

Supporting Statement
Business Opportunity Rule
16 C.F.R. Part 437
(OMB Control Number: 3084-0142)

1. Necessity for Collecting the Information

Since 1978, the Federal Trade Commission (“FTC” or “Commission”) has enforced the Trade Regulation Rule on Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures (“Franchise Rule”), 16 C.F.R. Part 436 (OMB Control No. 3084-0107). The Commission amended the Franchise Rule on January 23, 2007, separating it into two parts, 16 C.F.R. Parts 436 and 437. Part 436 is the amended Franchise Rule, which covers the sale of business format franchises. Part 437 is the Trade Regulation Rule on Disclosure Requirements and Prohibitions Concerning Business Opportunities (“Business Opportunity Rule” or the “Rule”), and it covers the sale of non-franchise business opportunities.¹ The disclosure requirements in Part 437 are essentially identical to the original Franchise Rule.

The original rulemaking record revealed evidence of widespread deceptive and unfair practices in the sale of franchises and business opportunities. To correct these problems, the Business Opportunity Rule requires business opportunity sellers to furnish to prospective purchasers a disclosure document that provides information about the seller, the seller’s business, and the nature of the proposed business relationship. Additional disclosures are required if a seller makes claims about the earnings a purchaser can achieve with the business opportunity that is offered for sale. The seller must also preserve the information that forms a reasonable basis for such claims.

The Rule requires that all disclosures be made at least ten business days before any sale, and that sellers use disclosure documents compliant with the form and content specified by the Rule. The Rule also requires disclosures of all material facts. It does not regulate the substantive terms of the relationship between business opportunity seller and purchaser.

2. Use of the Information

Prospective business opportunity buyers use the disclosures both to become better informed about the prospective investment and to verify the seller’s representations.

If the business opportunity seller chooses to make financial performance claims, disclosures are necessary to enable a prospective purchaser to analyze the credibility of those claims. For example, a business opportunity seller might represent to a prospective purchaser that s/he should expect annual sales of \$50,000. Without the Rule, the prospective purchaser might have difficulty in assessing the accuracy or reliability of the claim. To make sure the prospective purchaser can accurately assess the claim, the Rule requires the business opportunity

¹ Part 437 continues to govern sales of non-franchise business opportunities, pending completion of the Business Opportunity rulemaking proceedings advanced in a Notice of Proposed Rulemaking published on April 12, 2006.

seller to: (1) indicate the number and percentage of purchasers whose performance equaled or exceeded the claim; and (2) save and offer to show prospective purchaser the background material upon which the claim is based. This allows the prospective purchaser to form an independent judgment about the reliability of the claim. It also discourages the use of unrealistic financial performance claims, because the business opportunity seller knows that the prospective purchaser can determine whether an earnings claim is credible by examining the background material. The Rule also requires that any background material must be shown to the Commission during a compliance investigation so that the Commission can evaluate whether or not the basis for the claim is reasonable.

3. Consideration of Using Improved Information Technology to Reduce Burden

Since the Rule went into effect in 1979, the expanded use of computers has reduced the time needed to generate initial disclosure documents, prepare updates, and audit financial statements. Consistent with the aims of the Government Paperwork Elimination Act, 44 U.S.C. § 3504 note, the Commission is considering amending the Rule to permit business opportunity sellers greater latitude in using new technologies, in particular the Internet, to further reduce compliance costs. See Revised Notice of Proposed Rulemaking, Business Opportunity Rule, 73 Fed. Reg. 16110 (March 26, 2008). Business opportunity sellers would be able to reduce significantly printing and distribution costs through the expanded use of email and the Internet to furnish disclosure documents.

4. Efforts to Identify Duplication/Availability of Similar Information

More than twenty states have some kind of business opportunity sales regulations. These state regulations, however, are not uniform, varying widely both in their coverage and in the disclosure requirements. Accordingly, coordination with all states to reduce duplication efforts would be impracticable. The Commission is considering amending the rule to streamline the disclosure requirements substantially and thereby reduce the compliance burden. See 73 Fed. Reg. 16110.

5. Efforts to Minimize Burden on Small Businesses

Unlike business opportunity regulations in many states, the Rule does not require a seller to register or file disclosure documents with the government as a prerequisite to a sale. Thus, compliance with the RPBOR does not invoke the fees usually associated with registering or filing disclosure documents, a consideration that might be especially important to small businesses.

6. Consequences of Conducting Collection Less Frequently

Any reduction in the frequency of collecting information required by the Rule would not be appropriate given the Rule's purpose to ensure that all prospective business opportunity purchasers receive valuable and accurate pre-sale information about the proposed investments.

7. **Circumstances Requiring Collections Inconsistent with Guidelines**

The collection of information in this Rule is consistent with all applicable guidelines contained in 5 C.F.R. § 1320.5(d)(2).

8. **Consultation with Outside Sources**

The Commission has had a long history of seeking outside input regarding the Franchise Rule and the Business Opportunity Rule. In 1995, the Commission conducted a review of the Franchise Rule as part of its program to review periodically all Commission trade regulation rules and guides, and published in the Federal Register a Notice for Comment on the Rule. See 60 Fed Reg. 17,656 (April 7, 1995). Among other things, the Commission sought comment on: (1) the continuing need for the Rule; (2) the costs and benefits of the Rule; and (3) what changes, if any, should be made to the Rule to reduce the burdens and costs imposed on the firms subjected to its requirements. In addition, the Commission sought comment on whether the Franchise Rule's disclosure requirements are appropriate for business opportunity sellers, whether there should be a separate business opportunity trade regulation rule and, if so, the scope of coverage. In response, the Commission received numerous comments from franchisors, franchisees, business opportunity sellers, state regulators, trade associations, law firms, and academicians. The Commission also held two public workshop conferences on the Rule, in which 56 individuals participated in round table discussions on the Rule or otherwise made statements for the record. All of the comments and the transcripts of the public workshop conferences were placed on the public record.

Subsequently, the Commission published an Advance Notice of Proposed Rulemaking ("ANPR") in the Federal Register, announcing its intention to consider amending the Franchise Rule. See 62 Fed. Reg. 9,115 (February 28, 1997). In the ANPR, the Commission summarized the Rule review record on the continuing need for the Franchise Rule. At the same time, the Commission proposed promulgating a separate business opportunity rule, which received overwhelming support from commenters.

Through the ANPR, the Commission also sought comment on multiple issues regarding a separate business opportunity rule, including: (1) the proper scope of any business opportunity sales rule; (2) how to define the term "business opportunity"; and (3) the types of disclosures that are warranted for business opportunity sales.

In response to the ANPR, the Commission received 167 comments through letters, e-mail, and a telephone message line. In addition, the Commission has held six public workshop conferences throughout the United States, three of which focused exclusively on business opportunity sales issues. Sixty-four individuals participated in the workshops, including franchisees and franchisee representatives, franchisors, business opportunity sellers and representatives, state franchise and business opportunity regulators, and computer consultants. The workshop conferences generated transcripts totaling 1,548 pages. As with the responses to the Rule review, commenters continued to express wide support for separating the disclosure requirements for franchisors and for business opportunity sellers through the promulgation of a

separate business opportunity rule.

In 1999, the Commission proposed a revised disclosure law that would, among other things, separate the disclosure requirements pertaining to business opportunities from those pertaining to business-format franchises. 64 Fed. Reg. 57,294 (October 22, 1999) (“Notice of Proposed Rulemaking”). Though the discussion of compliance burdens focused primarily on those requirements the Franchise Rule imposed upon business-format franchises, the Notice of Proposed Rulemaking identified some of the compliance burdens upon business opportunities. No comments were received on that issue.

In 2007, the Commission issued a Statement of Basis and Purpose (“SBP”) on the Franchise Rule and the Business Opportunity Rule. See 72 Fed. Reg. 15,444 (March 30, 2007). Apart from explaining the changes to the Franchise Rule, the SBP explained that business opportunities previously covered under the Franchise Rule would remain covered, without any substantive change, under a new trade regulation rule pertaining only to business opportunities, the Business Opportunity Rule. The SBP engaged in a full Paperwork Reduction Act (“PRA”) analysis of the burdens the Business Opportunity Rule would impose on covered entities.

Finally, the Commission sought public comment regarding its latest PRA clearance request for this Rule. See 73 Fed. Reg. 38,451 (July 7, 2008). The PRA compliance estimates published in this latest notice are identical to those published in the SBP. The Commission received no comments. Pursuant to PRA implementing regulations under 5 CFR Part 1320, the Commission is providing a second opportunity for public comment on its burden analysis, contemporaneous with this submission.

9. Payment or Gift to Respondents

Not applicable.

10. Assurances of Confidentiality

The collection of information in this Rule is consistent with all applicable guidelines contained in 5 C.F.R. § 1320.5(d)(2). To the extent that information covered by a recordkeeping requirement of the Rule is collected by the Commission for law enforcement purposes, the confidentiality provisions of Sections 6(f) and 21 of the Federal Trade Commission Act, 15 U.S.C. §§ 46(f) and 57b-2, will apply.

11. Sensitive or Private Information

Under the Rule, a business opportunity seller must disclose certain purchaser’s names, business addresses, and telephone numbers. This information lets prospective purchasers conduct their own due diligence investigation of the business opportunity seller’s claims; in particular, earnings claims. No other information about individual purchasers must be disclosed. For example, sellers who choose to make an earnings claim based upon the earnings history of current purchasers need not identify in the disclosure document the individual purchasers whose

information formed the basis of the earnings claim nor disclose their individual earnings.

12. Estimated Annual Hours and Labor Cost Burden

The estimated annual hours burden is 16,750 hours. Based on a review of trade publications and information from state regulatory authorities, staff believes that, on average, from year to year, there are approximately 2,500 business opportunity sellers, with perhaps about 10% of that total reflecting an equal amount of new and departing business entrants.

The burden estimates for compliance will vary depending on the particular business opportunity seller's prior experience with the original Franchise Rule. Staff estimates that 250 or so new business opportunity sellers will enter the market each year, requiring approximately 30 hours each to develop a Rule-compliant disclosure document. Thus, staff estimates that the cumulative annual disclosure burden for new business opportunity sellers will be approximately 7,500 hours. Staff further estimates that the remaining 2,250 established business opportunity sellers will require no more than approximately 3 hours each to update their disclosure document. Accordingly, the cumulative estimated annual disclosure burden for established business opportunity sellers will be approximately 6,750 hours.

Business opportunity sellers might need to maintain additional documentation for the sale of business opportunities in states not currently requiring these records as part of their regulation of business opportunity sellers. This might entail an additional hour of recordkeeping per year. Accordingly, staff estimates that business opportunity sellers will cumulatively incur approximately 2,500 hours of recordkeeping burden per year (2,500 business opportunity sellers x 1 hour).

Thus, the total burden for business opportunity sellers is approximately 16,750 hours (7,500 hours of disclosure burden for new business opportunity sellers + 6,750 hours of disclosure burden for established business opportunity sellers + 2,500 of recordkeeping burden for all business opportunity sellers).

The estimated annual labor cost is approximately \$3,595,000. Labor costs are determined by applying applicable wage rates to associated burden hours. Staff presumes an attorney will prepare or update the disclosure document at an estimated \$250 per hour. As applied, this would yield approximately \$3,562,500 in labor costs attributable to compliance with the Rule's disclosure requirements ((250 new business opportunity sellers x \$250 per hour x 30 hours per seller) + (2,250 established business opportunity sellers x \$250 per hour x 3 hours per seller)).

Staff anticipates that recordkeeping would be performed by clerical staff at approximately \$13 per hour. At 2,500 hours per year for all affected business opportunity sellers (see above), this amounts to an estimated \$32,500 of recordkeeping cost. Thus, the combined labor costs for recordkeeping and disclosure for business opportunity sellers is approximately \$3,595,000.

13. Estimated Capital and Other Non-Labor Costs

The estimate capital and other non-labor costs are \$3,887,500. Business opportunity sellers must also incur costs to print and distribute the disclosure document. These costs vary based upon the length of the disclosures and the number of copies produced to meet the expected demand. Staff estimates that 2,500 business opportunity sellers print and mail 100 documents per year at a cost of \$15 per document, for a total cost of \$3,750,000 (2,500 business opportunity sellers x 100 documents per year x \$15 per document).

Business opportunity sellers must also complete and disseminate an FTC-required cover sheet that identifies the business opportunity seller, the date the document is issued, a table of contents, and a notice that tracks the language specifically provided in the Rule. Although some of the language in the cover sheet is supplied by the government for the purpose of disclosure to the public, and is thus excluded from the definition of “collection of information” under the PRA, see 5 CFR 1320.3(c)(2), there are residual costs to print and mail these cover sheets, including within them the presentation of related information beyond the supplied text. Staff estimates that 2,500 business opportunity sellers complete and disseminate 100 cover sheets per year at a cost of approximately \$0.55 per cover sheet, or a total cost of approximately \$137,500 (2,500 business opportunity sellers x 100 cover sheets per year x \$0.55 per cover sheet).

Accordingly, the cumulative non-labor cost incurred by business opportunity sellers each year attributable to compliance will be approximately \$3,887,500 (\$3,750,000 for printing and mailing documents + \$137,500 for completing and mailing cover sheets).

14. Estimate of Cost to Federal Government

Based on recent years’ past experience monitoring compliance with and enforcing the Rule, and projected over the prospective 3-year clearance ahead, staff estimates that annualized cost for such activities will be approximately \$154,000. This estimate takes into account the Commission’s cost of identifying non-compliance in the marketplace, investigating targets, and prosecuting law enforcement actions in federal district court. The estimate includes time spent by attorneys, economists, and investigators, as well as clerical and support staff costs.

15. Changes in Burden

Not applicable.

16. Statistical Use of Information

There are no plans to publish any information for statistical use.

17. Failure to Display of the Expiration Date for OMB Approval

Not applicable.

18. Exceptions to the Certification for Paperwork Reduction Act Submissions

Not applicable.