FEDERAL TRADE COMMISSION

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FEDERAL TRADE COMMISSION

In the Matter of:	)	
	)	Matter No. R-511003
FRANCHISE RULE	)	Volume 2

Friday, November 21, 1997

Federal Trade Commission
6th St. And Pennsylvania Ave., NW
Washington, D.C. 20580

The above-entitled matter came on for testimony, pursuant to notice, at 9:15 a.m.

APPEARANCES:

ON BEHALF OF THE FEDERAL TRADE COMMISSION:

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ON BEHALF OF THE AMERICAN FRANCHISEE ASSOCIATION:

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ALSO PRESENT:

Michael W. Chiodo, Executive Director, Domino's Franchisee Assoc.

Richard W. Galloway, RPM Pizza, Inc.

Nelson Hockert-Lotz, Domino's Pizza

Robert L. James, Division of Consumer Services, Florida

P R O C E E D I N G S

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MS. HOWARD: Good morning. My name is Myra Howard. I'm an attorney at the Division of Marketing Practices at the Federal Trade Commission. Today is November the 21st, 1997. This is the second day of our sixth and final public workshop conference regarding the Commission's franchise rule and its advanced notice of proposed ruling.

Today's meeting is open to the public. And, unlike yesterday's meeting, there's no set agenda. Today, members of the public are invited to make statements for the record concerning any franchise or business opportunity issues they wish to discuss. This is a reminder that the meeting today is a public meeting, and all statements will be transcribed and placed on the public record including on our internet website.

With that, if you could state your name for the record and begin.

MR. CHIODO: My name is Michael W. Chiodo, C H I O D O. I'm executive director of the Domino's Franchisee Association and former franchisee. I owned from one up to nine with a total of 12 franchises over a period of almost 13 years. I want to make a couple points.

One is renewal of contracts. When I signed my agreement and then when I went to renew my agreement for my area, which was the second phase, I had a single-unit store, sold it, moved to another state, opened up in a new area. When I went to renew my contract, depending on what contract I had, I was required to pay an additional three or four percent, which I found with the profits I was making, it was restrictive to me.

Another point I want to make is the sourcing of goods which I know affects the franchisees across the board. The scenario that's really created is, you sign a contract. We're supposed to be able to buy goods from a number of sources, provided that those sources come through the approval process. In theory, it's a great idea because we want consistency. That's part of why I have a franchise, part of why I was willing to pay the royalty.

One of the real exposures of that scenario is, through their approval process, it can become very difficult for a competing source of goods to be allowed to reach the franchisee in their store. So, particularly in the Domino's case where you have an equipment and supply division, Domino's will set up deals with certain suppliers, they run their equipment and supplies through the equipment and supply division and then to the franchisees.

Well, if, for instance, I want to buy a competing oven because I felt I can get a better deal or the price was high through the Domino's system, it really becomes completely up to the discretion of Domino's Pizza whether or not that competing oven can be sold to me.

Now, again, in theory, that can be a great idea because we want to make sure the oven works. In practice, I find that in some circumstances, it would appear that it becomes really restrictive to the point where you end up with one source. Particularly right now we are basically, for the different sizes of stores, we have one source of oven, we have one source of uniforms, we have one source of cheese. So, some of these things then, in practice, work out to be different than what they seem to be in theory.

One other issue I have as the executive director of the Franchisee Association is, I am not allowed to reach the new franchisees. That's entirely up to the discretion of Domino's Pizza. The UFOC every year puts them in, and I am allowed to go through that, if I can get my hands on it, and find the new people. But as they come in, I'm not allowed to see that and they have no information or knowledge.

There's no part of their training that introduces me as the association executive, so I have really no way to contact those people and they have no way of finding out, prior to -- certainly through Domino's any way in our system -- prior to buying your franchise, that there's an association. And there may be some issues that they may want to consider prior to signing their agreement, which I think in some situations becomes a concern. That's my point.

MS. HOWARD: Thank you.

MR. TOPOROFF: Do you have any questions?

MS. HOWARD: Yes I do, actually. If a prospective franchisee inquires as to whether or not there is a franchisee association, do you know what they're told?

MR. CHIODO: No, I do not.

MS. HOWARD: But unless they inquire, unless they also found out from another source, you're saying they wouldn't have a way of finding out directly from the franchisors.

MR. CHIODO: The franchisor, in our situation, has a series of trainings that they go through. And although I have requested to be a part of that training to inform the franchisees that there's an association and the things that we do, that's been refused. So, I know that there's no part of their formal training in the formal process that introduces them to the association.

MS. HOWARD: Do you think it would be useful to have an item in the UFOC or the disclosure document that would state whether or not there was such an association, give the name, address and contact person?

MR. CHIODO: I absolutely think that would be fair.

MR. TOPOROFF: I have a few questions about the association. My name is Steve Toporoff. I'm also with the Division of Marketing Practices. Could you explain a little bit about how the organization came into being and a little bit about its history?

MR. CHIODO: Sure. The organization was, through a few steps of evolution that started back in about 1981, which actually was formed by the company to address issues with the franchisees and give them all a forum, was a regional -- was basically five different regions.

Back in about the '89 range, the franchise leadership decided it should be a national organization. And in 1991, we actually went to Europe and organized European franchisees in Central America and organized a Central America franchise and created an international franchise account. Then, back in -- a lawsuit was filed in '95.

In 1995 for me, shortly after I sold my pizza stores, the franchise association was named on an antitrust -- federal antitrust lawsuit against Domino's Pizza. Shortly after that, Domino's, which had assisted funding the association -- initially funded all of it, and now at this point was assisting -- ceased funding. They were housed in Ann Arbor for convenience of meeting with people and stuff. That was removed -- the office was removed, and for the last couple years basically been independent, funded entirely by our own efforts.

And the communication which we had had, which started out -- tell me the ideas, tell me what the challenges are, let's work together on this -- seemed to me like once we reached a certain level of conflict, no longer were the ideas really welcome -- and not just on the antitrust sourcing of goods issues, but on other issues that may be contractual or any other real issues -- that the input from the association is not as welcome certainly as it used to be.

MR. TOPOROFF: I just want to make sure I understand this clearly. So, initially the group was started with either the endorsement of sponsorship or participation of headquarters and the franchise law.

MR. CHIODO: Correct.

MR. TOPOROFF: And now it is, what, completely independent of the franchisor?

MR. CHIODO: Correct.

MR. TOPOROFF: Of the existing franchisees in the Domino's system, what percentage would you say are members of this group?

MR. CHIODO: We have 39 percent of the U.S. stores and just over 300 franchisees. The number of franchisees in the system in the U.S. is approximately 1,200.

MR. TOPOROFF: Now, as far as the structure goes, you said the group is currently located in Ann Arbor.

MR. CHIODO: Currently, we're located out of Chicago.

MR. TOPOROFF: Chicago. Now, is there one central office?

MR. CHIODO: In Chicago.

MR. TOPOROFF: Now, are there regional offices, as well, or is that just one central office in Chicago?

MR. CHIODO: One central office.

MR. TOPOROFF: What communications, if any, does the group have with the franchisor at this stage?

MR. CHIODO: As a group, as a representation of those franchisees, the primary source of communication is through me. And the primary means is informal and primarily unpublishable. It's conversation that I may have with the current situation with the lawsuit. With the feelings from the company regarding the association, we aren't able to officially interact, we can't set up a contract committee that has some of our board members specifically designed so that we get different points of view. That kind of communication does not exist.

MR. TOPOROFF: Okay. I think that's all the questions that I have.

MS. KEZIOS: I have some questions. My name is Susan Kezios, president of the American Franchisee Association. Mike, do you want to explain a little in more detail, when you sold your franchises, some of the reasons? I mean, you talked about the increase in royalty. Upon renewal, it wasn't exactly you were renewing the same contract you had, is what I'm understanding. Is that correct?

MR. CHIODO: That's correct.

MS. KEZIOS: So, was the increase in royalty the only change you had a problem with?

MR. CHIODO: Increase in royalty and increase in advertising funds that totalled, depending on my contracts, depending when they were signed, three or four percent.

MS. KEZIOS: Did you have, when you decided -- did you sell all your stores at once, or did you get -- did you transfer them to somebody else piecemeal, one at a time?

MR. CHIODO: During the course of my franchiseeship, I bought one, two, three, four -- six stores -- bought five and built seven and sold in different periods.

MS. KEZIOS: Did you have post-termination covenants not to compete?

MR. CHIODO: Yes, with the franchisees who I sold them to, yes.

MS. KEZIOS: Meaning that franchisees couldn't be involved in a pizza business.

MR. CHIODO: Meaning I couldn't be involved in a pizza business.

MS. KEZIOS: Oh, once you left?

MR. CHIODO: Correct. Once I sold to him, I couldn't compete against him.

MS. KEZIOS: Did you have protected territories in your contracts with Domino's?

MR. CHIODO: I did, yes.

MS. KEZIOS: Do they now? Do they have that on the renewal contracts?

MR. CHIODO: They have protected territories, yes, different for single-unit franchise owners, different versus area franchisees, because I was both a single unit and an area. And some of the stores that I owned were single unit and then I had a big area. And then on the area, I was basically drawing a big line and that was my -- that was my space. Nobody could invade it basically. On the single unit, it became a lot more complicated. There's always been a continual -- I always call them border wars between franchisees and franchisees, corporate stores and franchisees, where somebody will move in and take some of the territory. And there's a system of mapping and protection that's supposed to be there. But in the reality of how it works, it becomes very difficult, and the border wars are very common, actually. So, even though you may have a protected area, there's still opportunity for that protected area to be violated.

MS. KEZIOS: By either a franchisee or a company-owned store.

MR. CHIODO: Either franchisee or company-owned store, be it by them coming in illegally, if you will, or be it by a store opening and the company saying, well, we need to change your area a little bit because this store really can service this better.

MS. KEZIOS: How is the protected territory disclosed to you? Do you remember that? What does it say? Does it say in the document, single-unit franchisees have this kind of protected territory? I'm asking you if you can remember, too, because I know it's been a while. Or area development franchisees have another protected territory? Do they then go on to say, It comes to our attention from time to time -- I'll use your phrase -- border wars occur? Do they go that far and disclose? Do they start telling you the practical reality of what starts happening as you're a small business franchisee in a disclosure document?

MR. CHIODO: I don't recall anything that gave me the impression that anyone would ever be threatening me or being into my area when I franchised. I must say for myself, I was personally protected just because of my locale. And the way they did it and described it in the contract, was both Route 137 to Hines (phonetic) Road south to -- as well as putting a map and drawing.

MS. KEZIOS: And just one other thing. What about venues, choice of law, if you have a dispute with the franchisor? Did Illinois law prevail because we have that, or did you have to go into Michigan?

MR. CHIODO: I know that we had to go to

Michigan at one point. I don't honestly know. I know at one point we did.

MR. TOPOROFF: Any other?

MS. KEZIOS: Was that a problem to go to Michigan?

MR. CHIODO: One of my franchises was in Michigan and the rest of mine were in Illinois. So, it wasn't a problem personally with me, but it has been a problem with other franchisees.

MS. KEZIOS: In what sense?

MR. CHIODO: If you have a problem, you have to go fight in the Michigan courts. As a matter of fact, we had an issue during the time that the association was primarily funded by Domino's. I had been elected by the franchisees and represented all of them and had an office in the executive wing. And we had some issues that we wanted to address with them, and it was -- it was very difficult to get any high level of attorney anywhere in Michigan, even though we had to go there. Because I had an attorney who had been with me since the beginning of my franchise who was helping me get somebody who was more specialized and bigger in these issues we were dealing with. And all the big firms had some connection to Domino's, and basically we were restricted from using them.

MS. KEZIOS: So, that made it difficult for you to find representation in the state that wasn't beholden to Domino's?

MR. CHIODO: Correct.

MS. KEZIOS: Would it help, upon renewal, if just the very process of renewal was not described as renewal?

MR. CHIODO: Renewal, to me, personally, means let's keep going, continue on with what we have. I know one of the big issues I had was the second largest franchisee at the time when I had this elected position in Michigan when they were -- when the association was funded by Domino's -- he was extremely upset because of the increase in royalties and advertising upon renewal that he was undergoing. And it really represented hundreds of thousands of dollars over the course of a year each year in renewing these contracts for 10 years. He had felt that the question had been asked at the time of his original contract, and he was told it's not going to affect money. The clause which I believe was in there was, You will sign the then-current contract. Well, that's okay if you're just -- some laws have changed and you need to make some adjustments. But when you start to affect the essence of the contract, like the numbers, you've kind of changed your agreement. It's not really a renewal. It's like starting over.

MS. KEZIOS: So, maybe describing it somehow differently, relicensing. "Rewrite" might at least -- when you're buying a franchise, you'll know you're not going to renew the same contract. Mentally you were prepared to renew -- go on making business changes, but I don't want you materially changing provisions for that might affect my gross, my net, my property, my assets, my equity. So, I'm asking you, would it help, just the semantics, to change "renewal" to "rewrite"? Would that help somebody in realizing it's not going to be the same contract?

MR. CHIODO: I would definitely change it from "renewal." Whether "rewrite" is the right word, I would have to think about it. The thing that would be helpful is to describe the changes that are allowed to take place. Because the then-current contract, if I started with royalties at four and a half percent and now it's seven percent, well, that's a substantial difference. I mean, the people think the profit margins in pizza are so big. They're not. And three or four percent can be 30, 40, 50 percent or even more of your profit.

MS. KEZIOS: So, it would help perhaps when they say the then-current contract -- maybe, for example, "we have been known in the past -- in the past, we have been known to increase royalties by X percent, increase advertising fees." I mean, that would be a little more truthful disclosure, and it would mean something to a person coming in. The words "then-current contract" might not mean reality to somebody coming in. Oh, yeah, I'll sign the then-current contract.

MR. CHIODO: It would seem to be a much fairer approach. They would be much more forewarned of the reality of what may happen 10 years down the road. Now that you're already in the community, you're doing your thing and you've got your life and somebody comes along after 10 years and says, Now, you have to give 40 percent of your profits back to us. And, you know, maybe services have increased, maybe they've stayed the same, maybe they've decreased due to their own budgetary restraints. Yet 30 or 40 percent of your profits has to go to them. And it's basically sign it or "see ya."

MS. KEZIOS: And especially if you've got three or four stores and you've got post-termination covenants. If you just get rid of one store and you've got one that comes up for renewal two years later, do you have a post-termination covenant not to compete with this second -- from this first store to the second store? Say, you say, Forget it, I'm not signing this new contract, I'll get rid of this store, but I got two years left here at the old rate.

MR. CHIODO: Sounds familiar.

MS. KEZIOS: So, what do you do? Don't you have a post-termination covenant? Aren't you supposed to not be in the pizza business after you sell off this store? What happens?

MR. CHIODO: I've not signed a contract that says I can't compete with this store. Now, I can't go in this area and then once I have sold all of the rest of them, I couldn't compete -- I think it was a 50-mile radius.

MR. TOPOROFF: So, then the covenant would not kick in until you were totally out of the business.

MR. CHIODO: Totally out.

MS. KEZIOS: And then go back to the sourcing, when you were talking about the sourcing of supplies. Go back and talk about -- you made the general comment that, It sounds good. We get our products for consistency sake or supplies from one source, but the practical reality of it is not so. And you kind of faded off there. Give us some practical reality of what you mean by that? What isn't good about that? Who should you be able to buy from?

MR. CHIODO: Well, here's a scenario that's current on the Domino's Pizza system. There is a supplier who is -- was supplying uniforms, a large uniform supplier to Domino's Pizza for a number of years while I was a franchisee. Lost a bid. Weren't allowed to supply any more. New suppliers are in. Domino's decides that there's going to be an image change and you need to update uniforms. Great idea. You need to do that from time to time. And now, there's one uniform supplier. This old uniform supplier puts in an application year and a quarter later, still is not approved. The date for purchasing your uniforms to turn over your stores, -- so in other words go from the old to the new -- the date is coming up for December 31. And a year and quarter ago, this uniform supplier had applied and gone through all the processes.

And I'm not going to get into any of those details, but here we are. We're coming right up to the end. They're still not approved to be the supplier. That would be okay if the philosophy was, Give a good uniform and have it be top quality and give it at a good, fair price. The price that people are paying for the uniform, although it may be fair, depending on how you judge it, certainly isn't low. And the quality is clearly inferior to what Domino's normal standards are.

Yet, there's still only one supplier, even though we have another supplier who's been trying to get in the game. That other supplier would not be distributing through Domino's equipment and supply, where the distributor that's currently doing the inferior product -- which is pretty clear through tears and fading and all that that have been going on -- supplies through the equipment and supply division. So, it may be a good idea to have a uniform supplier to get the best deal and you can control these. Here's a situation where you're getting an inferior product. You're certainly not getting it cheaply. We've got another supplier who's been proven in the industry, serves -- you name the big ones, they're there. And for one reason or another is not being approved.

MS. KEZIOS: So, what recourse do you have?

MR. CHIODO: None. And practical reality, it just would be nice to say that there was a process for making sure that -- that you could speed that along. But you really can't. It's a matter of processes within Domino's. Some of it certainly is justified, and they need to go through those processes. You just look at the facts and say, you know, these people supplied for years. It's been a year and a quarter. We're running to the deadline. We clearly got an inferior product, which you think a franchisor would say, we've got to get better uniforms out there, we have got to do something about this. But here's a situation from the franchisee side, brought in this other supplier and said, let's get someone else approved. But it hasn't happened. That's one example.

MS. HOWARD: On that same issue, do you recall what your disclosure document said about sourcing?

MR. CHIODO: I honestly --

MS. HOWARD: If it described whether or not, or what the process was?

MR. CHIODO: I honestly don't specifically, other than approval process through Domino's.

MS. KEZIOS: Do you have to use -- are you required to use their approved suppliers?

MR. CHIODO: In some instances, yes. If I want to buy a pizza cutter, no. If I want to buy an oven or anything to do with image, uniform, signage, yes.

MS. KEZIOS: You don't recall in the UFOC if it said this? This basic distinction you've just drawn that certain items you need to buy from us through approved vendors, and others you can buy on your own. Did it say that?

MR. CHIODO: Yeah. You know, Susan, I'm not sure whether it's an operating procedure or whether it's in the contract itself. Probably negligent there. But I do know that there's an approval process and you have to buy approved goods through Domino's on anything. I believe it just really indicates that some items that we will require you to have or to use will be -- will need to be approved.

MS. KEZIOS: Bought through approved suppliers. And they're also told there was an approval process.

MR. CHIODO: Right.

MS. KEZIOS: But what you're saying is that, I guess Domino's corporate is either not following their own approval process or unjustifiably stalling the approval process of this uniform supplier.

MR. CHIODO: I'm not drawing either one of those conclusions. I've just drawn out an example where you would think it would seem logically that, unless I'm missing something, in the best interest of the system, to get these other people out there, and they're still not out there.

MS. KEZIOS: Okay.

MR. CHIODO: Now, if you look at all the documents, perhaps as any approval process, sometimes it's in one guy's court, sometimes it's in the other guy's court, and where all that time frame goes, I'm not going to make the leap to say that Domino's is clearly being unfair in the situation. I'm just looking at it and saying, hmmm.

MR. TOPOROFF: Anything else?

MS. KEZIOS: No.

MS. HOWARD: Off the record.

(Pause in the proceedings.)

MS. HOWARD: We're back on the record, and just as a reminder, this is a public meeting and a transcript of today's proceedings will be placed on the public record.

Would you please state your name?

MR. GALLOWAY: My name is Richard W. Galloway. I work for RPM Pizza. It's the largest franchise in the Domino's Pizza franchise system. Our stores are in Mississippi and Louisiana. I also have two sons, Chris Galloway and Roger Galloway, who are franchisees in the Domino's system. And I serve as their advisor on long phone calls on occasion.

I would really like to add something to what Mike Chiodo has said. When a young person comes into the Domino's system, he is eager to have his own business, or she is eager to have her own business. They are not used to reading legal documents. I don't believe they're used to reading much. They don't -- they don't read a whole lot. And they depend on almost exclusively what Domino's Pizza tells them about the franchise experience. And I don't -- I don't think that's necessarily bad.

The franchisor has invented a system that works and is profitable, and I am not here to paint the -- anything, you know, negative about that system. What I do take great issue with is the ability of a young franchisee to get decent advice when they franchise. The franchisor gives them a UFOC and says, here, you have to sign this within 48 hours, or there's a time period, take it to your lawyer, get back to us. The general experience is, if there is a lawyer involved, that individual is probably in general practice, does not know franchise law. But worse than that, has no experience in franchising.

There ought to be some way in the UFOC that the prospective franchisee's advisor can feed into a system that can give them back useful information. The kind of thing that your previous witness has talked about. If there was some means of identifying how the professional advisor could get that information for the franchisee, it would at least give the prospect a fighting chance to understand the system they're signing into. Now, I'll give you an example of what I'm talking about.

Various financing packages are offered from time to time by the franchisor, if the franchisee will go into difficult areas where the company wants to develop stores. None of those packages, to my knowledge -- and I've looked at a lot of them -- have the right to pay off those contracts without penalty. Now, if you go to a bank and borrow $40,000 or $50,000, and you work like hell, and you make profits, you can pay that loan off and get rid of the -- get rid of the interest expense. You can't do that. And that's kind of buried in things. It never really gets talked about.

Those kinds of things are not qualified for the franchisee. They're -- the franchisee's really enthusiastic about the help they're getting. And that is fine. That's a good thing. But buried in the fine print is the devil, and the devil, in many instances, are restrictions that are not really pointed out to them.

If I go to a bank today and borrow on a personal loan, I'm given a piece of paper that points out certain rights and responsibilities as a borrower. That's federal law. But where a franchisee is placing him or herself in the hands of a franchisor over a 10-year period, there isn't such a means of the franchisor protecting him or herself. And there isn't a way that the franchisor or the franchisee's advisor can feed into a system that could give them back that kind of information. So, if there was some place in the UFOC where that could be noted as a matter of -- when the advisor reads the UFOC -- or maybe a synopsis of the UFOC that an advisor could read. That would point them in the right direction. They would at least have the opportunity to gain the kind of information that they need.

Here's another example. You sign a 10-year franchise agreement and it states certain rules and regulations and expectations on the part of the franchisor. When you renew that, it's an entirely different document that you're renewing. But worse than that, the policies and procedures, and especially the business practices policies of the company, which have the same effect as a written contract, have also changed and you're bound by those, too.

Now, one of the ways that that impacts franchisees is that at the end of a franchise agreement, if you have 10 stores and you've acquired them one at a time, you have 10 different franchise agreements. Now, do you throw away your whole career because you don't like that? It's not a level playing field. They've got you where -- they've got you where you can't really move. Even though it's a -- they argue that, well, it's a contract, it's a binding agreement, et cetera, et cetera, you don't realize the position that you're going to be in, you know, at the end of that time.

Now, if someone came to -- if someone came to Mike Chiodo, who is the executive director of the franchisee association, an attorney called and said, Well, what happens on renewals? He'd be able to at least tell the advisor what the deal is. So, I think that there ought to be this means of pointing the advisor and the franchisee in the right direction in order to determine really the effect of what those agreements are. That's what I would like for you to do, or that's what I'd like for you to know about.

MS. HOWARD: Thank you. Susan, do you have some questions?

MS. KEZIOS: So, what you're saying about the business practices of the company changing over time, is that, in effect, the operations manual, if you will, becomes a contract that the franchisee has never signed and it can change and is fluid, yet that they have to be in compliance with it at all times.

MR. GALLOWAY: Right. Now, I'm going to separate the operations manual from how you make and deliver pizza, the business practices. For instance, what you do in the pizza store belongs in the operational manual. The business practices would say, We won't allow a franchisee to own an equity position in another franchise. That's against our policies. Now, I don't know if that's written down anywhere. I don't think it is, is it? Outside investment is written down, finally. But for a long while, outside -- the rule on outside investment was a word of mouth, a business practice kind of thing. And that's -- you don't get those kinds of things in the UFOC.

MS. KEZIOS: I'm also getting the sense -- when you talk about the new franchisee coming into the system and they're putting their lives in the hand of a franchisor for the next 10 years, I'm getting the sense they feel like they're being taken care of by the franchisor. They rely totally on the trust they've put into the franchisor. But also, they're contemplating like they're building equity in themselves over the 10 years. And when, in reality, it's more like kind of renting an apartment, where the landlord can change the deal and will change the deal. And I'm trying to get a sense from you as to how that may be disclosed in the document.

MR. GALLOWAY: I think the only way it can be is if there is some resource listed in the UFOC that -- that, you know, they could go to to find out about it.

MS. KEZIOS: So, perhaps listing the existence of an independent franchise association and knowing how to get in contact?

MR. GALLOWAY: And defining what they can do. Defining what benefit that has for the franchisee.

MS. KEZIOS: You think the franchisor should define the benefit it has for the franchisee.

MR. GALLOWAY: I think that should be pointed out in reasonably decent language.

MS. KEZIOS: This is another source of information.

MR. GALLOWAY: Right.

MR. TOPOROFF: Any other questions? Okay.

MS. HOWARD: Thank you very much.

MR. HOCKERT-LOTZ: Nelson Hockert-Lotz, H O C K E R T -- L O T Z, and I'm a franchisee with Domino's Pizza. I'd like to say that I think one of the reasons I'm here is not because Domino's is a lousy franchisor, but because Domino's is actually one the best franchises in the country. It's a fabulous company and it's full of fabulous opportunity.

However, the world we live in today is not the world of our parents or grandparents. Today's small business environment is an utterly different, small business environment from what we had 20 years ago, and utterly different from what we had 40 years ago.

We have a global marketplace, not a local marketplace. We have a media-driven marketplace. And for most of us who start out as young people in American business today, franchises are not an opportunity, they are virtually a necessity.

I think it's critical for people to understand that I can't go and open a pizza place, and certainly not a series of pizza places, in many markets without signing as a franchisee with a major chain. Now, there are niche markets where, indeed, there is opportunity for independence. But the franchises hold the opportunities for my generation and for the next generation.

People who own -- open burger stores that say Bill's Burgers today, are not successful. They cannot get their piece of the economic pie. They cannot provide for their children in most cases. So, given the fact that involvement in a franchise or a larger business concept is almost a necessity -- the same way that at one time cars were made in barns, and when Ford Motor Company came along, cars would never be made in barns again, most food, most printing, most dry cleaning -- we are seeing the whole franchisation of our economy. And it's critical that the young people today and tomorrow have the opportunity to buy into that. And Domino's continues to be a fabulous company and a great opportunity.

However, the contract I signed with Domino's in 1984 as a young man just came up for renewal, and the franchise contract I was given to sign is an utterly different contract. And I think it's important to look at some key differences that, I think, certainly raise business questions, and I think in some cases even raise ethical questions. I think there are things in this contract that should not be legal.

Government has an important role to regulate a marketplace, when things become grossly unfair, and a balance of power. That's why, although you'll find people in fast food who may criticize the government for it, it's a critical function of government to set minimum wage standards. At the same time, in the franchise world, we have multinational companies that are being regulated state by state by different state laws, which is why there will be a whole bunch of state riders at the beginning and end of every UFOC.

Some of the issues that were brought up by the renewal that I just signed -- and I just signed because I had no choice but to sign -- there is, after the investment of 20 years of your life -- and it's been 20 years and four months that I've been with Domino's Pizza, first an employee and then as a manager, and finally as a franchisee -- after 20 years of investment in Domino's Pizza and assisting Domino's Pizza in building their system, serving on their committees, working very hard to bring value to the markets and new systems to their system, it is not economically feasible for me to get out. I don't particularly want to get out. What I would like to do is have a fair contract, a contract where I don't have questions about the ethics of the contract, in addition to factual areas of the contract.

Domino's Pizza has what were called "areas of primary responsibility" but essentially exclusive territories under my original contract. Under my current contract, there -- they now reserve the right to compete with me in the same lines of business under different marks within my own exclusive area. They have taken my exclusive area and given me -- saying, okay, you can deliver and make your money and capitalize your business, which is a critical issue, based on this population of 15,000 people within this area. However, we are giving you a circle that is one-ninth that size and that is now your exclusive area, except where we may compete with you with other concepts or under other marks. Okay. So, they give me an area with 15,000 people and then they give me an exclusive area in which they agree not to compete, not to award other franchises that are one-ninth that size.

There is no business in Domino's Pizza that could actually survive -- or very few businesses in Domino's pizza -- that could actually survive if they were paired to the exclusive area that is actually awarded in the contract. It is not economically feasible, and it would be impossible to capitalize -- or we would capitalize the business very, very differently. So, we rely on verbal assurances that are specifically banned within the contract in order to base our business.

This is not a good business decision. No attorney in reviewing this would say, you know, you have this little tiny area, and you're relying on a handshake for the bigger area that they specifically reserved the right to put other Domino's Pizza stores in. Domino's Pizza, at their whim and will, could put any small Domino's operator, or any large one, out of business very quickly simply by putting other stores within their primary area. Now, my regional directors assured me verbally that, of course, they would never do such a thing. But the contract clearly gives them that right at their sole discretion.

In the renewal, there was a blanket EFT authorization for -- naming Domino's Pizza as a signor, if you will, on my checking account to their benefit at any time they choose to use it.

MR. TOPOROFF: Could I just interrupt? Could you explain that a little? I'm not clear what that means.

MR. HOCKERT-LOTZ: Okay. And I have a copy of it. With my renewal contract, I got a form to be filled out by my bank and myself that gives Domino's Pizza the right to unlimitedly debit or credit my checking account without my approval. I mean, I'm signing a blanket approval that forever they will be able to go into my business checking account and my business savings accounts and credit or debit to their benefit without any further authorization from me.

Now, in my letter to Domino's Pizza, they sent me back a letter -- I did not complete this -- they sent me back a letter that says "Additionally, the authorization agreement for prearranged payments, debits -- for prearranged payments, direct debits was returned incompleted. This form is a required part of your 1997-'98 standard franchise agreement and needs to be completed by your bank. We will not execute your renewal documents to the above-referenced store until this form is completed in its entirety" which would terminate any franchise, which is how I support my family.

So, I sent them back a letter telling them they would find their EFT authorization enclosed and fully completed and that I want to stay in Domino's Pizza. It's a great system and I love it, period. Because Domino's is. That said, "I believe that the mandatory use of a blanket EFT debit authority can, in many cases, constitute a taking of property without due process. I firmly believe that such takings of property without due process are unethical and un-American. I'd love to be able to say they're illegal. I think they should be. Currently, only the IRS is able to perform such takings of property without due process, and nearly every other person in the United States is working with Congress, as we speak, to strip the IRS of an onerous power precisely because it's unethical and un-American." But I have no choice, but with my protests, to sign a contract that I believe is morally repugnant in that regard. And this is not a lousy franchise. There are franchises -- and certainly Subway comes to mind -- that are almost a shell game, that are corrupt beyond belief.

Domino's is a great franchise. And yet their contract is not something that should be allowed by law. We have -- we covered the diminished exclusive areas, the extremely diminished areas of primary responsibility, which few, if any, stores would be profitable. Under the contract, it says, I can approve -- I can purchase approved products from any supplier, although they do give themselves some new rights in the renewal contract to require that I purchase certain things exclusively from them. But under my previous contract, while they say I can purchase products from any supplier, the truth is that they hold the approval process so tightly to their chest that it is not possible.

To give you an example. I have a local sign fabricator who's fabricated my signs for many, many years. Domino's has aggressively tried to sell me their signs. But it was a reasonable thing. We put up great signs, he did a great job, they'd come and approve them. They come out with a new sign concept. I said, Could I have the specifications, because they say in my contract they will supply me with those specifications. And they said, Well, we can't give you those specifications because we haven't finalized those specifications, so you'll have to buy the signs from us. I said, Well, you can't manufacture the sign without specifications. There must be specifications. He said, I'm sorry, we don't have specifications. I said, Let's say I could get the specifications from one of your current manufacturers, how does the approval process go? And he said, Well, you know, you could do that if we had specifications, but the flip side is that we have not yet established an approval process. We're working on establishing a committee to establish an approval process. And then, when we have the specifications, we will be able to allow you to have your sign maker, if he is approved, build that sign for you.

Now, I don't know about you, but you see a lot of signs if you live in the suburbs, and the signs are not rocket science. They're not brain surgery. They are very basic structures. And this sign, like most signs, is a very, very basic thing that hundreds of manufacturers could manufacture to the highest standard.

I bought the sign from them. They subsequently published the specifications for their signs which only they sell. And they didn't even have the decency to build the sign that they sold me to their own specifications, which they later published. But they were perfectly able to sell me a sign. Their sign did not have to meet their specifications, and it simply had to come through their profit-making division.

And this is a good company in the franchise world, if not a great company. But the abuses of the power in the relationship are something that need to be curbed, because we don't live in the world of 20 years ago where we have a local marketplace where I can build my own little successful pizza chain. Those are fast going by the board. They are an extreme rarity today and in a main-line pizza business -- not a specialty pizza business but a main-line pizza business -- those operators are going out of business in much higher rates than they will ever be replaced. The franchise world needs to be a fair world because it is our marketplace of the future.

We could go into a number of other things, certainly the new contract. We have advertising cooperatives that we have -- that we contribute to based on our voting and mutual commitments to one another. Domino's has given themselves broad rights to vote our voluntary contributions and raise them to significantly higher levels. The idea that the company can vote my vote because I sign their contract and call it a voluntary cooperative, it's an interesting structure.

And again, I say, Domino's is a great

franchise. The abuses that -- I talk to other franchisees -- which I'm obviously not going to testify to today -- but the abuses in other franchise systems are far more outrageous, and there is not the underlying value that there is in a Domino's franchise.

I want to be a Domino's pizza franchisee for another 20 years. And I want to help this be a great company, I want to improve my franchisor. At the same time, there are abuses of the power relationship after the fact, and particularly upon renewal, that are unfair and that should not be legal.

Does anybody have any questions?

MR. TOPOROFF: I don't.

MS. KEZIOS: Would the changing the word "renewal" help, seeing that you absolutely did not get a renewal of your old document? Calling it "rewrite"? I mean, what should they say in the UFOC is going to happen at the end of your term so that you would be prepared to know that it's going to be a fundamentally different contract.

MR. HOCKERT-LOTZ: The truth is that they should say, "After 10 years, we will -- your business will cease, and you may, at your option, rewrite a new contract with us." But that business that I purchased in 1984 has ceased. So, renewal isn't -- it is not a renewal in a contract sense. It is not an extension in a contract sense. You will be terminated after 10 years, but we will give you the right to review our new contract and sign it, if you choose. Because that's the reality.

MS. HOWARD: What was your understanding when you originally signed your contract about renewal?

MR. HOCKERT-LOTZ: My understanding of renewal, first of all, as a very young businessman who came from the Domino's Pizza system -- I mean, we're all former Domino's managers. Our great education is making pizzas. My limited experience, on asking the franchisee that I worked for, was that renewals simply weren't an issue. He had, and I assumed I had -- I would have, essentially the same contract from an operating perspective and legal perspective.

Now, he started his business with a -- with a franchise contract that was written literally on the back of a restaurant placemat when he opened his first store. He was the first franchise, the first Domino's franchise out of Michigan. He's a great man and a great pizza man. But, you know, the franchise contract has changed a great deal since then. It was my understanding, and I think that Domino's really encourages -- and let me further say that I think

Domino's encourages people to think this is your business and will remain your business for life. Domino's spends a great deal of time pushing the wealth building of the business opportunity. This is a way for a manager to become very wealthy, and it's a lot of hard work.

However, once you are a franchisee, you find that it's very, very difficult, should you ever want to get out, to take value with you. In my old contract, there was no mention of any customer list, and customer lists essentially didn't exist in a very organized way. Now, in the new contract, Domino's Pizza has appropriated, for themselves, a customer list that I've spent more than $50,000 developing and with no compensation. Again, from my view, that's a taking of property without compensation.

Do I have a choice of not signing this contract? No, I'm essentially -- my business is terminated and I cannot get in the same business in the same community where I own my home, where my friends and family are established. I have to try something entirely different.

Now, I don't know what your background is, but if you can imagine stepping out on the street one day and being told you can never practice anything in the scope of law, that you have to start washing cars or flipping burgers and work your way up an entirely different -- you know, learn an entirely different business from scratch. And, you know, the success of Domino's Pizza is based on the fact that their franchisees are people who have successfully proven they can run Domino's Pizza stores. And that's a good thing.

On the other hand, it's also been a very good thing that they're a very sophisticated company dealing with a lot of pizza makers. It's an utterly unlevel playing field where they plan the business based on the fact that people are not going to make entirely informed decisions about the contract. Because if they did, nobody would build a Domino's Pizza store for the -- I'm not going say nobody -- the people who build a Domino's Pizza store in the area where you could actually build a profitable Domino's Pizza store, within Domino's defined exclusive areas as opposed to what they promise you verbally or give you as a delivery area, is subject to change at their exclusive option. Nobody would franchise the business and nobody would finance it. So, that's one example of where the business is built on something that is specifically outside the contract.

Again, Domino's Pizza is a great franchise company, and franchising is what has made them great. They have a group of great franchisees, but I don't think that gives them the right, no matter how great they are as a company, to come in and take what is mine and demand that I, without compensation -- and demand that I sign a contract that gives them exclusive -- that gives them unlimited access to my checking account without my notification, or without my approval. I don't think that should be legal.

So, I -- there are issues that can't be fixed by disclosure before the sale. They just can't be fixed. There has to be an ongoing oversight of the franchise industry, or I think what most of us who are franchisees would really like, a body of franchise law under which certain practices that are clearly unfair and unethical are banned, and we simply have the right to sue and enforce ourselves. We would rather not drag the FTC or the federal government into enforcing every little franchise infringement. What we would like is to be able to defend our rights in the courts of law and court of law within our own state or within some reasonable geographical area.

MS. KEZIOS: You said you were given verbal assurances that were banned in the contract.

MR. HOCKERT-LOTZ: Yes.

MS. KEZIOS: Does that mean there's an integration clause that you signed in the contract that said you're not relying on any promises made outside the contract?

MR. HOCKERT-LOTZ: There is something to that effect. I could not recite that. Yes, but, in fact, you must.

MS. KEZIOS: Okay. And I'm assuming because you say you were forced, you had no choice, you had to sign the renewal contract, you had to sign the EFT or you don't get renewed is because you got a post-termination covenant not to compete? You're going to be out of business. Your life has changed.

MR. HOCKERT-LOTZ: Yes.

MS. KEZIOS: And you find the fact that you really -- this is not your own business, you find out that you really don't own your own business, and there is something misleading. There was something misleading going on in the pre-sale and even all through the process -- build some wealth in yourself, buy some more equipment, buy another store --

MR. HOCKERT-LOTZ: I don't know that there is intentional misleading or that there was at some point back in 1984. I think that -- I think a lot of misleading statements are made in enthusiasm for the business in hopes that everything continues to go the way it goes now.

MS. KEZIOS: Enthusiastic statements on their side?

MR. HOCKERT-LOTZ: Sure, but that's not what the contract says.

MS. KEZIOS: That's what I'm saying. That's not what the contract reads. So, you are still relying, as sophisticated a franchisee as you are, 20 years experience --

MR. HOCKERT-LOTZ: You must --

MS. KEZIOS: You are still relying on promises that go beyond the corners of the contract.

MR. HOCKERT-LOTZ: Absolutely. There is no choice. And I presume these contracts are written by franchise contract lawyers and that there is substantial, additional reserving of rights in each renewal contract by the franchisor that encroaches significantly upon the business -- the portions of my Domino's Pizza business that I at one time believed were exclusively mine, and would like, and believed should be. But that's not what my current contract says.

For instance, a reasonable exclusive area is a necessity to do business under a franchise. And the exclusive area -- you know, if they give me an exclusive area that's financially unfeasible, they're giving everybody an exclusive area that, in most cases, would be utterly financially unfeasible to run a profitable business. And then give a larger area with a neat little map that you can deliver to which they say they reserve the right to develop. This -- you can't make sound business decisions based on, you know, this set of, okay, we're giving you a limited right to this and a absolute right to something that's not economically feasible.

MS. KEZIOS: But don't you think that the Federal Trade Commission could prohibit franchisors from making those kinds of promises, for telling you, a new franchisee or mature franchisee, that this is your own business? You don't think the Federal Trade Commission can prohibit franchisors from marketing business that way?

MR. HOCKERT-LOTZ: That's a very interesting question. I hadn't thought of it that way, and yet -- and yet I could see a very strong argument for -- for not being -- for prohibiting a franchise situation, or certain franchise situations, from being marketed as Domino's Pizza is with an own-your-own-business concept. Because that's not --

MS. KEZIOS: Exactly.

MR. HOCKERT-LOTZ: -- that is not, strictly speaking, entirely true.

MS. KEZIOS: Absolutely. Not from your testimony. So, that is absolutely something FTC could prohibit franchisors from doing, in their marketing, in their advertising, in their verbal assurances to franchisees. Especially if, in a renewal, the FTC would insist that the franchisor say, Your business, as you know it, will cease to exist at the end of your contract and you have --

MR. HOCKERT-LOTZ: Should be required.

MS. KEZIOS: Because that would be truthful disclosure, right?

MR. HOCKERT-LOTZ: Yes.

MS. KEZIOS: It's not a renewal. It's not a mere extension of the current contract.

MR. HOCKERT-LOTZ: This is an utterly new and completely different contract without which I can't do business.

MS. KEZIOS: And the other thing that the FTC could require is that the franchisors clearly state that this will probably, and most certainly, be a fundamentally different contract that they have the right to write and that you --

MR. HOCKERT-LOTZ: That should be clear.

MS. KEZIOS: -- and that you are not offering any input in how the contract is rewritten.

MR. HOCKERT-LOTZ: I was specifically given a letter saying I could make -- that any contract with any amendments, additions, deletions, et cetera, any changes of any sort whatsoever, would be rejected.

MS. KEZIOS: So, it was basically press hard, there's three copies, is what they were saying to you?

MR. HOCKERT-LOTZ: There is no negotiation. There is no --

MS. KEZIOS: And so the FTC could absolutely require that the franchisors give what they claim they are giving, which is truthful disclosure as to what is going to happen at the end of the term because you have a gun held to your head. You can't do anything else because you signed.

MR. HOCKERT-LOTZ: Renewal is probably a misleading term for what I have just done in signing a very significantly different contract from the contract I originally signed. That's true.

MS. KEZIOS: I have no other questions.

MR. HOCKERT-LOTZ: But I want to -- I want to reinforce, I know other people in franchise businesses. Domino's is a great franchise. And for Domino's and McDonald's to have the problems with exclusive area and renewal that both Domino's and McDonald's, which are two of the best franchises in America that bring real value to the next generation of business people and have also squeezed out the opportunity for independence to compete. Because a big part of my job as a Domino's Pizza franchisee is to ensure that nobody establishes a successful pizza delivery business in my area. And we are very good at killing small businesses. It's part of our job. Domino's is good at it. We are good at it.

Therefore, I know better than anyone how critical this contract is to my financial success. Because it's -- it's an absolute jungle in the fast food business, and there are kings of the jungle. Nobody has successfully made the kind of money that I make in my market. Nobody has successfully competed with me to a point where they don't have to run their own little pizza store every day as a small business. And that's what the world is on the other side.

Even if I didn't have -- and I would love to have the opportunity to compete -- but you reach a point at renewal where your business ends and where the marketplace has changed so significantly because of the impact of franchises that you really don't have a choice, and your kids don't have a choice of opening non-franchised businesses in businesses dominated by franchises. You must choose a franchise, and the contracts are universally onerous.

MR. TOPOROFF: Thank you very much.

MR. HOCKERT-LOTZ: Did you have any questions?

MR. TOPOROFF: No additional questions, but I did want to thank you. We appreciate it. Very helpful comments.

I do have a few questions though for Susan. It seemed to me when you touched on the issues like, what does the term "renewal" mean and some of those other points, that there are two components to it. One is that there's a disclosure issue, and the other is that there's a consumer-education issue. And I know at the Federal Trade Commission, we have a consumer's guide to buying a franchise. I know the IFA, they have various publications on how to find a franchise or how to invest in a franchise. And I was wondering if your association, the AFA, whether you have any consumer education materials from your members' perspective that you give out to the prospective buyers.

MS. KEZIOS: Yes, we do. We've got like the top dozen lists of the worst franchise agreement provisions we recommend someone does not sign, either new or renewal. Yes, we do have pieces like that.

MR. TOPOROFF: Just for my own information, do prospective franchisees call and ask for information on occasions?

MS. KEZIOS: When prospective franchisees call and ask for information, we send that to them.

MR. TOPOROFF: Could it be possible to get a copy of your standard package?

MS. KEZIOS: Yes.

MR. TOPOROFF: That would be helpful. That's it.

MR. TOPOROFF: Good morning. Okay, we're continuing.

MR. JAMES: Good morning, my name is Bob James. I work for the state of Florida, division of consumer services to sell business opportunities in the state of Florida.

I'm here to discuss the proposed new document that we reviewed yesterday. And thinking about a couple of points last night, particularly about the provision about the buy back of products made and fabricated, I wanted to share with you a couple of cases that we've had in Florida. I won't mention the sellers' names. I don't think that's important at this point, but these were both Ponzi schemes.

The first one appeared to me in November of last year, and from November through late February, they had sold approximately $18 million. We discovered about $15 million offshore in a German bank. The other money was seized by another agency in the state and that money's in Dade County. There's about 6,000 consumers that bought that program. I'll explain to you what the program -- what are the -- pardon of my voice, I've got a terrible cold today.

But this was a scheme of stringing necklaces. Consumers would pay $1,000 to the seller and he would get a bag of beads and some string. And this was such a crude device -- it wasn't even a clasp -- he just knotted the string. And how it worked is, you would get enough beads to make enough beads for three different delivery periods. For your $1,000, you ultimately would return back $400 dollars profit. They'd pay you $1,400 back. You string a certain amount of beads for the first 29 days, you bring that back, you'd be paid a certain amount of money. This would happen three times and you would ultimately collect $1,400. Consumers who had got in early on it were making money. We felt these were typically Hispanics recruiting very low income people, working in garages, working in homes, even became more of multi-level marketing program at a later point that they recruited a friend in the neighborhood.

They were shut down in February. There's been two spin-offs in Florida, same exact deal. Stringing beads again. One was an offer of more money, greater threshold of $1,000 and the other was less. But we were made aware of these very early on and both of them have now ceased operations. They're no longer selling them.

MR. TOPOROFF: Can I just ask a few questions about that just so I'm clear? In these bead-manufacturing types of schemes, is it the case that the consumer buys the supplies from, we'll call it the promoter, and then after assembling the beads, sells it back to the promoter.

MR. JAMES: That's correct.

MR. TOPOROFF: Okay. I want to make sure.

MR. JAMES: There was -- the ultimate of this business was, it was a Columbian drug cartel. And I had the owner and the attorney meet me in Tallahassee to discuss it -- I had tried for several months through letters back and forth with the attorney. It was our position that it was very easy to reach suit. It's not rocket science. And when he came to our office in Tallahassee, the purported owner turned to the lawyer and said why aren't we buying and selling? And the attorney just collapsed and said he lost his argument. And the attorney attempted to file and took them several weeks to get a bond, and they finally did get a bond for

$50,000. Cost $18 million dollars but informed us it was not much money there to recapture to the consumers.

There was money made by the people who got in early. Some folks made serious money for this type of business, $18,000 they claim in a month. But they have now disappeared and the owner was not the real owner. He was shielded and fronted by the organization.

We have now another Ponzi that just come into Florida, rejuvenation of the worm farm. This was a seller from out of state who had a permanent cease and desist order against them from another state, and he had left the country and came back and was operating in his home state in Florida. This is, you buy $1,000 worth of worms, you build a two by four pen for them out in your backyard, you feed them, and he's supposed to buy the worms back. And then he's going to resell these worms to municipalities for their sewage waste.

He could never provide an end-buyer. We never proved the filing. We did manage to fight against them, as we did the bead manufacturer, and the bead manufacturer did not have an end-buyer either. They had told me the bead manufacturer, his buyer was going to be the J. C. Penny Company. And I contacted the J. C. Penny Company and they had never heard of him. I just wanted to get these two.

And by the way, there were two more worm farms that have now surfaced in Florida which are both selling for $300 which, as you know, my price was $500. So, they're not required to file on that statute.

MR. TOPOROFF: In addition to the two types of opportunities that you mentioned, the beads and the worm farms, are there other types of opportunity that you see? What kinds of products or what industries are they involved in?

MR. JAMES: The biggest area of complaints we have in our section is the home-based businesses. They are the envelope stuffing, the $27 envelope stuffing, where you can stuff envelopes and make $1,000 a week. We don't regulate it because, again, the limit threshold is far below our $500 fee. Most of these purchasers are probably elderly or very poorly-educated people. Reading their complaints when they come in, very poorly written. They tend to see these types of ads in the classified or tabloid papers. It's not much money.

I'm tracking -- one company now has 18 mail drops in south Florida. I go to the postal authorities, who I consider to be the regulatory agency in this but we get very little help from the postal service on this issue. It's not enough money for most of them to track. When you add up the complaints we have -- on one drop it's 80 complaints in one location times $27. It's just not enough dollars there to interest a regulator -- the post office.

Most people don't have real store fronts. They operate out of a post office box. They don't have a telephone. You can't track them. They don't respond to the complaints we send to the business. That's the big issue.

Many of these home-based businesses are manufacturing pill boxes for resell or doll babies. And I have one doll in my office that they -- I have never met the lady. I just have a picture of maybe an elderly lady that perhaps has good sewing skills and so she bought the program. It was $40-some dollars. For the $40, she got a -- what's the pattern called? It's called a pattern -- called when you sew something. She got a pattern and some material and I took the material over to one of the stores in town, and they said I could have bought the material for about $3.

But she then made a clown. And the idea was to sew this pattern together in the clown and send it back to the company and they would buy it back from her. So, she did that. She sent it back to the company and they returned it because the stitching was too tight around the edges and caused the material to pucker. They rejected that and they offered her another opportunity by selling her some pattern -- material again, using the same pattern she had -- you can apparently reuse the patterns over -- for about half, $20 for the material. Well, her pride was a little bit stung, so she tried again knowing she was a good seamstress. So, she sent the second doll back and it got rejected because the eyes were too close together.

Now, she has $60 invested in materials, plus her time, plus the mailing fee and two dolls at the house she can't really sell. She was led to believe she could do about one doll a week and make about $100 a week doing this.

MR. TOPOROFF: Another issue I want to bring up involves welfare reform. We have a concern at the commission that, as a result of welfare regulation -- or the deregulation -- the changes and modifications in welfare in the United States, that a number of people on public assistance who may be losing welfare benefits might turn towards business opportunities or other types of schemes for the basic income. Have you come across that at all in Florida?

MR. JAMES: No, I haven't. This, I know, was mentioned at a conference I attended in Utah this year. This is one of the issues they talked about and I have been watching for this and I have told other regulators in our section, but we have not experienced that yet.

MR. TOPOROFF: So that has not been an issue for you. Is there anything else you would like to get on the record?

MR. JAMES: Just a general in going back to the main thrust of the meeting yesterday, the business opportunity sellers, is the fact that most of these companies are operated by one man or one person. We don't know who they are. We have to no way to identify who the real seller is. They will tend to operate a business for about a year and typically a business opportunity might be a vending machine business. Operate for about a year. And for whatever reason, they will collapse the business, usually because they have misrepresented the earnings that the potential person was going to get, or collapse the business and they'll resurface a short time later under a different business name with a similar operation. And I think that these are designed by the sellers. This is not by accident. They're long, hard thought-out propositions they come up with to build a scheme of misrepresentations to defraud the public.

MR. TOPOROFF: Okay. Myra, did you have any questions?

MS. HOWARD: No.

MR. TOPOROFF: Thank you. Mr. James was the last speaker and there doesn't seem to be anyone else at this time, so we're going to close the meeting, I think.

I just want to thank everyone who attended today and the other public workshop conferences that we've held. I just want to note again, for the record, that the comment period is still open until December 31st. And after that time, we'll take the comments and digest them and proceed in the next step, which is to come out with a revised franchise rule and revised business opportunity rule. So, again, thank you.

(Whereupon, the hearing was concluded.)

C E R T I F I C A T I O N   O F   R E P O R T E R

DOCKET/FILE NUMBER: R-511003

CASE TITLE: FRANCHISE RULE

HEARING DATE: FRIDAY, NOVEMBER 21, 1997

I HEREBY CERTIFY that the transcript contained herein is a full and accurate transcript of the notes taken by me at the hearing on the above cause before the FEDERAL TRADE COMMISSION to the best of my knowledge and belief.

DATED: December 3, 1997

REGINA K. BATES

C E R T I F I C A T I O N   O F   P R O O F R E A D E R

I HEREBY CERTIFY that I proofread the transcript for accuracy in spelling, hyphenation, punctuation and format.

SARA J. VANCE, PROOFREADER