

Knowledge Is Power In The World Of Business Opportunities

You've thumbed through the business magazines, you've seen the ads, you've gone to a multitude of helpful trade shows, and you're finally ready to buy a business opportunity... or are you? Not so fast. Before you sign on the dotted line, there are a few things you should know.

While buying a franchise usually offers you a complete system for doing business, business opportunities generally offer much less guidance. After you buy the seller's idea

Land Of Opportunity

or product, you often have the freedom to name your business, develop your own operational systems, create a marketing plan and more.

With this greater freedom, however, comes a degree of risk. Fortunately, federal regulators are working to lessen that risk by cracking down on business opportunity sellers. Still, sellers are responding slowly to new regulation in many

"Let the buyer beware" still holds true in the biz op world. But boosted by federal regulations and your own research, you can come out on top.

cases, and you can't rely solely on Uncle Sam to protect you. Despite the increasing regulation, rule number one in the business opportunity arena is still "let the buyer beware."

State Of The States

In conversations with business opportunity enforcement authorities nationwide, the same message is repeated: They are determined to eradicate what they see as "outrageous" fraud in the world of business opportunity sales, and they are gearing up to accomplish this goal.

"We've beefed up our enforcement of the Connecticut Business Opportunity Investment Act over the past year, and we're very pleased with the results," says Ralph A. Lambiase, director of the Securities and Business Investments Division of the Connecticut Department of Banking. "We have a larger enforcement staff, and our state newspapers and individual investors are becoming better educated about business opportunities through our investor edu-

cation program and brochures."

Local newspapers are perhaps the most effective collaborators in state agencies' efforts to enforce business opportunity laws. "In Connecticut, a number of newspapers include a conspicuous notice in the business classified section suggesting that readers contact us before they invest their savings [in a business opportunity]," says Lambiase. "That way we can alert investors to potential registration or disclosure problems before their money is gone. We believe this is our best bet for helping people before they make a purchase, especially for those making smaller investments."

"We've also alerted the papers [by providing information on government regulatory actions] to sell-

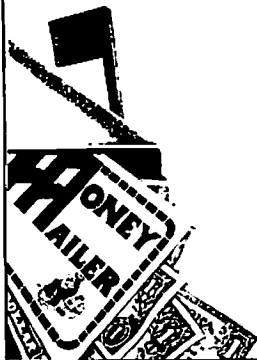
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BY ANDREW A. CAFFEY

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ers that have caused serious problems in the state," Lambiase adds. "Newspaper editors share our concerns about these companies, and tell us they now review their advertising more carefully. Frequently, the papers call us when they receive an advertisement to see whether the company is registered."

Michigan is following this trend. "We've seen more business opportunity programs come into Michigan in the past year," says Robert C. Ward Jr., the state's assistant attorney general. "The reasons are [the same as in many states]—high unemployment and many executives who have left corporate positions and have cash to invest."

"While the number of companies that register under our law is increasing," Ward continues, "there are some particularly outrageous problem areas. We've investigated several fraudulent vending machine

programs selling everything from candy to health food. They sell inferior vending equipment claiming it's high quality, and promise location assistance that doesn't materialize. Most outrageous, notices on their vending machines [fraudulently] claim that a portion of sales will be sent to certain nationally known non-profit organizations. This lends an unfortunate seal of legitimacy to the vending program, which in many cases is simply not true."

It's difficult to measure the number of enforcement actions taken by the various state agencies that enforce business opportunity laws, but every indication is that the numbers are going up. "Our enforcement program allows us to investigate every written complaint we receive about business opportunity transactions in Connecticut," says Lambiase, "and the number of complaints we receive has been increasing."

Seller Beware

Many entrepreneurs offering innovative programs to allow others to start their own businesses are not aware they are violating business opportunity laws. The following questions will help you determine whether you should be concerned about selling so-called "business opportunities" or "Seller-Assisted Marketing Plans."

1. Do you sell a program, materials or equipment that enables the purchaser to start a business? (Some states include enhancement or maintenance of an existing business.)
 2. Is there a payment of \$500 or more for goods, supplies, equipment or services? (Some state definitions have a lower threshold.)
 3. Do you make any of the following representations? (Representations include not only oral statements and written promises, but also advertising copy and promotional brochures.)
 - a) You provide assistance in locating sites for vending machines (or any coin-operated devices).
 - b) The business opportunity is a secured investment.
 - c) There is a market for any goods or services produced, sold or made by the purchaser.
 - d) You will buy back any products made, grown or sold by the purchaser.
 - e) The purchaser will operate a profitable business and will generate revenues in excess of his or her investment.
 - f) You guarantee money can be made. (A guarantee has been construed by one federal court where the word "guarantee" was never used, but the company's advertising conveyed that impression.)
 - g) You provide a "marketing plan" (an extremely broad concept).
 - h) You refund the purchase price if the purchaser is dissatisfied.
- Of course, there are exceptions and exclusions in these statutes, and they, too, vary from state to state.

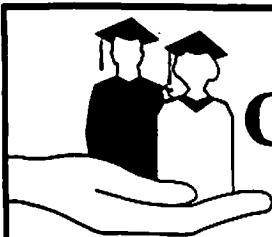
Federal Protection

Since 1979, the Federal Trade Commission's (FTC) Franchise and Business Opportunity Rule has required franchisors and business opportunity sellers to provide full presale disclosure to purchasers. The FTC can also bring civil actions against people or companies that violate the rule or mislead investors with deceptive practices. And lately, it has been bringing these cases against franchisors and business opportunity sellers at a faster pace than ever.

Eileen Harrington, a top enforcement attorney at the FTC's Bureau of Consumer Protection, makes the FTC's aggressive enforcement posture crystal clear. "In many instances, business opportunity packages are priced at \$495—on the theory, I suppose, that the price fails to meet the minimum \$500 investment requirement for the application of the FTC's Trade Regulation Rule," says Harrington. "But this won't stop us if there's consumer fraud. The FTC can bring action against fraudulent operators not only under the FTC Franchise Rule, but also under our law regarding misrepresentation and deceptive practices, and that's not limited by the investment level. We have been very successful pursuing this line of enforcement."

The FTC has brought approximately 30 cases in the past four years, most of them against business opportunity sellers. It has won civil judgments for violations of the disclosure requirements and secured court orders for huge sums to be repaid to injured purchasers.

"Our trade show enforcement efforts have also been very effective," says Harrington. "FTC staff members have visited a large number of franchise and business opportunity trade shows over the past year, and we will visit more in the future. We still find hyped-up earnings claims being made openly at trade shows; in fact, several investigations underway right now may lead to civil actions on the basis of unlawful and inflated earnings claims. We routinely contact trade show promoters to get their assistance in assuring compliance with federal law. We've even suggested these promoters may



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also be liable if deceptive practices take place at their shows."

Collaboration with state authorities has paid off handsomely for the feds, Harrington says: "The FTC is working closely with state attorneys general in our enforcement cases and investigations. That allows us to extend our reach and move quickly when we must." With the seriousness of someone out to change the very business of business opportunities, Harrington concludes, "We are everywhere!" (For another perspective on the FTC and its enforcement of franchise rules, see "Tough Enough?" on page 212.)

Buyer Beware

Despite all this stepped-up enforcement activity, business opportunity buyers are still largely on their own when choosing an opportunity to invest in. How do you protect yourself when buying a business opportunity? The answer is twofold: reliable information and common sense.

Gathering information is a substantial challenge, but is well worth the effort. (See "For More Information..." on page 91.) As in other areas of business, information is power, so find out everything you can about the company offering the opportunity.

Take advantage of the tools available to you. Does your state regulate business opportunity sales? Find out and contact the enforcement office. How long has the company been registered in the state? Are there complaints on file? The Better Busi-

ness Bureau is always a good place to check. Most important, interview other buyers to see if they are pleased with their purchase.

Use your common sense when buying a business opportunity; you'll need every ounce of it to counterbalance the siren song of profit. For reasons best left to sociologists, Americans often part with \$5,000 on the promise of making a profit more easily than they part with \$50 to buy a home appliance.

Be slow to invest; don't let yourself be rushed or cajoled into spending your money. The opportunity can wait another week, despite what sales representatives tell you about opportunities "going fast."

Negotiate every step of the process. Be creative about protecting your money: Use escrow accounts to make sure you receive delivery and are pleased with your purchase. Finally, seek the advice of either a lawyer or an accountant; it's money well spent in protecting your assets.

Back To The Future

The future of business opportunity regulation in this decade is clear: The FTC and the states are increasing enforcement and decreasing tolerance of deceptive or misleading sales tactics. Franchise and business opportunity trade shows are following this lead. Show promoters, under growing pressure from regulators, are less receptive to companies that make exaggerated earnings claims and fail to register their offerings

Rules And Regulations

Twenty-four states and the Federal Trade Commission regulate sales of "business opportunity ventures," also known as "Seller-Assisted Marketing Plans," but apply a wide variety of definitions as to what exactly is being regulated. Virtually any investment that allows the purchaser to start or maintain a business, and that makes claims regarding profitability, a marketing program or vending machine location assistance, risks being regulated under state or federal law. Laws may require the seller to give a disclosure document to prospective buyers before closing the sale, to register the offering with the state, or to comply with bonding and escrow regulations.

The 24 states regulating business opportunity sales are Alabama, California, Connecticut, Florida, Georgia, Indiana, Iowa, Kentucky, Louisiana, Maine, Maryland, Michigan, Minnesota, Nebraska, New Hampshire, North Carolina, Ohio, Oklahoma, South Carolina, South Dakota, Texas, Utah, Virginia and Washington.

—A.A.C.

with state authorities.

The business opportunity market will undoubtedly also be hit by fallout from the franchise wars being waged in Congress and numerous state legislatures. Business opportunities are often blamed for franchising's problems, and they make an easy target for political rage. As the franchise wars heighten the consciousness of politicians and enforcement agencies alike, business opportunity sellers can expect to feel the heat of additional scrutiny.

In this brave new world of regulation, business opportunity sellers are slowly becoming more sophisticated. It remains to be seen which companies can adapt quickly enough to survive what may well become the great business opportunity shakeout of the 1990s. ■

Andrew A. Caffey is a partner in the Washington, DC, office of Venable, Baetjer, Howard & Civiletti, where he heads a national practice team specializing in distribution, franchising and business opportunity law.

For More Information

There are several sources of additional information for business opportunity sellers and prospective buyers.

1. For Buyers: National Business Opportunity Services, P.O. Box 6271, Washington, DC 20015-0271, offers the *National Buyer's Guide* (\$16.95), which explains various types of investments (business opportunities, franchises, multilevel marketing programs, sales representatives, distributorships and dealerships); how to investigate these investments; steps you can take to protect your investment; and a summary of state and federal laws across the country protecting business opportunity buyers, franchisees, sales representatives and others.

2. For Sellers: National Business Opportunity Services (address above) also offers the *Business Opportunity Seller's Compliance Kit* (\$95), containing copies of all state business opportunity statutes, the Federal Trade Commission's (FTC) Franchise and Business Opportunity Rule as well as other useful materials. This organization has also announced plans for a new letter for business opportunity sellers with information on legislative and marketing news. Write for subscription information.

3. For Sellers And Buyers: A number of state enforcement agencies (attorneys general, consumer protection offices) and the FTC offer informative pamphlets on business opportunity sales. At the FTC, write to Public Reference Branch, Federal Trade Commission, Washington, DC 20580, or call (202) 326-3128 and request information about the Franchise and Business Opportunity Rule.

State business opportunity law administrators typically provide information on their state's laws, although some may charge you. Contact your state agencies. For a list of states regulating business opportunity sales, see "Rules And Regulations" on page 90. —A.A.C.

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