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Federal Trade Commission/Office of the Secretary,
Room H-135 (Annex S)
600 Pennsylvania Avenue, NW
Washington, DC 20580

RE: Revised Proposed Business Opportunity Rule, R511993

Position Statement of Babener and Associates on FTC Revised Proposed Business Opportunity Rule, R551993

Our law firm, **Babener and Associates**, is writing to continue to support ongoing comments and submissions of the DSA (Direct Selling Association), MLMIA (Multilevel Marketing International Association) and MLM DRA (Distributor Rights Association) regarding the FTC Revised Proposed Business Opportunity Rule, R551993. We fully support the FTC in its laudatory consumer protection objective to challenge fraudulent and deceptive business practices, but, along with other industry professionals, we respectfully offer constructive comments and recommendations to allow the FTC to achieve its objectives, and at the same time, to avoid an undue hardship to the MLM/Direct Selling industry and to the businesses of 15 plus million U.S. home-based direct sellers whose sales revenue exceed \$30 billion per year.

Profile of Firm Providing Comment:

For almost 25 years, this firm has served as legal advisor to start-up, emerging and mature direct selling companies headquartered throughout the U.S. and abroad. The firm has served as legal counsel to many members of the DSA and MLMIA and, over the years, its legal advice has been sought out by such leading direct selling companies as Avon, Shaklee, NuSkin, Nikken, Melaleuca, Longaberger, Tupperware, Excel Communications, ACN, USANA, Prepaid Legal, Discovery Toys, etc. We have served on the DSA Lawyer's Council and Government Relations Committee and as a supplier member of the DSA, and we have served on the board of directors and as general counsel to the MLMIA. We have published extensively on the subject of direct selling

and lectured at industry conferences and universities such as the University of Texas and University of Illinois. We have served as trial lawyer in many cases throughout the U.S. on the subject of direct selling. The firm posts an educational website on direct selling, www.mlmlegal.com. We are frequently called upon by the media as an expert on the subject of direct selling, we have served on conference panels with regulatory officials and we are one of a handful of law firms in the U.S. that specialize in the area of direct selling.

A Constructive Critique of the FTC Revised Proposed Business Opportunity Rule

As a preface, the following comments are offered with the utmost respect and appreciation of the FTC Staff analysis and explanation of the Revised Proposed Business Opportunity Rule. It is clear that the FTC listened attentively to the approximately 17,000 letter submissions regarding the appropriate scope of the Proposed Business Opportunity Rule and its impact on the MLM/Direct Selling/Direct Sales/Network Marketing industry. In fact, in no uncertain terms, the FTC opined that its intent was, in redrafting the Proposed Business Opportunity Rule, that traditional MLM/Direct Selling/Network Marketing Companies should be exempted from coverage of the new Proposed Business Opportunity Rule.

As to those businesses that must comply with the Revised Proposed Business Opportunity Rule, all observers agree that the FTC significantly limited the original mandate of disclosures and procedures that many complained would be overly burdensome to legitimate businesses. This Comment will not address the disclosure issue. Rather, this Comment addresses the definitional elements of the Revised Proposed Business Opportunity Rule to suggest further approaches to achieve the FTC's stated intent to exempt traditional MLM/Direct Selling programs from coverage of the Revised Proposed Business Opportunity Rule.

The Notice of Revised Proposed Business Opportunity Rule (RPBOR) represents a good faith start to narrow the scope of the FTC Proposed Business Opportunity Rule and to invite comments from the public to assist in this process. At the very least, the FTC, in its comments on the RPBOR is unequivocal in its stated intent to exempt the MLM industry, noting in its public statement:

On balance, based on this record and its law enforcement experience, the Commission does not believe it is practicable or sufficiently beneficial to consumers to attempt to apply the proposals advanced in this rulemaking against multi-level marketing companies, particularly when considering the burdens upon industry. The Commission, therefore, has determined that at this point, it will continue to use Section 5 to challenge unfair and deceptive acts or practices in the MLM Industry.

In fact, no less than ten references are set forth by the FTC with respect to its intent to exclude application of the RPBOR to MLM/Direct Selling companies. Those comments are couched in such terms as:

“The [Rule] has been pared back to exclude MLMs”;

“The Commission takes MLM companies out of the ambit of the Rule”;

“...these provisions would no longer apply to MLM companies”;

“they [MLM Companies] are excluded from the scope of the [Rule]”.

Unfortunately, The Revised Proposed Rule is Silent on the Exemption for MLM/Direct Selling

The expressed intentions of the FTC are much appreciated by the MLM/Direct Selling Industry. Unfortunately, the industry can take very limited comfort in the FTC comments, in that, at no place in the Revised Proposed Business Opportunity Rule is the MLM/Direct Selling exemption “called out,” nor is it even addressed. If adopted, as is, future statutory interpretation within the “four corners” of the actual rule, will find no guidance as to the FTC intention to exempt MLM/Direct Sellers from the Rule.

Although the drafters may perceive that “business assistance” as defined in the proposed draft is quite different for the classic “business opportunity” compared to MLM opportunities, there actually is a substantial “blur” as to the distinction. The proposed rule is triggered by an offeror who “provides outlets, accounts, or customers, including, but not limited to, Internet outlets, accounts, or customers, for the purchaser’s goods or services.” In today’s direct selling world, it is not uncommon for direct selling companies to offer lead generation, assistance in customer acquisition, institutional and co-op advertising to drive customers and prospects to distributors, web-branded sites that drive customers and prospects to distributors and replicating websites for distributors that are fed by company web and other media promotion. In other words, unless MLM/Direct Selling companies are exempted from the definition of “business assistance” or, unless the definition of “business assistance” is fundamentally changed, MLM/Direct Selling companies will likely be snared in the net of the Rule’s definition. Industry professionals would likely conclude that it is impractical to redefine “business assistance,” as the provided definition is quite typical of existing state business opportunity legislation

Assuming that the typical MLM/Direct Selling company does offer “business assistance” within the definition of the Revised Proposed Rule, all of the other elements will also likely be met to trigger applicability of the Rule to the MLM/Direct Selling company. The other elements are present in the typical MLM/Direct Selling offering:

- (1) **The solicitation to enter into a new business;**

(2) **The prospective purchaser must make a required payment.** (Virtually all MLM/Direct Selling companies require the purchase of a modestly priced “at cost” sales kit which would automatically trigger the Rule. Often, today, MLM/Direct Selling companies also mandate a replicated website, back office access for commission analysis and reports and internal communication, typically “at cost” also. The Rule does not exempt such purchases from “required payment.” The only exemption is for “purchase of reasonable amounts of inventory at bona fide wholesale prices.” The inventory exemption is of little assistance to MLM/Direct Selling companies in that it is almost a “nonexistent” practice for MLM companies to require inventory purchases. Industry “best practices” regard mandated inventory purchases as “symptomatic” of pyramid schemes. Such purchases are almost always optional and at the discretion of the distributor. In addition, many MLM companies are service providers where no inventory is involved, and many tangible product MLM companies, rather than promote purchase for resale of inventory, offer “order taking” and online and telephone purchasing by customers and distributors.)

(3) **A buyback policy for product or goods purchases.** (In fact, no reputable MLM/Direct Selling company fails to offer a buyback policy...a mandated industry consumer protection practice of members of the Direct Selling Association, of state MLM distribution statutes and a practice long enshrined as a sign of legitimacy in the landmark FTC administrative court decision involving Amway.)

Thus, although well intentioned to exempt MLM/Direct Selling companies from the proposed Business Opportunity Rule, the proposed language would not accomplish the objective. In the absence of adopting a threshold financial trigger (similar to \$500 typical thresholds in state business opportunity statutes) or expanding the exemption for “requirement payment” to include “at cost” or “not-for-profit” sales kits and marketing support materials and marketing system support, the typical MLM/Direct Selling company will be pulled into the ambit of the proposed Rule unless the FTC amends the Rule to specifically call out an exemption, per its stated intention, for traditional MLM/Direct Selling Companies. Such a blanket exemption might read:

MLM/Direct Selling companies are exempted from this Rule so long as any required payment during the first six months of distributor participation is below \$_____, and so long as the required purchase is for “at cost” or “not-for-profit” sales kits and marketing support materials and marketing systems support such as replicating websites or “back office” distributor systems for analyzing commissions, productivity and communication.

A Threshold Trigger or “At Cost” or “Not-for-Profit” Exemption has a Long Historical Precedent

Although, the adoption of a stand-alone Business Opportunity Rule may be a new endeavor for the FTC, it may look for guidance to its own Franchise Rule which provides a \$500 threshold exemption in a far more complex business opportunity arena. The FTC may look to state franchise statutes which typically exempt “purchase of goods”(which is broader in scope of exemption than merely “inventory”) at bona fide wholesale prices and also often adopt a \$500 threshold. The FTC may draw on guidance from a myriad of state MLM statutes and pyramid legislation in which it is not unusual to find an exemption for “at cost” sales and marketing materials.

Most importantly, in fashioning a free-standing Business Opportunity Rule, the FTC should draw on the successful implementation of Business Opportunity legislation at the State level which has been ongoing for several decades. Such legislation, which exists in approximately two dozen states almost invariably adopts a threshold required payment within the first six months, typically \$500, and also typically exempts the purchase of “at cost” sales support materials.

Of the two dozen states with Business Opportunity Statutes threshold exemptions, fourteen adopt \$500, four adopt \$300, four adopt \$250 and two adopt \$200. Not only is the threshold exemption precedent in Business Opportunity legislation “proven” and several decades old, almost all states also adopt a further exemption for “at cost” sales and marketing support materials that also exempts the typical MLM/Direct Selling business. In fact, although MLM/Direct Selling companies routinely register under state MLM Distribution statutes, it is “rare to never” for a MLM/Direct Selling company to register under a state Business Opportunity statute. A typical Business Opportunity exemption may be found in the South Dakota Business Opportunity Act, one of the states with a lower \$250 threshold:

South Dakota Codified Laws Section 37-25A-3, subsections (2) and (6)

(2) Any offer or sale of a business opportunity for which the purchaser is required to make a payment to the seller or a person recommended by the seller not to exceed two hundred fifty dollars during the period from any time before commencing operation to within six months after commencing operation of the business opportunity;

(6) Any offer or sale of a business opportunity for which the cash payment made by a purchaser for any business opportunity does not exceed five hundred dollars and the payment is made for the not-for-profit sale of sales demonstration equipment, material, or samples, or the payment is made for product inventory sold to the purchaser at a bona fide wholesale price;

Recommended: Call Out the MLM/Direct Selling Exemption and Other Typical Exemptions

In summary, the FTC’s stated intent, to exempt MLM/Direct Selling companies from the Revised Proposed Business Opportunity Rule, has clearly moved the discussion in a direction much appreciated by the MLM/Direct Selling industry and in keeping with the

detailed analysis of the issue set forth by the FTC. However, four recommendations are respectfully suggested to achieve the intent of the FTC that will further FTC objectives, create consistency with a long-standing state tradition of regulation of business opportunities, and finally, address the goals and needs of the MLM/Direct Selling industry:

- (1) Specifically call out the exemption for MLM/Direct Selling in the Revised Proposed Business Opportunity Rule;
- (2) Adopt a threshold exemption for required payments in the first six months, preferably \$500, but perhaps as low as \$200;
- (3) Adopt an exemption for the purchase of “at cost” or “not for profit” sales kits and marketing support materials and marketing systems support such replicating websites or “back office” distributor systems for analyzing commissions, productivity and communication;”
- (4) In the alternative, adopt a specific exemption for MLM/Direct Selling companies as follows:

MLM/Direct Selling companies are exempted from this Rule so long as any required payment during the first six months of distributor participation is below \$_____, and so long as the required purchase is for “at cost” or “not for profit” sales kits and marketing support materials and marketing systems support such as replicating websites or “back office” distributor systems for analyzing commissions, productivity and communication.

Respectfully Submitted,

Babener & Associates

Jeffrey A. Babener

