



July 17, 2006

Pamela G. Bailey
President & CEO

BY COURIER

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

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FEDERAL TRADE COMMISSION
RECEIVED DOCUMENTS

RE: Business Opportunity Rule, R511993

Dear Sir or Madam:

The Cosmetic, Toiletry and Fragrance Association (CTFA) hereby submits the following comments on the Federal Trade Commission's (FTC's) proposed Business Opportunity Rule, 71 Fed. Reg. 19054 (Apr. 12, 2006) (proposed rule); 71 Fed. Reg. 31124 (June 1, 2006) (extension of comment period). CTFA is the national trade association representing the cosmetic and personal care products industries. Founded in 1894, CTFA has almost 600 members whose businesses formulate, manufacture, distribute and market personal care products. Our members manufacture or distribute the vast majority of personal care products sold in the United States. The cosmetic industry takes pride in its long history of self-regulation. Examples of CTFA self-regulatory programs include the voluntary establishment registration and product ingredient registration by member companies; the establishment of the Cosmetic Ingredient Review, an independent scientific panel charged with assessing the safety of cosmetic ingredients; numerous technical guides and databases relating to cosmetic safety and regulation; and, most recently, the Consumer Commitment Code, a voluntary program that reinforces member companies' commitment to assuring the safety of their products. Our self-regulatory programs are not only effective, they save scarce government resources.

Some of CTFA's member companies utilize the direct selling business model, whereby a company's products and services are presented and sold to consumers, typically in the home, through a network of independent salespersons, commonly known as "direct sellers." These members would be directly and adversely affected by the proposed Business Opportunity Rule. Other CTFA member companies engage in licensing arrangements whereby they license their trademarks and/or service marks to individuals for the purpose of

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operating retail stores. These members may also be adversely affected by the proposed rule.

I. Comments on Behalf of Direct Sellers

The thrust of the proposed rule, which requires that the seller of a business opportunity provide a disclosure statement to a prospective buyer *prior* to the sale, appears to be based on the same basic concern underlying the FTC's so-called Franchise Rule – namely, the prevention of fraud or deception of prospective purchasers in connection with the sale. “The objective of the proposed Rule is to provide consumers considering the purchase of a business opportunity with material information they need to investigate the offering thoroughly so they can protect themselves from fraudulent claims.” 71 Fed. Reg. at 19082.

However, the unique characteristics of the direct selling industry render this type of rule ill-fitting to the industry and, indeed, altogether unnecessary. The nature of the direct selling industry differs from that of the franchise industry in several fundamental ways. For instance, whereas the purchase of a franchise typically involves a significant up-front investment, participation as an independent salesperson for a direct selling company does not. Direct sellers generally rely on their sales activities as a source of *supplemental* income, rather than as their primary income. The majority of direct sellers are individuals who seek, for example, to earn supplemental income for specific objectives (e.g., to fund holiday spending or to save for a vacation), who seek flexibility in work schedules, or who seek a social outlet (often women who stay at home). As a result, many direct sellers engage in direct selling activities in a part-time rather than full-time capacity. Notably, direct selling contracts can be cancelled at will by either party and do not contain non-compete clauses. These and other characteristics facilitate easy entry into, and exit from, the direct selling industry, without significant paperwork or other hurdles.

Moreover, our direct selling members adhere to certain safeguards and policies designed to protect their direct sellers, in accordance with the Direct Selling Association's (DSA's) Code of Ethics. Such policies include, for example, prohibitions against misrepresentations concerning identifying information about the company and/or opportunity, sales or profits, the nature of the goods or services offered, and terms of cancellation or refund policies; enforced inventory buyback offers (minimum of 90%) should an individual choose to exit the business; and requirements for written substantiation of earnings claims. Many direct selling companies offer full refunds for the low-cost sales kit (typically \$100 or less), the sole required purchase for one to become a direct seller.

Therefore, in light of the foregoing, any type of requirement for pre-sale disclosure to a prospective purchaser of a direct selling opportunity would not only be onerous for our members and substantially impede the ease with which

these arrangements are currently facilitated – it would afford no greater guarantee of buyer protection than do our members' existing consumer protection policies. Any type of "waiting period" during which members would supposedly be performing due diligence on the seller is unnecessary, given the minimal risk these business arrangements entail and the safeguards companies have in place to ensure that the financial risk to purchasers remains so. Similarly, the costs of compliance with the proposed requirements for disclosure of legal actions against the company, requested cancellations and refunds, and references greatly outweigh any putative benefits to the prospective purchaser.

Aside from the fact that the costs of tracking such information alone would be enormous, disclosure of legal actions is likely to confuse the purchaser, given that many of the types of actions that would fall within the ambit of the required disclosures might well be unrelated to the business opportunity. For instance, proposed Section 437.3(a) requires disclosure of information on legal actions related to *any affiliates*. If, for example, a large multinational company with many different business units also happens to have a direct selling subsidiary, then the requirement would arguably require disclosure of all of the specified legal actions throughout the larger organization, irrespective of how they related to or affected the direct selling business unit. If the FTC ultimately adopts some version of the proposed rule, it should be clearly and narrowly tailored to address the particular business unit or subsidiary in question, and not extend to affiliated or substantively unrelated business groups or activities.

Further, disclosure of references raises significant privacy and confidentiality concerns, and information on cancellations and/or refunds is unlikely to be a factor in a purchaser's decision, given the nature of this particular industry – i.e., the easy entry/exit model and the vast range of personal reasons individuals choose to participate.

In sum, the proposed disclosures are overly broad and likely to be of dubious, if any, value to a prospective purchaser of a direct selling opportunity in assessing the potential business risk. Our direct selling members conduct their businesses with veracity and integrity. Subjecting them to the types of requirements in the proposed rule would impose an unnecessary and substantial burden on the industry that might discourage prospective buyers from entry. It would in our view substantially undermine their business models, which are predicated upon strong consumer protection safeguards. More fundamentally, in view of the substantive overlap with the DSA Code of Ethics, the proposed rule would be unlikely to provide purchasers of direct selling business opportunities any additional tools or protection against risk. The FTC should therefore exclude the direct selling industry from the scope of the proposed rule. At the very least, direct sellers who comply with the DSA's proposed "Best Practices," which sets forth many of the safeguards discussed above, should be excluded from the proposed rule.

II. Comments on Behalf of Licensors and Other More Traditional Business Arrangements

We note that the breadth of the proposed definition of “business opportunity” could potentially be read to sweep in (i) licensing arrangements, whereby a company licenses the use of its trademark and/or service marks to individuals who are simply purchasing inventory from the licensor company; or (ii) other more traditional business relationships or proposals that do not appear to be the focus of the proposed rule. For instance, read literally, the proposed definition could be stretched to apply to a traditional sale by a manufacturer to a retailer of a new product or offering of products, business services or other business arrangements; or to the standard engagement by a manufacturer of an independent contractor to perform sales functions, not to individual consumers in the home per the direct selling model, but to beauty supply companies, salons, and other wholesale or retail entities. We request confirmation from the FTC that the definition is *not* intended to encompass such standard licensing arrangements and other more traditional retail-oriented arrangements. To that end, if the FTC decides to proceed with development of this rulemaking, we propose that the FTC amend the proposed definition of “business opportunity” with the following language to clarify its intent to exclude such arrangements:

§ 437.1(d). “Business opportunity means...

(3)(ii)...with business assistance;

Provided that a business opportunity shall not include (i) the sale of any marketing plan in an agreement, the primary purpose of which is to license a federally registered trademark or federally registered service mark, (ii) any business proposal or opportunity provided directly or indirectly to a retail or services customer, or (iii) the engagement by a manufacturer of an independent contractor to function as a sales representative to beauty supply companies, salons, and other wholesale or retail entities.

As a final point, the second prong of the “business opportunity” definition makes reference to “payment” or “other consideration” to the seller. “Consideration” is defined in the preamble to the proposed rule as a monetary payment, share of profits, or a current obligation to make a payment at a future date.” 71 Fed. Reg. at 19063. We believe the reference to “other consideration” in the actual proposed regulation is overly broad in that it could conceivably apply to purchase of product or other non-monetary payment. The phrase “other consideration” should therefore be deleted from proposed Section 437.1(d)(2).

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We appreciate the opportunity to comment on this topic. Please contact us if you have questions or need additional information concerning these issues.

Respectfully submitted,

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Executive Vice President – Legal and General Counsel