from being an adversary of consumers and consumer groups to being a friend, a partner, a protector.

Concerns About a Code

What would a code of ethics produce for DSA members? Pros and cons were often discussed, with the pros following mainly from the above two motivations -- it might pre-empt any serious legislative or regulatory invasion of the industry and it might reestablish the legitimacy of this business method in the eyes of consumers. The cons were, of course, the major concerns.

The thought of a code of ethics with administrative procedures and compliance mechanisms was distressing to some DSA members who had built their businesses from scratch, valued their independence, and wished to avoid interference from outsiders. A tacit belief in the fundamental philosophy of *caveat emptor* undoubtedly resided in the minds of a few. Some argued that problems with their customers were best kept within their own companies and handled in their own way. Some felt that they had sufficient safeguards, perhaps even their own ethics codes, to insure their own proper behavior. Many in this business were strongly entrepreneurial and thus disdainful of conforming to some broader and imposed industry standard. It is possible that some of these feelings also strongly implied a fear of getting caught up in internal industry politics. For example, could some other DSA member who was jealous or angry at my success make trouble for me by raising questions of my company's ethical behavior?

A second category of concerns involved legal issues. While it was possible that a strong ethics code might reduce or eliminate burdensome legislation, might it not also raise regulatory scrutiny regarding antitrust and restraint of trade issues? How strong must the code and its enforcement procedures be to give it sufficient "teeth" in the eyes of concerned regulatory bodies? Will a code strong enough to dissuade or punish improper practices need to be so strong as to intimate the likelihood of repressing competitors who are association members? And if it lacks sufficient "teeth" to avert or rectify the ills, of what value is it?

A third set of concerns centered around the independent contractor status of direct selling company salespeople. Because of their independent legal status, perhaps they would not abide by any ethics code anyway, especially those most prone to violate it. Even if a DSA member company were to make a sincere attempt to enforce the code, the time, effort, and cost necessary might be enormous. Further, since many companies recognized that they were really competing among themselves for good salespeople as much as or more than for customers, there was a fear that an ethics code and its associated implications and controls might drive away good salespeople from their firms. Conversely, some felt that this was precisely the reason why an ethics code was needed -- since a company has more direct control over its own employees and needs a mechanism such as this code to exert strong informal control over its independent contractors.

Finally, some industry members were troubled because they felt that the creation and promotion of a code of ethics was an admission of past guilt. After all, by joining DSA a company was overtly declaring an association with the "good guys" and a separation from the "bad guys" in the direct selling business. Now the striving to designate DSA members as ethical organizations might cast doubt that such was the case in the past. Further, there were many more direct sellers who were not DSA members than those who were members, and the code of ethics would not necessarily be honored by those outsiders who would then continue to blemish the image of direct selling.

Shaping the Code

The challenge to Brouse and DSA was three-fold: to formulate a code of ethics that would (a) resolve differences among DSA members, (b) assuage the objections of government officials, and (c) eliminate consumer injustices or misunderstandings and overturn any that occur. Succeeding in this challenge required vigorous efforts on two fronts -- internally with members and externally with regulators.

Internal Activities. The underlying philosophy of association leaders regarding code discussions might be termed "inclusive," meaning that members on all sides of the issue, representing firms with and without ethical problems in their histories, be included in the deliberations. Opportunities for debate were frequent and open. At each quarterly Board meeting, for example, the Code of Ethics Subcommittee under the leadership of James Doyle of Watkins Products, Inc., made a progress report, sometimes offered motions, and always entertained discussion.

Prior to the September 1969 meeting, the initial draft of the code was sent to Board members. Following some slight revisions at the meeting, Doyle moved its adoption. This first official attempt to install a code of ethics failed to pass, but the message was clear that a code of ethics was in the offing.

As the discussion about a code of ethics became more prevalent at Board meetings as well as informally between members, three positions emerged. Those favoring the code for the various reasons already noted occupied the first position. The second position encompassed those rather adamantly opposed. A third position was somewhat a compromise, with its members alleging that other DSA documents and statements already existed that made any new code redundant and unneeded.

Those strongly opposed to the code as being developed were not opposed to a statement of ethical standards itself, but rather had serious concerns about its administration. In particular, there was deep concern about enforcement procedures and the damage that could happen to a member firm accused of a code violation. For instance, the requirement that facts or documents pertinent to the issue at hand must be obtained and disclosed in any hearings or proceedings -- the legal process known as discovery -- might undermine a company's privacy or competitive position as well as prove embarrassing and even provide government agencies and regulators with ammunition for further legal pursuit. If sensitive facts or documents were not kept confidential, the subject firm might be placed in jeopardy.

Other negative feelings stemmed from the expected cost of administering a code. DSA members had recently seen a sizeable increase in dues because of the move, staff expansion, and other activities, and most were not sympathetic to a still larger dues payment to finance the administration of a serious code of ethics program. Perhaps these people felt that many instances of code violations would ensue, causing great travel costs, legal fees, and other administrative support costs. The opposition to that argument was simply that the presence of a code would reduce association expenses because its Washington lobbying effort could be reduced. A particularly troublesome point to some was the consequences to DSA if a member firm was accused and "convicted" of an ethics violation and subsequently decided to bring suit against DSA.

Many of these issues required careful treatment in the final administrative rules accompanying the code of ethics. Those representing the third position may have felt many of these same problems, but rather chose to build on existing statements inherited from NADSC. Some members in this latter group argued that DSA already had a statement of ethical behavior to which its members subscribed, and thus a new code of ethics was not needed. That statement was contained in a document titled "The Right Thing To Do," devised jointly by NADSC and the National Better Business Bureau in the very beginning of Brouse's tenure in early 1969. It was, in essence, a code of ethics, and treated many issues of salesperson-customer relations. The text of this document, found in Appendix C, was derived largely from the model consumer protection act proposed by the NADSC at the 1968 FTC hearings on consumer protection (see Part One).

Others taking this position suggested that the much shorter "Declaration of Principles," which was inherited from NADSC and reproduced in Part One, be used as the foundation of an ethics code and improved upon, if necessary. In fact, that declaration, renamed "Statement of Principles," was then currently circulating and attached to the DSA membership rosters, so it had not been forgotten as was the 1940 code shown in Appendix A. But neither "The Right Thing To Do" nor the "Statement of Principles" did what the emerging code of ethics was destined to do. The proposed code differed in two fundamental and critical ways by (a) making code compliance mandatory, not voluntary, and (b) providing detailed procedures for enforcing the code and dealing with complaints or accusations.

External Activities. Self-regulatory codes were not new, though most of those proposed previously by various associations did not maintain viability after FTC scrutiny. Gilbert was aware of this risk, having studied Commissioner Elman's statements and other FTC rulings. Gilbert sought the advice of William D. Dixon, formerly of the FTC Division of Advisory Opinions, for two good reasons. First, it was this FTC Division to which any DSA code would subsequently be presented for evaluation and approval. Second, while in this FTC position, Dixon wrote an analysis of past FTC advisory opinions on the topic of self-regulation (Dixon 1968). Many interesting cases had been scrutinized, ranging from the Sugar Institute case in the 1930s in which the Supreme Court recognized the desirability of association self-regulation, to numerous code proposals in the 1960s. Among the associations and issues involved were the Fashion Originators Guild in 1941 and the question of suppression of competition, the Associated Press in 1945 and its uses of fines and expulsion of members, the New York Stock Exchange in 1963 and its problem with inadequate due process, and the ethics code devised by the Paid-During-Service Magazine Subscription industry in 1967. The latter case was of particular relevance to the DSA situation as already noted earlier and in Part One, and received detailed attention in Dixon's analysis.

From a legal and regulatory perspective, it became clear that any DSA code must, if it were to gain FTC approval and serve as the desired deterrent to troublesome government regulation, pass three fundamental tests. It must (a) provide for due process; (b) not thwart competition as a result of imposing fines or other penalties for violations of code provisions; and (c) be sufficiently potent to make it meaningful to consumers and serious to association members.

These tests were carefully incorporated into the administrative policies and complaint procedures attached as integral parts of the code document. For instance, competition would be protected because the administration of the code and any complaints occurring would be handled by an independent code administrator, not affiliated with any DSA member company. To insure due process, if a complaint could not be resolved by discussions between the code administrator and the company involved, a hearing process would be instigated. Members of the hearing committee would be chosen so as to exclude any competitors of the accused firm, and the hearings would be confidential and closed to all outsiders including all other DSA members. No specific sanctions were to be administered, except that if a violation of federal or state law is deemed to have occurred, the administrator will, after properly notifying the accused, inform the federal or state government agency and cooperate in any further governmental investigation. The latter certainly offered a conspicuous degree of potency.

Final Adoption of the Code

The final adoption of the code of ethics occurred in three separate actions. The substantive provisions of the code were approved first at a Board meeting in March 1970. The procedural provisions gained approval at the next Board meeting in June. The entire code was then placed before the annual meeting of DSA later in June, where it was discussed and endorsed by a vote of the full membership.

March 1970 Board Meeting. On March 13, 1970, the Board of Directors of DSA met at the Barclay Hotel in New York City. Ethics Subcommittee chairman Doyle gave an initial report summarizing the development of the code to that day and describing the code provisions. Because he wanted to participate actively in the discussion, Board Chairman Sheridan relinquished the gavel to Mr. E. Cabell Brand, a Board member from The Stuart McGuire Company, Inc. A lively discussion ensued.

Concerns expressed by Board members summarized and focused the concerns voiced in many earlier discussions. Sheridan started the discussion by noting the high costs necessary to administer the code, perhaps requiring an increase in member dues. He also expressed concern about the possibility of attracting government intervention if a code were proposed, and predicted that DSA would face litigation if a member company were expelled from the association because of a code violation. Others responded to his points, suggesting that costs now directed to various legislative programs might be reduced and that expulsion of a member was not provided for in the code.

Each Board member was then asked to express his views on the code. The points made are summarized as follows:

- The code would do much to prevent anti-direct-selling legislation;
- DSA must stand for something and say so;
- The code would be an asset in the promotion of increased membership;
- Worthwhile moves always carry a certain risk;
- "The Right Thing To Do" is sufficient and a code is not necessary;
- It would be better to improve the Statement of Principles and use it to expel violators.

In addition, it was reported that the President's Council strongly favored a code, and that it would be unwise not to give weight to the feelings of these company presidents. One Board member queried if all members had to subscribe to the code. Gilbert responded that technically they would not, but as a practical matter they should or else they could not require new members to subscribe to any code of conduct adopted by DSA. This issue would subsequently be clarified in the next Board meeting.

It should be noted that essentially no discussion related to the substantive provisions of the proposed code -- the standards of behavior that the code addressed. Codes of ethics spelling out behavioral standards were not new to DSA, as evidenced by "The Right Thing To Do" devised in 1969. The wording of the proposed code was more concise, however, as the result of rigorous legal analysis by Gilbert, knowing that it would have to satisfy the scrutiny of the FTC or other government agencies if it became a self-regulatory policy of DSA. How the code provisions were selected was noted in a 1972 memo written by Gilbert to Brouse documenting the history of the code of ethics. Gilbert stated:

> The substantive provisions of the Code were drafted in light of the kinds of conduct that has been subject to criticism by the Federal Trade Commission and other state and federal law enforcement agencies.

There was no apparent disagreement that these standards, covering such issues as guarantees, full disclosure of terms of sale, and deceptive practices were important, necessary, and acceptable. Yet underlying much of the discussion at this meeting and previously in other settings were concerns about how the code would be enforced, reflecting an uneasiness in the minds of many members about their vulnerability to code violations.

No doubt much of this uneasiness stemmed from the use of independent contractors as salespeople, and the fact that the code called for DSA companies to assume voluntary responsibility for the actions of these independent contractors. This was an anomaly that the industry faced -- utilizing sales representatives who are independent businesspeople, not employees for whom the DSA firms are responsible, but at the same time being responsible for their proper and ethical behavior toward customers, behavior that reflects on the DSA firms and company reputations. Too much intrusion might drive these independent reps to sever their affiliation, but too little intrusion might be an implicit consent that "anything goes" in selling behavior.

When the discussion subsided, Acting Chairman Brand presented a motion that the code be adopted subject to preparation of administrative regulations by legal counsel. These regulations together with the code would be mailed to all members prior to the annual meeting in June, at which time a vote would be taken. Subcommittee Chairman Doyle seconded the motion and a vote was taken. Lingering concerns about the yet-to-be-completed regulations sections of the code caused four Board members to vote against the motion, while eleven voted to support it.[2] Mr. Sheridan then resumed the chair and went on to further business.

June 1970 Board Meeting. The next meeting of the DSA Board of Directors was held on June 13, 1970 at the Broadmoor Hotel in Colorado Springs. Ethics Subcommittee Chairman Doyle was absent from that meeting, so Gilbert presented a review of the code, noting that it was approved at the previous Board meeting pending final statements of administrative regulations. He emphasized that the regulations now proposed allowed for substantial due-process safeguards. He also clarified

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[2]Those supporting the motion (and their companies) were Brand (Stuart McGuire), Doyle (Watkins Products), John T. Joyce (C.H. Stuart & Company), Gordon P. King (Hanover Shoe, Inc.), Jules Levy, Jr. (Family Record Plan, Inc.), H. Thomas McGrath (Avon Products, Inc.), John Moses (Luzier, Inc.), Charles E. Nelson (Beeline Fashions, Inc.), Richard C. Polinsky (Minnesota Woolen Company), Joseph H. Stone (Stanley Home Products, Inc.), and A. G. Winfrey (Sarah Coventry, Inc.). Those opposed included Sheridan (Electrolux), William J. Halliday, Jr. (Amway Corporation), Earl P. Mantz (West Bend Company), and Patrick Tahaney (Tupperware Home Parties). Those abstaining included Anthony Ponticelli (Artex Hobby Products, Inc.) and Alvin L. Saeks (Puro Company, Inc.).

that all members of DSA must abide by the code, if adopted, whether or not they overtly subscribed.

Discussion then focused on some administrative provisions. Two amendments were made. One stated that any accused party should receive a copy of any written complaint that included the disclosure of the complainant. The other specified that the only documents that would be turned over to a government agency by the code administrator would be those necessary for prosecution. These amendments were seconded and passed. Again, no discussion was directed to any of the substantive portions of the code dealing with standards of behavior.

The motion was then made by Richard C. Polinsky (Minnesota Woolen Company) to accept the regulations to enforce the code, and the motion was seconded by H. Thomas McGrath (Avon Products, Inc.). The motion passed with only one dissenting vote, that of Board Chairman Sheridan. Apparently the clarification of administrative procedures since the previous Board meeting convinced three of the four previous opponents of the code to change their minds.

Following this vote, the Board approved a resolution requesting the principal officers of member companies to formally subscribe to the code by submitting a letter so stating from their board chairman. This resolution was not made a part of the code regulations themselves, however. A motion was also made and unanimously approved that the code be updated when necessary to constantly improve practices in the marketplace. This action confirmed that the entire Board membership favored the standards of behavior addressed in the code, and that any disagreements reflected in previous votes involved enforcement procedures.

A question was raised about why the Board action approving the code and its administrative regulations be ratified by the full membership at the annual meeting. DSA by-laws specified that Board approval was sufficient for adoption of an association regulation such as a code of ethics. Counselor Gilbert stated that a full membership vote was technically not needed, but was recommended because of the significance of this matter. He also stated that future changes in the code or its regulations would not require full membership ratification.

At this point, DSA had an officially-approved code of ethics complete with administrative regulations and enforcement procedures -- something this association or its predecessor had never achieved in its existence since 1910.

June 1970 Annual Meeting. Shortly after the Board meeting, the Annual Business Meeting of the Direct Selling Association took place on June 15 at the Broadmoor in Colorado Springs. To set the proper mood for considering the code of ethics, Brouse prepared large cardboard cutouts of "Mr. C" and "Mrs. C" (C for customer) who had "problems" with some direct selling experience, and placed them on the stage. When the time came to discuss the code, Gilbert addressed the membership, who had been supplied with copies of the code prior to arriving. He first explained the amendments approved by the Board two days earlier, and then reviewed the regulations section of the code in some detail. Sheridan, who was chairing the meeting, then asked for any questions, and considerable discussion evolved, both on the substantive contents of the code as well as on its regulatory procedures. Some examples of the dialogue are as follows:

- Member: In the past we have had some general understanding in our code which goes to the attitudes of such things as soliciting and hiring of other member company personnel. Is this particular code silent on that or are we going to consider it in discussing our code of ethics?

  Sheridan: The code is silent on that issue, correct Mr. Gilbert?

  Gilbert: Yes, sir.

- Member: I felt that the membership of this organization did not need a code, that those outside the organization were the ones that needed the code, and what was the thinking behind this code in regard to those who are not members; how will this affect them who do need a code but who are not members of this association?

  Sheridan: Jerry, do you want to respond?

  Gilbert: Well, perhaps ....

  Sheridan: (interposing) I will ask Tom McGrath to come up and make some comments.

  McGrath: I think it was the general feeling of the Board that this association existed for quite a number of years and member companies have upheld certain standards in the industry.

  As a matter of fact, the member companies have set the standards for the whole direct selling industry. We thought that this association should have a code of ethics that we could hold up to the world and say that as direct sellers here are the values we believe in.

As an association we have certain standards and there are companies outside the association that might want to join us and we don't have any provision to keep certain companies out of this association because we have no code of ethics. We felt that if companies wanted to join us we are delighted to have them if they are willing to subscribe to this code of ethics.

We cannot be responsible for people who are not members of our association. We would hope that our code of ethics for non-members would point the way to them to be able to live in this industry and preserve it.

We would hope that the standards that we ourselves set would become standards throughout all direct selling, whether they are members of this association or not.

In summary, I say again that we feel it is very important for this association to have ethical standards set before us that we can not only subscribe to but talk about and popularize. We feel that for the future this is vital and essential. I hope that answers your question.

• Member: What happens if the Code of Ethics Committee and the Administrator after referring it to a governmental agency finds that there is a violation, do we expel the member or do we permit the member to operate and act within the membership?

Gilbert: What happens after we have referred the complaint to the government agency and it has been successfully prosecuted, what do we do?

Member: Right.

Gilbert: Nothing. The law is such today, the atmosphere and code of ethics of trade associations, that we really don't have the legal authority to expel a member under that situation.

We have found that the legal position is that at this time we are not ready for it, nor is the Federal Trade Commission ready for it. But we do feel we have gone as far as we can possibly go at this point, and I might add this does give us, from a legal point of view, something to base our actions on.

- Member: Under this code, from whom will complaints be accepted by the Administrator?

Sheridan: From whom will the administrator accept complaints?

Gilbert: From anyone. I doubt very much that government officials really care about our code. If they have got a complaint, they have the necessary tools to deal with it. But as far as the member companies, the Administrator accepts complaints from anybody.

Member: Does that include your own member companies?

Gilbert: Yes.

Member: Anyone who wants to make a complaint can do so?

Gilbert: Yes.

- Member: In the event that the entire procedure were followed and it was found necessary to turn it over to a state or federal agency and the member company was found innocent, would there be any grounds for that member company to sue the association or its members?

Gilbert: Two points to answer that question. One, the code and regulations as adopted by this membership as they are provide that there would be no liability under this code by anyone of the association; and secondly, if you read the regulations you will note that any proceeding under this code, not the code itself, but any proceeding under it and any complaint is to be kept confidential by anyone in the association involved in a proceeding under the code; and even as I explained earlier in the filing of a complaint the only papers that would be filed are those papers, the minimum amount of papers, necessary for the filing of the complaint.

Member: I understand that, but at the same time the association has made complaint of the subject.

Gilbert: Let me go one step further; without this code anyone in this room has a right to make a complaint to a government agency. So long as you have something substantial you have no fear of liability.

When the questions subsided, Sheridan called for a motion to ratify and establish the code of ethics. After the motion was made and seconded, a member questioned having a vote at that time, but rather suggested having a mail vote after each company had an opportunity to review the code and its implications. That statement was taken as a motion, and it was seconded. No discussion was offered, and after an indeterminate voice vote, Sheridan called for members to vote again by standing. The motion to defer voting was defeated, with twelve standing to express favor and twenty standing to express opposition.

After a check to be sure a majority of DSA membership was present, a vote was taken on the original motion to ratify the code. Again, members were asked to stand to indicate their vote, and the result was thirty votes in favor and two votes against. Gilbert noted that he held four additional favorable votes as proxies, and that "some" members present were abstaining. (A subsequent recollection of a DSA staff member noted that the final tally, after all proxies were counted and some undecideds changed their minds was 43 to 30 in favor.)

As a wrap-up to this part of the meeting's agenda, Chairman Sheridan offered these supportive comments:

> Let me reassure you that any people who have misgivings, that there was a division over a period of a couple of years on this issue, and as a consequence of the division, Counsel and the Committee devoted long hours and the Board of Directors devoted many sessions to perfect an instrument, which we think will do credit to this association and to its member companies.
>
> We don't expect any legislative good out of it. We do expect a great deal of public relations good and a great deal of cleaning up in the entire industry, outside

of our association as well as inside it.

If this were just a simple exercise of semantics and we published a code we would be doing ourselves incomparable injury. However, there is every intention of abiding by and enforcing this code of ethics.

These were welcome words from the Board member whose opposition to the newly established Code of Ethics had been most protracted.

The Content and Character of the Code of Ethics

The official and complete statement of the Code of Ethics that was finally approved on June 15, 1970 appears in Appendix D. It contained three major sections: a preamble, a statement of the substantive components of the code of ethics, and a statement of regulations for enforcement.

Code Content. The preamble was simply a declaration that DSA member companies will adhere to the practices described, dealing with their responsibilities toward consumers.

The code section itself detailed in its first five parts the standards of behavior that the code supported. First, product or service offerings shall be described in an accurate and truthful manner. Second, guarantees shall be clearly stated and fulfilled. Third, the terms of sale and the identification of the seller shall be clearly communicated in writing to the customer. Fourth, the direct selling company shall be responsible for any improper conduct of its sales representatives; and fifth, no DSA company shall engage in any deceptive or unlawful practices.

Part six of the code section detailed the administrative policies, noting that an independent code administrator shall be appointed with authority to insure code compliance. This part also reiterated that member companies are responsible for code violations by their representatives, and that if a state or federal law has been violated, the administrator may inform the proper agency and cooperate in whatever action is forthcoming from that agency. Part seven simply stated that code amendments are possible with a two-thirds vote of the Board of Directors.

The section on enforcement regulations spelled out a five-step procedure for dealing with a complaint:

Step 1: Complaint must be received in writing, and is forwarded to the accused party. The administrator conducts an informal investigation.

Step 2: The administrator may (a) terminate action if the charges prove to be insupportable or frivolous, or (b) ask the accused for a response if a violation appears to have occurred; based on the response and/or subsequent action of the accused the administrator may then terminate the charges or notify the accused that he has the right to request a hearing by a special ethics committee.

Step 3: If a hearing is requested the administrator initiates action to form a special ethics committee, and procedures by that committee are carried out including a closed hearing and decision by secret ballot.

Step 4: If the special ethics committee finds that a code violation has occurred, the administrator consults with legal counsel to determine whether a violation of state or federal law is involved. If so, the accused is notified, as is the appropriate federal or state agency, as already noted in an earlier section.

Step 5: This is not really a separate step but rather some procedural stipulations, such as confidentiality of procedures, involvement of direct competitors of the accused, and limitations on what documents would be delivered to a federal or state agency if that became necessary.

Code Character. The focus of this code is consumer protection, reflecting the issues and concerns raised by consumerists in the various books, hearings, and regulatory actions noted in Part One. The Code gave no attention to relationships between the company and its sales representatives or ethical issues relating to sales representatives that do not involve consumers. The first dialogue presented above from the June 1970 annual meeting illustrates one of these issues -- companies hiring other company's salespeople. Later amendments, however, did address some of the problems reflecting company-salesperson relationships.

The Code is also positive in tone. It did not emphasize what not to do, but rather made positive statements -- the offer shall be accurate ... the terms of the guarantee shall be furnished to the buyer ... a written order or receipt shall be delivered to the customer ... etc. Even the statement concerning deceptive or unlawful trade practices is somewhat positive in tone, declaring that "No member company shall engage in these practices. A negative statement would read more like this: "Member companies shall not engage in such behavior." This overall positive tone helped avoid the impression that the Code was an attempt to make its member firms cease and desist from past unethical behaviors.

An important aspect of this code is its mandatory nature. While some association codes of conduct are voluntary (as were the predecessor codes of NADSC), this code required compliance by any firm desiring membership in DSA. A voluntary code often gives rise to the "free-rider" problem whereby a non-complying member shirks the responsibility while ostensibly retaining the affiliation with the ethical image of the industry association.

Finally, this code is strongly focused on supporting legal standards of behavior. Such codes can be characterized as "equilegal" implying that the ethical standards in the code are equivalent to legal standards. One aspect of the Code, however, is arguably above and beyond basic legal standards, or "supralegal." This occurs in the statements of member responsibility for the actions of their independent contractor salespeople. Taking responsibility for the actions of these independent sales personnel was, as already discussed, a controversial issue as the Code evolved, but failure to take this position would certainly have weakened the Code greatly. The consequences of this rather bold step were, of course, yet to be seen.

PART THREE

FOLLOWING THE CODE

Gaining membership approval of the Code of Ethics was a monumental step for the Direct Selling Association, stemming from the combined efforts of DSA president Brouse, counselor Gilbert, directors Brand, Doyle, McGrath, and many others. But the real test of the wisdom of this action was still in the future: What would the code provoke and what would it prevent? Many of the trends described in Part One that were seen as threatening to this industry continued through the decade of the 1970s and beyond.

Thus, one focus of this Part, which is titled "following" the Code, is to review what pertinent events and trends in DSA's marketplace and regulatory environment occurred "following" the passage of the Code, along with their impact on the direct selling industry and especially on some DSA member firms. Of course, it is impossible to know what might have happened instead if the Code of Ethics had not been vigorously debated and approved by DSA members, but it is clear that the problems and issues that served as the genesis of the Code did not wane. The second focus of this part on "following" the Code is to report the DSA actions carried out to insure that the association was "following" the mandate of the Code and to note what activity occurred involving DSA members as the direct result of the Code's existence.

Events and Trends Following Code Enactment

Consumerism. The consumer movement in the 1970s clearly remained vigorous and influential. A major study of U.S. consumers in 1976 perhaps best summarized the state of consumerism in this decade, indicating what government officials were discerning from their constituencies. Based on personal at-home interviews of more than 1,500 respondents across the nation, the study produced some strong conclusions (Louis Harris 1977). Consumers wanted three different kinds of changes. The first was a change in attitudes and perceptions of business managers regarding the sincerity of consumer problems, the extent of their needs, and the high level of their expectations in the marketplace. The second involved specific areas of change, including safer products, better quality and service, better guarantees and warranties, and better complaint handling processes. The third was an improvement in communications with the public by business firms about the steps they are taking to be responsive to consumer problems. In fact, the primary complaint against business was the difficulty of getting complaints and problems corrected.

Other findings from that study were pertinent to issues of direct concern to DSA members. Nearly half (47%) of the consumers interviewed had actually complained at least once during the previous year to a seller about a product or service purchased. Almost the same portion of these respondents (43%) were critical of the benefits they were supposedly receiving from government regulation, and most of these believed that regulation was more beneficial to business than to consumers. The majority (52%) favored creation of a new government agency devoted specifically to consumer advocacy. And finally, when asked their opinion on how effective industry self-regulation might be in comparison to regulatory efforts of the federal government or consumer activists, they gave poorest marks to the self-regulation option and had most confidence in consumer activists to solve their problems. But the full report of this study, which covered ninety pages, made no reference to direct selling, direct salespeople, or any specific direct selling practices.

Consumerism and selling were the subjects of a major *Fortune* magazine article a few years prior to the Sentry study (Burck 1972). It noted that "the art of salesmanship, particularly in its more persuasive and high-pressure forms, is up against the greatest challenge in its long history," and stated how the consumer movement pressured the FTC and other state and local regulatory agencies to intensify their activities in order "to scourge and abolish the abuses of persuasion." Among the specific activities mentioned were the FTC's proposed cooling-off rule (discussed later in this Part), as well as various cooling-off laws and door-opening ordinances passed by thirty-three states and ten cities. The article also noted that DSA, which represents the leading companies in the field, had produced a code of ethics for self-regulation and observed that "the FTC seems to think well" of the Code and related DSA activities to publicize the Code. This was an indirect but welcome indication that the DSA Code had indeed made a favorable impression on the federal regulators.

Direct selling as a business strategy was also making a favorable impression on consumers, as evidenced by its continued sales growth. A *Forbes* magazine article in mid-1971 detailed these growth trends for five large and publicly-held DSA members and quoted Brouse's observations on this trend ("Knock, Knock" 1971). Thus, while consumerism remained a conspicuous and potent force, it had not inhibited the energies of direct salespeople nor thwarted customer willingness to purchase from them.

Regulatory Activities. A number of changes occurred in the FTC in 1970 that would have an impact on this agency's focus and pursuits. Philip Elman, the outspoken advocate of increased regulation, departed as a Commissioner. At the same time, Miles Kirkpatrick replaced Caspar Weinberger as Chairman. Kirkpatrick was known for his strong consumer protection stance, having previously headed the American Bar Association study group in 1969 that reviewed the FTC after the appearance of the highly critical Nader report. That study group had endorsed a more vigorous proactive stance by the FTC instead of reliance on voluntary procedures of self-regulation by industry. As part of a general reorganization of the FTC, The Bureau of Consumer Protection was established and charged with the responsibility of creating trade regulation rules for the protection of the consumer (Hasin 1987). A trade regulation rule is a statement about a specific practice that the Commission views as unlawful, and is formulated and issued after executives in those businesses likely to be affected by the rule are given an opportunity to present their views at hearings. Such statements have the force of law for the industry in question.

The Director of this Bureau was Robert Pitofsky, who would later become an FTC Commissioner in 1978 and FTC Chairman in 1995. Brouse and Gilbert met with Pitofsky in early 1971 to get his reaction to the DSA Code. In a report on that discussion to the DSA Board of Directors meeting in June 1971, Gilbert conveyed that Pitofsky termed the Code an effective one and stated that his office would cooperate in its enforcement. The top priority of this Bureau under Pitofsky involved advertising practices, but a long-continuing concern about a cooling-off remedy for abuses in selling was to receive early attention.

Hearings on a trade regulation rule for a cooling-off period were begun in March 1971 under the direction of William D. Dixon. This was the same William Dixon who had earlier been consulted by DSA counsel Gilbert in the development of the DSA Code, and who was now the Assistant Director under Pitofsky in the Bureau of Consumer Protection. The issues addressed by this proposed rule were stated as follows ("Cooling-Off Period for Door-To-Door Sales" 1972):

> The complaints of consumers regarding door-to-door salesmen fall within five basic headings. These are: (1) Deception by salesmen in getting inside the door; (2) high pressure sales tactics; (3) misrepresentation as to the quality, price, or characteristics of the product; (4) high prices for low-quality merchandise; and (5) the nuisance created by the visit to the home by the uninvited salesman.

Among the many persons testifying at the hearings, which took place over seven days at two locations (Washington D.C. and Chicago), were J. Robert Brouse of DSA, Stephen Sheridan of Electrolux, and representatives from such DSA member firms as Avon Products, Dart Industries, Field Enterprises Educational Corporation, Health-Mor, Mary Kay Cosmetics, and Southwestern Company. Many of the consumer complaints aired in these hearings were already addressed by the DSA Code, and most of the complaints seemed tied to non-DSA member firms. However the DSA Code did not contain an explicit statement about a cooling-off period.

Because the DSA had established a proactive stance with its Code of Ethics, the tenor of the comments by DSA members was somewhat favorable toward the proposed rule. To take an opposition stance would be awkward if not inconsistent with the underlying philosophy of their own Code. In addition, the proposed rule might help substantially in improving the practices of non-DSA member firms and thus raise the image of the entire industry. Two items of controversy came to light, however. One involved a type of discrimination -- the rule would apply to sales in the home but not to sales through other methods of retailing such as in a store or through the mail. The second related to the many state laws specifying a variety of cooling-off procedures (see "Political-Legal Climate" in Part One). Many of these laws differed, including different lengths of the cooling-off period, different minimum dollar purchase levels needed to invoke the rule, and different procedures and paperwork required to inform customers of their rights under the law. DSA generally supported the cooling-off idea, but sought to have all the state laws conform to whatever federal standards emerged. The FTC apparently was not persuaded by the discrimination argument, noting that even if abuses occur in other types of retailing that did not justify failure to act in the case of door-to-door abuses. The problem of diverse state laws was also recognized by the Commission, but it noted that the FTC rule "does not exempt any seller from complying with the laws of any state ... except to the extent that such laws ... are directly inconsistent with the provisions of this [rule]."

On October 18, 1972, the FTC promulgated the trade regulation rule specifying a cooling-off period for door-to-door sales, and it became effective June 7, 1974. The essence of the rule stated that the seller must furnish to the buyer a statement that reads as follows:

> You, the buyer, may cancel this transaction at any time prior to midnight of the third business day after the date of this transaction. See the attached notice of cancellation form for an explanation of this right.

The notice had to be printed in 10-point bold face type with additional information about how to arrange for the return of the goods if the buyer cancels, and what is the buyer's responsibility for goods not picked up by the seller.

Some Specific Legal Actions. A number of direct selling firms were subject to FTC scrutiny and decisions as the decade of the 1970s progressed. Many also were involved in litigation in various states, and the consumer protection agencies or attorneys general of almost every state had, by mid-1972, initiated some kind of action against one of the firms discussed below.[3] The following discussion briefly notes some of the main federal government actions.

Encyclopaedia Britannica. The FTC issued a preliminary complaint against Encyclopaedia Britannica (EB) in July 1972. The complaint alleged misrepresentations to customers regarding the purpose of the salesperson's visit (e.g., conducting surveys rather than selling) and the specifics of the sales offer (e.g., promising original research service to buyers). In addition, the complaints alleged misrepresentations to sales recruits promising availability of positions as management interns, public relations, or other non-selling fields, as well as inflated potential earnings estimates (Wagner 1972). After various hearings and appeals, the FTC issued a final cease-and-desist order in March 1976, requiring EB to deliver by registered mail a copy of the order to each person representing EB in a selling capacity.

Grolier. Based on alleged violations similar to those in the EB case, the FTC asked Grolier to sign a consent agreement requiring its salespeople to hand to their prospects a five-by-seven-inch

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[3]A lengthy footnote in Cochran 1972, pp. 688-689, itemizes many of these state actions or investigations.

card stating the name and company of the salesperson and sales purpose of the call. Further, the FTC directed that the salesperson subsequently obtain the prospect's signature on the card before entering the home and beginning the sales pitch ("FTC: Belling Salesmen" 1972). The need to get the signature was later recanted, based largely on persuasive communications from DSA. Other issues essentially similar to the EB case were also involved, and after numerous appeals and hearings a cease-and-desist order was issued by the FTC in March 1978.

Holiday Magic. The FTC issued a complaint against cosmetics marketer Holiday Magic in January 1971, alleging in part that this company (1) used an unfair and deceptive lottery-type, multi-level, endless chain merchandising program; (2) recruited distributors through misrepresentation; and (3) restrained trade by fixing its distributors' resale prices, allocating sales territories, and restricting types of outlets for resale. Item (1) in particular focused on the issue of an illegal pyramid operation wherein distributorships rather than products were being sold to produce the bulk of the income generated. The other charges were not central to the nature of a multi-level sales organization, though very much at issue under Section 5 of the FTC Act (DeJute, Myers, and Wedding 1973). During this same time Holiday Magic applied for membership in DSA, but because it was an alleged illegal pyramid operation, the DSA Board (which must approve new members) deferred its decision. Holiday Magic, frustrated in its desire to gain the respectability accorded by DSA membership, brought suit against DSA. The matter was settled in 1973 when Holiday Magic agreed to drop the case "with prejudice" which precluded that firm from ever bringing suit against DSA again. The pyramid complaint was upheld by the FTC in a final order a year later.

Koscot Interplanetary. The FTC formally charged Koscot, a marketer of cosmetics made from mink oil, as an illegal pyramid scheme evidenced by its concentration on sales of its distributorships rather than sales of its products. In this often-referenced case, the FTC prevailed with a final order in 1975.

Bestline Products. Bestline was founded by a Holiday Magic alumnus to sell cleaning products, and gained the attention of the FTC in the early 1970s. The company agreed to cease and desist via a consent agreement prohibiting headhunting fees (for the sale of distributorships), misrepresentation of earnings, and nonrefundable inventory loading in mid-1972. Consumer complaints against Bestline continued, however, and the company became a concern to DSA because it was a DSA member. A report to the DSA Executive Committee in April 1974 noted that Bestline had entered into various consent agreements with several states, and some state regulators had agreed to let DSA handle some of the complaints through its Code of Ethics administrative process. Bestline did not appear in the 1980 roster of DSA members.

Dare-To-Be-Great, Inc. Dare-To-Be-Great sold a series of four courses of motivational lectures on cassette tapes. The courses were titled "adventures" and courses three and four emphasized the sale of Dare-To-Be-Great franchises. In May 1972 the Securities and Exchange Commission (SEC) brought action against this company based on securities law violation (A fascinating description of this operation is detailed in Cochran 1972.). In brief, the SEC believed that a security is being sold when the "investor" is not required to make significant efforts in the operation of the business to obtained the promised return. In essence, the SEC claimed that the purchaser of a Dare-To-Be-Great franchise was encouraged to recruit other franchisees, who in turn were encouraged to recruit still other franchisees, on and on. Once this chain began, the franchisee at the top of the pyramid would simply collect fees based on the numbers being recruited, and no further work was required. Other factors were involved as well, but the result was a successful suit by the SEC based on a charge of failure to comply with the securities laws.

Amway. In March 1975 the FTC issued a complaint against Amway involving five counts: (1) fixing resale prices to be charged by its independent distributors; (2) restricting the outlets through which its distributors may resell Amway products; (3) restrict advertising and promotional activities of distributors; (4) misrepresenting the amount of income potential available through "multiplication, duplication, and geometrical, unlimited or endless chain increases in the number of distributors or dealers recruited," and (5) falsely representing the ease of recruiting distributors and the amount of profits or earnings available from recruiting ("MBS Purchaser Under FTC Gun" 1977). The final cease-and-desist order was issued in May 1979. But this case was a landmark event regarding the definition of a pyramid operation, the focus of count four above. In this case, the FTC dismissed the allegations that Amway was a pyramid scheme based on the company rules requiring that its distributors make sales of Amway products to consumers and that every distributor must sell at least 70% of the total amount of products bought in a given month. The latter rule was established to prevent inventory loading, a characteristic of pyramid schemes whereby the distributor purchases quantities of products in order to qualify for bonuses or increased commissions but fails to sell the products to ultimate consumers, thus creating a storehouse of unsold inventory. The price fixing and trade restraint allegations were upheld, however, and were the subjects of the final cease-and-desist order.

DSA Actions Related to the Code

The adoption of the Code of Ethics imposed many responsibilities on its DSA guardians. There were administrative procedures to establish, such as the selection of a code administrator. There was a communication task to perform in order to inform various constituencies -- federal and local government officials, association member companies as well as nonmembers, direct salespeople in member and nonmember companies, and consumers and their representatives in consumer action organizations -- about the Code's existence and the benefits it offered. There was the hopeful expectation that this communication would markedly benefit the industry's image and