might  
25 be also helpful.

1           It seemed to me that a lot of the popular business  
2 opportunities that we saw out there and the ones that were  
3 generating a great deal of income involved getting into real  
4 estate training on how to purchase real estate or tax deeds or  
5 things of that nature. What I've started seeing now seems to  
6 be, it's sort of a vending machine business opportunity, but in  
7 this case vending machines that sell prepaid phone cards we  
8 started to see. So that seems to have been a popular one that  
9 we have seen.

10           But frankly, what I was talking about with Phil when we  
11 went over this, it seems that business opportunities that, you  
12 know, people's imagination and creativity is unlimited and it's  
13 hard to say that there's any one type of business opportunity  
14 that's very popular out there. All I can say is that from our  
15 limited experience, real estate seemed to be a big area and then  
16 it's been moving into recently we've been seeing cases or  
17 advertisements for phone cards, phone card vending machines.

18           MS. HOWARD: Okay. Dennis?

19           MR. WIECZOREK: Let me comment. I don't know that  
20 there's anybody that represents the business opportunity  
21 industry here, period. If it's an industry, it's sort of a  
22 subterranean industry. The best way to decide who's doing it is  
23 to open the classifieds and see a list of business  
24 opportunities. Franchisors don't consider themselves business  
25 opportunities. The direct selling people don't. And I think if

1 you go to the states, and I don't know if you have an idea of  
2 how many are registered, but our understanding of registration  
3 in states with business opportunity laws was that there will be  
4 a few registrations of what you would call pure business  
5 opportunities and then there would be, depending on the states,  
6 some that no one would ever consider to be business  
7 opportunities, but they happen to fall within the broad language  
8 of one or more of those statutes.

9 An example is, I think, Nebraska. Nebraska has a very  
10 broad reach. And I know of some major manufacturers who have  
11 sales reps or distributors who have no alternative but to be  
12 registered in several of the states that sell business. There  
13 are regular business opportunities. So, if we talk about  
14 business opportunities in that sense, there's probably very  
15 limited representation here and I don't know if you had a  
16 hundred meetings that many business opportunity types would show  
17 up anyway. I suppose that, you know, franchises could be viewed  
18 as, franchisors go out and sell and say, we have a wonderful  
19 business opportunity for you, but they are not doing that  
20 because they feel that it fits within the legal definition of  
21 business opportunity.

22 MS. HOWARD: John?

23 MR. BROWN: I would support exactly what Dennis is  
24 saying. And that is, generically speaking, there are a number  
25 of business opportunities being made available which strictly

1 speak under either the state laws or the FTC Rule are not deemed  
2 business opportunities. The Direct Selling Association, I  
3 think, can be characterized as an association that represents  
4 exempt business opportunities. And franchises, just as many  
5 franchisors will avoid the term of art business opportunity so  
6 that there's no confusion that they might be deemed a business  
7 opportunity under the law, likewise I think it's a common  
8 practice in the direct selling industry for companies to  
9 characterize what they offer as an income earning opportunity so  
10 as not to be viewed as a business opportunity, or at least not  
11 to create that presumption under the law.

12           And indeed, I think it's fair to comment that there are  
13 probably at least a few DSA members who have structured their  
14 income earning opportunity in such a way as to ensure that  
15 they're not subject to the regulations of the Business  
16 Opportunity Act, and we've had very frank discussions within our  
17 own industry, lawyer counsel meetings, government relation  
18 committee meetings, where we've simply made the point that, you  
19 know, business opportunity laws are something to be avoid. So  
20 when you go to a DSA seminar, someone will explain business  
21 opportunity laws and how to structure your operation so that you  
22 do not find yourself regulated, because it's viewed as something  
23 being heavy regulation, particularly with some of the state laws  
24 that it's simply too expensive, too cumbersome to handle. And I  
25 think that is the answer to the question of why does it seem

1 there's a lack of registrations under the biz op laws, it's  
2 because most sensible companies will make a special effort to  
3 avoid that regulation.

4 MR. TOPOROFF: Well, let's take a step back then.  
5 Let's not use the term business opportunity, because that is a  
6 loaded term. Let's use John's term, income opportunities.  
7 Let's forget about registration or what regulations might apply  
8 to these sales. Let's talk about just generally what kind,  
9 because before we get to tackling what kind of registration or  
10 what kind of disclosure the commission should consider, it's  
11 helpful to get a broader picture of just generally what is being  
12 sold out there, what kinds of opportunities are available to the  
13 public, the big picture. And that way we can take a step back  
14 and start looking at the pieces. So instead of using the term  
15 biz op or business opportunity, let's just talk in terms of  
16 income-producing opportunities.

17 MS. HOWARD: Well, Eric, I mean, what type of  
18 income-earning opportunities do your members offer?

19 MR. ELLMAN: It's really quite vast, the products and  
20 services that our association members and their sales people  
21 offer. Well, for example, here it's Longaberger baskets. It's  
22 Pampered Chef high quality kitchen ware, and Amway, which sells  
23 quite a number of products and services. It's encyclopedias  
24 like World Book, which is also headquartered here in Chicago.  
25 It's vacuum cleaners and it's quite a wide variety of products



1 and services. And the field of direct selling has been growing  
2 rapidly over the last number of years rather consistently, and  
3 it's really hard to predict what also might sell in the future.  
4 But we sell quite a lot of everything.

5 MS. HOWARD: Okay. And in terms of services, what  
6 types of services?

7 MR. ELLMAN: Well, we have a couple companies which  
8 have just gone into the direct selling business, direct selling  
9 long distance, which is they're offering long distance plans and  
10 selling in the person-to-person methods that our members  
11 traditionally sell in over coffee tables in living rooms and  
12 kitchen tables and that sort of thing.

13 Some of our member companies offer services as well.  
14 And it is, you know, it can be quite broad.

15 MS. HOWARD: Okay.

16 MR. TOPOROFF: Are most of your members, would you  
17 consider them as multi-level marketing type companies?

18 MR. ELLMAN: No. I would say that, I'm trying to  
19 remember the latest statistic. We have 150 corporate members.  
20 Better than half, probably close to two-third now, is probably  
21 multi-level. It's been a growing trend over the last number of  
22 years into the multi-level method of marketing.

23 In fact, the New York Times last year, I guess,  
24 published a front page article on the growth of direct selling  
25 in general and specifically focused on multi-level marketing as

1 companies, corporations continue to downsize or right size or  
2 whatever the term that you want to use, is white collar people  
3 who are losing their jobs are moving into direct selling,  
4 including multi-level marketing as well. But it wasn't that  
5 long ago that multi-level marketing was a small percentage. It  
6 is a growing part of our business.

7 MR. TOPOROFF: Dennis, you said that you represent at  
8 times various distributorships or licenses, license  
9 arrangements. Could you explain that a little bit?

10 MR. WIECZOREK: Well, if you have a, I mean, it could  
11 be a Fortune 100 company that is distributing its products  
12 through distributors, through sales reps, et cetera, and they  
13 find at times that if they require either by contract or by  
14 practice that any of these distributors or reps buy anything at  
15 all, whether its samples or demos or any kinds of materials that  
16 they potentially are subject to certain of the business  
17 opportunity, state business opportunity laws.

18 Now, a number of the state business opportunity laws  
19 have large company exemptions, so it's not a problem under the  
20 more modern laws. And actually some of the older laws, the  
21 North Carolinas and South Carolinas and Georgias, they have  
22 exemptions that apply to the offering of a marketing plan in  
23 conjunction with the use of a trademark, a registered trademark.

24 But there are a number of, it's a patchwork quilt,  
25 where there may be, in California, it may be in Nebraska and it

1 may be in Utah where some of these large companies will have to  
2 be registered in order to do business that no one ever conceived  
3 of being covered by these laws. Now, for every one of these  
4 companies that is out there complying or making a serious effort  
5 to look at these laws, there's probably ten to a hundred times  
6 that many that are either blissfully ignorant of the business  
7 opportunity laws or they ignore the business opportunity laws.  
8 Again, mostly, I would say legitimate companies that just don't,  
9 can't conceive of the notion that they would be characterized,  
10 stigmatized, by being called a business opportunity.

11 So, I mean, that's a big problem for companies who are  
12 out there doing business and trying to evaluate what's going on  
13 from state to state. I'm not necessarily arguing for preemption  
14 of state business opportunity laws, and it's probably not  
15 something that is on the agenda, but maybe it's something we can  
16 talk about at some point today. But the laws are, even more so  
17 than the franchise laws, state business opportunity laws go from  
18 A to Z in terms of coverage, exemptions, applicability, very,  
19 very patchwork in nature.

20 MR. TOPOROFF: John, did you have something to add to  
21 that?

22 MR. BROWN: Yeah. Just a general observation regarding  
23 the kinds of opportunities out there. In thinking about them,  
24 I've tended to break them down into two very broad categories.  
25 One is the opportunity that, in effect, there's perhaps almost

1 no price or very, very small price to be paid for the  
2 opportunity itself. And that is, with direct selling  
3 opportunities, most companies like to say it doesn't cost  
4 anything to become a distributor of our products. And that the  
5 materials that one receives may be provided at cost and there's  
6 not a significant cost associated with it so that you're not  
7 really selling the opportunity. All that you sell as a company  
8 are the trademarked products themselves. And, you know, if a  
9 person becomes a distributor and never sells the product, well  
10 then they became a distributor and they never sold a product.

11           And so, what that kind of opportunity is characterized  
12 chiefly by an expense over time of purchasing goods for resale.  
13 Whereas other business opportunities in some of the more  
14 legendary ones that go back into the '60's and '70's, and I'm  
15 thinking of chinchilla farms and some of the vending operations,  
16 Jerusalem Artichokes I recall from about a decade ago. There  
17 the focus was not on a trademarked product that was being made  
18 available. That was the cost over time, but the cost was the  
19 cost of those goods or that equipment that one would purchase in  
20 order to produce the goods that would be sold. And you tend to  
21 find, within the realm of business opportunities, whether  
22 they're exempt or covered business opportunities under law, they  
23 break down into those two categories. And at least the ones  
24 that were legendary rarely involved the sale of brand name  
25 products, whether it was the company's own brand name or some

1 other brand name, but some of the, at least best known  
2 problematic business opportunities were the worm farms and the  
3 chinchilla farms and artichoke farming opportunities.

4 And so I just wanted to, you know, add that  
5 characterization to the mix.

6 MS. HOWARD: You bring up a lot of different types of  
7 income-earning opportunities. I'd like for us to talk a little  
8 bit about how these are sold. What are the methods that are  
9 used? I mean, for instance, we know there's a lot of  
10 telemarketing of these types of opportunities. What other  
11 methods?

12 MR. D'ALESSANDRO: I think you've got to be careful  
13 when you say sold. This gentleman is saying, hey, you're not  
14 paying anything to come into business and be a distributor of  
15 ours. If you're not paying any money to somebody, what do you  
16 have to lose other than your time, which you've made a decision  
17 to give to that company. So, are we selling something or are we  
18 not selling something.

19 MS. HOWARD: Another way of putting it is how are these  
20 being offered?

21 MR. FINNIGAN: What we are seeing, as Dennis mentioned,  
22 the classified ads. We survey also ads in various magazines,  
23 Entrepreneur being one. We've seen advertisements now. There  
24 is an Internet web page in which they do advertise  
25 income-earning opportunities. So I guess those would be the

1 three main ones I've seen, just the classified advertisements,  
2 the newspaper magazines. Recently there was another big one.  
3 It's through seminars which are advertised on T.V. or in  
4 newspapers. There was recently one in a large central Illinois  
5 city advertising a seminar that was going to occur on actually  
6 it was this Monday to learn how to find income-earning  
7 opportunities.

8 So it's a variety of ways. The trade shows and  
9 seminars, classified ads with an 800 number. We've seen some  
10 Internet.

11 MR. D'ALESSANDRO: I think you've probably seen some on  
12 T.V.

13 MR. BROWN: Infomercials.

14 MR. D'ALESSANDRO: Like the early morning T.V.

15 MS. HOWARD: Is there any one particular method that  
16 you see as really being up and coming these days?

17 MR. ELLMAN: I would have to say the Internet, just  
18 because I'm on the Internet quite a bit. And I've sort of  
19 fallen into some news groups that do nothing but offer business  
20 opportunities. And that is a haven, I would think that that  
21 would be a haven for people perpetuating opportunities that are  
22 fraudulent or otherwise somewhat amiss. And I'm always getting  
23 unsolicited E-mail telling me that I can make thousands of  
24 dollars a week from my own home with very little effort as well.

25 But I would submit that that's a significantly booming

1 field, the electronic method.

2 MR. TOPOROFF: Do other people have experience with  
3 that, with the Internet and sales that could add to the subject?

4 MR. FINNIGAN: We have one case that involved a web  
5 page that was advertising a business opportunity. I would say  
6 that's a pretty big area. It has all the keys, for somebody who  
7 wants to conduct fraudulent activity, it has all the keys. It  
8 has the anonymous ability to create fictitious accounts. An  
9 ability to make contact and send information relatively  
10 anonymously and very difficult for, you know, for regulators to  
11 track them down and not a lot of regulation.

12 I think that's going to be an up and coming area. We  
13 are seeing a couple of cases in which advertisements of the  
14 potential. We came upon them, I think, through a different  
15 means, but also found that, you know, a web page and a variety  
16 of business opportunities are starting on web pages.

17 MR. TOPOROFF: From time to time today, we're going to  
18 take a vote, as it were, just so that we have some kind -- Eric  
19 is familiar with this, I think. We went through, and Dennis, we  
20 did the same kind of thing in previous workshops in Minneapolis.

21 So the vote right now on the table is, when the  
22 Commission considers whatever it should do with business  
23 opportunities, are Internet sales a key aspect that the  
24 Commission needs greater attention? So all I'm asking for is  
25 kind of a yes or no. You could abstain. You could hedge your

1     bets, whatever, but I would like to get a sense if there's  
2     consensus on that subject.

3             MR. BROWN: Can we discuss that very briefly before we  
4     vote?

5             MR. TOPOROFF: Sure. Go ahead

6             MS. HOWARD: Absolutely.

7             MR. BROWN: In my view, the chief challenge to dealing  
8     with the Internet in terms of law enforcement is simply to come  
9     to grips with the fact that there's a new technology. But  
10    fundamentally, it's simply a way to communicate. And some  
11    people talk on the phone, some people send mail, some people do  
12    television advertising, other people talk person to person.  
13    Some of these are, you know, low tech or no tech and others are  
14    more innovative ways to communicate. And so I don't -- my view  
15    is that if you simply include Internet communications as one of  
16    the many ways that an opportunity can be offered or advertised,  
17    then it's covered like any other form of communication. And I  
18    don't think that the law really has to take special cognizance  
19    of any particular technology unless for some reason the peculiar  
20    manner in which a law is drafted would be interpreted to exclude  
21    that form of communication, well then, yes, you'd want to make a  
22    specific point of including it.

23             But to me it doesn't matter which technology you use to  
24    communicate. The fact is if you communicate an offer, you've  
25    communicated an offer. You're either going to cover that



1 regulation or you're not.

2 MR. WIECZOREK: I want to probably be supportive of  
3 John's position. That is that I think while the Eric Ellman's  
4 of the world are becoming more numerous in terms of surfing the  
5 Internet, that the people who are most prone to be taken  
6 advantage of are people that haven't the foggiest notion of how  
7 to get on the Internet and how to do those kinds of things. So  
8 my sense is still that, while the Internet is something that the  
9 FTC should be interested in, that the traditional ways of  
10 selling, newspaper, whatever, are really directed at the people  
11 who need the most protection. That would be my sense of it,  
12 that people who are on the Internet theoretically, I would say  
13 most of them are more sophisticated, more educated, more able to  
14 exercise some judgment about what they're doing as opposed to  
15 someone who can buy a Chicago Tribune for 50 cents and look in  
16 the classifieds and go and through away \$5,000, you know, in the  
17 blink of an eye.

18 MR. TOPOROFF: Eric?

19 MR. ELLMAN: And let me echo the comments of John.  
20 Because there is, by all accounts, including the National  
21 Consumers League, a lot of fraud on the Internet does not, I  
22 don't think, engender a specific regulation of that specific  
23 method of communication. It's just something that the FTC has  
24 to take into account when it imposes its regulation, but I don't  
25 think that there's anything specific about that method of

1 communication that's necessary to regulation. It's just one  
2 more facet which the FTC has to look at in terms of any kind of  
3 regulation that it imposes.

4 MR. TOPOROFF: Well, on that point, two concerns come  
5 to mind. One is, the Commission very infrequently goes through  
6 the process of revising its rules. If we do so, it's once a  
7 decade at most. This is the first real substantive  
8 consideration of rule changes since the rule was promulgated in  
9 the late '70's. So suffice it to say, whatever we're going to  
10 do is going to carry us for the next decade if not longer. And  
11 while today Internet might be more sophisticated in the sense of  
12 using it and the number of different opportunities on the net,  
13 that could change radically from year to year. In five years,  
14 we could be in a completely different climate. So I think it  
15 would behoove the Commission to at least consider the issue.

16 Second, a concern that we have, and this is one that  
17 we're going to raise in greater detail in the franchise context  
18 when we have a meeting there in September, is what triggers the  
19 obligation to give out disclosures under our rule. And one of  
20 the key aspects is the first face-to-face meeting. Well, if  
21 goods and services or business opportunities or franchises for  
22 that matter are sold over the Internet or by telephone or have  
23 you, then there may not be in actuality a first face-to-face  
24 meeting. So the question becomes, what triggers the obligation  
25 to make disclosures if opportunities, we'll call them income

1 opportunities, are sold on the net.

2 So the question that I posed for a vote is not whether  
3 the Commission should regulate the Internet. That's not what  
4 we're talking about. It is basically getting at the notion, are  
5 business opportunities, income opportunities, more and more  
6 being sold on the net so that it is an area like telephone  
7 sales, like trade show sales, any number of other issues, that  
8 the Commission should at least consider when it contemplates  
9 amendments to the rule.

10 Basically, is this an issue of concern or really not?  
11 So with that, I would still like to take a vote. And we can go  
12 around the table starting with John.

13 MR. D'ALESSANDRO: I abstain.

14 MR. FINNIGAN: Yes.

15 MR. TOPOROFF: Dennis?

16 MR. WIECZOREK: Well, I have to elucidate on my answer.  
17 Because I think you're previewing the franchise area which is a  
18 concern. And that is, I think, yes, Internet sales will become  
19 more and more of a concern. I don't agree that they will be the  
20 primary concern but will become more of a concern. I am  
21 concerned that the Commission does switch the existing rule with  
22 the ten business day cooling off period that already exists in  
23 the franchise area to something that's going to require some  
24 form of disclosure or something that occurs when a web site pops  
25 up on somebody's computer screen. I think that is asking for

1 significant problems and definitional difficulties that will be  
2 a great concern to franchisors. So I guess I'm agreeing with  
3 you with some reservation.

4 MR. TOPOROFF: Okay.

5 MR. BENNETT: A qualified yes. We don't offer, we have  
6 a home page. We have information about how you can become a  
7 Longaberger associate on the home page. But there has to be a  
8 face-to-face meeting in order for that associate to sign up. So  
9 I don't think it would have an impact on us. As you broadly  
10 state in your question, I would say yes.

11 MR. TOPOROFF: Okay. Let me just follow up on that.  
12 Are you saying that when you get distributors for your company,  
13 it always is a face-to-face meeting? There is never, let's say,  
14 contracts sent through the mail or over the telephone?

15 MR. BENNETT: That's a good question. I can't say it's  
16 always a face-to-face meeting, but we know that our recruitment  
17 or when somebody sponsors someone, it's generally at one of our  
18 what we call show, where our products are demonstrated. And I  
19 was looking at the research today. Almost half of the people  
20 that sign up to sell our products ask about how do I sell these.  
21 Because of the affinity for the product. So I would say 99  
22 percent of the time it happens with a face-to-face, because the  
23 company doesn't sign them up. The associate recruits and  
24 sponsors a person. So I don't know the answer to that, but I  
25 would say that that's probably 100 percent. Yeah, it's probably

1 a face-to-face. I'd have to go back and take a look at it.

2 MR. TOPOROFF: John?

3 MR. BROWN: My vote in terms of the Internet is yes,  
4 whatever you do you should take into account the fact that  
5 business opportunities will increasingly be advertised or  
6 offered via the Internet. And then with the same caveat,  
7 Longaberger expresses, if not 100 percent, virtually 100 percent  
8 of the sponsorship activity occurs ultimately when the deal is  
9 done on a face-to-face, person-to-person basis.

10 MR. ELLMAN: And again, it's a qualified yes. But I  
11 think that there will be income-earning opportunities that will  
12 be more prevalent on the Internet as more people have access to  
13 it. But I don't think that the Internet is worthy of special or  
14 specific regulation. And if I could, I just want to follow up  
15 on the comments that Mike and John just made in terms of how one  
16 goes about recruiting a direct seller.

17 And Amway and Longaberger might be a little different  
18 than other direct selling member companies, because I'm not sure  
19 that all direct selling companies in some instances will offer  
20 sponsorship activities through a face-to-face meeting. There  
21 are a lot of people now, as people continue to exist in a more  
22 mobile, more technically oriented society, people are  
23 communicating more and more over the Internet via E-mail or what  
24 have you. And it is quite likely that sponsorship activities  
25 can and will be offered via electronic means. If you've got

1 friends who live in different cities and are communicating  
2 primarily over the Internet and one happens to be a distributor  
3 for one of our direct selling companies loves the opportunity  
4 and is doing quite well and wants to share that with friends in  
5 different cities. And that's being done over the Internet. I  
6 think that is being done now and it will probably be more  
7 prevalent as years go on.

8 MR. TOPOROFF: Rick?

9 MR. GEU: My vote would be yes, we definitely have a  
10 concern about the Internet. However, the Pampered Chef  
11 basically does no business over the Internet. It is all done  
12 face-to-face at home parties.

13 MR. FINNIGAN: If I might expand on some comments.  
14 Other agencies are already passing rules and regulations in  
15 regards to Internet. One that is somewhat similar, because I  
16 just go over the requirements and certain other requirements  
17 that need to be provided, is the FCC. And they have rules, you  
18 know, discussing, can you provide proxy statements by E-mail?  
19 What kind of disclosure statements, if you want to sell  
20 securities over the Internet, how do you go about doing that?  
21 How do you prove that it was delivered? The various state  
22 regulators in the securities area have started taking a look at  
23 that. So, it's an area where other agencies have been able to  
24 draft regulation dealing with it, and I think that, like it or  
25 not, it's an area that is going to be regulated and it's an area

1 where there's increasing business activity.

2 MR. BENNETT: In thinking about your question, if  
3 someone contacts us as a result of seeing our home page and say,  
4 how do I sell your products? We will have an associate in their  
5 geographical area contact them to encourage them and show them  
6 how to get involved and to actually sign them up. So in  
7 thinking about it, it's 100 percent face to face for us.

8 MR. TOPOROFF: Okay.

9 MS. HOWARD: All right. Well, moving along. Dennis,  
10 you actually brought this up and it's something that we need to  
11 explore a little bit more. Talking about the state of business  
12 opportunity regulation. And you talked about the patchwork.  
13 Can you say a little bit more about that and if anyone else has  
14 some additional comments?

15 MR. WIECZOREK: Yeah. The business opportunity laws  
16 follow several general patterns. The original set of business  
17 opportunity laws came out of the southeast and those laws  
18 focused on, if I remember, the four-part definition of the types  
19 of representations that are made. There's usually something  
20 about you'll provide locations for the business opportunity,  
21 buyer to sell products, usually vending machines, things like  
22 that.

23 The business opportunity seller will buy back whatever  
24 it is that the buyer grows, breeds, et cetera. The third part  
25 is usually a guaranty, some sort of representation that involves

1 a guaranty by the seller that the buyer will have some level of  
2 income. And then the fourth part is something about that the  
3 seller will provide a marketing plan. And then the exemption  
4 that came out of that that was available to franchisors was a  
5 follow-on sentence to that that said, If this marketing plan is  
6 provided in conjunction with a registered trademark, then  
7 there's an exemption.

8 So that was the initial set of laws. And then after  
9 that, it started, the laws started mutating and changing and  
10 states were throwing things together because of, I assume,  
11 perceived problems with, you know, the stories that we used to  
12 hear were elderly people would have their life savings taken  
13 away by these kinds of companies. So the laws started spreading  
14 out. And then, in recent years, probably the more prevalent  
15 pattern has started to be something resembling the model  
16 business opportunity law put out by Nicusso. And I think  
17 Oklahoma is one of the newer states. And actually, Illinois is  
18 probably the newest state in terms of that kind of regulation.

19 But you can approach it from a couple of standpoints.  
20 If you're a franchisor doing business, generally you can be  
21 exempt from all of the state business opportunity laws unless  
22 you don't have a federally registered trademark. There are  
23 three states that you have to worry about, Connecticut, Maine  
24 and North Carolina. If you're a manufacturer or a company  
25 that's trying to distribute its products and you have sales reps



1 or manufacturer's reps or even distributors where they have to  
2 put in some money for samples or something like that, then you  
3 have to review them all. And in most cases you'll be exempt if  
4 you're big because there is a tendency to provide exemptions for  
5 large companies, but there are still several states, California  
6 is an example. The California Seller Assistant Marketing Plan  
7 Law is a law that's very broad in its application.

8 So, right now the laws are not uniform. They're not  
9 consistent. If you're doing a good job in reviewing your  
10 responsibilities state to state, you have to examine them all  
11 and there is really no rhyme or reason as to where you'll be  
12 exempt necessarily or where you'll be covered. And if you are  
13 covered in some of these states, you can't do business unless  
14 you have a bond. You can't do business unless you use a  
15 disclosure document, et cetera, et cetera.

16 You know, I think the bottom line out of all this is  
17 that, and it sort of relates to the bullet point above this one,  
18 about who represents the business opportunity interest, you  
19 know, frankly I don't think anybody does. I don't think you'll  
20 get any comments from the business opportunities we're talking  
21 about, the business opportunity types that you sue, they're not  
22 represented here. I don't know that any of them commented.  
23 Maybe you're getting some phone calls, but those are the folks  
24 that really don't care what kind of regulation you have because  
25 they're not going to comply anyway. And those are the folks

1 where the regulation is necessary.

2 MR. TOPOROFF: Are you saying that those folks are the  
3 scam artists?

4 MR. WIECZOREK: Well, I don't know what they are, but  
5 they are companies that are doing business. Probably a good  
6 number of them are scam artists. And I don't think any of the  
7 regulation that you're going to implement is going to be  
8 complied with. It's really more of an enforcement issue than a  
9 disclosure or regulation issue up front.

10 MS. HOWARD: Eric?

11 MR. ELLMAN: I would have to agree with that last point  
12 that Dennis made. That part of the goal of all of these  
13 disclosures that are imposed upon business opportunities and  
14 franchises is to protect the public, but there's a lot of  
15 protection that no amount of disclosures is going to accomplish  
16 because there are just a ton of people that are never going to  
17 register no matter how many disclosures you impose upon these  
18 people. Just because of the fraudulent nature of many business  
19 opportunities.

20 MS. HOWARD: Okay. Well, we can sort of hold that  
21 thought for a little bit later. We're going to touch on that  
22 more in a little bit. We just had someone join us. Would you  
23 like to introduce yourself?

24 MR. SANSON: Sure. Phil Sanson from the Illinois  
25 Securities Department.

1 MS. HOWARD: Good to see you. Well, you came in at  
2 just the time that we were talking about sort of the state of  
3 state laws in the business opportunity area. And I was about to  
4 ask David if he could talk to us about Illinois, but I'll ask  
5 either of you.

6 MR. FINNIGAN: I would like to comment.

7 MR. SANSON: I'll let you.

8 MR. FINNIGAN: Our law pretty much allows what Dennis  
9 outlined there. It's a two-prong test. I mean, you have to  
10 meet a \$500 threshold. So what we do see is people, you know,  
11 advertising their product at \$499 or below. I guess I  
12 personally don't consider that too much of a problem because I  
13 think that you have to put a threshold. Otherwise, you're going  
14 to have a lot of business. We already have enough business as  
15 it was. We would just as soon, I guess, keep it at the \$500.

16 The second one is, you have to meet a six-part test,  
17 which is, again, you know, it's buying locations. It's finding  
18 out what's repurchased that the product. That they're  
19 guarantying income, that they will refund the purchase price and  
20 that they'll provide a marketing plan. Most of the business  
21 opportunities that we've seen out there are wise. This law has  
22 been out for a while, so they usually advertise in such a way  
23 that it doesn't meet one of the five tests or most of the cases  
24 that I bring were alleging that it's a business opportunity  
25 because they're offering a marketing plan.

1           And briefly, that's basically, I mean, you get buy  
2 training or get assistance on the operation, marketing, or I  
3 should say, operation or marketing of the plan. The law has  
4 been in effect since the 1st of January of '96. We just made  
5 some amendments to it which went into effect on July 8th of this  
6 year. We brought in a number of unfortunate actions.  
7 Unfortunately, I don't have any statistics in that regards.

8           I think our experience is that, pretty much what Dennis  
9 has said, is that we don't have a lot of registrations. We're  
10 starting to get some more people that are interested in  
11 registering. That could be somewhat about the knowledge of the  
12 law, because we've been very diligent in bringing enforcement  
13 actions. For the first six months to a year, we had been  
14 basically, because there wasn't a lot of knowledge out there, it  
15 was a new law, we were basically trying to encourage people to  
16 register. We would take a much more lenient action. Now, we're  
17 taking more of a stronger enforcement action. I think that's  
18 encouraging registration.

19           But in general, most of this is geared towards those  
20 people who aren't going to register anyway. The basic agreement  
21 long term is it gives us a club over someone who hasn't  
22 registered. And I think that's quite a bit of the focus where  
23 we're at at this time with it.

24           MS. HOWARD: How did your law come about?

25           MR. FINNIGAN: Do you want to respond to that, Phil?

1           MR. SANSON: Basically, it's between the Attorney  
2 General's office and us. It's an unregulated field. And it's  
3 going to make the Secretary of State's office ask the  
4 legislations to allow that. So, it's in the Secretary of  
5 State's office.

6           MS. HOWARD: Now, you had mentioned, David, that it was  
7 based on, is it based on the model?

8           MR. FINNIGAN: Yes. It is based on the model act. And  
9 frankly, I think that it is, the original act was basically  
10 taken word for word from that model act. We made a couple of  
11 changes to it. One was to make it clear that we were referring  
12 to a federally registered trademark. Whereas, before it wasn't  
13 clear. One point had talked about federally registered  
14 trademark. And then I think another part of the act it just  
15 simply said a trademark, which we had to include a state  
16 registered trademark. So a lot of what we did was just to clear  
17 up things, technical matters like that, but pretty much it's the  
18 model act that's been passed by other states.

19           MS. HOWARD: Just as a note. A number of different  
20 commenters have pointed to your law as sort of a good model to  
21 follow.

22           MR. FINNIGAN: Well, that's probably because we were  
23 fortunate to be one of the most recent ones to pass it. So we  
24 have been able to learn from a lot of the mistakes of other  
25 states. There are lessons that they have learned. It includes

1 a variety of exemptions which I think are pretty good  
2 exemptions. There's a couple that I think we need to work on.  
3 We have a net worth exemption. We have the franchise exemption.  
4 We have a federally registered trademark exemption. There's  
5 also a catch-all which allows the Secretary of State to  
6 designate, upon request, that a certain type of income-earning  
7 or a business opportunity be exempt.

8 Is there any others that you can think of, Phil?

9 MR. SANSON: Those are the main ones.

10 MR. FINNIGAN: Those are the main ones.

11 MR. HOWARD: Now, you mentioned that yours is a  
12 registration law. Do you also have a bonding requirement?

13 MR. SANSON: There's a surety bond, but that's just  
14 basically a \$25,000 net worth. If it's less than that, if a  
15 company has guaranteed profits or earnings. So, unless that  
16 occurs, that really doesn't go into effect.

17 MS. HOWARD: How about other state laws? Dennis, are  
18 you aware of, for instance, do most acts impose a bonding  
19 requirement?

20 MR. WIECZOREK: No. It's a mixed bag. There are some  
21 that it's required. There are, in some respects, it's similar  
22 to the franchise laws in that in a few states you send your  
23 application in and it's rubber stamped and it's instantaneous.  
24 There's not much to do. In other states, I think Connecticut is  
25 one of the most prominent ones. They give you a real going over

1 when you try to get registered because their assumption is is  
2 that business opportunities are bad. And they should make sure  
3 that whoever it is that is foolish enough to register with them  
4 gets put through the mill. But there are, you know, there are  
5 variations out there. Again, the people who shouldn't be  
6 subject to the laws but are caught can usually figure out a way  
7 to work their way around the state laws. Again, not all of the  
8 state laws. There's always going to be a few that will capture  
9 some, but most of them, the more recent ones like Illinois, are  
10 more patterned after the model law. And that seems to take care  
11 of the larger companies, the more legitimate companies, and the  
12 scam artists are never going to comply anyway.

13 MS. HOWARD: And are most of the laws registration laws  
14 as opposed to simply disclosure laws?

15 MR. WIECZOREK: Yeah. Most of them are registration  
16 laws, yeah.

17 MS. HOWARD: Anything else?

18 MR. TOPOROFF: I just have a question for Eric. In  
19 your organization, do you also represent work at home type of  
20 income opportunities?

21 MR. ELLMAN: Well, I'm not sure what you mean by work  
22 at home. But what I can say is all of the direct selling, most,  
23 if not all, of direct selling is a home-based enterprise.  
24 People are in the sales of direct selling go in a lot of places.  
25 It can be in the customer's home. It can be in the direct

1 seller's home. It can be in an office, anything that's not a  
2 fixed retail location. But in terms of the administration of  
3 the business, that administration of the business is being done  
4 from home, whether it's making phone calls to set up  
5 appointments for sales or whether it's making appointments to  
6 discuss the income-earning opportunity. So if that's what you  
7 mean by work at home, then yes. But if you mean by work at home  
8 where companies will send beads out to the --

9 MR. TOPOROFF: That's where I was getting at.

10 MR. ELLMAN: No. That is not us. No member company of  
11 ours, no sales people are in the business of manufacturing raw  
12 goods, whether it's putting beads on a necklace or growing  
13 chinchillas or stuffing envelopes. Right. That is not us.

14 MR. BROWN: If I can add to what Eric just said.  
15 Actually, I think it's fair to say that the whole proposition of  
16 direct selling is antithetical to work at home. The point is  
17 that if you're going to be a successful direct seller you have  
18 to get out of your home and go talk to other people. It's not a  
19 deal where you can, you know, in the privacy of your own home,  
20 you know, earn some kind of substantial income. But in fact,  
21 it's quite the opposite of that.

22 MR. TOPOROFF: What's the difference between direct  
23 selling and direct marketing?

24 MR. ELLMAN: There is a big difference. And we're  
25 often confused. But essentially the big difference is that in



1 direct selling, the contact between the buyer and the seller is  
2 personal. There is a face-to-face meeting between the buyer and  
3 seller in a variety of non-fixed retail locations such as I  
4 mentioned homes or offices, that sort of thing.

5 Direct marketing, for lack of a better word, is more  
6 impersonal. Where it is through catalogs transactions or  
7 telemarketing or perhaps even Internet sales. But there's the  
8 face-to-face element that is unique that makes a direct seller a  
9 direct seller.

10 MR. TOPOROFF: Before we move on, I just wanted to nail  
11 down a little bit more to the extent that we can whether there  
12 are trade associations or other groups that represent income  
13 opportunities. I know that the Direct Selling Association, I  
14 assume the Direct Marketing Association carries some of that. I  
15 understand that there is possibly located here in Chicago a  
16 vending industry group. That is like the North American Vending  
17 Association, what have you. Be it as it may, are there other  
18 types of groups that may represent a segment of income  
19 opportunities like direct selling? Are you aware of any other  
20 groups in the field?

21 MR. ELLMAN: I'm not.

22 MR. TOPOROFF: Dennis?

23 MR. WIECZOREK: There was some reference I remember  
24 seeing in the news to a business opportunity sort of  
25 organization in Washington or Bethesda or something.



1           In particular, again, as the Commission considers  
2   revising its rule, certainly the Commission staff want to focus  
3   narrowly on where there is a problem. We don't have much  
4   interest in regulating a field where there aren't complaints,  
5   there is no pervasive problem, that is working well and that  
6   consumers are basically satisfied.

7           So of the universe of income opportunities, we need to  
8   focus on where there are problems and how to identify them. So,  
9   for this purpose, I'm going to start off by, again, focusing on  
10  what are the specific characteristics of business opportunities  
11  or income opportunities that are a problem and perhaps those  
12  that are not.

13           To get the ball rolling, one area where I think perhaps  
14  is a distinguishing factor is earnings representations.  
15  Certainly from our experience at the Commission, we see time and  
16  time again different opportunities that purport to offer huge  
17  incomes, earn \$100,000 a year with no experience necessary,  
18  part-time, no selling, that kind of thing. I think us, when we  
19  see those kinds of representations made, alarm bells go off, at  
20  least initially.

21           So, I want to explore that and possibly other  
22  characteristics that we can look toward as identifying what  
23  possibly could be, again, a fraudulent or deceptive business  
24  opportunity. Anybody have any thoughts on that? Eric?

25           MR. ELLMAN: Well, two come to mind immediately, as

1 perhaps some ways to examine what is legitimate and what is not.  
2 And some of the things that we've had experience with is that  
3 the higher the cost of the buy-in, for lack of a better time,  
4 that is potentially an indicia of fraud, as is the absence of an  
5 inventory repurchase policy, a buy-back policy, if you will.

6 One of the things that we're very proud of in our  
7 industry is that in our code of ethics we have a 90 percent buy-  
8 back policy and every member company must adhere to that. And  
9 that is, if a distributor, if a direct seller decides to leave  
10 the business for any reason whatsoever, our member companies  
11 will repurchase resalable inventory on hand at 90 percent of the  
12 cost that the direct seller had paid for it. And I'm not so  
13 sure that fraudulent operators offer that same kind of a  
14 guaranty.

15 MR. TOPOROFF: Okay. Well, let me ask this. Is there  
16 a distinction also that could possibly be drawn in terms of what  
17 the business opportunity is offering in the sense that, I  
18 understand the direct sellers basically focus on the sale of a  
19 product. Is a possible distinction the sale of equipment? As I  
20 understand the direct sellers, they buy a known product and they  
21 basically become distributors and they offer those products for  
22 sale. They don't assemble anything as such. So would a  
23 possible red flag be the sale of equipment with which the  
24 investor takes the equipment and then offers it, uses it to  
25 manufacture something or uses it for the sale of other products

1 in the case of, let's say, vending. They buy a vending machine.  
2 They in turn stock it and then offer goods to the public.

3 So, is there a notion that equipment sales could be  
4 part of the tip-off on what's accepted?

5 MR. WIECZOREK: I don't think so. I think there are  
6 just as many problems with inventory being sold that's  
7 unsaleable, that's overpriced. I don't really see a big  
8 distinction between those at all. They're equally bad. Let's  
9 put it that way.

10 MR. TOPOROFF: So it's not a characteristic that in and  
11 of itself is going to mean anything?

12 MR. WIECZOREK: I mean, there are some companies that  
13 will sell vending machines, that will sell store displays,  
14 things like that, but I don't think that typifies the industry  
15 as being the most fraudulent behavior or the companies that will  
16 always, if they sell equipment, are likely to be fraudulent. I  
17 would see it being similar with inventory also.

18 MR. TOPOROFF: David or Phil, do you have anything to  
19 add on that?

20 MR. SANSON: I haven't really seen much distinction  
21 really, Steven, between equipment, products.

22 MR. FINNIGAN: I think it's a false distinction. I've  
23 just discussed a case in which there was a business opportunity,  
24 a fraudulent one in which they were selling a recognized  
25 product. And we have business opportunities which involve the

1 sale of equipment. So, I think that trying to make a  
2 distinction based on whether they're selling equipment is going  
3 to be fruitless.

4 MR. TOPOROFF: Is there a distinction in terms of  
5 support or assistance?

6 MR. SOKOL: In terms of speaking with some of the  
7 purchasers of these opportunities, they don't often have a clear  
8 picture as to what the purchase price went towards. They are  
9 usually led to believe that, let's say, for example, in a  
10 \$12,000, \$15,000 purchase, \$7,000 to \$8,000 worth was for the  
11 inventory. Another couple thousand in the display rack type  
12 scenario is for the display rack. And then if they want to know  
13 what the other \$2,000 is for, and they're told anything ranging  
14 from goodwill to customer service or the right to use the name  
15 of the company, whatever name that might be.

16 MR. TOPOROFF: Anybody have anything else to add on  
17 that particular point? John?

18 MR. BROWN: I guess just probably this reiterates  
19 earlier comments. Whether it's something that would, I don't  
20 think the distinctions were drawn would be appropriate to carve  
21 out in the law so much as they're red flags for enforcement  
22 concern. And you had mentioned income representation and the  
23 nature of those representations. And I think some on their face  
24 raise questions and others don't. The larger the investment the  
25 greater the concern. And then beyond that I think it is true

1 that when you have a recognized trade name or trademark, that is  
2 a better situation than when there is none at all or it's one  
3 that no one recognizes, or very few people would recognize.

4 And so, you know, those are red flags, if you will, but  
5 I don't think they're the basis for making distinctions within a  
6 regulatory framework.

7 MR. TOPOROFF: The Direct Selling Association, the  
8 typical members, when they go to sell their opportunity, do they  
9 offer any kind of training or assistance? Is that part and  
10 parcel?

11 MR. ELLMAN: No. And in fact, we cannot, because all  
12 the direct sellers are independent contractors. And by putting  
13 training requirements on the companies, whether forced or  
14 voluntary, of the sales people, you would run a serious risk of  
15 having these people characterized as employees, and that's not  
16 something that either the companies or the direct sellers  
17 themselves want because the companies like the independence, as  
18 do most of the sales people themselves, because they are  
19 essentially their own business people, and they're not  
20 interested in becoming employees of the company.

21 MR. TOPOROFF: John?

22 MR. BROWN: During the break we were having a  
23 conversation about whether the opportunity itself is for sale or  
24 are you selling something else. And, you know, certainly for  
25 Amway, and I think it's not uncharacteristic of a lot of direct

1 selling companies is that what we'll say is that, in our case,  
2 the Amway opportunity is not for sale. It's basically available  
3 to anyone. And what you purchase are specific items. And those  
4 are identified. So you don't have this vague characterization  
5 of, well, you spent so much for this and you spent so much for  
6 that and then, well, this third area is, you know, basically the  
7 cost of the opportunity itself. The opportunity to sell Amway  
8 products, that doesn't cost anything in Amway. Basically you  
9 purchase the sales kit, which is going to cost less than \$200  
10 and that's going to have two components to it. One is  
11 literature that you need to understand the business and to  
12 conduct the business. And then products, and all of that is  
13 subject to, you know, being repurchased by the company if the  
14 person decides that the opportunity is not for them.

15           And I think that's characteristic of the direct selling  
16 industry that basically the opportunity being offered by the  
17 company, when you consider that we want to absolutely maximize  
18 the number of people who will try it, we want to keep the costs  
19 low. That is how we maximize participation and so that's the  
20 approach. I think most direct selling companies take that  
21 approach. They're trying to keep the cost as low as they  
22 reasonably can under the circumstances.

23           MR. TOPOROFF: Dennis?

24           MR. WIECZOREK: Let me ask Eric something. You said  
25 earlier that direct sellers provide no training?



1           MR. ELLMAN: The companies don't. The companies don't  
2 provide training to the sales people. Now, there might be  
3 training in the context of one recruit providing guidance or  
4 training to another person that they have recruited in the sales  
5 business, but I would not characterize it so much as training as  
6 I would sort of, well, I guess some people would consider it  
7 training because you're offering, you know, guidance and  
8 suggestions and help as to how you go about running your direct  
9 selling business.

10           MR. WIECZOREK: The reason I say that is that I don't  
11 know if this is where Steve is going. He can speak for himself  
12 on this issue, but, you know, a lot of the statutes talk about,  
13 in the franchise area and the business opportunity area, talk  
14 about providing any level of assistance, guidance, training,  
15 manuals, how to do it, know-how, et cetera, and I would find it  
16 hard to believe that your members don't provide any of that at  
17 all.

18           MR. ELLMAN: Well, no, our members certainly provide  
19 their sales people with marketing manuals and materials, but  
20 essentially these people are in business for themselves. And  
21 they, you know, they review the marketing manuals. Perhaps  
22 there are some videotapes and that sort of thing. And perhaps  
23 it's just our different opinion as to what constitutes training  
24 or not. If they, you know, read the manual that's provided or  
25 watch a videotape, that is, you know, there is some degree of

1 training, but it is not training in the sense of employer-  
2 employee context.

3 MR. D'ALESSANDRO: You can probably correct me if I'm  
4 wrong. You're probably saying that they don't train you in how  
5 to sell. They may educate you on product knowledge.

6 MR. ELLMAN: In many respects that's true. Right, that  
7 you're getting some information about the products and you're  
8 getting helpful suggestions as to who you might want to contact  
9 and people in your kid's soccer team. You might want to contact  
10 your friends and neighbors and people that you come into contact  
11 with every day. And they might provide suggestions as to, you  
12 know, you make a separate space in your house and you have one  
13 place in your house where you do the administrative functions of  
14 your business and that sort of thing. But you are the one that  
15 goes out and does all the selling and if you need help or  
16 suggestions or advice as to how you go about running that  
17 business, generally speaking, you're going to be in  
18 communication with the person that recruited you as opposed to  
19 the company itself.

20 MR. TOPOROFF: Does the company have, let's say, an 800  
21 number where distributors could call in and ask for advice or  
22 assistance?

23 MR. ELLMAN: I think that that assistance is available  
24 more for product issues. Is this product good for this or can I  
25 say this when I talk about this particular product. But I just

1 don't think that any of our companies offer, you know, advice as  
2 to how you go about, an 800 number where you can get advice  
3 about running the business.

4 MR. TOPOROFF: John?

5 MR. BROWN: Everybody's right. Speaking for Amway, and  
6 obviously we're fairly mature in the sense that we've been  
7 having at it for about 40 years. So, the system that we have in  
8 place for ensuring that our distributors have the greatest  
9 opportunity for successful possible given the nature of our  
10 opportunity, I think, you know, we're fairly well developed  
11 along that road. And I think what Eric is saying is that in  
12 order to become a distributor for most direct selling  
13 opportunities, strictly speaking, there is not some kind of  
14 detailed training required in order to become a distributor.  
15 Indeed, you know, Amway's choice of products that we sell and  
16 the way we make the opportunity available to people is, again,  
17 to make it as simple and understandable as possible so that  
18 detailed training is not necessary.

19 On the other hand, we do a lot to try to make sure  
20 that, you know, people will have the materials and the  
21 information necessary to be successful. Whether one wants to  
22 characterize that as training, education, guidance, whatever,  
23 the bottom line is you're trying to help people. But it's not  
24 something that they're required to do specifically. And indeed,  
25 we'll do any number of marketing of product expositions around

1 the company regionally and locally that people, if they choose,  
2 they can attend, or they may choose not to. And so, yeah,  
3 there's a lot of information, a lot of guidance provided. And  
4 frankly, in my view, for Amway, again, it's the fact that we  
5 keep the required costs or the initial purchase low and keep  
6 everything voluntary so that you do not become a business  
7 opportunity for purposes of the Act.

8 And that's the whole point. But, you know, are we  
9 providing guidance that if the price tag were higher and if that  
10 cost \$5,000 to become an Amway distributor, you know, do we  
11 provide sufficient guidance and a marketing plan such that it  
12 would meet the requirements of business opportunity law or the  
13 franchise law, and I think, you know, I'd leave to the  
14 interpretation of the law enforcement people, but I'd be very  
15 concerned counseling Amway Corporation on that issue. So, yeah,  
16 we do provide guidance. We do provide assistance. But strictly  
17 speaking, is it training? Well, I don't know. It depends what  
18 one would mean by that.

19 MR. TOPOROFF: Rick?

20 MR. GEU: To reiterate what John is saying and  
21 specifically for the Pampered Chef, we have available to our  
22 consultants videos, training manuals, but we do not train them  
23 from the company's point of view. The company does not train  
24 the consultants. They train each other. Networking is a big  
25 part of our training and learning how to do the business.

1 Networking, I mean, we provide the opportunities for them to  
2 network, encourage them to network, but they get together and  
3 they look and talk about what works, you know, for them, what  
4 doesn't work.

5 MR. ELLMAN: And many of our member companies will  
6 conduct either annual or quarterly or somehow seminars about  
7 working in the business. But all that is entirely voluntary.

8 MR. WIECZOREK: I would, bottom line, at least from my  
9 perspective, is that it would be a mistake to create a business  
10 opportunity rule that says that you are exempt if you provide no  
11 training or assistance or something like that. Because that's  
12 not going to take care of the issues that we're talking about.

13 MR. TOPOROFF: Right. I want to ask the state  
14 regulators, in the types of cases that they bring, is training  
15 and assistance an element that they see frequently?

16 MR. SANSON: It's the main thing, usually, training and  
17 assistance. Some type of marketing plan, support, training,  
18 advice. We look at that as a marketing plan. That is how a  
19 marketing plan is defined.

20 MR. TOPOROFF: Adam?

21 MR. SOKOL: Training certainly is a variable. I've  
22 actually been just sort of jotting down the lists of types of  
23 different complaints that we get. And as to training, we have  
24 had a couple of cases in which people either attended a seminar  
25 or watched a video in which there was a point hammered home in

1 that with our training and our assistance, there's no way you  
2 can fail with this opportunity. What people would do would then  
3 get a, purchasers would get a "training tape" or a training  
4 booklet in which was as simple as, Make sure you look someone in  
5 the eye. Speak slowly and confidently. Say please and thank  
6 you." And that is what the company referred to as training.  
7 That then would trigger a complaint to our office saying, this  
8 isn't what I thought I was paying for.

9 MR. TOPOROFF: Okay. You mentioned, Adam, that is,  
10 just mentioned another aspect that I wanted to touch on. And  
11 that is, guaranties of success. I know in the cases that we  
12 bring, I guess guaranties of success are a close cousin to  
13 earnings representations. I want to ask the direct sellers in  
14 your particular organizations or members of the Direct Selling  
15 Association, are there either guaranties of success in the  
16 broadest sense of the word or other kinds of representations  
17 that the companies might make in terms of earning an income?

18 MR. ELLMAN: Well, I would hope that nobody in our  
19 industry makes guaranties of success, because nothing is  
20 guaranteed in anything anywhere. And I'm not aware of companies  
21 that do make such guaranties. Now, they do tell you that if you  
22 work hard and you apply yourself you might succeed and you might  
23 not, but you have a lot better chance of succeeding the harder  
24 that you work. And I think that's the message that our  
25 membership conveys to their sales people as well as to potential

1 recruits.

2 MR. BENNETT: I would echo that. We don't make any  
3 guaranties of success. In fact, what we like to stress is that  
4 it's really the flexibility of their schedule. Now, they can  
5 have as many shows or work as hard as they want to at it or as  
6 little as they want to at it. And actually that's the kind of  
7 supplemental lifestyle most of our folks have full-time jobs and  
8 they do this as a way to supplement a family income or to  
9 collect the product or to take a vacation. So, they know what  
10 their goals are, individual goals are, and they structure their  
11 business to reach those goals. So, no, we don't make any  
12 guaranties.

13 MR. TOPOROFF: Are there any company policies against  
14 distributors making those kinds of claims?

15 MR. ELLMAN: Many of our companies have, in fact, all  
16 of our companies have policies and procedures which say a number  
17 of things. One of those, many companies have restrictions on,  
18 in some form or another, direct sellers for that particular  
19 company making outrageous earnings claims to other people. No  
20 direct seller who is a member of our association should ever be  
21 telling anyone that it's easy to make a lot of money very  
22 quickly without any kind of effort whatsoever. The message that  
23 should always be conveyed, and I think most of our, if not all  
24 of our member companies have this message conveyed to direct  
25 sellers through talking to their potential recruits that there

1 are no guaranties of success. And if you work hard and apply  
2 yourself, you might do well and you might not. But obviously,  
3 you have a better chance of making money if you apply yourself  
4 and do the work.

5 MR. TOPOROFF: John?

6 MR. BROWN: I would say it's probably accurate in the  
7 direct selling industry that, if not every company, practically  
8 every company will specifically prohibit any guaranty of  
9 success. And I think particularly in today's environment, to  
10 make those kinds of guaranties not only would run afoul of, you  
11 know, virtually every kind of business opportunity consumer  
12 protection act out there, deceptive trade practice acts, but  
13 likewise, as a matter of civil liability, when you're seeking to  
14 attract to your opportunity, you're inviting trouble to guaranty  
15 success. It's a promise that can't possibly be kept.

16 Again, so it doesn't sound like we go around saying,  
17 gee, you can have this opportunity if you want it, but, you  
18 know, it's not that good. That is not the marketing strategy of  
19 direct selling companies. I don't think it's the marketing  
20 strategy of franchise opportunities or anybody else. We  
21 endeavor to make the opportunity as attractive to people as we  
22 possibly can. And I think to try to properly characterize it,  
23 what we emphasize is that there's hard work involved, that not  
24 everyone will be successful, but you can be, and we don't  
25 presume to know who that's going to be. And, you know, in the



1 direct selling industry you can point to countless examples of  
2 people who have gone to professional school who were successful  
3 or people who had a, you know, junior high school education were  
4 successful. And you have people from all walks of life and  
5 backgrounds. So we try to emphasize the point that there are  
6 countless examples of people from all walks of life who have  
7 been successful with the opportunity, but not everyone is  
8 guaranteed success. And so that generally is the message that I  
9 think is conveyed.

10 MR. TOPOROFF: John?

11 MR. D'ALESSANDRO: I agree with this gentleman, but I  
12 feel what really happens is is that the individual in his own  
13 mind says, that's a guaranty of success. He twists the  
14 information around to believe that that is going to happen.

15 MR. TOPOROFF: Dennis?

16 MR. WIECZOREK: Well, actually that's interesting you  
17 say that because there's that old North Carolina case involving  
18 the North Carolina Business Opportunity Law where some, I don't  
19 remember the name of the company, it was Private Industries or  
20 something like that. They made representations about earnings.  
21 A North Carolina court said that was a guaranty. They made no  
22 guaranty, but the court said that's a guaranty.

23 So, again, you know, if the Commission is considering a  
24 rule that would say that you are a biz op if you make any  
25 representations about sales, earnings, profits, expenses, et

1 cetera, I think that may be problematical to some of these  
2 gentlemen because I suspect some of your people are out there  
3 saying, well, if you sell 100 of these, this is how much money  
4 you could make. Or if you sell 20 of these, this is what your  
5 profits will be. It's not a guaranty, but they're providing  
6 information that says that here's what the margins would be on  
7 various levels of sales. And if that's a criteria for becoming  
8 a business opportunity, then I think you're going to capture a  
9 whole lot of folks that really don't want to be covered by these  
10 laws and probably shouldn't be covered by these laws.

11 MR. TOPOROFF: Eric?

12 MR. ELLMAN: I don't know if we're going to get into  
13 this later on or not, but let me just follow up on what Dennis  
14 says. That since you were talking about representations and  
15 guaranties and that sort of thing, is that it would be very  
16 difficult for direct sellers, direct selling companies, to do  
17 business without presenting some degree of representations. And  
18 it would be unfortunate if we were prohibited from doing that  
19 type of function. We never promise the sun and the sky. We  
20 never promise that you'll make a lot of money doing minimal  
21 work. But there have to be discussions about, you know, what  
22 potential profit margins there are, because we need to present,  
23 to present an income opportunity, you have to be able to present  
24 it fairly and accurately. And to do that, to give some people  
25 an idea of how much money that they might be able to make, no

1 one's going to potentially take advantage of an opportunity if  
2 they have no idea what you're getting into. And one of those  
3 things that you need to know what you're getting into is  
4 potential sources of income.

5 MR. TOPOROFF: Well, I wanted to ask Phil or Dave and  
6 perhaps others. It's my understanding that in Illinois' biz op  
7 statute, and comparable ones in other states, isn't it the  
8 definition that either --

9 MR. SANSON: If I say, I'm sorry. Go ahead.

10 MR. TOPOROFF: That it's a sell of appointments or  
11 lease or whatever of products plus a representation that you  
12 will either earn back the same amount or some other type of  
13 provision that's key to earnings?

14 MR. FINNIGAN: There's essentially six tests. And the  
15 first one is that it's some sort of offer to sell business or  
16 product or good or service. You meet the \$500 threshold and you  
17 meet one of six tests, one of which is a guaranteed income, a  
18 refund of the monies that you paid, that they'll find you  
19 locations for vending machines or pay phones, and then the last  
20 one, which is the one that we use almost invariably for 90  
21 percent of all the cases that we bring, is that you're going to  
22 provide a marketing plan, because that tends to be the problem.

23 Most of the people out there, this model act has been  
24 out there for a while. They pretty much know that if you do one  
25 of those first five, that that's going to make you a biz op. So

1 they don't do one of those five. They don't guaranty an income.  
2 They specifically, in fact, we have one where they went through  
3 and they specifically said, you, the buyer, sign saying, you  
4 agree that we are not guarantying you. Your price will be  
5 refunded. We're not guarantying to purchase your product.  
6 We're not guarantying you an income. So, pretty much that leads  
7 us to, if we want to bring a case of arguing that providing a  
8 marketing plan.

9 MR. TOPOROFF: And it's not just clear. The statute  
10 speaks in terms of a guaranty of income, or is it that you will  
11 earn certain income?

12 MR. WIECZOREK: The Illinois statute is a little  
13 different than many of the other statutes. California is more  
14 typical. California says that if you represent that the  
15 purchaser will earn, is likely to earn or can earn in an amount  
16 in excess of the initial payment paid by the purchaser for  
17 participation in the seller-assisted marketing plan. So there  
18 are, I would say the majority have language similar to that that  
19 say something about the seller representing that you may be able  
20 to earn more than you put in.

21 And if it says that, if anyone is out there selling  
22 business opportunities and doesn't either expressly or impliedly  
23 say that, then they're not going to sell anything. So,  
24 everybody makes that representation. So it's almost a given  
25 that that representation will be made. And obviously an

1 Illinois case, invariably someone will imply or expressly say,  
2 we will provide you with a way to market this product, market  
3 this service, and you capture everything basically, by the  
4 California format or the Illinois format.

5 MR. FINNIGAN: The specific language with regards to  
6 the income is that the seller guaranties that the purchaser will  
7 derive income from business which exceeds the price paid to the  
8 seller.

9 MR. TOPOROFF: But it is in terms of guaranties, isn't  
10 it?

11 MR. FINNIGAN: The specific language is guaranty.

12 MR. BROWN: I have a question. David, have you ever  
13 come across a business opportunity that didn't meet the  
14 marketing plan language of your statute?

15 MR. FINNIGAN: No. And in fact, that's the route that  
16 we usually go. It's because almost invariably for it to be a  
17 business opportunity you have to be able to provide some sort of  
18 training or manual or assistance or promotional literature or  
19 something like that. And in effect, just to jump ahead, in  
20 regards to that proposed language in the notice, that seems for  
21 us to be the one that works. Is that there's some sort of  
22 minimal threshold amount and that they're providing some sort of  
23 assistance or marketing plan. Because otherwise that seems for  
24 us to cover the great variety of creativity of people who are  
25 able to offer a variety of different business opportunities and

1 still meet that, and I think with the exceptions, be able to  
2 meet the concerns of the industry.

3 MR. TOPOROFF: Anybody have any thoughts on that? I'm  
4 going to get back to marketing plans in a second. I just want  
5 to probe another issue. And that is the use of testimonials.  
6 First of all, is there anything in the Illinois statute that  
7 addresses the use of testimonials?

8 MR. FINNIGAN: No.

9 MR. TOPOROFF: Okay. I want to ask the direct sellers.  
10 Is the use of testimonials common, routine, rare in your  
11 organization?

12 MR. ELLMAN: That's a good question. I would say that  
13 it does exist, but I'm not familiar with every company's method  
14 of operation. But I do know that there are companies that use  
15 testimonials. And by that, that can come in a variety of ways.  
16 It can be saying that I've used products and I love it, or it  
17 can be a product testimonial like that, or it can be an income  
18 testimonial where somebody will say, I've been with this company  
19 for X number of years. It's allowed me to pay for my son's  
20 college tuition or it's allowed me to pay off some credit cards  
21 or that type of thing.

22 Those are, I think, the more common in terms of income  
23 representations than saying I earned \$10,000 last year or  
24 something like that. That does happen, but it's more common to  
25 say that working in my own business selling this company

1 products has allowed me greater income flexibility and has  
2 allowed me to do more things with more money.

3 MR. TOPOROFF: John?

4 MR. BROWN: I would observe that product testimonials  
5 within the direct selling industry tend to be put forth by known  
6 personalities. A competitor of ours recently signed up a famous  
7 model to give testimonials regarding their beauty products and  
8 skin care products. So that's quite common. When it comes to  
9 success with the business itself, testimonials have no relevance  
10 unless it's someone who realized success themselves personally,  
11 like a distributor who would, in effect, give a testimonial  
12 about their experience being with the Amway business or what  
13 have you. And indeed, it is that, you know, frankly the whole  
14 sponsorship effort is, in effect, a sort of testimonial.  
15 Because if I think you'd be a great Amway distributor and I  
16 really want you to become an Amway distributor, I'm going to  
17 have a tough time convincing you of that if I give no personal  
18 testimony regarding the nature of the opportunity myself.

19 And so, it's almost driven by personal testimony in  
20 terms of pursuing the business and whether it's worthwhile.

21 MS. HOWARD: Do you find what Eric said also goes for  
22 the Amway distributors in terms of the types of testimonials  
23 they give? In other words, as opposed to, yeah, I made \$10,000  
24 last year. Yes, I was able to pay off my Visa bill.

25 MR. BROWN: They tend to be more general. We recommend

1 against making specific income representations and instead  
2 prefer that people talk about the benefits that the business  
3 have given them. And indeed, you know, in our own industry code  
4 of ethics, and clearly everybody in the association signed off  
5 on that. Basically, the restriction on income earning  
6 representations, separate and apart from they must be true, is  
7 that they have to be based on documented evidence. In other  
8 words, you can't do an income representation that, in effect,  
9 was, well, while it could potentially be true, it's invented.  
10 No one ever had that experience, nonetheless that's the  
11 representation you're giving. You know, and our business is  
12 like, if you're going to make a number representation, it has to  
13 be one that somebody has in fact experienced and that has to be  
14 documented. So you have to be able to prove specifically that  
15 representation made. That's an industry standard as opposed to,  
16 you know, a specific Amway one.

17 MR. TOPOROFF: I want to ask the regulators. In the  
18 cases with complaints that they see, is the issue of  
19 testimonials or shills or phony references, is that a  
20 characteristic that comes up? And you can quantify that in any  
21 way.

22 MR. SANSON: The same as using like quotes, is that  
23 the same thing you're asking, Steve?

24 MR. TOPOROFF: I'm sorry, what?

25 MR. SANSON: Is that like asking for quotes of a



1 distributor, a quote from a distributor, is that what you're  
2 saying?

3 MR. TOPOROFF: Sure. Either that or --

4 MR. SANSON: Because we do have a lot of that that Dave  
5 and I work on. If there's a projection or if there's a quote  
6 that says this, where's the evidence or what kind of supporting  
7 documentation that you have made this about. And then when we  
8 ask it from the company, but that's what they don't want -- they  
9 don't give it out because it isn't true. And that's where a lot  
10 of the misreps.

11 MR. FINNIGAN: That's probably about half the cases  
12 where you'll have, you know, they'll say, I invested in this and  
13 I've made this da, da, da. And they'll say, they'll have a  
14 first name and a state that they're in. We'll see that.

15 Our statute doesn't really deal with that. So, it's not  
16 something I really get too involved with. I think Phil is part  
17 of the registration question. We'll want to ask more  
18 information about that. Again, I think trying to focus on  
19 testimonials is probably going to be fruitless. I agree with  
20 what the industry just indicated as it is a legitimate marketing  
21 tactic if done appropriately. You know, and especially as Eric  
22 says in the Direct Selling Association, if you're meeting  
23 someone personally or if you recruit someone personally. And  
24 naturally you're going to talk about your own experiences, and  
25 that's a testimonial.

1           So, again, I hate being such a cynic, but I think that  
2 area is probably going to be kind of fruitless.

3           MR. TOPOROFF: I'm going to get to John in one second,  
4 but I want to ask Adam about his experience.

5           MR. SOKOL: Just to specifically answer your question  
6 regarding the use of skills, the answer is yes, we certainly  
7 have had complaints in which either a purchaser asked for  
8 references or were provided a list of references. And upon  
9 further investigation, it's been discovered that the person  
10 giving the testimonial either was an employee of the company or  
11 paid to state that he or she had earned X amount of money and  
12 certainly, well, probably won't be able to substantiate that.

13           MR. TOPOROFF: John?

14           MR. D'ALESSANDRO: I think there's different types of  
15 testimonials. If you're talking about guarantying money,  
16 earnings and the like, that's one type. But if you're talking  
17 about testimonials about product and what it can do and what it  
18 can't do, that's a different situation.

19           MR. TOPOROFF: Well, let's talk about testimonials  
20 either of how great the company is or how wonderful a particular  
21 opportunity might be.

22           MR. SANSON: I just look at earnings basically, Steve.  
23 That's the main thing, the red flag, is the earnings potential.

24           MR. TOPOROFF: Eric?

25           MR. ELLMAN: But if somebody makes an earnings claim

1 and it's not true, then that is actionable, not only under the  
2 FTC and Unfair and Deceptive Trade Practices, but also I would  
3 imagine every state's Unfair and Deceptive Trade Practices Acts.

4 MR. TOPOROFF: Another characteristic that I wanted to  
5 explore is exclusives, exclusive territories. Whether that is  
6 possible distinction between the deceptive scams and the more  
7 legitimate ones. Certainly in the cases that we have broadly  
8 seen representations of exclusives, is that something that the  
9 legitimate industry uses as well?

10 MR. BROWN: I can only speak for Amway. We do not have  
11 exclusive territories that we offer. We don't break people up  
12 geographically in assigned territories. So, you know, our  
13 operation, and we try to maximize market penetration. That's  
14 our strategy. It's a classic low ticket seller strategy in the  
15 marketplace for direct sellers. And I would leave to Eric to  
16 say whether, if there's a DSA company that does break up by  
17 territory. I think a few do, but it's not characteristic of the  
18 industry.

19 MR. ELLMAN: Direct selling companies typically do not  
20 assign people to exclusive territories for a number of reasons,  
21 not the least of which is the fact that a company and the sales  
22 people, their independent contractor status would be in  
23 significant jeopardy, I would think. With looking at other  
24 factors, if one of those factors was assigning people to  
25 exclusive territories.

1           Now, to get to your question. Whether just because  
2 somebody has a specific territory, exclusive territory, is an  
3 indicia of a fraud, I really don't know the answer to that. All  
4 I can speak to is the fact that direct selling is not an  
5 exclusive territorial business.

6           MR. TOPOROFF: Dennis?

7           MR. WIECZOREK: I don't see any distinction at all.  
8 There are some fraudulent companies that say, we give you a  
9 territory, we give you a route, an exclusive route. There are  
10 others that say, sell it, go anywhere with it. I don't view it  
11 as a viable distinction.

12           MR. TOPOROFF: Under the Illinois statute, is there any  
13 provision that addresses exclusives, exclusive territories? Is  
14 that a factor that's in the statute?

15           MR. SANSON: That's a location or location assistance.  
16 It's in there.

17           MR. TOPOROFF: Which I'm going to get to in a second.  
18 But on the precise issue of an exclusive territory, that's just  
19 --

20           MR. FINNIGAN: No.

21           MR. SANSON: No.

22           MR. TOPOROFF: Okay. Moving on to locations and  
23 accounts. I have two questions on that one. One is, again, is  
24 that something that legitimate industry offers, locations or  
25 particular accounts, and I'll use the term account fairly

1 broadly in the sense of finding a market for you. Also, I want  
2 to ask whether just the concept of locations and accounts is too  
3 narrow. Whether there are other forms of assistance that  
4 perhaps more deceptive business opportunities may offer that's  
5 other than just locations and accounts that you should consider.

6 So, on the first issue, are offers of locations and  
7 accounts a characteristic that might distinguish between  
8 legitimate and more deceptive business opportunities? Dennis?

9 MR. WIECZOREK: No.

10 MR. TOPOROFF: Okay. And what is that?

11 MR. WIECZOREK: Because, again, there's a variety of  
12 activities going on out there. Some of the statutes do say that  
13 representations regarding finding accounts, finding bars to put  
14 vending machines in, et cetera, they have those as potential  
15 representations that could qualify you as a business  
16 opportunity. But I don't view that as being an indicator of  
17 illegitimacy, just as we won't provide you any accounts or any  
18 territories is the opposite.

19 You know, you can think of route salesmen out there who  
20 are selling potato chips or soda or anything. And they have  
21 routes and they have territories. They may even get accounts,  
22 but I don't think that makes that automatically questionable as  
23 far as being an illegal business opportunity. So again, I don't  
24 see any distinction between that.

25 MR. FINNIGAN: There certainly is a problem with

1 vending machines, pay phones, and we were talking about the  
2 prepaid phone cards. I have to agree with Dennis. I mean, I'm  
3 sure, even though maybe there's not anyone here right now, I'm  
4 sure that there are some legitimate vending machine companies  
5 that go out and have distributorships and they offer a location,  
6 but there is also a great deal of people who are offering the  
7 pay phones, the vending machines and the prepaid phone cards who  
8 are definitely scam artists, and they're a problem.

9 But again, it's a broken record trying to make a  
10 distinction based on one -- the problem is that every one of  
11 those things, locations, earning statements and I can't remember  
12 the other, are actually legitimate business tactics to use if  
13 they're used properly. And to try to carve a bright line  
14 exemption based on, bright line rule based on one of those is  
15 going to be fruitless.

16 MS. HOWARD: Well, how about things like claims of  
17 location assistance that are tied into guaranties? I mean, does  
18 that turn it from being, you know, maybe okay to not?

19 MR. FINNIGAN: I haven't had experience with that, so I  
20 can't really answer that.

21 MR. ELLMAN: If I may, if it's a guaranty and the  
22 guaranty is not in fact a guaranty, it's still a violation of  
23 law, because it's going to violate an Unfair and Deceptive Trade  
24 Practice Statute.

25 MR. TOPOROFF: John?

1           MR. BROWN: At the risk of being utterly simplistic,  
2 but I think it's really true, the difference between fraudulent  
3 business opportunities and those that are honest is that one is  
4 fraudulent and the other one's honest. And we can't escape that  
5 fact. I mean, that's the bottom line. And I, you know, again,  
6 because we live with always trying to ensure that our  
7 opportunities are not regulated under the biz op statutes or the  
8 trade regulation rule, we talk a lot about the influence of the  
9 laws and to the degree that there are certain things, you know,  
10 trigger mechanisms, and David's story about a contract that  
11 actually listed, you know, we promise that, you know, and you  
12 understand that we won't do anything to help you, number one.  
13 And number two, that we won't buy back anything that we sell  
14 you. And number three, and some other, you know, some other  
15 promise is to say that we won't do something for you is, it's a  
16 perverse unintended consequence of the law if what the law  
17 really drives people to do is, and for example, you know, in the  
18 direct selling industry, inventory repurchase obligations are  
19 universal because we've made a code of ethics of the  
20 association. Well, if the law forced us not to do that, in my  
21 view, that would be a very bad thing.

22           And so, again, we've always kind of viewed the biz op  
23 laws as they were structured the way they were understanding  
24 that no one would comply with them because anyone who would be  
25 subject to it would change their operation to not be. And it

1 sounds strange, but there are many, many more income-earning  
2 opportunities being offered legally throughout the United States  
3 than there are those, and not subject to the biz op laws, than  
4 there are being offered subject to the biz op laws. It is  
5 because of the level of regulation that the biz op laws involve.  
6 Most biz op authors don't view that regulation as being cost  
7 effective and so it basically makes it possible for some kind of  
8 business opportunities being offered. And all the rest, maybe  
9 they're operating outside the law or they're not being offered  
10 at all.

11 MR. TOPOROFF: Well, we're going to get to that, the  
12 next topic in the agenda. But is locations and, well, let's  
13 stick with accounts. Is accounts something that direct sellers  
14 are involved with? Are there promises of a market that will  
15 help you distribute your goods or arrange for a market? Let me  
16 give you an example.

17 And I'm not pointing a figure at the industry by any  
18 means. But in medical billing, for example, a representation  
19 that is frequently made is, we will provide you with lists of  
20 doctors, or we will provide you with people who in turn could  
21 provide you with lists of doctors. So when you sign on, there's  
22 a representation that there will be accounts readily available.  
23 Accounts is just a proxy, if you will, for a market, that we're  
24 setting you up in this business and we will provide you with a  
25 market.



1           MR. ELLMAN: In terms of providing accounts, our  
2 companies make no guaranties that there are, in terms of, that  
3 there's going to be -- for example, our companies are not going  
4 to identify potential customers specifically called Jane Smith  
5 at 123 Neighborhood Street. That's just not going to happen.  
6 But, our companies sell products because our companies make  
7 products or have licenses for products because they believe that  
8 there is a market for that. And people will become a direct  
9 seller because they think that there is a market for it.

10           If I want to become an Avon sales person, if I want to  
11 become an Avon lady, I'm not going to become an Avon lady unless  
12 I think that people are going to buy what I'm going to sell.  
13 But and in that respect, you know, there is some idea of a  
14 marketplace.

15           MR. TOPOROFF: Well, I think there's a distinction  
16 between selling products or services with the expectation that  
17 there will be a market versus buying an opportunity where part  
18 of what you're buying is the expertise and access to a market  
19 that has purportedly already been developed.

20           MR. ELLMAN: Well, in that sense, you know, it's  
21 really, I think, a question of semantics. Because, for example,  
22 let's take a direct selling companies that manufactures  
23 nutritional supplements. And they might suggest that people  
24 aren't eating as healthy as they could be. They don't have  
25 enough time to exercise. And in that respect, they are

1 suggesting that there is a market for nutritional products. And  
2 I'm not sure if you would consider that to be a guaranty of a  
3 market, but it's clearly a suggestion that there is a potential  
4 market out there. But I'm not going to sell something unless I  
5 think people are going to buy it.

6 MR. TOPOROFF: For the regulators.

7 MR. D'ALESSANDRO: Do you think that people are saying  
8 that's bad or good?

9 MR. ELLMAN: I'm saying that it's a good thing for  
10 companies to suggest that, you know, we've got this great  
11 product and we're making it because we think that there is a  
12 need out there and we think you should come sell for our company  
13 because we think there's a great need and you might make money  
14 and we might make money as well.

15 MR. D'ALESSANDRO: I sell nutritional supplements  
16 that's what you're talking about.

17 MR. ELLMAN: Well, good.

18 MR. TOPOROFF: In the Illinois statute, just to clarify  
19 for the record. There is a provision or one of the  
20 characteristics is locations and account assistance, is that  
21 correct?

22 MR. FINNIGAN: Yes.

23 MR. TOPOROFF: Dennis, do you know if that's typical  
24 for most state biz op statutes?

25 MR. WIECZOREK: It's fairly common, yeah. It's common.

1     Yeah. The seller or a person recommended by the seller will  
2     provide or assist the purchaser in finding outlets or accounts  
3     so the purchaser's products or services will assist the  
4     purchaser. I mean, I was going to follow up and say that, you  
5     know, I could see some situations where a direct seller or any  
6     other company would say, well, we're going to pull down a list  
7     of women who are not working and who are on X mailing list and  
8     we'll give it to you and you should market for these people on  
9     this list. I mean, is that finding accounts? Locating  
10    customers? Assisting in finding accounts? Well, yeah. And I  
11    would view that as being a little different than a business  
12    opportunity seller saying, we're going to sell you 100 vending  
13    machines and we're going to call up 1,000 buyers and get you to  
14    put those machines in those buyers. I think that's a different  
15    situation. And that's where more of the fraudulent activity has  
16    occurred rather than someone saying, we're going to do a  
17    download of a mailing list from some service that's going to  
18    target the kinds of customers that you might want to go to.

19             You know, I don't know if Amway or somebody, maybe not  
20    Amway but maybe one of your people down below would say, here's  
21    a mailing list that I picked up that has 1,000 names on it.  
22    Give them a call. They might be interested in doing something  
23    with you. And if that's finding accounts, that's going to be  
24    fairly all-inclusive, I think.

25             MR. TOPOROFF: But I think, again, there might be a

1 distinction between a representation that accounts exist or that  
2 you are going to get assistance in developing these accounts as  
3 part of the inducement for buying into the particular  
4 opportunity versus something that a company might do as part of  
5 its general marketing or whatever that's not necessarily an  
6 express representation up front. And I think that that's  
7 possibly a key distinction. Adam, do you have any thoughts on  
8 that?

9 MR. SOKOL: Well, just in terms of assistance in  
10 developing accounts, there's two types of scenarios in which  
11 I've encountered. The one is that, Dennis' example of the  
12 mailing list or whatever list is downloaded. I mean, we've had  
13 simple unfair and deceptive, we just call it misrepresentations  
14 as to what kind of mailing list you're going to get. We've had  
15 a company which said you're going to get up to 300 hot leads of  
16 the certain type of person who is going to buy that product and  
17 then the purchasers were dismayed to receive only a mimeograph  
18 of 25 people that lived on the same block or within the same zip  
19 code that were not of the same gender or in the same age bracket  
20 of the people that they were led to believe on the list that  
21 they would get.

22 Secondly, in terms of establishing accounts, we've had  
23 the people who have used locators or locating services. And  
24 that has been a part of a number of sort of widespread  
25 regulatory and enforcement efforts such as the license product

1 sweep that went on this summer in which people were given names  
2 of locating companies or were promised locating assistance from  
3 the company in which they'd purchased. And then those locating  
4 companies or the company that was offering them the locating did  
5 not follow through on what people believed they were purchasing.  
6 They were led to believe that they would have these accounts  
7 established for them by the company, by the seller going in and  
8 establishing an account for them and their job was then to just  
9 service those accounts.

10 MR. TOPOROFF: Another characteristic that was raised  
11 in some of the comments is high pressure sales. First off, I  
12 want to ask, under the Illinois statute, is there anything that  
13 addresses that, high pressure sales?

14 MR. FINNIGAN: No.

15 MR. TOPOROFF: So that's not a factor?

16 MR. WIECZOREK: How do you define high pressure sales?

17 MR. TOPOROFF: That's a question. Okay. I think it's,  
18 you're right, it's a tough one. I think it's kind of, you know  
19 it when you see it. And I'm not suggesting that this high  
20 pressure sales should be a factor. I'm just asking whether  
21 there are any policies, for example, in the Direct Selling  
22 Association or its members that would address the issue of high  
23 pressure sales. Does it come up, or how is that dealt with?

24 MR. ELLMAN: Well, I'm not so sure that you can  
25 identify high pressure sales when you see it, because everybody

1 is different. And what might be high pressure for one person  
2 might not be high pressure for another, and you have no way of  
3 knowing that perhaps until all is said and done. And you  
4 grabbing somebody by the shoulders and shaking them might be  
5 high pressure, but you don't know when high pressure begins and  
6 when it's lukewarm pressure.

7 Now, in terms of prohibitions or anything like that in  
8 our industry, our companies strongly encourage their sales  
9 people not to take part in any kind of high pressure tactics.  
10 In fact, in terms of a consumer transaction, the reason we  
11 supported 20 some odd years ago the cooling off period which the  
12 FTC and every state has, is to avoid that kind of high pressure  
13 in terms of the sales types of transaction.

14 But one of the protections that our industry has, which  
15 is not necessarily designed to avoid high pressure, it's really  
16 more of to combat the problem of inventory loading, is that if  
17 somebody feels that they had purchased products or that their  
18 direct selling opportunity is not really for them, they have an  
19 opportunity, if they decide to leave the direct selling  
20 business, to return their products or inventory that they've  
21 purchased and get a 90 percent refund.

22 MR. TOPOROFF: John?

23 MR. BROWN: Amway Corporation, and I think a great many  
24 direct selling companies, avoid a lot of headaches along those  
25 lines of what, you know, trying to determine whether there was

1 high pressure and inappropriate pressure and so forth. The  
2 whole issue is obviated by offering an inventory repurchase to  
3 distributors or, in the case of the sales kit, you know,  
4 affording the persons, in our case, 90 days simply, you know, if  
5 you're unhappy, give it back and you're out of it. You know,  
6 you're done. You don't have to worry about it.

7           So, in effect, it's a combination of cooling off and  
8 somewhere along the line a person's eyes get bigger than their  
9 stomach in terms of the amount of inventory they can handle.  
10 Again, they likewise return that pursuant to the inventory  
11 repurchase obligation. And so, you just get past that whole  
12 issue because it's nothing to argue about. If you felt it was  
13 subject to high pressure, then get your money back and you're  
14 done. And so, it's not a problem.

15           MR. TOPOROFF: Well, we're going to move on. Phil?

16           MR. SANSON: The distinction would be easiest, high  
17 pressure classified as a sale less than ten days, with the ten  
18 day disclosure waiting period. So I guess you're trying to  
19 pinpoint high pressure can be classified where a company comes  
20 in, does a seminar, got the credit card receipts set up at the  
21 seminar. Well, you know, there's no ten day period when you buy  
22 it there.

23           MR. TOPOROFF: So basically, right. What everyone or a  
24 number of people are saying is that you have the ten day cooling  
25 off period up front, that that really should take care of any

1 high pressure sales problems.

2 MR. WIECZOREK: When does the ten days start?

3 MR. TOPOROFF: That's a different issue. But the fact  
4 is that there is ten days. What I tried to do in this session  
5 is go through the various characteristics and try to figure out  
6 do they apply to legitimate industry or not, whether they would  
7 be relevant totally or whether they shed some light on what's  
8 possibly a deceptive sale.

9 In the afternoon what we're going to do is, after  
10 lunch, is try to think of what should be covered by the rule,  
11 meaning, what could a definition of business opportunity be.  
12 And at that time what I would like to do is take some of these  
13 characteristics and fine tune them, weed through them and figure  
14 out which are the ones that we should most focus on.

15 Before we go on to the last item before lunch, which is  
16 why does there appear to be low compliance, I just want to give  
17 anybody else an opportunity to say anything about possible  
18 distinctions between legitimate and deceptive business  
19 opportunities. Adam?

20 MR. SOKOL: I do want to add just sort of one more  
21 thing as I was making a checklist as to the common complaints  
22 that we've had. One of the primary problems that occurs is  
23 after the purchase the purchaser is relying on the support of  
24 the seller to furnish what certain products, goods, inventory,  
25 what have you, and they're met with an assortment of problems



1 ranging from nobody answering the telephone but more frequently  
2 just having whatever product that they want supplied to them be  
3 unavailable. And that can continue for a period of months which  
4 then leads to the person realizing well, wow, I've been trying  
5 this for three months. I can't get the stuff that I'm ordering.  
6 I'm losing all this money. I don't see myself getting the money  
7 back. And then turning around and wanting a refund from the  
8 seller, in which they're unable to get. And that is something  
9 that's been a pattern in numerous business opportunity  
10 investigations that we've taken care of and as well from other  
11 states.

12 MR. TOPOROFF: Anyone else on this point? Okay.

13 For the next 15 minutes, 20 minutes or so, I think Myra  
14 and I will basically be quiet. This is our opportunity to learn  
15 from you why you think there might be low compliance with  
16 business opportunity laws. What's wrong with business  
17 opportunity laws. Any other advice that you may want to impart.  
18 Again, the two of us, Myra and myself, go back to our office in  
19 the next few months and contemplate recommendations for the  
20 Commission on modifications to the Business Opportunity Rule.  
21 So, I know Dennis had mentioned some concerns before about the  
22 state of, or the worse state of business regulation among the  
23 various states. Do you have anything to add on that subject?

24 MR. WIECZOREK: Well, I think it would be preferable to  
25 have a unitary standard. A unitary standard would probably

1 induce more awareness of the rule, more familiarity with it, and  
2 would probably create a better and more even enforcement field  
3 also. The fact is that the FTC Business Opportunity Rule is  
4 pretty toothless. It covers very little. Probably most of the  
5 state business opportunity laws have broader coverage than the  
6 FTC rule.

7 But the state laws are uneven. You may have a tough  
8 law in California and you'll have no law in Oregon. And while  
9 if you compare it to franchising, although there are plenty of  
10 problems in franchising, at least there is a fairly unitary  
11 scheme of regulation. There's a fairly unitary definition  
12 that's used. In business opportunity regulation, there is no  
13 uniform definition. There is no, in fact, why I think most  
14 companies don't comply is because they don't see much  
15 enforcement of the law.

16 And the laws are drafted to be so all-encompassing that  
17 you have a lot of companies operating out there that say they  
18 can't mean to have included me within this scheme. And these  
19 are the legitimate companies. I'm not talking about the scam  
20 artists now. So, I think this polyglot, patchwork of statutes  
21 with non-uniformity, general lack of enforcement just creates an  
22 environment where there is very little compliance and there's  
23 very little penalty for non-compliance.

24 MR. TOPOROFF: John?

25 MR. BROWN: I'd make an observation. And everyone from

1 the State of Illinois can either concur with the thought or  
2 correct it, at least for the State of Illinois. The past 16  
3 years that I've been with Amway Corporation and dealing with  
4 legislation and regulations relating to biz op laws, it has  
5 struck me that the way business opportunity laws work in fact is  
6 not to provide investors in business opportunities with a  
7 disclosure document which assists them in making a judgment,  
8 because there's minimal compliance with the Act. You know,  
9 that's not a frequent occurrence.

10 What is a frequent occurrence is that a complaint is  
11 received by the Securities Division or the Attorney General's  
12 Office or, you know, a trade office within the state about a  
13 fraudulent business opportunity and then that agency or office  
14 is aided in their enforcement dealings with the fraudulent  
15 operation because they don't have to necessarily prove that  
16 somebody lied, you know, stole or cheated. All they have to  
17 prove is that you didn't give them the disclosure document. And  
18 so you've nailed them.

19 And so, it seems to me that, again, I find what the  
20 apparent purpose of the Act, to provide people with information,  
21 is a fiction and the reality of the Act is that it is a  
22 convenient enforcement tool and perhaps not a bad one. Maybe  
23 it's not bad to do it that way, but let's be frank. That's  
24 what's going on. So, that's my observation about the impact of  
25 the law.

1           MR. ELLMAN: In fact, the Nicusso model says as much in  
2 its prefatory remarks that the Commission recognized that not  
3 registering is really most likely going to be the hammer that  
4 states are going to use to bring down people for fraudulently  
5 operating.

6           MR. TOPOROFF: Let me ask this. Is it possible that  
7 the costs and difficulties in registering in the various states  
8 make it too high for even, let's say, legitimate, let alone scam  
9 artists. Legitimate companies to comply with biz op laws?  
10 Eric?

11           MR. ELLMAN: I can just speak for the direct selling  
12 industry. Assuming that we had to comply with state business  
13 opportunity laws, the cost to our industry would be profoundly  
14 enormous. We have 7.2 million direct sellers nationwide. Now,  
15 imagine that the cost of states of getting 7.2 million forms in  
16 would be absolutely outrageous. In fact, we probably have close  
17 to a million sales people alone in the State of Illinois. And  
18 I'm not so sure that the state is equipped to handle a million  
19 disclosure documents.

20           The turnover in our industry is rather significant. We  
21 recruit on average 69,000 to 70,000 new direct sellers every  
22 single week. So, the cost of getting 70,000 documents every  
23 single week into the office of the states would be rather  
24 significant.

25           But leaving aside that issue for the moment and getting

1 back to our industry, if you've got a disclosure document which  
2 is 50, 60, 70 pages deep or more, and you've got somebody who,  
3 you know, is really only trying to become a direct seller and  
4 make a few thousand dollars a year and they're saying, well,  
5 geez, you know, I only want to be an Avon lady. Why do I have  
6 to read this or why do I have to hand this out to every one of  
7 my friends who I say how great working for Avon is. And we were  
8 discussing this at the break, is that because the profit, well,  
9 I shouldn't say the profit margin, because most direct sellers  
10 only make a few thousand dollars a year and you've got a  
11 disclosure document which says, consult your attorney. Well, if  
12 you meet with an attorney for an hour, you've already eaten up  
13 your profits for the first quarter of the year.

14 And the cost of compliance to our industry would be  
15 beyond extraordinary.

16 MR. TOPOROFF: Do the regulators have any thoughts on  
17 that?

18 MR. FINNIGAN: I think that our laws essentially are  
19 registration and a disclosure requirement, and I think it is a  
20 legitimate purpose of the state to require registration. I  
21 would agree that it does provide us with a hammer when someone  
22 fails to register. But the purpose of the registration is that  
23 it allows us to gather information and provide it to the public,  
24 in addition to the disclosure requirement.

25 I think that perhaps, Eric, you're a bit confused in

1 regards to the registration requirements under the Illinois  
2 Business Opportunity Act. The first one is that it's the  
3 opportunity itself that's registered. There's only one  
4 disclosure document that's provided to our office, which it  
5 explains that it is an opportunity and provides information  
6 about the officers and directors and, you know, business history  
7 and things of that nature. It does not need to be sent in to us  
8 every time you make a sale or have a business opportunity. And  
9 it only needs to be -- a new one needs to be sent into our  
10 office if there's been some sort of change or an officer has  
11 been changed.

12 MR. ELLMAN: But not every state is that way. Some  
13 states require annual renewals and the disclosures that are  
14 required in many other states can be significant.

15 MR. FINNIGAN: What it means is that it required 70,000  
16 documents to be sent in. My second point is that we register  
17 the opportunity. We do not register, for lack of a better term,  
18 the sales persons or the employees or the people who are going  
19 out and offering these business opportunities. So I guess I was  
20 questioning whether or not the amount of paperwork and  
21 documentation that you have just cited as being required of your  
22 members is really that of, at least under the Illinois law.

23 MR. ELLMAN: Well, I'm not necessarily suggesting that  
24 you would be receiving 70,000 pieces of paper or documents every  
25 single week, but your end, the regulators end, depending on the

1 state, can be significant. But from our end, it's going to be  
2 significantly more burdensome because if you're presenting an  
3 offer to somebody, say this is a great opportunity, you know,  
4 look into it, sign up or what have you, you're going to have to  
5 present various kinds of disclosure documents. And that's where  
6 the burden is going to most heavily fall on us. Regulators in  
7 various states will be burdened, but not nearly to the extent  
8 that we will.

9 MR. FINNIGAN: To answer your question, first of all,  
10 and I can only speak about Illinois, Phil can also expound upon  
11 it. I think the reason why we don't have a large amount of  
12 registrations is one, because ours was the most recent act out  
13 there. We learned from the lessons of the other acts. And so  
14 there's quite a few exemptions for the legitimate income-earning  
15 opportunity businesses to fall under the net worth, the  
16 trademark, the franchise. So, most people are able to find an  
17 exemption, if they look at it and are legitimate. And frankly,  
18 the person who this Act is targeted at, the scam artists aren't  
19 going to register. So, you know, they're not going to register  
20 and the legitimate people will find some sort of exemption that  
21 applies to them.

22 MR. TOPOROFF: And again, this afternoon we are  
23 definitely going to talk about exemptions. That is definitely  
24 on the agenda.

25 MS. HOWARD: David, can I follow up on something? Do

1 you think the scam artists would be more apt to register if the  
2 disclosure document was three pages instead of 30?

3 MR. FINNIGAN: No, and frankly, no, I just don't think  
4 that they would. I mean, the reason why they're scam artists is  
5 because -- and the reason why we want registration is because we  
6 want to be able to locate, track these people down, and that's  
7 why we want this information. And obviously, inherently, that's  
8 not something they're going to want to provide.

9 MR. ELLMAN: And even if they did register, which they  
10 wouldn't do anyway, no matter how many pieces of paper. Even if  
11 you had to fill out a yellow stickie, they still wouldn't do  
12 that. But even if they did register, there's nothing that would  
13 prevent them from filing fraudulent disclosure documents.

14 MR. TOPOROFF: Anybody else have anything else to add  
15 on the subject of why there appears to be low compliance with  
16 the disclosure of business opportunities?

17 MR. SANSON: Some of the companies, the ones that do  
18 apply, the registration is abandoned because they didn't have an  
19 audit to review financials. So, that's one, another reason. I  
20 think the FTC just requires a balance sheet. Well, under our  
21 Act, it's either a limited review or an audit financial.

22 MR. TOPOROFF: We require an audit financial also. You  
23 know --

24 MR. SANSON: Okay. Because a lot of, well, \$2,000 to  
25 them, and they don't want to pay it.



1 MR. TOPOROFF: Anything else? Otherwise, we are going  
2 to break for lunch.

3 (Whereupon, at 11:45 a.m., the  
4 meeting was recessed, to reconvene  
5 at 1:00 p.m., this same day,  
6 Thursday, August 21, 1997.)  
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19 A F T E R N O O N S E S S I O N

20 (1:05 p.m.)

21 MR. TOPOROFF: Before we begin the next agenda item, I  
22 just wanted to mention again that there will be opportunities at  
23 the end for any of the observers to make statements on the  
24 record. I will remind everyone at that time. Just offhand, by  
25 a show of hands, are there any of the participants who want to

1 make a statement later today? None. Okay. Well, I'll make an  
2 announcement again in case people change their minds or in case  
3 there are others who aren't here yet.

4 All right. The next agenda item is what opportunities  
5 should be covered by the Rule. Perhaps a better way of stating  
6 that is, what should be the definition of business opportunity  
7 for disclosure purposes? For the discussion this afternoon, we  
8 are going to assume that there is going to be some disclosure  
9 requirements under the Rule. So, whether there should be,  
10 whether there shouldn't be disclosure is not an item that's up  
11 for discussion right now. We are going to assume, again, that  
12 there will be disclosure. It's just a question of what should  
13 that disclosure document look like.

14 So, we had this morning a fair amount of discussion on  
15 characteristics that may or may not be relevant in  
16 distinguishing business opportunities. We talked about problems  
17 or obstacles to complying with the Rule. But again, for our  
18 purposes right now, we're going to focus on what the definition  
19 should be.

20 I also want to mention, before we took a break for  
21 lunch, that I had noted that we had talked about individual  
22 characteristics in isolation. Now is an opportunity to put them  
23 together and really focus on what distinguishes, perhaps, taken  
24 in its entirety, fraudulent business opportunities that again we  
25 would want to cover in the Disclosure Rule versus those of a

1 more legitimate business.

2 So, I'm going to start with the ANPR's definition, the  
3 proposed definition of a business opportunity, which is perhaps  
4 the broadest that we could possibly envision. And in essence,  
5 what it means is, any time you're selling, and again, we'll use  
6 an income opportunity with more than nominal assistance, that  
7 that should be covered by the Rule.

8 Now, when we put that out for comment in the ANPR, the  
9 discussion that goes along with it stated that we were floating  
10 that as an idea for discussion. So, it doesn't necessarily mean  
11 that that's what the Commission is wedded to revising the  
12 definition to reflect. It is more a thought piece. On that, I  
13 would like to have some discussion on that proposal. That is,  
14 that we should focus on companies who offer opportunities where  
15 there is more than nominal assistance.

16 Anybody have any comment on that? John?

17 MR. BROWN: As a stand alone definition of the business  
18 opportunity, obviously the concern that it raises for Amway  
19 Corporation is that we feel very strongly that there should be a  
20 threshold below which or above which opportunities are not  
21 covered. Below which would be those opportunities which are  
22 offered at such a low cost that the level of regulation inherent  
23 in a biz op or an FTC rule would be inappropriate. And then I  
24 think there is a strong argument, while not applicable to Amway,  
25 I think there is a strong argument that with investments of a

1 certain size, people should be adequately represented by counsel  
2 and by other professionals such that they don't really require  
3 the specific protection of the Government. However, that's not  
4 Amway's concern.

5 In terms of another more general observation, I think  
6 the definition is actually somewhat consistent with the  
7 practical result of many of the state biz op laws, and that is  
8 that the very specific activities which could possibly make an  
9 offer a business opportunity for purposes of the law really  
10 become irrelevant in the face of the one provision which talks  
11 about having a marketing plan and providing assistance, which is  
12 so broad that it's really inconceivable that someone could be  
13 offering a business opportunity and not provide some kind of  
14 guidance, marketing assistance and so forth, that wouldn't bring  
15 them under the Act. And so, in a way, it's a more simplified  
16 version of what is presently really the policy of a great many  
17 states.

18 MR. TOPOROFF: David?

19 MR. FINNIGAN: I would agree. That's practically  
20 that's where we've gone to. In fact, in discussing this with  
21 Phil, we came down to that the one thing that a business or  
22 income-earning opportunity cannot mess with is that they almost  
23 inherently have to offer some sort of assistance or training or  
24 marketing plan. I mean, you can craft, I think, any other  
25 income-earning opportunity in just those five other indicia

1 being an income-earning opportunity, but you can't, or at least  
2 I just don't think it theoretically possible to avoid providing  
3 promotional literature, training manuals, training, assistance  
4 or something like that. So I think that that's a very good  
5 definition to start from. And even though it is broad, it may  
6 be very, you know, an all-encompassing net, you work from there  
7 and then you carve out the exemptions. I think that way you get  
8 a very workable definition that doesn't come up with these false  
9 distinctions that we were all, you know, pointing out when we  
10 were talking about well what are indicia. Is location  
11 assistance indicia? Is income earning statements an indicia?  
12 No. A guaranty, no. But marketing plan or something more than  
13 nominal assistance, I think, is a very good indicia.

14 MR. TOPOROFF: Is there a specific definition for  
15 market plan?

16 MR. FINNIGAN: Yes, we do. We have a definition of  
17 marketing plan in our statute, which is pretty broad.

18 MR. TOPOROFF: For example? I don't mean to have you  
19 read it into the record. But just generally, what does it  
20 cover?

21 MR. FINNIGAN: Again, I talked about, it's basically  
22 providing training or assistance in operating the business and  
23 it gives three examples, promotional literature, and then it  
24 talks about training and operating manuals on providing  
25 marketing and operating the business opportunity. And the third

1 one escapes me right now, but again, it's in the state statute  
2 and you can take a look at that.

3 MR. TOPOROFF: Okay. Well, let me pose this to the  
4 participants here. If the Commission were to adopt a definition  
5 of business opportunity that focused more or less on, let's use  
6 Illinois' statute as an example, on marketing plans. Is the  
7 term marketing plan sufficient to capture the types of deceptive  
8 practices that we want? Or is that term in and of itself  
9 overbroad? Dennis, any thoughts?

10 MR. WIECZOREK: Well, I'm wondering, comparing the  
11 language which is proposed in the ANPR, this really focuses on  
12 assistance as opposed to nominal assistance. More than nominal  
13 assistance as opposed to marketing plan. You know, I don't want  
14 to get into a metaphysical analysis of what's the difference  
15 between those two. They're pretty darn close. But there is  
16 something to be said for the tried definition of marketing plan,  
17 because that seems to be a fairly commonplace term that's used  
18 in the state statutes. Are you missing anything? It would be  
19 very, again, I think you're talking about the head of a pin as  
20 to the difference between what you would catch with nominal  
21 assistance versus what you will catch with marketing plan, other  
22 than, it seems to me just as a grammatical matter, that  
23 marketing plan covers more and nominal assistance seems to  
24 provide an exit for someone who says, well, it was nominal.  
25 Obviously, you can define nominal like marketing plan and you're

1 back to where you started anyway.

2 But just as a definitional matter, I wonder if it's  
3 better to use the marketing plan language rather than nominal,  
4 more than nominal assistance. The other point I want to make is  
5 that, in general, I think this definition is way overbroad.

6 MR. TOPOROFF: Which definition?

7 MR. WIECZOREK: The definition of business opportunity  
8 in the ANPR. But, I mean, I would prefer that it be a very  
9 narrow definition without the need for exemptions. But I can't  
10 offer anything in place of that. I think this is probably the  
11 only practical way to get at this, is to use a very broad  
12 definition and then make sure you have an extensive laundry list  
13 of exemptions that takes out the legitimate companies. That's  
14 just theory as opposed to language right now.

15 MR. TOPOROFF: Is there case law in the states that  
16 construe the term marketing plan? Not necessarily in Illinois.  
17 I'm saying in states generally. Is that a concept that is well  
18 defined in law?

19 MR. WIECZOREK: Well, there are franchise cases now  
20 that have defined marketing plan, and I'm sure there are  
21 interpretative opinions out of the FTC that talks about  
22 significant assistance, which is not that different than more  
23 than nominal assistance. I think significant doesn't really  
24 necessarily mean significant under the Franchise Rule.

25 And, you know, the cases, there's a case in Michigan

1 that was just decided within the last few months. And the  
2 issue, the court said, well, there was a manual, there was some  
3 training, there was some assistance. Those kinds of things were  
4 provided. That's enough to be a marketing plan. So there are  
5 some franchise cases out there.

6 Business opportunity cases are few and far between. I  
7 would be that in terms of reported decisions that there can't be  
8 more than maybe ten, maybe ten that deal with substantive issues  
9 as opposed to this was an enforcement action. And obviously,  
10 you have a lot of enforcement actions, and the states do, too.  
11 But in terms of appellate courts or trial courts issuing  
12 decisions, there's very few. Probably less than ten, I would  
13 bet.

14 MR. TOPOROFF: Eric?

15 MR. ELLMAN: I think that the definition that's in the  
16 ANPR is pretty broad. And I think that it can only be  
17 appropriate, and it has the significant potential of taking in a  
18 lot of legitimate people, direct sellers and otherwise. And it  
19 would be a bad definition standing by itself without recognizing  
20 the legitimacy of certain businesses, including direct selling,  
21 for which we would not be able to live with this definition by  
22 itself.

23 MR. TOPOROFF: Adam, based upon your experience, if we,  
24 we meaning the Commission, had a definition of business  
25 opportunity that really focused on the concept of marketing



1 plan, would that be broad enough to capture the type of  
2 deceptive scams that we see?

3 MR. SOKOL: I'm really not sure that there's any one  
4 thing that is going to be broad enough to capture everything.  
5 Obviously, with marketing plans, there's going to always be,  
6 there's going to be something different, some other variable,  
7 that doesn't fit into what was previously defined. But I can't  
8 really give an affirmative yes.

9 MR. TOPOROFF: Okay. In addition to marketing plan,  
10 are there any other characteristics or, I suppose the best  
11 example would be from Illinois, the list of the various  
12 characteristics that need to be met to fall within the statute.  
13 Are there comparable kinds of characteristics that we should  
14 consider as part of the definition of business opportunity so we  
15 would have marketing plan plus, is there anything else in  
16 particular?

17 MR. WIECZOREK: Well, I don't know if you consider a  
18 minimum and a maximum as part of the initial definition or part  
19 of the exemption list, but I think it's silly to start at zero.  
20 You should not start at zero. There should be a minimum point  
21 at which the law kicks in. And probably a maximum point where  
22 the law goes away.

23 MR. TOPOROFF: And we're going to be talking about  
24 those, yes. So if you could hold off on that.

25 From the regulators' point of view, is there anything

1 that you have found?

2 MR. SANSON: Location assistance. Sometimes with  
3 vending machines, there's not really a training or marketing  
4 plan, but they do offer location with the vending machines. So  
5 if you could put that in there.

6 MR. TOPOROFF: Well --

7 MR. SANSON: Because that's a different -- that's a  
8 member, too, of our statute, where the marketing plan is our  
9 sixth step.

10 MR. TOPOROFF: Is there a distinction though? Does  
11 marketing plan incorporate the concept of location assistance  
12 and accounts?

13 MR. SANSON: We don't have, no.

14 MR. TOPOROFF: I understand in the Illinois statute  
15 it's separate. I'm saying, in theory or conceptually, to have  
16 marketing plan, does that incorporate the notion, or an example  
17 would be assistance?

18 MR. FINNIGAN: I think you could fit that in there.  
19 And I guess one of the concerns that I have when we're talking  
20 about this is that you have to include some other indicia in  
21 there. Otherwise, there are people who are legitimately selling  
22 equipment, but they're not selling a business opportunity. An  
23 example is that I have been to Sam's Club and I've seen, you  
24 know, vending machines that you can purchase there, but I don't  
25 think they're selling a business opportunity. But if you don't

1 include some sort of marketing plan or some other indicia, then  
2 Sam's Club would be included in there or, you know, if somebody  
3 goes to Sears and buys a chain saw and they're going to use that  
4 for their business of chopping down firewood. So you have to  
5 have some sort of, you know, you either have to have a marketing  
6 plan or some other indicia in there.

7 I think marketing plan, I think, in my opinion, covers  
8 almost every example that I can think of. Maybe there's some  
9 out there, but, you know --

10 MR. TOPOROFF: Well, that's precisely what I was  
11 getting at.

12 MR. FINNIGAN: I'm just saying, I can't think of  
13 anything else that you can add to that that can't be  
14 manipulated. If you try to include, you know, locations or the  
15 other ones, that could still be manipulated. So I think that  
16 marketing plan gives you the best coverage of everything you  
17 could possibly think of. Maybe there will be a couple of things  
18 that fall through the crack, but I guess I'm not too concerned  
19 about it. I think that most everything that we want to cover,  
20 or that the FTC would want to cover would fall under marketing  
21 plan or nominal assistance.

22 MR. WIECZOREK: The only possibility would be  
23 situations where it's the work of the more traditional  
24 work-at-home situations stuffing envelopes or stringing beads or  
25 whatever. I mean, I assume there's going to be some sort of

1 guidance or manual that would be, it's not that hard to figure  
2 out. But, you know, you are growing worms or whatever. They're  
3 not really, I mean, marketing plan connotes that there's going  
4 to be some marketing made. They're going to teach you how to  
5 market to the public. And in those situations, there's really  
6 not necessarily any public involvement at all. These people  
7 are, you know, they're working a job at home. And they buy  
8 something. You know, whether it's worm starter kit or, you  
9 know, 10,000 envelopes or whatever it is they buy.

10 So it may be that there's going to have to be something  
11 that would capture those kinds of things. Either that or  
12 stretch the definition of marketing plan to include, and  
13 actually the Illinois law does talk about instructions or  
14 assistance. We figure there would have to be a little bit of  
15 some degree of instruction in those situations.

16 MR. SOKOL: Right. I think in our Section 515, we have  
17 marketing plan, including preparing or providing, subpart three,  
18 operational, managerial, technical, financial guidelines or  
19 assistance. I think operational, managerial assistance can be  
20 interpreted very broadly.

21 MR. TOPOROFF: And that would cover, well, let me ask  
22 directly, Phil and David, is your statute -- does your statute  
23 cover what we would commonly know as the work-at-home schemes,  
24 like putting the beads together or envelope stuffing?

25 MR. SANSON: We haven't perceived that.

1           MR. FINNIGAN: We haven't had any cases like that yet.  
2 You know, involving where they're putting parts or something  
3 like that. We've had home businesses, but it's required that  
4 you make sales either through the phone or something like that.  
5 Those may not actually be biz ops.

6           MR. SANSON: It seems like most of the envelopes, that  
7 stuff, is below the \$500 payment anyway. So, that's kind of why  
8 we don't see too much.

9           MR. TOPOROFF: Okay. John, did you want to add  
10 something before?

11          MR. BROWN: No. I'll wait until we start a discussion  
12 of exemptions.

13          MR. TOPOROFF: Okay. Well, this is time for one of  
14 those votes. If the Commission is going to consider a business  
15 opportunity definition, should the basis or the essence of that  
16 definition rely on the concept that's, let's say, put forth in  
17 the Illinois statute of a marketing plan or seller-assisted  
18 marketing plan? Would that do it? Is there enough clarity on  
19 that issue? We'll take a vote. We'll start with Dennis.

20          MR. WIECZOREK: I think so, yes.

21          MR. TOPOROFF: Adam?

22          MR. SOKOL: I'm going to pass.

23          MR. BENNETT: I think I'll pass, abstain.

24          MR. BROWN: I would say that whatever, and I don't know  
25 if this is a yes or a no, but however the FTC proceeds, I'd like

1 to see it proceed in a way that is consistent, uses terminology  
2 that is consistent with state laws or at least what we find out  
3 the state, you know, there are many differences among the  
4 states. I'd like to see some continuity developed. And we have  
5 in fact suggested the Illinois law largely because of the  
6 marketing plan element of the definition. We think that's  
7 appropriate and covers what has to be covered.

8 MR. TOPOROFF: Eric?

9 MR. ELLMAN: We think the Illinois approach is a pretty  
10 good approach and we have indicated that in our comments. So  
11 I'll repeat that consistency of the state laws as much as can be  
12 consistent with the patchwork is relatively important. But  
13 perhaps from our perspective, of course, the most crucial, in  
14 addition to when you were discussing about who is covered by a  
15 definition, I think we also need to look at who's not being  
16 covered. And that is an issue of significance to us as well,  
17 and that deals, of course, with the exemptions which we'll  
18 discuss shortly.

19 MR. TOPOROFF: Rick?

20 MR. GEU: I abstain.

21 MR. TOPOROFF: Phil?

22 MR. SANSON: I would say yes.

23 MR. TOPOROFF: John?

24 MR. D'ALESSANDRO: Yes.

25 MR. FINNIGAN: Yes.

1           MR. TOPOROFF: Anything else that we should be aware of  
2 when we craft the definition of business opportunity? Any other  
3 concerns?

4           MR. WIECZOREK: Can I ask a question of Eric?

5           MR. TOPOROFF: Sure.

6           MR. WIECZOREK: And that is, a lot of the older  
7 statutes have buy back language in it. How does that jive with  
8 the DSA's position on requiring members to buy back any  
9 inventory from a member? I mean, in your case it's a salutary  
10 purpose? Under the laws I think the idea was that that's the  
11 worm farms and chinchilla ranches?

12           MR. ELLMAN: Exactly. Well, that's an excellent  
13 question. And since you brought it up, I'll bring it up here.  
14 One of the things that we wanted to impress upon the Commission  
15 and staff during the buy back is that we've never been entirely  
16 pleased with the older statutes which say that if you buy back  
17 stock that makes you a business opportunity. And obviously,  
18 that definition exists, or some part of the definition exists to  
19 deal with the stuffing envelopes and the beads and the worm  
20 farms and that sort of thing.

21           But from our perspective, it's a consumer protection  
22 issue. We developed our buy back to prohibit inventory loading  
23 and to prevent people from being loaded down with a garage full  
24 of stuff. We would encourage any definition that you not cast  
25 somebody as a business opportunity simply because they offer

1 consumer protection like an inventory buy back. I don't know if  
2 you can distinguish between buy backs that are designed as a  
3 method of protecting consumers as opposed to repurchase  
4 arrangements where they are designed to bilk consumers. I don't  
5 know if there's a way you can distinguish. But the existence of  
6 an inventory repurchase policy should not automatically make one  
7 a business opportunity.

8 MR. TOPOROFF: John?

9 MR. BROWN: Relating to what Eric just said, and over  
10 the years having studied a number or read a number of studies  
11 concerning biz op fraud and the nature of that fraud, it's my  
12 understanding that that particular language, which you find  
13 particularly in a number of older biz op statutes, really  
14 related precisely to the phenomenon of the worm farms and other  
15 kinds of business opportunities where you were to be provided  
16 guidance and assistance on producing something, assembling  
17 something or producing it. And the way to convince the offeree  
18 that this was a viable opportunity was then to say, and if you  
19 don't think you could find a market for these valuable goods,  
20 well, don't worry, we have markets for you and we'll buy them  
21 back.

22 And so, it was -- that's a different thing from someone  
23 who is selling laundry detergent and, you know, home care and  
24 personal care products who says, you know, you purchase these  
25 things and you resell them to your customers. But if you should



1 decide to leave the business, you give them back, that which you  
2 have still in your possession.

3           And I think the fraud that existed, you know, back,  
4 particularly in the '60's and '70's with some of these  
5 opportunities was that there was no intention on the part of the  
6 offeror to ever purchase back the goods that were assembled or  
7 produced by the offeree. And that really wasn't the business  
8 that they were in. They were in the business of selling the  
9 opportunity. They weren't in the business of selling Jerusalem  
10 artichokes. They just weren't in that business. And so, it was  
11 patently fraudulent.

12           And early on today, I indicated that, you know, one of  
13 the ironies of the biz op laws the way they're drafted in a  
14 number of states is that they are a disincentive for a business  
15 opportunity offeror to provide a bona fide buy back because you  
16 literally, they figured out some way to avoid the marketing plan  
17 language. You know, if they would offer the buy back, then that  
18 would be the hook that brought them in. So they don't do that.

19           And, you know, our view of, Amway's view and the view  
20 of the direct selling industry generally is that there are  
21 certain activities that should be encouraged and not discouraged  
22 by virtue of the law. And the inventory buy back is a good  
23 thing. It shouldn't create coverage under the law. And  
24 likewise, keeping to costs down is a good thing for  
25 opportunities and that's why having a threshold below which

1 coverage does not kick in we think is a good thing.

2 MR. WIECZOREK: back. The buy back language I don't  
3 think is supportable in a potential rule. Because aside from  
4 the discussion of the direct sellers, there have been several  
5 franchisors that have gone out to the market and said, you can  
6 test drive this franchise for six months or a year. If you  
7 don't like it, you can get all your money back. That would seem  
8 to be a good thing. Instead when these franchisors started  
9 looking at biz op laws around the United States, they found that  
10 all of a sudden they had subjected themselves to certain state  
11 business opportunity laws, and that was a big problem.

12 So, I would urge that that portion of a definition of  
13 business opportunity not be included in a rule.

14 MR. TOPOROFF: Any other thoughts on that issue? Okay.  
15 Before we move on, there's a few other points I want to raise.  
16 It's not necessarily in terms of defining a biz op, but there  
17 are certain other characteristics of the rule that I think might  
18 be unique when it comes to business opportunities as opposed to  
19 franchises. And one is the triggering mechanism.

20 Right now disclosure is triggered by one of two events.  
21 Either first face-to-face meeting or at least ten days before  
22 sale is consummated, either by signing a contract or by  
23 tendering a payment. One of the comments that we heard from,  
24 Andy Caffey, made it a point of noting that he believes the term  
25 personal meeting is irrelevant because that's just not the way

1 business opportunities are sold. They are sold over the  
2 telephone. They're sold through the mail. And they're sold  
3 through the Internet and other modes, but not necessarily in a  
4 face-to-face meeting.

5 Now, this discussion on when the rule should be  
6 triggered is really distinct from the same issue in the context  
7 of franchise sales, which we are not going to discuss today.  
8 That will be discussed at the next meeting in September. So I  
9 don't want to get hung up on that. The two don't necessarily  
10 need to be the same. So, for purposes of our discussion right  
11 now, I want to again address the triggering mechanism and the  
12 concept of personal meeting, whether that is a relevant term for  
13 the sale of business opportunities. Any thoughts? David?

14 MR. FINNIGAN: Well, clearly the rule as it is now is  
15 deficient in that it talks about a face-to-face meeting, and I  
16 think from our own experience that the media that you just  
17 indicated are used quite often. And perhaps the rule should be  
18 back towards the latter one, which was the ten day after tender  
19 of payment or contract signing, something like that is probably  
20 going to be more useful than a face-to-face ruling. Clearly  
21 there are some situations, I guess, trade seminars and shows  
22 where there is a face-to-face meeting, but there's also a lot of  
23 biz opportunities that are sold, telemarketing, Internet,  
24 through the mail.

25 MR. TOPOROFF: Well, would it be helpful to at least

1 retain the notion of face-to-face meeting so that if in fact  
2 there is one, at least that's captured. Would that make sense?  
3 Or is it so unlikely that there's going to be a face-to-face  
4 meeting?

5 MR. FINNIGAN: I guess it's my viewpoint is that it's  
6 just better to come up with a broader definition. And I think  
7 that the second rule covers a face-to-face meeting also. Rather  
8 than, I guess, my personal viewpoint is, you always want to try  
9 to come up with a rule that takes care of everything and the  
10 face-to-face one doesn't, but the second one does. That one  
11 just needs to be tweaked a little bit more and you can keep the  
12 face-to-face one or remove that one.

13 MR. TOPOROFF: Well, part of the reason that, at least  
14 when it comes to franchise sales, that there's the first  
15 personal meeting requirement is franchise sales are usually  
16 negotiated, and it could be a period of several months between  
17 the time somebody becomes interested and learns about the  
18 opportunity, negotiates the contract and signs on the dotted  
19 line. And one of the concerns that we have is that people  
20 should get disclosures early in the process before they're  
21 hooked and they become committed to this.

22 Is there a similar kind of concept of being hooked when  
23 it comes to a business opportunity? Are there negotiations or  
24 is it more like the sale of a product off the shelf? Here's the  
25 opportunity, you buy it.

1           MR. FINNIGAN: It's more like that. I mean, Phil maybe  
2 can talk a little bit more on this also, but I don't think that  
3 there's a lengthy -- I shouldn't say I think. I mean, just from  
4 the cases that we had, it is not a lengthy process. They  
5 attended a seminar and they heard a presentation on it. There  
6 was credit card machines in the back of the room. They bought  
7 it at that time. Or they called an 800 number. They talked  
8 with someone. They received some literature in the mail. That  
9 one might be a little bit longer, but we're not talking -- at  
10 the most, with the seminars, we're talking 15 minutes to half an  
11 hour, an hour maybe. You know, through the mail or phone number  
12 or through the mail an advertisement or through the phone, it  
13 might be, you know, a couple of days to a week. We're not  
14 talking very long negotiations that a lot of thought or a lot of  
15 time in these things. Would that be your experience also, Phil?

16           MR. SANSON: It's relatively short. A day at the most.

17           MR. TOPOROFF: What is your triggering mechanism under  
18 the statute? I'm sorry. What's the triggering mechanism?

19           MR. FINNIGAN: Well, it's \$500.

20           MR. TOPOROFF: Not in terms of the threshold. In terms  
21 of disclosure obligation.

22           MR. SANSON: Ten business days.

23           MR. TOPOROFF: Ten business days. So you don't have a  
24 first face-to-face meeting?

25           MR. SANSON: That's not in our Act.

1           MR. TOPOROFF: Adam, what do you think? If there's the  
2 ten business day provision alone, would that be sufficient to  
3 trigger a disclosure obligation?

4           MR. SOKOL: Should be.

5           MR. TOPOROFF: Should be. Anybody else have anything  
6 to add on the subject? Okay.

7           Finally, I just want to add or raise the subject. Is  
8 ten business days sufficient? Is it too long? Is it too short?  
9 Again, we're talking about biz op sales. Or is it about right?  
10 No one has any thoughts. Well, I'll assume it's adequate.  
11 There doesn't seem to be any particular problem with ten  
12 business days. John?

13           MR. D'ALESSANDRO: I think business days is confusing  
14 today. Businesses working seven days a week. I think I'd have  
15 to define it as --

16           MR. TOPOROFF: Two weeks?

17           MR. D'ALESSANDRO: Or ten days or fourteen days, but  
18 not ten business days.

19           MR. TOPOROFF: Okay.

20           MR. WIECZOREK: I would agree with that. We have  
21 problems figuring out what Federal holidays count, what doesn't  
22 count. I think you can make it very straightforward and just  
23 say days. I would also get the sense that a shorter time period  
24 would probably be adequate. You see cooling off periods under,  
25 what is it, door-to-door sales is three days, I think? You

1 know, there are shorter time periods. I think the idea is to  
2 stop someone from being high pressured into buying that day,  
3 because, you know, the salesman sits there and says, well,  
4 unless you do it right now. It's like going to a car dealer.  
5 Unless you buy it now, it may not be here tomorrow. I think as  
6 long as it's a few days, I think that's adequate. I don't know  
7 that ten is required. I would think that it could go shorter, a  
8 seven day or ten calendar days.

9 MR. TOPOROFF: Now, one distinction between the ten  
10 business days for franchise and biz op sales versus door-to-door  
11 sales is, door-to-door there's no disclosure document that we're  
12 encouraging respective buyers to go inside and talk to their  
13 accountants and lawyers and what have you. So I think whatever  
14 the time frame might be adequate has to factor in allowing  
15 sufficient time to go to other professionals for assistance.  
16 But again, as opposed to door-to-door, which is solely the  
17 consumer's decision. People don't really go to other  
18 professional assistance in deciding whether to cancel buying  
19 household wares that are sold door to door. So I think that  
20 there's a distinction.

21 MR. WIECZOREK: Although in theory, a biz op disclosure  
22 is shorter, significantly shorter than any franchise disclosure.  
23 And as you know, there's significant problems with getting  
24 people to read the franchise disclosure documents, because they  
25 are so long. So, I would go for a calendar day period that

1 could be shorter than ten days.

2 MR. TOPOROFF: Any other thoughts on that? Otherwise,  
3 we'll move on. Okay. Myra?

4 MS. HOWARD: Okay. We next want to take a look and  
5 see, we're trying to get an idea of what disclosures or  
6 prohibitions are relevant to the sale of biz ops. And again,  
7 we're looking at the broad picture here. What I'd like to do is  
8 just run down sort of the list of things that are presently in  
9 the FTC Rule that are in the UFOC and then get suggestions and  
10 comments on what else should perhaps be included or what else is  
11 relevant.

12 So, we're going to have sort of three categories here.  
13 We're going to have the category of it's absolutely crucial,  
14 must be included. The category of absolutely irrelevant, forget  
15 about it. And then the sort of in between, it's relevant, but,  
16 you know, there's a balancing act to be done.

17 So, the first provision is simply name, address, place  
18 of business, and whether or not, if there's a parent company,  
19 name and address of that company. Anybody have any thoughts?

20 MR. WIECZOREK: It seems kind of crucial.

21 MS. HOWARD: Seems kind of crucial. Are we in  
22 agreement that that's kind of crucial?

23 MR. WIECZOREK: Yes.

24 MS. HOWARD: Okay. I mean, some of these will be  
25 extremely quick. If there's another name under which the



1 company will do business. Also crucial?

2 MR. WIECZOREK: Yes.

3 MS. HOWARD: Agreement. Okay. Yeah. And if anyone  
4 has comments or wishes to explore these, please jump right in.

5 How about if there's a trademark or a trade name  
6 associated, and if there is, to list what it is? Crucial?

7 MR. ELLMAN: Yes.

8 MS. HOWARD: Business experience of current directors,  
9 executive officers for X number of years back? John, you're  
10 shaking your head no?

11 MR. D'ALESSANDRO: They would lie about that.

12 MS. HOWARD: Pardon?

13 MR. D'ALESSANDRO: They could lie about that very  
14 easily and exaggerate the point.

15 MR. ELLMAN: But that can be done with anything in the  
16 disclosure document. They can even lie about their name.

17 MR. TOPOROFF: Well, I think there is a reason that  
18 type of disclosure is in the franchise disclosure document is  
19 the prospective buyer is relying on the expertise of the  
20 franchise seller for assistance, control, trademark, those kinds  
21 of things. Where I don't know is in the sale of a business  
22 opportunity, is anyone relying on the expertise of the seller  
23 that would make a significant difference what the seller's  
24 background and experience is?

25 MR. WIECZOREK: It's a close call.

1           MR. FINNIGAN: You know, if I was a purchaser of a biz  
2 op, I mean, it would be relevant to me if the people who are  
3 loaning this have previous bankruptcies or have had business  
4 failures, those sorts of things and I think that is what would -  
5 - I think that's what would be covered under the history. So, I  
6 don't know if that rises to being crucial, but I think it may  
7 fall more under a two plus rather than a number one category.  
8 So, I think this is a two plus.

9           MR. TOPOROFF: Eric?

10          MS. HOWARD: Okay. So are we to assume this is going  
11 to be one of those in between categories?

12          MR. WIECZOREK: My comments are, and you want to make  
13 this disclosure document as short as possible. And I think you  
14 should be very careful about selecting crucial information,  
15 because this stuff, we know in the franchise area that the  
16 documents are not read. And you're stepping -- and I don't want  
17 to demean, but the people who are getting these documents that  
18 they're probably less sophisticated than franchisees. And the  
19 likelihood that they would read a 20-page disclosure document is  
20 very low. So if you could get it down to a two, three, four-  
21 page document, I think that would be great. That would be  
22 perfect.

23          MS. HOWARD: I think that is exactly what we're trying  
24 to get at here. I mean, we certainly don't want to exclude  
25 anything that people think is absolutely crucial. And likewise,

1 we don't want to include things that are absolutely, you know,  
2 unnecessary or just only marginally helpful.

3 MR. WIECZOREK: Well, in the Franchise Rule, if you  
4 look at some disclosure documents, you have personnel lists that  
5 will go on for five, six, eight pages. Some of the large fast  
6 food companies have 100 people in Item 2. So, I mean, maybe if  
7 you wanted to compromise somewhere, you could pick out the  
8 president or the chairman or the CEO and make that person be the  
9 person that's listed in here. But I don't view this as  
10 absolutely crucial.

11 MS. HOWARD: Okay. Well, one of my questions also is  
12 kind of a follow-up to this and it sort of touches on the point  
13 that you just brought up. In our experience we have seen that  
14 in certain biz ops the actual principals will keep their names  
15 out of things. So, in fact, they can have someone who's the  
16 president of the company that really has nothing to do with  
17 running the company.

18 MR. WIECZOREK: Well, you can handle that differently.  
19 I think David started down this path. And that is, you may list  
20 the chairman or the CEO but is there any other officer, director  
21 or principal shareholder that has litigation history or  
22 bankruptcy history. And if so, list them. If not, don't put  
23 them in.

24 MS. HOWARD: Perhaps someone with management  
25 responsibility?

1 MR. WIECZOREK: Something like that.

2 MR. D'ALESSANDRO: That's a good point. You want to  
3 know who the shareholders are other than the officers.

4 MR. SOKOL: I think what you're hinting at though is  
5 one of the issues that isn't there in terms of business  
6 opportunities that are coming across our desks right now, is  
7 that certain individuals are appearing in the disclosure  
8 documents of one company as the president of this company,  
9 appearing in for another company as a regional sales manager and  
10 yet a third as a secretary or treasurer. And, I mean, granted  
11 this might be just a small percentage of business opportunity  
12 sellers out there, but they are out there jumping from one  
13 company to another, and they're almost interchangeable because  
14 the formula for that business opportunity is almost -- it's part  
15 of a set formula. They're just really, they're trading names  
16 and they're trading companies, depending on what state they're  
17 dealing with or who they've had a past history with.

18 MS. HOWARD: Okay. All right. How about the business  
19 experience of the actual company and the parent company? The  
20 length of time in business, length of time they've sold that biz  
21 op, things like that? Is that crucial, not crucial or somewhere  
22 in between?

23 MR. D'ALESSANDRO: I think it is.

24 MS. HOWARD: John?

25 MR. D'ALESSANDRO: I think it is.

1 MS. HOWARD: You think that's crucial? Dennis?

2 MR. WIECZOREK: Yeah.

3 MS. HOWARD: General agreement. Adam?

4 MR. SOKOL: I mean, I sort of think it's a gray area in  
5 that some of these companies they're set up as corporations for  
6 one purpose maybe a couple of years ago and then a certain  
7 opportunity they've started to sell they put in under this  
8 umbrella corporation. But, I mean, it's really the individuals  
9 that, you know, have set this up, and it's not part of any  
10 corporate scheme because as soon as this business opportunity or  
11 selling dries up, they're going to throw in another. So, I'm  
12 just not sure how relevant the corporation, you know, I'd like  
13 to know something about the corporation, but I still want to  
14 focus on the individuals running the corporation.

15 MS. HOWARD: So the corporate form perhaps isn't as  
16 important as who's behind it?

17 MR. SOKOL: Right. I mean, obviously I want some  
18 information still.

19 MS. HOWARD: Okay. All right. We touched on this  
20 already, but litigation history? Is that important, crucial?  
21 Assuming people will actually --

22 MR. TOPOROFF: Tell the truth.

23 MS. HOWARD: Tell the truth.

24 MR. WIECZOREK: Well, it depends on the litigation that  
25 you're covering. I think the breadth, I'm looking at the model

1 act and the model act covers similar kinds of things as the  
2 Franchise Rule. And I don't know. Obviously, violation of  
3 business opportunity law, that's relevant. Securities laws,  
4 commodities law, franchise law, fraud, embezzlement, fraudulent  
5 conversion, restraint of trade, unfair deceptive practices,  
6 misappropriation of property or comparable allegations, is that  
7 necessary? I don't know. I think that may go too far. I know  
8 in the franchise area you cover everything that's material. It  
9 could be a personal injury suit for a billion dollars that would  
10 be included. You know, it should focus on the kinds of activity  
11 that would cause concern whether it's related to fraud or  
12 violations of business opportunities or something like that.

13 MS. HOWARD: Okay.

14 MR. TOPOROFF: What happens if it was limited to  
15 violations of consumer protection laws? I guess consumer  
16 protection laws read very broadly to cover, I suppose,  
17 securities, biz op, franchise?

18 MR. WIECZOREK: Well, you get into issues regarding,  
19 you know, advertising law violations. I'm not sure that that's  
20 necessarily relevant. I mean, in general, I think I agree with  
21 you, but there are, you're going to capture some things that  
22 aren't necessarily important. Also, all criminal violations,  
23 felonies, you know, we consistently run into that problem in  
24 franchising where people have DUI's and whether that's relevant  
25 to a franchise offering. So, all criminal proceedings aren't

1 necessarily relevant either.

2           So, I think you should focus on business opportunity  
3 laws or perhaps consumer protection laws that have some relevant  
4 to the offering.

5           MS. HOWARD: Okay. Well, how about fraud? Should that  
6 be something that should definitely be disclosed? Litigation  
7 that involves fraud? I see some nods.

8           MR. WIECZOREK: I would say no.

9           MS. HOWARD: You would say no.

10           MR. WIECZOREK: I would say no, only because fraud is  
11 routinely alleged in just about every piece of civil litigation  
12 that you run into. And it could be between two large commercial  
13 organizations, you know, alleging that they lied when we entered  
14 into this distribution agreement. It's routinely, in  
15 franchising again, a franchisee who's smart will add fraud to  
16 the allegations in the complaint, whether there's fraud or not,  
17 so that you have to disclose it to make the company suffer, so  
18 to speak. So, I wouldn't automatically include fraud because  
19 there's just too much garden variety stuff that shouldn't be  
20 covered.

21           MR. FINNIGAN: I guess the answer is, I think it's  
22 crucial information. It's how to limit it because, just looking  
23 at the annual reports of companies, they all have, almost every  
24 one of them will have some sort of litigation history when you  
25 go through in the reports. They've got to figure out a way to,

1 I think you need to know the litigation history, but you've got  
2 to figure out a way to limit it to what is relevant. And I  
3 think that is what Dennis is talking about.

4 MR. SOKOL: What about litigation history with a law  
5 enforcement body concerning fraud?

6 MR. WIECZOREK: That would be preferable, absolutely.

7 MS. HOWARD: Okay. Can you clarify that, Adam?

8 MR. SOKOL: Well, has any individual or has this  
9 company been the target of any law enforcement action alleging  
10 fraud, as opposed to Dennis' example, instead of sued by private  
11 litigants.

12 MR. WIECZOREK: In securities, if a public company's  
13 stock goes down by a significant percentage, they will get sued.  
14 And fraud will be alleged and securities law violations will be  
15 alleged. Every public company is sued, you know, at one time or  
16 another, for that.

17 MS. HOWARD: How about disclosing cases brought by  
18 former or current biz op purchasers? Do you have a similar  
19 problem with that or do you think that that would be crucial?

20 MR. WIECZOREK: Well, it depends on the nature of the  
21 allegations. If it's a breach of contract claim, I don't  
22 necessarily think that that should be put in, unless it's  
23 somehow material, otherwise material in terms of amount or  
24 whatever. But if a biz op buyer says that they didn't provide  
25 the pizza oven to me on the day that they were supposed to and



1 they breached their contract, I don't think that's important  
2 enough disclosure to go in here.

3 MR. TOPOROFF: What happens if there were three dozen  
4 people who have the exact same allegation?

5 MR. WIECZOREK: Unless it becomes material as a  
6 financial matter, I don't view it as a disclosable event.

7 MR. TOPOROFF: Anybody have any thoughts on that?

8 MR. FINNIGAN: I think that if there's material  
9 litigation involving business opportunities and there are  
10 similar lawsuits, that probably should be disclosed. Whether  
11 it's this actual business opportunity or maybe another one that  
12 was operating by the same persons. I do understand Dennis'  
13 concern because of our society. And again, we have to go back  
14 to any company that you can think of. You know, a Fortune 500  
15 company, they've got some sort of litigation history. So the  
16 thing is a crafty one. But I think the law enforcement fraud  
17 and prior litigation history, no matter what it is, involving  
18 business opportunities is relevant.

19 MR. TOPOROFF: John, are you defending anyone?

20 MR. D'ALESSANDRO: No.

21 MS. HOWARD: Okay. How about whether or not the  
22 company or individuals are subject to current state or federal  
23 injunctions? Crucial? I see some nods yes. Any disagreement?

24 Okay. Now, we're getting back to one that I think John  
25 mentioned. Whether or not directors or executives have filed

1 for bankruptcy within X amount of years previous to that. You  
2 think that's crucial?

3 MR. D'ALESSANDRO: Yes.

4 MS. HOWARD: Okay. Anyone disagree? All right. How  
5 about a factual description of the business opportunity? You  
6 think that needs to appear in a disclosure document? David,  
7 you're sort of shaking your head.

8 MR. FINNIGAN: No. I think if they don't know what  
9 they're buying. I think if there's one thing that the companies  
10 are using pretty good is giving some sort of description about  
11 what it is their selling and in the interest of keeping these  
12 things as short as possible, I think that the advantages of  
13 including it is not weighed by the disadvantage of a longer  
14 document.

15 MS. HOWARD: Okay. People agree with that?

16 MR. D'ALESSANDRO: Yes.

17 MS. HOWARD: Yes. All right. How about the total  
18 amount of money that has to be paid in order to commence  
19 operations? So if there's a set price, that has to be  
20 disclosed. Or if there are various levels that you can enter  
21 in, those need to be disclosed. Adam?

22 MR. SOKOL: There definitely should be some financial  
23 variable. There's no doubt about it. I mean, obviously those  
24 numbers can be played with, but I would like to see something  
25 put down as to what --

1 MS. HOWARD: Okay. Crucial information? Okay. And  
2 how about whether or not any or all of those fees are refundable  
3 and what that policy would involve? Yes, not really? Adam,  
4 what do you think?

5 MR. SOKOL: Well, again, I mean, there should be some  
6 sort of refund policy statement. But to what extent, I really  
7 can't offer.

8 MS. HOWARD: Okay. Is this a between item, maybe not  
9 crucial, important, yes?

10 MR. D'ALESSANDRO: In between.

11 MS. HOWARD: Not even important?

12 MR. D'ALESSANDRO: I'd say in between.

13 MS. HOWARD: In between. All right. How about whether  
14 or not there are recurring funds and, if so, what they are and  
15 what they involve?

16 MR. FINNIGAN: I'm sorry. What was that?

17 MS. HOWARD: Whether or not there are recurring funds  
18 that have to be paid.

19 MR. SOKOL: Recurring costs.

20 MS. HOWARD: Recurring costs.

21 MR. FINNIGAN: Yeah. I mean, that's important and, in  
22 effect, what it kind of leads up to is, and maybe this is one of  
23 the things within that list there. Is, there needs to be a  
24 disclosure of other fees or expenses that are not necessarily  
25 covered by the company or by the initial purchase. An example I

1 could come up with is in the nature of pay phones. When a  
2 person purchases the pay phones, and we've had this case, they  
3 purchase the pay phones and then they get a location service  
4 that goes with it, what they don't realize is that there's three  
5 major costs that's not disclosed to them. One is that it's a  
6 regulated activity so they have to go through, I guess, you're  
7 familiar with it. One is that they don't realize that they have  
8 to get approval and they get a license.

9           Secondly, they don't realize that there's hook-up  
10 charges from the phone company. And third, there might be a  
11 line charge to put in a line there. So, there needs to be, if  
12 there isn't already a rule like that, there needs to be a  
13 disclosure to them about other fees that are not necessarily  
14 covered in this purchase of this business opportunity that might  
15 occur from said parties.

16           MS. HOWARD: Okay. People think that's crucial?

17           MR. SANSON: Yes.

18           MS. HOWARD: Dennis?

19           MR. WIECZOREK: Yes.

20           MS. HOWARD: Okay. How about restrictions on sources  
21 of products or services? Whether or not --

22           MR. TOPOROFF: Is that an issue at all that's relevant?  
23 The answer is yes.

24           MS. HOWARD: Is that really more of a franchise issue?

25           MR. WIECZOREK: Yes.

1 MS. HOWARD: Okay. And similarly, the names of  
2 affiliates that you'd be required to purchase from. Is that  
3 more a franchise issue?

4 MR. WIECZOREK: Yes.

5 MS. HOWARD: All right. And this is sort of related to  
6 the recurring fees that would have to be paid. These are  
7 services or supplies, products that you would be required to  
8 purchase or lease similar to that? Yes.

9 MR. D'ALESSANDRO: Why would -- you're doing business  
10 with them, you know what products you're going to be buying.

11 MR. SANSON: Did you say services to?

12 MS. HOWARD: Right. Or supplies or things that you're  
13 required to buy, not just up front, but throughout the process.

14 MR. D'ALESSANDRO: I think that would go along with  
15 what you know of the business you're buying into. You're really  
16 not buying it. You're buying a right.

17 MR. SANSON: I guess it would go along with additional  
18 training? Is that what your services are referring to?

19 MS. HOWARD: Something like that.

20 MR. D'ALESSANDRO: I think it's part of a franchise  
21 issue.

22 MR. SANSON: I would say yes, because we've seen some  
23 additional training that once people buy it, they find out I  
24 don't know how to operate this. And well, do you want this  
25 training? It's another \$1,000. So services means training

1 obviously, yes.

2 MS. HOWARD: Anyone else have a comment about that?

3 MR. WIECZOREK: Well, I mean, if you think of the  
4 beginning of the disclosure document and you say that this  
5 business opportunity involves the sale of pay telephones and you  
6 are required to buy your pay telephones from us, I mean, if  
7 that's all the disclosure is, fine. I mean, that's not a  
8 problem. That's not going to take up a lot of space. I think  
9 there probably is some relevance to the buyer knowing that he  
10 must buy certain things from the seller. Again, these probably  
11 are so apparent and so, they know they're getting into this, but  
12 I can't imagine a sentence saying, this is the business you're  
13 in and you've got to buy certain things from us. I can't  
14 imagine that that's a big problem in terms of taking up a lot of  
15 space, and just sort of giving a general background on what's  
16 going on in this whole business opportunity.

17 MS. HOWARD: Okay. All right. How about material  
18 terms and conditions of financing arrangements? Number one, do  
19 we see financing arrangements in biz ops, or is that more a  
20 franchise situation?

21 MR. SANSON: I don't see too much.

22 MS. HOWARD: Okay.

23 MR. TOPOROFF: In direct selling, there's usually no  
24 financing arrangement, is there?

25 MR. ELLMAN: No.

1           MR. SANSON: We have a case called Capital Investments  
2 where they ask you to put down \$1,500 and pay a total of \$5,000.  
3 And then they charge you interest on the money that you loaned  
4 from them. So, that's kind of rare.

5           MS. HOWARD: Okay.

6           MR. TOPOROFF: As a general proposition, is financing  
7 an issue for biz op sales?

8           MR. SANSON: No.

9           MR. FINNIGAN: No.

10          MR. WIECZOREK: No.

11          MR. HOWARD: Okay. How about material facts about  
12 whether or not the biz op purchaser is limited in certain areas,  
13 such as what products they can sell? Is that not really a biz  
14 op issue?

15          MR. SANSON: I don't think so.

16          MS. HOWARD: How about their customers? How about  
17 geographic area?

18          MR. TOPOROFF: Exclusive location.

19          MS. HOWARD: Exclusive territory, exclusive areas?

20          MR. SANSON: I would --

21          MS. HOWARD: In short of someone thinking that that's  
22 crucial --

23          MR. FINNIGAN: No.

24          MS. HOWARD: You think that's really not. All right.

25          MR. TOPOROFF: Wait. Before we move on. I want to ask

1 Adam that. The issue that's up for grabs is whether a  
2 disclosure document should have a provision that discusses  
3 whether there is an exclusive territory? And again, we're  
4 talking about business opportunities, not franchises?

5 MR. SOKOL: Sure. The question is whether the  
6 disclosure document should say whether the purchaser's been  
7 promised?

8 MR. TOPOROFF: Right, exclusive territory.

9 MR. SOKOL: I guess I'm starting to be of the opinion  
10 that something like that, in which the purchaser is told  
11 something, I'd like to see it on paper, too.

12 MR. TOPOROFF: I think I'm concerned because I know in  
13 cases that we've got, part of the pitch was especially like  
14 vending and displays, there would be an exclusive territory.  
15 It's kind of what grabs people's attention right away.

16 MR. SOKOL: How are you distinguishing, or are you  
17 distinguishing between exclusive territory and limited territory  
18 in which three people are granted the right to sell in Chicago?

19 MR. TOPOROFF: Actually either one, either one. I  
20 think any provision that purports to give people certain right  
21 in terms of the territory, whether it's exclusive or limited,  
22 whatever, because I think it's part and parcel of the likelihood  
23 of their success. If somebody has an exclusive or limited  
24 territory, that may represent that there's a bigger market out  
25 there that you can grab, as opposed to if it's a free-for-all



1 and everybody and their next-door neighbor is able to sell, then  
2 it's by far less of an expectation of success.

3 So before we move on, I just want to mention again. Is  
4 either an exclusive or a limitation or any kind of right to a  
5 territory an issue that we should consider further?

6 MR. WIECZOREK: At most an affirmative or a negative.  
7 I don't think, if you look at a franchise disclosure document,  
8 the section on territory is usually fairly vague, nebulous, you  
9 know. You get a zip code. You get a county. It's just a page  
10 of semi-worthless language. So if you put in this disclosure  
11 document, yes, you get an exclusive territory or you don't, that  
12 would be fine. But I wouldn't go much beyond that, again  
13 looking for brevity, focusing on brevity here.

14 MR. TOPOROFF: John, do you have any thoughts on that?

15 MR. D'ALESSANDRO: I agree with Dennis.

16 MS. HOWARD: All right. How about a provision that  
17 specifies the purchaser of the biz op to participate a certain  
18 amount? Is that relevant at all in biz op, or is that really  
19 more a franchise issue? We have heads shaking no. Is it  
20 agreement that it's more of a franchise issue?

21 MR. TOPOROFF: Well, let's make the record clear.

22 MS. HOWARD: Make the record clear.

23 MR. TOPOROFF: That seems to be more a franchise issue  
24 than a biz op issue?

25 MR. SANSON: Yes.

1 MS. HOWARD: And other similar types of purchaser  
2 obligations, would those fall into the same category?

3 MR. SANSON: Yes. It's more a franchise.

4 MS. HOWARD: Okay. How about a statement disclosing  
5 the term or duration of an agreement, do biz ops generally have  
6 a term, David?

7 MR. FINNIGAN: No. Not that I've seen.

8 MS. HOWARD: Okay. Has anyone seen biz ops that  
9 specify a number of years or a period of time in which you can  
10 operate it? No?

11 MR. TOPOROFF: Is there any concept like that in direct  
12 selling?

13 MR. ELLMAN: As in income-earning opportunities  
14 contrasted with business opportunities? It really depends on  
15 the company. Some companies have agreements that last for a  
16 year. Some perhaps two and some are perhaps indefinite.

17 MR. TOPOROFF: John?

18 MR. BROWN: Speaking for Amway, I think this is  
19 reflective of industry practice. The contract is annual and  
20 it's automatically renewable by the distributor, unlike the  
21 concern that is in the franchise industry and related industries  
22 where someone may lose the opportunity, the valuable opportunity  
23 to sell, and the potential for the company to seek to put  
24 somebody else in that place. The marketing strategy of direct  
25 selling very typically is to find as many sellers as possible to

1 maximize the number of distributors marketing the goods and  
2 services, and therefore, we do quite the opposite of the concern  
3 you expressed.

4           When people don't renew, we try to go back to them and  
5 say, please renew.

6           MR. TOPOROFF: What does renewal mean?

7           MR. BROWN: Renewal simply means that they continue to  
8 be Amway distributors and can continue to order products and  
9 resell them. The reason we have a renewal process is that our  
10 roles of distributors would just continue to grow larger and  
11 larger and wouldn't reflect the fact that somebody has  
12 discontinued the business. It's their way of telling us without  
13 having to literally quit in order for us to know that they're no  
14 longer in the business. Renewal simply means filling out a  
15 piece of paper and saying, I renew.

16           MR. TOPOROFF: Are there any additional fees?

17           MR. BROWN: No.

18           MR. TOPOROFF: On renewal?

19           MR. BROWN: No.

20           MS. HOWARD: Is it a contract that is signed?

21           MR. BROWN: In effect, it's a renewal of the contract  
22 that they signed when they first became distributors.

23           MR. ELLMAN: In fact, Federal law requires to take  
24 advantage of direct seller status. Meaning --

25           MR. TOPOROFF: Are we talking tax law?

1           MR. ELLMAN: Yeah. We're talking about the tax law.  
2 To be a non-employee under the Internal Revenue Code, you have  
3 to be presented with a contract which says, you are going to be  
4 an independent contractor. But that is, you know, a portion of  
5 a larger contract which you have which you may have to sign.

6           MS. HOWARD: So perhaps instead of an item in a  
7 disclosure document discussing renewal, if a copy of the  
8 contract was included, would that suffice?

9           MR. ELLMAN: Well, let me interject something at this  
10 point. Because I've been operating for the last 20 minutes or  
11 so under the assumption that these would apply to companies that  
12 have crossed a threshold, which is set currently at \$500. If  
13 any of these had to apply to the direct selling industry, as I  
14 have mentioned earlier, it would be a significant burden on the  
15 companies as well as the sales people.

16           Assuming for the sake of argument that these did apply  
17 to us, and I would prefer not to assume that because --

18           MR. TOPOROFF: Well let's assume that.

19           MR. ELLMAN: Well, let's assume that this would be a  
20 significant disincentive to recruiting. And I'll give you one  
21 specific instance why. Let's say that a disclosure document has  
22 to be presented at the first face-to-face meeting. And let me  
23 provide a not so ridiculous, and in fact, quite probable  
24 scenario that John here is an Amway sales person and he and I  
25 have run into each other at a restaurant, a supermarket or what

1 have you. And we get into a discussion somehow to the effect  
2 that, yes, I hear you've recently become an Amway sales person.  
3 And John will say, yes, it's a great opportunity, you know. I'm  
4 pretty new at it, but I see some potential. Things are going  
5 pretty well. You should look into it.

6 And he starts to talk to me about the Amway  
7 opportunity. Now, if he's not carrying a three or five-page  
8 disclosure in his back pocket, then we have, you know,  
9 potentially triggered some violations of any kind of  
10 hypothetical federal regulation.

11 Not only that, if you're a direct seller and you give  
12 out these documents, let's assume for the sake of argument that  
13 the document applies to the company, it relates to the Amway or  
14 Mary Kay or Pampered Chef or Longaberger, whomever. The more  
15 official legal documents that you get, the less likely you're  
16 going to be involved in the business because you're not going to  
17 want to give this out every time you discuss the opportunity  
18 face to face. And you might be discouraged if you get some kind  
19 of legal document that says, here, the FTC requires me to give  
20 you this. Particularly if it even says, you know, consult  
21 counsel. Because if you consult counsel, as I indicated, if you  
22 meet with him or her for a half an hour, you've already eaten  
23 through your first quarter's profits.

24 But even more so, more burdensome, is if the sales  
25 person has to fill out one of these documents for his or her own

1 self. If he's got to list his or her own name and address,  
2 litigation, that sort of thing, because he is the one that is  
3 actually offering the opportunity, then that is going to be  
4 significantly more problematic than the scenario which I just  
5 mentioned.

6 MS. HOWARD: I appreciate your concerns. And maybe we  
7 can touch on those later. But right now, I'd like to see if we  
8 can just get through this list and on to bigger and better  
9 things.

10 MR. ELLMAN: Sure.

11 MS. HOWARD: So the question was, do we need an item  
12 within a document disclosing the amount of time in which the  
13 business opportunity is going to be valid for, or would it be  
14 sufficient to have a contract so that if, you know, the contract  
15 stated, this is for one year, that would be sufficient? Or is  
16 this not an issue with business ops?

17 MR. WIECZOREK: I think in general if the contract  
18 covers any of these issues, the contract should be attached and  
19 that should be enough, whether it's term, whether it's sourcing  
20 restrictions, whether it's any of those issues. Obviously, name  
21 and address and personal and litigation history, that's not  
22 going to be in the contract. But I think the disclosure  
23 document should try to focus on non-contractual issues. Factual  
24 data as opposed to resummation, regurgitation of the  
25 contract itself.

1           MR. FINNIGAN: Part of the disclosure document should  
2 be the contract so they've got that to look at. And if it's  
3 covered under the contract, then it doesn't need to be covered  
4 under the other disclosure document.

5           MS. HOWARD: Okay.

6           MR. TOPOROFF: So if the disclosure document was real  
7 short and covered those items that aren't reflected in the  
8 contract, and a copy of the contract, standard contract, is  
9 included, your general sense is that that would be sufficient?

10          MR. FINNIGAN: That's in fact how we do it under  
11 another Illinois statute, the Business Brokers Statute, which  
12 has a disclosure requirement. And that they can provide a  
13 disclosure statement and a copy of the contract. And if the  
14 contract covers everything that they're required to disclose,  
15 then all they need to do is put on a separate sheet of paper  
16 those things that are not in the contract which they're required  
17 to disclose.

18          MS. HOWARD: Do you see any downside to that or any  
19 potentials for companies to, you know, start handing out, you  
20 know, five-page contracts with all sorts of items in extremely  
21 fine print?

22          MR. FINNIGAN: I guess they could do that with a  
23 disclosure statement also. So, I guess, and I just guess you'd  
24 have to unfortunately have some sort of something that said that  
25 you can include a contract as long as it's, you know, it's

1 readable or a reasonable person can read it.

2 MR. WIECZOREK: Or to say in the disclosure document  
3 that there are five or six or ten areas that you should  
4 specifically check in the contract because they're important and  
5 other important issues. So direct the reader to go look at the  
6 contract in a certain area.

7 MS. HOWARD: So, this information would then either  
8 appear in the disclosure document or in the contract, whichever  
9 the biz op seller chose to do? That's a yes?

10 MR. FINNIGAN: Yes.

11 MR. WIECZOREK: Yes.

12 MS. HOWARD: Okay. So, I have a whole list here of  
13 items like, well, renewal conditions. That would be -- it seems  
14 like that might fall into a similar category of disclosing the  
15 term, number of years. Okay.

16 Are items such as conditions where the biz op seller  
17 can refuse to renew, is that relevant or is that a franchise  
18 issue?

19 MR. FINNIGAN: That seems to be a franchise issue.

20 MS. HOWARD: Okay. Conditions where the purchaser can  
21 terminate? I mean, is the whole concept of termination relevant  
22 to business opportunities?

23 MR. WIECZOREK: Well, it may be, but it's in the  
24 contract.

25 MS. HOWARD: Okay. All right. How about provisions of



1 any covenant not to compete? Is that relevant in this context?

2 MR. WIECZOREK: It's in the contract.

3 MS. HOWARD: In the contract.

4 MR. WIECZOREK: Yes.

5 MS. HOWARD: Agreed?

6 MR. TOPOROFF: Well, first of all, is it relevant?

7 MR. FINNIGAN: No.

8 MR. WIECZOREK: It's probably not relevant. I've never  
9 seen a non-compete in a biz op situation.

10 MS. HOWARD: Okay.

11 MR. TOPOROFF: Well, let me ask the direct sellers. Is  
12 there any covenants not to compete?

13 MR. ELLMAN: Some companies do and some companies  
14 don't. Some companies will say, and it varies from company to  
15 company, some companies will have a non-compete clause while  
16 you're selling for this other company. Some will be for while  
17 you're working and six months after or a year after you quit,  
18 for whatever you determine. It's really too broad to make an  
19 observation.

20 MS. HOWARD: Okay. Does that clause appear in their  
21 contract?

22 MR. ELLMAN: Sometimes it's in the contract. Most  
23 often I've seen it in, I'm trying to think. I'm trying to  
24 think. I have seen it in marketing plans and I've seen it in  
25 the contracts and sometimes it's in both.

1 MS. HOWARD: Okay. Yeah?

2 MR. BROWN: I would say more typically it can occur  
3 either way, as Eric pointed out. The practice tends to be that  
4 the person receives a contract which is frankly quite detailed,  
5 but you have to get everything in there. So, it incorporates by  
6 reference the marketing plan, which is a separate document. And  
7 within that document you'll have rules of conduct and other  
8 matters that are addressed. And typically, the question of  
9 whether the distributor is allowed to sell the goods of a  
10 competing company, for example. That would be included in  
11 there.

12 Frankly, whether they can quit one business and go to  
13 work in another, I don't ever recall seeing that, which is the  
14 more classic non-compete kind of clause, at least in the  
15 employment sense. But to the degree that's going to be  
16 addressed at all, it would be addressed in the marketing plan  
17 materials which are incorporated by reference into the  
18 distributor contract.

19 MR. TOPOROFF: Well, since you mentioned the marketing  
20 plan, should a disclosure document, in addition to including a  
21 copy of the contract, include a copy of any marketing plan?

22 MR. BROWN: Say that again?

23 MR. TOPOROFF: Should the disclosure document include  
24 not only a copy of the contract but also a copy of the marketing  
25 plan? It seems to me if there are significant terms and

1 conditions that are in some other document than the contract,  
2 then perhaps whatever the other document is, maybe it's a  
3 marketing plan, call it whatever you want, whether that should  
4 be included in the disclosure document as well?

5 MR. ELLMAN: Well, assuming for the moment that we  
6 would have, direct selling would have to comply --

7 MR. WIECZOREK: We should put something on the record.

8 MR. ELLMAN: That's right. It's a continuing  
9 objection. Considering for the moment that direct selling would  
10 have to comply, I think it might be more appropriate to put  
11 disclosure documents inside a marketing plan because of the  
12 greater administrative efficiency and as a way to avoid the  
13 burden being placed on the industry.

14 MR. TOPOROFF: But on the precise question, should all  
15 relevant documents be disclosed, however it's disclosed, whether  
16 one is attached to the disclosure document or the disclosure  
17 document is incorporated into another piece of paper, just  
18 conceptually, should there be disclosure of all the relevant  
19 documents that set out terms and conditions?

20 MR. ELLMAN: Well, it might be easier to say that in  
21 the disclosure document that there are other documents to which  
22 you need to refer to gain the material aspects of the plan. I  
23 don't know if giving anybody a large pile of papers the size of  
24 the Brooklyn yellow pages at one time is going to allay any of  
25 the concerns that have been expressed, or that the more paper

1 you get, the less likely you are to read it, particularly if the  
2 first thing is a mandated document by the Federal Trade  
3 Commission that is encouched in some legal terminology.

4 MR. TOPOROFF: But are the marketing plans that you're  
5 referring to yellow pages? Or are we talking about a few pages?

6 MR. ELLMAN: It really depends on the company. The  
7 bigger, more mature companies will tend to have larger documents  
8 to go along with it. The bigger the product line, the more  
9 pieces of paper you're going to have that explain the various  
10 products and services that might be offered by the company.  
11 Newer, more start-up companies, they tend to have less products  
12 and because they're newer they tend to have less paperwork that  
13 goes to the client.

14 MR. TOPOROFF: Dennis?

15 MR. WIECZOREK: I disagree with including any of that  
16 material with the disclosure document. It's not a whole lot  
17 different than a franchisor with their operating manuals, which  
18 never hit the franchisee's desk until they sign the contract.  
19 And number one, it would be the Brooklyn phone book if you have  
20 to include it with the disclosure document.

21 Secondly, you're also probably revealing some degree of  
22 confidential information to people who may well be shopping.  
23 And I think it would be -- and number three, try to figure out  
24 what the marketing plan is and what documents encompass the  
25 marketing plan, you know, I can see company's ads, all of our

1 brochures, all of our -- and we've got to attach them to the  
2 disclosure statement. And I think that's a big mistake.

3 MR. TOPOROFF: What happens if the disclosure document  
4 had a catch-all provision that said, other contractual terms or  
5 contractual terms, see the attached copy of our contract. In  
6 addition to the terms and conditions set out in the contract, we  
7 also impose the following. And you could list them one, two,  
8 three. So that when you pick up the disclosure document with  
9 the contract, that one document taken as a whole, the investor  
10 will know all of the terms and conditions of the arrangement.

11 MR. WIECZOREK: If it's not a contract, it can't be  
12 enclosed. So, yes, if there are five contracts, there's one  
13 contract on doing this and another contract on doing that, they  
14 should all be attached. But if the business opportunity seller  
15 says, well, we have these other things that we suggest or we  
16 encourage, the buyer is not obligated to use that or is not  
17 obligated to observe those other documents.

18 MR. TOPOROFF: John?

19 MR. BROWN: The thing that I struggle with conceptually  
20 is that, in effect, when you talk about the marketing plan, it  
21 is the thing that is for sale. And to put it in a different  
22 context, certain disclosures were required to be made to a buyer  
23 of a car. It would be absurd to say, and included with the  
24 disclosures you must also provide the car, because that, after  
25 all, is what you're buying. And how can you get full disclosure

1 unless you give the person the car. Well, but, wait a minute.  
2 Disclosures are one thing. The car is something else. That is  
3 the thing that's being purchased. And, you know, your point  
4 about proprietary information is not necessarily relevant to the  
5 direct seller because our material is so ubiquitous and we want  
6 everybody to become a direct seller, and so it's not strictly  
7 speaking proprietary, but it really is not something that  
8 someone is supposed to have unless they in fact become an Amway  
9 distributor.

10 So, the fact that there is a marketing plan is  
11 important information, but all the details, the rules of conduct  
12 and all of that stuff which, as far as we're concerned, is the  
13 Amway sales and marketing plan, that is our business reference  
14 manual and it's like a small catalog.

15 MR. TOPOROFF: Well, I think how we got to where we are  
16 right now is, if I'm not mistaken, Myra asked about renewal or  
17 terms and conditions affecting renewal. And it was suggested  
18 that some of that, some of those terms and conditions might not  
19 be in the contract but might be in a separate document known as  
20 the marketing plan.

21 I think our concern is, once we start splitting up  
22 terms and conditions and some are in the contract and some are  
23 in some other document, will the potential customer here lose  
24 out. If we say, because one possibility is, well, we'll have in  
25 the rule, you have to attach a contract. And what we might end

1 up seeing is contracts that are bare bones that have two  
2 provisions, and all the rest of the terms and conditions that  
3 might apply could be buried in some other ancillary document.  
4 So I think the key is, whether you call it a marketing plan or  
5 call it whatever you want, the key, I think, is when a consumer  
6 picks up the disclosure document, either in the text of the  
7 disclosure itself or in attachments to it, that they can learn  
8 and have access to knowing what the full terms and conditions  
9 that are going to apply.

10 MR. WIECZOREK: But you're still ignoring the issue of  
11 what's determined condition. If it's not obligatory, it's  
12 irrelevant. If they say -- if it is not in a contract, then the  
13 buyer is not obligated to perform, is not obliged. There is no  
14 basis for the seller to say, you must do X, Y and Z because it's  
15 over in this other brochure that we've got over there that we  
16 never gave to you. The buyer can say, good-bye, I'm not doing  
17 it, because I didn't sign anything that said I had to do it.

18 MR. FINNIGAN: I think the problem is is that clearly I  
19 think disclosure documents have to include the disclosure  
20 document and the contract. And if the contract says, you must  
21 comply with all the terms and conditions as listed in the  
22 marketing plan which is enclosed, which is incorporated by  
23 reference here.

24 MR. WIECZOREK: That's part of the contract then.

25 MR. FINNIGAN: And in that situation then I think they

1 have to provide that marketing plan. And I think that's how we  
2 got here, is that they have to provide, you know, the disclosure  
3 statement and the contract. And if the contract refers to other  
4 documents, you know, and are incorporated by reference within  
5 that document, they have to provide that, too, so that the  
6 consumer knows what they're getting. Or if they take it to  
7 their attorney or some other professional to review it, that  
8 they've got that.

9 MR. WIECZOREK: The only negative with that is in  
10 franchising, all franchise agreements say, you must also comply  
11 with our operating manuals. And operating manuals in the case  
12 of a McDonald's would fill, you know, half of this table. And  
13 to then say that that needs to be disclosed, it's not going to  
14 happen. And number two, it will certainly never get read. So I  
15 don't know where you draw the line in terms of what needs to be  
16 disclosed.

17 MS. HOWARD: How about in the biz op context though,  
18 does that sound like a workable idea, what David suggested?  
19 John, you're shaking your head.

20 MR. D'ALESSANDRO: I don't think so.

21 MS. HOWARD: Why not?

22 MR. D'ALESSANDRO: Because, as Dennis said, it's going  
23 to be too much. It's irrelevant for these people who are  
24 entering into this agreement. So, it isn't going to make any  
25 difference.



1           MR. FINNIGAN: But if it's irrelevant, then why are  
2 they being made to comply with it by the company? If it's that  
3 irrelevant to them, then they shouldn't have to comply with it.  
4 I guess I should be glad about it.

5           MR. D'ALESSANDRO: It is not irrelevant, but the  
6 individuals entering into that agreement, it's irrelevant to  
7 him.

8           MR. WIECZOREK: What I would suggest, maybe again, this  
9 is cutting it down the middle a little bit, is if there is such  
10 a thing, the contract says, you must observe the terms and  
11 conditions of our operating manual, then instead of attaching as  
12 a copy, you say in the disclosure document, in addition to the  
13 contract that's attached to this, one of you said this earlier,  
14 you must also comply with our operating manual, and you should  
15 review that before you sign, or something like that. Maybe that  
16 would be better. You don't have to attach the whole damn thing  
17 to the disclosure.

18           MS. HOWARD: Okay. What do you think about that, John?

19           MR. BROWN: Well, again, you know, this is why Amway is  
20 so happy that it's not a business opportunity. There is a  
21 fellow associate with a major franchise who once gave a talk on  
22 the disclosure documents and what's necessary, and I appreciated  
23 what he said because, you know, the bottom line is, there is  
24 only so much that anyone can do for two parties in a  
25 negotiation. The bottom line is, those two parties have to

1 handle it and decide what they can tolerate themselves. As this  
2 fellow put it, look, there's no question about it, then when  
3 we're dealing with a franchisee, we're saying, you have to trust  
4 us. Of course, this happened to be a franchise. That's just  
5 the very best in the world. And so, his fundamental point was,  
6 there's a critical mass of information that you have to have in  
7 order to make a sound judgment, but as for, you know, operating  
8 manuals and so on, if the franchisee or the business opportunity  
9 offeree is not comfortable without this material, what they view  
10 as material information, if they're that not comfortable signing  
11 the deal unless they see that and the position of the franchisor  
12 or the offeror of the business opportunity is, that's  
13 proprietary information. There are competitors who would give  
14 blood to see that. And I don't know what, if you think you're  
15 going to see that before you put, you know, money down on this  
16 deal, you know, snowball's chance that will ever happen, my  
17 friend.

18 Well, then they have no deal. They have no deal.  
19 What, realistically what we're worried about with business  
20 opportunities, and not exempt business opportunities, what we're  
21 worried about is, you know, these typically are not negotiated  
22 deals. They're prepackaged programs. Here's what you get for  
23 your money, and the disclosure, I always understood, you know,  
24 what it was supposed to do. And again, we talked earlier in the  
25 day about the reality of it, is that it tends only to apply to

1 people who are ignoring it and that's how we, you know, stop  
2 them from doing what they do. But, it ideally is supposed to  
3 tell you something about the company, the organization, the  
4 people that simply isn't part of the contractual arrangement at  
5 all. It's additional information so you know who it is you're  
6 dealing with.

7           It's your own responsibility to understand what deal  
8 you're striking. That's in the contract. But with regard to  
9 additional disclosures, that's stuff that really isn't, strictly  
10 speaking, part of the deal. It's things you ought to know about  
11 the person you're dealing with before you enter into a deal with  
12 them. They may be undercapitalized. They may have criminal  
13 records and rap sheets a mile long. They may have had failed  
14 businesses in the past that were just like this one. You know,  
15 those are all the things that are disclosure information that I  
16 think the biz op laws drive at and, you know, but in terms of  
17 the contract itself and the deal that's drawn, that's between  
18 the parties.

19           MS. HOWARD: So, are you saying that you don't think  
20 that a disclosure document should include a contract?

21           MR. BROWN: The contract is something you should  
22 receive when you enter into a deal. And you can mandate that  
23 there be a written contract, but that is separate from the  
24 disclosure document which has other information. In other  
25 words, if you're going to ask this person to sign this contract,

1 you shall disclose the following. And it's additional  
2 information that would not be included in the contract. No  
3 one's going to write in the contract, you know, here's our  
4 financial condition. No one's going to write in there, and by  
5 the way, the president of the company served eight years in the  
6 penitentiary for fraud. You know, all of those things are not  
7 going to ever appear in the contract. And so, those are  
8 disclosures which are separate from it.

9 Now, you know, if there's a standard contract, should  
10 it be included? I think anybody negotiating a deal ought to  
11 see, by its nature, they should read the contract and maybe the  
12 disclosure document should say, you know, be sure to read the  
13 contract and understand it. But again, you know, I go back to  
14 the automobile example. You know, is the automobile included as  
15 a disclosure? No. It's the thing that you're buying. And  
16 likewise, the contract is the thing that represents your deal.

17 MS. HOWARD: Okay. Well, let's sort of take a vote on  
18 this because I thought that we had, people had sort of agreed  
19 that it was important to include a contract with a disclosure  
20 document. Do people basically agree with that, or are there  
21 other people that agree with John, that that's really something  
22 that, you know, it's up to the buyer later on to take a look at  
23 it or at some point to take a look at? Dennis, what do you  
24 think?

25 MR. WIECZOREK: I would agree that the contract should

1 be attached.

2 MS. HOWARD: Okay.

3 MR. WIECZOREK: I think you have to do one or the  
4 other. Either you have to provide disclosure about the contract  
5 or you have to attach the contract.

6 MS. HOWARD: In other words, is this something that a  
7 prospective purchaser should really be able to take a look at  
8 ahead of time, along with those other pieces of information that  
9 John referred to that aren't going to appear in the contract?  
10 David?

11 MR. FINNIGAN: Yes.

12 MS. HOWARD: Okay. Eric?

13 MR. ELLMAN: I want to just say something about that.  
14 If you're talking about attaching the contract to the disclosure  
15 document, well, the prospective person has the option of either  
16 signing the contract or not signing the contract. And I don't  
17 know why that has to be given up front. I think it's something  
18 that can certainly come later.

19 MS. HOWARD: Okay. David, do you have a comment to  
20 that?

21 MR. FINNIGAN: I think it's just relevant that they, I  
22 mean, the purpose of disclosure is to give them all the  
23 information about what they're investing in and their rights and  
24 responsibilities plus other additional information. And I think  
25 that having the contract so that they can review it and read

1 through it, you know, and within a ten day period, which is what  
2 we were setting up here, because that was reasonable. I guess  
3 the question is, how much additional information. I can  
4 understand the concerns about the operating manuals and  
5 marketing plans, but I think that if there's important material  
6 terms that are referred to in other documents and incorporated  
7 by reference within the contract, then they need to have some  
8 sort of opportunity to review those.

9 MS. HOWARD: All right. Is it fair to say that we  
10 don't have agreement on this issue? That some people really  
11 think that a contract does not have to be included with the  
12 disclosure document. Others feel that it really should be. Is  
13 that a fair assessment of where we are? Okay. We'll take that  
14 one down and move on.

15 How about statements disclosing the total number of  
16 purchasers that are operating at any particular point in time,  
17 say the last fiscal year? Or the total number of company-owned  
18 outlets. Maybe we can eliminate some of these or get a few of  
19 these out of the way quickly. Are company-owned outlets  
20 relevant in biz ops?

21 MR. WIECZOREK: No.

22 MS. HOWARD: Agreement with that? Not relevant here?  
23 Okay.

24 Well then, how about the number of purchasers, say for  
25 the last fiscal year?

1           MR. TOPOROFF: Myra, are you asking specifically the  
2 number or are you including in that the names and addresses?

3           MS. HOWARD: No. Those are going to be two separate  
4 issues. The first is the number of purchasers. So, for  
5 instance, we, you know, I think fairly commonly, at least in  
6 complaints that we've received from people, you know, we hear  
7 that, well, they told us there were, you know, 250 purchasers or  
8 5,000 purchasers last year. Should that be something that's  
9 disclosed in a document? Is that relevant? Is it essential?  
10 Or is it somewhere in between?

11           MR. ELLMAN: In a direct selling context, I think it  
12 has the potential to be harmful, because let's take the example  
13 of a new start-up direct selling company. And in their previous  
14 fiscal year, which was their first fiscal year, they've had, I  
15 don't know, a hundred direct sellers in their company. And  
16 you're looking at a document which says, well, somebody's got to  
17 be wrong with this plan if they've only got a hundred people out  
18 of 250 million in the whole country purchasing it. I think that  
19 has the potential of being harmful. And I think there's other  
20 legitimate businesses that would find that same situation as  
21 well.

22           MR. TOPOROFF: Would it be harmful if there also was  
23 disclosure of how long the company has been in business, so that  
24 somebody could look see item one, item two, company has been in  
25 business for six months?

1           MR. ELLMAN: Well, I don't know what the relevance  
2 would be about whether it matters how long it was in business.

3           MR. TOPOROFF: Well, I'm saying, like a hundred in and  
4 of itself doesn't necessarily mean anything.

5           MS. HOWARD: But taken in a context, in other words,  
6 your example, the company just started up last year, you know.  
7 And you look and see a hundred, oh, okay, they just started up  
8 last year. But if the company has been in business for ten  
9 years and you see that there's a hundred purchasers the previous  
10 year, maybe that would have a different impact.

11           MR. ELLMAN: Well, I don't know. You know, there might  
12 be some companies that have, that sell a high ticket product  
13 which not a lot of people buy. And let's take, well, I don't  
14 want to mention any business specifics, but let's say that a  
15 company has a specific high ticket product which is not going to  
16 attract as many purchasers and the company's been in business  
17 for 30 or 40 years and does not have what some people might  
18 perceive as a lot of direct sellers. And that could have a  
19 negative impact on whether or not somebody's going to sign up  
20 for this company.

21           MS. HOWARD: Right. So is this sort of a crucial piece  
22 of information or sort of relevant but not essential?

23           MR. TOPOROFF: Well, I have a question.

24           MS. HOWARD: Okay.

25           MR. TOPOROFF: Are we looking, or is the question



1 that's on the floor the raw number of how many outlets are open  
2 in a given time or does it also include the numbers that have  
3 failed?

4 MS. HOWARD: Well, I think what we've been talking  
5 about is actually how many were operating, say, in the previous  
6 fiscal year as opposed to how many have operated at some point  
7 and how many are now operating. I think we'll get into how many  
8 have failed shortly. But at this point it's simply a question  
9 of how many current biz op purchasers are out there selling,  
10 say, for the last fiscal year. Is it relevant or is it just  
11 maybe relevant?

12 MR. WIECZOREK: It seems kind of important.

13 MS. HOWARD: Kind of important. Okay.

14 MR. WIECZOREK: Seems important. Let's put it that  
15 way, yes.

16 MS. HOWARD: All right. Do we have any agreement?  
17 John?

18 MR. BROWN: Well, just from a practical perspective,  
19 you know, Amway Corporation makes a lot of noise about how long  
20 it's been around and that is for us a selling point for people  
21 looking for an income-earning opportunity. So, from a  
22 competitive perspective, it's important. Again, speaking about  
23 a subject that is not of direct concern to us, but when you're  
24 talking about biz ops, I would think that it would be important  
25 for someone to know how long a company has been offering

1 opportunities and if they've been around for a long time, that  
2 would be valuable information in terms of disclosure.

3 In terms of the number of people that are out there,  
4 again, that varies. Business opportunities are not all the  
5 same. Amway considers that to be, you know, a very sensitive  
6 competitive issue. And as an income-earning opportunity  
7 offeror, other business opportunities might not be quite so  
8 concerned about it. So that, to me, is all over the map.

9 MS. HOWARD: Okay. Adam?

10 MR. SOKOL: I don't know if this is a practical  
11 combination of Mr. Brown's point and the amount of people out  
12 there or not, but it seems to me, first, from my experience,  
13 there are a lot of business opportunities out there that have  
14 only been available for a year or less. And the number 100,  
15 which Eric threw out, could mean a lot of different things. A  
16 company that's been offering this opportunity only for three  
17 months that has 100 opportunities out there already, they may  
18 well be selling to anybody who walks into the door. And they  
19 don't know, we don't know how that system will hold up.

20 I'm wondering if there is, as part of the disclosure,  
21 XYZ Corporation has 100 distributors, has sold 100 business  
22 opportunities, you know, slash 65 have been operating since  
23 1995, or something like that. My colleague points out also  
24 that, you know, what kind of disclosure is there for, you know,  
25 this is a new untested business opportunity. It's been in

1 existence for less than one year. I think that needs to be  
2 disclosed to some extent.

3 MS. HOWARD: Okay. Is it safe to say we have some  
4 disagreement on this issue? All right. Yes?

5 MR. BROWN: Just to make a point. Again, you know,  
6 it's easy for Amway Corporation. It's easy for representatives  
7 of the direct selling industry to idly make comment with regard  
8 to certain disclosures that have to be made when we, you know,  
9 earnestly would wish to ever have to avoid making that. And I  
10 say all of this, again, for a reason, and that is, you know, we  
11 don't have anyone who is in the biz op business, strictly  
12 speaking, in the biz op business here, and I would have to  
13 wonder, you know, what their reaction would be to being forced  
14 to divulge precisely how many biz ops they've sold or, you know,  
15 things that they would consider of strategic competitive  
16 interest. And I don't speak for them.

17 MS. HOWARD: Well, you know, unfortunately, you're  
18 right. They're not here. And they were certainly all invited.

19 MR. BROWN: Whoever they are.

20 MS. HOWARD: Whoever they are. Wherever they might be.  
21 They were invited along with the rest of you.

22 MR. TOPOROFF: Not only that, the current rule does  
23 require those disclosures. So it should not come as any shock  
24 to biz op sellers that all of a sudden there's this requirement.  
25 If anything, the presumption is that the Commission has a rule

1 that's based upon a record and it should continue as is unless  
2 there's a record or evidence to suggest otherwise. So, John?

3 MR. BROWN: How about virtual absence of business  
4 opportunities as a matter of record?

5 MR. TOPOROFF: What, here?

6 MR. BROWN: Here, and, I think, the discussion has  
7 been, there are precious few registrations. Now, is that simply  
8 because that whole area simply has no purpose to exist other  
9 than to engage in fraud or is it because regulation exists at  
10 the Federal level and at the state level which is so Draconian  
11 that no one can survive it.

12 MR. TOPOROFF: Well, I think that there are three  
13 possible conclusions one can draw from the absence of what we  
14 would consider rank and file biz ops from this event. One is,  
15 that they genuinely may not know that there's the Federal  
16 Register announcement and what the Commission is doing. I find  
17 that a little hard to believe because this has been picked up in  
18 the trade press. Attorneys who represent biz op sellers, I  
19 would imagine, represent some franchise systems,  
20 distributorships or whatever. And I think that they can get  
21 that information. Although, I don't know that for a fact.

22 Another possibility is that they've read the ANPR and  
23 agree with it and there's nothing to comment. They see where  
24 the Commission is going and it suits them fine for their  
25 industry and, because if they didn't, they would be here.

1           The third one is that they could not care less. That  
2 either because they are scams or frauds or they just think that  
3 the states or the Federal Trade Commission are not going to get  
4 them. That if they get fined or caught, it's just the price of  
5 doing business and this isn't a big deal.

6           Now, I'm not prepared to draw any of those conclusions.  
7 I just offer them as possibilities. But, the fact is that we  
8 are having these workshops. We are more than happy or welcome  
9 the thought that certainly direct sellers are here, that it is  
10 open to the public, and anybody could participate. And we have  
11 a job to do and we're going to do it. This isn't the end of the  
12 story. After the conclusion of the comment period in these  
13 workshops, we'll go back to our offices and draft something,  
14 recommendations for the Commission, and the Commission will  
15 publish those in the Federal Register as proposed rules.

16           So, there will be many more opportunities for people to  
17 comment as well. It is our hope that people would help us out  
18 and comment and give us their thoughts early in the process to  
19 avoid controversy and wrinkles down the road. But, you know, we  
20 take participants as they come. So, on that one I don't know  
21 that there's that much more to say other than we have some state  
22 regulators who are involved in the issue. We have people who,  
23 whether they're covered by the Rule or not, or at least business  
24 folks who are close to the core issues, and hopefully we'll get  
25 feedback.

1           Where were we?

2           MS. HOWARD: Well, we were trying to move along here  
3 from -- so, let's see if we can do that.

4           How about the issue of listing names, addresses and  
5 phone numbers of X number of purchasers of the biz op?

6           MR. TOPOROFF: Current and former.

7           MS. HOWARD: Current and/or former. Is this relevant  
8 in the sale of biz ops? Is this crucial information? Does this  
9 sort of protect prospective biz op purchasers from the problem  
10 of being given shill references later on down the line?

11          MR. TOPOROFF: Let me ask David and Phil, in your  
12 disclosure law, are there requirements that the biz op seller  
13 give out that kind of information, names and addresses of  
14 purchasers?

15          MR. SANSON: It asks for names and addresses of  
16 purchasers who have requested refunds.

17          MR. TOPOROFF: That requested refunds. That's  
18 interesting. How do you find that that works?

19          MR. SANSON: Well, it seemed to cover it. If there's a  
20 lot of requested refunds, they are implied to a potential  
21 purchaser to possibly call that person or the company to find  
22 out. I haven't heard too many complaints from that provision.

23          MR. TOPOROFF: Adam, do you have any thoughts on that,  
24 on the list of current owners is limited to only those that  
25 requested refunds?

1           MR. SOKOL: As I stated before, we have had complaints  
2 regarding shills. It's certainly an interesting issue. I can't  
3 give an intelligent answer one way or the other, but it's  
4 certainly an interesting issue. I think it needs to be explored  
5 further.

6           MS. HOWARD: Is there agreement on that?

7           MR. FINNIGAN: I guess those two issues, the witnesses  
8 and then, not the witnesses, the purchasers and the number of  
9 biz ops that have been sold are relevant. Again, I think what  
10 we're starting to deal with is, again, is it, with the number of  
11 purchasers, that's a hard one to figure out, to put in a  
12 relative context, as has been brought up here. And as to the  
13 number of purchasers, you use the number X. I mean, is there  
14 some sort of number of purchasers that they have to list? You  
15 said X purchasers. Does the Rule, as it is currently written,  
16 state the number of purchasers and addresses they're supposed to  
17 give?

18           MS. HOWARD: Well --

19           MR. TOPOROFF: At least ten.

20           MR. FINNIGAN: At least ten?

21           MR. TOPOROFF: And in the UFOC, it would be 100. Well,  
22 let me ask this. The reason in part that the names and  
23 addresses, telephone numbers, is included in a UFOC or a  
24 franchise disclosure document is that the Commission believes  
25 that, let me restate that.

1           One way for potential investors to check up on what the  
2           company is offering and how well it is doing and whether they  
3           keep their promises, an independent source of information, if  
4           you will, or at least another source of information, is to go to  
5           the people who directly bought these things and see how they're  
6           faring. So you don't have to necessarily rely on the franchisor  
7           and franchisor sales person. Does the same concept hold true in  
8           business opportunities? It would seem to me that even more so  
9           where business opportunities do not have, to the same extent  
10          that franchises do, a nationally recognized trade name and  
11          presence where the average person might know, just through their  
12          general experience, how well or not a system is doing. Biz ops,  
13          which come and go, you don't necessarily have name recognition  
14          and there's a lot of trust that's put in the representations  
15          made by the seller. Even more so shouldn't there be disclosures  
16          of the people who have actually bought these things so that  
17          potential investors can go out and see for themselves or check  
18          up whether this is a good opportunity?

19                 MR. FINNIGAN: It would certainly be more useful also,  
20                 of course, this would be kind of difficult to do, but it would  
21                 be more useful if the purchasers that are disclosed are the ones  
22                 in the same state or where they're located it, but that may be a  
23                 little bit too oneristic to require.

24                 MR. TOPOROFF: That's actually what our rule requires.

25                 MR. FINNIGAN: Oh, is it?



1           MR. TOPOROFF: We start with the premise that the names  
2 and addresses have to be disclosed in that state. And if not in  
3 that state, in the surrounding state and then you go broad. So  
4 the hope is, yes, because sometimes it could be, there could be  
5 reasonable differences.

6           MR. FINNIGAN: How does the Commission deal with the  
7 privacy issue for these purchasers? What if the company  
8 legitimately or illegitimately makes the argument that, you  
9 know, that privacy is a big issue with their purchasers and they  
10 don't want to have their names disclosed?

11          MR. TOPOROFF: It hasn't come up. It hasn't come up.  
12 And I was not around during the original rule-making, so I  
13 couldn't tell you whether that was an issue or not. In all the  
14 cases that we have brought and dealing with various defendants,  
15 I don't know that that issue was ever raised.

16          MR. FINNIGAN: So no one's ever brought up the we can't  
17 find anybody who wants to disclose their name defense?

18          MR. TOPOROFF: It's an obligation that they have to  
19 disclose. And I assume that if somebody purchases a business  
20 opportunity or a franchise and they get the disclosure document,  
21 they're going to see that names and addresses are disclosed.  
22 So, I would imagine that they are at least on constructive  
23 notice that their names may be disclosed. It just hasn't come  
24 up. It hasn't come up.

25          MS. HOWARD: Okay. We will put that down as one to

1 explore further. All right. For instance, how about the number  
2 of voluntary terminations or non-renewals? We've sort of  
3 touched on this, but is that really more a franchise issue when  
4 we talk about terminations, non-renewals? Or is that even  
5 relevant in this area?

6 MR. D'ALESSANDRO: It is relevant.

7 MR. FINNIGAN: I don't think it's relevant.

8 MR. TOPOROFF: Well, is it relevant how many people  
9 left the system? So that a business opportunity seller may have  
10 sold 1,000 opportunities and, let's say, in 1995 and if you  
11 trace those people in 1996, you'll find, let's say, for example,  
12 that 50 percent have dropped out and maybe the next year, if you  
13 trace those people, you'll find out that another 45 percent have  
14 dropped out, and out of the original group in 1995, in 1997,  
15 there are only 5 percent remaining?

16 MR. FINNIGAN: Wouldn't that be covered under business  
17 failure, the disclosure?

18 MR. TOPOROFF: Right. I mean, I don't know that we  
19 necessarily need to be wedded to the precise list or definition  
20 that the Rule currently sets out. It's more conceptually,  
21 should there be disclosure of the number of people that have  
22 come or gone in the system.

23 MR. FINNIGAN: In a context of failures, I think that  
24 is relevant, and a crucial piece of information to know, what is  
25 the success rate of this business opportunity.

1 MS. HOWARD: Is there agreement on that? John?

2 MR. BROWN: From the perspective of direct sellers,  
3 again, I don't know how the world of biz ops would, that's  
4 different, would view this, but in the direct selling industry,  
5 Amway Corporation would fight tooth and nail to not disclose the  
6 names of its distributors because that's, in effect, our  
7 customer list.

8 And I can tell you that if under any law it was  
9 required for a person to become a distributor they had to be  
10 given the names of all distributors, one, it would be an  
11 incredibly long list. But two, the first people to quickly  
12 indicate interest in becoming Amway distributors would be Nuskin  
13 distributors, who would then get that list and then go to those  
14 people and say, you don't want to do that. You want to do  
15 Nuskin. It's, in fact, valuable competitive information.

16 And so, as a direct selling industry concern, and in  
17 terms of the dropout, we talk a lot about the fact that in the  
18 direct selling industry most people who become direct sellers,  
19 at the time they become direct sellers, don't know if that's  
20 what they want to do or not, but given the very low cost, ease  
21 of entry situation, they can try it out, and if they don't like  
22 it, you know, they give their kit back and they're out of it.

23 Thus, it's not a problem in our industry in the sense  
24 of causing people any harm. But on the other hand, a dropout  
25 rate would cast a very negative light, which we would view to be

1 very unfair, given our success, and so, you know, from the  
2 direct seller perspective, we would not want to have to disclose  
3 that. But that's our unique perspective on the issue.

4 MS. HOWARD: Eric?

5 MR. ELLMAN: As I mentioned earlier, we have a very  
6 high turnover rate for a number of reasons. And in the direct  
7 selling context, giving some kind of information relating to  
8 turnovers is very misleading. First of all, it takes a certain  
9 kind of breed of person to become a direct seller. There's not  
10 a lot of people who are very good at it, who are willing to  
11 contact friends, neighbors, acquaintances and other people that  
12 they run into and try to sell them products and services. And  
13 people would try it for a very short period of time and dropped  
14 out because they realize they're not good at it or it's not for  
15 them or what have you.

16 Secondly, there's a lot of direct sellers who take  
17 advantage of direct selling because they find it to be a fairly  
18 seasonal business. For example, teachers, we have, there's a  
19 lot of direct sellers who happen to be teachers who sell only in  
20 the summertime and who might terminate or not renew at the end  
21 of every summer or fall, but appreciate the extra income that  
22 selling in the summertime provides. Other people might work in  
23 just the back half of the year to sell products and services to  
24 pay for holiday gifts for their friends or their family and  
25 might again quit in the springtime whenever the holiday season

1 ends.

2 So, I think that a dropout attrition situation  
3 disclosures for the direct selling industry is potentially very  
4 dangerous.

5 MS. HOWARD: Okay. Any other comments on this idea?  
6 All right. This is one we'll keep looking at. How about the  
7 concept of a listing of the business opportunity sellers'  
8 obligations. For instance, around the idea of training. I  
9 mean, a part of the package is training. Does that need to be  
10 spelled out in a disclosure document?

11 MR. WIECZOREK: No, not if it's in the contract.

12 MS. HOWARD: Okay. Agreement with that? And if it's  
13 not in the contract, it should be in a disclosure document?

14 MR. WIECZOREK: Well, if it is not in the contract then  
15 the seller is not obligated to provide it. Similar to the  
16 situation with the buyer not being obligated to comply with  
17 things that aren't in the contract. You know, either the  
18 problem is that you could say anything here about whether it  
19 should go in or it shouldn't go in because if it's not  
20 obligatory, the seller could say just about anything. We'll  
21 provide X, Y and Z, but we're not obligated to provide it. They  
22 wouldn't have to provide it, theoretically. So, I'm not sure  
23 that you'll get too far with this.

24 MS. HOWARD: What about an instance where they say,  
25 we're going to provide X, Y and Z, period. But it doesn't

1 appear in the contract? But they have made the representation  
2 that that is part of the package?

3 MR. D'ALESSANDRO: It's happened.

4 MS. HOWARD: It's happened, John?

5 MR. D'ALESSANDRO: In franchises, it's happened, yes.

6 MS. HOWARD: Has it happened to you personally, or do  
7 you care to tell us at all about that?

8 MR. D'ALESSANDRO: It is involving personnel from  
9 another outlet and it was not in the contract, but it was in the  
10 disclosure. It was forced to relinquish. This individual  
11 wanted to move from the other operation to my operation. But  
12 that was related to franchises.

13 MS. HOWARD: Okay. So, in the biz op context? David,  
14 what do you think?

15 MR. FINNIGAN: I kind of lean towards that, you know,  
16 if they provide a contract and it's an obligation, it should be  
17 in the contract. It doesn't need to be in the disclosure  
18 statement. I guess the concern is that there may be a lot of  
19 oral statements that are made that, you know, we're going to do  
20 X, Y and Z, and it's not in the contract, but the investor is  
21 relying upon that. I guess the rule is that, you know, is that  
22 obviously you can't rely upon oral statements. I don't know how  
23 you resolve that problem.

24 MS. HOWARD: All right. You know what I think? It is  
25 time to move on. Maybe we could just extremely rapidly go

1 through a couple of things. Sort of just have some rough votes.  
2 Crucial, not crucial or somewhere in the middle, so we can get  
3 on to the next topic.

4 Public figure involvement. Is that relevant in this  
5 arena?

6 MR. WIECZOREK: No.

7 MS. HOWARD: No? Okay. How about listing or including  
8 financial statements?

9 MR. TOPOROFF: Audited financial statements.

10 MS. HOWARD: Audited financial statements of the biz op  
11 seller? Is that crucial information? Just, you know, yes?

12 MR. TOPOROFF: Let me ask. Is that required under  
13 Illinois statute?

14 MR. SANSON: Yes and no. You can have that or --

15 MR. TOPOROFF: But you do have some kind of financial  
16 disclosure?

17 MR. SANSON: Yes.

18 MS. HOWARD: Okay. Should there be some financial  
19 disclosure, how about that question?

20 MR. WIECZOREK: I really don't see it. I can see the  
21 need in theory, but in reality, I don't know that any biz op  
22 buyer is really going to understand what's going on with any  
23 financial statement anyway. I think it may be another  
24 requirement that's going to be imposed that will push people not  
25 to comply because to get an audit or even to get a review is an

1 expensive undertaking. So, frankly, in this area, I'm not sure  
2 that a financial makes a whole lot of difference. From a  
3 disclosure standpoint, I don't think it will be well understood  
4 anyway.

5 MS. HOWARD: So there's some disagreement here?

6 MR. TOPOROFF: Yes.

7 MS. HOWARD: Yes. Okay. How about the issue of  
8 earnings claims? If earnings claims are made, should there be  
9 something written? Should there be substantiation that's  
10 required to be given? Real quick vote.

11 MR. SANSON: Yes.

12 MS. HOWARD: Yes.

13 MR. FINNIGAN: Yes.

14 MS. HOWARD: Is this crucial?

15 MR. SANSON: Yes.

16 MR. TOPOROFF: As the Rule currently requires.

17 MS. HOWARD: That's right. Yes?

18 MR. SANSON: Yes.

19 MS. HOWARD: Okay. We've discussed attaching a copy of  
20 the contract. And there was some disagreement, is that right,  
21 at this point?

22 MR. SANSON: Yes.

23 MR. FINNIGAN: Yes.

24 MR. WIECZOREK: Yes.

25 MS. HOWARD: Okay. All right. I think that's it.



1           MR. TOPOROFF: Just one other thing on this topic of  
2 what should be in a disclosure document. Is there anything in  
3 Illinois statute that you require by way of disclosure that we  
4 do not at the Federal Trade Commission, that you also find to be  
5 particularly useful? Or does the Federal Trade Commission's  
6 disclosure document really cover the bases?

7           MR. SANSON: I think it's all covered.

8   (A short recess was taken.)

9           MR. TOPOROFF: Back on the record. Okay. We're going  
10 to do something a little bit out of sequence. Normally we would  
11 have participation at the end. However, there are at least one  
12 person who would like to make a statement on the record who is  
13 going to leave shortly. So to give people a little bit of a  
14 break, also, we can give Mr. Tingler an opportunity to state a  
15 comment for the record.

16           Now, before we do so, just please introduce yourself  
17 and spell your name and who you represent.

18           MR. TINGLER: My name is Robert Tingler, T-I-N-G-L-E-R.  
19 I am the Franchise Bureau Chief of the Illinois Attorney  
20 General's Office. And I appreciate the opportunity just to make  
21 two quick points that came up as a result of listening to the  
22 discussion.

23           One is in regard to a waiting period, whatever it may  
24 turn out to be. First, I should qualify the fact that I deal 99  
25 percent franchises, occasionally with business opportunities.

1 For policy type decisions, I would defer to the Secretary of  
2 State's Office for virtually anything which should be done with  
3 rules and regulations. But one thing that I did encounter in a  
4 business opportunity situation was that this particular company  
5 would make their sale and get their money and the delivery of  
6 the items would come after an agreed three-day waiting period.  
7 By the time the person had figured out that this was just either  
8 not for them or a total mess from the beginning to end, it was  
9 untried and not likely to succeed, they had an uphill battle to  
10 try and get their money back.

11 And I'm just throwing out for the possible future  
12 discussion some method whereby someone could at least require  
13 that they complete the delivery of the key items that they're  
14 buying so that the purchaser has a legitimate period of time to  
15 make a true decision.

16 The other thing was a very overall view of the business  
17 opportunity situation where it seems to me like there are two  
18 very large categories of business opportunities. One being  
19 where an ongoing relationship is anticipated, and the other  
20 where the relationship ends when the sale is made. And that  
21 some of the rules and regulations, I think, the discussion  
22 should revolve around what may be the more critical situation of  
23 the ongoing relationship, but not lose sight of the fact that,  
24 you know, a one-time sale is important, too, for some people if  
25 they're spending quite a bit of money.

1           But that these categorizations, I think, may influence  
2 how the rule might read if you think about the two different  
3 types of situations. The ongoing relationship might, for  
4 instance, be an instance where you want audited financial  
5 statements because you're depending upon the financial viability  
6 of that company for your future, if you want to keep in this  
7 system, whatever it may be. If it's a one-time sale, then you  
8 look at the package, you think it's something that might work,  
9 and if the company goes out of business, you've still got the  
10 package and the ideas and so forth. Theoretically, you could  
11 continue on.

12           The other thing on those situations where the  
13 relationship is over when the sale is made, that might influence  
14 how you write the rule on the number of sales that you've made  
15 and how many of those are still in business because you can't  
16 trace those people. You haven't the faintest idea what they've  
17 done with their package when they've walked out the door. And  
18 you're not about to call them up on the phone and say, did you  
19 succeed? Are you still doing this? So, those are just some  
20 thoughts to throw on the table. I appreciate it.

21           MR. TOPOROFF: Does anybody have any questions for  
22 Mr. Tingler? Okay, thank you.

23           MR. TINGLER: You're welcome.

24           MR. TOPOROFF: And that gets us directly into our next  
25 area, which is what types of alternatives to disclosure might be

1 applicable here? And one of them that was proposed by Mr.  
2 Tingler just now, I don't know if it was as an alternative  
3 necessarily, but perhaps as a supplement to, is some kind of  
4 cooling off period or right to cancel. The same kind of concept  
5 was raised in the comments of John Baer, who basically said that  
6 all that's needed in this area is strong anti-deception  
7 authority, such as Section 5 of the Federal Trade Commission  
8 Act, coupled with a cooling off period.

9 So, I just want to open up the floor to any discussion  
10 about cooling off periods generally, or any other possible  
11 alternatives that might work in this field, either in addition  
12 to disclosure or as a substitute for disclosure. Eric?

13 MR. ELLMAN: First of all, I think that there's ample  
14 coverage for a lot of fraud and deception in Section 5. And  
15 that should be taken into consideration. And I would suggest  
16 perhaps an alternative to a cooling off, and that would be the  
17 existence of a viable buy back policy. It's worked very well in  
18 the direct selling industry for a number of years. And it has  
19 been widely praised by a lot of members of the law enforcement  
20 community.

21 The purpose of any kind of disclosures or regulations  
22 area, is to cut down on fraud and deception and to limit the  
23 risks of a business opportunity. And I think that something  
24 that the Commission might want to consider is one of those ways  
25 to avoid those risks are to make it as minimal, make the risk as

1 minimal as possible and limit a consumer's exposure to risk and  
2 to fraud by requiring that those who are offering business  
3 opportunities offer a 90 percent repurchase policy.

4 MR. TOPOROFF: Now, are you suggesting that the  
5 repurchase policy be an obligation under the Rule or that those  
6 companies that have such a policy should be exempt?

7 MR. ELLMAN: Either one. I might suggest that, as an  
8 alternative to the regulation that you might want to consider a  
9 90 percent buy back policy.

10 MR. TOPOROFF: Well, we're going to get to exemptions  
11 in a minute.

12 MR. ELLMAN: Well, this isn't necessarily an exemption,  
13 but it is an alternative to disclosure.

14 MR. TOPOROFF: On the cooling off period, right now I  
15 suppose you could consider the ten day review period as somewhat  
16 of a cooling off period. It's technically not a cooling off  
17 period because the way I conceive of cooling off periods, it's  
18 more that you could rescind what you've already entered into.  
19 Where this is more a delay to give you time to review the  
20 disclosures in order to make a wise decision and then you  
21 invest. So, it is somewhat different. We discussed before the  
22 ten day cooling off period, or the ten day delay period. I  
23 don't think that we need to get into that.

24 But, Mr. Tingler's suggestion, should there be some  
25 kind of cooling off period at the end or post-sale? Meaning, if

1 I sign, I'm an investor and I sign on January 1st, I either sign  
2 a contract or give money for a business opportunity, would it be  
3 helpful if I'm given the right, let's say, to be able to cancel  
4 that contract at some other point, be it ten days, two weeks,  
5 whatever the time period is? But should the business  
6 opportunity purchasers have that right to cancel, or basically  
7 to rescind their contract?

8 MR. BENNETT: I hate to keep bringing up the buy back,  
9 but in effect, the buy back is an extended cooling off period.  
10 In the instance of our company, we have 100 percent buy back,  
11 and it extends for the life of the contract. They can cancel.  
12 They can get out. They can return their kit at any time. So,  
13 the buy back is, in effect, if it's worded correctly, it's an  
14 extended cooling off period, if you will.

15 MR. TOPOROFF: Should that kind of program be  
16 mandatory?

17 MR. BENNETT: It would not bother us because we adhere  
18 to it. We actually go above the DSA Code. We have 100 percent  
19 buy back. And that's been for the length of the company, or for  
20 the duration, the history of the company.

21 MR. TOPOROFF: John?

22 MR. BROWN: Obviously, I support the notion of  
23 recognizing in some way under the law the buy back and the  
24 cooling off as being effective risk reduction techniques. You  
25 know, this is where it really is a struggle when you have the

1 utter absence of other kinds of business opportunities present.  
2 I don't know how it would impact on their legitimate operations  
3 to the degree that there are some out there.

4 For Amway, given the low cost of getting involved with  
5 it in the first place, for us to say, look, in the first three  
6 months, if you should change your mind, just give back the kit.  
7 We know you've opened it up. We know that it can't be used  
8 again. You can get it all back. You get your money back. And  
9 the deal is square, and it's over. You've got three months to  
10 do it. Anytime after that, if you have inventory in your  
11 possession and you decided to leave the business, so long as  
12 it's not damaged or spoiled inventory, you can give it back and  
13 get your money back.

14 But that's our unique circumstance where there really  
15 shouldn't be that much of a dollar outlay in the first place.  
16 In a case where somebody is offering a business opportunity  
17 that's substantially more expensive, I don't know how realistic  
18 a proposition that would be. A cooling off period that would be  
19 after the contract is signed but before any goods change hands  
20 might be a possibility. But again, if you've laid out  
21 substantial dollars and somebody sends you equipment, goods and  
22 so on, that really can't be given back and made use of again,  
23 for them it might not be a tolerable proposition. And that's  
24 why I'm looking at it in the terms of an exemption as opposed to  
25 a mandate. It would be, you know, a possibility.

1           MR. FINNIGAN: I think at first the buy back sounds  
2 like a great alternative, but I don't think they're the same. I  
3 think that a rescission is a good idea and it has to be  
4 disclosed that there is a rescission, too. So, if you can't  
5 completely obviate the disclosure requirement, at the very least  
6 they have to disclose that there's this rescission period that's  
7 ten days or however length it is, and then they get a full  
8 refund. The problem with the buy back, if you allow a buy back,  
9 I think it should be for a significantly longer period. The  
10 problem with the buy back is that the company, well, it has to  
11 be goods that aren't spoiled. So it's not completely like a  
12 rescission. The Direct Selling Association, it's a 90 percent  
13 recovery. I assume that you make the investor pay the mailing  
14 costs to send it back. So there's a lot of other hidden costs  
15 that go in with a buy back. So it's not necessarily the same as  
16 a rescission.

17           So, I think to say that they are the same is not  
18 correct. I think you could do either one. I think if it's  
19 going to be a buy back, you know, it should be a longer period.  
20 If it's only going to be 90 percent, it should be an even longer  
21 period than 100 percent buy back.

22           MR. TOPOROFF: Let me ask our state expert, Dennis, are  
23 you aware of any state biz op statutes that incorporate a right  
24 to rescind or cooling off period, or call it whatever you want?  
25 Are there states that incorporate that?



1           MR. WIECZOREK: No. I can't profess expertise on this.  
2 I think there are a couple, but it's not prevalent. I remember  
3 seeing some. There may be some in terms of bonding that the  
4 bond can be utilized if a guaranty is not performed. But I  
5 don't know -- I have a vague recollection there may be one or  
6 two states that have a rescission period afterward.

7           But my opinion is that it's a bad idea, because I think  
8 it allows people to shop. They can go through the whole  
9 process. They can get the, whatever it is they're going to get,  
10 and then they can take proprietary information, whatever, send  
11 it all back to the seller, and do their own thing. Set up their  
12 own firm. Competitors would love to have this kind of thing  
13 available to it. I'm sure they would routinely shop the other  
14 competitors to see what they're up to, because it's a way to get  
15 everything that you need and then walk away.

16           MR. TOPOROFF: Is that a concern, when we're talking  
17 about biz ops as opposed to franchises? Is there proprietary  
18 information?

19           MR. WIECZOREK: It's probably less of a concern, but I  
20 think that some of the legitimate companies would be worried  
21 about shoppers. After all, this person is getting a disclosure  
22 document two weeks before he or she buys, and has two weeks to  
23 evaluate, two weeks to talk to an attorney or an accountant.  
24 After they do all of that, they then buy it and then they get  
25 cold feet. I'm not sure that that's such a good policy

1 rationale to give people multiple swings at the plate before  
2 they finally have to commit themselves to something.

3 MR. TOPOROFF: What happens if this, again, was a  
4 substitute for disclosure but not as an addition to disclosure?  
5 So let's say an investor went through the sales process,  
6 received a contract and the contract, one of the terms were, you  
7 can rescind this contract in ten days or a week after delivery,  
8 however you want to couch that, would that make it more  
9 palatable?

10 MR. WIECZOREK: Well, my theory is premised on a  
11 disclosure document being given. And that should be enough.  
12 But if you eliminate the disclosure document and you provide a  
13 rescission period, I think that would probably be a good  
14 alternative, yes.

15 MR. TOPOROFF: Now, for biz ops, and again, as distinct  
16 from franchises, would it be preferable to follow a cooling off  
17 period, a rescission approach, or disclosure approach?

18 MR. WIECZOREK: Well, again, the issue is, who is it  
19 that we're talking about in terms of business opportunity  
20 sellers and probably most of the ones that are out there doing  
21 evil deeds will ignore the disclosure requirement anyway. And  
22 also, the disclosure will be a mixed blessing in terms of  
23 whether it's going to be read and whether it's going to be  
24 understood.

25 So, I guess to my mind, just off the top of my head, it

1 would be preferable in the biz op scenario, to have a rescission  
2 period than a disclosure.

3 MR. TOPOROFF: Now, does the same issue come up that  
4 we're basically trusting scam artists to rescind the contract  
5 and give back money, basically?

6 MR. WIECZOREK: I think it's the same issue. I think  
7 it's the same issue with the disclosure. Sure.

8 MR. TOPOROFF: So there's on real guaranty there  
9 either, number one, that the company will still be around, let  
10 alone honor its rescission?

11 MR. WIECZOREK: Yeah, but the one thing I will add to  
12 that is that, you know, if the FTC has a rescission rule and the  
13 states continue with the disclosure business opportunity laws,  
14 you know, that's sort of adding two evils together in a  
15 patchwork basis across the United States unless the FTC  
16 preempts. So I'd be concerned about a state where you have to  
17 give disclosure, but then under the FTC rule, you have to  
18 provide rescission.

19 MR. TOPOROFF: John has something to say?

20 MR. D'ALESSANDRO: I think the scam artists are not  
21 going to be able to buy anything back since they probably have a  
22 shell company. And there's on money in the company to give  
23 back. So, to have something like that, you won't get anything  
24 out of it.

25 MR. BROWN: If we analyze everything from the

1 perspective of the assumption that the company is just scamming  
2 people, then the disclosure is a waste of time, rescission is a  
3 waste of time, buy back is a waste of time. So, it's all a  
4 waste of time. The only point of it is that they'll violate it  
5 and therefore we have a tool to go after them. And that is in  
6 reality what often happens. I guess I'm looking at the whole  
7 notion of possibly having a rescission period as an alternative  
8 for some possible biz ops to disclosure. Is that right now  
9 there seems to be an acknowledgment, I may be wrong, but there  
10 seems to be an acknowledgment that there are not that many  
11 business opportunities out in the marketplace filing business  
12 opportunity disclosures. And if the concern in the market is  
13 that business opportunities really have to structure their  
14 operations to avoid the disclosure because it is burdensome from  
15 a competitive perspective or from whatever perspective is  
16 relative to them, having an alternative might encourage biz ops  
17 to structure themselves in a way that's more market-oriented and  
18 not so concerned with regulation. In other words, they're very  
19 comfortable doing the rescission. They're just never  
20 comfortable doing the disclosure.

21           It might represent a more reasonable way to regulate  
22 that would encourage some legitimate business opportunities to  
23 come into the market that aren't presently available. I don't  
24 know that that is the case. There just don't seem to be that  
25 many biz ops that register running around. But I should think

1 that offering some alternatives might increase the number of  
2 legitimate business opportunities, and presumably that would be  
3 good for the marketplace.

4 MR. TOPOROFF: One last question on this. Could we  
5 have an, like a menu, if you will, Choice A, you disclose.  
6 Choice B, you don't have to disclose but you have to have  
7 rescission. Would that work? So that way, conceivably, if a  
8 company decides it's too cost prohibitive to have disclosures,  
9 they could avoid that. But the flip side of it, they would be  
10 under an obligation to give rescission? Would that kind of  
11 system work?

12 MR. WIECZOREK: I think it's makes sense, yes.

13 MR. TOPOROFF: David?

14 MR. FINNIGAN: I think you could do that.

15 MR. TOPOROFF: Anyone else?

16 MR. BROWN: I think it's a good idea.

17 MR. TOPOROFF: John?

18 MR. D'ALESSANDRO: I agree.

19 MR. TOPOROFF: That's a plus. Well, let me just now --  
20 Adam, do you have any thoughts on that?

21 MR. SOKOL: To be honest, I'm not sure that I like it,  
22 but I would defer to David on that.

23 MR. TOPOROFF: Okay. And again, these are just various  
24 proposals. Someone, meaning Eric, mentioned before that I give  
25 a disclaimer that I don't speak for the Commission at all. So,

1 I'll just say that now. I don't speak for the Commission.  
2 Neither of us, neither Myra or myself, speak for the Commission.  
3 What we're doing here today is just probing, asking questions,  
4 telling you what our experiences have been. And by no means are  
5 we speaking for the Commission, nor is anything etched in stone  
6 at this point. Not by a long shot.

7 MR. WIECZOREK: Up until now I think you have been  
8 speaking for the Commission. Because you haven't given the  
9 disclaimer, right? We can take a vote on that, if you like.

10 MR. TOPOROFF: Okay. On that note, we'll turn to the  
11 last of the agenda items. And that is possible exemptions.

12 What I would like to do is use the direct sellers'  
13 comment and its supporters, basically, their comment, as a model  
14 and go through the various issues there and discuss perhaps what  
15 are the pros, cons and maybe some costs involved.

16 The first item is one that I really don't think needs  
17 too much discussion, and that is that there has to be a required  
18 purchase, as opposed to voluntary purchases. I think right now  
19 that is the state of the law. Our franchising business  
20 opportunity regulation applies only when there's a required  
21 purchase. And I don't know that that is necessarily going to  
22 change. I don't see why it would.

23 MR. WIECZOREK: By the way, under some state laws there  
24 is no required purchase requirement. And I think it would be  
25 advantageous to make that a key element of the law.

1 MR. TOPOROFF: Well, what do they say?

2 MR. WIECZOREK: The purchaser buys. The purchaser  
3 pays. It's an optional payment. It's covered.

4 MR. TOPOROFF: David, under your statute, do you have a  
5 required payment or is it any payment?

6 MR. FINNIGAN: I believe it's required.

7 MR. TOPOROFF: I believe it's required. Is there any  
8 real discussion that needs to discuss that issue? I'm sorry?  
9 No, otherwise, we'll move on.

10 The next big item is the threshold. And a number of  
11 commenters have really been all over the board on the subject.  
12 Direct sellers have suggested that the Commission raise the  
13 minimum required payment to \$1,000. There are those who have  
14 suggested that we lower it to about \$300 in one case, \$100. I  
15 think that there are other proposals out there.

16 One concern that I have is, if we raise the threshold,  
17 would that, let's say \$1,000 being the new threshold, would that  
18 basically be saying that up until \$1,000, meaning \$999, it would  
19 be perfectly acceptable for biz op sellers to offer. And what  
20 we're going to do is, instead of right now we see a slew of  
21 companies that sell for \$495 or \$499, what they're going to do  
22 is just sell for \$999 and are we really solving the problem?

23 MR. FINNIGAN: That's exactly what he'll say. They'll  
24 go right to \$999 and that's the experience with every state, no  
25 matter. I guess maybe the \$100 probably would be a little bit

1 too low, but I think almost every threshold, either in Illinois,  
2 since it's \$500, you have a lot of people selling at \$495. You  
3 know, in other states I think it's like \$200, \$300, you know,  
4 and you'll see the sales at \$199. I think if you put it at  
5 \$100, that probably is not economically feasible to sell a  
6 business opportunity at \$99 a shot, but I think you do need to  
7 have some sort of threshold. We see, at \$500, that seems to be  
8 working out pretty well.

9 I think that if you try to put it too low, you're going  
10 to end up opening up, too. You need a limit in the sort of  
11 cases that you're going to be looking at.

12 MR. TOPOROFF: Eric?

13 MR. ELLMAN: I thought you'd never ask.

14 MR. BROWN: He's waited since 9:00 o'clock this  
15 morning.

16 MR. ELLMAN: I'm going to take the rest of the  
17 afternoon off. I'm going to leave now. Raising the threshold  
18 is important for a number of respects. And let me go back to  
19 the inception of the \$500 threshold. It's well documented, but  
20 I just want to make this clear. And when the interpretive  
21 guides and the statement were released to this Rule back in  
22 1978, the Commission said that the Rule should focus on those  
23 franchisees who have made a personally significant monetary  
24 investment and who cannot extricate themselves from an  
25 unsatisfactory relationship without suffering a financial



1 setback.

2           And that comes up in the other statement, that the  
3 Franchise Rule back in 1978. I think that was valid back in  
4 1978. And it remains just as valid today. The problem is is  
5 that \$500 in 1978 is worth well beyond \$1,000 today. And I  
6 think that inflationary pressures would indicate, I think  
7 demand, that the threshold be raised up to \$1,000, which is less  
8 than what \$500 would be worth today, but I think \$1,000 seems a  
9 rather reasonable way to go.

10           If this Rule is not going to be reviewed for yet  
11 another 10 or 20 years, then \$500 from 1978 would be worth even  
12 significantly less in the future. I think we have to take that  
13 into very serious consideration. There are some companies who  
14 price their sales kits at just under \$500. I'm talking about  
15 legitimate direct selling companies that price their sales kits  
16 at just under \$500, for good reason. Because of the burdens  
17 that go along with complying with business opportunity laws.  
18 And in some cases, these companies might be taking losses on  
19 those kits.

20           But I think that the inflationary pressures demand that  
21 this be raised to \$1,000. \$1,000 is fairly more significant of  
22 a loss than \$500. However, if you couple that with a buy back  
23 guaranty, then the risk is, of course, less, and rather  
24 dramatically. But even if you don't couple it with any kind of  
25 buy back guaranty, then, you know, as I said, \$1,000 is some

1 degree of money to a lot of people if they lose it. However, I  
2 think that at some point the consumers have to take some  
3 responsibility for themselves. And they have a responsibility  
4 to investigate whatever they're getting into. And \$1,000 is an  
5 exemption for small businesses with little financial risk like  
6 direct sellers. And it puts some responsibility, it takes some  
7 burdens off direct selling companies sales people that might not  
8 be able to comply with the aspects of the Rule, and I think it  
9 puts some burdens appropriately upon some consumers.

10 MR. TOPOROFF: Well, let me ask you two questions. One  
11 is, your reading from the record is right, but I think you have  
12 to take into consideration that the Commission's  
13 characterization or statements were addressing both business  
14 opportunities and franchise sales. And I think if we eliminate  
15 franchise sales, I think the typical buyer of a biz op perhaps  
16 \$500 is much more significant to them than perhaps someone going  
17 to buy a franchise. So, is there a distinction when it comes to  
18 the threshold for franchises versus business opportunities?

19 MR. ELLMAN: However, everything that I've seen and  
20 read by going through the Consumer Protection Reports that come  
21 out periodically and talking with other consumer protection and  
22 law enforcement people, everything that I've heard is that when  
23 they investigate and prosecute business opportunity fraud, it's  
24 to the tune of several thousand dollars. It's not often in the  
25 case of a few hundred dollars. And I think that if you want to

1 focus your attention on where the fraud is, that's where you go  
2 because that's where consumers seem to be -- that's where a lot  
3 of the fraud seems to be centered, in the thousands of dollars.

4 MR. TOPOROFF: Well, I don't know even from our law  
5 enforcement experience if that's true or not. But putting that  
6 aside, if, let's say, the threshold was to remain the same,  
7 \$500, or even lower, would your concerns be addressed if there  
8 were other kinds of exemptions in the rule so that direct  
9 sellers or other kinds of legitimate folks would not be covered  
10 by the Rule anyway? Why is it so critical if the people you  
11 represent, let's say, are not going to be covered by the Rule,  
12 why is it so critical that the threshold be raised?

13 MR. ELLMAN: Well, in the absence of any other  
14 protections, it's extremely crucial. But let me throw out a for  
15 instance. That if the threshold was lower than \$500, but there  
16 was an exemption that you didn't have to comply if you had a 90  
17 percent buy back, I think that's probably something that our  
18 industry can live with, because we have a buy back now and it's  
19 been rather successful.

20 But in the absence of protection along those regards,  
21 then raising the threshold, certainly at minimum keeping it  
22 where it is, is absolutely critical. And raising it to \$1,000  
23 is extraordinarily important.

24 MR. TOPOROFF: Let me throw out another thought. And  
25 that is, what impact, if any, should we consider the recently

1 enacted Welfare Reform Bill, which basically means that people  
2 are going to lose benefits or receive benefits only if they  
3 receive certain employment. And we have a project at the  
4 Commission that's looking at those kinds of issues right now.  
5 It could very well be that in a year or two there will be a  
6 flood of people who are looking for opportunities so they can  
7 document employment, and those opportunities might be \$50, \$100,  
8 what have you.

9 And I could tell you, I've already seen some kinds of  
10 schemes. I don't want to necessarily call them schemes, because  
11 I don't know. We haven't investigated them. But there is the  
12 possibility in the near future that there will be any number of  
13 opportunities there that will be sold for minimal size. Does  
14 that factor in at all?

15 MR. ELLMAN: Well, I would encourage many of those  
16 people that we're trying to get off welfare to try direct  
17 selling as an opportunity to create or supplement some income.  
18 But be that as it may, I honestly don't know how to respond to  
19 that. I don't think that because there is a potential for fraud  
20 out there we should hamper the ability of legitimate businesses  
21 to operate in the marketplace.

22 MR. TOPOROFF: John?

23 MR. BROWN: To follow up on what Eric is saying, and to  
24 respond to the question of the possible impact of a much larger  
25 group of people requesting business opportunities. One,

1 lowering the threshold of the biz op disclosure requirements, I  
2 don't think will have any impact on people who are targeting  
3 those persons who are afflicted with poverty or are otherwise  
4 disadvantaged. Those people, the scam artists, the con artists  
5 and the perpetrators of fraud, they're going to do what they do.  
6 And it will be a question of the resources of the State of  
7 Illinois and the Federal Trade Commission under Section 5 to  
8 deal with people who lie, steal and cheat. They will do that  
9 either by failing to make proper disclosures or they'll do that  
10 by engaging in fraudulent conduct. And I don't think that whole  
11 issue is truly relevant to this question. And indeed, I would  
12 question how a disclosure of financial statements to people who  
13 are fresh off welfare is going to serve them well. I would like  
14 to think that there are other things that would matter more to  
15 them. And one is the very fact of enforcement posture on the  
16 part of, be it the State of Illinois or the Federal Government,  
17 to go after these frauds when they occur.

18 David made the point, and I think it's a sound one,  
19 that, and be it the Federal Trade Commission itself made the  
20 point just about 20 years ago, that at a certain point the level  
21 of regulation represented by the Trade Regulation Rule is not  
22 appropriate. And they set that at \$500. Amway Corporation  
23 wholeheartedly agrees with the setting of that threshold at that  
24 time. And I think, given the CPI, putting that \$500 now to  
25 approximately \$1,200, it makes sense to examine a movement of

1 that threshold. Because I come at it from a different  
2 perspective than perhaps someone who is trying to cover as many  
3 opportunities by law as possible. I come at it from the  
4 perspective that I know opportunities that have been priced at  
5 \$495, and perhaps they're legitimate and good opportunities that  
6 have been priced at \$495 solely to avoid the \$500 limit in  
7 certain state laws and the FTC Act, or Trade Regulation Rule.

8           If we take the view that that's a good thing because it  
9 held the price down and made it available to people, I suppose  
10 we can really celebrate and knock it down to \$5 so that  
11 everybody gets one for \$4.95. But the reality is, we know  
12 logically that what that really means is that the market is not  
13 setting the price of the opportunity where it would like to.  
14 It's reacting arbitrarily to a limit set by government.  
15 Government has to set limits sometimes to do the right thing.  
16 And so, what we're trying to figure out is what is the right  
17 level. We've suggested \$1,000 because the evidence suggests  
18 that given the amount of money typically involved with major  
19 business opportunities, \$1,000 or above is going to deal with  
20 those. But those under \$1,000, they're still subject to the  
21 law. They can't lie, steal and cheat with impunity. They can  
22 be prosecuted either by the State of Illinois or by the Federal  
23 Trade Commission. And that's only right.

24           But the question is, at what point does this regulation  
25 impact them, and I think \$1,000 is justified. And I certainly

1 think some increase is due. We don't have the CPI incorporated  
2 into the reg, and that would be unreasonable to do that simply  
3 to draw a bright line, but it's been 20 years, time to look at  
4 it again. Raise it to \$1,000 and you do essentially what you  
5 did in '78 with \$500.

6 MR. TOPOROFF: Is your suggestion of \$1,000 based upon  
7 any analysis, study, any other factors other than ordinary  
8 inflation?

9 MR. ELLMAN: Frankly, no. And the reason that we  
10 suggested \$1,000 is because we first looked at, there are  
11 companies in our association that would like to see that  
12 threshold raised, to increase it to allow their business  
13 flexibility. So we went back and looked at the bill, which was  
14 \$500. And that's our starting point. And I think the natural  
15 starting point is what is \$500 worth today? Well, it's worth  
16 over \$1,000. And asking for \$1,200 just didn't really seem  
17 reasonable. And the \$500 was sort of arbitrarily set in 1978,  
18 so we created an arbitrary \$1,000 to follow on the equal  
19 arbitrariness of the \$500, which seemed rather logical in its  
20 arbitrariness, if there is such a thing.

21 But so we looked at that to what \$500 would be worth  
22 today. And then we realized that we're not going to go through  
23 this exercise again until well into the next century. And there  
24 needs to be some flexibility for the direct selling industry,  
25 who, assuming that the threshold stays at \$500, I'm not so sure

1 that we can live with the \$500 threshold in 2010, or 2015 or  
2 beyond.

3 MR. TOPOROFF: Well, one of my concerns, again, about  
4 the threshold is, just looking at an inflation factor, I don't  
5 know if that tells us the whole tale. Because the people who  
6 may have been investing, it assumes that it's the same people  
7 who were investing 20 years ago when the Rule was created, for  
8 the same folks today and what their level of income is, so that  
9 if they invested \$500 in 1978, let's make it 1980, well, it's  
10 the same kind of folks, more or less, who are investing today,  
11 and their income should have risen by whatever. And therefore,  
12 if you factor in inflation, \$1,000 more or less matches.

13 But I don't know, and what I would like to get more  
14 information on, if it's available, is who are the folks who are  
15 buying these opportunities. It's not necessarily the same folks  
16 in 1980 who are going in and buying these opportunities today.  
17 And maybe \$500 means a lot more to those people today than \$500  
18 even meant to the crowd who were buying the business  
19 opportunities.

20 MR. ELLMAN: Well, I'm not sure if we'd be able to get  
21 any evidence, because they're not here, for whatever reason.  
22 And I'm not sure they'll ever show up.

23 MR. TOPOROFF: John?

24 MR. BROWN: I'm operating from the assumption that \$25  
25 means a lot to a person who's lost it. And, you know, I think



1 if somebody is, you know, scammed for \$10, they should be held  
2 responsible for it. And I don't see how, you know, again,  
3 detailed disclosure documents or registration requirements would  
4 address the person who got scammed for \$15, \$25, \$100. The  
5 whole point of it from my perspective is that the \$1,000  
6 threshold is reasonable and appropriate in terms of providing  
7 the flexibility necessary to allow business opportunities to,  
8 legitimate business opportunities. I'm worried about the  
9 legitimate ones. The illegitimate ones we should hammer and get  
10 rid of them as best we can, knowing that they'll always exist.

11 But, you know, at what point should the disclosure and  
12 other regulatory, special regulatory requirements kick in and,  
13 for that purpose, I don't think \$1,000 is a large sum of money.  
14 Any amount of money is a large sum of money if it's going to be  
15 stolen. And so, you know, I think we get off track if we say,  
16 well, does that mean a con artist will be able to operate under  
17 \$1,000? Well, of course it will. They can operate under \$1,000  
18 and they can operate over \$1,000. In fact, what reality is,  
19 again, and without having seen a substantial study of the matter  
20 in the past, say, two or three years, but still anecdotally for  
21 people who follow the Consumer Protection Reports and people who  
22 follow the Better Business Bureau Report and so on, as my office  
23 does, anecdotally, the frauds are in the thousands of dollars.  
24 And I do think it's relevant that the Federal Trade Commission  
25 looked at this in tremendous detail. The dollar fraud that was

1 occurring back in the late '70's was typically in the many  
2 thousands of dollars.

3 But to say that, well, will people miss, you know,  
4 under \$500? Absolutely. And that's inexcusable. And people  
5 who engage in fraud at any level should be prosecuted. But it's  
6 a question of when this particular kind of regulation should  
7 kick in. And I think \$1,000 is eminently reasonable.

8 MR. TOPOROFF: Any other thoughts on the issue of a  
9 threshold? Dennis?

10 MR. WIECZOREK: Well, one possibility is to go with a  
11 regime over \$1,000 where you have a choice of disclosure or  
12 rescission, and below \$1,000 your only obligation is to just  
13 offer rescission. Create the disclosure obligation after you  
14 get above a certain level. But require rescission at any level,  
15 above a certain amount. I don't know whether it would be \$500  
16 or \$200 or something. That's something to think about.

17 And by the way, for the record, I wanted to put on. I  
18 reviewed all the state laws who order rescission. I think there  
19 were seven states with rescission remedies, ranging from three  
20 days to 30 days, California, Iowa, Kentucky, Maine, Nebraska,  
21 Ohio and Washington. So they have time periods ranging from  
22 three to five to seven to thirty days.

23 MR. TOPOROFF: And the time period is measured from the  
24 time they sign the contract?

25 MR. WIECZOREK: Yes.

1 MR. TOPOROFF: David?

2 MR. FINNIGAN: I think on the threshold requirement,  
3 first off, a very good argument could be made that there should  
4 be no threshold requirement. I mean, basically the reason why  
5 we have a threshold requirement has more to do with this idea of  
6 economy and efficiency and how much regulation there should be.  
7 Secondly, I think \$500, I can understand, you know, from a kind  
8 of intellectual point the inflation argument, but, you know, as  
9 John was saying, \$500 to most individuals is a lot of money to  
10 lose.

11 And thirdly, what we're seeing is, and I think I  
12 alluded to this beforehand, is people specifically working to  
13 get themselves under the statutory threshold requirement. And I  
14 can understand the business costs, but, you know, as a regulator  
15 we come from the viewpoint of we want registration. And if a  
16 company chooses to put themselves under, that's fine. If they  
17 want to make money and they want to sell over \$500, then they  
18 have to register. And I think to a certain extent there is some  
19 merit the regulation versus the business cost, but, you know,  
20 our viewpoint, being the regulator's viewpoint, this is tending  
21 towards the view that if you're going to sell over the threshold  
22 requirement, then you have to register. And I think \$500 is a  
23 very good threshold requirement.

24 MR. TOPOROFF: Any thoughts on Dennis' proposal, and  
25 that is, over \$1,000 a biz op seller would have the option of

1 offering a disclosure document or rescission. Below \$1,000 they  
2 would have to offer rescission? Eric?

3 MR. ELLMAN: I would feel much more comfortable if it  
4 were under \$1,000 that you have a buy back policy. For the  
5 reasons that we stated before, we had it for a while. It seems  
6 to work for the direct selling industry. The risk that a  
7 consumer would have is perhaps not as much as their rescission  
8 offer. However, it's still a less significant sum of money, 90  
9 percent, of course, of \$1,000 would be \$900 they'd be getting  
10 back and perhaps \$100 they were losing. And I think that's a  
11 pretty minimum risk when you factor in the potential burdens  
12 that would be placed on the direct selling industry by offering  
13 30 day rescission policy.

14 MR. TOPOROFF: John?

15 MR. BROWN: Just to make sure. What I thought, Dennis,  
16 you were proposing was kind of a multi-tiered approach. Over  
17 \$1,000 it would be rescission, the alternatives of rescission or  
18 disclosure. And then I thought what you were saying is from  
19 \$500 to \$1,000, one would be required to provide, the rescission  
20 would apply. And then under \$500, as it is today, you're not  
21 deemed a biz op for purposes of the Rule. Was that what you  
22 were suggesting?

23 MR. WIECZOREK: Yeah.

24 MR. BROWN: Okay. I don't have a problem with that.  
25 Obviously my position is that it ought to be \$1,000, but, you

1 know, I don't have an objection on behalf of Amway to that  
2 multi-tiered approach.

3 MR. TOPOROFF: Okay. We're going to move on. The next  
4 item that we wanted to mention is, right now in interpretive  
5 guides to the Rule, the Commission has said that it will not  
6 deem to be a required purchase purchases of inventory at --  
7 reasonable purchases of inventory at bona fide or wholesale  
8 prices. Which basically means that investors who want on their  
9 own initiative to buy inventory for resale is discretionary, and  
10 that is not going to be considered a required payment. As I  
11 said, that is only found in the interpretive guides to  
12 Commission policy. Should that be made into an express  
13 exemption?

14 MR. ELLMAN: Yes.

15 MR. BROWN: Yes.

16 MR. TOPOROFF: Well, let's take a vote. Eric said yes.  
17 John said yes. Anybody else care to vote?

18 MR. BENNETT: Yes.

19 MR. GEU: Yes.

20 MR. TOPOROFF: David?

21 MR. FINNIGAN: I'm not sure. I'll pass.

22 MR. TOPOROFF: Okay. Dennis?

23 MR. WIECZOREK: The only issue in my mind is whether,  
24 how to value the inventory. You know, in franchising we're  
25 pretty comfortable that if someone is buying a T-shirt, there's

1 a reasonable basis to determine bona fide wholesale prices. If  
2 someone is buying a diet supplement, nutritional supplement,  
3 whatever, I guess there are ways to compare that, but there are  
4 some things that you can think of where, you know, the bona fide  
5 wholesale price of baby worms. I don't even know. Some of  
6 these things are just not susceptible to that kind of valuation.  
7 So that's the only concern I would have.

8 But I think that this is a big problem with a lot of  
9 the state business opportunity laws is that they don't have, or  
10 I don't know if any of them have an inventory for purchased for  
11 resale at bona fide wholesale prices. I don't know if any of  
12 them have an exemption for that. And that does create a lot of  
13 problems in a more standard manufacturer-distributor situation,  
14 but that's the nature of the business. So, I think it would be  
15 helpful with the caveat that there are some things that in a biz  
16 op sense are somewhat difficult to value.

17 MR. TOPOROFF: John? You have anything to add?

18 MR. D'ALESSANDRO: I have to agree with -- I'd go along  
19 with that.

20 MR. TOPOROFF: John?

21 MR. BROWN: I was just going to say that establishing  
22 bona fide wholesale price can be a challenge, but I think in  
23 terms of defining it and interpreting it, that can be done. And  
24 I don't think it's unreasonable to place the burden on the one  
25 claiming the exemption to prove the point. And if you've got

1 something is called a wholesale price but it doesn't seem to  
2 have any reality in the marketplace in terms of, you know, there  
3 being resales of this item, so how can you, you know, say that  
4 there's a wholesale price. You know, I think if you, for an  
5 exemption, if you place the burden on the party claiming the  
6 exemption to prove it, that that kind of solves that. So that's  
7 my sense of it.

8 MR. TOPOROFF: In your ethical codes or contracts or  
9 anything, is there any provisions that define more specifically  
10 the terms wholesale price, bona fide or purchases, anything like  
11 that, that we could use as guidance either in the text of the  
12 Rule itself or in possible amendments to the interpretive  
13 guides?

14 MR. ELLMAN: No. We don't have anything like that. It  
15 might take a little bit of effort to come up with some kind of  
16 general ideas as to what that might mean, but it shouldn't be  
17 that difficult.

18 MR. BROWN: We don't have really that issue in our  
19 industry, so it's pretty garden variety.

20 MR. ELLMAN: If I may read from the Illinois Franchise  
21 Act, it has an exemption from the definition of a franchise fee.  
22 And among one of those things that a franchise fee does not --

23 MR. TOPOROFF: Can I just --

24 MR. ELLMAN: Sure.

25 MR. TOPOROFF: Are you talking about the franchise

1 regulation or the biz op?

2 MR. ELLMAN: They're all put together. It's put  
3 together. But a franchise fee does not include, among other  
4 things, the purchase or agreement to purchase goods for which  
5 there is an established market price versus an established  
6 market at a bona fide retail price subject to a bona fide  
7 commission or compensation plan.

8 And moving aside just for a second from the issue of  
9 inventory, we had also, I believe, in our comments suggested  
10 that a business opportunity exemption not include the purchase  
11 of a sales kit.

12 MR. TOPOROFF: We're going to get to that.

13 MR. ELLMAN: Oh, we are? Okay.

14 MR. TOPOROFF: It's on the list.

15 MR. ELLMAN: Good.

16 MR. TOPOROFF: Is there any other debate about the bona  
17 fide inventory purchases? Okay. So it was kind of a split  
18 decision whether that should be made an expressed exemption  
19 under the Rule.

20 MR. WIECZOREK: I don't know if it was split.

21 MR. TOPOROFF: Well, on this side from the direct  
22 sellers. David, however, had reservations.

23 MR. FINNIGAN: I don't believe we have that exemption.  
24 And I'm not really too familiar on it, so I'd rather just pass.

25 MR. BROWN: David just wasn't sure about his good



1 feeling about that.

2 MR. FINNIGAN: I guess it was my lunch.

3 MR. TOPOROFF: Well, we're going to move on. And the  
4 next item is the buy back. Right now there is no exemption in  
5 the Franchise Rule for companies that offer any kind of buy  
6 back. The question on the table right now is should there be an  
7 exemption for those kinds? And again, what we're talking about  
8 is in the biz op context, not necessarily a franchise context.  
9 But for biz op sellers, whether there should be an exemption  
10 where companies do offer some kind of buy back.

11 And along with that, I would like to know why in the  
12 Direct Sellers Association is it set at 90 percent, the buy back  
13 policy that you have, as opposed to, let's say, 95 percent or  
14 100 percent?

15 MR. ELLMAN: Let me --

16 MR. BROWN: I'll answer that.

17 MR. ELLMAN: Yeah. Why don't I defer to -- who was  
18 involved in the formation of the rule, the policy, before I got  
19 there.

20 MR. BROWN: I participated in the code drafting  
21 committee that introduced that provision into the DSA Code. And  
22 the reason it's 90 percent, and there are a number of companies  
23 that -- Amway does 100 percent, but allows a 5 percent handling  
24 fee to be charged, depending on the circumstances. Where  
25 there's some costs that are absorbed in doing the buy back, so

1 ours is essentially 95 percent. Some companies, as Mike pointed  
2 out, do 100.

3 The reason it was set at 90 and there was a lot of  
4 discussion regarding that, was you did not wish to have  
5 distributors inventory load themselves. In other words, there  
6 has to be some consequence to making the decision to purchase  
7 inventory. We discourage our distributors from carrying. We  
8 don't want them to have eyes bigger than their stomachs in terms  
9 of inventory. We don't want them to carry a lot of it. If  
10 there's essentially zero risk to carrying inventory, then they  
11 will habitually overbuy because there's no downside to it. So  
12 having, in our case, a 5 percent handling fee or industry-wide  
13 having a 10 percent charge, if you will, is a, we deemed to be a  
14 sufficient impediment for distributors not to overbuy inventory.  
15 And so that was the reason for it.

16 And the reality is for member companies of the Direct  
17 Selling Association, when the buy back is utilized by a  
18 distributor to return merchandise, the hit on the company is  
19 much more than that 10 percent. You know, it's oftentimes the  
20 loss is complete. Because even though the products are saleable  
21 in the hands of the distributor, when it got back to the company  
22 it was not something that they could realistically repack into  
23 its inventory and then sell it to another distributor.

24 So, the company doesn't win on that deal at all, but it  
25 does serve as an impediment for distributors not to overstock

1 inventory.

2 MR. TOPOROFF: Are there any terms and conditions to  
3 the refund? Are there any circumstances where the companies  
4 just will say, sorry, you're not entitled to a refund?

5 MR. ELLMAN: And there are a couple of instances. Yes.  
6 One, it has to be commercially resaleable, meaning that it's got  
7 to be packaged essentially in the same form as it was received  
8 by the consumer, which, I think, makes perfect sense. And  
9 secondly, if an item is seasonal, if it's a holiday item, you  
10 can't return it the following August. Or if it's a special  
11 promotion, a one time kind of promotion, it cannot be returned  
12 either because it's still not resaleable. Those are essentially  
13 the only restrictions.

14 MR. TOPOROFF: So, for a seasonal item, is there a time  
15 period that they could get the refund or no refund at all?

16 MR. ELLMAN: That's not spelled out in our code. We  
17 have a code administrator who is independent of the DSA who is a  
18 former FTC staff person.

19 MR. TOPOROFF: Anybody I know?

20 MR. ELLMAN: I don't know. Bill Roan. But anyway, he  
21 is a former FTC staff person. And he is in charge of  
22 interpreting the code. And I really honestly couldn't speak for  
23 him and what his interpretation would be as to whether there's a  
24 three months, six months, or what have you.

25 MR. TOPOROFF: And on the special items, is that also

1 the same price?

2 MR. ELLMAN: Again, it's the same price.

3 MR. BROWN: Again, the code committee that drafted the  
4 provision was advised by a number of member companies,  
5 particularly Christmas items, they pointed out that those  
6 realistically could not be supported by the buy back rule, but  
7 that what they did in those circumstances was they would  
8 disclose up front that this was a Christmas item not subject to  
9 the buy back. And so, by virtue of the rule, if someone has  
10 items and they happen to be Christmas items but they don't  
11 designate those, you know, disclose those to the distributor as  
12 not being subject to the buy back, then the buy back would  
13 apply, because you failed to specify those as, you know,  
14 seasonal or special items.

15 And quite frankly, again, from the industry  
16 perspective, it was understood that this would be a limited set  
17 of products. For the vast majority of products, the vast  
18 volumes of products that distributors purchased, you know, they  
19 would be subject to the buy back. So, for purposes of an FTC  
20 Rule, things would have to be more explicitly stated. You know,  
21 because you don't have the same industry practices market-wide  
22 as we do in our particular segment of industry. Bottom line is  
23 that that's the way it works in our situation.

24 MR. ELLMAN: Let me just point out. In the interests  
25 of the disclosure, is that when a customer, or I shouldn't say

1 customer, when a direct seller is returning inventory, the  
2 companies will many times, and it is permissible under the code,  
3 to deduct from that 90 percent that's due back any commissions  
4 that have been paid on the sale of that product. For example,  
5 if a direct seller sold product, or let me say, if the direct  
6 seller purchased products from the direct selling company and  
7 then that direct seller turned around and sold it to another  
8 direct seller, and the second direct seller. Now, I've  
9 completely lost my train of thought.

10 MR. BROWN: Why don't you let me finish it.

11 MR. ELLMAN: Why don't I defer to the imminent John  
12 Brown to finish this.

13 MR. BROWN: Distributors on volumes of product will  
14 receive certain commissions. It's assumed that the product will  
15 be resold to consumers. And so, in effect, they're getting  
16 their compensation for the sale based upon the volume of product  
17 purchased. If some of that product comes back, then the amount  
18 of commission that was paid, assuming that the product was going  
19 to be sold to a consumer, that will be deducted or backed out.  
20 But in effect, that's another way of looking at it is that the  
21 person is going to get their net price returned to them.

22 MR. TOPOROFF: Does that hold true with you, Eric?

23 MR. ELLMAN: I couldn't have said it better myself.

24 MR. TOPOROFF: I understand. Does that hold true where  
25 the product, let's say, was sold to the end user consumer and

1 then the consumer in turn brought it back for a refund and then  
2 it made its way back up the chain? Would that work?

3 MR. BROWN: In that case what happens is the companies,  
4 in our case we call it satisfaction guaranteed. That's not an  
5 inventory buy back situation. That, instead, is a customer  
6 satisfaction, or in some cases, maybe a cooling off situation,  
7 but in our case a satisfaction guaranteed. In that case, the  
8 distributor gives the money back to the consumer pursuant to  
9 their satisfaction guaranteed, and then we recompense the  
10 distributor. And then we get the product back.

11 MR. TOPOROFF: Because the policy is basically talking  
12 where it never leaves the system?

13 MR. ELLMAN: That's right. Otherwise, when it's in the  
14 hands of the consumer, then it's considered a consumer  
15 transaction.

16 MR. TOPOROFF: Any thoughts on the issue on the table?  
17 And that is, whether the Commission should consider an inventory  
18 buy back refund policy exemption to the Rule?

19 MR. WIECZOREK: What are you going to do with the state  
20 laws that deal with this issue by saying that a required buy  
21 back makes you a business opportunity under the statute?

22 MR. TOPOROFF: Well, that's something we'll have to  
23 consider, obviously. But in isolation, if we just look at the  
24 Federal Trade Commission and what it's doing, does that make  
25 sense to have that kind of exemption?

1 MR. WIECZOREK: Yes.

2 MR. BROWN: Well, obviously my vote is yes. And we  
3 would hope for the -- to address the question about what about  
4 the states. We're hoping that the FTC takes a lead role in this  
5 and will serve as a model for states to follow.

6 MR. TOPOROFF: Okay. The next issue is the purchase of  
7 not-for-profit kits. Did I characterize that correctly?

8 MR. ELLMAN: That is correct.

9 MR. TOPOROFF: Demonstration kits.

10 MR. ELLMAN: Sales aids and other sales materials.

11 MR. TOPOROFF: Before we discuss whether that's a good  
12 idea for an exemption or not, can we just explain what that's  
13 all about. How's that?

14 MR. ELLMAN: Sure, absolutely. In the direct selling  
15 situation, direct sellers, in order to, many times, to start  
16 their business, will purchase, in many cases, are required to  
17 purchase a sales kit. And that sales kit can be from anywhere  
18 between \$50 or several hundred dollars. And that sales kit will  
19 include, oftentimes, a number of things. It will include some  
20 brochures, product brochures, and otherwise. It will oftentimes  
21 include, it will occasionally include the marketing plan. It  
22 will include videotapes that will be used to demonstrate  
23 products to potential customers. It can also include samples as  
24 well, product samples, not only for the direct seller to use,  
25 but also, more importantly, to give those samples to customers

1 to help them decide whether or not they want to go ahead and  
2 purchase this product.

3 So, that's essentially what we're talking about here.  
4 It can include a number of sales aids, all of which, again, are  
5 also subject to our DSA buy back policy, which not only includes  
6 inventory but also sales aids, as long as it's reusable, again,  
7 would be subject to the repurchase policy. So that's what we're  
8 contemplating by the issue of sales kits.

9 I can't remember now what the percentage, but I believe  
10 a strong majority of states' business opportunity laws have  
11 exemptions for sales kits purchased at a bona fide wholesale  
12 price. And I think our business would request such a practice,  
13 as would the consistency of the current practices at the state  
14 level.

15 MR. TOPOROFF: Let me ask you. How often is it the  
16 case that direct sellers actually offer these kits at a  
17 not-for-profit rate?

18 MR. ELLMAN: I would say very, very little. The vast  
19 majority of companies, and perhaps the entire membership of the  
20 DSA, offers sales kits at wholesale prices.

21 MR. GEU: We offer them basically at cost and the  
22 retail price is probably three or four times that.

23 MR. TOPOROFF: So this exemption would really be very  
24 narrow.

25 MR. BROWN: The notion behind it was that there are a



1 few companies in the direct selling industry who strictly follow  
2 a not-for-profit offering of a sales kit. They can prove to  
3 you, they can establish, in other words, they can prove the  
4 exemption, if there were such an exemption, that they earned  
5 absolutely no profit on the sale of their kit to new  
6 distributors. And the feeling was that it would be a  
7 particularly perverse fraud that would do it on a not-for-profit  
8 basis. In other words, you know, no one's going to commit a  
9 fraud on a not-for-profit basis. Frauds are committed, you  
10 know, to earn money. Therefore, for those companies they just  
11 shouldn't be subject to the Rule because they're offering a  
12 sales kit at cost, not for profit.

13 MR. TOPOROFF: So if we wanted to focus on exemptions  
14 that would really alleviate the disclosure burden, let's say, on  
15 direct sellers, am I correct in understanding that this  
16 not-for-profit purchase of kits is really not a high priority  
17 item?

18 MR. ELLMAN: Well, I think it's important in a number  
19 of respects. It's certainly not as high as thresholds, as are  
20 thresholds, but it is important for a number of reasons. One,  
21 because it would be consistent with state regulation in this  
22 regard. And it would also aid those, and it is important  
23 because it's not really, if you want to cut down on fraud, one  
24 way to do it is to exempt those companies, those operations that  
25 are not fraudulent and the way to not operate as a fraud is to

1 not operate with any kind of profit.

2 And I think, as I recall, the interpretive guides seem  
3 to suggest as well that you want to exclude sales kits in  
4 addition to inventory. And I think these are all current  
5 Commission practices, so it would not be any significant stretch  
6 for the Commission to take what is currently in practice and put  
7 it and give it the full force and effect of the regulation.

8 MR. TOPOROFF: Okay. Any discussion on this item? Any  
9 pros, cons, any other concerns? The possibility of an  
10 exemption? Okay.

11 I want to go back to -- all right. One last thing, and  
12 that is, should there be an exemption for a sophisticated  
13 purchaser. In addition to having a minimum threshold, should  
14 there be a maximum where if a purchaser buys something, let's  
15 say, I'll use a ridiculous amount, \$1 million, whether they  
16 should be out from under disclosure? Are there business  
17 opportunities or should we at least consider the possibility  
18 that there are business opportunities that really may be at the  
19 high end and that those are not the kinds of folk, those  
20 investors are not necessarily the kind of folks that are going  
21 to get scammed or whether there's even a history of abuse in  
22 that high area? Is that something we should consider?

23 MR. WIECZOREK: Yes. But there's two aspects to it.  
24 One would be a high-priced opportunity. The other would be a  
25 sophisticated investor who buys anything. So that if someone

1 has a net worth of \$1 million, for example, that person should  
2 not be protected if he's buying a \$5 business opportunity or a  
3 \$1 million business opportunity. And then, in addition, someone  
4 who's buying a business opportunity priced over a certain level,  
5 say it's \$100,000 or \$50,000 or \$1 million, whatever it is, that  
6 that should also not be regulated.

7 In theory and probably in practice, people buying those  
8 opportunities are sophisticated. They have the advice of  
9 counsel. They know what they're getting into and they don't  
10 need these protections.

11 MR. TOPOROFF: Do the state statutes address this?

12 MR. WIECZOREK: Yes, some of them do. I think the more  
13 modern ones, again, Illinois, the model act you have.

14 MR. TOPOROFF: What does Illinois say?

15 MR. BROWN: The realm of covered groups or business  
16 opportunities is from \$500 to \$50,000.

17 MR. TOPOROFF: That's the cost of the opportunity?

18 MR. BROWN: The cost of the opportunity. Now, in terms  
19 of the net worth of the individual, I would defer to Dennis and  
20 his knowledge of the statutes.

21 MR. WIECZOREK: It's based on the model act pretty  
22 clearly. The purchaser with a net worth of not less than  
23 \$250,000.

24 MR. TOPOROFF: This is the Illinois statute?

25 MR. WIECZOREK: Illinois statute. Immediate cash

1 payment of over \$25,000. If the immediate cash payment does not  
2 exceed 20 percent of the purchaser's net worth, exclusive of  
3 certain things. There's a number -- there may be others that  
4 I'm missing, but there are several related to that. And other  
5 states have similar sophisticated investor exemptions, either  
6 based on the investor or on the price of the business  
7 opportunity.

8 MR. TOPOROFF: Before we move on and on, I'm going to  
9 turn the mike, so to speak, back to Myra to give us a preview of  
10 what's coming down the road. But before we do that, I just want  
11 to give everybody any other opportunities at the table and also  
12 on the sidelines to comment on any of the issues that we have  
13 addressed today. Dennis?

14 MR. WIECZOREK: I'm sort of surprised we're not talking  
15 about more exemptions. And maybe you've already made some  
16 decisions. But I've got a list of 20 here based on biz op laws  
17 and other situations that I think are deserving of  
18 consideration. I won't recite all of those.

19 MR. TOPOROFF: Can I make a suggestion?

20 MR. WIECZOREK: Yes.

21 MR. TOPOROFF: Could you file that with us as a  
22 supplement to your comments?

23 MR. WIECZOREK: Sure. Except that there's one that's  
24 particularly important. That is, an exemption that is common in  
25 many of the biz op statutes, and that's a large company

1 exemption, a large offeror exemption. And that is not something  
2 that the Rule has now. A number of franchise laws have large  
3 company exemptions. A number of state business opportunity laws  
4 have large company exemptions. And that's very useful in some  
5 of the distribution contexts that we were talking about earlier.

6 MR. TOPOROFF: How does that work?

7 MR. WIECZOREK: If the biz opportunity seller has a net  
8 worth of \$5 million or greater or \$10 million or greater,  
9 they're not required to comply with the law.

10 MR. TOPOROFF: And how does that protect consumers?

11 MR. WIECZOREK: It doesn't protect consumers in the  
12 direct sense, but the assumption is that a large company that is  
13 selling business opportunities or franchises is --

14 MR. TOPOROFF: Legit?

15 MR. WIECZOREK: Is legit, yes.

16 MR. BROWN: Or at least they can't hide. They're too  
17 big to hide.

18 MR. WIECZOREK: Have substantial net worth. If there  
19 is litigation, they can satisfy that. It's unlikely they'll go  
20 away. They can argue about the dollar amount, but the idea is a  
21 substantial seller exemption. And that's fairly common in a  
22 number of the business opportunity laws. And then otherwise, I  
23 won't mention the rest, but I would assume that a number of the  
24 exemptions that are in the Rule now would carry over from the  
25 franchise and biz op rule to a biz op rule so that there would

1 be the availability of the exemptions for partnerships,  
2 employer-employees, fractional businesses, et cetera. That  
3 would be helpful.

4 MR. TOPOROFF: As a general proposition, I would say  
5 that that's going to look good.

6 MR. WIECZOREK: And to the extent that there are others  
7 that I suggest, I'll put that in writing.

8 MR. TOPOROFF: Please do.

9 MR. WIECZOREK: Okay.

10 MR. TOPOROFF: Also, if anybody has anything else that  
11 they want to supplement their comments or submit additional  
12 comments, again, please do.

13 I just want to make sure. Is there anybody among the  
14 observers who wish to offer comment? No? Okay. I'm going to  
15 turn it back to Myra.

16 MS. HOWARD: All right. Just a real quick preview of  
17 what's ahead. As you know, we're planning a meeting in Dallas.  
18 The plan there is to pretty much build on what we've talked  
19 about here. We expect that we'll do sort of a brief version of  
20 what we've done here there. So, for instance, the full day  
21 today will probably comprise about a half a day to give those  
22 people opportunity to also comment on these issues. But we'll  
23 be able to incorporate suggestions and thoughts that have come  
24 out of today's to help speed that along.

25 And then the basic goal is to start fleshing out some

1 of these issues in further detail, and start really looking at  
2 some specifics. Talk more about, for instance, exclusions.  
3 Talk more about inclusions. And also to really look at the  
4 idea, the concept of earnings claim issues.

5 So, the idea was today to be a little bit more on the  
6 general level. Next time in Dallas to get a little more  
7 specific. And then in Washington, to really be looking at very  
8 specific proposals that will get us on the way to a Rule  
9 proposal.

10 One thing I'm wondering. I guess you asked this off  
11 the record, but is anyone here planning on going to Dallas  
12 and/or Washington for further discussions?

13 MR. ELLMAN: Well, I know that if you're planning on  
14 having a session in Dallas, the Direct Selling Association will  
15 be there. We do have a number of member companies headquartered  
16 in the greater Dallas area. I don't know that they're  
17 particularly anxious to participate, but that remains to be seen  
18 at this point.

19 MR. TOPOROFF: Well, I think it's fair to say that the  
20 response that we got for the Dallas meeting at this stage, and  
21 it is about two months away, is minimal. There might be a  
22 handful of people in Dallas. I could think of maybe at this  
23 point, maybe three or four at most who requested to participate.  
24 I don't know in the next few weeks or so whether we'll get more  
25 requests or not, but we may reconsider whether it's worthwhile

1 to hold the meeting in Dallas and perhaps we'll skip. And  
2 certainly we'll have the second meeting where people can offer  
3 their comments on the record. That we intend to keep. Perhaps  
4 we'll just have a more substantive discussion in Washington, and  
5 we'll keep everybody posted.

6 MS. HOWARD: The plan now is to have a session, but I  
7 think we will contact those people who have expressed interest  
8 to make sure they're still interested and then take it from  
9 there.

10 MR. WIECZOREK: The difficulty for us is that if you  
11 have three meetings and you would like our participation in  
12 terms of drafting and getting more specific, it's more difficult  
13 to attend three than it is two.

14 MR. TOPOROFF: Sure.

15 MR. WIECZOREK: If you cancel Dallas and have  
16 Washington, I'm sure that will be a lot easier to do than to go  
17 to all three.

18 MS. HOWARD: Okay.

19 MR. TOPOROFF: Well, another alternative is to have  
20 this kind of meeting in Dallas with a whole different set of  
21 participants and then combine the two groups, if you will, for  
22 the Washington meeting. That has yet to be determined, but  
23 we'll keep people posted.

24 So, I want to thank everybody for being here today. I  
25 know it's been a long day. And we really appreciate your





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C E R T I F I C A T I O N   O F   R E P O R T E R

DOCKET/FILE NUMBER: R511003

CASE TITLE: Franchise Rule

HEARING DATE: August 21, 1997

I HEREBY CERTIFY that the transcript contained herein is a full and accurate transcript of the notes taken by me at the hearing on the above cause before the FEDERAL TRADE COMMISSION to the best of my knowledge and belief.

DATED: 9/5/97

\_\_\_\_\_  
MARY FRITZ

C E R T I F I C A T I O N   O F   P R O O F R E A D E R

1           I HEREBY CERTIFY that I proofread the transcript for  
2 accuracy in spelling, hyphenation, punctuation and format.

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SARA J. VANCE

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