

OUR REF SDM/DTMP/SDM/ECR/FTC

YOUR REF

maclay murray & spens LLP

Federal Trade Commission/Office of the Secretary,
Room H-135 (Annex W)
Re: Business Opportunity Rule, R511993
600 Pennsylvania Avenue, NW
Washington, DC 20580

17 July 2006

Dear Sirs

Business Opportunity Rule, R511993

We are writing in response to the proposed Business Opportunity Rule, R511993 ("the Proposed Rule"). We would like to bring a number of issues to the Commission's attention that we believe should be given further consideration. We are a primarily UK-based commercial law firm. The comments have been prepared by our European, Competition & Regulatory department who have wide experience of advising clients in relation to distribution agreements. We envisage that the Proposed Rule, as currently drafted, has the potential to impact on a number of distribution arrangements not covered by the current Franchise Rule and which appear to fall outside the primary intended focus of the Proposed Rule.

1. SCOPE OF THE PROPOSED RULE

The Proposed Rule is primarily aimed at safeguarding against fraud in the sale of business opportunities aimed at consumers; work-at-home and pyramid schemes being examples given. However, we believe that, in practice, the rule has real potential to affect common distribution arrangements which it may not be intended to affect; or, if it is intended to do so, in our view targets inappropriately.

2. DEFINITION OF "BUSINESS OPPORTUNITY"

The definition of business opportunity is currently, in our view, too far reaching. We suggest that a different approach should be taken to exclude certain situations from falling within the definition of a business opportunity. The definition could either be redrafted or an 'exception based approach' adopted.

The definition that establishes the Proposed Rule's scope (section 437.1(d)) details three definitional elements of the term "business opportunity": (1) a solicitation to enter into a new business; (2) payment of consideration, directly or indirectly through a third party; and (3) either an earnings claim or an offer to provide business assistance. As currently drafted, these elements have the potential to impact on distribution arrangements which the Proposed Rule is perhaps not intended to affect. We also foresee that the sale of an existing distributorship business built up by the vendor will often be covered.

2.1 Solicitation of a potential purchaser to enter into a new business

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This is clearly capable of covering situations where one company approaches another to act as its distributor or where a distributor approaches another entity with a view to selling its distributorship business.

2.2 Payment or other consideration

In the context of the appointment of a distributor by a substantial manufacturing business, the distributor making payment at the outset is somewhat unusual, but not unknown. An obvious example is where a brand is particularly sought after and there may be competition amongst US-based companies to secure the distribution rights. Deferred payment arrangements (future share of profits etc) can also occur in ordinary distribution arrangements. As referred to above, consideration will exist upon the sale of a business.

2.3 Earnings claim or representation of business assistance

Given the wide scope of the arrangements which can fall within the definition of a "business opportunity", this part of the definition causes us particular concern and which we foresee potentially giving rise to litigation. Allegations could very possibly arise that an earnings claim has been made in the context of the negotiation of a distribution contract. This is particularly so given the intentionally wide definition of what constitutes an earnings claim. The dividing line between discussions which fall within the Proposed Rule and discussions which do not is unclear. Earnings claims are likely to be made when a distributorship is being sold by the existing distributor.

Further, suppliers may assist distributors in ways currently falling short of the significant control or assistance required under the Franchise Rule, but such as to fall within the definition of business assistance in the Proposed Rule. The definition of business assistance is very broad and a wide range of activities frequently undertaken by suppliers could trigger the application of the Proposed Rule.

3. LACK OF A DE MINIMIS LEVEL

The rule applies to all businesses regardless of the number of business opportunities they offer in any given year. We suggest that it would be sensible to set a *de minimis* level of the number of business opportunities which must be offered before the proposed rule applies. For example, if the rule did not apply unless at least five business opportunities (as currently defined) were being sold within the United States in any given year, this would certainly exclude from the scope of the rule all of our clients who would be potentially affected and also, we suspect, the vast majority of other substantial foreign manufacturing businesses whose ordinary distribution arrangements might be affected. An alternative solution would be if the Proposed Rule did not apply to those already in business.

4. THOSE ALREADY IN BUSINESS

We do not believe that those already in business are necessarily in need of the protection afforded by the new rule. It would be interesting to consider the proportion of complaints the Commission receives regarding business opportunity sales which relate to those already in business. We are strongly of the view that an existing businessperson is far less likely to be adversely affected by such schemes than someone not already in business. In this regard, we would suggest that the Commission either delete the phrase "or a new line or type of business" entirely or consider some form of exemption for those who have reasonable business experience.

5. DISCLOSURE REQUIREMENTS

5.1 The Litigation Disclosure Requirement

Business opportunity sellers are currently not permitted to comment on the outcome of litigation - only basic details of litigation can be submitted. We would suggest that parties be entitled to include factual comments on the outcome of any litigation that they were involved in rather than simply stating that they were involved in litigation. The requirement as currently drafted could potentially cause unwarranted concern about legitimate business opportunities.

5.2 The References Requirement

The requirement to provide contact information for prior purchasers as references could prove to be impractical and unworkable in some instances. For some manufacturing companies, there may well be no comparable distributors. In a possible scenario involving a supplier appointing its first US distributor, there may only be a limited number of possible references, these will be in other countries and of very limited value as a reference. In this regard, it may be appropriate to have the requirement apply only to business opportunities previously granted in the United States.

5.3 Quarterly Updating

This is an unnecessary burden on businesses particularly where a business only has a very small number of distributors and may not change its distribution arrangements for several years. This would involve a disproportionate amount of costs and burden for businesses.

5.4 The Disclosure Document

The draft disclosure document is perhaps suitable/appropriate to deal with the sale of business opportunities to consumers such as work-at-home schemes. However, as stated earlier, the scope of the rule potentially catches common distribution agreements between companies. In this context, the document is largely irrelevant and not sufficiently sophisticated to be useful to the purchaser of the business opportunity in any meaningful way.

6. CONCLUSION

We have highlighted a number of areas of concern arising from the proposed business opportunity rule. Unless substantially amended, the rule potentially acts to discourage foreign manufacturing businesses from doing business in the United States of America - it is likely to act as a regulatory barrier to entry and disincentive to doing business in the US. It may also have the undesirable effect of causing some companies to structure their distribution arrangements so as to not fall within the rule rather than on the basis of the most economically efficient distribution solution. We believe that such difficulties could be avoided by adjusting the definition of what will qualify as a business opportunity or adopting an exception based approach.

Yours sincerely

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