
Shaklee Corporation

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Executive Vice President
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**Via Federal Express**

July 13, 2006

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

Re: Proposed Business Opportunity Rule, R511993

Dear Sir or Madam:

Shaklee Corporation ("Shaklee") submits these comments in opposition to the proposed Business Opportunity Rule R511993 published in the Federal Register on April 12, 2006 to the extent it is intended to apply to Shaklee and similarly situated direct selling companies. Although Shaklee applauds the efforts of the Federal Trade Commission ("FTC") to reduce business opportunity fraud, Shaklee believes that the Proposed Rule will not accomplish its intended results. It would, however, impose extraordinary economic burdens that could undermine the viability of legitimate direct selling companies, threaten the livelihood of small distributors, and reduce the availability of valuable goods and services.

Shaklee recommends that the Commission withdraw the proposal and consider a series of workshops to determine whether a rule can be an effective tool against the fraudulent marketing of business opportunities, and if so, what approach the rule should take. Should a promising proposal emerge from the process, Shaklee believes it would be so different from the current proposal that an entirely new comment period would be necessary.

About Shaklee

Shaklee was founded in 1956 in Oakland, California and is one of the oldest direct selling companies in the United States. There are approximately 750,000 Shaklee Members and Distributors in the five countries where Shaklee operates, generating approximately \$500 million in sales. Shaklee's top-ranking Distributors have an average tenure with Shaklee of 34 years.

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Shaklee Corporation

Federal Trade Commission/Office of the Secretary

July 13, 2006

Page 2

Shaklee is well known for its high quality nutritional, personal care and household products. As the number one natural nutrition company in the U.S., Shaklee manufactures and distributes vitamin and mineral, soy protein, sports nutrition, fiber and botanical products. Shaklee introduced in 1960 one of, if not the, first biodegradable household cleaners in the U.S. – Basic-H® Concentrated Organic Cleaner – which later became an official Earth Day product.

Shaklee became publicly traded in 1973 and was listed on the New York Stock Exchange in 1977. In 1982 Shaklee was named a Fortune 500 company. In 1989 Yamanouchi Pharmaceutical Co., Ltd., then the third largest pharmaceutical company in Japan, acquired Shaklee, making it privately held once again. In 2004, two New York equity firms purchased Shaklee. Roger Barnett, the managing director of one of the firms, took over as Chairman and CEO of Shaklee.

Shaklee operates network marketing businesses in five countries – the U.S., Canada, Japan, Malaysia and Mexico – as well as a distributorship in Singapore. Plans are underway to open several new markets in the next year. The Company operates multiple manufacturing and research & development facilities and holds more than 48 patents and patents-pending. In addition, Shaklee has published more than 100 clinical studies.

Shaklee became the first company in the U.S. to be certified as Climate Neutral™ by the Climate Neutral Network, meaning that the Company offset 100% of its CO2 emissions. Shaklee sponsored a rural electrification project in Sri Lanka, India to replace kerosene lamps and diesel generators with solar photovoltaics that reduce greenhouse gas emissions and improve health for rural-dwelling families. Shaklee supported the construction of the Rosebud Sioux Tribe Wind Turbine Project – the first large-scale Native American owned and operated wind turbine. Shaklee also supported a project to switch school buses in San Bernardino County, California from petroleum-based diesel fuel to biodiesel fuel formulated from recycled cooking oil.

In 2001, Shaklee received The Edmund G. “Pat” Brown Award from the California Council for Environmental and Economic Balance. Shaklee also received the 2001 Savings by Design Energy Efficiency Integration Award co-sponsored by the American Institute of Architects and California Council. In 2002 Shaklee received the U.S. Environmental Protection Agency Climate Protection

Award. That same year, Shaklee received the Environmental Stewardship Award from Social Accountability International. In 2003, Shaklee received the Environment & Sustainability – Gold Medal awarded by the Nutrition Business Journal. Also in 2003, Shaklee received the National Association of Environmental Professionals “National Environmental Excellence Award.” In 2004 Shaklee received the IntegriTREE Award from New Leaf Paper.

Beginning in 2005 Shaklee became a major partner of the Green Belt Movement, founded by Kenyan scholar Dr. Wangari Maathai, winner of the 2004 Nobel Peace Prize. This year Shaklee launched “A Million Trees. A Million Dreams™” campaign to reduce greenhouse gases by planting trees across the U.S. and Canada and contributing to planting an equal number in Africa.

The Shaklee Business Model

Members sign an application with Shaklee to purchase Shaklee products at a discount. They pay \$19.95 and receive, in addition to a discount, a product catalog, information about the Company, and periodic special promotions available only to Members. Although it is possible to sign up initially as a Shaklee Distributor for no additional cost, more than 85% of those who sign up with Shaklee do so as Members, or wholesale buyers. It is from this group of product users that Shaklee Distributors develop. After using Shaklee products for months or years and recommending them to friends and neighbors, Members often decide to build a business. Once a Member has referred to her Distributor a sufficient number of neighbors, friends and relatives, the Distributor may suggest that the Member can earn the price of her products by herself becoming the Distributor to those she has referred. If the Member accepts the offer of the earning opportunity, there is no additional application to sign or compensation to pay; Members need only supply their Social Security Number or Tax Identification Number to Shaklee in order to sell products and earn bonuses.

Shaklee Distributors typically attract new Distributors and Members through small in-home meetings or parties. For example, a Distributor may ask a friend or neighbor to host a “healthy home party” at which the Distributor will discuss and demonstrate Shaklee household cleaners. The hostess may receive a special gift or bonus for her efforts. If invitees like the products, they often will sign a Member application at the event and place a product order. The enjoyment of the party or meeting is crucial for recruiting purposes. If an application and federal disclosure form had to be handed out and collected a week later, the

pleasant memories of new friends and exciting products would evaporate in the mandated descriptions of litigation, earnings prospects and the knowledge that each of their names and telephone numbers could be distributed to strangers. Undoubtedly few applications would be submitted.

Distributors operate their businesses in many different ways. Some choose to have all their Members purchase directly from the Company, and some maintain an inventory sufficient to supply their Members themselves. Some choose to have the Distributors they develop be paid bonuses directly by the Company; others pay the bonuses themselves. Although the Company offers training programs for Distributors, some choose to train the Distributors they develop, and others avail themselves of the Company programs. As independent contractors, Distributors are free to operate their businesses as they see fit. Therefore, the Company provides "business assistance" as that term is defined by the Commission to approximately one-half of its Distributors. Assuming *arguendo* that no earnings claims are made, this would lead to the absurd situation where one-half of Shaklee Distributors are engaged in a business opportunity, and the other half are not.

Approximately ninety percent of Shaklee Distributors are women who seek to augment their family income by working from home part-time.

The Disclosure Requirements and Seven Day Waiting Period of the Proposed Rule Would Create Significant Burdens and Barriers to Entry

While the public policy goal of protecting prospective purchasers from business opportunity frauds is a laudable one, we fear that the proposed rule would stigmatize and burden legitimate direct selling businesses and their distributors while not significantly reducing fraudulent activity. With its simultaneous elimination of the \$500 threshold of the Franchise Rule and expansion of the definition of "business opportunity" to cover most references to earnings or any provision of "business assistance," the Proposed Rule would trigger coverage of virtually every meeting among Distributors and prospective Members.

In practice, this means that what has until now been a very simple process would be required to change dramatically. For example, when an individual wishes to sign an application to become a Member – a wholesale buyer – would that person have to be given a disclosure statement and told to wait seven days before signing? The only prudent practice would be to disclose. A responsible

direct seller would not risk violations of the rule by assuming that a meeting could take place without someone mentioning the earnings prospects of distributors. Yet, the disclosures would be nearly impossible to comply with given the specifications of the Proposed Rule. This would place direct sellers at a distinct disadvantage compared to their competitors in buying clubs. How would COSCO or Sam's Club react to such a requirement? (By the way, the fee for both those membership clubs is higher than the \$19.95 currently charged by Shaklee.)

Since when one becomes a Member is the only point at which an application is signed, would Shaklee have to introduce a separate application and disclosure for Distributors? In that event, when a product customer calls in her Social Security Number to begin building a business, must the Company mail her not only a new form to sign, but also a disclosure statement and ask her to wait seven days, even though at this point the Member typically is quite familiar with the Shaklee earning opportunity?¹

Shaklee believes that if it were required to adopt either of the above approaches, its business would be seriously crippled. Distributors would be at a distinct disadvantage in attempting to explain to those who simply want to purchase products at a discount that they must receive a detailed disclosure document and wait seven days before signing an application to become a wholesale buyer. Prospective customers likely would view this as a statement by regulators that there is something wrong with purchasing products from a direct selling company. Customers would be expected to shy away since they face nothing comparable in any other channel of distribution.

And if that were not sufficient, customers would have to agree to allow their name, address and telephone number to be given to complete strangers who express an interest in the Shaklee earning opportunity. In this day and age of identity theft, privacy policies, and increasing protection of such consumer

¹ Under the Shaklee business model there is no consideration paid by the purchaser to the Company for the business opportunity since there is no additional fee required or paid when a Member becomes a Distributor. The Proposed Rule, however, would specify the sharing of profits as consideration. It is unclear how this would apply, if at all, to direct selling companies.

information, the Commission's suggestion to make such information readily available to anyone flies in the face of common sense and reason.²

If a new application, disclosure document and seven-day waiting period were required for a Member to become a Distributor, the number of Members who choose to build a small home-based business would dramatically decline. At one point in the 1990s, Shaklee did introduce separate Member and Distributor applications. We attempted to train our Distributors to offer both the opportunity to purchase products at a discount and the opportunity to build a business and to allow the prospect to choose. Distributors became confused with two different ways to start in Shaklee and, as a result, offered neither. Sponsoring rates dropped substantially, and in less than a year, the program was dropped. The Company returned to one application form, and business soon returned to its customary sponsoring rate.

An equal impediment to recruiting is the waiting period. Sign-ups occur at an in-home meeting or party, or at a one-on-one presentation. The cost of becoming a Shaklee Member is so nominal that it would seem ridiculous to ask a prospect to wait seven days (or any time period) before deciding to sign up to purchase products at a discount. The \$19.95 that Shaklee charges is less than COSCO or Sam's Club charges for membership and is less than the cost of all manner of household appliances and goods. If applications had to be handed out and prospects told they must wait seven (or any number of) days before signing and returning them as required by law, it would just as though regulators had painted a big "X" on the backs of direct selling companies, warning consumers "not to go there." This requirement alone would deal a tremendous blow to Shaklee and other direct selling companies. In addition, in Shaklee's case, the waiting period is totally unnecessary as the Company has long had a 90% buy back requirement for products, including the Member kit, purchased within the last two years.

As mentioned above, an individual can supply her Social Security Number at the time she signs an application and begin building a business right away, but that is the exception rather than the rule. Most people wish to become familiar with the products as consumers before considering selling the products to others. For

² It would be tempting for distributors of competing direct selling companies to express interest in an earning opportunity in order to obtain a list of 10 local distributors to target for their own businesses. More nefarious purposes can be readily imagined.

either, not only the waiting period, but also the disclosure requirements of the Proposed Rule, discussed in greater detail below, would create significant barriers to entry for legitimate direct selling companies such as Shaklee.

The Cost of Compliance Outweighs the Benefits of the Disclosure Requirements

The Rule as proposed requires that a seller state either the name, city and state, and telephone number of all purchasers who purchased the business opportunity within the last three years, or the name, city and state, and telephone number of at least 10 purchasers within the past three years who are located nearest to the prospective purchaser's location.

No direct selling company would publish the name, city and state, and telephone number of all those who became distributors within the last three years. A company's distributor and customer lists are its most important and confidential information which competitors must be kept from accessing, for all the reasons noted in comments filed with the Commission in response to the ANPR. That means a direct selling company would have to comply with the referenced requirement by providing the name, city and state, and telephone number of at least the 10 purchasers within the past three years who are located nearest to the prospective purchaser's location. This is not a list that the distributor could prepare, because those she recruited personally might not be those located closest to the prospective recruit. Therefore, each list of 10 or more would have to be prepared upon request by the company for its distributors.

Shaklee conducted a survey of its Distributors in June/July 2006. The Company sent an email invitation to 4211 Distributors and asked how many people they approached about becoming Shaklee Members or Distributors within the last month. Responses were received from 1025 of those invited. Results of the data indicate that the average number of people approached was 12. The Distributors then were asked of those, how many were interested in receiving information concerning the earning opportunity. The average number so interested was five.

Shaklee has approximately 235,000 Distributors in the United States. Shaklee estimates that approximately 80,000 of such Distributors are active in any given month. If each required an average of five reference lists per month, the Company would have to create 400,000 such lists per month.

The average time per call in the Shaklee call center is three minutes. The average cost per employee answering calls is \$21 per hour. The Company estimates that creating a customized reference list for each prospect would require an additional 1,200,000 minutes of call time per month. This would require the Company to employ an additional 270 call center employees, at an additional cost of \$5,670 per hour, \$226,800 per week, and \$11.8 Million per year. Obviously, if the Company's operating costs increased by \$11.8 Million per year, the Company's profitability would be dramatically affected. The Company would be forced to limit the number of calls each Distributor could make for reference lists. Such a limitation would severely impair the ability of a distributor to build her business, which would dramatically impact the sales and profits of any direct selling company.

The recordkeeping requirements of the Rule as proposed also would entail significant and wasted expense. Currently, Shaklee maintains on file all applications filed by its Distributors. These are too numerous to keep in paper form; therefore, the Company copies them onto a microfiche tape and retains the tape indefinitely. Under the Rule as proposed, the Company would need to retain for three years a copy of each customized disclosure statement, the earnings disclosure statement if attached, the list of references, the list of legal actions, and the receipt for the disclosure statement.

Based upon the survey conducted by Shaklee in June/July, this would mean an additional two million documents would need to be retained each month, or an additional 24 million documents per year. Shaklee would either have to pay a third party records company to store such a voluminous quantity of records, or all such records would need to be retained on microfiche, as Shaklee currently does with its application forms. Application forms are scanned by call center employees in times when call volumes are relatively low. However, it would not be possible for existing employees to scan such a large number of documents in their non-telephone time. Significant additional staff would either have to be hired, or the task would need to be contracted. Alternatively, the Company's records management and storage costs would be expected to increase by \$10,000 per month. Either alternative would create an unacceptable expense level.³

³ Significant additional expenses, which Shaklee has not yet quantified, would be incurred in creating and updating the list of legal actions and the cancellation/refund disclosures, as well as in educating and training Distributors concerning the new requirements.

These same requirements would impose unwarranted burdens upon Distributors, as well. Before a Distributor could recruit any prospect, the Distributor would need to call the Company and request a list of the ten individuals who signed up within the past three years living closest to the prospect. This would mean an extra five calls per month by the Distributor to the Company, which would add telephone expense and take up the valuable time the Distributor has to devote to her small home business.

The recordkeeping requirements would burden the Distributors, as well. They currently maintain applications submitted directly to them, receipts for product purchases made directly from them, and bonus statements for themselves and any Distributors they pay directly. If they also had to retain a copy of each disclosure statement, the list of references, the list of legal actions, and the receipt for the disclosure statement for every person to whom they present the opportunity, their storage requirements could easily expand beyond a small area in the home and make maintaining this simple home business unattractive.

In short, the expenses that just one company and its distributors would incur if the Rule were to take effect is several times greater than the \$4 million initial estimate and \$3.2 million annual estimate that the Commission has calculated for the entire industry. Taking into account that thousands of businesses and hundreds of thousands of individuals would have to comply, the overall cost of this Rule is likely to exceed \$100 million.

The Proposed Legal Action Disclosure Requirement is too Broad, Disfavors Long-Tenured Companies, and Encourages Companies to Violate Employment Laws

The proposed requirement that companies offering business opportunities must disclose all litigation over a ten-year period involving claims of fraud, deception or misrepresentation would generate irrelevant and disparaging information to prospective members or distributors of established companies. Litigation is a fact of life for any substantial company that has been in business for years. And no matter the dispute, litigation frequently entails claims of misrepresentation or similar issues. Most such allegations are never proven, but the disclosure of such disputes will nonetheless disparage the reputation of established

businesses and impede their ability to compete. Against these costs, Shaklee can identify no benefits that such requirement would confer.

In addition, by extending the disclosure requirement to literally all employees in the sales area, a company would want to screen prospective sales department employees for involvement in such actions. However, to do so could well contravene both federal and state employment laws.

The Rule Could Classify Every Contract as an Earnings Claim While Imposing Impossible Burdens on All Sellers Who Make Earnings Claims

The definition of earnings claim is so broad that it would apply to virtually every contract describing the financial terms of distribution. A "representation that...conveys...a specific level or range of actual or potential sales, or gross or net income or profits, [including but not limited to any] calculation that demonstrates possible results based on a combination of variables...." (Section 437.1(h)) is the essence of any contract between any person who sells goods or services on behalf of another. Read literally, this provision makes it impossible to avoid making earnings claims if a direct seller enters into contracts with, or describes payments to, distributors.

The Requirement to Provide an Analysis of Purchasers "Characteristics" Will Make it Impossible to Make an Earnings Claim

The Proposed Rule would require that a seller disclose:

Any characteristics of the purchasers who achieved at least the represented level of earnings, such as location, that may differ materially from the characteristics of the prospective purchasers being offered the opportunity;

Section 437.4(a)(4)(vi). In direct selling businesses, earnings do not typically depend upon geographic location since many, if not most, distributors have earnings derived from locations other than where they live. Rather, earnings depend upon myriad leadership abilities and talents of the individual. It would be impossible to compare these characteristics to those of a prospective purchaser. Fundamentally, this requirement means that no earnings claims could be made. But if it is impossible to enter into contracts without making earnings claims, then this requirement also would mean that violations are inevitable for any direct seller who enters into contracts describing how distributors are paid.

The Cancellation and Refund Request Data Requirement is Ambiguous and Does Not Provide the Prospect with Useful Information

Section 437.3(a)(5) requires companies to:

State the total number of purchasers of the same type of business opportunity offered by the seller during the two years prior to the date of disclosure. State the total number of oral and written cancellation requests during that period for the sale of the same type of business opportunity.

Many Shaklee Distributors do business as partnerships, corporations or Limited Liability Companies. Shaklee receives numerous requests to add and delete members of these entities. In some instances, this requires the entity to be dissolved and reformed under a new Federal Employer Identification Number. All of these are oral or written requests for cancellation of one form or another, but all are information which is completely useless to a prospective distributor and a waste of time and expense to tally.

Conclusions to be Drawn

The Rule as proposed is unworkable for direct selling companies and their distributors and ineffective at combating the fraudulent sales of business opportunities. Direct selling companies should be exempted from the Rule by maintaining the reasonable threshold requirement of the Franchise Rule.

The \$500 threshold in the Franchise Rule was never intended to distinguish fraudulent operators from legitimate companies. Its purpose was to quantify an investment that justified the disclosures that the Rule required. After thirty years of inflation, the Franchise Rule threshold has declined to a fraction of its initial value. The Commission does not explain in its proposal why this diminished threshold is no longer appropriate to identify business practices that are likely to impose significant harm to consumers. Nor does the Commission explain how a rule would have enhanced the agency's ability to prevent such frauds from occurring in the first place. Consumers with more information are of course less likely to be deceived than consumers with less information. But this simple proposition does not distinguish business opportunities from any other transaction in the marketplace.

If the \$500 set by the Franchise Rule has proved to be too high, then the Commission should explain how it has missed the mark and how it should be adjusted to allow legitimate direct selling companies to continue to operate without the enormous burdens imposed by the Rule as proposed. Whether the level should be changed at all is open to question. The one threshold that makes no sense is that in the current proposal. Alternatively, the Commission should rely upon Section 5 of the FTC Act, under which it has ample authority to deal with companies committing fraud upon the public. Such companies will not comply with the Rule as proposed in any event. It will only burden legitimate companies, as to which it is not needed in the first place.

Similarly, there is no reason to expect the proposed waiting period before a person can sign an application to be more effective than far less intrusive alternatives. For example, the Commission might apply a cooling off period during which the purchaser would have a right of rescission. The current three-day cooling off period for purchases of products has worked well for consumers. Before imposing a requirement that could cripple direct selling, the Commission should explain why such alternatives would not be sufficiently effective.

The 10 reference list requirement should be discarded for direct selling companies. In Shaklee's case, large numbers of Distributors list themselves under "Shaklee Distributor" in the White Pages of the telephone directory. Hundreds of Distributors maintain a personal web site on Shaklee.net. A prospect would have no difficulty finding 10 or more Shaklee Distributors with whom to discuss the opportunity. Customized lists not only are unnecessary, they create significant privacy concerns for the Distributors whose information is disclosed to, and potentially misused by, complete strangers.

It is not clear that the legal action disclosure requirement could ever be sufficiently tailored to meet its intended objective. At a minimum, the legal action must relate fundamentally to the earning opportunity, but any attempt to draw this distinction in a rule that applies to numerous industries is likely to miss the mark. Routine business disputes that have allegations of misrepresentation, which are all too common in today's business world, should not be required to be disclosed. Actions involving "sales managers" or literally any employee of the sales department of a company would require a company to screen for this in the hiring process – a practice that would not be permitted by the employment laws of this Company's home state of California.

Shaklee Corporation

Federal Trade Commission/Office of the Secretary

July 13, 2006

Page 13

A company should not be required to list the characteristics of the purchasers who achieved the represented level of earnings that may differ materially from the characteristics of the prospective purchasers. In direct selling businesses, earnings do not typically depend upon geographic location. Rather, they depend upon the leadership abilities and talents of the individual. It would be impossible to compare these characteristics to those of a prospective purchaser. Fundamentally, this requirement means that no earnings claims could be made.

Shaklee receives many requests to delete one or more names from a partnership, corporation or Limited Liability Company. It is unclear whether such requests would have to be counted as cancellation requests and reported to a prospect. These would be difficult and burdensome to track and report, and would be useless information to a prospect in any event.

In conclusion, the Rule as proposed does not fit Shaklee or the typical direct selling company. Such companies should be exempted through an industry classification or a proper threshold requirement. Even if aspects of the Rule as proposed are retained, the Rule needs a major reassessment and revision before it could reasonably be implemented by direct selling companies and their distributors.

Respectfully submitted,

Marjorie L. Fine

MLF/ams