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Bureau of Consumer Protection

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Can You Recognize a Business Opportunity Fraud?

A Maryland couple paid \$35,000 for a vending machine business opportunity on the promise they could net \$7,500 a month. They got a list of 25 business locations where they could place their machines. But when they tried to deliver the machines, none of the businesses wanted them. Six months after investing their money, the couple had yet to make \$50.

A Michigan man invested more than \$20,000 in an offer involving display racks of current music stars' CDs and tapes, but he didn't get the promised products. Instead, he got CDs and tapes of music from the 1960s, 70s and 80s. Many of the CDs appeared to be "used."

Another man invested more than \$10,000 in an opportunity in Florida involving candy machines. He found that the glass carousels on the machines didn't allow the candy to stay fresh: It melted, cracked or turned to powder.

Every year, thousands of consumers across the nation fall prey to fraudulent business opportunity promoters, even though many potential entrepreneurs are diligent about meeting with the promoters, checking references and verifying the business' legal status before they pay any money. Indeed, the Federal Trade Commission (FTC) says that fraudulent business opportunities consistently rank in the top 10 categories in the FTC's database of consumer fraud complaints.

"Some scam artists are really sophisticated," says Dan Salsburg, an attorney for the FTC. "They know exactly how to keep consumers from guessing the true nature of their business, by rounding up phony references or creating misleading documents."

But while the scams can be difficult to detect, Salsburg says there are tell-tale signs of fraud that a savvy consumer can learn to spot. For example, many fraudulent promoters use the classified sections of newspapers and magazines to advertise the so-called opportunities. Many offers show up as spam email or in Internet ads. The ads typically involve vending machines for candy, soda, snacks or personal care items; display racks for greeting cards, compact discs, perfume or similar items; or opportunities to buy into medical billing or envelope stuffing businesses or activities related to the Internet.

Other tip-offs to fraud include claims of high pay in a short period of time (weeks or months) for little effort ("work only hours a week"), and claims about ideal work conditions, like the ability to "set your own hours," "be your own boss," or "work from home." The opportunities may sell for several hundred dollars to tens of thousands, Salsburg says, with the average cost about \$5,000.

According to the FTC, many business opportunities offered through the classifieds or via spam email are “phantom” opportunities that have little chance of success — for example, a business with little or no demand in the market; cheap, low-quality or out-dated merchandise; poor customer service; and few, if any, locations. The locations that are offered often get little customer traffic.

So what’s a consumer to do? The FTC says it’s critical for consumers interested in buying a business opportunity to know their rights. For example, the FTC’s Franchise Rule requires most business opportunity promoters to provide certain kinds of information. Says Salsburg: “Consumers should know to look for the information. If it’s not there, the opportunity isn’t worth pursuing.”

The Franchise Rule

The FTC Franchise Rule is designed to protect would-be business owners from abuses by fraudulent promoters. The Rule requires promoters of business opportunities that sell \$500 or more to provide prospective buyers with certain information. For example, if the promoter claims — even in an ad — that buyers can make a certain amount of money, the number and percentage of previous purchasers who achieved that level of earnings must be included.

Promoters also must provide a franchise disclosure document that includes basic information about the promoter’s company, including whether it has faced any lawsuits from purchasers or lawsuits alleging fraud. In addition, the promoter must give potential purchasers the names, addresses and phone numbers of at least 10 previous purchasers who live closest to the potential buyer.

If you’re interested in pursuing a business opportunity, the FTC advises you to:

- Look at the ad. If it includes an earnings claim — but not the number and percentage of people who achieved it — the business opportunity seller is probably violating the law.
- Search the business opportunity’s franchise disclosure document for a statement about previous purchasers. If the document says there haven’t been any previous purchasers but the seller offers a list of references, be skeptical: the references probably are phonies.
- Get the list of 10 previous purchasers and interview each in person, preferably where their business operates. This can help reduce the chances of being misled by phony references.

Even if the business opportunity sells for less than \$500 and is not required to provide this information, Salsburg advises consumers to get it anyway — in writing. And, the FTC attorney says, “take your time. Promoters of fraudulent business opportunities often use high-pressure sales tactics to get you to buy in. But if the business opportunity is legitimate, it’ll be around when you’re ready to decide.”

Other Preventive Measures

Additional tips from the FTC:

- If the business opportunity involves selling products from a well-known company, call the legal department of the company whose merchandise you would be selling. Find out whether the promoter is affiliated with the company, and ask whether the company has ever threatened trademark action against this promoter or others.
 - Consult an attorney, accountant or other business advisor before you sign any papers or pay any money. If the promoter requires a deposit, ask your attorney to establish an escrow account until you close the deal.
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- Contact the attorney general's office, state or county consumer protection agency and Better Business Bureau, both where the business opportunity promoter is based and where you live, to find out whether there is any record of unresolved complaints. While a complaint record may indicate questionable business practices, a lack of complaints doesn't necessarily mean that the promoter and the business opportunity don't have problems. Unscrupulous dealers will change names and locations to hide a history of complaints.

Reporting Possible Fraud

If you suspect a business opportunity promotion is fraudulent, report it to:

- the FTC. File a complaint online at www.ftc.gov or call toll-free 1-877-FTC-HELP (1-877-382-4357).
- the state attorney general's office where you live and where the business opportunity promoter is based.
- your county or state consumer protection agency. Check the blue pages of the phone book under county and state government.
- the Better Business Bureau in your community and where the promoter is based.

The FTC works for the consumer to prevent fraudulent, deceptive and unfair business practices in the marketplace and to provide information to help consumers spot, stop and avoid them. To file a complaint or to get free information on consumer issues, visit www.ftc.gov or call toll-free, 1-877-FTC-HELP (1-877-382-4357). The FTC enters Internet, telemarketing, identity theft and other fraud-related complaints into Consumer Sentinel, a secure, online database available to hundreds of civil and criminal law enforcement agencies in the U.S. and abroad.