



#### This 3DAdvisors Report Covers:

- ✓ **Insider Trading:** Insider Trading Behavior
- ✓ **Accounting:** Quality of Earnings Issues
- Governance:** Corporate Governance Issues

## Court of Appeal Reinstates All “Causes of Action” Avon Products, Inc. (NYSE:AVP) Update

June 28, 2004

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Avon Products, Inc. is a global manufacturer and marketer of beauty and related products. The Company's business is comprised of direct selling, which is conducted in North America, Latin America, Europe and the Pacific. Avon's products fall into four product categories: Beauty, which consists of cosmetics, fragrances and toiletries (CFTs); Beauty Plus, which consists of jewelry, watches and apparel and accessories; Beyond Beauty, which consists of home products, gifts, decorative items and candles, and Health and Wellness, which consists of vitamins, an aromatherapy line, exercise equipment and stress relief and weight management products. The Company has operations in 58 countries, including the United States, and its products are distributed in 85 more countries, for a total coverage of 143 markets.

### Summary of 3DAdvisors Findings for AVP

- ▶ **Accounting:** Court of Appeal Reinstates All “Causes of Action”
- ▶ **Insider Trading:** Insiders have been quiet, but two recent sales are noteworthy

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### Discussion of 3DAdvisors Findings

#### Accounting: Court of Appeal Reinstates All “Causes of Action”

After the market close on Friday, June 25<sup>th</sup>, we received notice from the attorney for the plaintiffs (Huron Maki & Johnson) in the Avon (channel stuffing) class action case, that the Court of Appeal had issued an order reversing the original orders of the trial judge who had dismissed three of the four causes of action filed by the plaintiffs. In two separate rulings, the trial judge had dismissed claims of Fraud, Breach of Contract and Unfair Competition.

In our last Avon report dated 05/25/04, we had indicated that Huron Maki and Johnson had filed a Petition for Writ of Mandate with the Court of Appeal, which, under California law, is a legal device to request the appeals court to review the decision of the trial judge to dismiss these causes of action. Filing the writ is an expeditious alternative

to the appeal process, which would otherwise not begin until all active portions of the suit are heard.

Jeffery Huron, from Huron Maki and Johnson, had indicated to us his optimism that the court was seriously considering the Writ filed by his firm. He was correct. Two weeks ago, Mr. Huron told us that the Court of Appeal, on its own volition, had obtained a copy of the trial court judge's June 1<sup>st</sup> order dismissing the Plaintiff's three claims and invited the firm, in effect, to submit another writ to the court. Mr. Huron was very encouraged by these developments, which had occurred by mid-month. Once again, he was correct as the court subsequently ordered the trial judge to reverse both of his orders (the trial judge, Judge Wendell Mortimer had dismissed the three causes through two separate orders), in effect reinstating all three dismissed claims. Mr. Huron informs us that, prior to this, Judge Mortimer had been reversed 18 separate times on appeal in other cases, which is considered a high number. The following are excerpts from the order issued by the Court of Appeal, forwarded to us by Huron Maki and Johnson:

"Alternative Writ of Mandate and Order/The Motion to consolidate Case No. B174825 with Case No. B175973 for all purposes is granted. Good cause appearing, you are commanded, immediately upon receipt of this writ, either to: (a) vacate your rulings of March 16, 2004 and June 1, 2004, in Los Angeles County Superior Court Case Number BC292702...The new order should be issued by July 2, 2004, with a copy submitted to us via facsimile by July 2, 2004: or (b) in the alternative Show Cause before this court, at 9:00 a.m., on October 26, 2004...Real party's return to the petitions shall be served and filed on or before July 21, 2004. Petitioners may serve and file a reply on or before August 11, 2004."

Clearly, Huron and his team are invigorated by these developments. We also note that, upon the original dismissal of these claims, Avon had twice issued 8K's, promptly disclosing the original court decisions, decisions that inured to Avon's benefit. As of the release of this update (06/28/04, 8:30 AM EDT), there has been no disclosure, from Avon, revealing its recent setback. As we strongly suspect that one will be slow in coming, if it comes at all, we wanted to be sure our clients are made aware of the situation and advised that this case not only is far from over but also appears to have regained its earlier momentum.

See our prior reports and updates on AVP for additional information on the "channel stuffing" class action lawsuit, as well as for information on the indicative insider trading, accounting, and governance behavior we have observed.

#### Insider Trading: Insiders have been quiet, but two recent sales are noteworthy

Other than the sale by director **Paula Stern** described in our last update, insiders at Avon have been relatively quiet, at least for a company where we have grown accustomed to seeing aggressive selling behavior over a sustained period. There were, however, two recent sales, which we believe are noteworthy for several reasons, not the least of which are the management roles played by these insiders.

- **Robert Toth (51)**, President of Avon International. Toth has recently sold his largest-ever block of shares. On June 14<sup>th</sup>, he exercised two series of non-expiring options (clearing out both series) to acquire 83,708 shares. One option had a strike price of \$19.65 and wasn't set to expire until 2/09 while the other cost \$17.62 and carried an expiration date of 12/09. He then immediately sold all the acquired shares at \$44.04. The sale, which was only his second open-market transaction since his initial Section 16 filing in 2002, **reduced his actionable position by 35%** (common stock plus exercisable options).
- **Janice Marolda (43)**, Chief Accounting Officer and Controller. Marolda's sales are more significant than they appear on the surface. She recently exercised options for 4,738 shares (expiring in 2011), which she sold on June 22<sup>nd</sup> for \$45.61 each. The last of these options had vested in February and she no longer holds any from that series. For the past year, she has displayed an interesting proclivity towards exercising options as they vest (far before expiration) and selling all the underlying shares. She currently holds exercisable options and shares totaling just 6,259 shares.

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