



U. S. Department of Justice

Civil Division

Washington, D.C. 20530

July 12, 2006

Federal Trade Commission
Office of the Secretary
Room H-135 (Annex W)
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580

Re: Business Opportunity Rule, R511993

Dear Mr. Secretary:

These comments on the Federal Trade Commission's proposed trade regulation rule entitled "The Business Opportunity Rule" are submitted by the Office of Consumer Litigation of the United States Department of Justice. The Commission's Notice of Proposed Rulemaking asks that comments refer to Business Opportunity Rule, R511993. We appreciate the opportunity to comment on the proposed rule.

As the Commission well knows, the Office of Consumer Litigation has litigated scores of civil penalty actions against sellers of fraudulent business opportunities offering everything from vending machines to mini-ATM machines.¹ We have also prosecuted dozens of individuals for their involvement in such fraudulent ventures, invoking the contempt powers of the court as well as the federal criminal code.² In the decade we have been intensively involved in this work, we have become intimately familiar with the workings of fraudulent business opportunity hucksters. We have brought this expertise to bear in reviewing the notice of proposed rulemaking for the new Business Opportunity Rule which is slated for 16 C.F.R. Part 437. Federal Trade Commission staff has done an excellent job of distilling the current Franchise Rule requirements to their essence in the context of business opportunity sellers, and devising a simpler and hopefully effective rule to regulate the sale of this frequently abused marketing system.

Section 437.5(e) of the proposed rule prohibits misrepresenting that any governmental entity, law, or regulation prohibits a seller from furnishing earnings information to a prospective purchaser. It would be useful to prohibit, in addition, misrepresenting that the law forbids

¹ Beginning with "Operation Telesweep" in 1995, this Office has filed 61 complaints alleging Franchise Rule violations by 145 defendants, both corporate and individual.

² Since 1995, this Office has brought criminal charges against approximately 43 individuals related to contempt of court or fraud in the sale of business opportunities.

disclosure to potential purchasers of the identity of other purchasers of the business opportunity. We are aware of numerous fraudulent business opportunity sellers who deflect consumer requests for current distributors by falsely claiming that the law forbids disclosing their identity, which, of course, is exactly opposite of the truth.

Section 437.5(r)(2) prohibits a seller from failing to disclose any personal relationship or any past or present business relationship, *etc.*, but does not say with whom it is a failure to disclose such a relationship. Presumably this refers to the same people involved in section 437.5(r)(1). It might be best to restructure this section to provide:

- r) Fail to disclose, with respect to any person identified as a purchaser or operator of a business opportunity of the type offered by the seller:
 - (1) Any consideration promised or paid to any such person. Consideration includes . . . ;
 - (2) Any personal relationship or any past or present business relationship other than as the purchaser or operator of the business opportunity being offered by the seller.

It would be useful if the disclosure document, Appendix A, was captioned "BUSINESS OPPORTUNITY DISCLOSURES REQUIRED BY FEDERAL TRADE COMMISSION, 16 C.F.R. PART 437." In order to obtain civil penalties for rule violations, we must prove "knowledge or knowledge fairly implied on the basis of objective circumstances that such act is unfair or deceptive and is prohibited by such rule." 15 U.S.C. § 45(m)(1)(A). Having the suggested language in the caption would help us show the knowledge required by this statute in civil penalty actions. We have seen many business opportunities that were established by individuals who worked at prior business opportunity sellers. They employ a disclosure document that follows the format required by the current FTC Franchise Rule. They claim that the disclosure document merely copies what a former employer used. If the disclosure document includes reference to the FTC and the Rule, this eliminates any significant question as to whether the defendant had actual or implied knowledge as required by the statute.

Page 41 of the Notice of Proposed Rulemaking says that "providing locations" includes "an offer to furnish a list of locations" and "providing a list of locators." Section 437.1(n) of the proposed rule defines "Providing locations, outlets, accounts, or customers[.]" That section does not explicitly incorporate "offer to furnish a list of locations" and "providing a list of locators." While the language of section 437.1(n) is broad enough to encompass offering to furnish a list of locations or providing a list of locators, it would be useful if it explicitly incorporated these two phrases. We are certain that unscrupulous business opportunity sellers, or their lawyers, will attempt to draw a distinction of some sort between, for example, "suggesting" a locator, which is explicit in the definition, and "providing a list" of locators, which is what many fraudulent business opportunities do. We would prefer to avoid that argument.

The Notice of Proposed Rulemaking solicits comments on balancing the need to enable prospective purchasers to verify sellers' claims with privacy concerns (NPR, p. 55). Specifically, the NPR seeks comments on whether the Rule should permit purchasers the opportunity to opt-out of the disclosure of their contact information. The Rule should not permit such an opt-out. It would be an easy matter for telemarketers to talk consumers into opting out, describing to them what a hassle it becomes for those who do not opt-out because of all the demand that arises for their time and attention. Indeed, this could become part of a fraudulent inducement to buy the business opportunity, since the discussion would stress how great the demand for the opportunity has become in light of the success of the existing distributors. Consumers could well be left with a contrived list of references made up of shills and paid references. The only useful list of references is one that includes a grouping of genuine distributors that the opportunity seller cannot shape. The existing Franchise Rule includes such a requirement; it should not be watered down.

The NPR requests comment on whether business opportunity sellers should be permitted to add to the mandated disclosure document materials required by state disclosure laws (NPR, pp. 62-63). While the states may wish to impose additional disclosure obligations on business opportunity sellers, those additional disclosures should be in a separate document and not be permitted to clutter the federally required disclosures. The single short disclosure document the proposed rule requires presents in one place crucial information presented in a concise format. Purveyors of fraudulent business opportunities will seek every opportunity to water down this document with extraneous information to hide any negative information it may contain. Consider the disclosures under the current Franchise Rule that some such sellers who are subject to federal court orders arising from Franchise Rule litigation make. Rather than simply listing the order and describing it as the Franchise Rule requires, it is common, where the disclosure requirement is not simply disregarded, for sellers of fraudulent and questionable business opportunities to recite in the disclosure document that "None of the firm's officers, directors, or controlling employees are subject to any federal court order, etc., etc., etc." The "not subject to" discussion goes on at length, and ends with a brief "except for . . ." disclosure of the relevant order. Presumably the intent of this method of disclosure is to minimize the impact of the federal court order, and, indeed, to provide a long and boring description denying any relevant orders so that the consumer will give up reading before even finding the actual disclosure. Nothing more than required or allowed by the current draft of the business opportunity rule should be permitted to similarly dilute the required disclosures.

I hope you find these views helpful. If you have any questions, do not hesitate to contact me.

Sincerely,

Kenneth L. Jost
Assistant Director
Office of Consumer Litigation