

REGULATORY CAPTURE – The FTC’s Flawed Business Opportunity Rule

**Compiled by Jon M. Taylor, MBA, Ph.D.
Consumer Awareness Institute**

This revealing report demonstrates the need for public officials who can stand up against powerful special interests. You will discover how the DSA (Direct Selling Association) lobby helped the MLM (multi-level marketing) industry gain an exemption from the FTC’s (Federal Trade Commission’s) Business Opportunity Rule, leaving consumers unprotected from the most unfair and deceptive of business practices, proving the need for a firewall between regulators and those they regulate – and for public officials with the skill, the will, and the resources to stand up to powerful special interests.

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- Douglas M. Brooks, Martland & Brooks, LLP, attorney, franchise, distribution and consumer protection litigation, including cases involving MLM firms
- Robert Fitzpatrick, Robert L. Fitzpatrick, President, Pyramid Scheme Alert, author – *False Profits* and operator of the web site www.pyramidschemealert.org,
- Bruce Craig, former Assistant Attorney General, State of Wisconsin – litigated landmark cases against Koscot Interplanetary, Amway, and other MLM companies
- Stephen Barrett, M.D., publisher of Consumer Health Digest, operator of anti-quackery websites and the web site www.mlmwatch.org,
- Eric Scheibeler, former federal auditor, author – *Merchants of Deception*

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PREFACE

The letters and comments that follow are selected from documents totaling thousands of pages in the FTC rulemaking process, related to the FTC's Business Opportunity Rule, which was first proposed in 2006 and finalized after an extensive and controversial rulemaking process in December of 2011. The formatting and type has been condensed to save pages, and in some cases only excerpts are provided. However, links or references to more complete documentation are provided.

Headings and introductions to

communications are in **bold face type**. [Comments inserted by Jon M. Taylor are bracketed. Emphases by JMT are in *italics*.]

NOTE: MLM's inherent flaws have been known for decades. These flaws in MLMs (that I have labeled "recruitment-driven MLMs" or "product-based pyramid schemes") will become apparent to anyone who reads Chapter 2 of my book *Multi-level Marketing Unmasked* (formerly *The Case against Multi-level Marketing – an Unfair and Deceptive Practice*).

BACKGROUND AND SUMMARY

In covering to the DSA/MLM lobby, the FTC subordinated the interests of consumers to the interests of the MLM industry in exempting MLM – the most unfair and deceptive, the most viral and predatory, and the most prevalent of purported "business opportunities" – from its Business Opportunity Rule.

In 2006, the FTC proposed a Business Opportunity Rule (BOR) that was intended to provide some protection for consumers against unfair and deceptive acts or practices (UDAP) in the field of business opportunities, such as envelope stuffing, vending machines, and MLMs (multi-level marketing programs). However, the DSA (Direct Selling Association) responded with an aggressive \$4 million lobbying campaign that overwhelmed FTC staff working on the Rule.

What resulted was a demonstration of the corrupting influence of special interests that affect public policy against the public interest. The documents included or cited here testify to the need for citizens to demand not more – nor less – regulatory scrutiny in protecting citizens, but *better* regulatory efforts – even if we have to pay more for qualified and courageous public servants who will work for the public good.

In 1995, Boston MLM plaintiff attorney Douglas M. Brooks submitted a comment letter to Donald S. Clark, Secretary to the FTC regarding the Franchise and Business Opportunity Rule, when considering revisions to the original Rule passed in 1979. A careful reading of this letter will help the reader understand the historical background and

need for a rule to protect consumers who might become prospects for MLMs, as well as other far less prevalent packaged business opportunities (envelope stuffing, vending machines, etc.) which fell below the threshold for franchise investments. Mr. Brooks' comments about the situation faced by the Commission was correct, and the response by the DSA/MLM lobby was accurately predicted. His letter (which follows this introduction) will precede our review of proposals, decisions, and communications that comprised the BOR rulemaking process.

In 2000, Bruce Craig, former Assistant AG in Wisconsin and litigator in landmark cases against MLMs, wrote to FTC Chairman Robert Pitofsky and FTC economist Peter Vander Nat, providing useful background for BOR rulemaking.¹ The fundamental flaw and legal implications of MLM's endless chains of recruitment were persuasively explained, as were the legal underpinnings for considering such schemes as per se illegal.

Unfortunately, in 1979, the FTC, after a vigorous defense by Amway attorneys, ruled that Amway was "not a pyramid

¹ See Appendix 2E in Chapter 2 of my book *Multi-level Marketing Unmasked* for Amway's "retail rules."

scheme,” assuming certain “retail rules”² were adhered to. These rules have never been enforced, and MLMs have proliferated – until several hundred MLMs are now defrauding tens of millions of victims of tens of billions of dollars every year. Since the 1979 Amway decision, hundreds of millions of MLM recruits have suffered hundreds of billions of dollars in losses – making it by far the greatest consumer scam in history.

A review of Chapter 11 of my book *Multi-level Marketing Unmasked* will help the reader understand the power and effectiveness of the DSA/MLM lobby in preventing or nullifying state statutes that could adversely affect MLM firms. In fact, in the month preceding the announcement of the initial Rule, the DSA had successfully influenced the Utah Legislature to gut the Utah statute against product-based pyramid schemes by defining “direct selling” (including MLM) as not a pyramid scheme if products were offered for consumption by anyone – which could include participants.

In legislative hearings I and an MLM victim had vigorously objected to the hidden purpose and deceptive language of the bill, but the state Attorney General testified that it was “a good bill designed to protect against the worst pyramid schemes – those that don’t sell legitimate products.” I knew from my research that the most damaging of pyramid schemes were product-based. But the legislature accepted his testimony, and the bill passed. On checking the AG’s record of campaign contributions, he had received about \$250,000 in campaign contributions from MLM companies (\$500,000 to this date). Utah has become a safe haven for MLM companies. Other states have been similarly affected by DSA-initiated legislation.

I have analyzed the compensation plans of about 500 MLMs and found that all of them disregard normal market competition. Dependent on unlimited recruitment of a network of endless chains of participants, they assume infinite markets, which don’t exist in the real world. They also assume virgin markets, which don’t exist for long. They are therefore inherently flawed, unfair, and deceptive. Where data is available, this conclusion is validated with loss rates

averaging 99.7%. And if those at the top of the pyramids, who are harvesting most of the commissions are left out of the calculations of average incomes, ***about 99.99% lose money. The chances for new recruits to earn significant profits is virtually ZERO.***

In fact, in a 1974 ruling, the FTC found in the very structure of “multi-leveling” or “pyramid selling” . . . ***an intolerable potential to deceive.***” This statement has proven to be prophetic. Worldwide feedback and 18 years’ research convinces me (and anyone willing to look objectively at the evidence) that MLMs are not only the most unfair and deceptive, but also the most viral and predatory – and the most prevalent – of all classes of business opportunities. ***Tens of millions of MLM participants lose tens of billions of dollars annually, making it likely the greatest consumer scam in history.***

After extensive comparative analyses of alternative business models, the endless chain of recruitment aspect of MLM became the basis for the first of my four CDCs (causal and defining characteristics or “red flags”) of a recruitment-driven MLM, or product-based pyramid scheme, as explained in Chapter 2 of the book *Multi-level Marketing Unmasked*. They are causal in that they cause the high loss rates and defining in clearly distinguishing MLM from all other types of business practices.

These four CDCs have since been tested against the compensation plans of approximately 500 MLMs I have analyzed and have been found in all of them, providing a generalizable model of MLM as an unfair and deceptive practice – the very thing the FTC was founded to protect against.

Unfortunately, the arguments presented by Mr. Craig and other consumer advocates were ignored, as the FTC continued to allow fraudulent MLM companies to proliferate with only occasional cases brought against less than 1% of MLMs that were using the same endless chain recruitment model. Meanwhile, a powerful lobby formed when MLM industry leaders joined the Direct Selling Association (DSA), which acted as a cartel to choreograph the dialogue of deception on which MLMs depend. MLM promoters enlisted the help of the DSA in rebranding MLM as “direct selling” – and were successful in getting regulators, the

² Op.Cit., Chapters 10 and 11

media, and much of the general public to accept MLM as legitimate direct selling. Academia remains conspicuously silent.

The Initial Business Opportunity Rule, as proposed in 2006 was a good rule that would require reasonable disclosures and other provisions that would have provided some protection against questionable MLMs as well as other business opportunities. A major assumption underlying the Rule was that there were “good” and “bad” MLMs, and that the Rule would help consumers make informed decision on whether or not to participate. At the same time, we should hold no illusions that even with a good disclosure rule, MLM fraud would stop. MLM promoters are skilled at distorting statistics and other disclosures to appear acceptable.

The DSA realized that if true information about MLMs were disclosed, and if prospects were allowed time to do some research, recruitment could be adversely affected. Persons who understood basic statistics may balk if they knew that less than one out of a thousand recruits earned the income held out to them at opportunity meetings. And if they were provided references and allowed time to call them and to do research on the Internet, only the most unsophisticated would join.

So the DSA/MLM (“pyramid lobby”) undertook a massive \$4 million lobbying effort, including an appeal for comments to millions of MLM participants, who were provided with form letters to use and warnings about the effects it would have on their “business.” FTC officials were impressed by over 15,000 comments that came in, most of them objecting to applying the Rule to MLMs.

It is now clear now that 15,000 was an extremely low rate of response, perhaps as low as one out of a thousand to whom the appeal went out. Later telephone interviews we conducted with a sample of those who submitted comments revealed that most of them were responding to deceptive warnings about how the Rule would ruin their efforts to recruit new people. When we explained to them the true intent of the Rule, most favored the disclosure requirements. However, nearly all of them objected to the 7-day waiting period, fearing it would hamper their recruitment efforts. We also discovered that at least some of the comments were

not actually submitted by the commenter, but were submitted online without their knowledge by someone in their upline or in the company itself – a form of electronic forgery.

In addition, we learned that most of the commenters surveyed were not relying on MLM as their sole source of income. And even though they used their expenses as a tax write-off and claimed to be successful at selling and recruiting, few could honestly say that they were receiving more money from the company than they were paying to the company in products and services.

The DSA/MLM lobby used its implied voting block of more than 15 million “direct sellers,” as well as political contributions, to pressure 86 Congressmen to write the FTC, asking them to exclude MLM from having to comply with the Rule. Former high level FTC officials, hired by the very companies they had been paid to protect against, also wrote FTC officials to urge an MLM exclusion.

All of this intense lobbying, with deceptive but carefully crafted arguments, overwhelmed FTC officials, who caved to their demands and wound up excluding MLMs from the ambit of the Rule. They dismissed qualified independent research that proved conclusively (from the MLMs own reports) the critical need for a Rule to protect against the entire MLM industry as an inherently flawed, unfair, and deceptive practice.

As an unintended consequence of the Rule, all “business opportunities” will have an incentive to convert to an MLM format. In effect, the FTC will have actually facilitated the spread of unfair and deceptive practices – the very thing the FTC was established to protect against. The Rule as passed must be vacated if consumers are to have any protection from such unfair and deceptive practices as is characteristic of MLM.

In the collection of letters and reports that follow you will find a blow-by-blow account of the rulemaking – or “regulatory capture” – that led to the deeply flawed MLM exemption to the final Business Opportunity Rule. All of this information (over 600 pages) was mailed with a personal letter to top FTC officials, but the response was merely a form letter.

Attorney Douglas Brooks made an incredibly accurate prediction of DSA/MLM resistance to any law or rule that might harm its members, even if it was important for consumer protection

In 1995, attorney Douglas M. Brooks submitted comments to the FTC regarding the Franchise and Business Opportunity Rule. In his comments, he effectively articulates the need for disclosures by MLM companies to minimize deception and loss. The situation then faced by the Commission is accurate, and the response by the DSA/MLM lobby is predicted with incredible accuracy.

For excellent historical background on the legality and inherent flaws of multi-level marketing, read also the letters from Bruce Craig, former assistant to the Wisconsin Attorney General, to then FTC Chairman Robert Pitofsky and to FTC economist Dr. Peter Vander Nat. (They are available in Appendices 2E and 2F of Chapter 2 of *Multi-level Marketing Unmasked*).

Martland & Brooks, Attorneys At Law
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August 10, 1995

Donald S. Clark, Secretary, Federal Trade Comm.
Sixth & Pennsylvania Avenue, NW, Rm. H-159
Washington, DC 20580

Re: 16 CFR Part 436 -- Comment³

Dear Mr. Clark:

This letter is in response to the Commission's Request for Comments concerning the Trade Regulation Rule on Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, 16 CFR Part 436 [the "Rule"]. This letter specifically addresses that portion of the request concerning whether the FTC Rule should be extended to apply to multi-level marketing plans, that is, questions (9) through (16), entitled "The Applicability of the Rule to Business Opportunities."

Our views, as outlined in more detail below, are as follows:

1. Although some multi-level marketing distributorships might constitute "franchises" within the meaning of the Rule, the matter is open to doubt, and multi-level marketing firms uniformly take the position that they are not franchises.

2. Even if multi-level marketing distributorships are not considered to be franchises, pre-sale

disclosure in some form is necessary in order to avoid deception.

3. The pre-sale disclosures would not need to be as extensive or detailed as those required for franchises, due to the smaller investments typically required to operate multi-level marketing distributorships.

4. Earnings information in the pre-sale disclosures should be mandatory, due to the high incidence of deceptive earnings claims by the promoters of multi-level marketing plans.

5. There should be an outright prohibition of certain forms and features of multi-level marketing plans, such as "breakaway" plans and minimum purchase requirements, due to their inherent capacity for deception and unfairness.

In Section I below we give a brief background of multi-level marketing, including an outline of our experience in this area. We address the specific questions raised by the Commission concerning the applicability of the Rule to multi-level marketing in Section II. We discuss in Section III some features of multi-level marketing which should be prohibited outright. In Section IV we outline the current regulatory environment concerning multi-level marketing plans. Finally, in Section V we discuss the need for regulatory action and further study in this area.

I. Background

"Multi-level marketing", sometimes referred to as "network" marketing or direct sales, is a technique for the distribution of products or services in which independent distributors perform a dual function: selling the product or service and recruiting new distributors. As in more traditional distribution systems, distributors are at least theoretically

³ Formatted in two columns and smaller type to save space

expected to purchase and resell products, usually through direct sales to consumers. The key distinguishing feature of multi-level marketing, however, and the feature which undoubtedly provides its main attraction, is that distributors who successfully recruit other distributors may receive commissions or bonuses based not only on purchases by their own recruits, but also on purchases by distributors recruited by their recruits, and so on (their downline").

Theoretically, at least, multi-level marketing companies pay commissions and bonuses only upon the sale of products or services by distributors to consumers; i.e., persons who are not part of the distributor structure. Over the years, however, there have been a series of sometimes spectacular failures and misadventures by companies, including Glenn Turner's "Dare to Be Great" and "Koscot Interplanetary" programs, Bestline Products, Holiday Magic, the Cambridge Diet, FundAmerica, the International Loan Network and Consumers' Buyline, Inc., in which the ultimate consumers were comprised mainly of distributors. Even well-established multi-level marketing companies have regularly attracted enforcement actions by state and federal regulators, including the Commission. Prominent examples include Amway, Nu Skin International, Herbalife International and National Safety Associates, all of which have been forced to modify their marketing practices.

Despite these problems, multi-level marketing has become a billion dollar industry in this country, involving millions of "independent" distributors. In recent years some of the more successful firms have expanded overseas, particularly in the Pacific rim nations, as well as in Canada, Mexico and Europe. Some multi-level marketing firms based in other countries, notably Canada, recruit actively in this country.

While our primary expertise is in franchising, this firm represents and has consulted with many former distributors in multi-level marketing companies. We have analyzed scores of different multi-level marketing plans. We are currently representing former distributors in one certified and several putative class actions involving multi-level marketing programs. In the course of our representation of these clients, we have had occasion to take depositions of dozens of current and former participants in multi-level marketing plans, as well as officers and employees of multi-level marketing companies and suppliers to multi-level marketing companies. We have also interviewed scores, if not hundreds, of distributors who have contacted us regarding their experiences with this form of doing business, and have received completed questionnaires (in connection with matters being litigated) from hundreds more. We hope that our perspective will assist the Commission in determining to require pre-

sale disclosures in the sale of multi-level marketing distributorships, and to prohibit the use of certain formats of multi-level marketing.

II. The Applicability of the Rule to Multi-Level Marketing

[What follows are responses to specific questions concerning the Trade Regulation Rule on Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures — JMT]

(9) To what extent do business opportunity sellers currently comply with the Rule?

We are not aware of any promoter of a multi-level marketing plan which considers its plan subject to the Rule or which provides a disclosure statement in accordance with the Rule. There is little doubt that most multi-level marketing distributorships meet the trademark and control or assistance elements of the definition of a franchise under the Rule. 16 CFR §436.2(a)(1)(i)(A) and (). Most such plans (at least those which have considered the issue) seek to qualify themselves under the minimal payment exemption, 16 CFR §436.2(a)(3)(iii), asserting that the total required payments are less than \$500. within 6 months after commencing operations. The arguments which are usually made to invoke the exemption are that (a) the only "required" payment is the nominal fee (usually between \$35. and \$100.) for a "starter kit" or "distributor kit" to become a distributor; and (b) the distributor's purchases of products from the promoters, which may well exceed \$500. within the first six months, constitute the purchases of reasonable quantities of merchandise at bona fide wholesale prices.

These arguments are suspect. While the pre-printed form distributorship contracts generally contain self-serving provisions to the effect that the nominal initial fee is the only "required" fee, the actual operation of a multi-level marketing distributorship involves substantial additional payments for sales aids purchased from the promoters, as well as other business expenses, as described in more detail below. We have not seen any contractual mechanisms which would preclude a distributor from spending more than \$500. in sales aids, for instance, within the first six months of operation. It is highly questionable whether a distributor could effectively operate without the use of such items.

In addition, most multi-level marketing plans have some minimum purchase requirements in order for distributors to qualify to earn commissions. That is, even if a distributor has recruited other distributors (and thus created a "downline") and those distributors purchase products, the "sponsoring" distributor may not be entitled to commissions unless he meets his own

minimum purchase requirement during the payout period. This feature of a plan calls into question whether a distributor's purchases are truly in "reasonable quantities." The goal of most multi-level marketing distributors is to establish a "downline" of distributors which will generate commission income far in excess of the minimum product purchase requirement. Other systems provide a threshold level of purchases (often ranging from \$2,000. to \$4,000.) which entitle distributors to earn commissions. While theoretically the threshold could be reached after several months of retailing a sufficient amount of products, many distributors are urged to "buy in" when they sign their distributorship agreement, by simultaneously submitting an order at the threshold amount.

Finally, the prices at which distributors purchase products may not be bona fide wholesale prices. The products are generally quite expensive, with the "wholesale" prices paid by distributors often being higher than retail prices of comparable products. Promoters, accordingly, tend to stress the "uniqueness" and high quality of the products. It is questionable whether the prices paid by distributors are bona fide wholesale prices. Multi-level marketing companies must charge significant markups to distributors in order to fund the various commissions and payouts, which are redistributed to other distributors. Nu Skin, for instance, claims that it pays "up to 58 percent of revenues from product sales back to the Distributor." Since commissions are not equally divided among all of the distributors (some Nu Skin distributors receive \$150,000. or more in commissions per month), the distributors at the bottom of the marketing structure end up paying significantly more than a "wholesale" price for Nu Skin products.

In addition, since distributors only qualify to receive commissions in a given month if they have met their minimum purchase requirements, and since not all distributors meet these requirements every month, the company will never have to payout the entire portion of its revenues designated for commissions. This "inflation" of the so-called "wholesale" prices is born out by the actual experience of multi-level marketing distributors, who are rarely able to earn significant "retail profits".

(10) What are the costs and benefits of the Rule to business opportunity sellers subject to the Rule's disclosure requirements?

(11) What are the costs and benefits of the Rule to prospective purchasers of business opportunities?

As noted above, sellers of multi-level marketing distributorships do not currently attempt to comply with the Rule. The prospective costs and benefits of extending the Rule, in revised form, to multi-level

marketing plans are discussed in the responses to questions (15) and (16) below.

(12) To what extent do purchasers of business opportunities obtain relevant and material information from the required disclosures? Explain.

Formal disclosure documents similar to those required by the Rule are rarely provided to prospective distributors, and usually in compliance with orders issued in enforcement actions brought by the Commission or state attorney generals. Most multilevel marketing systems do not have any consistently enforced mechanism for ensuring that distributors receive timely, accurate and complete disclosures. Even in systems which provide some earnings information to distributors, it may be up to the recruiting distributor whether to disclose this information to prospective distributors.

Information concerning multi-level marketing plans is typically provided in video and audiocassette tapes and brochures. The quality of these materials vary widely. In some systems, especially start-up companies which cannot afford high production costs, distributors are permitted to prepare their own materials. There may or may not be adequate procedures for the company to review and evaluate such materials. The more sophisticated firms prohibit or tightly control the use of distributor-produced promotional materials. Even in company-produced marketing, however, there is typically a dearth of hard data, and often a vast amount of misinformation and disinformation provided to prospective multi-level marketing distributors. The marketing pitches generally include the following elements:

1. Multi-level marketing is said to be more effective than "traditional" forms of marketing. Multi-level marketing companies do not have to spend large sums on advertising and marketing, since all of the marketing is done by the distributor force. As discussed below, however, it is questionable whether the cost of paying commissions to distributors results in any real savings over the sums not spent on traditional forms of advertising and marketing.

2. Multi-level marketing has been endorsed by the Wall Street Journal and Harvard Business School; of course no such endorsements have ever been made. There are frequently references to "futurist" texts such the "Age Wave" and statements that the multi-level marketing technique will account for a large percentage of product distribution in the years to come.

3. There are often references to economic uncertainties, layoffs, downsizing, the inadequate retirement savings of most Americans, etc. Multi-level marketing is presented as an answer to all of these woes.

4. The only investment "required" to participate is the purchase of a "distributor kit" or "starter kit" at

nominal cost, typically between \$35 and \$100. The actual cost to participate, however, is often much greater. Since the starter kit usually does not contain any sample products, distributors are told that they should purchase a selection of products -- usually there are prepackaged product sample packages available, often priced at a level sufficient to meet the distributor's monthly purchase requirement.

In addition, distributors are urged to purchase sales aids, such as audio and video cassette tapes, presentation binders, form distributorship contracts, product information pamphlets and other items. Moreover, distributors are urged to attend "opportunity" or "training" meetings on a weekly basis, or even more frequently. While prospects may attend for free, distributors are typically expected to contribute to the cost of the meeting room and, occasionally, the cost of flying in "heavy hitter" distributors to speak at the meetings. Distributors also incur costs to participate in telephone conference calls, traveling to meetings and conventions, running classified advertising and other business expenses, as well as products purchased as promotional giveaways.

5. Promoters often state that multi-level marketing is not "a pyramid," that unlawful pyramids only exist where there are no products sold, or where there are large up-front purchase requirements, and that these problems do not exist with this company. It is well-settled, however, that the actual sale of products does not preclude a marketing system from constituting an unlawful pyramid.

6. There are usually references to the importance of "momentum"; i.e., join now or you will lose out on a once-in-a-lifetime opportunity. In his standard marketing pitch, one high level Nu Skin distributor used to explain his previous failure in another multi-level marketing plan as due to the fact that the "bus was already full" by the time he joined. "Momentum", accordingly, is the flip side of the problem of market saturation. Since multi-level marketing firms rarely if ever impose any limits on the number of distributors, nor do they grant protected territories or markets, late-joining distributors simply do not have the same opportunity for success that earlier entrants do because markets become saturated.

7. There are testimonials by current distributors both as to the high quality of the products sold by this company, and as to their financial success, after only a short period of time. These earnings claims are rarely accompanied by references to average earnings and other information affecting a prospective distributor's actual opportunities for success. Such disclosures are generally made, if at all, only in systems which have been subjected to FfC or state attorney general enforcement actions, or in systems which anticipate such actions. There is no disclosure of the business expenses which top distributors must incur in order to attain the represented earnings. Some top distributors receive reimbursements for

their marketing activities from the company; these payments are never disclosed to prospective distributors either.

Notwithstanding the glowing testimonials (which may be accurate reflections of the earnings of the individual distributors giving them), the percentage of distributors who reach the highest levels of many programs is generally less than 1%, and usually comprise persons who were recruited in the early stages of development. None of the earnings information complies with the requirements of the Rule, at 16 CFR §436.1(b) through (e), i.e., that the claim be relevant to the distributor's geographic market, that there be a reasonable basis for such claims, that the underlying data be prepared in accordance with generally accepted accounting principles, and that there be disclosure of the number and percentage of distributorships which have earned the stated level of earnings.

8. The products are generally described as "unique" and of higher quality than available elsewhere. In some cases these representations are simply not true. In the Omnitrition system, for instance, nutritional products having the same or similar formulations were available through mail order catalogs, generally at lower prices than the "wholesale" prices paid by distributors. In some cases the claims made for these products, particularly in the nutritional area, cannot be supported.

9. Distributors are admonished to avoid "dream stealers", i.e., persons who make negative comments about multi-level marketing.

(13) Should the Commission clarify the Rule by adding a separate definition of the term "business opportunity?" Explain.

(a) Should such a definition of "business opportunity" be expanded beyond the current definition of a "business opportunity" franchise? Explain.

(b) Should such a definition include the sale of other business arrangements such as multi-level marketing, seller assisted marketing plans, work-at-home plans, and certain distributorships and licenses? Explain.

We believe that pre-sale disclosures should be provided for purchasers of multi-level marketing distributorships. As noted in our response to question (9) above, some multi-level marketing distributorships would constitute "franchises" under the current definition. Since the only serious issue as to the applicability of the Rule to multi-level marketing is in the "minimal payment" exemption, 16 CFR §436.2(a)(3)(iii), the definition could be clarified in several ways:

A. By eliminating the minimal payment exemption.

B. By defining "payment" (the Rule does not currently contain such a definition) to include payments for the purchase of inventory in a plan which involves both the sale of products and the recruitment of new distributors by existing distributors, whose purchases may result in the payment of compensation to other distributors.

As discussed below, we believe that the required disclosures need not be as extensive as those required for traditional franchises, although earnings information should be mandatory. As a matter of clarity in rule-making, it might be advisable to promulgate a separate rule directed at multi-level marketing, rather than to modify the existing rule.

(14) Should the Commission revise the Rule's disclosure requirements for sellers of business opportunities? Explain.

(a) Should the Commission require a different disclosure document for business opportunities?

(b) What information do purchasers of business opportunities need that is not currently required by the Rule?

(c) What disclosures currently required by the Rule should be eliminated?

The following disclosures (as designated in §436.1(a) of the Rule) should be required for multi-level marketing distributorships, with modifications as noted:

(1) Names and Trademarks of the Company

[no change]

(2) Business Experience of Directors and Officers

In addition to experience of the directors and key officers, there should also be disclosure of the experience of the distributors who reach the highest levels of the plan. In many cases these individuals, although nominally "independent distributors" who theoretically participate in the plan on the same basis as all of the other distributors, are the key promoters of the plan. Due to their ability to control or influence large downlines, however, these individuals can have a crucial impact on the operations of the company.

Many multi-level marketing firms have been established by distributors with experience in other multi-level marketing programs. In these "distributor-driven" programs, the upper echelons of the distributor structure may be established prior to the

official "launch" of the company. Our experience suggests that very few distributors who join after the initial stages achieve any significant level of success.

Other firms have jump-started their growth by recruiting "heavy hitters" from other multi-level marketing companies, with the understanding that they will bring a large portion of their downline distributors with them. Due to the impact of losing a large downline, some multi-level marketing companies have become rather aggressive in enforcing contractual prohibitions against recruiting one's downline into another system, and there is an increasing amount of litigation arising from these conflicts.

(3) Business Experience of the Company
[no change]

(4) Criminal Convictions, Civil Actions and Injunctions
[no change]

(5) Bankruptcy History
[no change]

(6) Description of the Distributorship
[no change]

(7) Payments Required to Commence Operations

There should be disclosure of payments which, although not contractually required, may be necessary for effective operation of the distributorship. As discussed above, these include the purchase of sales aids, advertisements, product samples, meeting and travel expenses, telephone charges and other business expenses.

(8) Recurring Payments

In most multi-level marketing systems there are no recurring required payments, other than an annual renewal fee. There should be disclosure, where applicable, that certain levels of product purchases must be maintained in order to preserve the right to receive commissions or bonuses upon the purchases by a distributor's downline. This disclosure may properly be a part of Item (6), which would eliminate the need for this item.

(9) Required Business with Affiliates

In most multi-level marketing plans, distributors purchase products and sales aids directly from the company, making this item superfluous.

(10) Purchase or Lease Requirements

This item is probably superfluous, provided that disclosure of payments which may be necessary is made as set forth in Item (7) above.

(11) Revenue from Suppliers

This Item is superfluous, unless the system contemplates distributors purchasing from a third party.

(12) Financing Arrangements

This Item is probably superfluous, although many multi-level marketing companies permit (or encourage) the payment for products by credit card.

(13) Restrictions on Customers and Territories [no change]

(14) Personal Participation

This Item is probably superfluous, since all multi-level marketing distributorships require the personal participation of the distributor. As discussed below, failure to include such a requirement might result in the distributorship being characterized as a security.

(15) Distributorship Agreement

All of the subparts of this Item are applicable to multi-level marketing distributorships, although most clauses are much simpler than current franchise agreements. Most multi-level marketing distributorship agreements are one or two page, pre-printed forms. Generally the distributor can terminate at will, while the company can only terminate for cause. Renewal is usually automatic, although sometimes a modest renewal fee is required. The boiler plate terms should be explained in "plain English." Choice of forum/venue clauses, including arbitration clauses, are frequently included with the boiler plate terms. Most of the distributors with whom we have spoken are surprised to learn of the existence and legal effect of these clauses. The current trend is to enforce such clauses, at least when they appear in more traditional franchise or distributor contracts. For the vast majority of multi-level marketing distributors, enforcement of a clause requiring them to litigate or arbitrate disputes in distant fora presents an impossible burden; the inclusion of these clauses should be considered an unfair practice.

(16) Number of Distributorships and Terminations

Due to the wide variations in recruitment patterns, and the high rate of attrition, year to year

comparisons are likely to be deceptive. It would be more useful for prospective distributors to see the month-to-month numbers of new distributors and terminations. Disclosure should be required for each of the twelve months preceding the date of the disclosure statement, so that trends and patterns in recruitment and attrition rates can be ascertained.

Subpart (ii) of this Item is inapplicable to multi-level marketing distributorships, since there are no "company-owned outlets." Subpart (iii), which calls for the addresses of nearby franchisees is unrealistic, given the recruiting patterns of multi-level marketing and the lack of any fixed place of business or territory for most distributors.

(17) Site Selection

This Item is inapplicable to multi-level marketing distributorships, which generally do not have protected territories and are marketed as "home businesses."

(18) Training Programs

Some multi-level marketing companies offer "training" programs of varying levels of sophistication. These are usually optional, and occur after the distributor has executed the agreement.

(19) Public Figures [no change]

(20) Financial Information

The standard multi-level marketing pitch often refers to the company's financial stability, including such statements as the company has always paid its commission checks. Many prospects are aware of the collapse of other multi-level marketing companies, and seek or expect some assurance as to the financial stability of the company whose business opportunity they are considering. Accordingly, financial statements should be required in the disclosure statement. The Commission can

anticipate objections from multi-level marketing companies that the provision of financial statements, especially if they are required to be audited, will be an insurmountable barrier to entry for many companies. See, e.g., Statement of Basis and Purpose Relating to Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, IV.B.20., Bus. Franch. Guide (CCH) ~6337.

(21) Form of Disclosure [no change]

(22) Material Changes - Currency Requirement

Most multi-level marketing firms utilize widely available computer programs in the operation of their marketing plans. These programs are easily capable of generating the statistical data necessary for the disclosures. It would be a minimal burden to require the generation of new earnings disclosures on a quarterly basis, at least, and to require prospective distributors to sign an acknowledgement that they have received the disclosure document. In addition, most multi-level marketing firms have newsletters or magazines which are mailed regularly to all distributors. It would be a minimal burden to require that the current disclosure document be included in each such mailing. Continuing disclosures should be required because many of the marketing efforts in these businesses are devoted to encouraging distributors to continue investing in the system (i.e., by meeting their monthly minimum purchase requirements) or to bring back lapsed or inactive distributors back into the fold.

III. Earnings Claims -16 CFR §436.1(b)-(e)

We believe that it is essential that relevant, accurate and non-deceptive earnings information be disclosed to prospective multi-level marketing distributors. Unrealistic and outrageous earnings claims is the most problematic area of multi-level marketing.

Many multi-level marketing companies have taken the position that testimonial earnings claims are permissible, so long as they are "accurate", in the sense that the distributor may actually have received a check in that amount. Such claims are highly deceptive in that they typically represent the gross commission earnings of the distributor and do not reflect the distributor's often substantial business expenses. Testimonial earnings claims are also deceptive in that they are not accompanied by information concerning the average earnings of distributors.

At a minimum, the average monthly earnings of active distributors at each level of the marketing plan, including the average length of time distributors have been active at each level, the actual numbers of distributors at each level, and the average product purchases at each level, should be disclosed, for each of the twelve months preceding the date of the disclosure document. If the company uses a payout period other than a month, it should disclose the above information for each payout period during the prior year.

The possibility of market saturation, including the number of active distributors and their earnings on a state-by-state basis, should be disclosed. In addition, the rate of attrition, that is, a comparison of the number of newly recruited distributors against the number of distributors who have terminated or become inactive, on a monthly basis, should be disclosed.

As noted above, the computer programs utilized by most multi-level marketing companies are readily able to generate these data on a monthly basis. Given the historical pattern of deceptive earnings claims in this industry, and the strong likelihood that testimonial earnings claims will continue to be made regardless of the most vigilant policing efforts by the company, disclosure of earnings information should be mandatory.

(15) What would be the costs and benefits to firms that would be subject to such revised disclosure requirements?

The Commission will undoubtedly receive protests that any mandatory disclosure requirement in multi-level marketing would constitute insurmountable barriers to entry.

Sophisticated multi-level marketing companies, however, including a few which have been subject to enforcement actions by the Commission (Amway and Nu Skin, for instance) are already providing some disclosures to prospective distributors, without any apparent impact on their recruiting success.

It is probably true that some firms, which to date have been able to commence multi-level marketing programs with relatively little capital, would not have been able to do so under a mandatory disclosure regime. We respectfully suggest that greater barriers to entry would have a salutary effect on this industry. A firm which does not have the wherewithal to prepare an acceptable disclosure document is probably going to be unable to police the recruiting activities of its distributors, and may well collapse, leaving hundreds or thousands of unpaid distributors. The industry as a whole would benefit from the weeding out of fraudulent and inadequately capitalized firms.

(16) What would be the costs and benefits of such revised disclosure requirements to purchasers of business opportunities?

Prospective distributors may end up paying slightly higher entry fees to join multilevel marketing plans which have increased compliance costs. Due to the large number of distributors, however, the additional cost per distributor is likely to be quite small. The benefits, in the form of greater disclosure and avoidance of fraudulent and inadequately capitalized programs, would far outweigh the modest costs.

IV. Unfair Features of Certain Multi-Level Marketing Plans

There are a wide variety of designs which have been utilized by multi-level marketing companies to

structure commission payments, and a wide variety of terminology used to describe the various levels of participation, the various types of payout, and the various requirements and qualifications which distributors must meet to advance in rank, to maintain their rank, and to earn the payouts. There are certain types of plans for which presale disclosure is an inadequate remedy to combat deception and unfairness. The following types of plans, in particular, should be prohibited:

A. "Breakaway" plans. In these plans, distributors typically have a "group volume" requirement, in addition or instead of a "personal volume" requirement. The "group" consists of the distributor, plus his or her entry-level recruits. As entry level recruits advance in the program, they "breakaway" and their purchases no longer count towards their sponsor's group volume requirements. Theoretically, however, the sponsor gains, because he can now earn a new type of payout on purchases by his "breakaways" provided that the group volume requirement is met. Of course, in order to continue meeting the group volume requirement, the distributor must either recruit new distributors or purchase the required amount of products himself. The "Nu Skin" marketing plan is a breakaway type plan, and demonstrates the extraordinary levels of income which can be attained by some participants. Breakaway plans tend to generate the most lopsided disparities in earnings between distributors at the highest and lowest levels. Earnings in the range of six figures per month are possible only for a tiny percentage of distributors, but these earnings are used to market the plan to distributors who cannot possibly duplicate those results. The huge earnings disparities cannot be justified on any functional basis; the key factor in a distributor's chances of making those earnings is timing - later entrants simply cannot achieve the same earnings, no matter what their efforts may be.

B. "Matrix" plans. In these plans, distributors are limited in the number of recruits that can be placed directly below them in the marketing structure. Any distributors they sponsor in excess of this number are placed in lower ranks, which results in a benefit to the intervening ranks (purchases by a distributor three levels below his sponsor will result in commissions to a distributor two levels below the sponsor, etc.). Prospective distributors in these systems are often told that their downlines may be built for them, if distributors in their uplines are active recruiters. The "matrix" feature, accordingly, encourages the worst aspect of multi-level marketing, the idea that distributors can make money simply by purchasing their minimum requirements each month and waiting for their downline to grow and generate a large volume of commissions.

C. Monthly Purchase Requirements. Many multi-level marketing plans require distributors to meet monthly minimum purchase requirements in order to earn a payout on purchases by their recruits. While these firms will hotly deny that distributors are "required" to purchase anything, minimum purchase qualifications are the effective equivalent of a requirement, given that the primary attraction of multi-level marketing (to distributors at least) is the possibility of earning commissions on a large number of distributors, rather than "retail profits." There is, however, no functional justification why a distributor should have to purchase any set amount of products in order to qualify to receive commissions on his downline's purchases. Presumably, a distributor's compensation for buying and selling products is the retail markup, while his compensation for recruiting and training new distributors is the commissions and other payouts generated by those distributors' purchases and sales. The monthly minimum purchase requirement is simply a device to ensure a large captive market.

C. Choice of Forum/Venue Clauses. As discussed above, these clauses have the effect of precluding most multi-level marketing distributors from enforcing their legal rights.

V. The Current Regulatory Environment

Multi-level marketing companies are currently subject to a crazy quilt of overlapping federal and state statutes. The key provisions are outlined below. All of them share the defect that enforcement is reactive, rather than proactive.

A. The Federal Trade Commission Act and State "Little FTC" Acts

The operation and promotion of multi-level marketing programs, particularly the use of inflated or unrealistic earnings claims, have been found to be "unfair or deceptive" in violation of the FTCA and various state statutes modeled after it. See, e.g. *United States v. Bestline Products Corp.*, 412 F.Supp. 754 (N.D. Cal. 1976); *In the matter of Ger-Ro-Mar, Inc.*, 86 F.T.C. 841 (1975); *Dare To Be Great, Inc. v. Commonwealth of Kentucky ex rel. Hancock*, 511 S.W.2d 224 (Ky.App. 1974) (Glenn Turner's "Dare to Be Great" selling plan was found to violate Kentucky statute prohibiting false, misleading or deceptive practices in the conduct of any trade or commerce, Ky.Rev.Stat. §367.190); *State ex rel Miller v. Santa Rosa Sales and Marketing, Inc.*, 475 N.W.2d 210 (Iowa 1991); *State ex rel Sanborn v. Koscot Interplanetary, Inc.*, 512 P.2d 416 (Kansas 1973).

With both the FTCA and its state cognates, enforcement of the prohibitions against "unfair or deceptive" acts or practices has been on a case-by-

case, post hoc basis. The absence of a private right of action under the FTCA, see, e.g. *Bell v. Health-Mor, Inc.*, 549 F.2d 342 (5th Cir. 1977), and the finite budgets of the FTC and state regulators, have the effect of allowing a substantial number of multi-level marketing firms to operate "below radar level". While some state enforcement authorities have moved aggressively against multi-level marketing schemes which operate in an unlawful manner, enforcement of state "little FTC" acts has been uneven due in part to budgetary constraints, lack of interest on the part of some state attorney generals, or lack of an effective private right of action.

Most sophisticated multi-level marketing promoters are familiar with the standards developed by the Commission in the Amway case. Almost all multi-level distributorship agreements pay lip service to the "Amway rules" and contain contractual prohibitions of "inventory loading" and retail sales requirements modeled after those approved in the Amway case. The actual observance and enforcement of these requirements, however, ranges from spotty to nonexistent. The reason for this, in our estimation, is that the Amway rules do nothing to eliminate any incentive distributors may have to violate them. For instance, programs which condition a distributor's receipt of commissions upon his or her purchase of a minimum volume of products create an incentive to load up on inventory.

Most sophisticated multi-level marketing companies have contractual clauses which are designed to thwart the practice of purchasing products solely for the purpose of qualifying to receive commissions (often referred to as "inventory loading"). A commonly used proviso requires distributors to "certify", when making an order, that they have sold or consumed at least 70% of their prior month's order. In systems with relatively low monthly purchase requirements, a distributor may be able to meet this requirement entirely through personal use of the products --thus the so-called distributor is also a consumer. In systems with higher monthly requirements these clauses are often simply ignored, often with the knowledge and tacit encouragement of the company. As with earnings claims, actual enforcement of these clauses occurs primarily in systems which have already attracted regulatory attention.

Almost all multi-level marketing firms, again in recognition of the "Amway rules", offer refunds to distributors who request them to repurchase their inventories after terminating their distributorships, typically at 90% of the distributor's cost, less shipping and handling. These refund rights are generally not an effective or complete remedy. Distributors are typically taught to use products themselves in order to be effective sales persons. They are also encouraged to use the products as sales aids, giving them or selling them at cost to prospective distributors. Obviously,

products which are disposed of are not available for refund. In addition, there is no refund for the business expenses incurred by distributors, or for the time spent fruitlessly attempting to succeed in a program where the "bus is already full." Also, many companies impose difficult or unrealistic conditions on obtaining refunds. For instance, several companies refuse to pay refunds on products which were allegedly purchased in violation of "inventory loading" prohibitions. Finally, many disappointed distributors are either not aware of their refund rights, or are too embarrassed to admit failure by submitting a refund request.

B. Federal and State Securities Laws.

The courts have repeatedly held that the definition of "investment contracts" under the federal and state securities laws is sufficiently broad to include multi-level marketing plans in which it can be established that distributors make an investment in a common venture premised on a **reasonable** expectation of profits to be derived from the entrepreneurial or managerial efforts of others. *United Housing Foundation v. Forman*, 421 U.S. 837, 95 S.Ct. 2051, 2060-61, 44 L.Ed.2d 621 (1975); *Securities and Exchange Commission v. W.I. Howey Co.*, 328 U.S. 293, 299, 66 S.Ct. 1100, 1103, 90 L.Ed. 1244 (1945) ("[t]he test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others."). See, e.g. *Securities and Exchange Commission v. Glenn W. Turner Enterprises, Inc.*, 474 F.2d 476, 480-83 (9th Cir.), cert. den., 414 U.S. 821 (1973); *Securities and Exchange Commission v. Koscot Interplanetary, Inc.*, 497 F.2d 473, 478-485 (5th Cir. 1974); *Piambino v. Bailey*, 610 F.2d 1306 (5th Cir.), cert. den., 449 U.S. 1011 (1980), appeal after remand, 757 F.2d 1112 (11th Cir. 1985); *Securities and Exchange Commission v. International Loan Network, Inc.*, 770 F.Supp. 678 (D.D.C. 1991), aff'd, 968 F.2d 1304 (D.C.Cir. 1992); *Davis v. Avco Corp.*, 371 F.Supp. 782 (N.D. Ohio 1974), aff'd sub nom *Davis v. Avco Financial Services, Inc.*, 739 F.2d 1057 (6th Cir. 1984), cert. den., 470 U.S. 1005, 472 U.S. 1012, 105 S.Ct. 1359, 105 S.Ct. 2713; *Mitzner v. Cardet International, Inc.*, 358 F.Supp. 1262 (N.D. Ill. 1973); *Frye v. Taylor*, 263 So.2d 835, 840-41 (Fla.App. 1972); *Bond v. Koscot Interplanetary, Inc.*, 246 So.2d 631 (Fla. App. 1971), appeal after remand, 276 So.2d 198 (Fla.App. 1973); *Florida Discount Centers, Inc. v. Antinori*, 226 So.2d 693 (Fla.App. 1969); *Frye v. Taylor*, 263 So.2d 835 (Fla.App. 1972).

Despite these authorities, the application of securities concepts is not an ideal regulatory solution to all of the problems of multi-level marketing. For example, even the most blatantly pyramidal forms of multi-level marketing require some effort on the part of the distributors. Determining whether this quantum of effort disqualifies a particular program from being an investment contract under the Howey definition

can consume a great deal of judicial resources. Most sophisticated promoters of multi-level

marketing programs are well aware of these issues, and have drafted their distributorship contracts and promotional *materials accordingly*. Moreover, multi-level marketing programs which avoid characterization as securities may still be highly deceptive in their operation and promotion. Finally, it is highly unlikely that any multi-level marketing company would, at its inception, attempt to register its offerings as "securities". Approval is unlikely and the cost of registration would be prohibitive for all but the largest firms.

C. Federal and State Antitrust Laws

Several aspects of multi-level marketing create a potential for running afoul of the antitrust laws. However, there have not been any recent, significant prosecutions of multi-level marketing firms under the antitrust laws. Most multi-level marketing firms include statements in their pre-printed form contracts, and their policies and procedures, to the effect that distributors are free to set their own retail prices. We have not seen any substantial evidence of price-fixing in the programs we have investigated, although some distributors do not seem to have understood that they had a right to sell at prices other than the manufacturer's suggested retail prices. The most common problems associated with retail pricing by distributors, in our experience, is that the "wholesale" prices paid by distributors are so high they are unable to consistently make any retail profits. Many distributors have advised us that if they sold products at all, they sold at cost or at a small mark-up, in order to maintain their qualifications in the program and so preserve the opportunity to earn bonuses and commissions on their downlines.

One potential for antitrust investigation involves firms which charge different prices for products depending on what level the distributor has reached. In those firms where all distributors purchase directly from the company and sell to consumers, rather than other distributors, there is probably little or no justification for a functional discount. In effect, the "discounts" in such programs are a means of compensating distributors for their recruitment activities.

D. Other State and Federal Statutes

1. State Anti-Pyramid Sales Acts.

Many states have specific statutory prohibitions against "pyramid marketing" or "chain schemes". See, e.g. *Bounds v. Figurettes, Inc.*, 135 Cal.App.3d 1, 185 Cal. Rptr. 480 (Cal.App. 1982) (multi-level lingerie distribution company violated California "endless chain" scheme statute, Penal Code §327); *Koscot Inter-planetary, Inc. v. Draney*, 530 P.2d 108

(Nev. 1974); *People ex reI Hartigan v. The Dynasty System Corp.*, 128 Dl.App.3d 874, 471 N.E.2d 236 (1984); *State ex reI Corbin v. Challenge, Inc.*, 725 P.2d 727 (Ariz.App. 1986); *State ex reI Edmisten v. Challenge, Inc.*, 284 S.E.2d 333 (N.C.App. 1981). Aside from problems arising from the lack of uniformity in the definition of "pyramid" or "endless chain", these statutes do not consistently provide any protection against conduct which may be unfair or deceptive, while not running afoul of the specific statutory definition.

2. Federal and State Anti-Lottery Acts.

A number of states have long-standing prohibitions against "lotteries", which have occasionally been used to prosecute multi-level marketing companies. See, e.g. *Bond v. Koscot Interplanetary, Inc.*, 246 So.2d 631 (Fla.App. 1971), appeal after remand, 276 So.2d 198 (Fla.App. 1973) (voiding contract which contemplated participation in multilevel marketing plan as a lottery against public policy); *Florida Discount Centers, Inc. v. Antinori*, 226 So.2d 693 (Fla.App. 1969); *M. Lippincott Mortgage Investment Co. of Florida v. Childress*, 204 So.2d 919 (Fla.App. 1968).

The federal Postal Lottery statute, 18 U.S.C. § 1302, has also been used against multi-level marketing firms, although there is no private right of action. See *Bell v. Health-Mor, Inc.*, 549 F.2d 342 (5th Cir. 1977).

3. State Referral Sales Acts.

Some multi-level marketing firms have been prosecuted under state statutes prohibiting "referral sales". See, e.g. *Chapel Hill Spa Health Club, Inc. v. Goodman*, 90 N.C.App. 198, 368 S.E.2d 60 (N.C.App. 1988) (retail installment contract for sale of spa membership was void under North Carolina referral sales statute, N.C.Gen.Stat. §25A37, because it was contingent upon the procurement of prospective customers provided by the purchaser); *State ex reI Miller v. Santa Rosa Sales and Marketing, Inc.*, 475 N.W.2d 210 (Iowa 1991). These statutes, as with the other types of statutes discussed above, vary in their definitions of unlawful conduct and existence of private rights of action; and enforcement is uneven.

E. Private Actions

Many of the statutes listed above, such as the securities statutes and state "little FTC" acts, provide private rights of actions to persons injured by unlawful conduct. Such actions, however, face the additional constraint that an individual distributor's damages are unlikely to be large enough to justify the substantial legal fees involved. In most cases, the only viable recourse is through the class action

device, and class actions have regularly been certified in cases involving multi-level marketing companies. See, e.g. *Davis v. Avco Corp.*, 371 F.Supp. 782 (N.D.Ohio 1974), *affd sub nom Davis v. Avco Financial Services, Inc.* • 739 F.2d 1057 (6th Cir. 1984), cert. den., 470 U.S. 1005, 472 U.S. 1012, 105 S.Ct. 1359, 105 S.Ct. 2713 (1985); *Piambino v. Bailey*, 610 F.2d 1306 (5th Cir. 1980), appeal after remand, 757 F.2d 1112 (11th Cir. 1985); *Marshall v. Holiday Magic, Inc.*, 550 F.2d 1173 (9th Cir. 1977); *Nguyen v. FundAmerica, Inc.*, [CCH] Fed. Sec.L.Rep. 1195,497 (N.D.Cal. 1990). But see *Coe v. National Safety Associates, Inc.*, 134 F.R.D. 235 (N.D. Ill. 1991) (certifying class), *rev'd on reconsideration*, 137 F.R.D. 252 (N.D. Ill. 1991).

In addition to the practical difficulties of obtaining class certification, and the substantive obstacles inherent in the available causes of action, sophisticated multi-level marketing promoters, like their counterparts in the franchising industry, are adept at adding procedural obstacles, such as arbitration clauses, choice of venue clauses and choice of law clauses. But see *Rhodes v. Consumers' Buyline, Inc.*, 868 F.Supp. 368 (D.Mass. 1993) (refusing to enforce contractual arbitration clause because distributorship agreement violated public policies against pyramid marketing schemes).

Finally, the available private remedies, like the available regulatory enforcement mechanisms, are primarily reactive in nature. In many systems, the litigation process is not commenced until the marketing company has already begun to collapse, leaving most distributors without any remedy for misfeasance or nonfeasance by the promoters.

VI. The Need for Regulation and Further Study

We feel very strongly that some form of disclosure, less extensive than that required for franchises, should be required for distributorships in multi-level marketing companies, in order to avoid deception. In addition, as noted above, certain features of multi-level marketing plans, due to their inherently capacity for deception and unfairness, should be prohibited altogether.

The overwhelming majority of the distributors we have interviewed, deposed, consulted with or received questionnaires from, have had negative experiences with multi-level marketing. These experiences range from the loss of a few hundred dollars to mortgage foreclosure and marital discord. While we have not attempted to conduct any formal surveys, we have been provided with statistics by several multi-level marketing firms, generally in response to discovery requests and subject to confidentiality orders, concerning the recruitment, purchases, earnings and attrition of distributors.

Based upon all of this information it is beyond dispute that in this industry the number of successful

participants is minuscule in comparison with the number of failures. Many of the plans we have analyzed appear in effect to be wealth redistribution systems, rather than product distribution systems.

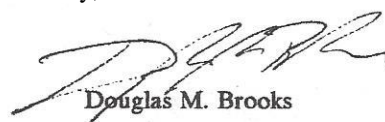
Our view of this industry is perhaps colored by the fact that we typically are only contacted by individuals who are dissatisfied with their experiences in these programs. There is, however, clearly a need for further study in this area, given the paucity of academic research on multi-level marketing firms. Very few business or graduate schools have given any serious attention to this industry. Hard data are hard to come by, since the vast majority of multi-level marketing firms are privately held corporations. We would urge the Commission to conduct or solicit independent studies of this industry, rather than to rely wholly on industry sources, such as the Direct Sales Association, which are biased in favor of multi-level marketing and their members firms, some of whom are among the worst offenders.

It is tempting to draw parallels between multi-level marketing and franchising. In some ways, the status of the multi-level marketing industry is comparable to the stage at which franchising was twenty-five years ago, when the Commission began the hearings which led to the promulgation of the Rule. It may be unwise, however, to attempt to shoe-horn multi-level marketing into the regulatory structures which have proved, on the whole, to be beneficial for franchising. Many multi-level marketing distributors start off as consumers, not businessmen. The low cost of entry of a typical multi-level marketing opportunity inevitably attracts a greater percentage of unsophisticated investors than a franchise. The lengthy and detailed disclosure documents which have become common in franchising would tend to confuse many participants in multi-level marketing programs. In addition, the expense and burden of drafting complex disclosure documents would create a substantial barrier to entry for prospective multi-level marketing companies -- although this might not be a bad result, given the large numbers of thinly capitalized and outright fraudulent firms which have utilized this form of marketing.

There is a vast amount of misinformation and disinformation associated with the marketing of even the best multi-level marketing plans. We believe that regulation directed both to pre-sale disclosure and to the formats under which multi-level marketing programs operate is essential, given their grave and demonstrated potential for deception and unfairness.

We appreciate the opportunity to present our views to the Commission.

Sincerely,



Douglas M. Brooks

On April 5, 2006, the FTC announced its Initial Proposed Business Opportunity Rule (IPBOR):

News Release For Release: April 5, 2006

FTC Proposes New Business Opportunity Rule

The Federal Trade Commission is proposing a rule to protect consumers from bogus business opportunities and further enhance law enforcement efforts in this area. The rule would cover business opportunities commonly touted by fraudsters, while minimizing compliance costs for legitimate businesses. Currently, the FTC brings law enforcement actions against fraudulent business opportunities under two laws, the Franchise Rule and the FTC Act. Neither is specifically designed for the unique scams that occur frequently with business opportunities.

The FTC has brought more than 200 enforcement actions against business opportunities using the Franchise Rule since it took effect in the 1970s, and numerous cases against work-at-home and multilevel marketing companies under Section 5 of the FTC Act. Since 1995, the Commission has conducted 12 sweeps on business opportunities.

The proposed rule would eliminate the \$500 minimum investment requirement from the Franchise Rule, meaning it would apply to all business opportunities, even if they have a smaller start-up cost. The proposed rule also would eliminate many of the 20 disclosures that are required for franchises (trademarks, for example), but do not apply to business opportunities. Instead, the proposed rule would require a one-page disclosure addressing five items: whether or not sellers make earnings claims; a list of any criminal or civil legal actions against the seller or its representatives that involve fraud, misrepresentations, securities, or deceptive or unfair trade practices; whether the seller has cancellation or refund policies and such policies' terms; the total number of purchasers in the past two years and the number of those purchasers seeking a refund or to cancel in that time period; and a list of references.

The proposed rule would not require any business opportunity seller to make an earnings claim. However, if they did make an earnings claim, they would be required to provide additional substantiation in the form of an "Earnings Claims Statement."

The proposed rule also would prohibit unfair or deceptive practices that are common among fraudulent business opportunity sellers, including:

- misrepresentations about the material terms of the business relationship;
- the use of skills;
- misrepresentations of endorsements or testimonials;
- failure to honor territorial protection guarantees; and
- failure to honor refunds.

The proposed rule takes into consideration the comments from the Advance Notice of Proposed Rulemaking issued by the Commission in 1997. The Commission is seeking comment on the proposed rule for 60 days after the Notice of Public Rulemaking is published in the Federal Register, followed by a 20-day period for rebuttals. The comment period will close on June 16, 2006, and the period for rebuttal comments on July 7, 2006. Comments should be addressed to the FTC, Office of the Secretary, Room H-135, 600 Pennsylvania Avenue, N.W., Washington, D.C. 20580. The FTC is requesting that any comment filed in paper form be sent by courier or overnight service, if possible, because U.S. postal mail in the Washington area and at the Commission is subject to delay due to heightened security precautions.

The Commission vote to approve a notice of proposed rulemaking was 5-0.

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 in [English](#) or [Spanish](#) (bilingual counselors are available to take complaints), or to get free information on any of 150 consumer topics, call toll-free, 1-877-FTC-HELP (1-877-382-4357), or use the complaint form at <http://www.ftc.gov/ftc/complaint.htm>. 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.

Media Contact:

Jacqueline Dizdul
Office of Public Affairs
202-326-2472

Staff Contact:

Steven Toporoff
Bureau of Consumer Protection
202-326-3135

16 C.F.R. Part 437: Business Opportunity Rule: Notice of Proposed Rulemaking to Promulgate a Trade Regulation Rule to Prohibit Business Opportunity Sellers From Failing to Furnish Prospective Purchasers With Material Information Needed to Combat Fraud and Other Unfair or Deceptive Acts or Practices

- [Text of the Federal Register Notice](#)

Federal Register Notice: Go to –

www.ftc.gov/os/2006/04/R511993BusinessOpportunityRuleNoticeofProposedRulemaking.pdf

(To see FTC's footnotes, go to actual notice.)

FEDERAL TRADE COMMISSION

16 CFR Part 437

Business Opportunity Rule

AGENCY: Federal Trade Commission.

ACTION: Notice of proposed rulemaking.

SUMMARY: The Federal Trade Commission (the "Commission" or "FTC") is commencing a rulemaking to promulgate a trade regulation rule entitled "The Business Opportunity Rule" (or "the Rule"), based upon the comments received in response to an Advance Notice of Proposed Rulemaking ("ANPR") and other information discussed in this notice. The proposed Business Opportunity Rule would prohibit business opportunity sellers from failing to furnish prospective purchasers with material information needed to combat fraud and would prohibit other acts or practices that are unfair or deceptive within the meaning of section 5 of the Federal Trade Commission Act ("FTC Act").

The proposed Business Opportunity Rule calls for streamlined disclosures that, compared to the Franchise Rule, substantially reduce the compliance burden. Therefore, the kinds of limits written into the Franchise Rule are not necessary to achieve an appropriate balance between prospective purchasers' need for pre-sale disclosure and the burden imposed on business opportunity sellers. Accordingly, the proposed Rule has no minimum cost threshold, no inventory exemption, and no limit on scope based on the type of assistance promised as part of the offer. Nor is the coverage of the proposed Rule limited to transactions where the purchaser of the opportunity sells goods or services directly to end-users other than the business opportunity seller. In short, the scope of coverage of the proposed Rule is much broader than that of the Franchise Rule, while the compliance burden is much lighter.

Excerpts applicable to MLM:

b. Pyramid Marketing Schemes

Like business opportunities covered by the existing Franchise Rule, pyramid schemes often deceive consumers with the promise of large potential incomes. It is not uncommon for promoters of these schemes to claim potential incomes of thousands of dollars a week or month. Because of the claimed high earnings potential, pyramid schemes are highly successful in attracting prospective investors. For example, one pyramid program attracted more than 150,000 consumers who collectively paid over \$80 million during the course of three years. Indeed, cases brought under section 5 against pyramid marketing promotions have resulted in huge consumer redress, such as \$40 million in *Equinox* and \$20 million in *SkyBiz.com*.

The prevalence of false earnings claims is not the only similarity between pyramid schemes and business opportunity frauds covered by the current Franchise Rule. Many induce new recruits with the promise of an ongoing commercial relationship that will enable recruits to operate their own business selling various products or services. Typically, they promise to provide recruits with promotional assistance. Some also offer training. Few, however, reveal their high drop-out rates, much less the fact that the vast majority of those who have joined the program—often 90 percent or more— will not recoup their investment.

Further, since 1990, the Commission has brought 20 cases against pyramid schemes under section 5.79 These matters have involved a wide range of purported product sales or investments, ranging from the mundane 80 (nutritional supplements, beauty aids, weight-loss products, and water filters) to the unusual (auto leasing, charitable giving, unsecured credit cards, credit repair, travel agency credentials, Internet malls, and Internet access). Indeed, pyramid fraud has gone high-tech, flooding the Internet and consumers' email boxes

The Commission staff's analysis of consumer fraud complaint data also demonstrates the

prevalence of deceptive pyramid marketing schemes. For the period January 1997 through December 2005, Commission staff found that consumers lodged 17,858 complaints against pyramid schemes, reporting alleged aggregate injury level of over \$46 million (\$46,824,347). Indeed, complaints against pyramid marketing companies⁴ consistently ranked among the top 20 injury categories reported in consumer fraud complaints to the Commission. For example, during the period 1997 through 2005, pyramid marketing schemes ranked among the top 20 injury levels each year⁵, except in 2003, as follows:

Year	Rank	Injury
1997	9 th	\$352,769
1998	5 th	1,858,787
1999	10 th	2,011,012
2000	4 th	12,632,132
2001	10 th	10,685,083
2002	16 th	9,685,722
2003	(Not in top 20)
2004	18 th	2,264,112
2005	17 th	3,347,443

Were it not for the minimum investment and inventory exemptions in the Franchise Rule, many pyramid schemes would be covered because the same potential for abuse exists as with vending machines and rack display opportunities covered by the Franchise Rule. In view of the misrepresentations and omissions that fraudulent pyramid scheme promoters have used, as shown by consumer complaints and past Commission cases, pre-sale disclosures and prohibitions are necessary to protect potential recruits from deceptive practices.

Section E. The Proposed Rule

The proposed Rule is divided into nine sections. Section 437.1 would set forth the Rule's definitions. Section 437.2 would establish the business opportunity seller's obligation to furnish prospective purchasers with material information in the form of a written basic disclosure document. Section 437.3 would specify the content of the basic disclosure document. Section 437.4 would set

forth the requirements business opportunity sellers must follow if they elect to make earnings representations. Section 437.5 would prohibit a number of deceptive claims and practices in connection with business opportunity sales. Section 437.6 would set forth the Rule's recordkeeping provisions. Section 437.7 would expressly exempt from the Business Opportunity Rule those business arrangements that are covered by the Franchise Rule. Finally, two administrative sections- 437.8 and 437.9 - would address other laws, rules, and orders, and severability.

IMPORTANT NOTE:

FTC officials seem unaware of the extreme reluctance of MLM victims to file formal complaints⁶, so the injuries from victims of recruitment-driven MLMs, or product-based pyramid schemes, are severely under-represented.

The reader may ask: Why do so few MLM victims file complaints? It is because victims not only have been taught to blame themselves for any losses, but they also fear consequences from or to those they recruited – often close family and friends. And they fear self-incrimination, because in every endless chain recruitment program, every major victim of necessity becomes a perpetrator, recruiting others to have any hope of recovering his/her initial and ongoing investments.

Were MLM victims not so silent, the level of injuries of product-based pyramid schemes would surely rank at the top of the categories of fraud in the FTC's statistics – easily exceeding the total of all other business opportunity scams combined. We know from our research⁷ that tens of millions of MLM victims suffer tens of billions of dollars in losses every year.

⁵ We know from our research that the harm done to MLM victims is many times what the FTC perceives – tens of millions of victims lose tens of billions of dollars every year. Yet only a tiny percentage of them ever file complaints with law enforcement. See Chapters 7 and 9 of my book *Multi-level Marketing Unmasked*.

⁶ Reasons for the silence of MLM victims are explained in Chapters 2 and 9 of my book *Multi-level Marketing Unmasked*. I discovered the fear element when it took almost a year to get over 20 Nu Skin victims to file a formal complaint with Utah's Div. of Consumer Protection.

⁷ Op. cit. Chapters 2-7

The DSA issued a 336-page shotgun blast of arguments to defend a fundamentally flawed industry⁸

The Direct Selling Association (DSA) began their lobbying campaign with a salvo of self-serving and deceptive⁹ arguments frequently used by MLM promoters to recruit new people and to defend MLM against regulators, attorneys, the media and the general public. The staff never fully recovered from the initial blast.

Comment: 522418-12055
Received: 7/17/2006 6:00:15 PM
Organization: Direct Selling Association
Commenter: Joseph Mariano
State: DC
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-12055.pdf](#) [Download Adobe Reader](#)

Comments:

Please find attached part 1 of 11 of the Comments of the Direct Selling Association regarding Business Opportunity Rule, R511993. Because of the size of the submission, it has been divided into 11 parts. A web link to the entire submission is at <http://www.dsa.org/dsaftccomments/>. Please note that a copy was emailed to Steven Toporoff and two CD copies were hand delivered to the FTC on July 17, 2006. Thank you for your attention.

The submission of DSA comments on the FTC web site was in 11 parts:

2882 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12055
 2883 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12058
 2884 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12061
 2885 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12066
 2886 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12070
 2887 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12074
 2888 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12079
 2889 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12083
 2890 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12087
 2891 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12092
 2892 [Direct Selling Association](#) (Mariano, Joseph) (7/17/2006) # 522418-12096

Total for 11 parts: an opening salvo of 336 pages of arguments, urging the FTC to exempt MLMs from a Rule that might hurt their businesses, regardless of how helpful the Rule would be in protecting consumers from unfair and deceptive practices.

On the next pages is the executive summary, which is sufficient to understand their key points. The 336 pages of explanation can be read by clicking the links above, but **it is clear (to those familiar with the DSA's hidden agenda) that the intent is to obfuscate the issues for the FTC staff, rather than to clarify and contribute to the FTC mission of protecting consumers against unfair and deceptive practices.**

(All of the comments of the DSA – and 17,000 other commenters can be found by going to the index at the Public Comments page at – <http://www.ftc.gov/os/publiccomments.shtm>. Scroll down to #178 to find the comments listed alphabetically.)

⁸ The fundamental flaws in MLM as a business model are explained in Chapter 2 of my book *Multi-level Marketing Unmasked*.

⁹ Over 110 typical misrepresentations used in MLM recruitment are rebutted in Chapter 8 of my book (op.cit.). Many of these practiced arguments were used in the DSA comments.

EXECUTIVE SUMMARY (DSA)

The following is a summary of the key points raised by the Direct Selling Association (DSA) in our submission, points supported by surveys, data, experience, interviews and legal analysis. DSA is the non-profit national trade association of the leading firms that manufacture and distribute goods and services sold directly to consumers by personal presentation and demonstration, primarily in the home. More than 200 companies are members of the association, including many well-known brand names, doing approximately 95 percent of the industry's U.S. sales. There are also over 1,300 direct selling companies that are not members of the association.

Legitimate direct sellers play an important role in the national economy. For example, they permit providers of new products and services to enter the market more economically, offer a flexible, part-time opportunity for individuals to supplement their income, and broaden the array of product and service choices available to consumers. Unfortunately, fraudulent and unscrupulous businesses have often either passed themselves off as, or been confused with, the many legitimate companies that use the direct selling business model. DSA understands that the proposed business opportunity rule is intended to protect the public from the unfair and deceptive practices of these fraudulent operators, particularly those that operate work at home and pyramid schemes. Any meaningful and effective business opportunity regulation must recognize the fundamental differences between such business opportunity frauds and legitimate direct selling activities. However, the rule proposed by the FTC fails to do so and as a result of that failure would unnecessarily subject legitimate direct sellers to onerous requirements that would impose significant financial and administrative burdens while at the same time reducing the attractiveness and therefore success of direct selling.

There are several ways that the FTC could revise the proposed rule to ensure that legitimate direct selling companies are excluded. For example, the FTC might:

- Exclude from the rule's provisions those business opportunity sellers whose opportunities carry minimal (or no) cost or risk.
- Retain the definition of business opportunity contained in the Franchise Rule, which does not include most or all direct sellers.
- Better define "business opportunity" to cover to work at home, vending machine, and similar schemes, and not include direct sellers.
- Exempt companies that adopt and adhere to a set of industry best practices, including, for example, requirements relating to wholesale inventory purchases protected by buyback policies and/or a "cooling-off" right for salespeople.
- Exempt companies that are subject to a self-regulation process such as that offered by DSA.

DSA cannot overstate the harm to legitimate direct sellers that would result from the proposed rule. The rule presents two potential costs to legitimate direct sellers – the expenses associated with compliance and the impact of decreased business activities. With respect to compliance, the FTC has dramatically underestimated the time, effort, and expense necessary to collect information and provide disclosures for the array of issues addressed in the proposed rule. One company alone estimates that it would be faced with the responsibility to print and distribute some 15 million pieces of paper over a three year period as a result of the proposal. The FTC has also failed to acknowledge the significant harm to legitimate direct sellers, i.e., the loss of business that would occur if they were subjected to the requirements of the proposed Rule. Several of the most problematic requirements are addressed below.

The waiting period requirement in the proposed Rule is impractical and will fundamentally and adversely alter the way in which direct selling operates. The proposed rule requires that individuals wait at least seven days after they first express interest before they can sign up as a direct seller. Much legitimate direct selling recruiting takes place in personal, social meetings, often in a customer's home and often in a group. Interested recruits are ordinarily signed up on the spot. Imposing a waiting period would significantly increase the amount of time direct salespeople, most of whom work part time, would have to devote to recruiting activities, would divorce the transaction from the social interaction to which it relates, and would delay the earning opportunity for the prospective direct salesperson. Moreover, because one of the hallmarks of the direct selling business model is its ease of entry, this change would certainly result in the loss of interest by many recruits. Indeed, a recent survey of the general public indicated that the level of interest in direct selling by a prospective direct seller would drop at least 33 percent if a waiting period were instituted, and among those expressing the greatest likelihood of entering direct selling, the interest level would drop 57 percent. If the FTC continues to pursue a business opportunity rule, DSA urges the FTC not to include any waiting period, but instead to consider more realistic and less burdensome alternatives such as providing "cooling off periods" in which direct salespeople have an opportunity to cancel their relationship and receive a full refund.

The legal action disclosure requirement in the proposed rule is overbroad and unmanageable and will likely produce significant unintended consequences. The proposed rule requires that sellers of business opportunities disclose a list of civil or criminal legal actions for misrepresentation, fraud, securities law violations or unfair or deceptive practices involving the seller, its affiliates, officers, directors, sales managers or potentially, the millions of individuals who sell for them dating back ten years. Much of the legal action required to be disclosed by the proposed rule will be irrelevant to a prospective purchaser, most notably those actions which are unrelated to business opportunity sales. Moreover, while it is not clear, the proposed rule could be interpreted to require a direct selling company to disclose litigation involving any member of its independent contractor sales force. Many DSA members, some of whom have sales forces of hundreds of thousands, would have no feasible way to comply with such a requirement. Also, requiring direct selling companies to disclose legal actions to recruits encourages unscrupulous competitors to file more suits to gain a competitive advantage. The overall effects will again be to unnecessarily discourage recruits from pursuing legitimate direct selling activities and to harm the businesses of current direct salespeople. The mere listing of legal actions, including ones won by the company, would have a chilling effect on potential recruits, 90 percent of whom are seeking modest goals from their involvement in direct selling. A recent survey indicated that the level of interest in direct selling by a prospective direct seller would drop at least 29 percent if this burdensome disclosure was instituted, and among those expressing the greatest likelihood of entering direct selling, the interest level would drop 43 percent. If the FTC continues to pursue a business opportunity rule, DSA urges the FTC not to include any legal action disclosure requirement.

The cancellation and refund disclosure requirement in the proposed rule would be difficult to comply with and would provide prospects with little useful information.

The proposed Rule requires direct selling companies to record and track all opportunity sales transactions. Because of the sheer number of transactions (a function of, among other things, the ease of entry into and exit from the industry, recording and tracking that information would impose a significant, new burden on direct sellers. At the same time, that information would likely be of relatively little use to recruits because even a high turnover rate likely is a reflection of the nature of the industry, instead of an indication of a problematic seller. If the FTC continues to pursue a business

opportunity rule, DSA urges the FTC not to include disclosures about direct selling cancellations and refunds, as they are not indicators of fraud or deceit in our industry. On the contrary, our high turnover rate is a sign of the vitality of our industry and the ease of entry and egress.

The references requirement in the proposed rule disregards the privacy and property rights of recruits and sellers, respectively, and is simply not workable. The proposed rule would require direct sellers to disclose the names and contact information of current members of their sales forces without those members' authorization, and to disclose such information for future salespersons based on a simple disclaimer in the proposed disclosure document. This requirement provides woefully inadequate protection for direct salespeople's personal information and flies in the face of the FTC's commitment to protecting privacy. In addition, the names and contact information of their salespersons constitute a direct selling company's most valued trade secret and therefore should not be subject to compulsory disclosure. Finally, the option in the proposed rule to disclose the ten closest prior "purchasers," while arguably appropriate for business opportunities as historically understood is simply unworkable for direct sellers, at least for those direct selling companies with sizeable sales forces. Not surprisingly, the references requirement would significantly harm direct selling. A recent survey indicated that the level of interest in direct selling by a prospective direct salesperson would drop at least 38 percent if this reference requirement were instituted, and among those expressing the greatest likelihood of entering direct selling, the interest level would drop 71 percent. If the FTC continues to pursue a business opportunity rule, DSA urges the FTC not to include any references disclosure requirement.

Finally, the earnings claims disclosure requirement is too complicated and not useful *vis a vis* direct sellers. For example, the proposed rule requires disclosure of "[a]ny characteristics of the purchasers who have achieved at least the represented level of earnings, such as their location, that may differ materially from characteristics of the prospective purchasers being offered the business opportunity...." Because it is impossible to know with any degree of certainty what demographic/geographic and other factors might affect the earnings of direct sellers, and what impact they might have, direct sellers will have no practical way to comply with this provision. The Commission should allow greater flexibility in the form and substance of any earnings disclosures. If the FTC continues to pursue a business opportunity rule, it should consider allowing multiple forms of earnings disclosures and substantiation, including the prominent use of disclaimers in connection with earnings claims. DSA also urges the FTC to adopt a narrower more and specific definition of "earnings claims" than the one that has been proposed.

Conclusion

DSA supports and shares the FTC's goal of ridding the marketplace of fraudulent business opportunities. The proposed rule, however, would cast far too wide a net and in doing so would harm and possibly destroy many legitimate, lawful direct sellers. The proposed rule would also likely unnecessarily discourage many prospects from pursuing beneficial direct selling activities. Therefore, if the FTC continues to pursue a separate business opportunity rule, DSA urges the FTC to exclude from its requirements those legitimate, lawful companies that use the direct selling business model. DSA also urges the FTC to remove and/or limit many of the onerous or misguided requirements in the proposed rule, including those relating to a waiting period, legal action disclosures, cancellation and refund disclosures, references, and earnings claims. Direct selling companies are not sellers of business opportunities and should be exempted from any business opportunity fraud rule. DSA looks forward to continued participation in the rulemaking process.

A revolving door from consumer protection to fraud protection has evolved at the FTC.

Timothy Muris and Howard Beales, Jr. – comments on behalf of Primerica (#9260 – 43 pages), and Joan “Jodie” Bernstein on behalf of Quixtar (Amway/Altacor)

The DSA/MLM lobby wasted no time enlisting the comments of these former high-level officials to lobby for the MLM industry, which – considering the flawed and fraudulent model of MLM they were defending – meant they were lobbying against the interests of consumers. This revolving door from consumer protection to fraud protection should be very troubling to those interested in protecting consumers against unfair and deceptive practices – which should be the objective of the FTC, as that is their charge as clearly stated in Section 5 of the FTC Act.

Primerica Financial Services Inc. (Muris, Tim) (7/17/2006) # 522418-11929

Peter Schneider, Esq. **Timothy J. Muris, Esq.** Alexis Ginn, Esq. **J. Howard Beales, III, Consultant** Suzanne Loomis, Esq. O’Melveny & Myers, LLP Primerica Financial Services, Inc. 1625 Eye Street, NW 3120 Breckinridge Boulevard Washington, D.C. 20006 Duluth, GA 30099 (

To download the full 43-page report, go to –
www.ftc.gov/os/comments/businessopprule/522418-11929.pdf

Quixtar Inc. (Bernstein, Joan) (7/17/2006) # 522418-12039

Bryan Cave LLP, 700 Thirteenth Street NW, Washington, DC 20005-3960 (Submitted by Michael Mohr, VP and General Counsel, but with the name of Joan Bernstein’s name on top of the cover letter)

To download the full 45-page report, go to –
<http://www.ftc.gov/os/comments/businessopprule/522418-12039.pdf>

The FTC staff working on BOR rejected the only qualified, independent (not financed by the MLM industry), and industry-wide research ever done on the legitimacy and profitability (or lack thereof) of MLM as a business model.

Dr. Jon M. Taylor had by this time analyzed the compensation plans of over 350 MLMs (now over 500) and performed over 15 research studies on MLM over a period of twelve years – more independent research on the subject than by any other qualified research analyst. As one MLM analyst put it, **“Dr. Taylor has been doing the research the FTC should have been doing all along.”** However, the staff handling BOR rulemaking chose to dismiss his research, even though the data in his research was published by the MLM companies themselves, and his methodology and calculations were validated by several financial experts, including a CPA (and fraud examiner), a statistician, an actuary, a certified financial planner, and an asset evaluator.¹⁰ It should also be noted that Robert FitzPatrick corroborated Taylor’s conclusions on lack of profitability of MLMs in his report “The Myth of Income Opportunity’ in Multi-level Marketing,”

In a letter¹¹ from Christine Todaro to another staff member prior to the issuance of the Final Rule (name blocked in FOIA response), she stated:

*Mr. Taylor submitted comments on the Staff Report on the Business Opportunity Rule. His comments referred to the publication “THE CASE (FOR AND) AGAINST MULTI-LEVEL MARKETING: The Complete Guide to Understanding and Countering the Effects of Endless Chain Selling and Product-based Pyramid Schemes” by Jon M. Taylor, MBA, Ph.D. **This publication has not been approved by the FTC. Nor has the research discussed in the publication been approved by the FTC. (emphasis mine)***

Apparently, the FTC staff chose instead to accept and use the industry-slanted arguments (not substantiated by independent research) put forth by the DSA/MLM lobby, which the staff seemed unable or unwilling to dispute. Of course, it is possible that the staff did not want to make the effort to read the voluminous work referred to – or that they did not have sufficient background in math and elementary statistics to understand it and grasp its significance. And it is also possible that they are anticipating future employment – lobbying on behalf of the MLM industry after they leave the FTC – following the lead of former FTC officials Timothy Muris, Howard Beales, and Jodie Bernstein.

The full reports won’t be repeated here, only the comment submissions – to show the amount of research dismissed by the committee. The full comments can be accessed by clicking on the links for Consumer Awareness Institute at the ftc.gov web site – www.ftc.gov/os/publiccomments.shtm. Scroll down to Public Comments #178.

The comments citing my research are listed in order as listed on the FTC listing of Consumer Awareness Institute comments:

#70056 – preliminary report introducing research

#10051 – explanation of the 70-page “REPORT OF VIOLATIONS of the FTC Order for Nu Skin to Cease its Misrepresentations.”

#12684- –explanation of my “Survey of Tax Preparers.” which clearly demonstrates that it is rare for MLM participants to show a profit – in spite of their being promoted as the answer to people’s financial needs

¹⁰ Experts quoted in Chapter 7 and in the introduction of my book *Multi-level Marketing Unmasked* (formerly *The Case against Multi-level Marketing – an Unfair and Deceptive Practice*)

¹¹ The letter was obtained by means of a Freedom of Information Act request.]

#12748 – references the “Network Marketing Payout Distribution Study” – a standing challenge to the presidents of 60 of the largest network marketing (MLM) companies to “prove me wrong” on my conclusions about the abysmal loss rates of MLM participants

#10058 – more on the Nu Skin report

#10266 – still more on the Nu Skin report

#12262 – an overview of my research to date (which has been amplified considerably since) The full report follows the comment submissions.

#12585 – The “5 Red Flags of a Recruitment-driven MLM, or Product-based Pyramid Scheme” – which resulted from extensive comparative research comparing MLM with legitimate direct selling and other business models. These “causative and defining characteristics” (CDCs) had been tested in analyses of the compensation plans of 350 MLMs (over 500 by now). For those MLM companies for whom data could be obtained, the average loss rate exceeds 99%. No other research comparable to this had ever been done by competent independent researchers – yet the FTC staff dismissed it!

The first submission (#70056) – was a preliminary report introducing my research. It was updated by later submissions, so is not reproduced here.

Applicable submissions:

Comment number: 522418-10051

Received: 7/15/2006 4:28:25 PM

Organization: Consumer Awareness Institute - and Pyramid Scheme Alert

Commenter: JON TAYLOR

State: UT

Subject: Business Opportunity Rule

Title: Notice of Proposed Rulemaking

CFR Citation: 16 CFR Part 437

No Attachments

Comments:

ATTN: FTC OFFICIALS – This submission has direct relevance to the proposed Business Opportunity Disclosure Rule R511993, as it furnishes a case study in compliance (or lack thereof) with past FTC efforts by FTC officials to enforce disclosure requirements for a “business opportunity” that falls in the category of a pyramid marketing (or chain selling) scheme. In 1994, the FTC issued an Order for Nu Skin International (now Nu Skin Enterprises) and its representatives to cease and desist misrepresenting earnings of distributors. Supposedly in compliance, in 1997 and 1998, Nu Skin published a disclosure statement entitled “Actual Average Incomes.” In the year 2000, I inspected this document and found approximately 20 deceptions on a single page! Through Pyramid Scheme Alert, an organization that seeks to expose and prevent pyramid scheme fraud, I filed a paper entitled **REPORT OF VIOLATIONS** of the 1994 Order and communicated with FTC officials for over two years in an effort to get them to enforce the Order. Nu Skin immediately stopped publishing the report, and when they finally resumed, it was not made available to the public, but was treated as confidential information for its distributors. Through an informant, I got a copy of the new 2004 Nu Skin “Distribution Compensation Summary.” A few of the misrepresentations were corrected, but some major misrepresentations remained. The full and updated 70-page report can be downloaded at – <http://www.mlm-thetruth.com/Complaint-2FTC-7-15-6-NS-OneCol.pdf> Attached is the 2004 Nu Skin “Distribution Compensation Summary,” followed by a revised report with the modifications I would recommend to provide meaningful disclosure. These modifications would be more in line with the type of

disclosure required for other investments, such as securities or franchises – in which anything material to the likely performance of the investment must be disclosed. Though the initial sign-up fees are small for MLM and other chain selling programs, inducements are built into their compensation plans to either stock up or to subscribe to a minimum amount of products on an ongoing basis. Prospects as potential investors in their programs deserve as much honest and meaningful disclosure as investors in securities or franchises. Please read the suggested modifications carefully, along with the explanatory notes at the bottom of the page. One can see from these notes, which are honest and meaningful disclosure items similar to what would be required for other investments, why the DSA and its pyramid marketing (or chain selling) member firms are so strongly opposed to honest and genuinely helpful disclosure.

Sincerely, - Jon M. Taylor, Ph.D., President.

NOTE: This comment letter and associated report was revised in comments #10058 and #10266

Comment Number: 522418-12684
Received: 7/17/2006 11:34:15 PM
Organization: CONSUMER AWARENESS INSTITUTE
Commenter: JON TAYLOR
State: UT
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-12684.pdf](#) [Download Adobe Reader](#)

Comments:

ATTN: FTC personnel – Regarding the Business Opportunity Disclosure Rule R511993, my **survey of tax professionals** has much relevance to the issue of earnings disclosure that is addressed in the proposal. It was mailed earlier, but since no confirmation of your receiving it in your office could be obtained, I am attaching it now. I also formally request a hearing or forum pursuant to Section 18[c] of the Federal Trade Commission Act and Section F of the April 12, 2006, Notice of Proposed Rulemaking. I would be prepared to testify regarding the matters discussed in the tax report, as well as the submittal I sent earlier (tracking number 522418-12262). - Jon M. Taylor, Ph.D., President, Consumer Awareness Institute and Advisor, Pyramid Scheme Alert E-mail: jonmtaylor@juno.com Web site for MLM research and guides – www.mlm-thetruth.com

Comment Number: 522418-12748
Received: 7/17/2006 11:55:16 PM
Organization: CONSUMER AWARENESS INSTITUTE
Commenter: JON TAYLOR
State: UT
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-12748.pdf](#) [Download Adobe Reader](#)

Comments:

ATTN: FTC personnel – Regarding the Business Opportunity Disclosure Rule R511993, the **“Network Marketing Payout Distribution Study”** has much relevance to the issue of earnings disclosure that is addressed in the proposal. It was mailed earlier, but since no confirmation of your receiving it in your office could be obtained, I am attaching it now. This study consisted of a challenge issued to presidents of 60 of the most prominent MLM companies to voluntarily

disclose data regarding earnings of distributors that would help consumers make informed decisions. Personnel from six companies promised to respond with data, but none were able or willing to do so. I suspect upper management realized that the data was too damning. But the FTC could – and should require such information. More details on recommended disclosure, based on extensive research, is found in my earlier submissions (tracking number 522418-12262, et al) I also formally request a hearing or forum pursuant to Section 18[c] of the Federal Trade Commission Act and Section F of the April 12, 2006, Notice of Proposed Rulemaking. I would be prepared to testify regarding the matters discussed in the tax report, as well as the submittal I sent earlier (tracking number 522418-12262). Others with significant information to report relevant to the new rule include, Bruce Craig, former Assistant AG of Wisconsin, Robert Fitzpatrick of Pyramid Scheme Alert, Eric Schiebeler, Doug Brooks, an attorney specializing in this area who has worked on numerous similar cases, and Dr. Stephen Barrett, owner of the web site MLMwatch and numerous others, mostly related health quackery, which is common in MLM schemes.. - Jon M. Taylor, Ph.D., President, Consumer Awareness Institute and Advisor, Pyramid Scheme Alert E-mail: jonmtaylor@juno.com Web site for MLM research and guides – www.mlm-thetruth.com

Comment Number: 522418-12585
Received: 7/17/2006 11:02:29 PM
Organization: Consumer Awareness Institute
Commenter: JON TAYLOR
State: UT
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-12585.pdf](#) [Download Adobe Reader](#)

Comments:

ATTN: FTC personnel – One of the biggest challenges with the proposed business disclosure rule is the problem of definitions, especially “pyramid marketing schemes.” I spent many years on this topic, consulting with top experts and doing comparative analysis to identify the features that clearly separate exploitive pyramid schemes from legitimate business opportunities. “The **5 Red Flags**” clearly accomplish that. Extensive analysis of disclosures (as available), financial reports, and court records revealed that when these 5 Red Flags were in a compensation plan, the loss rate was 99%, and often close to 99.9%! The attached report prepared for the National White Collar Crime Center and for my consumer awareness web site (www.mlm-thetruth.com) clarifies the issues and helps evaluating MLM programs with potentially high loss rates. The need for disclosure is discussed on page 25. I also formally request a hearing or forum pursuant to Section 18© of the Federal Trade Commission Act and Section F of the April 12, 2006 Notice of Proposed Rulemaking. I would be prepared to testify regarding the matters discussed in the “5 Red Flags” report, as well as the submittal I sent earlier (tracking number 522418-12262). - Jon M. Taylor, Ph.D., President, Consumer Awareness Institute and Advisor, Pyramid Scheme Alert, Web site for MLM research and guides.

NOTE: Comments were revised in submission #12262.

Research and comments by another prominent consumer advocate, Robert FitzPatrick of Pyramid Scheme Alert (PSA) – whose research corroborated that of Dr. Taylor – stressing the need for adequate disclosure and waiting time, was also dismissed by FTC staff handling the Rule.

Robert FitzPatrick is the founder of Pyramid Scheme Alert, a non-profit consumer organization representing consumers worldwide. He is the author of the book *False Profits* and several useful articles about MLM which are posted on his web sites – pyramidschemealert.org and falseprofits.com. One of his most important reports is “The Myth of ‘Income Opportunity’ in Multi-level Marketing” – which is independent testimony corroborating that of Dr. Jon Taylor as to MLM’s abysmal loss rates. This report is a second witness to the critical need for adequate income disclosures (even more extensive than recommended in IPBOR) to be provided by MLM recruiters.

For the full report, go to Public Comments section of FTC web site at - www.ftc.gov/os/publiccomments.shtm Scroll down to Public Comments #178. Find Find submissions listed under both FitzPatrick and Pyramid Scheme Alert.

Comment Number: 522418-06415
Received: 7/6/2006 10:02:21 AM
Organization: Pyramid Scheme Alert
Commenter: Robert FitzPatrick
State: NC
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-06415.pdf](#) [Download Adobe Reader](#)

Comments:

Please accept the official comment of Pyramid Scheme Alert (PSA), a non-profit consumer organization. It is attached as an Acrobat PDF. Additionally, PSA requests to be invited to testify and offer its research at Hearings scheduled on the Business Opportunity Rule. Pyramid Scheme Alert (PSA) is the largest and most active non-profit consumer organization with the mission of analyzing, exposing and educating consumers about pyramid marketing schemes. Formed in November 2000, PSA assists thousands of consumers each year with email or direct phone assistance. Its website, <http://www.pyramidschemealert.org>, offers tools, research, and news for distinguishing pyramid schemes from direct selling. PSA directors and advisors have served as expert witnesses for the US Dept. of Justice and numerous state Attorney General offices in pyramid scheme prosecutions. The "pyramid marketing schemes" referenced in the FTC proposed rule harm more people than any other type of "business opportunity" fraud. They employ mass meetings to entrap consumers. They falsely promise income based on the trick of "geometric expansion" of an endless chain. They claim to offer viable income opportunities while inflicting losses upon 99% of all participants each year. "Pyramid marketing schemes"

disguise themselves as "direct selling". All such scams operate as "multi-level marketing (MLM)". In a separate mailing, Pyramid Scheme Alert has provided its statistical report documenting that more than 99% of all participants in major multi-level marketing schemes never earn a profit. Pyramid Scheme Alert proposes three components of the FTC rule requiring disclosures from multi-level marketing "business opportunity" schemes.

1. Disclosure of Retail-based Income Averages: The distinguishing feature of an MLM pyramid scam is the lack of profitable retail sales among most participants. Recruiting versus retailing is the dividing line between bogus, deceptive scams and legitimate direct selling. This standard has been applied consistently by the FTC in more than a dozen prosecutions, written into state laws, and repeatedly upheld by federal courts. Pyramid Scheme Alert, therefore, proposes that the FTC adopt rules that require the disclosure of average retail-based income for participants in each level of an MLM scheme. This data can be gathered by survey or direct reporting by participants. The FTC must insure that the data is verifiable.

2. Require that all multi-level marketing schemes make "income claim" disclosures: An "income claim" is inherent in all multi-level marketing operations, which, by definition, are "income opportunities." Therefore, no option should be allowed for any multi-level marketing company to check the box indicating it makes "no earnings claim".

3. Disclose total number of participants and average costs to participate: A common deception of pyramid marketing schemes is to provide recruits with a mean average of "income" for each level in the scheme's hierarchy or an overall mean average of "income" only for "active" participants. These mean averages are misleading and deceptive. They skew the average upward by excluding large numbers of participants that drop out during the year - as many as 60% of the actual total. An even more harmful practice is the omission of all costs - money paid out by participants to the income-opportunity-scheme - thus hiding large-scale losses by nearly all participants "Money paid out" includes incentivized product purchases and associated costs that are presented as mandatory or necessary to success, such as motivation seminar registrations, audio and video tapes, etc. When such costs are factored, 99% of participants lose money.

Thank you for the opportunity to offer comment. We are prepared to answer questions and to offer additional information.

Sincerely, Robert L. FitzPatrick, President PYRAMID SCHEME ALERT
RFitzPatrick@PyramidSchemeAlert.org

What follows is the section of the comment in which Mr. FitzPatrick recommends that MLM companies disclose the average *retail-based* income earned

Disclosure of the average *retail-based* income earned by each level of the hierarchy. This average must be documented with verifiable data on actual retail sales.

The distinguishing feature of the pyramid selling scam is the lack of retail sales. Retail sales activity is the dividing line between bogus, deceptive scams and legitimate direct selling. This standard has been applied consistently by the FTC, written into various state laws on pyramid

schemes, and repeatedly confirmed and upheld by federal courts. *Any rule seeking to cover multi-level marketing schemes that does not require disclosure of verifiable retail sales revenues will fail to protect consumers.* A rule that omits the critical retail sales level component could actually aid fraudulent schemes by seeming to endorse them for complying with less relevant and significant disclosures.

Withholding data on actual income from retail selling is the central element of deception in of disguised pyramid selling scam. By withholding this data, while also claiming to operate as a “direct selling” company, the pyramid scheme maintains the fiction of legitimacy and is able to convince consumers that it offers a viable income opportunity to large numbers of participants. Lack of retail sales, in fact, results in virtually no income opportunity being available to nearly all investors (recruited salespeople). The non-retailing, recruitment-based MLM is, in reality, nothing more than an endless chain recruitment scheme with a built-in 99% loss ratio.

In the disguised direct selling company, virtually no participants sell a significant amount of products to non-participants (retail) or earn an overall net profit from retailing. The only participants that achieve profitability do so from rebates gained from investments of new investors (salespeople). The end-users in the pyramid are the salespeople themselves. Recruiting is the essential and primary income activity for all new participants in order to recoup their investments.

A common practice of pyramid selling schemes is to claim to be retail-based “direct selling” businesses but to state that they are unable to supply income data from retailing. They frequently make the disclaimer, *“Independent Consultants can buy products from the Company at wholesale prices for resale to Clients or for personal use... Most Consultants personally use the products in addition to retailing them. As a result of these different scenarios, the company does not provide an estimate of average or actual Consultant income from retail sales.”*

If the proposed Business Opportunity Rule requires the disclosure of actual retail-based income *for each level of the scheme*, a consumer will be able to identify if income in the scheme is actually based almost entirely upon endless chain recruiting. Disclosure of retail sales income at each level will enable consumers to assess the validity of any MLM company’s claim that it is a legitimate “direct selling” business.

⁹ The state of North Carolina imposed a 70% standard in four pyramid scheme cases that it prosecuted in 1999. Indicating the vast reach of MLM pyramid frauds, the four relatively small MLM companies, Club Atlanta Travel, Destiny Telecomm International, Inc., Tele-Card International, and International Heritage, Inc., had enrolled 40,000 distributors in that one state alone. The settlement agreement between Destiny Telcomm International and North Carolina stated: “...at least 70% of all North Carolina sales shall be retail sales to persons who are not connected in any way to the Destiny sales force.” The ruling also excluded from the 70% portion, sales to individuals who subsequently became Destiny representatives.”

A better definition of what constitutes an illegal pyramid scheme was suggested by Bruce Craig, former assistant to the Wisconsin Attorney General.

Bruce Craig, former Assistant Attorney for Wisconsin, who was heavily involved in some of the earliest prosecutions against fraudulent MLMs/pyramid schemes submitted his comment letter, much of which repeats what he wrote in the letter at the beginning of this compilation – which is well worth reading. He does add an important item that is worth considering, and that is the need for an explicit definition of a pyramid offering to be established by the Commission. In addition to the Wisconsin law which also refers to the endless chain aspect of MM, he suggests as a respectable example the California Law PC327, which states:

327. Every person who contrives, prepares, sets up, proposes, or operates any endless chain is guilty of a public offense, and is punishable by imprisonment in the county jail not exceeding one year or in state prison for 16 months, two, or three years.

As used in this section, an "endless chain" means any scheme for the disposal or distribution of property whereby a participant pays a valuable consideration for the chance to receive compensation for introducing one or more additional persons into participation in the scheme or for the chance to receive compensation when a person introduced by the participant introduces a new participant. Compensation, as used in this section, does not mean or include payment based upon sales made to persons who are not participants in the scheme and who are not purchasing in order to participate in the scheme.

Comment included letter in 2000 to then FTC Chairman Robert Pitofsky

Comment Number: 522418-12306
Received: 7/17/2006 8:17:04 PM
Organization:
Commenter: Bruce Craig
State: NY
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-12306.pdf](#) [Download Adobe Reader](#)

Comments:

Comments contained in attachment below (in comments on FTC web site)

To access the full letter, go to -
www.ftc.gov/os/comments/businessopprule/522418-12306.pdf

Plaintiff Attorney Doug Brooks offers a cogent comment letter based on long experience in this field

Douglas Brooks has served as lead plaintiff attorney in several significant cases on behalf of victims of various MLM programs. Because of his diligent discovery research, he clearly saw the problems with MLM programs over 20 years ago. (See also his 1995 comments to the FTC regarding the Franchise and Business Opportunity Rule, which is included near the beginning of this compilation.)

Comment Number: 522418-10570
Received: 7/16/2006 5:54:41 PM
Organization: Martland & Brooks LLP
Commenter: Douglas Brooks
State: MA
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-10570.pdf](#) [Download Adobe Reader](#)

Comments:

Please see letter dated July 16, 2006 which is attached hereto. Exhibits A and B will be submitted separately. [reproduced below in 2 columns to save space]

July 16, 2006
 Federal Trade Commission, Office of the Secretary
 Room H-135 (Annex W)
 600 Pennsylvania Avenue, NW
 Washington, DC 20580

Re: **Notice of Proposed Rulemaking** **Business Opportunity Rule, 16 CFR Part 437**

Dear Commissioners:

I respectfully submit the enclosed comments and request for hearing concerning the proposed Business Opportunity Rule, pursuant to the Notice of Proposed Rulemaking as published in the Federal Register on April 12, 2006. I believe that the Proposed Rule represents an important step forward in the Commission's effort to protect consumers from fraudulent business opportunities, particularly multi-level marketing schemes.

I BACKGROUND AND STATEMENT OF INTEREST

I am an attorney duly licensed to practice law in the Commonwealth of Massachusetts since 1982. I have been in private practice my entire career, the first five years in a small general practice firm, the

next five years in a firm specializing in franchising and distribution law, and since then have specialized in consumer protection, antitrust and securities fraud litigation, including cases involving fraudulent business opportunities. I have represented plaintiffs and plaintiff classes in litigation involving a number of Multi-Level Marketing (MLM) systems, including *Webster v. Omnitrition International, Inc.*, 79 F.3d 776 (9th Cir.), *cert. den.* 519 U.S. 865 (1996); *Capone v. Nu Skin Canada*, 93-c-258 S (D.Utah); *Rhodes v. Consumer Buyline, Inc.*, 868 F.Supp. 368 (D.Mass. 1993); and *Jacobs v. Herbalife International, Inc.*, No. 2:02-cv-01431 (C.D.Cal.).

I have also served *pro bono* as a consultant or counsel to the operators of non-profit consumer information web sites such as www.pyramidschemealert.org, www.mlmsurvivor.com, www.mlm-thetruth.com, www.quackwatch.com,

www.merchantsofdeception.com and www.rickcross.com.

I am not writing this comment on behalf of any client, nor am I receiving any compensation in connection with this matter.

II. INTRODUCTION AND SUMMARY OF COMMENTS

While the proposed rule is designed to address deception and unfairness in a variety of business opportunities, my comments are intended specifically to address the impact of the proposed rule on Multi-Level Marketing (MLM) schemes. MLM, sometimes referred to as “network marketing,” is a method of distribution in which distributors can theoretically make money both by retailing products or services and also by recruiting new participants into the scheme.¹²

Over the past fourteen years I have interviewed or deposed hundreds of MLM distributors in dozens of different systems and corresponded with hundreds more. I have consulted with dozens of MLM industry critics and proponents, and have studied the securities filings of publicly traded MLM firms. In my opinion, most MLM firms operate in a deceptive or fraudulent manner and, whether by design or in effect, cause substantial damage to consumers without any redeeming benefit. In every system with which I am familiar, the vast majority of distributors lose most or all of their investments, while a small fraction, generally less than 1%, make large sums of money.

I believe that the root of the problem lies in distributor compensation schemes which reward recruitment rather than retailing, and that while prophylactic conduct or disclosure regulation may limit or avoid some harm to consumers, the only real solution is to prohibit marketing structures which will inevitably become pyramid schemes.

There is currently no effective restraint on the MLM industry, which has become an increasingly potent cause of injury to consumers, not only in the United States but world-wide. While the Commission and some state regulators have been active in prosecuting fraudulent MLM schemes, they generally act only when consumer complaints concerning a particular scheme have reached a critical mass, by which time substantial damage has already been done.

¹² Many MLM firms refer to themselves as “direct selling” companies, probably to avoid the opprobrium attached to the term “multi-level marketing.” But direct selling does not necessarily entail a multi-level compensation scheme for recruiting new distributors. All MLM’s are direct sellers, but not all direct sellers are MLM’s.

I appreciate that the Commission is taking a realistic approach by limiting the scope of its regulation to pre-sale disclosure. At this time it is probably not politically feasible to preemptively regulate the terms of MLM compensation plans. As such, the Commission’s proposed rule is an important and crucial step in the effort to prevent further consumer injury caused by the inherently deceptive and unfair marketing practices of MLM firms and their high-level distributors. But disclosure will not prevent consumer injury caused by pyramid schemes. I would urge the Commission to continue its rule-making process to develop regulations prohibiting those forms of MLM plans which inevitably tend to function as pyramid schemes.

III. THREE CRUCIAL PROBLEMS WITH MULTI-LEVEL MARKETING

A. Deceptive Earnings Claims and the Failure to Disclose Business Expenses

The Commission has quite understandably focused on the problem of false earnings claims, which are endemic in the MLM industry.

MLM earnings claims are usually based on the experiences of high level distributors, who may in fact be earning large sums of money, without disclosing the vanishingly small chance that a new distributor will achieve similar success and without disclosing the average earnings of distributors. Sophisticated MLM firms rely on “testimonial” earnings claims which may be factually accurate - because the distributor actually earned the amount claimed - but are extremely deceptive when compared to the entire distributor force, most of who make little or nothing and drop out within a year after joining.

For instance, in or about 2004, Herbalife International, Inc., one of the largest MLM firms, displayed the following “testimonial” earnings claims on its official company web site:

Deborah and Hugh A.: “Deborah earns over \$10,000 a month, and she’s aiming for President’s Team;”

Emily C.: “When you look at Emily C. she looks like a typical happy, healthy 22-year-old woman. But how many 22 year olds are earning \$32,000 a month and heading up an international business? That’s exactly what Emily is doing and she’s not planning on stopping there, either.”

Jason F.: “Today, at age 22, Jason averages \$18,000 a month!”

Rox Anna C.: "We are earning on average \$20,000 a month."

Laura B.: "Laura currently earns \$10,000 a month and has the freedom she's always wanted."

Mandy and Bob E.: "Last month we made about \$9,000, while enjoying a much better quality of life."

Michael and Michelle B.: "Their monthly income currently totals approximately \$11,000."

Glenn W.: "On average, we earn approximately \$20,000 plus a month."

Ted F.: "I never would have imagined it, but now I make \$7,000 a month."

Nancy and Frank W.: "We earn approximately \$15,000 a month working the business part time."

The accompanying disclaimer that these claims were not representative was hardly sufficient to bring home the extremely low probability that new distributors could achieve such results. Further information and analysis concerning deceptive earnings claims in the MLM industry is being submitted to the Commission by Jon Taylor and Robert FitzPatrick of Pyramid Scheme Alert.

In addition, MLM earnings claims never disclose the expenses incurred by distributors to obtain the represented levels of earnings. The figures used in MLM earnings representations are generally the gross amount of bonuses and commissions paid by the company to the distributor based on the sales of the distributor's "downline." Usually, in fact, the only reference in MLM promotional materials to expenses is the small cost of the initial startup package. There is no disclosure of the types and amounts of expenses distributors actually incur, including the purchase of promotional materials, mailing lists, postage, telephone, and travel and attendance at promotional meetings. Interestingly, there is also never any disclosure of the "retail profits" earned by the distributor. Undoubtedly this is because the percentage of a top earner's income generated by retailing products is insignificant. Evidence that the expenses incurred by distributors are substantial is set forth below in section IV regarding the 'Newest Way to Wealth,' as well as in the Comments submitted by Jon Taylor and Robert Fitzpatrick.

Finally, as discussed in more detail in the section III.B. below, MLM earnings claims do not reveal that high level distributors often have

opportunities to make money which are not available to the rank and file of the organization. These include fees for speaking at distributor meetings and conventions, the sale of distributor-produced promotional materials and kickbacks from third parties who sell products and services to a distributor's downline, including telephone conferencing services, credit card service providers, mailing list vendors and the like.

B. The Role of High Level Distributors - the "Tools Business"

In all MLM schemes the role of the high level distributor is crucial. High level distributors recruit and motivate their "downline" distributors to recruit more participants. They are featured speakers at company meetings and conventions, and their success is portrayed as something achievable by the ordinary person by dint of a little time and effort. One large MLM firm candidly describes the crucial function of its high level distributors as follows:

Supervisors contribute significantly to our sales and some key supervisors who have attained the highest levels within our distributor network are responsible for generating a substantial portion of our sales and for recruiting a substantial number of our distributors. . . .

Members of the President's Team work closely with us to develop and implement new initiatives and strategies for increasing sales and distributor productivity throughout our entire distributor organization. The President's Team members have under certain conditions the opportunity to participate in the President's Team Bonus, which for 2000 consisted of a total available awards package of one percent of our 2000 total product retail sales, or approximately \$16.8 million. The distribution of the President's Team Bonus is based in part upon each President's Team member's participation in corporate-sponsored training and motivational events. In this manner, we attempt to involve our most senior distributors in our sales, training, motivation and strategic planning efforts. In addition to these programs, we periodically offer a variety of special promotions related to particular products or sales periods, involving special cash bonuses, vacations and other awards.

Herbalife International, Inc., Form 10-K for the year ended December 31, 2000. Most large MLM firms would describe the importance of their high level distributors in a similar fashion.

In recent years there has been a growing phenomenon in which high level distributors produce and sell their own marketing systems and materials to other distributors in the same system. These systems are referred to in this comment as “lead generation systems,” but are also known as “the tool business,” “business support materials,” “motivational organizations” or “professional development programs.” The role of such systems in Amway/Quixtar is particularly well documented. See Carter, Ruth, Amway Motivational Organizations: Beyond the Smoke and Mirrors (Backstreet Publishing, 1999); www.mlmsurvivor.com; and www.merchantsofdeception.com. See also Report of Professor G. Robert Blakey (copy submitted herewith as Exhibit A; the “Blakey Report”).¹³

In the Amway system, at least, some high level distributors earn significant portions of their income from selling motivational “tools” to lower level distributors. “The income from the tool business of the major uplines reportedly far eclipses their income from the Amway plan.” Blakey Report at p. 16. There is no disclosure of this feature of the MLM business to prospective distributors.

MLM firms permit lead generation systems to operate alongside the primary MLM business for several reasons. The sale of lead generation systems enables high level distributors to supplement their income, and thereby provides an additional incentive for them to remain with the MLM firm. Moreover, high level distributors whose downlines constitute a large portion of a MLM firm’s business have substantial influence and “clout,” based in part on the implicit threat that if the distributors terminated their association with the company, it would have a material adverse effect on the company’s sales. “[L]arge distributors such as Yager could simply take his downline out of Amway, with potentially devastating results to DeVos and Van Andel.” Blakey Report at p. 16. Finally, the use of lead generation systems permits high level distributors to use more aggressive promotional materials and methods than the official company materials, which benefits the MLM firm by increasing artificial demand for their products while incidentally providing the MLM firm with a plausible defense (i.e., the materials were developed by over-zealous distributors without company authorization) in the event of regulatory problems with the distributor-generated promotional materials.

¹³ The Blakey Report, drafted by an acknowledged expert on federal and state “RICO” (Racketeer Influenced and Corrupt Organizations) statutes, was originally submitted in litigation between Amway and Procter & Gamble. It is now widely available on the Internet. See, e.g. http://www.cs.cmu.edu/~dst/Amway/blakey_report.pdf (visited 7/11/06).

C. Compensation Plans That Reward Recruitment and Discourage Retailing

The fundamental problem with MLM is that the typical distributor compensation plan provides economic incentives which reward recruitment and discourage retailing. In every MLM system the income of high level distributors is almost entirely derived from bonuses and commissions paid based on the purchases of their downline distributors. On the other hand, MLM products and services typically carry suggested retail prices which far exceed similar products and services available through traditional venues. I respectfully refer to the comment to the Proposed Rule submitted by Bruce Craig, former Assistant Attorney General for the State of Wisconsin, in which Mr. Craig makes a compelling case that the Commission should prohibit MLM compensation plans which operate in effect as pyramid schemes.

In most systems, there are ostensibly no minimum purchase requirements for the lowest level of the distributor chain. However, there are almost always minimum purchase requirements for higher level distributors to qualify to receive bonuses and commissions based on purchases by their downline distributors. These minimum requirements create an artificial market for the MLM firm’s products and services, as distributors are exhorted to meet their qualifying purchase amounts.

One simple method for reducing the damage caused by MLM systems would be to prohibit minimum purchase requirements at any level. In conventional distribution or franchise systems, the distributorship or franchise includes a territory or market with some degree of exclusivity. With such systems, the imposition of minimum purchase requirements is not unfair, since the franchisee or distributor has some degree of protection from competition by other franchisees or distributors in the same system and therefore has a reasonable opportunity to meet the required level of purchases or sales.¹⁴ With most MLM systems, however, there are

¹⁴ Many franchise and distribution systems have no express minimum sales requirements, although there are generally other performance standards which ultimately have a similar effect. Even so, most franchise and distribution systems have some degree of market protection. This may range from expressly defined exclusive sales territories to more elastic concepts. In some large franchise systems, for example McDonald’s and Burger King, there are no expressly defined territories assigned to each franchise. In both of those systems, however, the franchisor has developed sophisticated economic models for predicting the impact of proposed new stores upon existing stores.

never any protected territories or markets and there is no limit on the number of distributorships would may be granted in a given market. In fact, distributors are urged to recruit new distributors, all of whom are potential competitors in the market for selling the MLM firm's goods or services. When the number of potential distributors in a given market is unlimited, there is no functional justification for minimum purchase requirements of any kind.

IV. THE 'NEWEST WAY TO WEALTH' EXPERIENCE

A useful case study that demonstrates many of the problems identified above involves a defunct lead generation system developed by several Herbalife distributors called "The Newest Way to Wealth" (NWTW). NWTW was the subject of a class action lawsuit in the U.S. District Court for the Central District of California, *Jacobs v. Herbalife International, Inc.*, No. CV-02-01431 SJO. The NWTW system was designed to assist Herbalife distributors to recruit more distributors, through the use of a series of promotional mailings which were produced and sold by top level Herbalife distributors to their respective downlines, along with carefully scripted presentations which accompanied each mailing. The system violated Herbalife's own distributor rules and regulations against making unsubstantiated earnings claims and was terminated by Herbalife several weeks after the lawsuit was filed, although there was evidence that some Herbalife officers knew of the existence of NWTW and tacitly - at least - condoned it.

The NWTW promotional materials made numerous representations concerning the "incredible" incomes which participants could achieve if they "bought in" at the Herbalife Plan's "Supervisor" level and followed the NWTW System, including but not limited to the following:

- a. "The Second Package Video will show you how so many others are making incredible incomes with this opportunity. Herbalife has created more millionaires than any other company in the history! Currently, Herbalife has over 500 people on its prestigious President's Team who are earning between \$200,000 per year and \$5,000,000 per year! (Yes, you read the amount correctly - \$5 Million Per Year). In addition, there are thousands other [sic] people earning 6-figure income of \$100,000

per year or more. These people come from various backgrounds and ethnicity from welfare moms and 80-year-old grandmothers to teenagers and young adults between the ages of 17 and 19."

- b. "Several of these people reached the \$100,000 per year income level within 1 year by using our incredible mail order and Internet marketing program."
- c. "Your income at the supervisor level is practically UNLIMITED."
- d. "The supervisor position is undoubtedly the most advantageous and lucrative position to start your business, however, if you are not able to start at this level, please consult with your mentor to help you work your way to this level as quickly as possible."
- e. "distributors earn 30-50% more than almost any other company's distributors assuming the same sales volume. In fact, the company's compensation plan returns 73% OF THE TOTAL NET SALES to its distributors. That means that out of the \$1.8 Billion in sales in 1998, \$1.3 Billion was paid out to us, the distributors! That translates into incredible earning power for the individual distributor."
- f. Numerous "testimonial" earnings claims including "Larry & SK Clark, TX: In their first 60 days earned \$2,500"; "John & Leslee Beall, IN: By my 11th month in business I was earning over \$10,000 per month ... still part-time"; "TJ Juneja, DC: Made over \$7,000 per month within 7 months of starting with this program and quit his full time job as a CPA"; "Steve & Debbie Combs, CA: Less than five years ago our financial situation was a disaster. Thanks to this business opportunity we now have financial freedom and a monthly income of more than \$28,000"; "Leah Graham, WA: \$30,000 check last month"; and "Bret & Amber Bartholomew, NV: February's check over *\$60,000 just nine months using mail order!"

After several years of litigation, the Court approved a classwide settlement in 2004. The class was comprised of Herbalife distributors who had reached the "Supervisor" level - meaning that they had purchased at least \$4000 worth of Herbalife products in one month or at least \$2500 worth of Herbalife products in each of two consecutive months - and who had purchased any NWTW promotional

If these studies predict an impact on an existing store above a given threshold, say 10%, the new store will either not be built or the existing operator will be given the option to purchase it.

materials between February 15, 1998 and May 2, 2003. For “Former Supervisors” (persons who had either formally terminated their distributorships or had not been active for one year) the settlement established both a “settlement fund” which called for class members to submit claim forms with documentation detailing their economic losses from operating their Herbalife distributorships, as well as a “refund pool” by which they could claim the amount of their purchases of NWTW promotional materials. The claims were reviewed and evaluated by a professional claims administrator, whose report¹⁵ revealed the following:

- * The parties identified 8,772 potential class members. Notice of the settlement and claim form were mailed to each of these persons, and notice was also published in *USA Today*.
- * There were 7,779 class members who were potentially identified as Former Supervisors. These persons - comprising approximately 89% of the class - were entitled to make claims for economic losses.
- * Of these, 2,481 or about 32%, submitted eligible claims.
- * The aggregate economic losses of eligible claimants totaled \$19,731,186, indicating an average loss of \$7,953. Several individuals claimed - and proved to the satisfaction of the claims administrator - losses in excess of \$100,000.

The NWTW experience provides compelling evidence in favor of the Commission’s proposed rule, as well as more proactive regulation of MLM business opportunities. If adequate disclosures had been made to participants in NWTW at least some of these losses could have been avoided. Proponents of the MLM industry generally concede that there is a high rate of attrition among MLM distributors but they assert that losses are minimal because the costs to start and operate an MLM distributorship are so low. The NWTW data refute this dogma.

MLM industry proponents can be expected to argue that the NWTW claims data is not statistically representative of the industry. They may assert that the NWTW system violated industry norms and/or that the claimants are a self-selected group and not representative of the average MLM distributor. Two points can be made in rebuttal: First, the NWTW system operated without sanction for over five years

¹⁵ See Declaration of Michael Rosenbaum in Support for an Order Authorizing Distribution of Net Settlement Fund, relevant portions of which are submitted herewith as Exhibit B.

in one of the largest MLM systems in the world. Second, if the MLM industry truly wants more accurate statistics, it is within their power to collect such statistics. The fact that they have not done so suggests that they know they will be uncomfortable with the inferences which may be drawn from the information they collect.

I would urge the Commission to request the largest MLM systems to provide lists of current and former distributors for the purpose of conducting a survey of actual earnings experience.

V. INDUSTRY REACTION TO THE NPR

The Commission can anticipate a vigorous, well-funded opposition to the Proposed Rule. One MLM advocate outlined a multi-pronged attack, including not only filing a formal opposition via the Commission’s rule-making procedures, but utilizing personal contacts with Commission staff members, lobbying “key members” of Congress to delay or defang the Commission, drafting legislation to neutralize the impact of any Rule that the Commission ultimately adopts, funding press and media campaigns against the Proposed Rule, and organizing grassroots initiatives by distributors.¹⁶

A large portion of the negative responses already received by the Commission as of the date of this Comment are obviously the result of several such initiatives which -- far from being “grassroots” -- are obviously being funded and directed by large MLM firms, including several members of the Direct Selling Association (DSA). Given that the attrition rates among MLM distributors frequently approach 100% or higher per annum, it would interesting to determine how many of these respondents will still be associated with their respective companies a year from now. It would also be interesting to learn what these respondents are actually earning today. It is a sadly frequent phenomenon of MLM that participants who are caught up in the evangelical excitement of “the business” find it difficult to admit to themselves that the anticipated financial rewards have not come to pass.

VI. RESPONSES TO THE COMMISSION’S QUESTIONS ON SPECIFIC PROPOSALS

Definitions

1. Definitions of “business opportunity” and “new business”

¹⁶ See FTC Proposed Business Opportunity Rule Analysis by Jeffrey Babener, <http://www.mllegal.com/FTC%20Business%20Opportunity%20Rule/FTCProposed.html> (visited 7/1/2006).

The Commission requested comments concerning whether the definition of “business opportunity” in § 437.1(d) should be limited to solicitations to enter into a “new business,” with “new business” defined in § 437.1(k) as “a business in which the prospective purchaser is not currently engaged, or a new type or line of business.” The purpose of this part of the definition is to distinguish sales of business opportunities from ordinary sales of goods and services.

The Commission’s intent is to include a variety of different types of business opportunities within the scope of the Proposed Rule, including vending machine and rack display sales, work-at-home schemes and pyramid schemes. While it might be easier to design a regulation for each type of opportunity, the continuous development of new schemes and the creativity of business opportunity sellers would quickly have rendered some regulations irrelevant and required new regulations for new types of opportunities. Given the Commission’s goals, the proposed definition of “business opportunity” is appropriate and necessary. I propose that the definition of “new business” be modified so that it would read “a business in which either the prospective purchaser is not engaged, or which involves the sale of a new type or line of products or services in which the prospective purchaser is not engaged business.” The modification is necessary in order to eliminate potential ambiguity in certain recurring situations in the MLM industry.

For instance, a distributor in one MLM plan may recruit his or her downline distributors into another MLM. This may occur in a number of different contexts, including when the original MLM plan goes out of business, when the distributor terminates their involvement in the original MLM, when the original MLM terminates the distributorship of the distributor, or when the distributor intends to go into a new MLM while maintaining his or her distributorship with the new MLM. In each case, the solicited distributors may be said to be “currently engaged” in the business of recruiting distributors and selling a variety of products. Distributors who are solicited in such circumstances should be protected by the Rule, and the modified definitions will eliminate any ambiguity as to whether they are covered.

The Rule should also cover “serial” business opportunity purchasers, sometimes known as “MLM junkies.” The modified definition of “new business” makes clear that such a distributor is entitled to the protections of the Rule with each new business opportunity they purchase even though it may be similar to business opportunities in which they are already engaged.

Finally, faced with actual or perceived market saturation, MLM firms develop “new” business

opportunities and solicit their existing distributors to sell them. For instance, Nu Skin, a seller of personal care products, developed “Interior Design Nutritionals” and “Pharmanex”, separate MLM business opportunities involving the sale of vitamins and nutritional products, and “Big Planet,” a separate MLM business opportunity involving the sale of web site development tools. NSA, a multi-level marketer of home water filters, created the “Juice Plus” marketing network. In a somewhat different manner, Amway developed the “Quixtar” business opportunity, which is sold in North America while the Amway business opportunity is sold worldwide. Distributors who purchase such “new” opportunities should be entitled to the disclosures mandated by the Rule.

2. Definition of “business opportunity” involving “business assistance” or “earnings claims”

The Commission requested comments as to whether the definition of “business opportunity” needed to be qualified by including only opportunities which promise “business assistance” or which make “earnings claims.” Every MLM opportunity involves both promises of assistance and earnings claims.¹⁷ However, as the Commission has recognized with respect to the Franchise Rule, it is very likely that business opportunity sellers will attempt to structure or characterize their offerings in a manner designed to circumvent the application of the Proposed Rule. Phrasing the business assistance and earnings claims elements in the disjunctive, as in the Proposed Rule, will frustrate efforts to evade compliance.

3. Definition of “business opportunity” requiring consideration

The Commission requested comments concerning whether there should be a minimum payment threshold for a “business opportunity.” The Proposed Rule does not contain a minimum payment threshold. The undersigned concurs most emphatically with the Commission that there should

¹⁷ See *Meadow Fresh Farms, Inc. v. Sandstrom*, Bus.Franch.Guide [CCH] ¶ 8064 (N.D. 1983) (finding “marketing plan” element of franchise under North Dakota statute met where multilevel marketer of dry milk “alternate products” provided marketing plan with following elements: (1) detailed compensation and bonus structure, (2) centralized bookkeeping, (3) prescribed scheme for advancement through various levels of the program, (4) reservation of right to approve all promotional materials, (5) prohibition on repackaging of products, (6) assistance in conducting “opportunity meetings”, (7) suggested retail prices, and (8) comprehensive advertising and promotional program).

be no minimum threshold because, as the Commission states, “fraudulent business opportunity sellers will price their opportunities at an amount just under the threshold in order to avoid compliance.”

Most MLM business opportunities involve a nominal initial payment - well under the \$500 threshold which might invoke application of the Franchise Rule - which typically covers the cost of an introductory package, including promotional brochures, a distributor agreement, operating manual and sample products. MLM sellers frequently tout the low cost of this package in comparison to the relatively high cost for purchasing a traditional franchise. The true cost of the opportunity, however, does not become apparent until after the initial plunge. As with the ‘Newest Way to Wealth’ system discussed above, prospective distributors are typically told that the ‘real money’ is made by participants who advance to the next level of the plan, by purchasing a given amount of inventory. In addition, as discussed above, in many MLM companies, high level distributors are promoting ‘lead generation systems’ which require additional payments for promotional materials, mailing lists and support services. These payments can quickly mount.

4. Definition of “business assistance”

The Commission requested comments concerning whether the examples of business assistance set forth in § 437.1(c) are warranted. MLM opportunities typically promise training and support for distributors, which is covered under subsection (v), and administering the distributor compensation plan, which is covered under subsection (iv). These provisions are reasonable and necessary to accomplish the purposes of the Proposed Rule.

5. Definition of “business assistance” as including administering compensation plans

The Commission states that subsection (iv) of § 437.1(c) is intended to capture pyramid marketing programs that promise to track commissions based on the participant’s purchases and recruitment of other distributors. This type of promise is universal in the MLM industry, and is reasonable and necessary to accomplish the purposes of the Proposed Rule. The reference to recruitment of other distributors is sufficient to preclude unintended coverage of traditional types of commercial distribution arrangements.

6. Definition of “new business”

The definition of “new business” in the Proposed Rule should be modified as set forth in Comment 1 above.

7. Timing of Disclosures

The Commission requested comment concerning the requirement in § 437.2 that the disclosure document be provided at least seven calendar days before the purchaser signs a contract or pays any consideration in connection with the opportunity. This “cooling-off” period is analogous to a similar requirement in the Franchise Rule.

I recommend that not only should there be a cooling-off period for the initial purchase of business opportunities, but that existing distributors should be provided with updated disclosures on a quarterly basis.

The cooling-off provision recognizes one of the realities of distributor recruitment in the MLM industry. MLM promoters typically attempt to create an atmosphere of mystery and excitement concerning the new opportunity. Prospects are often invited to an “opportunity meeting” without being told the name of the company sponsoring the opportunity. Promotional events are designed to induce the prospect to “willingly suspend disbelief” when making the decision to join the scheme. A seven-day cooling off period is a reasonable requirement to permit the prospect to carefully consider the costs and risks of the proposed opportunity.

Industry opposition to this provision will be vigorous. The point will be made that the seven-day waiting period will be difficult or impossible to enforce in MLM systems because recruitment is done by distributors over whom the sponsoring company has limited control. MLM recruiters will undoubtedly develop methods to “game the system” to avoid the effect of this provision, with the tacit acceptance of the MLM firm. Nonetheless, the benefits of a cooling-off period far exceed the costs.

In addition, quarterly disclosures for existing distributors would impose minimal burdens on MLM Sellers while providing distributors the opportunity to assess their own performance in light of updated disclosures. It should be noted that, as discussed in more detail above, the typical MLM opportunity is presented as a involving limited risk because the initial “investment” is nominal. Distributors may participate in an MLM system for several months before they realize the actual costs incurred in running the “business” exceed their gross receipts. Imposing a seven-day (or shorter) waiting period will not avoid such losses. For this reason, I recommend that business opportunity sellers be required to provide the updated disclosures mandated by the Proposed Rule to existing distributors as well as prospective distributors. This will provide the distributor with important information relevant to his or her decision as to whether to continue investing time and money in their business. Since business opportunity sellers will already have the obligation to prepare updated disclosures on a quarterly basis, there would be little

burden in requiring them to provide the updated disclosures to their existing distributors.

8. Liability limited to “Seller”

The Commission requested comments concerning whether liability for failure to provide the disclosure document should be limited to the “seller,” as provided in § 437.3. The Proposed Rule defines “seller” as “a person who offers for sale or sells a business opportunity.” In the typical MLM sales situation, the business opportunity is “offered” for sale by an existing distributor, but the opportunity is “sold” by the MLM company. In its Request for Comments number 8, the Commission seems to have assumed that the language “offers for sale” excludes brokers or “other individuals or entities involved in a business opportunity sale.” It would exclude, for instance, high level distributors who are frequently involved in the sales of MLM distributorships several levels below them in their “downlines.” In light of the phenomenon of distributor-produced promotional materials discussed above, I recommend that liability be extended to distributors who produce or sell their own promotional materials.

9. Disclosure Document - Boilerplate Disclosures

10. Disclosure Document – Presentation

11. Disclosure Document - Clarity

The boilerplate disclosures required by the Proposed Rule are necessary and appropriate to alert prospective purchasers about the potential risks. The presentation of the Disclosure Document is direct and to the point.

12. Identification of Sellers

It is essential that prospective business opportunity purchasers know about the previous business opportunities offered by the Seller’s officers, directors, sales managers and persons performing similar functions, including high level distributors who produce and sell their own promotional materials. Such persons often have a history of involvement with other, failed business opportunity schemes.

13. Persons Required to Disclose Litigation History

The required disclosure of litigation history should include the Seller’s officers, directors, sales managers and persons performing similar functions, including high level distributors who produce and sell their own promotional materials.

14. Disclosure of Types of Litigation

The disclosure of litigation should include not only civil and criminal actions but also arbitrations, bankruptcies and breach of contract lawsuits by and against the Seller, its officers, directors, sales managers and persons performing similar functions, including high level distributors who produce and sell their own promotional materials. The requirement to include lawsuits brought by such persons is important because prospective distributors should know, for instance, if the Seller has seen fit to bring lawsuits against former distributors to enforce the terms of non-competition covenants or other terms of distributor agreements. Such disclosures may indicate potential problems with the business opportunity that are relevant to prospective purchasers.

15. Disclosure of Litigation History

The litigation history should include not only the caption, identification of parties, court, case number and filing date but also a brief summary of the disposition of the action, as suggested in the Commission’s Request for Comment number 15. Business opportunity purchasers are not likely to have access to legal counsel who could obtain or explain such information, so a mere listing of cases would be of limited utility. Moreover, business opportunity Sellers will likely want to identify instances where the final disposition of the case was in their favor. Requiring disclosure of the disposition of litigation would not materially add to the Seller’s burden.

16. Disclosure of Cancellation Policy and Attrition Rate

Section 437.3(a)(4) of the Proposed Rule requires the Seller to make disclosures concerning the terms and conditions of any refund or cancellation policy. Section 437.3(a)(5) requires disclosure of information concerning prior cancellation or refund requests.

Disclosure of the existence and terms of any cancellation or refund policy is essential. In particular, Sellers should be required to disclose whether the refund policy extends to items or services which are recommended to be purchased

Sellers should be required to state the numbers of cancellation or refund requests on a monthly or quarterly basis, as well as the number of new and existing distributors. Such information will enable the prospective purchaser to assess whether there is any trend of increasing or decreasing requests for cancellation or refunds, and also whether such requests constitute a large or small portion of new and existing participants. Sellers in the MLM industry generally acknowledge that there is a high rate of attrition amongst MLM distributors. Disclosure of the actual attrition rate is essential information for prospective distributors.

The Commission states, in its comment to Proposed Rule section 437.3(a)(5), that it believes that “it would be impracticable to mandate a drop-out rate disclosure.” This statement is not correct as to MLM firms, which, like business format franchises, maintain close, continuing contact with their distributors. MLM firms typically have sophisticated computer systems which track distributor purchases in order, among other things, to track and calculate commission and bonus payments. Providing information concerning the attrition of distributors, including refund and cancellation requests, would not be burdensome. Industry protestations to the contrary should be viewed with skepticism.

17. Disclosure of 10 Prior Purchasers

18. Disclosure of National List of Purchasers

19. Privacy Concerns of Distributors

20. Contact Information for Prior Purchasers

One of the fraudulent promotional techniques used by MLM firms is the use of “shills” - i.e., persons who have supposedly (or even actually) succeeded in the business by following the promoters’ plan. MLM recruitment meetings typically include the introduction of one or more highly successful distributors, who make express or implied claims about their income from the plan. Written promotional materials also typically include testimonial earnings claims as in the NWTW system described above. Section 437.3(a)(6) of the Proposed Rule is a creative response to the inherently deceptive use of earnings testimonials by requiring the Seller to provide either a list of the 10 prior purchasers nearest to the prospective purchaser, or a national list of prior purchasers, with contact information. MLM industry proponents will certainly attack this proposal as both unworkable and violative of the privacy rights of distributors.

As between the two alternatives, the requirement to provide a national list of distributors would be less burdensome on MLM Sellers than the 10 closest distributors, especially given the nature of the MLM recruitment process. All MLM firms must keep their list of distributors current in order to track orders and pay commissions. Such a list could certainly be sorted by geographic area, which would enable prospective purchasers to contact distributors near them. However, prospective purchasers should have the ability to contact distributors in other geographic areas. A given MLM system may be relatively new in one state, with the result that many participants on the contact list may have limited experience, while contacting distributors in areas where the company has been active for a longer period will yield a richer range of experience.

Any assertion by MLM firms that they are concerned about the privacy rights of their distributors should be viewed with extreme suspicion. In traditional distribution systems, no distributor has any interest in keeping his or her distributorship “secret.” All publicity is good publicity. The real concern of MLM proponents is that, due to the high attrition rates of most MLMs, many of the persons on the contact list will inevitably be failed distributors. Given the widespread use of testimonial earnings claims by successful distributors, the Commission’s proposal will provide crucial balance to the prospective MLM distributor.

MLM firms will also complain that the requirement to provide a national list of distributors will enable their competitors to contact and recruit their distributors. The Commission could prohibit such use by other business opportunity sellers. In addition, the disclosure of contact information could provide prospective distributors with the option of checking a box stating that they do not want to be contacted by other business opportunity Sellers, in a manner similar to the “Do Not Call Registry” maintained by the Commission and state regulators.

New business opportunity purchasers should not be given the option to opt-out of disclosure of their contact information to prospective purchasers. The MLM recruitment process is very susceptible to the type of manipulation anticipated by the Commission, which would result in the list being limited to shills. However, business opportunity purchasers who purchased prior to the adoption of the Proposed Rule - including not only existing distributors but terminated distributors - should probably be given the right to opt-out of disclosure.

21. Other Disclosures

There is a need for other types of disclosures by business opportunity Sellers. As discussed above, the actual costs of operating a MLM distributorship are significant. The MLM Seller should be required to list the types of business expenses incurred by distributors, with approximate ranges based on surveys of distributors. There should also be disclosure of any arrangements under which the Seller or high level distributors receive consideration from third parties who provide products or services to distributors. This is addressed in part in section 437.5(r)(1) of the Proposed Rule, but should be expanded expressly to cover third parties.

22. Earnings Claims

23. Use of Industry Information

I concur with the comments of Robert Fitzpatrick of Pyramid Scheme Alert and Dr. Jon

Taylor concerning the content and depiction of earnings claims disclosures.

24. Prohibited Acts or Practices

In addition to the matters listed in section 437.5 of the Proposed rule, MLM Sellers should be prohibited from limiting any private right of action a purchaser may have arising from conduct which may violate the Proposed Rule. There is no private right of action for violation of section 5 of the FTC Act, although most states provide a private right of action under their own "little FTC" statutes. Since the Commission cannot possibly take enforcement actions for every violation of the rule, which may involve thousands of distributors in hundreds of different MLM systems, preserving private rights of action is essential to accomplish the purposes of the Proposed Rule. Sellers should be prohibited from including mandatory arbitration clauses, bans on class actions, choice of forum or venue clauses, or other limitations of remedies, in their distributor agreements.

25. Liability of Third Parties

In light of the phenomenon of distributor-produced promotional materials (see sections III.B. and IV above), liability for violation of the Proposed Rule should be extended to high level distributors who produce and/or sell their own promotional materials. MLM Sellers should also be liable for the conduct of such high level distributors. This requirement will motivate Sellers to police the actions of their own distributors, which is essential in order to accomplish the purposes of the Proposed Rule.

26. Interplay of State and Federal Regulation

The Commission's approach is appropriate in light of the fact that very few states have disclosure statements applicable to all of the various types of business opportunities covered by the Proposed Rule.

27. Record Retention


The Proposed Rule requires MLM Sellers to retain records for a period of only three years. A longer period would be essential, since some violations may not come to light within three years. Since most companies retain their tax records for at least seven years, a record retention requirement of seven years would not be too burdensome.

The Commission queried concerning record keeping of cancellation requests. Most such requests already generate a written record (because of the necessity of writing a refund check to the distributor) and it would not be burdensome to require Sellers to keep and maintain such records.

VII. REQUEST FOR HEARING

The undersigned requests a hearing pursuant to Section 18(c) of the Federal Trade Commission Act and Section F. of the April 12, 2006 Notice of Proposed Rulemaking. I would be prepared to testify as to the matters set forth above.

Respectfully submitted,



Douglas M. Brooks

Another comment submitted by Douglas Brooks is labeled Exhibit A, which is the fascinating report by Professor Robert Blakely of Notre Dame Law School, comparing Amway to organized crime.

As an expert in organized crime, Professor Blakely found some striking similarities between the way that organized crime families operate and the way the Amway business is conducted. It is well worth reading to better understand why a rule regulating MLM programs like Amway is essential. To access this report, go to – www.ftc.gov/os/comments/businessopprule/522418-10579.pdf

Important testimony and research from international consumer health advocate and sponsor of MLM Watch web site Stephen Barrett, M.D. – who also supports the research of Taylor and FitzPatrick

Dr. Stephen Barrett is the sponsor of Quackwatch and several other health-related websites which offers guides and warnings to help consumers avoid health scams of all types. He found that misrepresentations regarding health claims were common in MLM, so he has also sponsored MLMwatch.com, which reports on both the health and financial fraud of numerous MLM companies.

(Because of its relevance, it is included below.)

Comment Number: 522418-10018
Received: 7/15/2006 4:03:19 PM
Organization: Quackwatch
Commenter: Stephen Barrett
State: PA
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
 No Attachments

Comments: See letter below.

STEPHEN BARRETT, M.D., CONSUMER ADVOCATE
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 July 15, 2006

Federal Trade Commission
 Office of the Secretary, Room H-135 (Annex W)
 600 Pennsylvania Avenue, NW
 Washington, DC 20580.
 Re: Business Opportunity Rule, Matter No. R511993

Dear Sirs:

Enactment of an effective Business Opportunity Rule would help millions of people and would be one of the most significant actions in the FTC's history.

Work-at-home plans, party plans, and multilevel marketing (MLMs) have some characteristics that are common and other that are not. Thought should be given to whether each part of the rule is applicable to all types of business opportunities and whether sections should be added that apply to only one or a few types of opportunities. The comments below are meant to apply only to MLMs.

Since 1980, I have investigated more than 150 MLM companies offering health-related products and found that none gave a realistic picture of probable income. I recommend the following:

1. No exemption or threshold for earnings claims

Because the promise of high income is the cornerstone of MLM recruiting, all MLMs should be required to comply with the earnings-claim disclosure rules and no MLM company should be permitted to make "no earnings claims." For the same reason, the applicable threshold for coverage of the rule should be zero. Even a \$100 threshold would exempt MLM companies who solicit millions of people every year.

2. Minimum 3-day cooling off period

Prospective distributors should have an opportunity to think about any proposal while not in the presence of the seller. A waiting period will permit consultation with friends, family, or other advisers. The bottom line is to reduce the probability of impulse purchases. I believe that 3 business days is sufficient for this purpose and that a longer period might adversely impact legitimate business opportunity sellers.

3. Meaningful disclosure

Great care should be taken in constructing the details of the rule so that MLM disclosures are clear, meaningful, and conspicuous. The FTC should develop a list of specific questions for companies to answer. This can ensure that the significant data are disclosed and that all companies have a level playing field. As part of the development process, the FTC could ask the Direct Sellers Association to suggest parameters.

4. Suggested disclosure parameters

All MLMs should be required to disclose the following in a clear and understandable format (such as easily interpreted percentile columns), and separate from all other materials furnished to prospective distributors:

- a. Total company revenue from US-based distributors
- b. The total number of US-based distributors involved in the company for at least three years or since the company's founding if the company is less than three years old

c. The number of terminations and the number of new recruits for each of the past three years in the United States.

d. The net increase (new ones less those who drop out) in the number of distributors in the various ranks of the upline as a percent of all who have been distributors for three years

e. The percentile incomes of all who have signed up for a distributorship in the United States. (e.g., "the top 10% averaged \$___, the next 10% averaged \$___, etc.") Percentile income is far more meaningful than "average" income (total company income divided by the number of distributors) because including the highest earners would make the "average" higher than most distributors make. Income data should not be limited to those a company would describe as "active distributors."

f. Income should be defined as money the company pays to distributors minus all money distributors pay to the company. However, it should be disclosed that this does not take into account distributor expenses such as advertising, exhibiting, travel, purchase of sales aids from non-company sources, or other overhead.

g. The percentage of US-based distributor income derived from sales outside of the United States

5. Disclosure Must Be Conspicuous

To ensure that the rules are conspicuous and to help the FTC monitor compliance, copies of all disclosures should be given to each distributor and posted on each company Web site. In addition, all distributor Web sites that solicit new distributors should either post the earnings statement or link to it on the company Web site.

To facilitate comparison and further consumer education, the FTC should maintain a site that contains the final Business Opportunity Rule, the individual company disclosures, and other information that would assist prospective investors.

I would welcome an opportunity to testify.

Sincerely yours

Stephen Barrett, M.D.

A massive volley of questionable submissions overwhelmed FTC staff. 17,000 MLM participants (out of millions) submitted comments as instructed by their company or upline.

Comments of 17,000 persons, probably 99% of them MLM participants who have been encouraged by their sponsoring MLM to file a comment and were been given instructions or form letters spelling out what to say. We estimate that this appeal went out to at least 10-15 million MLM participants, so the 15,000 (17,000 less as many as 2,000 bogus or duplicate submissions) could represent close to 1 out of 1,000 who were contacted.

We learned from interviews in a telephone survey of those we could reach that most of those who did submit comments were not against including MLM in the Rule when it was presented to them honestly. But many were misled when told by their companies that the FTC wanted them to reveal personal financial information and identity information that could lead to cross-recruiting or identity theft, etc. We also found some who did not send the comments, so someone from the company had sent electronic submissions in their name. This was, in effect, electronic forgery. The results of the telephone survey follow the list of form letters below.

Approximately 12,000 of the 17,000 comments were electronic submissions and were organized alphabetically and posted on Public Comments section of the FTC web site, as seen below. Again, go to –

<http://www.ftc.gov/os/comments/businessopprule/index.shtm>, and scroll down to #178

178 FTC Matter No.: R511993 16 CFR Part 437 Notice of Proposed Rulemaking: Business Opportunity Rule

Public Comments

|A|B|C|D|E|F|G|H|I|J|K|L|M|N|O|P|Q|R|S|T|U|V|W|X|Y|Z|

Form Letters

NOTE: The “Form letters” referenced at the bottom were paper submissions following a generic form letter template, as explained on the following page.

Over 5,000 generic form letters were submitted. When accessed, each was followed with a list of other persons using the same generic form letter. When one studies them carefully, it becomes clear that the companies issuing the form letters often misrepresented the purpose of the Rule and the difficulty of complying by individuals.

(FTC) Note: Over 5,000 of the public comments that were filed in paper form with the Commission on this proceeding were variants of "form letters" - i.e., letters that are based on all or part of a generic form letter template. Accordingly, the FTC is posting only one representative public comment for each different form letter variety identified. The FTC has created this separate "Form Letter" index page to distinguish these form letter examples from other letters, so that members of the public can find them more easily on the site. Appended to each of these representative comments is a list of the names of additional commenters who submitted that particular variety of form letter. Please note that these appended lists are limited to paper submissions only; form letters submitted via electronic means are posted individually on the site, and can be found in the general alphabetical index by commenter name.

1. [Adorante, Nicholas](#) (6/19/2006) # 522418-70084
2. [Anonymous](#) (7/14/2006) # 522418-70649
3. [Bennett, Patricia](#) (6/7/2006) # 522418-70231
4. [Besemann, Sandra](#) (6/30/2006) # 522418-70222
5. [Blake, Sheryl L.](#) (7/10/2006) # 522418-70352
6. [Bradley, Scott](#) (7/14/2006) # 522418-70164
7. [Brown, Tom](#) (7/14/2006) # 522418-70653
8. [Cook, Margaret A.](#) (7/3/2006) # 522418-70599
9. [Danielewicz, Ron](#) (7/5/2006) # 522418-70709
10. [Davis, Don](#) (6/20/2006) # 522418-70131
11. [Dixon, Amy](#) (7/12/2006) # 522418-70246
12. [Dodson, Eugene V.](#) (7/5/2006) # 522418-70361
13. [Douglas, Marcia](#) (6/12/2006) # 522418-70122
14. [Douglas, Roland](#) (6/12/2006) # 522418-70068
15. [Evans, Simon J.](#) (6/15/2006) # 522418-70300
16. [Frischeisen, Hans](#) (6/19/2006) # 522418-70299
17. [Greenwalt, Françoise](#) (6/5/2006) # 522418-70655
18. [Hornbuckle, Keet](#) (6/7/2006) # 522418-70350
19. [Johnson, Tommy](#) (6/28/2006) # 522418-70567
20. [Kleist, Cynthia A.](#) (6/13/2006) # 522418-70066
21. [Long, John](#) (6/27/2006) # 522418-70337
22. [Macke, Alicia](#) (6/20/2006) # 522418-70675
23. [Mahoney, Francina](#) (6/26/2006) # 522418-70463
24. [Neddo, Shirley](#) (6/13/2006) # 522418-70576
25. [O'Brien, Ellen](#) (6/20/2006) # 522418-70301
26. [Perkins, Stephen](#) (7/10/2006) # 522418-70461
27. [Polites, Joan](#) (7/17/2006) # 522418-70688
28. [Porter, Jason](#) (7/10/2006) # 522418-70341
29. [Price, Violet](#) (6/19/2006) # 522418-70490
30. [Raines, Krista](#) (7/11/2006) # 522418-70618
31. [Rolls, Jean](#) (6/7/2006) # 522418-70064
32. [Roman, Jennifer](#) (6/22/2006) # 522418-70689
33. [Ruiz, Cynthia](#) (7/10/2006) # 522418-70368
34. [Ruiz, Elaine](#) (7/10/2006) # 522418-70364
35. [Tirado, Gisela](#) (7/10/2006) # 522418-70356

The results of a telephone survey of IPBOR commenters show the questionable validity of the conclusions drawn from the 17,000 pro-MLM comments

Consumer Awareness Institute survey conducted by Jon M. Taylor, MBA, Ph.D.

The FOIA office of the FTC refused to satisfy our request for specific address information on the 17,000 names of persons who filed comments regarding the Initial Proposed Business Opportunity Rule (IPBOR) in 2006.¹⁸ However, by doing a Yahoo People Search of unusual names, my ad hoc assistants were able to get over 300 hundred names with addresses and phone numbers. We were able to reach about 285 of them by telephone, with 275 usable responses.

The FOIA office finally sent 900 names with cities identified, for which we were more easily able to find the identifying information with the same search. However, they were for a narrow time period when the vast majority were from participants in one company – Shaklee. Out of 55 survey questionnaires mailed out in a written test survey, only four responded, and one of these reported that he had not written the comments and that he did not like the exemption. (Ten were returned as undeliverable to address.) So the response from this limited test mailing was so limited that I decided not to do a mailing to full 900 names.

A careful review of the results from the more productive telephone survey of 275 commenters produced interesting findings:

1. It appeared from our initial phone calls that more than half of the comments were filed fraudulently by the MLMs (MLM companies) or by upline leaders. However, it had been almost six years since the comments were filed, and many had a hard time remembering. When we called back and read the comments back to them, most remembered that they had written it or forwarded a form letter from the company, adding their names and a few comments at the end. So it now appears
2. Many of those whose comments were filed in their name without their permission were sent a survey which misrepresented the purpose of the Rule. For example, they may have been asked if they were willing to disclose the names of their downline (who could be “cross-recruited”), or personal financial information, etc. Then, apparently, their upline or company officials who sent the survey felt justified in filing comments in their name.
3. Most of the commenters had been with their MLMs for many years and seemed to be objecting to the Rule to protect their turf. For example, requirement for average income statistics were misrepresented as personal commissions from purchases by their downlines, etc. Almost all were still buying and selling the products, and most were still recruiting. The 95% of MLM participants who had dropped out (as is the case in most MLMs) were underrepresented in the samples’ i.e., few of them filed comments.
4. Some (long-term participants) were selling substantial amounts of products. Almost all claimed to be profiting, to be reporting profits on their taxes, and to be using their MLM activity for a tax write-off. However, contrary to the arguments filed with the FTC by DSA/MLM lobbyists, MLM was seldom their sole source of income. Only about 3% of our sample of commenters claimed that MLM was their sole source of income.

¹⁸ It is likely that few commenters supplied street addresses, since only the state was required in the online form for comments.

5. However, when asked about the ratio of money in (money received from the company) vs. money out (money paid to the company, including purchases of products and services), most balked or became defensive, saying, “That’s none of your business,” or “ I can’t divulge that,” etc. Or they admitted that they did not know. *Apparently they have been brainwashed into seeing their “pay-to-play” purchases of \$60/bottle fruit juice or \$100/month vitamins as a necessary personal expense, and not as a business expense for analytical purposes (except when filing their taxes). It appears that (with a few exceptions) even those who had been with the MLM for many years did not come out ahead financially from their participation in their MLM.*
6. *Almost all still saw their MLM as a “good income opportunity” – even those who lost money. This is cognitive dissonance personified.*
7. *Asked if they would have enrolled had they known that 99% of participants lost money – incredibly – most said “yes.” However, some qualified their response by saying “it takes effort, ”or “I know someone who is doing very well at it,” etc. This attitude is what I call a “lottery mentality” – the belief that even if the odds are stacked incredibly against them, they could be that one winner who is rewarded handsomely.*
8. *Approximately 55% of those we surveyed did not approve of the MLM exemption, feeling that disclosure of information about the company was a good thing. However, most did not approve of a 7-day waiting period – which was dropped from the final Rule anyway. And many suggested they would not support a rule requiring them to disclose any personal information – which we know was not requested in the IPBOR (beyond their name and state).*

FTC staff seek comments of former FTC Chairman-turned lobbyist Timothy Muris

Lois Greisman and other FTC staff requested the comment from Timothy Muris to help them craft a revised RULE to satisfy the DSA/MLM lobby – and in effect rebut those of us advocating on behalf of consumers. See the following page for a copy of the email which refers to the Muris comment This was obtained as part of the response to an FOIA request for documents from our group of consumer advocates.

His comments are too lengthy to include in full here, but my rebuttals of the key arguments put forth by Muris follow the staff request for the Muris letter. The full Muris comments can be obtained at the following web addresses on the FTC website. *It is interesting to see how much the set of arguments*

used by Muris were parroted by the BOR staff in the staff report to members of the Commission justifying the MLM exemption – which was not an easy task, since it is so nonsensical to anyone who is informed on the massive fraud perpetrated by MLM programs. See Chapters 2-10 of my book “Multi-level Marketing Unmasked.” Chapter 8 lists the many misrepresentations displayed in the MLM culture of deception upon which MLM depends. These MLM programs are by far the most prevalent and the most unfair and deceptive of “business opportunity” offerings – which are precisely what the FTC should be using its rulemaking authority to help prevent.

Initial Proposed BOR – July 17, 2006 –

www.ftc.gov/os/comments/businessopprule/522418-11929.pdf

Rebuttal September 29, 2006 –

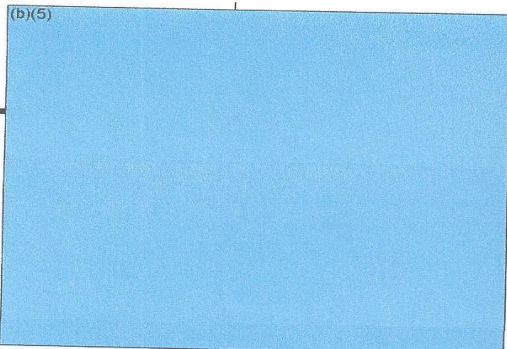
www.ftc.gov/os/comments/businessopprule/rebuttal/522418-13260.pdf

Revised BOR, May 27, 2008 –

www.ftc.gov/os/comments/bizoprevised/comments/535221-00056.pdf

Williams, Regina

From: Greisman, Lois C.
Sent: Thursday, July 20, 2006 2:52 PM
To: Williams, Regina
Subject: Fw: Muris Comment



For fed exp pls. L

-----Original Message-----

From: Toporoff, Steven <STOPOROFF@ftc.gov>
To: Hile, Allen W. <AHILE@ftc.gov>; Greisman, Lois C. <LGREISMAN@ftc.gov>; Hobbs, Karen S. <KHOBBS@ftc.gov>
Sent: Thu Jul 20 14:50:51 2006
Subject: Muris Comment



rs11993 - Primerica
Financial ...

I was able to find Muris' comment among the 13000k comments posted on commentworks. Attached is a copy. I also printed it out, in the event you want a hard copy.

Steven Toporoff
Federal Trade Commission
Room 288
600 Penn. Ave., NW
Washington, DC 20580
Phone: (202) 326-3135
Fax: (202) 326-3395

to
cc
cc
cc
cc
cc

False and misleading arguments put forth by former FTC Chairman-turned-lobbyist Timothy Muris about IPBOR – on behalf of Primerica Financial Services, Inc., and the MLM industry – debunked by Dr. Jon Taylor

NOTE: Since his key arguments are summarized in the items listed in the Table of Contents, I have debunked each of these one by one (plus the Executive Summary), with my comments highlighted in bold italics after each applicable Muris statement.

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9260 [Primerica Financial Services Inc.](#) (Muris, Tim) (7/17/2006) # 522418-11929

**FEDERAL TRADE COMMISSION Project No. R511993
COMMENT of PRIMERICA FINANCIAL SERVICES, INC.
on the NOTICE OF PROPOSED RULEMAKING
on the BUSINESS OPPORTUNITY RULER511993
FILED JULY 17, 2006**

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<i>[FALSE. All MLMs, dependent upon endless chain recruitment, assume infinite markets – which do not exist in the real world. They are therefore inherently flawed, unfair, and deceptive.]</i>	
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A. The Impact on Primerica and Its Agents Would Be Devastating.	14
<i>[MISLEADING. The purpose of the Rule is to protect consumers, not a flawed industry. If an unfair and deceptive practice suffers because of the Rule, that is not a bad outcome.]</i>	
B. The Burdens Imposed by the Proposed Rule Are Enormous, and Will Fall Disproportionately on Legitimate Businesses	15
<i>[FALSE. The notion that passing out a one-page disclosure form provided by the company is burdensome is ludicrous. When franchises are presented to prospects, the Franchise Disclosure Document can be hundreds of pages long. The second part of that statement is also absurd. Legitimate businesses can survive transparency, while scams may not.]</i>	
1. This Is Not a Simple One-Page Disclosure.	16
<i>[MISLEADING. Of course, it may not be so simple if a company must go to great lengths to distort its statistics so that prospects cannot get the information they need to protect themselves.]</i>	
2. The Waiting Period Is a Substantial Burden and Will Debilitate Primerica’s Recruiting Efforts.	16
<i>[MISLEADING. What does it say about a company if it cannot survive a “think-it-over” period of a few days?]</i>	
3. The Litigation Disclosure Is Extremely Burdensome and Highly Misleading, Particularly for Legitimate Businesses in the Financial Services Sector	18
<i>[MISLEADING. Prospects have every right to know if a company or its officers are or have been the subject of legal action or investigations.]</i>	
4. The Reference Disclosure Is Extremely Burdensome and Will Harm Privacy and Business Confidentiality Interests.	23
<i>[FALSE. Giving out names and telephone numbers is no more burdensome or harmful than listing one’s phone number and address in the telephone book – unless the company fears that the references will be less than complimentary of the program.]</i>	
5. Disclosure Related to Earnings Claims Would Not Distinguish Legitimate Businesses from Frauds.	26
<i>[MISLEADING. Identifying fraud is not the primary purpose of the Rule. However, if it was apparent from income disclosures that less than one in one thousand recruits make any profit, that is enough</i>	

to avoid what is certainly a bogus business opportunity. Whether or not it qualifies as intentional fraud could be a matter for the courts to decide.]

C. The Rule Would Crush Small, Independent Businesses.	27
[CORRECTION: The Rule could crush phony business opportunities – those that are dependent upon deception to survive.]	
D. The Rule Exceeds the FTC’s Rulemaking Authority, and Is the Equivalent of Placing an Entire Industry under a Consent Decree	30
[MISLEADING. The Rule should help the FTC to fulfill its mission – and authority – to protect against “unfair and deceptive practices in the marketplace. The latter half of the statement questions the appropriateness of a federal agency to issue any rules at all.]	
1. The Rule Exceeds the Commission’s Authority under the FTC Act. ...	30
[False. The Rule implements the Commission’s authority under the FTC Act.]	
2. The Rule Is an Arbitrary and Capricious Exercise of the Commission’s Authority.	31
[FALSE. The Rule is an application of the FTC’s charge to protect against “unfair and deceptive practices in the marketplace.” Shame on Muris and Beales – who worked for the FTC supposedly to provide consumer protection under Section 5 – to even suggest this.]	
3. The Factual Predicates for the Rule Are Not Supported by Substantial Evidence.....	34
[FALSE. The evidence is substantial, except for Muris, Beales, and FTC staff who are unwilling (or unable) to examine and evaluate the evidence presented to the FTC.]	
IV. THE COMMISSION SHOULD MODIFY THE PROPOSED RULE TO COVER ONLY THE FRAUDULENT TRANSACTIONS IT SEEKS TO REGULATE.....	35
[MISLEADING. To be effective, the Rule should cover all purported business opportunities.]	
A, The Rule Should Exclude Licensed Insurance Companies and Registered Broker-Dealers Because They Are Already Subject to Extensive Regulation.	35
[MISLEADING. Based on extensive research, apparently such regulation is insufficient to protect against “unfair and deceptive practices in the marketplace.”]	
1. Regulatory Qualification Requirements and Supervision by Regulators Make It Highly Unlikely That Insurance Companies and Registered Broker-Dealers Will Engage in Business Opportunity Fraud.....	35
[FALSE. But they do. One has only to look at A.L. Williams and other MLMs that have engaged in financial products to see the falsity of this claim.]	

2. As Applied to Insurance Companies, the Proposed Rule Runs Afoul of the McCarran-Ferguson Act.	36
<i>[MISLEADING. The McCarran-Ferguson Act partially exempts insurance companies from the federal anti-trust legislation that applies to most businesses. The issues addressed by BOR are not typically regulated by agencies that regulate insurance products.]</i>	
B. Exclude Legitimate Companies.	38
<i>[MISLEADING. To an informed analyst, highly leveraged and top-weighted programs like Primerica are no more legitimate than other recruitment-driven MLMs.]</i>	
C. Define Pyramids and Cover Only Pyramids.....	38
<i>[MISLEADING. An exclusive focus on pyramids was not the primary purpose of the Initial Proposed Rule.]</i>	
D. Retain the Existing Definition from the Franchise Rule That Covers Business Opportunities and Expand Based on Demonstrated Problems.	39
<i>[This could have been done, but (as discussed early in this report by Bruce Craig and Douglas Brooks – and in the FTC announcement itself), the FTC decided a separate rule was needed.]</i>	
E. Narrow the Consideration Provision.	40
<i>[MISLEADING. MLM compensation plans typically have a small signup fee, which is just a ruse to mislead regulators. The more substantive “pay-to-play” features of the plan come into play when the participant seeks higher levels of commission or rank advancement to where significant profits are possible. the MLMs that have been in business the longest are the most fraudulent. See Chapters 2 and 4 of my book <u>Multi-level Marketing Unmasked</u> (formerly <i>The Case against Multi-level Marketing – an Unfair and Deceptive Practice</i>).]</i>	
F. Exclude Companies That Have Been in Business for a Significant Number of Years, or That Post a Performance Bond.	41
<i>[MISLEADING. Some of the MLMs that have been in business the longest are the most fraudulent. See Chapters 2-7 of my book <u>Multi-level Marketing Unmasked</u></i>	
V. CONCLUSION AND REQUEST FOR HEARINGS	42

EXECUTIVE SUMMARY

The proposed Business Opportunity Rule (“Rule”) pursues the laudable goal of preventing fraud in the work-at-home, pyramid and vending machine marketplaces. But the Rule does not narrowly define and prohibit the specific practices in which the Commission has observed fraud. Nor is it limited to the types of business opportunities that have given rise to consumer complaints and Commission enforcement activity. Instead, the proposed Rule would broadly apply to legitimate and well-established financial services businesses, such as Primerica, as well as the large and growing U.S. direct selling industry—an industry that generates nearly \$30 billion in revenues annually, providing income for more than 13.6 million Americans. As a practical matter, the Commission’s goal of eliminating fraudulent work-at-home and pyramid schemes threatens legions of legitimate businesses that contribute greatly to the American economy and to the livelihoods of millions of middle-income Americans. The Commission should revise the Rule to narrow its scope and proposed remedies to address fraudulent practices related to work-at-home, pyramid marketing and vending machine schemes directly, while excluding legitimate businesses from its burdensome requirements.

[FALSE AND MISLEADING. Muris begins with a compliment for the original goal of the Rule, but then faults the FTC for not defining it the way promoters of MLMs like Primerica want it defined. Muris suggests that Primerica and the direct selling industry is legitimate and should be given a pass from the Rule. Anyone informed on the issues would challenge that. Rebranding MLM (or product-based pyramid schemes) as direct selling is part of the DSA strategy to give legitimacy to what is likely the most unfair and deceptive practice, if not the most successful con game in history – MLM. The vast majority of the 13.6 million Americans are victims of schemes that promise relief from financial hardship but actually cause losses to approximately 99.7% of participants – or 99.99% if you eliminate those at the top who are getting most of the commissions paid out by the company. Read all chapters of my book, documenting years of research on hundreds of MLMs – Multi-level Marketing Unmasked (formerly The Case against Multi-level Marketing – an Unfair and Deceptive Practice). Read especially Chapter 8 “MLM – a Litany of Misrepresentations,” which lists over 110 misrepresentations used in MLM recruitment campaigns. Apparently, FTC Chairman-turned lobbyist Timothy Muris has fallen into this pervasive culture of deception upon which MLM depends. In fact, in 18 years of dealing with this culture of deception, I seldom see a report with more fallacies and misleading statements per page. It is disturbing to realize that Timothy Muris was once Chairman of the FTC – supposedly the nation’s consumer watchdog.]

IPBOR REBUTTALS: Dr. Jon Taylor rebuts 17,000 comments (from 28 MLMs) – in effect, challenging one voice

Most IPBOR rebuttals were by Dr. Jon Taylor (CAI and PSA). His 28 rebuttals to MLM arguments constituted most of the rebuttal comments filed, as listed below. Following this list are the introductions for comments rebutting Quixtar, the Chamber of Commerce for the USA, and the DSA, with submission for rebuttal comments of DSA's comments as an example.

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Rebuttal Comments

American Council of Life Insurers (Tate, Lisa) (9/29/2006) #522418-13256
Barrett, Stephen (9/29/2006) #522418-13267
Boucher, Kelly (9/18/2006) #522418-13238
Brown, Cindy (8/22/2006) #522418-13204
Bryan, Joni (9/12/2006) #522418-13229
Clements, Len (9/27/2006) #522418-13244
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (8/7/2006) #522418-13112
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (8/7/2006) #522418-13113
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (8/8/2006) #522418-13115
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/21/2006) #522418-13241
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13249
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13250
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13251
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13252
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13254
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13257
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13259
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13262
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13263
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13264
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13265
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13266
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13268
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13269
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13270
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13271
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13272
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13273
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13274
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13275
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13276
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13277
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/29/2006) #522418-13278
Consumer Awareness Institute - and Pyramid Scheme Alert (Taylor, Jon) (9/30/2006) #522418-13279
Crosby, Michael (9/20/2006) #522418-13240
Direct Selling Association (Varney, Christine) (9/29/2006) #522418-13253
Drumheller, Sheri (9/8/2006) #522418-13225
Franklin, Carol (8/20/2006) #522418-13199
Friedman Kaplan Seiler & Adelman LLP (Neier, Hal) (9/28/2006) #522418-13246
Friedman Kaplan Seiler & Adelman LLP (Neier, Hal) (9/29/2006) #522418-13247
Herbalife International of America, Inc. (Chapman, Brett) (9/29/2006) #522418-13248
Johnson, Steven (8/7/2006) #522418-13110
Johnson, Steven (9/1/2006) #522418-13214
Krugman, Michael (8/31/2006) #522418-13213
Leisenring, Larry (8/22/2006) #522418-13206
Li, Kathryn (8/23/2006) #522418-13208
McDermott, S (9/19/2006) #522418-13239
Murphy, Michelle (8/21/2006) #522418-13201
Pre-Paid Legal Services, Inc. (Feinstein, Margaret) (9/29/2006) #522418-13255
Primerica Financial Services, Inc. (Muris, Timothy J.) (9/29/2006) #522418-13260
(highlighting mine)
Quixtar Inc. (Mohr, Michael) (9/29/2006) #522418-13258
Shah, Becki (9/6/2006) #522418-13223
Stephan, Jessica (9/8/2006) #522418-13224

False and misleading Quixtar (Amway) comments by former FTC official-turned-lobbyist “Jodie” Bernstein – as well as comments by the U.S. Chamber of Commerce and the DSA – rebutted in comments by Dr. Jon Taylor

Comment Number: 522418-13268
Received: 9/29/2006 8:02:13 PM
Organization: CONSUMER AWARENESS INSTITUTE & PSA
Commenter: JON TAYLOR
State: UT
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-13268.pdf](#) [Download Adobe Reader](#)

Comments:

ATTN: FTC Personnel - These comments constitute our rebuttal of the submission (tracking no. 522418-12039) by Joan (“Jodie”) Bernstein, with Bryan Cave LLP, on behalf of Quixtar, Inc., which is essentially Amway recycled to avoid the “Amway stigma”. What is incredible is the fact that the comment is introduced by Jodie Bernstein, the former Director of Consumer Protection for the FTC. Not only did Ms. Bernstein supply the same nickname she used at the FTC, but she addressed her cover letter to Donald S. Clark, the Secretary of the FTC – something the rest of us were firmly instructed not to do, but to send to the Commission without addressing it to a single person. So Ms. Bernstein used her “in” with the Commission to gain undue access. As a consumer advocate, I also find the fact that she is representing Amway/Quixtar absolutely stunning. It makes me wonder what she was doing while acting as Director of Consumer Protection at the FTC. Was she fully engaged or connected with what was going on; viz. the massive fraud committed daily by Amway/Quixtar worldwide? If I had been in her position and been actively involved in consumer protection, Amway/Quixtar could not pay me enough money to have my name associated in any way with Amway. After all, it was Amway that created the “800-pound gorilla in the Commission chambers” (quoting Bruce Craig, former Assist. AG for Wisconsin), when it outfoxed the FTC judge who ruled in 1979 that Amway was not a pyramid scheme, subject to the “Amway rules” – which Amway has thumbed its nose at ever since. And look-alike product-based pyramid schemes or chain sellers have been proliferating ever since, causing tens of millions of consumers to be defrauded out of tens of billions of dollars every year worldwide. Of course, Quixtar (Amway) is a member of the DSA, and their comments reflect those of the DSA and member firms. So I am attaching the latest revision of my comments to the DSA and member MLM firms. It is all relevant to this submission and clearly answers their objections to the proposed rule.

– Sincerely, Jon M. Taylor, Ph.D., President, Consumer Awareness Institute. E-mail: jonmtaylor@juno.com - Web site for MLM research and guides - www.mlm-thetruth.com

Rebuttal of comments by the U.S. Chamber of Commerce

Comment Number: 522418-13279
Received: 9/30/2006 12:09:11 AM
Organization: CONSUMER AWARENESS INSTITUTE & PSA
Commenter: JON TAYLOR
State: UT

Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-13279.pdf](#) [Download Adobe Reader](#)

Comments:

ATTN: FTC Personnel - These comments constitute our rebuttal of the submission on behalf of **Chamber of Commerce of the USA**, by Bruce Josten, regarding the proposed new business opportunity rule R511993 (Tracking No. 522418-07418). While we would like to think of the US Chamber of Commerce as unbiased and favoring consumer protection, I have it on good authority that Amway and the DSA have had much influence on it, including the inclusion of Amway family members on its board. I am not certain of the details, but could get them if the FTC is interested. Also, we have found Chambers of Commerce around the country to be of little help to consumers in this arena, since many MLM's are dues-paying members of their local CC's. So I am attaching comments rebutting the DSA's arguments, which are highly relevant to this submission and clearly answers their objections to the proposed rule. Sincerely, Jon M. Taylor, Ph.D., President, Consumer Awareness Institute and Advisor, Pyramid Scheme Alert - E-mail: jonmtaylor@juno.com - Web site for MLM research and guides – www.mlm-thetruth.com

Rebuttal by Dr. Jon Taylor of the comments by the Direct Selling Association (DSA)

Comment Number: 522418-13112
Received: 8/7/2006 8:11:26 PM
Organization: CONSUMER AWARENESS INSTITUTE & PSA
Commenter: JON TAYLOR
State: UT
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-13112.pdf](#) [Download Adobe Reader](#)

Comments:

As president of Consumer Awareness Institute, and Advisor to Pyramid Scheme Alert, both non-profit organizations that specialize in preventing and exposing pyramid scheme fraud worldwide, I offer the attached **rebuttal of comments by the Direct Selling Association (DSA)**, comments numbered 522418-12055 through 522418-12096 by Joseph Mariano. Headings for key points discussed in the attachment include: Qualifications of this analyst, Dr. Jon M. Taylor (and request for a hearing) The Direct Selling Association, recently taken over by chain sellers, now promotes chain selling (pyramid marketing) - even more than legitimate direct selling. Using the "5 Red Flags" analysis of compensation plans, the harm in chain selling, or pyramid marketing schemes, can now be identified, and such schemes (many of them DSA members) can finally be clearly differentiated from legitimate business opportunities. The DSA lumps together legitimate direct selling with chain (pyramid) selling, which meets the technical definition of an illegal pyramid scheme in most jurisdictions. Using deceptive tactics, the DSA lobbies to legalize blatant chain (pyramid) selling. The DSA appears willing to engage in any deception to further its ends - including the web version of ID theft. The DSA and DSA member firms have mobilized their massive lists to get participants to write in their "concerns" and objections to the proposed business opportunity disclosure rule - based on templates or form letters supplied by the DSA or member firms or consultants. DSA data and arguments are so highly questionable that most of their input should be discounted in developing a meaningful business opportunity disclosure rule. Specific rebuttals of DSA's detailed arguments are in the attachment.


REBUTTAL OF COMMENTS BY DSA (522418-12055 to12096) AND MEMBER MLM FIRMS REGARDING FTC BUSINESS OPPORTUNITY RULE R55193


By Jon M. Taylor, MBA, Ph.D., President, Consumer Awareness Institute


Summary of opening remarks in Taylor's rebuttal of the DSA comment


The attachment is quite long, so the opening arguments are summarized below:


- Jon Taylor has the credentials to comment, including the most extensive research on the subject.
- MLM has been successful in re-branding itself as legitimate direct selling, even there are distinct differences between legitimate direct selling and MLM (a.k.a., endless chain selling, recruitment-driven MLMs, or product-based pyramid schemes).
- 3. The DSA has been taken over by MLMs and now promotes chain selling more than legitimate direct selling.
- MLM is "the 800-pound gorilla in the Commission chambers." Since ruling in 1979 that Amway was not a pyramid scheme, the FTC has been challenged to stop or control MLM abuse, but has been unable or unwilling to do so.
- Using the well-researched "5 Red Flags"¹⁹ analysis of compensation plans, the harm in "recruiting MLM's," can now be identified, and such schemes (many of them DSA members) can finally be clearly differentiated from legitimate business opportunities. The 5 Red Flags are as follows:

 1. Recruiting of participants is unlimited in an endless chain of empowered and motivated recruiters recruiting recruiters.

 2. Advancement in a hierarchy of multiple levels of "distributors" is achieved by recruitment, rather than by appointment.

 3. Initial and/or ongoing purchases (products, sales "tools," etc.) by "distributors" are required or "incentivized" in order for them to be eligible for commissions and to advance in the business ("pay to play").

 4. For each sale, company payout to the total upline of participants equals or exceeds that for the person actually selling the product, creating an inadequate incentive to sell products directly and an excessive incentive to recruit.

 5. The company pays commissions and/or bonuses to more than five levels of "distributors." (In MLMs with less than 5 levels, they are compensated for in greater top-weighting in #4)

- In its reports, The DSA lumps together chain selling (MLM) programs with legitimate direct selling programs.
- Using deceptive tactics, the DSA and its MLM member firms lobby to legalize uneconomic MLM chain selling programs. This was dramatically demonstrated in Utah legislative hearings, when the DSA and MLM spokes persons duped the legislature with deceptive language and implications of a huge voting block they must answer to.

¹⁹ For a complete discussion of the 4 (and usually 5) red flags of recruitment-driven MLM, go to Chapter 2 in my book *Multi-level Marketing Unmasked* (formerly titled *The Case against Multi-level Marketing – an Unfair and Deceptive Practice*).

- In legislative hearings, the DSA blatantly misrepresented the FTC. FTC attorney James Kohm was quoted out of context to the DSA's advantage.
- Like its member MLM firms, the DSA appears willing to engage in deception to further its ends – including the web version of ID theft. They created a web site to redirect viewers from anti-MLM web site – until we challenged on their violation of their own code of ethics.

Continuing the actual letter of comment —

The DSA and DSA's MLM member firms have mobilized their massive lists to get participants to write in their "concerns" and "objections" to the proposed business opportunity disclosure rule – based on templates or form letters supplied by the DSA or MLM member firms or consultants.

Sampling the first 200 of the initial comments posted on the FTC web site in response to the invitation for the public to comment on the business opportunity rule, it appeared that the vast majority (over 95%) of MLM participants submitting comments are opposed to the proposed rule – or want it modified so as not to disclose meaningful information. These follow a clear pattern, and we know that most are filling out a form letter or template (apparently initiated by the DSA), to which they are attaching their names. One even submitted the form letter without a signature (Scott Jeff, tracking # 522418-00037)

When the larger number of comments (12,994 of over 17,000 submitted) were finally posted, I sampled 100 comments (every 100th comment) and came up with the revealing statistics in Exhibit A. All but one MLM company or participant opposed meaningful disclosure. It is interesting to note that both of the two ex-MLM participants emphatically expressed approval of honest and meaningful disclosure. It is also relevant that only one person was identified with any other type of business opportunity than MLM, and he was against the rule, as he believed it did not apply to his business. This supports the argument that a business opportunity rule that lumps MLM's and party plans with other types of business opportunities could be a mistake. The proposed rule is clearly an issue for MLM/party plan companies – and should apply primarily (or only) to them.

Exhibit A: Random sample of 100 responses to FTC invitation to public comments on proposed business opportunity rule

MLM or party plan companies or participants who oppose the business opportunity rule as proposed by the FTC	94
Respondents who did not identify did not identify their MLM company, but appeared to be affiliated with an MLM company (because comments parroted objections of DSA) – opposed to FTC business opportunity rule	<u>2</u>
Total MLM respondents opposing FTC rule as proposed	96
MLM participants favoring rule as proposed	1
Ex-MLM participants who oppose honest and meaningful disclosure	0
Ex-MLM participants who favor honest and meaningful disclosure	2
Respondents not identified with MLM or party plan – opposed to rule	<u>1</u>
Total sample	<u>100</u>

One of the objections, as voiced by these MLM submitters, is that it could negatively affect their income. However, it is clear from the above-mentioned tax survey and other research that few participants other than TOPP's ever show a profit on their taxes (though

they may seek a deduction for some expenses). Therefore, of the 17,000 respondents, most of whom are MLM participants, the vast majority are not likely earning a profit, but are merely hoping to some day profit from what has been proven to be uneconomic for all but the TOPP's. Hopefully, meaningful disclosure will discourage many from participating at all, as they would be much better off doing something else.

DSA data are so skewed and its motivation and arguments so highly questionable that most of their input should be dismissed in developing a meaningful business opportunity disclosure rule.

Considering all of the above, I urge FTC officials to disregard or consider invalid the data and arguments put forth by the DSA to justify and extol their mission and practices, including the "DSA Code of Ethics." Nearly all of their statistics combine chain selling MLM's with legitimate direct selling, hugely skewing and contaminating the results. And the DSA code of ethics does not go nearly far enough; e.g., it does not prohibit endless chain recruitment of participants as primary customers.

Please also discount DSA arguments against meaningful disclosure. On careful analysis, using the "5 Red Flags" research report cited above, as well as tax studies and other corroborative research, it appears that the motivation to resist such disclosure comes more from fear of revealing the truth to prospects than from legitimate objections. After all, if prospects had clearly disclosed to them that their odds of profiting from an MLM were less than 1 in 100, even with their best efforts (without deception), few would participate.

In summary, it is my well-founded belief that DSA input should be dismissed because DSA objections to honest disclosure reflect the fact that the interests of the DSA in concealing the truth are diametrically opposed to FTC interests in protecting consumers and fostering fair trade. Still, I will offer some rebuttals to points raised in the "Executive Summary" on page 4, which is expanded on in later parts of the series of DSA submittals. So these comments apply to the entire series of DSA comment submissions.

Specific rebuttals of DSA points:

[NOTE: DSA comments below are in italics, followed by my rebuttals in regular type.]

1. "Legitimate direct sellers play an important role in the national economy."

This statement by the DSA is true on the face of it. But unfortunately, the DSA's use of the term "legitimate direct sellers" includes both illegitimate MLM chain sellers as well as legitimate direct sellers – and fails miserably to make the distinction. In fact, the comments offered by the DSA reflect the observation of consumer advocates that MLM's have the greatest weight and influence with DSA lobbyists and communicators.

2. There are several ways that the FTC could revise the proposed rule to ensure that legitimate direct selling companies are excluded. Then the DSA lists 5 exclusions, that I will label items "a" to "e":

a. Exclude from the rule's provisions those business opportunity sellers whose opportunities carry minimal (or no) cost or risk.

The fact that the cost of initial sign up is low is deceptive – a mere ruse. In addition to expensive starter kits that promoters imply are essential for success, MLM's typically "incentivize" the ongoing sale of products and services to new recruits – often on a subscription basis amounting to hundreds or even thousands of dollars over time. These purchases are "incentivized" by making them necessary to qualify for commission or to advance in the scheme.

b. Retain the definition of business opportunity contained in the Franchise Rule, which does not include most or all direct sellers.

Here is an example of the DSA using the term “direct sellers” to include both legitimate direct sellers and MLM chain selling schemes, both of which are represented in its membership. If anything, the definition needs to be tightened specifically in the case of MLM schemes.

c. Better define “business opportunity” to cover work at home, vending machine, and similar schemes, and not direct sellers.

In comparison, many “work at home” and “vending machine” opportunities are far more legitimate than the MLM chain sellers who are members of the DSA. While I don’t have statistics to support this, my judgment and observations (having worked in the field of business opportunities for 35 years) are that their loss rates are likely to be far below the 99% loss rate of DSA/MLM member firms.

d. Exempt companies that adopt and adhere to a set of industry best practices, including, for example, requirements relating to wholesale inventory purchases protected by buyback policies and/or “cooling-off” right for salespeople.

DSA industry standards, including the “DSA Code of Ethics,” are woefully inadequate and even misleading, as explained above.

Inventory purchases buyback policies are too restrictive to be helpful. MLM recruits are encouraged to open and share their products, not to keep them unopened. Then they cannot qualify for a refund. In fact, a financial officer for Nu Skin told me that refunds total only 3½% - which is easily absorbed by the company with the large cost-of-sales to revenue ratio Nu Skin enjoys. Besides, few victims of MLM recruitment realize that they have been scammed. Instead, they tend to blame themselves or to fear recrimination if they seek a refund which would affect those who recruited them, who could be close friends or relatives.

The “cooling off” provision would be useful, especially if honest and meaningful disclosure were required and prospects were encouraged to search the web for the pros and cons of the MLM in question.

e. Exempt companies that are subject to a self-regulation process such as that offered by DSA.

This is addressed above. The self-regulation provided by the DSA is set up to protect not so much the participants, as the defrauding member companies.

3. DSA cannot overstate the harm to legitimate direct sellers that would result from the proposed rule.

Any harm incurred from compliance by MLM’s should be compared to the much greater harm (in time, effort, and expense) suffered by victims of MLM’s, including DSA member firms. Recent research demonstrates that millions of victims lose billions of dollars worldwide every year from participation in these MLM’s. For proof of this in just one DSA member firm, consider the massive harm suffered worldwide by victims of the Nu Skin scheme. Though the FTC issued an Order in 1994 for Nu Skin to cease its misrepresentations of earnings of its distributors, Nu Skin kept right on misrepresenting earnings, even after PSA challenged its compliance. A few changes were made by 2004, but not half of what was needed to protect new recruits.

The “REPORT OF VIOLATIONS of the 1994 FTC Order for Nu Skin to cease its misrepresentations” is very relevant to the proposed rule, and every FTC official involved in the rulemaking process would do well to read it. The report was attached to my comment filed July 16 (tracking # 522418-10266). More recent misrepresentations are recorded in Appendices F and G as an update of the same report (see tracking # 522418-10051) The full 70-page report can be downloaded (with key points summarized on the contents page) from this page –

mlm-thetruth.com/research/mlm-statistics/nuskins-numbers/

4. The waiting period requirements in the proposed Rule is impractical and will fundamentally and adversely alter the way in which direct selling operates.

This result could be a very good thing for consumers. In fact, based on recent research conducted by myself and others on DSA member firms, if all DSA member firms suffered severe setbacks in number of persons recruited into their programs, it would signal a victory for both the FTC and for the consumers it is pledged to protect. And I would go further in suggesting that the FTC recommend all prospects search the web for both positive and negative information on specific companies before making a decision to participate. It is only on the web that such information is available in any depth. They can query the search engine by making two or more entries such as the following:

- (1) (name of company) – “advantages or legitimate company”
- (2) (name of company) – “fraud or scam or pyramid scheme”

With the enormous search capabilities of search engines such as Google, such a search would yield an abundance of sites expounding on the pros and cons of most any MLM program.

Also, a well-researched 5-step do-it-yourself evaluation process for deciding on MLM participation (using the “5 Red Flags” discussed above) is available for free online at – www.mlm-thetruth.com/evaluating-mlms/.

5. The legal action disclosure requirement in the proposed rule is overbroad and unmanageable and will likely produce significant unintended consequences.

Though not all legal actions result in convictions, the very existence of law suits or complaints to law enforcement of large damage amounts or in significant numbers is a red flag that should be considered before a prospect makes a decision to participate. But I believe that the “5 Red Flags” report above lists red flags that are even more significant than are complaints filed or legal actions taken. In any event, law enforcement seldom takes action against the massive number of MLM abuses that occur daily. Much of the blame for this rests with victims, who rarely file complaints. In law enforcement, the squeaky wheel gets the grease. No complaints, no action.

Many wonder why it is so rare for victims of MLM’s to file formal complaints or to seek legal action against MLM’s. There are many reasons for this, including their having been conditioned to believe that failure is their fault, the fear that they will suffer consequences from or to their upline or downline – who could be close friends or family, the fear of self-incrimination (since in chain selling MLM’s every major victim is a perpetrator – in order to recoup his/her investment), and the reminders by MLM promoters that “if their program were illegal, it would have been shut down long ago.” So there is a circular phenomenon in MLM: No law enforcement because there are so few complaints – and no complaints because law enforcement seldom acts. This is further explained in my comments dated July 13 (tracking #522418-12262) and in my report “Top ten things I learned from Ten Years’ Research on MLM.” It can be viewed or downloaded (now “Summary of Findings” at – www.mlm-thetruth.com/research/reports/key-conclusions/).

6. The cancellation and refund disclosure requirement in the proposed rule would be difficult to comply with and would provide prospects with little useful information.

Both arguments are self-serving and not reflective of consumer needs, as explained above. And with modern computers that all these MLM companies use, compliance would not be difficult at all. Consumers need to know this type of information, and the FTC is wise to demand that it be disclosed.

(second part of #6) *On the contrary, our high turnover rate is a sign of the vitality of our industry and the ease of entry and egress.*

Does the writer live on another planet where free enterprise does not exist? Only a person inexperienced in business options would make such a statement. It is certainly an insult to the intelligence of FTC officials to assume they would buy this argument. A high turnover rate is a serious red flag in *any* business.

7. The references requirement in the proposed rule disregards the privacy and property rights of recruits and sellers, respectively, and is simply not workable.

As mentioned in my July 13 comments (see # 5 above), these references would be extremely helpful, as they are for franchise prospects. But what is needed is a list of ex-participants, as the vast majority of MLM chain sellers will soon be ex-participants, as the prior DSA comment suggests. As I explained in my July 13 comments, at least half of the references should be from ex-participants. However, I expect that MLM officers will find a way to supply sympathetic friends or family to be references and will somehow reward them for saying what they want them to say – making them little better than shells. Knowing the pattern of deceptive behavior routinely engaged in by MLM's, I honestly doubt that much good will come of this requirement.

8. Finally, the earnings claims disclosure requirement is too complicated and not useful vis a vis direct sellers.

Complicated? Not useful? Have the DSA communicators ever seen the disclosures required by franchisers? Have they not seen the complicated financial disclosure documents required by the SEC for stocks of publicly traded companies? By comparison, the earnings claims disclosure requirement of the FTC would be a piece of cake.

And if strict disclosure rules apply to stocks for publicly traded companies and for franchises, the widespread deceptions used in MLM recruiting would suggest that disclosure for MLM companies should be even more strict. MLM recruitment depends of many misrepresentations, 30 of which are listed at – www.mlm-thetruth.com/tools1/consumerguides/typical-mlm-misrepresentations/ member firms have historically avoided voluntarily providing meaningful disclosure documenting earnings claims. In fact, I surveyed the presidents of 60 leading MLM firms in the hopes of getting information crucial to the making of good decisions by prospects of MLM programs. The results were predictable: None of the MLM officers were willing to provide the requested information. The “Network Payout Distribution Study” was reported in my July 1 and July 17 comments (tracking # 52218-12748).

This study illustrates what we consumer advocates have known for years; viz., most MLM's are uneconomic, or beneficial to a handful of people at the top of a pyramid of participants at the expense of a multitude of downline victims, over 99% of whom lose money (after subtracting company purchases and other expenses). So such MLM's will seldom disclose useful information voluntarily. Honest and meaningful disclosure of earnings information must be mandated by the FTC, similar to what the FTC requires for franchises and the SEC requires for the stocks of publicly traded companies.

In addition to the aforementioned tax study, I have gathered statistics on earnings of MLM's (for which such data was available) and compared them with statistics on odds of winning at gambling in Las Vegas casinos. After debunking the deceptions in the reporting of the MLM's, I found the odds of profiting from craps or the roulette wheel at Caesar's Palace in Las Vegas were far greater than for participating in MLM's, including some members of the DSA. These statistics were sent by express mail July 1, and they can be obtained online at –

www.mlm-thetruth.com/research/mlm-statistics/shocking-stats/

And as I explained in my (aforementioned) July 13 comments to the FTC, what is needed is not less disclosure, but far more disclosure, so far as it is honest and meaningful. Not only should average moneys paid to participants at given levels in the pay plan be reported, but also average moneys paid by participants to the company in products and purchases. It is the net figure reflecting money in, minus money out, that is important for prospects to make an intelligent decision. (See Exhibit B)

It does not matter if the products purchased from the company are used, sold, given away as samples, stored, or disposed of (and the services used); the total average of payments to the MLM company needs to be disclosed if earnings disclosure is to be meaningful. This is particularly relevant for MLM chain sellers, since our research demonstrates that most of the revenues received by these companies come from recruits (in the form of incentivized purchases), and not from sales to legitimate customers not in the network of participants. Such honest and meaningful disclosure would show that nearly all participants lose money, even before operating expenses are subtracted. For these reasons, the DSA will come up with every possible excuse for not disclosing such information.

Based on extensive research, including analyses of hundreds of MLM compensation plans and resultant extreme loss rates, it is clear that the requirement to disclose earnings and purchases of participants is the most important step that the FTC can take to inform consumers and to prevent consumer abuse. See Exhibit B for an ideal form that would satisfy the criteria of honesty and relevance for MLM prospects – without violating individual privacy.

Many of these suggestions were also explained in the July 7 comments by Robert Fitzpatrick of Pyramid Scheme Alert (tracking #522418-06415).

In the DSA conclusion paragraph on page 7, several errors are apparent. For example, *“The proposed rule, however, would cast far too wide a net and in doing so would harm and possibly destroy many legitimate direct sellers.”*

I would suggest that while this may be a small problem for legitimate direct sellers, it certainly would not apply to MLM chain sellers who are members of the DSA. They need far more strict rules, not less.

FTC personnel should take note that of the comments that came in, very few of the legitimate direct sellers submitted comments complaining about honest disclosure. The great volume of complaints came mainly from MLM’s – most of whom were from the DSA membership ranks.

“Direct selling companies are not sellers of business opportunities and should be exempted from an business opportunity fraud rule.”

On both counts, nothing could possibly be further from the truth. While MLM promoters are careful not to position their programs as business opportunities in SEC filings or before regulators, they frequently speak of their programs as “business opportunities” in their recruitment campaigns, including at large rallies that I have personally witnessed. As to the second part of that statement, if any “income opportunities” need a strict business opportunity fraud rule, it should be the MLM chain sellers represented by those among the DSA roster.

Other comments that provide valuable insight for FTC personnel

In rebutting the DSA comments, I believe some important comments on the side of consumer protection by other top experts in this field deserve serious consideration by the Commission, since they sharply contradict the comments of the DSA. So rather than

restating their arguments, I would just like to recommend they be given serious attention. They include the following:

Bruce Craig (tracking number 522418-12306) – served as Assistant Attorney General for the state of Wisconsin for 30 years, during which he litigated a number of pyramid scheme cases, including extensive litigation against Amway in the early 1980's and Koscot Interplanetary, Holiday Magic, and Bestline in the early 70's. These cases were pursued with the cooperation of Commission staff.

Douglas M. Brooks of Martland & Brooks, LLP (tracking number 522418-10570 – plus exhibits – with tracking numbers 10572 and -10579) – has intimate knowledge of legal problems with disclosure of meaningful information, as in the Nu Skin case cited earlier.

Robert Fitzpatrick – (tracking numbers 522418-06415 –70036) Mr. Fitzpatrick's article "The Myth of 'Income Opportunity' in Multi-level Marketing" is a must read for anyone considering the issue of earnings disclosure of participants in MLM programs.

Pyramid Scheme Alert, also by Robert Fitzpatrick – (tracking numbers 522418-06415, -70036, and –70037) This non-profit organization seeks to expose and prevent pyramid scheme fraud world-wide.

After reading what these experts have to say, one can see agreement with my comments (listed under Consumer Awareness Institute and Pyramid Scheme Alert (Taylor, Jon – tracking numbers 522418-70056, -10051, -12684, -12748, -10058, 10266, -12262, and -12585) – all based on extensive research, much of it drawn from official documents of the MLM companies themselves. These clearly show the need for meaningful disclosure, negating the objections of the DSA as suggested above. The requirements for honest and meaningful disclosure are outlined in these comments. See Exhibit B for a form that would provide honest and meaningful disclosure without violating individual privacy.

Exhibit B – a simple form that would provide honest and meaningful disclosure:**Annual Company Revenues received by WealthPlus International, Inc.¹
– Plus Payments to – and Purchases from –
Participants² Who Had Enrolled³ in WealthPlus within the Past Three Years²**

Total WealthPlus revenues for the year	\$95,000,000
Total payments ⁴ in commissions and bonuses to participants for the year	\$40,500,000
Total of all purchases of products and services for the year from Wealth Plus by (the same group of) participants who were enrolled and authorized to recruit other participants within the past three years	\$90,000,000
Average purchases of products and services from WealthPlus per participant	\$900
Average commissions and bonuses paid by WealthPlus to participants	\$405

– Breakdown of payments to participants –

Total annual payments received by participants at different levels⁵ from WealthPlus in <u>commissions & bonuses</u>	Average purchases for each level	Number of participants*	% of total participants
Over \$500,000	\$20,000	0.001%	1
\$250,000-\$499,999	\$15,000	0.005%	5
\$100,000-\$249,999	\$12,000	0.01%	10
\$50,000-\$99,999	\$10,000	0.05%	50
\$25,000-\$49,999	\$8,000	0.1%	100
\$10,000-\$24,999	\$6,000	0.5%	500
\$5,000-\$9,999	\$4,000	1.0%	1,000
\$1,000-\$4,999	\$2,500	10.0%	10,000
\$1-\$999	\$1,200	25.0%	25,000
\$0 – participants who made purchases but did not qualify for commissions ⁶	\$400	62.0%	62,000
\$0 – participants who enrolled but made no purchases since enrolling ⁷	\$0	<u>1.3334%</u>	<u>1,334</u>
TOTAL PARTICIPANTS		<u>100%</u>	<u>100,000</u>

See “EXPLANATORY REFERENCE NOTES FOR FTC OFFICIALS” on the following page.

EXPLANATORY REFERENCE NOTES FOR FTC OFFICIALS:

¹ WealthPlus International, Inc. is merely a fictitious name used for illustrative purposes. Also, all of the numbers used in this chart are fictitious and for illustration only.

² These statistics include ALL persons who contracted with the company as participants within the past three years (or other designated time period). This is to correct the deceptive reporting practice of some MLM firms that count only “active distributors” in the past year (or other limited time period). They eliminate the recruits that dropped out. Their base for comparison thus represents only a small slice of the total recruits. Also, while eliminating participants that contracted to join and then dropped out, this small base of participants is compared with participants who may have taken five to twenty years to achieve a certain level. The result is numbers that are extremely skewed, making the MLM “opportunity” appear to be profitable for most recruits. The above form would correct these deceptions.

³ Enrolled participants are persons who signed a contract allowing them to buy products at discounted or wholesale prices from the company and authorizing them to recruit other persons into the company, from which the enrolled participant could profit (in commissions, bonuses, etc.) from sales to said persons.

⁴ This number must include ALL purchases from the company, including products, training, sales aids, telecommunications and other electronic aids, etc. This makes it possible for recruits to see if it is likely that more money will be received from the company than is paid to it. It also will help determine if the company is a legitimate business opportunity or merely uses the “business opportunity” as a ruse to get participants to buy products – with few real customers outside the network of participants.

⁵ Instead of reporting income by designated payout levels (Blue Diamond, Diamond, Ruby, etc.) these dollar categories make possible comparisons between MLM companies and make transparent the income distribution that hitherto has been obfuscated by complex compensation plans that are difficult to compare. Note that the breakdown of payments includes some very high income levels. This is to validate the claims of some MLM promoters of huge incomes.

⁶ Listing persons who bought products but got no payout from the company makes transparent the persons who did not “qualify” for commissions due to failure to buy (sell) a minimum number of products in order to qualify for commissions or to advance in the scheme.

⁷ The listing of those who enrolled but bought no products would be those persons enrolled in order to satisfy a “head count” of recruits for companies who have such requirements in order for participants to qualify for commissions or to advance in the scheme.

NOTE ON SIMPLICITY AND PRIVACY – Companies today use computers that would make the processing of this information fast and relatively simple. It would not be a burden for them and none to individual participants. And no person would need to have his/her information associated with his/her name, so privacy should be no concern.

CONCLUSIONS

I believe that an honest and meaningful business opportunity disclosure rule is possible and fair to both companies and consumers (prospects), at least as it applies to MLM companies and participants, which apparently represents over 95% of respondents to the FTC invitation for public comments. It would require a form that makes possible comparisons between programs and makes transparent what has heretofore been carefully hidden; viz.- the TRUTH.

After careful review of the arguments put forth by the DSA and member firms against disclosure requirements in the proposed rule, I have designed a form that would satisfy the needs of consumers who are confronted with MLM recruitment. At the same time, it should not be rejected by honest MLM sponsors and sponsors of legitimate business opportunities; i.e., those interested in promoting fair trade and in maintaining integrity in the marketplace. Please study carefully *Exhibit B – a form requiring honest and meaningful disclosure: “Annual Company Revenues received by (any MLM company) – Plus Payments to – and Purchases from – Participants Who Had Enrolled in WealthPlus within the Past Three Years”*

The FTC is faced with a crucial choice in its final rulemaking as it affects MLM. Will the new “business opportunity” rules reflect the objections of the DSA/MLM lobby – or its own mission to protect consumers and promote fair trade?

After reviewing the above rebuttal comments and the comments made by top experts as listed above, it is clear that meaningful disclosure as outlined in my comments above and as submitted July 13 (tracking number 522418-12262) is needed. It is also clear why the DSA and DSA member MLM firms are so fiercely opposed to meaningful disclosure. If the truth were known about what a losing proposition MLM is for almost all participants (at least 99% lose money, after subtracting expenses), sensible people would not join up and the programs would collapse like a house of cards.

So the FTC personnel responsible with the final rulemaking are faced with a very clear choice between two mutually exclusive options:

1. They will act to fulfill the mission of the FTC as suggested in its own posting regarding the Business Opportunity Rule, which is as follows:

“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.”

As clearly explained above and supported by evidence in the associated reports to which I have referred, such deceptive practices are embodied in nearly all of the MLM firms that are members of the DSA. As the research demonstrates, they routinely engage in “fraudulent, deceptive, and unfair business practices.” And also as explained above, the DSA itself engages in such practices.

In other words, the motivations and practices of the DSA and its member firms are antithetical to the objectives of those providing consumer protection, which should include the FTC. So if the FTC is to fulfill its mission “to provide information to help consumers spot, stop, and avoid” such practices, by protecting consumers the business opportunity rule will discourage – and even severely hurt – the DSA and its MLM member firms. Who would join their programs if they knew the whole truth?

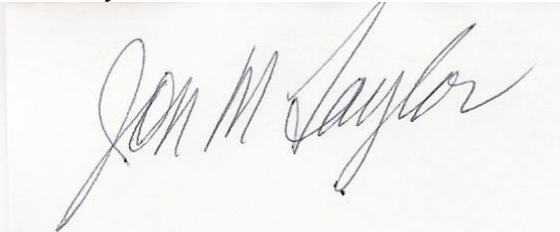
Or –

2. The FTC could yield to the powerful influence and pressures of the DSA and its member firms, including the cover letter by Jodie Bernstein (who, incredulously, was formerly Director of Consumer Protection for the FTC!) on behalf of Amway/Quixtar/Alticore, one of the industry's worst offenders in using fraudulent, deceptive, and unfair business practices to exploit vulnerable consumers worldwide. As is apparent from their comments, the DSA and MLM member firms and their recruiting participants are clearly opposed to honest and meaningful disclosure. If the FTC chooses this option (or to leave things as they are), consumers worldwide will continue to suffer, and the FTC as a regulatory arm of the US government will be severely compromised.

It is clear from the comments of the DSA and member firms, as well as the comments of those of us who are speaking on behalf of consumers, that the FTC cannot satisfy the needs of consumers and of the DSA (and MLM's) at the same time. If you help consumers, you hurt the DSA (and MLM's). Conversely, if you help the DSA (and MLM's), you hurt consumers.

I want to take this opportunity to thank FTC officials for their courage in opening this enforcement issue to public input. It is the hope of myself and others donating our time to warn and protect consumers that the FTC will forge ahead with meaningful reform and not give undue weight to the DSA, whose interests are 180 degrees from those of consumers and of those seeking a fair and equitable marketplace.

Sincerely,

A handwritten signature in black ink on a light-colored background. The signature reads "Jon M. Taylor" in a cursive, flowing script.

Jon M. Taylor, Ph.D., President, Consumer Awareness Institute
and Advisor, Pyramid Scheme Alert

E-mail: jonmtaylor@juno.com

Web site for MLM research and guides – www.mlm-thetruth.com

Rebuttal of DSA and MLM firms by Dr. Stephen Barrett of mlmwatch.com

Comment Number: 522418-13267
Received: 9/29/2006 7:47:21 PM
Organization: Quackwatch
Commenter: Stephen Barrett
State: PA
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-13267.pdf](#) [Download Adobe Reader](#)

Comments:

The Direct Selling Association, most of whose members are companies that do multilevel marketing, has submitted a lengthy statement (#2882-2892) with this conclusion: "DSA supports and shares the FTC's goal of ridding the marketplace of fraudulent business opportunities. The proposed rule, however, would cast far too wide a net and in doing so would harm and possibly destroy many legitimate, lawful direct sellers. The proposed rule would also likely unnecessarily discourage many prospects from pursuing beneficial direct selling activities. Therefore, if the FTC continues to pursue a separate business opportunity rule, DSA urges the FTC to exclude from its requirements those legitimate, lawful companies that use the direct selling business model. . . . Direct selling companies are not sellers of business opportunities and should be exempted from any business opportunity fraud rule. " This statement is preposterous. I have investigated more than 150 companies that sell health-related products. All were promoted with glowing but deceptive accounts of how much money can be made. In an age where the public demands accountability, nobody should be exempt. I have attached additional suggestions.

DSA's attempt to rebut CAI (Jon Taylor) and PSA (Robert FitzPatrick)

The full comment letter follows.

Comment Number: 522418-13253
Received: 9/29/2006 3:55:44 PM
Organization: Direct Selling Association
Commenter: Christine Varney
State: DC
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-13253.pdf](#) [Download Adobe Reader](#)

Comments:

Attached (below) are the Direct Selling Association's rebuttal comments regarding Business Opportunity Rule, R511993.

HOGAN &
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September 29, 2006

Chnstine A. Varney Partner
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Federal Trade Commission
 Office of the Secretary
 Room H-13 5 (Annex W)
 600 Pennsylvania Avenue, N.W.
 Washington, DC 20580

Re: Notice of Proposed Rulemaking for the Business Opportunity Rule, Project No. R511993- Rebuttal
 Comments of the Direct Selling Association

Dear Secretary Clark:

The Direct Selling Association ("DSA") is pleased to submit these rebuttal comments regarding the Federal Trade Commission's ("Commission") proposed Business Opportunity Rule ("Proposed Rule").

The initial comments of the Direct Selling Association confirm the long-standing commitment of the association and its members to stop business opportunity fi-aud, and set forth and substantiate in detail our legitimate concerns about certain elements of the Proposed Rule. These rebuttal comments will not repeat that discussion and substantiation. We were gratified, though not surprised, that the vast majority of other comments reflect views that are quite similar to those that have been made by DSA, including some 17,000 individual comments submitted by interested and concerned individuals who might be adversely affected by the Proposed Rule. These citizens describe themselves variously, including as single mothers, disabled veterans, and college students (and one as an assistant state attorney general). Additionally, we note that dozens of direct selling companies expressed their concerns about the impact of the Proposed Rule on their time-tested business models. Consumer leaders expressed their concern

with the Proposed Rule's impact on legitimate businesses. General business leaders expressed interest and concern on behalf of direct sellers and other small businesses. Other industries expressed their opposition to the Proposed Rule as drafted and suggested changes consistent with some of DSA's suggestions, and academicians expressed concerns about unintended consequences of the proposal.

In stark contrast, there are very few comments in support of the Proposed Rule as drafted; a handful of these comments are highly critical of the direct selling industry. These comments inaccurately question not only the commitment of DSA and its members to fair and honest practices, but also the standards of law and consumer protection set out by the Commission and many states over the last 30 years.¹ The paucity of these comments, when compared to the large outpouring of comments that are consistent with DSA's initial observations, is, we believe, illustrious of the merits of DSA's position. DSA is proud of its record of consumer protection and education and its long history of working cooperatively with law enforcement and all interested parties to ensure that consumers are protected against many types of marketplace fraud. We trust that the Commission is aware of many of DSA's efforts. In any case, the Commission will, we trust, benefit from some further illumination regarding the deficiencies of fact and analysis in the assertions made in the handful of comments that are critical of direct selling.

The theme of these comments seems to be that the Commission should abandon its long-established recognition of the legitimacy of the direct selling industry and should regulate or make illegal all direct selling that uses a multilevel form of compensation. In effect, those commentators would seek to deny the legitimacy of direct selling through the adoption of a rule by the Commission. These comments effectively reject prior Commission analysis, as well as law and regulation at the federal, state and local levels of government, that set out the standards for distinguishing legitimate sales companies from fraudulent activities that focus improperly on recruiting while neglecting end-user sales.² These comments provide no credible basis for the fundamental positions they espouse or for the "relief" they seek for a number of reasons.

Scope of the Proposed Rule

First, the comments misconceive the scope and purpose of the Proposed Rule. The Proposed Rule before the Commission is not a rule about the legitimacy of multilevel marketing. It is in essence a disclosure rule. DSA's comments and those of many of its members and their sales people reflect significant concerns about the effect of some aspects of the Proposed Rule on legitimate companies and their sales people. They also provide numerous and compelling facts that refute many of the premises in the few comments that would propose to expand the scope of the Proposed Rule to go beyond disclosure to consider a rule against multilevel marketing.

Satisfaction and Income of Direct Sellers

Second, the comments that would propose to eliminate direct selling include numerous examples of purported "facts" that are not substantiated in the comments, are in fact inaccurate, and are refuted by

¹One of the commentators involved has been taken to task for statements about another self-regulatory organization. (See "BBB was Wrongly Maligned" Deseret Morning News (Salt Lake City Utah) 8/2/96).

² The Commission has set out a long line of decisions describing the differences between legitimate direct selling companies using multilevel compensation and pyramid schemes. These decisions, described in DSA's initial submission on p. 19, have been relied upon by the public, the direct selling industry and law enforcement as the standard for defining pyramids.

information in DSA's prior comments and in the comments of thousands of individuals who have engaged in direct selling. For example, the linchpin of the comments attacking the direct selling industry is the claim that more than 99% of direct sellers that participate in a multilevel direct selling compensation plan

lose money. Although this claim is made repeatedly throughout several comments (each citing the other as corroboration in an echo chamber of misinformation), it remains both unsubstantiated and unverifiable. None of the comments making this claim provide any information as to how this percentage was calculated. While at least one commentator provides an anecdotal description of the information he reportedly considered or consulted in making the claim, one will look in vain for precise and verifiable information as to exactly how the purported calculation was made and what numbers were included in it. For example, the comments provide no data regarding the types of sales person revenues (including profits on retail sales) that went into the purported calculation, the overall amount of those revenues, the types of expenses that were included, the overall amount of those expenses, the number of distributors considered in the calculation, how that number was derived and what it represents, the period covered by the calculation, or any other numbers critical to the calculation. This commentator also ignores the distinction between salespeople and consumers who join a direct sales company primarily or solely for the purpose of purchasing products for themselves, and misunderstands personal consumption by salespeople as a cost of doing business. In this erroneous analysis, product purchases by direct sellers for personal consumption are treated as somehow inappropriate. Such unsubstantiated statements are simply not credible and cannot be the basis for a rulemaking or for a negative judgment on the legitimacy of direct sales companies.

An examination of professionally conducted and statistically accurate data, collected by DSA and reputable research analysts over a period of years, indicates that, while making money is not necessarily the exclusive reason people enter direct selling, more than one-half of direct sellers report that their net income from direct selling after taxes and after expenses is positive.³ Ninety one per cent of direct sellers say that direct selling meets or exceeds their expectations as an activity where the harder they work the more money they can make. In addition, a positive net income is reported by nearly one-half of *new* direct sellers --those who have been in the industry for less than a year. The same statistics hold true for those direct sellers who do not continue in the industry. The vast majority of direct sellers rate their experience with direct selling as excellent, very good, or good. Eighty per cent of direct sellers have been with their company for one year or more and 34% for five years or more. Eighty five per cent of direct sellers say that direct selling meets or exceeds their expectations as a good way to supplement their income or as a way to make a little extra money for themselves. ⁴

These few commentators so critical of direct selling have also speculated that sales to customers other than direct sellers are insignificant. That assertion is, however, again refuted by other research. The significant selling of product by direct sellers to non-direct sellers is shown by the following statistics. Nearly all direct sellers (97%) earn money from personally selling product, and 34% do not earn money from the sales of others but just from their own personal sales. Half (50%) of U.S. adults purchase product using the direct-selling retail channel during a year.⁵ It is important to note that individual direct sellers can be and often are the ultimate consumers of product for their own personal use.

³ 1999 National Salesforce Survey, MORPACE International, Inc. (www.morepace.com). The study involved telephone interviews with 2,037 U.S. direct sellers from 36 direct selling companies. The study is instructive regarding direct selling multilevel compensation plans because, since 1998, 82% or more of direct sellers have been affiliated with multilevel direct selling companies. (*Direct Selling Growth & Outlook Survey*, various annual issues, Nathan Associates Inc.)

⁴ Id

⁵ *2004 General Public Attitudes toward Direct Selling*, Burke, Inc. (www.burke.com). The study interviewed 1,001 U.S. adults by telephone.

Direct Selling and Consumer Protection

Third, the comments attacking direct selling companies depend on the wholly unsubstantiated (and erroneous) claim that there are far more complaints about direct selling than the relatively minor number that are publicly reported. The commentators offer no "support" for this claim other than their personal

views and anecdotal reports that those who would otherwise complain are reluctant to do so because it would reveal them as "failures" in direct selling. In fact, there are ample and effective means for any present or former direct sales persons who may have concerns to express them. The Commission itself solicits such complaints. Anyone who claims to be harmed by a business opportunity may file a complaint via a simple form on the Commission's website.⁶ We have no doubt that the Commission also gives close and adequate attention to any such complaints. Similarly, DSA has a long-established Code of Ethics that requires members to advertise the Code broadly and to describe how complaints may be forwarded to DSA. DSA actively investigates all complaints and enforces its Code in an effort to prevent any kind of harm to consumers or salespeople. State and local authorities provide a host of similar opportunities for anyone who is concerned to submit complaints. These procedures set in place by the Commission, DSA, and others ensure that the direct selling industry operates in a manner that is beneficial both to those who join the direct selling industry and to consumers. To claim otherwise due to an alleged lack of opportunity to submit comments or concerns about direct selling companies or an alleged reluctance to pursue those opportunities is, at best, unsubstantiated speculation that is refuted by the record of effective adoption and utilization of a variety of complaint procedures.

Conclusion

DSA and its member companies respect and appreciate the opportunity to work with the Commission in its long-standing shared effort and commitment to eliminate fraud in the marketplace, while recognizing direct selling as a pro-competitive and legitimate channel of distribution for goods and services. Our comments reflect that commitment but seek to highlight instances in which the specific provisions of the Proposed Rule would be unduly burdensome, ineffective, or in violation of privacy or other rights. With that in mind, we would look forward to the opportunity to participate in any hearings and/or workshops the Commission might conduct to continue the dialogue about those factors in the Proposed Rule that are problematic for legitimate direct selling companies.

If hearings or workshops are held, the DSA would like to participate regarding all of the topics set out in its July 17th submission, as well as any additio *[sic]*

Christine A. Varney
Counsel to Direct Selling Association

cc: Joseph N. Mariano

⁶ [https://rn.ftc.gov/pls/dod/wsolcq\\$.startup?Z~ORG~CODE=PU01](https://rn.ftc.gov/pls/dod/wsolcq$.startup?Z~ORG~CODE=PU01)

NOTES ON DSA DECEPTIONS:

The deceptive practices of the MLM industry are reflected in the deceptive arguments voiced by its prime lobbyist, the DSA. Examples include: (1) their surveys of consumer satisfaction, and income without separating out MLM from legitimate direct selling.²⁰ (2) We too have surveyed MLM participants and find that few are able to claim that the money they receive from the MLM is more than what they pay to the company in products and services. We did provide references to the research we and others had done on MLM loss rates, based on the companies' own published reports. (3) As for their Code of Ethics, some of the most egregious MLMs have passed muster with the DSA until some agency or private action has pointed out their massive fraud.²¹ As for reasons that few victims complain, read Chapter 9 of my book *Multi-level Marketing Unmasked*. In fact, read the whole book!

²⁰ See Chapter 2 of my book *Multi-level Marketing Unmasked (formerly The Case against Multi-level Marketing – an Unfair and Deceptive Practice)*.

²¹ Op. cit., Chapters 10 and 11.

Rebuttal of CAI and PSA by Quixtar (Amway), with Jody Bernstein, another past FTC official-turned-lobbyist, signed on²²

Comment Number: 522418-13258
Received: 9/29/2006 4:50:30 PM
Organization: Quixtar Inc.
Commenter: Michael Mohr
State: MI
Subject: Business Opportunity Rule
Title: Notice of Proposed Rulemaking
CFR Citation: 16 CFR Part 437
Attachment: [522418-13258.pdf](#) [Download Adobe Reader](#)

Comments:

Enclosed for your consideration is a Rebuttal Comment Submitted by Quixtar Inc. to the U.S. Federal Trade Commission in Response to the Proposed Business Opportunity Rule, R511993

IMPORTANT NOTE:

In her comment letter, Joan (“Jodie”) Bernstein (with Altacor V.P. Michael Moore) repeats much of the deceptive dialogue of the DSA, but what she says isn’t as important as who she is – or WAS. As a former high level official at the FTC – with contacts still there, she is able to influence the rulemaking process in not-so-subtle ways. She and two other former officials – Timothy Muris and J. Howard Beales, Jr. III. – were sought out for their comments by DSA and other MLM officials. It would be interesting to know what they were paid to do this. One must wonder – what kind of person would convert from consumer protection to fraud protection – and still live with themselves. **This kind of revolving door – at the behest of powerful special interests – is one of the abuses we as consumers and citizens must continually be on the alert to avert.** (*not a bad alliteration*)

To see Ms. Bernstein’s full comment letter, go to –
www.ftc.gov/os/comments/businessopprule/rebuttal/522418-13258.pdf

²² As did Timothy Muris and Howard Beales, Jr. III

The sheer number of false and misleading statements²³ by former FTC Chairman-turned-lobbyist Timothy Muris is stunning.

The false and misleading statements in the comment number in the hundreds – far more than any I have examined during the rule-making process. Many of these deceptive arguments, as well as his comments filed in July, provided rationale and even terminology for the staff to use in its report to the Commissions justifying the MLM exemption.

It is disturbing to us as consumer advocates to realize that the same person who made so many false and misleading statements was once chairman of the FTC – the agency some consider the nation’s “consumer watchdog” – charged with protecting the public from “unfair and deceptive practices in the marketplace.” To better display a sample of some of the more obviously misleading statements, together with rebuttals by Dr. Jon Taylor, they are displayed in the table below.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
<p>(I) INTRODUCTION AND SUMMARY OF REBUTTAL COMMENT: The overwhelming majority of comments submitted in response to the Commission's Proposed Business Opportunity Rule evidences three critical points:</p>	<p>Of course, the overwhelming majority of comments are filed by MLM promoters defending their turf. The appeal for comments by the DSA/MLM lobby went out to as much as 1,000 times as many MLM participants as those who actually commented. Most were copying or adapting a form letter supplied by their MLM sponsors. We learned from a telephone survey that at least some may have been forged or submitted without the permission of the named submitter.</p>
<p>(1) the rulemaking record contains no evidence supporting such a broad rule that will undeniably sweep in a huge number of legitimate companies and individuals,</p>	<p>Evidence was presented, but it should be multiplied by many times for MLMs, as our research shows that very few victims file complaints with law enforcement. They have been taught that failure is their fault for not “ working the system.” And because of the endless chain of recruitment, major victims have recruited others in hopes of recouping teir investments and eventually realizing the huge incomes they were promised. So they fear consequences from or to friends and family they have recruited if they complain.</p>
<p>(2) the Proposed Rule would have a devastating impact on the viability of these legitimate business and the individuals who support their families through participating in them, impacting the American economy by an estimated \$57.6 billion per year and reducing competition and consumer choice in numerous market sectors,</p>	<p>In the case of MLMs, the huge sales amounts quoted represent gains for the companies, but losses for participants – except for TOPPs (top-of-the-pyramid promoters). As for competition and consumer choice, all MLMs assume infinite markets, which do not exist in the real world. They totally ignore proven laws of supply and demand. They are therefore inherently flawed, unfair, and deceptive. Wolrd-wide feedback convinces us they are also extremely viral and predatory.</p>

²³ Submitted September 29, 2006

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
and (3) the costs of the Proposed Rule (both economically and in terms of the loss of privacy) are dramatically greater than estimated in the Notice of Proposed Rulemaking ("NPRM) and will greatly outweigh any possible benefit.	Nothing could possibly be further from the truth. Read chapters 2, 7, and 12 of my book <i>Multi-level Marketing Unmasked (formerly The Case against Multi-level Marketing – an Unfair and Deceptive Practice)</i> .
. . . For these reasons, Primerica suggests that the Commission publish a new Proposed Rule aimed squarely -and solely -at fraudulent conduct, and use that refined proposal as the basis for further rulemaking proceedings.	To those who are informed (and not by the DSA or MLM industry) the most fraudulent and prevalent of packaged business opportunities are the hundreds of MLMs that have sprung up since the tragic 1979 FTC v. Amway decision. Considering the FTC's weak response to the DSA/MLM lobby, a rule that effectively addresses MLM fraud is highly unlikely.
(II.) THE RECORD REVEALS THAT THERE IS NO BASIS FOR COVERING THE WIDE RANGE OF LEGITIMATE COMPANIES THE PROPOSED RULE" REACHES	No basis? See the above-mentioned book, an early version of which was referenced in several of my comments.
(IIA) There Is No Evidence of Widespread Fraud in the Direct Selling Industry.	There is ample evidence from the published reports of the MLMs themselves. Read my book – and the report by Robert FitzPatrick titled: "The Myth of 'Income Opportunity' in Multi-level Marketing." Download from his web site at – www. pyramidschemealert.org
(IIA) Of the more than 17,000 comments submitted in response to the NPRM, only a handful (just over 1 %) supported the Rule. Given the size of the direct selling industry in the United States (involving over 13 million Americans), the number of commenters expressing problems with legitimate companies is truly miniscule.	What would an informed person expect? The appeal for comments went out to over ten million MLM participants, and just over one in 1,000 responded. Why not more than that? And is this just a numbers game? The fact that virtually ALL independent consumer advocates were united in supporting the initial Rule is what is significant – and should not be considered "miniscule." We are donating our time and do not have \$4 million to spend lobbying to get consumers to write in.
(IIA) Further, the lack of any payment for recruiting removes any incentive for individual agents to make such misrepresentations. There is no basis for regulating Primerica, or any company with a similar structure. . . .	In MLMs, the lack of a signup fee when recruited is inconsequential. The real "pay-to-play" feature comes into play when a recruit seeks to qualify for significant commissions or for rank advancement. Many lose thousands of dollars scrambling to get to or stay at a higher level of qualification – supposedly where the money is.
(IIA) As with Primerica agents, these comments overwhelmingly support the business opportunity in which the individual participates. Moreover, these comments consistently report that up-front costs are very small, and subject to refund policies that allow a prospective participant to recover virtually all up-front costs if the opportunity is not right for them.	Based on reports by MLM companies, refund provisions are seldom exercised, but not for the reasons assumed by MLM promoters. Recruits have been strongly encouraged to open and use the products – to "be a product of the products." If the packages are opened, they do not qualify for a refund. Some are embarrassed to admit failure. Others are still believing all the hype about the magical healing powers of the "pills, potions, and lotions" they were sold. We have learned from feedback from thousands of victims and their families that few victims realize (without extensive deprogramming) that they have been scammed. And they don't want to offend the friend or relative that introduced them to the products – even though the "hard sell" may have been by someone else.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
<p>(IIA) The absence of any significant number of complaints belies any conclusion that any fraud or deception in the direct selling industry is common enough to warrant a new rule.</p>	<p>The FTC admits that it has received thousands of complaints over MLM or pyramid marketing schemes. As discussed above, the percentage of victims who muster the courage to file complaints about any endless chains recruitment scheme is small. If one multiplies the number of complaints the FTC has received by a multiple of hundreds, a more realistic estimate of victims can be made. My own research shows that in Utah, at best on in on thousand victims of MLM programs files a complaint with the state's Division of Consumer Protection.</p>
<p>(IIB) Comments describing other direct selling companies highlight the fact that such opportunities are especially important to women, people with disabilities, seniors, and African-Americans. For these groups and many others, easy entry and exit, the flexibility of work hours, and the opportunity to work from home all combine to make direct selling particularly attractive. These comments sound a warning that the effects of the Proposed Rule will fall disproportionately on segments of the American population who are least able to withstand them.</p>	<p>Disadvantaged people, as well as any others, are nearly always impoverished by MLM to the degree of their participation. Those who invest the most in time and money, lose the most. Muris has not studied the compensation plans of hundreds of MLMs, as I have done, and posits from total ignorance of these plans. To make any significant amount of money, beyond a minimum wage, requires many months of sustained full-time work, with those entering a given market first having a huge advantage. To someone who understands these pay plans, the notion of anyone earning income from seasonal or part-time work is ludicrous.</p>
<p>(IIC) Almost all of the substantive commentary supporting the Proposed Rule came from two affiliated organizations that submitted several comments each. These comments have a single-minded focus on pyramid schemes. They are unconcerned with fraudulent work-at-home schemes, vending machine route scams, and the other specific frauds targeted in the NPRM.</p>	<p>This single-minded focus on MLM is based on over a decade of research on hundreds of MLMs, convincing us that MLM is far more damaging than all other consumer scams put together. Vending machine scams and other purported income opportunities are insignificant in comparison.</p>
<p>(IIC) Instead, they [critics of MLM] allege that many direct selling companies are really illegal pyramids. To reach this conclusion, these commenters string together a series of unfounded assertions and "data" that is both unrepresentative and unreliable. The commenters then opine, again without supporting evidence or even logic, that this pattern of fraud is hidden from view not because the alleged victims do not report it, but rather because they cannot recognize it. According to one of these commenters, it is "extremely rare for MLM victims to recognize the fraud in an MLM intensive de-programming by a knowledgeable consumer advocate."</p>	<p>To any capable independent analyst who is informed on the issues, MLMs (as opposed to legitimate direct selling) are the most extreme and harmful of pyramid schemes by any measure – loss rates, aggregate losses, and number of victims. The data we use in our reports come from the companies themselves, and the methodology and calculations used in my reporting was validated by independent financial experts. Our observations regarding victims' fear and hesitation to report fraud comes from feedback from thousands of MLM victims and families worldwide who have contacted us – many pleading for help and inquiring why the FTC does not act to control MLM abuse.</p>
<p>(IIC) . . . If the Commission wishes to address pyramid schemes through rulemaking, it should fashion a definition of such schemes, and narrow the Rule to businesses falling within that definition. Neither the comments nor the NPRM, however, provide any basis for imposing a sweeping, burdensome rule on legitimate businesses in the hope that pyramid schemes will reveal themselves. Certainly, the disclosures the Commission has proposed will not accomplish that task.</p>	<p>This is a red herring put forth by Muris – and echoed by a compliant FTC staff. The purpose of IPBOR was never to reveal whether or not a program is an illegal pyramid schemes. Its purpose was to provide information to consumers to help them make informed decisions when considering a proposed business opportunity.</p>

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
<p>(IIC) The comments supporting anti-pyramid provisions assert that pyramid schemes are widespread, and present themselves in the "disguise" of direct selling companies. Their evidence for this assertion is completely unreliable. One "study," for example, relies on a survey of selected tax preparers about their clients' incomes. Aside from the fact that such a sample necessarily excludes those who prepare their own taxes, even the comment admits it is unethical for the tax preparers to disclose this information.</p> <p>Another "study" is a quarter century old analysis of the tax returns of distributors for a single company in a single state - a company that the Commission determined was not a pyramid. Moreover, these commenters allege losses based in part on counting as costs what the record makes plain is a benefit for many participants - the ability to purchase for personal consumption products they like at a significant discount. Other comments offer better evidence that flatly contradicts these claims. One comment, for example, reports an independent survey that finds an "average" distributor earns \$418 per month, an above average distributor earns \$2,523 per month, and a top distributor earns \$12,217 per month</p>	<p>Reliable data from MLM is very difficult to obtain, since they are loathe to reveal information that would expose their flawed programs that are so unprofitable for new recruits. It requires much creative research to get beneath and debunk the many deceptions upon which MLM depends. The information from tax preparers was obtained without their revealing names or other personal information. This is all spelled out in the report, which Muris obviously scanned without serious intent of understanding the necessary methodology or its significance.</p> <p>The Wisconsin study is relevant, as Amway still uses essentially the same compensation plan. The IRS data cannot be questioned, unless filed fraudulently. If Muris had attended some MLM rallies, he would know that products are sold in a climate of hype or in "a culture of deception." One study has shown MLM multi-vitamin products to be priced at several times the price of competitive products in retail stores – even at wholesale. They are simply not retailable to any significant degree. Our feedback suggests that those who do buy at retail are often "sympathy buyers" or "counterfeit customers" – as explained in chapters 2 and 4 of my book. The DSA statistics cited are always slanted, and typically without drawing a distinction between legitimate direct selling and recruitment-driven MLMs, or product-based pyramid schemes.</p>
<p>(IIC) It is one thing to say that many participants in direct selling do not make very much money. That point is not in dispute, and in fact is freely discussed in the comments of many direct selling companies. The reality is that many participants work part-time, some do so only seasonally in certain businesses, and others participate for a short time and then decide that the opportunity is not a fit for them. Low incomes do not reflect fraud, they reflect the reality that most people who work part-time or sporadically will not earn much money.</p> <p>It is another thing to assert that almost all participants lose money. The facts in the record provide no basis for deducting assumed "costs" from the available income estimates and jump to the conclusion that participants actually lose money.</p>	<p>Part-time and seasonal income from MLM is a DSA myth repeated by Muris, assuming regulators and the public will buy the argument. Careful study of hundreds of MLM programs has demonstrated that none reward part-time or seasonal effort significantly. The promised rewards go to those who build huge downlines – and were one of the first to join in a given market.</p> <p>Our assertions, backed by company statistics, that virtually all new MLM recruits lose money is based on a simple money-in-versus-money-out analysis. It has been confirmed in a recent telephone survey of BOR commenters that most could not say that they had received more money from the MLM company than they had paid out in products and services. And this was <u>before</u> subtracting operating expenses.</p>
<p>(IIC) Other direct selling companies [other than Primerica] also allow distributors to lace consumer orders directly with the company after those orders have been received. In any direct selling company with a similar structure, the assumption that inventory purchases from the company reduce income simply evaporates, providing no justification for applying the Proposed Rule.</p>	<p>Whether the products are distributed by the company or by an upline distributor is irrelevant. The person who recruited the distributor who buys the products gets commission overrides even if shipped by the company. With MLMs, most "pay-to-play" purchases are by monthly auto-ship. Since these products are typically far more expensive than similar products from standard retail outlets, they would not likely have been purchased except to participate in the program. They should therefore be counted as an expense in analyzing the profitability of the MLM as a "business opportunity."</p>

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
<p>(IIC) The handful of comments critical of direct selling also assert that many direct selling companies exist solely by virtue of "internal consumption" (sales of products to participants in the business), and are therefore illegal pyramids. This commentary simply ignores the fact that some direct selling businesses have many participants who regard the opportunity as a "buyers club," allowing them to obtain products for personal consumption at a discounted price. The Commission staff itself has recognized the legitimacy of this organizational form. The fact that buyers clubs exist does not convert legitimate direct sellers into illegal pyramids.</p>	<p>Actually, I would not object if an MLM were promoted as a "buyers' club" which gives participants the opportunity to pay <i>more</i> for some good (and some highly questionable) products. But that is not how they are sold. They are sold as part of an "income opportunity." They are sold false hope. Those who invest the most can lose a lot of money, to say nothing of wasted time and effort. In the statement "<i>The Commission staff itself has recognized the legitimacy of this organizational form.</i>" Muris is referring to a staff letter from James A. Kohm, Acting Director of Marketing Practices, Fed. Trade Comm'n to Neil H. Offen, President, Direct Selling Ass'n, at 1 (Jan. 14,2004). This statement is often quoted out of context by DSA/MLM spokesmen. If one reads the entire letter, a different perspective emerges.</p>
<p>(IIC) There is no record evidence to support the contention that internal-consumption based business opportunities are so widespread that the Commission should regulate the entire direct selling industry in the manner the commenters desire.</p>	<p>FALSE. Muris is ignoring the research referred to in our comments, which is made available free of charge on our web sites. For a more thorough treatment of the subject, read my book, which was referred to in my comments (but which Muris obviously ignored).</p>
<p>One comment sets forth five purported "red flags" to identify that an arrangement is a pyramid scheme. These "flags" ask whether a person is required to "pay to play" to participate in the arrangement, participants are rewarded solely for recruiting, and compensation is greater for recruiting than it is for selling products to retail customers. . . . The "five red flags" also include arbitrary and unsupported criteria involving the number of levels of an organization (more than five levels is a red flag) and the relationship between commissions to the distributor making the sale and others in the organization (more total commissions to higher levels than to the agent who makes the sale is a red flag). There is no basis for these "criteria." Entirely conventional organizational forms have substantially more than five levels of employment relationships. A manufacturer who sells to a wholesaler who sells to retailers may appear to involve three levels. But the manufacturer has (at least) a CEO, a manager, an assistant manager, and a production worker. The distributor and the retailer have a similar structure. If the different levels are revealed explicitly -as they are in the contracts that organize a multi-level marketer -there could be at least 12 levels between the top of the organization and the consumer. The red flag based on commissions faces similar problems. It would be highly unusual for the retail clerk who makes the final sale in a conventional distribution arrangement to earn a commission that exceeded the total payments to his or her "upline" -the higher levels of the economic organization.</p>	<p>Obviously, Muris did not read my report at any depth before criticizing it. The levels referred to were levels of sales management.</p>

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
(IIC) In summary, the comments do not present persuasive evidence of widespread fraud in the direct selling industry, nor do they establish a sufficient factual basis for subjecting legitimate companies like Primerica to the Proposed Rule. At best, the comments may support an effort by the Commission to define what constitutes a pyramid scheme, if the Commission believes that such a definition would assist its enforcement efforts. If the Commission wishes to depart from the flexible standards under Section 5 of the FTC Act and attempt to define pyramids with specificity, it may certainly do so. But it cannot, and should not, cripple an entire industry to ferret out pyramid schemes that only exist in the minds of the commenters.	To an informed reader who has examined the evidence we have presented, the first statement is false. The defining or ferreting out of pyramid scheme issue was not the primary purpose of the Rule. But since he brought up the issue of pyramid schemes, the most extensive analysis of product-based pyramid schemes is included in my book, in which I make the case that the most damaging of pyramid schemes are those that are product-based (MLMs), by any measure – loss rates, aggregate losses, and number of victims. Product-based pyramid schemes exist not only in the minds of us commenters, but in the dwindling financial resources of millions of victims of MLM fraud.
(IID) Initially and as discussed above and in its principal comment, Primerica believes the record lacks any evidence justifying the scope of the current Proposed Rule, and lacks any factual support for key propositions.	If one includes in the record the comments of qualified consumer advocates and independent small business analysts, this statement is blatantly false.
(IID) Finally, each section of this rebuttal comment presents a list of the facts relevant to that section of the comment that Primerica believes are established in the present record. If the Commission disputes these facts, or believes that other commenters dispute them, Primerica believes that hearings and cross-examination are necessary to resolve the issues, if only because the Commission's view of the facts is not, at this point, a part of the record. The threshold issues of fact include: 1. There is no evidence of widespread business opportunity fraud, or unfair or deceptive acts or practices, among licensed life insurers and registered broker- dealers.	1.FALSE – One has only to read our reports and search the Internet for significant evidence of unfair and deceptive practices for any product class of MLMs, including those offering financial products.
2. There is no evidence of widespread business opportunity fraud, or unfair or deceptive acts or practices, in the direct selling industry.	2. FALSE – There was an abundance of evidence referred to in our comments
3. Based on the Commission's enforcement experience, the only prevalent business opportunity frauds are work-at-home schemes, schemes involving the sale of vending machines, rack locations, or ATMs, and schemes in which compensation to participants is based primarily on payments for recruiting others into the scheme. (Number 4 is OK.)	3. FALSE – Though only an infinitesimally small percentage of victims file complaints against MLMs, the Commissions had received thousands as reported. Business opportunity frauds in programs such as work-at-home schemes, schemes involving the sale of vending machines, rack locations, or ATMs, are insignificant in comparison to MLM fraud.
5. Consumers will not, or will not be able to, differentiate between legitimate and fraudulent business opportunities based on their compliance with the Rule.	5. Again, this is a red herring. This is not the primary purpose of the Rule. The Rule was intended to provide information to help consumers make wise decisions when considering a purported business opportunity.
6. The record provides no indicia of the prevalence of pyramid schemes in the marketplace, compared to legitimate multilevel marketing or direct selling opportunities.	6. The distinction between product-based pyramid schemes and legitimate MLMs is a distinction without a difference – except for the existence of products. See comments by Bruce Craig, former assistant to the Wisconsin Attorney General.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
7. There is no incremental benefit of the Rule including businesses that pay commissions based primarily on sales, with no minimum purchase requirement, and no payments for recruiting.	7. Pay-to-play is typically activated as soon as an MLM participant seeks commissions or rank advancement.
8. The benefits (if any) of including such businesses under the Rule do not justify the costs.	8. FALSE – except for the MLM companies profiting from deceiving the public.
9. There is no evidence that unfair or deceptive acts or practices are prevalent among direct selling companies in business five years or more.	9. FALSE. Some of the worst MLMs are over five years old. Again, we are drawing a distinction between legitimate direct selling and MLM – which the DSA lobby has re-branded as “direct selling.”
10. There is no incremental benefit of the Rule including companies that have been in business for five years or more, or companies that otherwise post a bond.	10. FALSE – for the hundreds of MLMs I have analyzed, the length of time is irrelevant.
11. The benefits (if any) of the Rule including companies in business five years or more, or that otherwise post a bond do not justify the costs.	11. FALSE – same as #10
(IIIA) Based on a conservative estimate that the Proposed Rule would reduce Primerica's recruiting by 25 percent, Primerica projected an economic loss of \$1 billion for Primerica alone over the next ten years if the Proposed Rule is promulgated.	Good! These losses suffered by MLM companies represent gains for prospective recruits that would have otherwise been defrauded by them.
(IIIA) Evidence submitted in other comments demonstrates that this estimate was indeed conservative. In particular, the Direct Selling Association ("DSA") conducted a survey about the extent to which the Proposed Rule would reduce the willingness to participate in direct selling. The results of the DSA survey showed that participation would be reduced by as much as 85 percent if the current proposal is promulgated. A reduction of this magnitude likely would cause several billion dollars of damage to the company over the next ten years. Primerica would not be alone in suffering such great harm; the DSA study suggests an annual impact on the U.S. economy of \$57.6 billion from the Proposed Rule. The DSA survey, together with the comments of many other direct selling companies and participants, reveals that the Commission's estimate of the economic impact of the Proposed Rule was far too low. The economic damage would not end with direct selling companies themselves. Instead, it would flow directly to the 13.6 million Americans who participate in such businesses.	As for DSA statistics, they are skillfully skewed in favor of their members MLM firms. The more these firms suffer, the more the public – and prospective victims – benefit.
(IIIA) As discussed in Primerica's principal comment, its independent agents would necessarily bear the substantial compliance burdens of the Proposed Rule, even if, contrary to the Rule's current language, they are excluded from the definition of "business opportunity sellers."	Giving out a 1-page form prepared by the company is not a substantial compliance burden, although in many cases, supporting documentation would be needed.
(IIIA) Providing the litigation disclosure and retaining the associated paperwork, as well as creating, providing, and keeping copies of the references disclosure, would directly cost Primerica's agents time and money.	Same answer as the last one.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
(IIIA) Providing the litigation disclosure and retaining the associated paperwork, as well as creating, providing, and keeping copies of the references disclosure, would directly cost Primerica's agents time and money.	Same answer as for the last two.
Moreover, any waiting period would require multiple visits with potential recruits, imposing further costs. Along with the dramatic reduction in their ability to recruit new agents into the business, these costs would make the Primerica opportunity untenable for many agents. The supplemental income they receive from Primerica, which is critical to meeting their personal financial goals and supporting their families, would simply vanish.	Such repeated visits and further investigation by prospects is a good thing. Income of new agents may vanish – not because of the Rule, but because of Primerica's top-weighted compensation plan
(IIIA) Other comments make clear that distributors affiliated with other direct selling companies are similarly situated.	When Muris refers to "other direct selling companies," it is obvious that he has been somehow incentivized to speak not just in behalf of Primerica, but also on behalf of other MLMs.
(IIIA) The Proposed Rule would directly affect the household incomes of millions of American families.	As far as affecting the household incomes of millions of American families, the affect of the Rule could be very positive for those that refuse to join because they conclude from the information provided that the "opportunity" is more pretended than real.
(IIIA) Because the Proposed Rule will reduce or eliminate the competition that direct sellers provide in numerous sectors of the economy, it will also adversely affect consumers. Primerica's competitors are primarily traditional insurance companies and broker-dealers. For insurance and financial services, Primerica provides consumers with an alternative to traditional firms, and offers a distribution network that reaches a segment of the American population that its competitors have historically ignored. The inevitable reductions in Primerica's sales force would make insurance and financial services less available to this segment of the American people.	The compensation plans of all of the hundreds of MLMs I have studied ignore the laws of supply and demand. Competition becomes irrelevant. The Initial Proposed Rule would have had a net beneficial effect on the American people, especially those who chose not to join an MLM.
(IIIA) Subject again to its belief that rulemaking hearings are premature and that a more narrowly-focused proposed rule should precede any such hearings, Primerica proposes the following designated issues of fact relating to the economic impact of the Proposed Rule for any hearings conducted with respect to the Proposed Rule as it currently stands: 14. The Rule will dramatically and negatively impact the 13.6 million Americans who participate in legitimate direct selling to generate income for their households.	14 FALSE. It could benefit prospects by giving them information to make better decisions about MLM participation.
15. Direct selling businesses make a large contribution to the American economy, totaling approximately \$72 billion.	15. Legitimate direct selling may contribute to the American economy. Recruitment-driven MLMs sap resources from consumers and legitimate businesses.
16. The Rule will dramatically and negatively affect the contribution of the direct selling industry to the American economy.	16. Good – because it is essentially a negative contribution.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
17. The Rule will circumscribe consumers' ability to use direct selling opportunities to meet their needs, particularly those who desire flexible part-time earnings opportunities or supplemental income.	17 FALSE AND MISLEADING. Only those who are uninformed about MLM compensation plans would even suggest that MLM rewards part-time or seasonal participation.
18. The Rule will reduce direct sellers' recruiting by at least 25 percent, and as much as 40-80 percent, thereby adversely affecting their ability to maintain or grow their sales forces and businesses.	18. Good! This may be a curse for MLM recruiters, but a blessing for consumers.
19. The reduction in direct sellers' ability to attract new agents will substantially reduce their product and service sales, adversely affecting both the direct selling companies and the income earned by individuals participating in them.	19. Ditto #18.
20. The reduction in direct sellers' ability to attract new agents will also impact consumers who rely on direct selling for goods and services that are not available elsewhere.	20. If they are not available elsewhere, there must be a good reason.
21. Undermining Primerica's ability to maintain its sales force will cause middle-income consumers who have traditionally not been served by the insurance and financial services industry to lose a substantial point of access for life insurance protection in the event of the death of a breadwinner, retirement savings, and other financial services.	21. Such point of access for life insurance will be replaced by eager salesman from more legitimate traditional companies.
22. The Rule's substantial burdens and the costs of complying with its requirements would make recruiting more onerous for individuals involved in direct selling, and would therefore give some companies the incentive to compensate agents for recruiting activities, a result opposite of the intended effect of the Rule.	22. This "reverse incentive" would be worse with the MLM exemption because legitimate direct selling companies will likely convert to an MLM model to avoid having to comply with the Rule.
23. Very few, if any, legitimate companies could comply with the Rule using a simple one-page disclosure form; rather, for most legitimate companies, the disclosure form would be lengthy and complicated.	23. The Franchise Disclosure Rule is often hundreds of pages long, and they manage to comply.
24. Perpetrators of business opportunity fraud would be more likely than legitimate businesses to use a one-page form, if they complied with the Rule at all.	24. This could include some MLMs as well.
25. For the average direct selling company, the length of the disclosures required by the Rule, including the litigation disclosure, the earnings claim disclosure, the refund disclosure, and the reference disclosure, would consume many pages. For a large multi-national direct-selling company like Primerica that is part of a larger corporate family, the required disclosures could be thousands of pages long.	25. "Thousands of pages" is surely an exaggeration. Much more complicated franchises don't require that many pages for their disclosure documents. All the FTC staff would have to do is walk down the hall to the franchise office in their building to see what is typical for them.
26. The Rule would require disclosures to be given to many millions of consumers each year.	26. So what? If millions of consumers are recruited by MLMs each year, then those millions deserve adequate disclosures to make informed decisions.
27. The reference disclosure, and potentially the earnings claim disclosure, require customization for each prospect who receives the disclosures. The cost of preparing these customized disclosures will be large, and will not be matched by any commensurate benefit to consumers.	27. FALSE AND MISLEADING. The cost is exaggerated and the benefit to consumers is underestimated.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
28. The NPRM estimates that there are 150 multilevel marketing companies, but in reality, there are at least 1,500 direct selling companies that would be subject to the Rule.	He does not make a distinction between MLM and legitimate direct selling companies that are not based on endless chains of recruitment.
29. The NPRM's estimate of the total number of hours for covered businesses to initially comply underestimates the cost of the Rule by several orders of magnitude.	The purpose of the Rule was not to make it easier for sellers of business opportunities, but to make it easier for consumers considering them to make informed decisions.
30. Legitimate direct selling companies, as opposed to fraudulent schemes, will bear the vast majority of compliance costs required by the Rule.	Muris is obviously considering direct selling companies like Primerica that use an MLM marketing model to be legitimate direct selling companies, a positions that deserves to be challenged.
31. Based on the record before the Commission, including the DSA survey that forecasts a decline in recruiting in the range of 40-80% and cost estimates from companies such as Primerica that estimate the revenue loss from reduced recruiting will be \$1 billion over ten years, the cumulative expected cost of the Proposed Rule (including direct costs and lost revenue) will be orders of magnitude higher than the Commission's estimate.	This may be true for the companies, but for consumers it is certainly an improvement over the unregulated sale of business opportunities, such as MLMs.
32. The Rule's definition of "seller" makes individual agents "sellers" subject to all the required disclosures on a personal level.	This is good for prospects.
33. Requiring individual agents to meet these personal disclosure requirements will cause the individual agents to incur cost and burdens that they are ill-equipped to handle, and will further increase the compliance burden on companies that monitor their agents' compliance.	This is also good, as it should incentivize those recruiting to be more careful and more informed.
(34 and 35 not contested) 36. Individual agents will not have sufficient knowledge to respond to consumers' questions regarding each of the disclosures, such as the litigation disclosure, refund disclosure, earnings claim disclosure, and reference disclosure.	It would not hurt for them to be so informed before they attempt to recruit persons whose lives could be significantly affected.
37. Individual agents' lack of a response or inability to respond to questions about the disclosures will discourage prospective recruits from participating in direct selling companies.	This could also be good for prospects.
38. Individual agents will incur costs based on the Rule's required disclosures that they are likely not capable of bearing without incurring net losses in their businesses, including costs in time and resources to potentially customize, print, and provide disclosures to all potential recruits, as well as store copies of signed disclosures.	If the purported business opportunity cannot endure the costs of transparency, that in itself may be a sign that it is not a solid opportunity.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
(IIIB) The more likely consequence of the Proposed Rule is that legitimate companies will comply, suffering the costs and business disruptions that inevitably will follow. Perpetrators of fraud either will ignore the disclosure requirements or will provide false disclosures, then point to the disclosures made by legitimate companies to argue that the fraud is actually the safer and more reliable opportunity. Thus, the Proposed Rule would have the perverse consequence of benefiting perpetrators of fraud and making consumers more vulnerable to fraudulent business opportunity schemes.	An even more perverse result will likely occur with the MLM exemption. Legitimate sales and business opportunities will be powerfully incentivized to convert to the flawed MLM model which is built on endless chains of recruitment. The assumption of an infinite market. ²⁴ in a finite world makes an MLM inherently flawed, unfair, and deceptive.
39. Perpetrators of business opportunity fraud will not comply with the Rule, including making the required disclosures truthfully, observing the seven-day waiting period or refraining from making false earnings claims and promises of assistance.	The assumption that long-established MLMs are not perpetrators of business opportunity fraud must be questioned. Read chapters 2-7 of my book.
40. The effect of the Rule's required disclosures on legitimate businesses, combined with the lack of compliance by fraudulent actors, will be to cause consumers to believe that legitimate businesses are more risky and more deserving of suspicion than fraudulent business opportunity schemes.	This is an assumption that has yet to be proven. If it were true, why would franchises, which have much more demanding disclosure requirements, be respected by new franchisees who spend a fortune to get into them?
41. Fraudsters will use written disclosures as a shield to defend themselves against claims of oral misrepresentation, making it more difficult for the Commission and other enforcement agencies to successfully pursue those committing fraud.	This same logic could be used for franchisors and for publicly traded investments.
(IIIC) Any Waiting Period Would Be Highly Detrimental to Direct Selling Businesses and is Completely Unnecessary. One of the clearest examples of regulatory overkill is the Proposed Rule's seven-day waiting period before a person can participate in a business opportunity. In its principal comment, Primerica devoted substantial discussion to the highly damaging nature of this requirement, the compliance burden associated with it, and the unprecedented nature of applying a seven-day waiting period to an expenditure of \$200 or less. The comments submitted by others in response to the Proposed Rule support these conclusions. For example, the DSA survey concluded that the waiting period, by <i>itself</i> , would reduce participation in direct selling businesses by 60 percent! Many commenters echoed the theme that because a waiting period is virtually unheard of in the American marketplace, it would inevitably imply that a relationship subject to such a waiting period must be very dangerous indeed.	For business opportunities like MLM, which are notorious for a litany of misrepresentations ²⁵ used to recruit new people, as waiting period makes a lot of sense. The waiting period could apply to making a significant investment. However, it is common for MLM promoters to claim there is little or not sign-up fee and then incentivize recruits to invest hundreds or even thousands of dollars to qualify for higher commissions or payout level. MLMs deserve the reputation of being questionable investments, so a waiting period would reinforce that. It is true that if prospect took some time to ask around and do a diligent computer search on the Internet for problems with an MLM, many would not join. This would be good for consumers, though the fraudulent MLMs would suffer. It is not the role of the FTC to protect fraudulent MLMs.
Numbers 42-52 give further reasons for eliminating the waiting period.	These reasons are no more consumer-friendly than those presented above.

²⁴ Taylor, Jon M. *Multi-level Marketing Unmasked*, Chapter 2.

²⁵ Op. cit., Chapter 8.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
(IIID) The Litigation Disclosure Would Be Unfair to Legitimate Companies, Would Impose Massive Compliance Costs, and Would Provide No Benefit to Consumers.	If one is committed to consumer protection, it makes a lot of sense to reveal to prospects any legal actions, past or present, final or pending, against the company. Prospects who will be spending money, time, and effort promoting a program deserve to have this information.
Muris then posits a long series of arguments, adding numbers 53-66 to support this view.	will not take the time to unravel these arguments one by one. The foregoing rebuttal comments are sufficient to see the pattern of deception necessary to defend his position.
(IIIE) The References Disclosure contemplated by the Proposed Rule Would Impose Even Further Compliance Burdens, Would Undermine Privacy Interests, and Would Require the Disclosure of Confidential Business Information.	References could be handled discretely and could focus on references nearby. This would not help recruitment if the company has much to hide. If it was legitimate and profitable, references could only help the company in its recruitment efforts.
"Issues of fact" numbered 67-80 support his (and the DSA's) view on references, which is likely what the DSA encouraged him to justify.	I will not take the time to unravel these arguments one by one. The foregoing rebuttal comments are sufficient to see the pattern of deception necessary to defend his position.
IV. THE COMMENTS HAVE PROVIDED MANY ALTERNATIVES FOR NARROWING THE PROPOSED RULE A. The Record Continues to Provide No Basis For Including Licensed Insurance Companies and Registered Broker-Dealers in the Proposed Rule.	If any financial services company chooses the MLM model to market its products, that is basis by itself for it to be included in the Rule. (See chapter 2.)
(IV B) The Record Supports Exclusion of Legitimate Companies That Do Not Exhibit the Key Elements of Pyramid Schemes. As for internal consumption, Muris again posits the "buyers club" analogy.	Muris's definition of a pyramid scheme is very limited and reflects only weak regulatory efforts to define them. A much more rigorous, consumer-friendly, and research-based definition is carefully explained in Chapter 2 of my book.
(IV C) The Comments Support An Effort to Define Pyramid Schemes. . . . The principal challenge in using a regulation, rather than enforcement efforts, to define pyramid schemes is drawing bright-line tests that will allow the business community to structure arrangements in compliance with the Rule.	Not surprisingly, the "bright-line tests" terminology found its way into the staff report. Both Muris and the FTC staff dismiss my 18 years of research on hundreds of MLMs to answer this challenge, which I believe I have done. Though my reports refer to months of comparative analysis, backed up by decades of sales and entrepreneurial experience (and which I taught in college classes) and though the data used was from the companies themselves, and the methodology validated by financial experts, the FTC staff reported that "the FTC does not accept the research of Dr. Jon Taylor." How convenient. They don't have to bother reading and trying to understand it.
(IVD) Expanding the Existing Franchise Rule to Address the Frauds Identified in the NPRM Remains a Viable Approach.	Read the letters by attorney Doug Brooks and former assistant to Wisconsin AG Bruce Craig early in this report.
(IVE) Narrowing the Definition of Consideration Would Alleviate Much of the Overbreadth.	The low initial fees, if any, are merely a ruse to deceive regulators and prospects. The real "pay-to-play" costs are found in the compensation plans. To earn significant commissions and rank advancement to a level where profits are possible required a sizable investment in purchases of products and services from the company. Again, read Chapter 2. "overbreadth" – a handy term for the DSA/MLM lobby.

False or misleading statements by former FTC Chairman-turned-lobbyist Timothy Muris	Debunked by Dr. Jon M. Taylor, Consumer Awareness Institute (mlm-thetruth.com)
(IVF) Excluding Large, Long-Lived, and Financially Responsible Companies Is Supported by the Rulemaking Record.	Though the record my refer to “fly by night” operations, it includes no evidence that long-lived companies are more responsible, especially in the MLM field. In fact our research shows that some of the oldest MLMs are the most fraudulent. They have learned to “re-pyramid” from country to country to avoid market collapse. Read chapters 2 and 3.
(IVG) Primerica Supports a 90 Percent Refund 1 90 Percent Buy-Back Exclusion.	This refund provision is good, but not sufficient protection against massive fraud. Read my book.
(IVH) The Earnings Claims Disclosure Will Not Benefit Consumers.	It is hard to see how even former FTC Chairman-turned-lobbyist, Muris can defend this view. Read chapters 2 and 7.
Numbers 88-93 are “issues of fact” to argue that an earnings claim will not benefit consumers.	Read chapter 7 to see the fallacy of these arguments. Based on data provided by MLM companies that publish average earnings of participants, approximately 99.7% of participants lose money, or 99.99% if TOPPs (top-of-the-pyramid promoters) are left out because they skew statistics significantly. The odds of profiting from a single roll of the dice at craps in Las Vegas are many times the likelihood of profiting from joining any MLM after the first ones to join establish their positions atop their pyramids, or downlines.
V. CONCLUSION: THE ISSUES CONNECTED WITH THE PROPOSED RULE ARE NOT SUFFICIENTLY DEVELOPED TO ALLOW FOR A FAIR, EFFICIENT RULEMAKING PROCESS	<p>For all of the above reasons, this concluding statement is patently false.</p> <p>I must say that Muris does nothing to contribute to the fairness of the rulemaking process by his influence over the staff, one of whom – Lois Greisman – was his assistant when he was FTC Chairman. He was obviously working with the DSA in its \$4 million lobbying campaign.</p> <p>It should also be noted that Muris was appointed Chairman by George Bush after his close victory in the 2000 presidential election. It is likely that Bush would not have been elected were it not for the Amway family, his second largest financial supporter.</p> <p>Bush thanked the Amway family by appointing as Chairman of the FTC the head of the Amway legal team - who was none other than Timothy Muris. From that time on, Virtually all actions against product-based pyramid schemes came to a halt. So – Timothy Muris went from fraud protection to consumer protection and back to fraud protection. This is a person we once trusted to head the nation’s “consumer watchdog” – the Federal Trade Commission.</p>

Congress weighed in on BOR – after campaign donations from MLMs and an implied huge voting block as an incentive to help exempt MLM

The DSA lobbied Members of Congress to oppose “direct selling” inclusion in the Rule.
 1st set of comment letters from Congressmen – 109 pages (sample letter on next page)

2nd “ ” ” ” “ from Congressmen – 35 pages

Set of comments from Senators – 30 pages

To view comments, use links or URLs below – or the following pdf files:

Senators-FTC-BOR-071212

<http://www.ftc.gov/os/comments/businessopprule/congress/071212crapoetalbizop.pdf>

Representatives-FTC-BOR-07112

<http://www.ftc.gov/os/comments/businessopprule/congress/071204sessionsetalbizop.pdf>

<http://www.ftc.gov/os/comments/businessopprule/congress/071129scottetalbizop.pdf>

RepesMatheson-FTC-BOR071030

Repes-Alexander-Corker-FTC-BOR-071213

178 FTC Matter No.: R511993 16 CFR Part 437 Notice of Proposed Rulemaking: Business Opportunity Rule

Comments From and Letters to Members of Congress

- **Representatives** Pete Sessions, Gary Ackerman, Jeb Hensarling, Mike Rogers, Artur Davis, Ralph Hall, Gregory Meeks, Howard Coble, Carolyn Maloney, Mark Souder, Edolphus Towns, Elijah Cummings, Melvin Watt, Albert Wynn, Eliot Engel, Vernon Ehlers, Paul Brown, Neil Abercrombie, Robert Aderholt, Lincoln Diaz-Balart, Michael Simpson, Lynn Westmorland, Michael Burgess, Mark Steven Kirk, Kenny Marchant, Mike Conaway, Marsha Blackburn, Bill Sali, Tom Price, John Culberson, John Carter, Tom Feeney, Tom Cole, Sue Myrick, Ron Paul, Joe Wilson, Luis Fortuno, Steve Chabot, Mike Pence, William Delahunt, Danny Davis, Eric Cantor, Dan Boren, Mary Bono, Jo Bonner, Gerald Weller, Spencer Bachus, Rob Bishop, John Shimkus, Darrell Issa, Zach Wamp, and Roy Blunt
 (URL- www.ftc.gov/os/comments/businessopprule/congress/071204sessionsetalbizop.pdf)
 - **Senators** Michael Crapo, Richard Shelby, George Voinovich, Orrin Hatch, Elizabeth Dole, John McCain, Saxby Chambliss, Richard Burr, James Inhofe, Johnny Isakson, Kay Bailey Hutchison, John Cornyn, Tom Coburn, and Larry Craig
 - **Representatives** David Scott, Albert Wynn, Barbara Lee, Corrine Brown, John Lewis, Eleanor Holmes Norton, Eddie Johnson, Gregory Meeks, Danny Davis, Elijah Cummings, Melvin Watt, Carolyn Kilpatrick, Yvette Clarke, Emanuel Cleaver, Donna Christiansen, and Laura Richardson
 - **Senator** Mel Martinez
 - **Representative** Jim Matheson
 - **Senators** Lamar Alexander and Bob Corker
-

**Sample letter from the Congress of the United States
Washington, D.C. 20315**

November 16, 2007

Deborah Platt Majoras, Chairnan
Federal Trade Commission 600
Pennsylvania Avenue, NW
Washington, DC 20580

RE: Business Opportunity Rule (R511993)

Dear Madam Chairnan:

, the undersigned members of the United States House of Representatives, write to express our concern regarding the Federal Trade Commission's (FTC) proposed Business Opportunity Rule.

As Members of Congress and representatives of the American people, we recognize the FTC's important consumer protection role. Like you, we are committed to protecting the public from unfair and deceptive business practices.

In response to the proposed Business Opportunity Rule, the American public submitted more than 17 000 comments to the FTC. It is our understanding that the vast majority of Americans who commented were opposed to the rule as presently proposed. We are also troubled by the potential for this proposed rule to over-regulate legitimate business activities.

It appears to us that the proposed rule is too broad. It has the potential to harm many existing, long-standing, legitimate companies, and to impair the ability of many Americans to engage in legitimate business opportunities. Specifically, we are troubled that the proposed Business Opportunity Rule would severely restrict the legitimate activities of American businesses including direct selling companies.

We strongly encourage the FTC to work with potentially affected individuals and business groups to develop an alternative proposal that achieves the FTC's desired goals, while not adversely affecting legitimate business ventures. We appreciate your consideration.

Sincerely,

List of signatories —

Cc: Commissioner Pamela Jones Harbour, Commissioner
Jon Leibowitz Commissioner
William E. Kovacic Commissioner
J. Thomas Rosch

[For the full list of Senators and Representatives who signed on to this DSA-initiated comment, go to – www.ftc.gov/os/publiccomments.shtm – and scroll down to #178.]

On March 18, 2008, the FTC announced its Revised Proposed Business Opportunity Rule (RPBOR):

News release and Federal Register

243; 16 C.F.R. Part 437; Matter No.: R511993; Business Opportunity Rule: Revised Notice of Proposed Rulemaking

[Public Comments and Rebuttal Comments](#)

[News Release](#) (March 18, 2008)

For Your Information: March 18, 2008

FTC Approves Federal Register Notice Seeking Comments on Revised Proposed Business Opportunity Rule

Commission approval of Federal Register notice: The Commission has approved the publication of a Federal Register notice seeking comments on a revised proposal for a **new trade regulation rule governing business opportunities**. Dating from 1978, the FTC historically has had a single rule covering two distinct types of offerings: franchises and business opportunity ventures. Many of the very familiar national fast-food restaurants and hotels, for example, are franchises, business opportunity ventures include vending machine routes, rack display operations, and medical billing schemes ventures. These ventures, unlike franchises, typically do not involve the right to use a trademark or other commercial symbol. Nevertheless, they do call for the opportunity seller to provide purchasers with locations for machines, or with accounts, or clients, and have been covered by the Franchise Rule.

In April 2006, the Commission proposed a separate Business Opportunity Rule that would cover just business opportunities ventures. Part of the proposal was to expand coverage to business arrangements that were not formerly covered by the Franchise Rule and to streamline disclosure obligations. (Business opportunities formerly covered by the Franchise Rule remain covered under an interim Business Opportunity Rule.) The revised notice announced today modifies the April 2006 proposal for the Business Opportunity Rule. The revised notice of proposed rulemaking (RNPR) will be published soon and is available now on the FTC's Web site and as a link to this press release.

After evaluating the comments received on the April 2006 notice, the Commission has decided to issue an RNPR that is more narrowly focused than the April 2006 proposal. As proposed now, the Business Opportunity Rule would still cover those schemes currently covered by the interim Business Opportunity Rule, and it would expand coverage to include work-at-home schemes. **The revised proposal, however, would not reach multi-level marketing companies or certain companies that may have been swept inadvertently into scope of the April 2006 proposal. The revised proposed rule also streamlines the requirement to disclose material information by eliminating requirements to disclose the number of cancellations and refund requests that a business opportunity seller receives or the litigation history of sales personnel.**

The Commission will be accepting comments on the RNPR until May 27, 2008. Thereafter, rebuttal comments can be made by June 16, 2008.

The Commission vote approving publication of the notice was 5-0. (FTC File No. R511993; the staff contact is Monica E. Vaca, Bureau of Consumer Protection, 202-326-2245; see related press release dated [April 5, 2006](#).)

Copies of the documents mentioned in this release are available from the FTC's Web site at <http://www.ftc.gov> and from the FTC's Consumer Response Center, Room 130, 600 Pennsylvania Avenue, N.W., Washington, DC 20580. Call toll-free: 1-877-FTC-HELP.

MEDIA CONTACT:

Office of Public Affairs
202-326-2180

Related Documents: 16 C.F.R. Part 437: Business Opportunity Rule: Revised Notice of Proposed Rulemaking To Amend the Trade Regulation Rule To Require Business Opportunity Sellers To Furnish Prospective Purchasers With Specific Information That Is Material To Their Decisions As To Whether To Purchase A Business Opportunity, and That Should Help Prospective Purchasers Identify Fraudulent Offerings.

- [Text of the Federal Register Notice](#)

Relevant excerpts from the Federal Register Notice:

FEDERAL TRADE COMMISSION
16 CFR Part 437, RIN 3084-AB04
Business Opportunity Rule

AGENCY: Federal Trade Commission.

ACTION: Revised Notice of Proposed Rulemaking.

SUMMARY: The Federal Trade Commission (the “Commission” or “FTC”) is publishing a revised Notice of Proposed Rulemaking to amend Part 437, the trade regulation rule governing sale of business opportunities that are not covered by the amended Franchise Rule. The revised proposed Business Opportunity Rule (or “the Rule”) is based upon the comments received in response to an Advance Notice of Proposed Rulemaking (“ANPR”), a Notice of Proposed Rulemaking (“NPRM”), and other information discussed in this notice. The revised proposed Business Opportunity Rule would require business opportunity sellers to furnish prospective purchasers with specific information that is material to the consumer’s decision as to whether to purchase a business opportunity and which should help the purchaser identify fraudulent offerings.

The proposed rule also would prohibit other acts or practices that are unfair or deceptive within the meaning of Section 5 of the Federal Trade Commission Act (the “FTC Act”). . .

SUPPLEMENTARY INFORMATION:

This Revised Notice of Proposed Rulemaking seeks comment on a revised proposed Business Opportunity Rule. In addition to minor wording and punctuation changes to improve clarity, the revised proposed rule modifies the initial proposal in six significant ways:

- It narrows the scope of the proposed Rule to avoid broadly sweeping in sellers of multi-level marketing opportunities, while retaining coverage of those business opportunities sellers historically covered by the FTC’s original Franchise Rule (and by the FTC’s interim Business Opportunity Rule), as well as coverage of sellers of work-at-home schemes;
- It cures a potential overbreadth problem that may have inadvertently swept in companies using traditional product distribution arrangements;
- It eliminates the previously-proposed requirement that a covered business opportunity seller disclose the number of cancellation and refund requests it received;
- It eliminates the requirement to disclose litigation history of certain sales personnel (while retaining the requirement to disclose litigation history of the seller, its principals, officers, directors, and sales managers, as well as any individual who occupies a position or performs a function similar to an officer, director, or sales manager);

- It adds a requirement to include a citation to the Rule in the title of the required disclosure document; and
- It prohibits misrepresenting that the government or any law forbids providing prospects with a list of prior purchasers of a business opportunity.

The Commission invites interested parties to submit data, views, and arguments on the proposed Business Opportunity Rule and, specifically, on the questions set forth in Section J of this notice. The comment period will remain open until May 27, 2008. To the extent practicable, all comments will be available on the public record and placed on the Commission's website: <http://www.ftc.gov/os/publiccomments.htm>. After the close of the comment period, the record will remain open until June 16, 2008, for rebuttal comments. If necessary, the Commission also will hold hearings with cross-examination and post-hearing rebuttal submissions, as specified in Section 18(c) of the FTC Act, 15 U.S.C. 57a(c). Parties who request a hearing must file a comment in response to this notice and a statement explaining why they believe a hearing is warranted, how they would participate in a hearing, and a summary of their expected testimony, on or before May 27, 2008. Note that because the NPR has been revised, parties interested in a hearing must resubmit their request in comments to this Revised NPR. Parties testifying at a hearing may be subject to cross-examination. For cross-examination or rebuttal to be permitted, interested parties must also file a comment and request to cross-examine or rebut a witness, designating specific facts in dispute and a summary of their expected testimony, on or before June 16, 2008. In lieu of a hearing, the Commission will also consider requests to hold one or more informal public workshop conferences to discuss the issues raised in this notice and comments.

IMPORTANT NOTE: The entire 124-page notice will not be reproduced here. Much of it is a long rehash of the arguments put forth by the DSA, Quixtar (Amway), and former FTC Chairman-turned-lobbyist Timothy Muris as to why MLM ("direct selling") should be exempt from the Rule. Then an effort is made to go through the motions of appearing to carefully craft a useful rule – even though it is essentially meaningless, since by far the most prevalent sellers of "business opportunities" are MLM companies, as well as the most fraudulent – which would be exempt from the Rule. As my book clearly demonstrates, MLM as a business model depends on unlimited recruitment of a whole network of endless chains of recruitment of participants as primary customers. The compensation plans of all of the approximately 500 MLMs I have analyzed (as of this writing) assume an unlimited market, which does not exist in the real world. They also assume virgin markets, which do not exist for long. They are therefore inherently unfair and deceptive – the very type of businesses the FTC was charged to protect against. Worldwide feedback convinces me that MLMs are also extremely viral and predatory. To any independent analyst (not connected to the MLM industry), to exempt MLM from the BOR is nothing short of absurd.

The full notice can be downloaded at – www.ftc.gov/os/2008/03/R511993business.pdf
However, the proposed form for disclosure for business opportunities that are not MLM related, is reproduced on the following page.

APPENDIX A. BUSINESS OPPORTUNITY DISCLOSURES
Required by Federal Trade Commission, 16 C.F.R. Part 437

Seller: [Name] _____ [Address] _____
 [Phone] _____ Salesperson: _____ Date: _____

The following information can help you in deciding whether to buy a business opportunity. Note, however, that no governmental agency has verified the information. To learn more about business opportunities, call the FTC at 1-877-FTC-HELP (877-382-4357) or visit the FTC's website at ftc.gov/bizopps/. Also, check with your state's Attorney General.

Yes No (Either the "YES" or "NO" box must be checked for the following three disclosures)

EARNINGS: The seller or its representatives states or implies, or has stated or implied, a specific level of sales, income, or profit you can make or that current or former purchasers have earned. If so, the information must be set forth in an "Earnings Claims Statement" attached to this page. Read this statement carefully. You may wish to show this information to an advisor or accountant.

LEGAL ACTIONS: The seller or its key personnel involved in the sale of business opportunities have been the subject of a civil or criminal action involving misrepresentation, fraud, securities law violation, or unfair or deceptive practices within the past 10 years. **If so, the seller must attach a list of all such legal actions.**

CANCELLATION OR REFUND POLICY: The seller offers a cancellation or refund policy. **If so, the seller must attach a statement describing its policy.**

REFERENCES: The seller must provide you with contact information for at least 10 of its purchasers located nearest to you (or, if there are fewer than 10, all purchasers). You may wish to contact them to verify the seller's claims. If you buy a business opportunity from the seller, your contact information can be disclosed in the future to other buyers.

	Name	City	State	Zip	Telephone Number
1.					
2.					
3.					
4.					
5.					
6.					
7.					
8.					
9.					
10.					

Received by:

Date

As quoted below, the DSA boasted of influencing (corrupting) the FTC rulemaking process with a \$4 million lobbying campaign for MLMs to continue business unimpeded by BOR

In its April 2008 Industry News, the DSA boasted of its all-out concerted effort to gain the MLM exemption, spending a total of \$4 million to protect the industry from having to provide information damaging to the MLM industry (though helpful to MLM prospects). Its success at getting 17,000 MLM participants to comment impressed the FTC staff, compared to only 187 persons who spoke up for consumers and victims. But note – Since victims seldom complain, 187 comments was actually very good, considering there are only a handful of consumer advocates and victims who dare to speak out on this issue.

And getting 10-15 thousand (non-duplicated and non-forged) comment letters out of as many as 15 million participants in MLM's – or perhaps 1 in 1,000 to whom the appeal went out – is not so good. The FTC staff were unduly impressed.)

One might wonder – were the SEC not in existence, how many publicly-traded companies would write their objections to having to provide detailed reports for investors. But then the number of those who would insist on it would be large also, so this may not be a good comparison. Investors can be very vocal and demanding, whereas MLM victims almost never complain. This is a great protection for a fundamentally fraudulent industry. For reasons for the silence of MLM victims, see Chapters 2 and 9 of my book *Multi-level Marketing Unmasked*.

[Comments inserted by Jon Taylor are highlighted in brackets.]

Excerpts from:

“A United Industry Makes Its Case: FTC Revises Proposed Rule,”

by Brittany Glenn

[Though the article is copyrighted, under the doctrine of “fair use” for the sharing of important information very much in the public interest, I am quoting selected portions to help the reader understand what the DSA is boasting about – and admitting to – in this article. I have highlighted important passages and have added some notes in brackets – JMT]

On March 18, 2008, the Federal Trade Commission issued a revised notice of its proposed Business Opportunity Rule, originally published on April 5, 2006. The good news: Within the 124-page document, the FTC specifically states that legitimate direct selling companies will be exempt from the proposed Rule. The revised Business Opportunity Rule is narrower in scope than the initial Rule, and the FTC straightforwardly asserts, “The revised proposal does not attempt to cover MLMs.”

The industry can exhale—at least temporarily. The process isn't over. The FTC has requested comments to the proposed revised Rule by May 27, 2008, and rebuttal comments by June 16, 2008. . .

The initial proposed Business Opportunity Rule was rife with potential pitfalls for the direct selling industry's companies and distributors. Companies would have needed to provide recruits with lengthy disclosure statements before they joined; impose a seven-day waiting period from the time the activity is presented and the time a prospect joins the business; and disclose the names, addresses and phone numbers of at least 10 sellers of the product. Additionally, an

“earnings claim” was more broadly defined so that a picture or a pay stub could trigger extensive disclosure documents.

Industry Say and Sway

The Direct Selling Association played a key role in eliciting the revised ruling. The effort was spearheaded by DSA’s Business Opportunity Task Force chaired by Michael Lunceford, Senior Vice President of Government Relations for Mary Kay Inc., and the DSA government relations committee, chaired by Josephine Mills, Executive Director of Global Government Affairs for Avon, along with DSA President Neil Offen and Executive Vice President Joseph Mariano.

Companies such as Avon, Herbalife, Mary Kay, Primerica, Quixtar, Shaklee and many others worked very hard to communicate the industry’s perspective to the FTC. Thousands of individual distributors personally wrote to the FTC, asking the commission to consider the consequences that such a rule would have on their home-based businesses. Eighty-four members of Congress also wrote to the FTC to express their concerns about the original Rule. Companies and distributors wrote to the FTC, opposing the original Rule. The FTC received more than 17,000 comments expressing concerns regarding the proposed Rule. Of the 17,000 comments, only 187 supported the initial proposed Rule. . .

The Revised Rule cites the comments of DSA, key company players and individual distributors.

The response that the proposed Rule elicited must have been somewhat overwhelming, but—to the commission’s credit—the FTC carefully considered every word spoken or written. In the revised Rule, the FTC writes, “The Commission believes the proposed Rule is too blunt of an instrument to cure fraud in the MLM industry. The Commission has determined that it will use the flexibility inherent in Section 5 of the FTC Act to address particular frauds in the MLM industry.”

Lunceford, having been a lobbyist for nearly 35 years—27 of those years with Mary Kay—notes the revised Rule is “remarkably different” from the original. “We’re quite pleased,” he says. “This [revised Rule] is a striking development. The FTC is truly saying the right things. The commission made it abundantly clear that it was exempting direct selling companies from the Rule. .

. [“The FTC is truly saying the right things.” This is an excellent example of “Regulatory capture.” – JMT]

Kudos aside, however, the rulemaking procedure is still in process. At this point, nothing is written in stone. . . .

Strategic Alliances

The DSA submitted comments to the FTC in July 2006, followed by supplemental comments in the fall of that year. *“Our strategy was to make certain key points in our comments and ask individual companies to write about the points that were important to them, but also deliver an overall cohesive message,”* Mariano says.

Both Avon’s Mills and Mary Kay’s Lunceford worked very closely with the DSA to coordinate their strategies. *“Avon participated in Congressional visits with DSA member companies and worked with the DSA to develop strategic initiatives in the event that the Rule was not revised,”* Mills says.

Mills describes the work accomplished by the DSA staff and government relations committee. *“The government relations committee visited with the FTC to discuss its intent, what led to such a proposal and why it felt such a proposal was necessary,”* she says.

[These communications were not disclosed in response to an FOIA request we made to the FTC. – JMT]

“The committee met with Congressional members to gain their support and coordinated efforts with members of other associations, member companies and individual direct sellers. In fact, the DSA government relations and communications committees coordinated production of a video of a group of direct sellers, including Avon representatives, discussing how the proposed Business Opportunity Rule would impact their businesses.”

*Mariano says the DSA and certain industry companies retained experts on “substantive areas of the rulemaking process and procedure”— **including former FTC commissioners.** [Former FTC Chairman-turned lobbyist Timothy Muris, for one – JMT]*

***“These rulemaking experts also helped us develop arguments that would be the most helpful to the FTC in accomplishing their goals of dealing with business opportunity fraud while protecting our interests as legitimate direct sellers,”** he says.*

Stock Talk

On March 20, 2008—two days after the revised Rule was announced—the investment banking firm Canaccord Adams released a flash update titled, “Sunny Skies for Direct Selling,” written by Scott Van Winkle, CFA, and Diederik Basch, CFA. Van Winkle is Managing Director of Equity Research—i.e., a stock analyst—for Canaccord Adams. . . .

The flash update reads, “While we expected that the Business Opportunity Rule would be revised, the proposed revisions are more favorable than we expected.... [a victory for the DSA/MLM lobby, but a huge setback for consumers as targeted prospects] We view the revisions to the Business Opportunity Rule as a significant positive for the channel and the stocks, which have been outperforming the broader market.”

According to Van Winkle, when the initial proposed Business Opportunity Rule was introduced in April 2006, stock prices dipped for publicly traded direct selling companies. “There was definitely an impact on investor confidence,” he says. *“Following the issuance of the FTC’s proposal, there was some negative media attention. Every time media attention comes out with a negative outlook for certain stocks, they usually dip.”* . . .

Did stock prices jump after the FTC announced its revised proposed Business Opportunity Rule? Surprisingly, no. Not yet, anyway. “I thought there would be a little more of a ‘relief rally,’” admits Van Winkle. “But I think it’s hard to measure some of this in the near term. *When investors consider potential investments, they go through a laundry list of opportunities and risks. In the future, when investors go through their list, there will be one less risk for direct selling companies. So there are long-term ramifications of this revised Rule.*”

[One less risk for MLMs, but one more risk for prospective recruits, 99% of whom lose money. See Chapter 7 of my book Multi-level Marketing Unmasked – JMT]

United Front

DSA President and CEO Neil Offen is very pleased at this latest turn of events and proud of the industry’s concerted efforts. “It is almost unprecedented what the FTC has done,” Offen says. *“The commission has tried to accommodate our industry completely. I am convinced that our industry will not be covered by this Rule. This is a great victory for the DSA, the team that worked on this and—most of all—the industry.*

Mariano agrees that Primerica brought significant resources to the table.

[For example, former FTC Chairman-turned lobbyist Timothy Muris – JMT]

“Mary Kay, Avon and Shaklee too had a big impact on the thinking of the commission,” he adds. “Shaklee probably had more individual distributors write to the FTC than any other company. Other companies submitted comments, such as Quixtar and Herbalife—both corporately and through members of their salesforce. It was a team effort.”

And what a team it was. “We had a task force with 15 companies represented on it and about 25 executives who participated in the process,” Mariano says. “We also worked with the

Government Relations Committee, which comprises more than 50 companies and about 70 executives.

“Many companies brought unique perspectives and contributions to this effort, whether it was with congressional contacts, substantive development of the arguments or leadership in communicating the issues to their field,” Mariano says. “There’s plenty of credit to be spread around.”

Big Bucks

Offen estimates that *among the DSA and the industry companies that hired outside counsel, economic consulting firms and other experts, more than \$4 million was spent to address the proposed Rule.*

[The very fact that they would spend so much money and effort on protecting MLM recruiters from disclosing information to help consumers make a wise decision and from allowing a think-it-over period should tell you something – JMT]

“Deborah T. Ashford, a partner at Hogan & Hartson, is our general counsel, and their assistance was absolutely critical to our success” Mariano says. “Their assistance was invaluable in this process—and will continue to be, I suspect.”

Congress Weighs In

In 2006, 50 members of Congress wrote to the FTC to express their serious concerns about the adverse impact the proposed Rule could have on direct sellers. In 2008, 84 members of Congress, on both sides of the aisle, signed a second letter on behalf of direct sellers.

“I think it’s a seal of approval on our industry that 15 percent of Congress members weighed in on our behalf,” Offen says.

[Political contributions and touting of a large voting block helps! – JMT]

Mariano says the DSA had a crucial advantage when communicating with members of Congress: “The fact is, the merits were on our side,” he says. “We know who we are; we know what the problems with the Rule were and why the Rule shouldn’t have applied to direct sellers. When we went to Capitol Hill and asked members of Congress from both the House of Representatives and the Senate to express their interest and concern on our behalf, it was merely a matter of laying out the merits of our case.

“We told members of Congress that we represent more than 15 million people who’ve sold products for the direct selling industry,” Mariano continues. “A number of our member companies and their facilities were located in their districts. On average, there are about 35,000 people involved with direct selling companies per congressional district and even more who are customers.”

[Most of those 15 million (and 35,000 local) are actually victims suffering losses.²⁶ – JMT]

Additionally, *several companies had key contacts with members of Congress as good corporate citizens.* “Their elected representatives know who they are and, by virtue of their good government relations work and presence in their communities, we were able to take advantage of these preexisting relationships,” Mariano says.

Not Over ’Til It’s Over

As mentioned earlier, the rulemaking process is not over. “The FTC has taken a huge step in the right direction to address the concerns of the direct selling industry,” Mariano says. “However, there are still a number of steps to undertake before this process is finished. It’s not that we aren’t happy and satisfied with the revised proposed Business Opportunity Rule, but keep in mind that it is just that—proposed. The process is open until it’s closed. There’s always the possibility for changes in the specifics of the Rule.

²⁶ Op.cit., Chapter 7.

“The process will continue for at least another number of months and conceivably much longer than that,” Mariano says. “We are now in an ‘open comment’ period for revisions until May. Then a rebuttal period takes effect at the beginning of July. There’s the possibility of workshops or hearings, and then there’s the final consideration by the Federal Trade Commissioners themselves. So we’re looking at the fall of 2008 at the earliest for finalization of this Rule.”

Lunceford shares Mariano’s caution. *“I think we can declare victory once we see the final Rule,”* he says.

Mills is also circumspect in assessing the future. “There is no guarantee that the final rulemaking will take effect exactly as worded now, but *we feel confident—based on the number of times the FTC quoted comments made by the DSA, Avon and other companies—that the FTC understands the direct selling industry,*” she says. “We believe the FTC is communicating in good faith when it states that it does not intend for the revised proposal to impact legitimate direct selling companies.”

However, there will be changes in the language of the Rule, Mariano believes. Changes that will affect the industry? “We can’t know that until we see the language,” he says. “You’ve heard the expression, ‘the devil is in the details.’ In this case, the details are the specific words of the proposal.”

Shared Mission

Offen reminds the industry that *the DSA shares a mission in common with the FTC—to rid the marketplace of pyramid schemes and bad actors that pose as direct selling companies.* “We’ve had a very good relationship with the FTC in the past, and we’ll have an even closer relationship in the future,” Offen says. *“We share the desire to protect consumers of our products and opportunity.”*

[Does any informed person believe him when he says these things? Read Chapters 2 and 7-11 – JMT]

Mills agrees. “The FTC’s open communication has been critical in this matter,” she says. *“It appears the FTC spent a tremendous amount of time on this matter in both drafting the initial proposal and then meeting with the DSA and individual companies to hear our concerns and better understand our business models.* It is apparent that the FTC painstakingly reviewed the 17,000 comments from interested parties, including companies and individual direct sellers, after which the commission drafted the revised proposal. The revised Rule will enable the FTC to accomplish its initial goal of protecting consumers from outright scams without overburdening law-abiding legitimate direct selling companies or millions of individual direct sellers.”

“In essence the FTC said [in its revised proposed Rule], ‘While we’re rejecting the proposed Rule because it’s unnecessary and over-burdensome for legitimate companies, we affirm the ability and the need to go after any wrongdoers of Section 5,’ ” Mariano says. *“The DSA could not be more supportive of that. We share a common interest with the FTC to eliminate bad actors in the marketplace.”*

[Wrongdoers? Bad actors in the marketplace? It’s endemic in such a flawed industry. Read Chapter 2 of my book Multi-level Marketing Unmasked – JMT]

The DSA will continue to keep a vigilant eye on the rulemaking process. In the meantime, it appears that “sunny skies for direct selling” do indeed lie ahead. *[Sunny skies for MLMs, but dark skies for consumers who were given to understand that the FTC was acting to protect against (or help prevent, rather than facilitate) unfair and deceptive practices. – JMT]*

**Terse – and highly appropriate – comments about RPBOR
by Dr. Stephen Barrett.**

Comment Number: 535221-00063
Received: 5/27/2008 8:23:55 PM
Organization: Quackwatch
Commenter: Stephen Barrett
State: NC
Agency: Federal Trade Commission
Rule: Business Opportunity Rule
No Attachments

Comments:

I have followed the MLM marketplace for nearly 30 years and examined the offerings of hundreds of MLM companies. I am shocked and disappointed that the FTC has decided to exclude MLMs from the Business Opportunity Rule. More people are affected by misleading MLM claims than by any other type of health product marketing. The vast majority of newly recruited MLM distributors do not make significant income, a fact that MLM recruiters do not disclose. In addition, few if any health-related products have a legitimate market because they provide no significant benefit, are grossly overpriced, or both. Meaningful disclosure, which might deter millions of people each year from wasting their time and money by signing up as distributors, would cost very little. Moreover, the FTC lacks both the willingness or the resources to attack misleading claims by hundreds of companies on a case-by-case basis. I notice, by the way, that although the FTC's analysis responded to every other comment that I saw, it did not mention or respond to my original comments about the basically fraudulent nature of the MLM industry.

Comments about RPBOR by the Dr. Jon Taylor, who had provided extensive information about MLM fraud and supporting research – research the FTC staff chose to dismiss

Comment Number: 535221-00006
Received: 5/15/2008 6:50:40 PM
Organization: CONSUMER AWARENESS INSTITUTE - & PSA
Commenter: Jon Taylor
State: UT
Agency: Federal Trade Commission
Rule: Business Opportunity Rule
Attachments: [535221-00006.pdf](#) [Download Adobe Reader](#)

Comments:

ATTN: FTC officials: Please read carefully the attached comments regarding the Revised Business Opportunity Rule. Also, my comments submitted as rebuttals to the original Rule are a summary of thousands of pages of research and feedback from all over the world. So I would suggest you read those again as well. In the attached comments, together with information on my web site (www.mlm-thetruth.com) I have provided good evidence to suggest the wisdom of scrapping any revised Business Opportunity Rule that exempts MLM (multi-level marketing) from compliance with the Rule. Such an exemption would only serve to encourage MLM promoters to continue even more blatant fraud against consumers who may be considering any MLM program that depends for its very existence on a complex set of deceptions to survive and grow. And as explained, replacing meaningful disclosure with the use of Section 5 is not a step forward. Section 5 has been used only very sparingly in such cases, and the FTC does not have the manpower or other resources to investigate the hundreds of fraudulent MLMs we have observed. A rule requiring meaningful disclosure for all MLMs would be much more cost effective and realistic. I understand the enormous pressure placed upon you by the DSA, its member firms, and Congressmen who are beholden to them. But the very integrity of our free market system is at stake, to say nothing of the financial well-being of millions of people who are struggling to find some way to supplement their income – without being ripped off by one of the hundreds of MLM/pyramid or chain selling schemes that are actively recruiting. No rule, is better than a bad rule - or a rule that leads consumers to believe they have some protection, when in fact they are left exposed to the worst schemes. The FTC has a mission to prevent fraud, deception, and unfair business practices in the marketplace. A Business Opportunity Rule that exempts MLM is an abrogation of that mission. It would be far better to scrap the Rule altogether, and start afresh when a consumer friendly (as opposed to anti-regulatory) political climate that allows you enact a rule consistent with the FTC's mission. Sincerely, Jon M. Taylor, MBA, Ph.D., President, Consumer Awareness Institute, and Advisor, Pyramid Scheme Alert

Serious Problems with the Revised Business Opportunity Rule

A setback for consumers. The March announcement by the FTC that a revised Business Opportunity Rule would exempt multi-level marketing programs is a tragic setback for consumers, a stark capitulation to the MLM (multi-level marketing) industry lobbied by its lobby the DSA (Direct Selling Association), and a reversal of course by the FTC in carrying out its mission to protect consumers from unfair trade practices. Instead, officials have chosen to yield to political pressures and exempt the worst of all classes of fraudulent “business opportunities.”

Section 5 not much protection. Falling back on Section 5 of the FTC Act to deal with unfair and deceptive practices offers no assurance to consumer advocates that things will improve. Since the 1979 finding by an FTC judge that Amway was not a pyramid scheme - subject to “rules” an emphasis on retail sales - thousands of MLMs have come and gone, and several hundred remain. Tens of millions have been victimized worldwide, experiencing hundreds of billions of dollars in aggregate losses worldwide. Let me explain how I come up with these numbers.

MLMs based on 30 typical misrepresentations. From 14 years of research and consumer advocacy, I have identified 30 typical misrepresentations used in MLM recruitment campaigns (see Appendix A). That means that virtually every recruit into an MLM program is a victim to the degree that he/she purchased products based on these deceptions. This is why a rule requiring meaningful disclosure is such an important protection for consumers.

Why the silence of MLM victims. The original Business Opportunity Rule proposal reported that in 2005, the FTC had received 17,858 complaints, placing it consistently among the leading categories of complaints. Actually, this is a gross underestimate of the harm by MLM. These statistics fail to recognize that victims of endless chain selling (a key feature of MLMs) programs almost never file complaints – less than one in a thousand victims, based on my research. Why? Primarily fear of self-incrimination and fear of consequences from or to those in their upline or downline –those they recruited or who recruited them, which is often close friends and relatives. And many blame themselves for their losses, as they are taught that failure is their fault for not “working the system.”

Another reason for the silence of victims is the inaction of law enforcement. Recruits are told that if the program was an illegal pyramid scheme, it would have been stopped long ago. But in law enforcement, the squeaky wheel gets the grease. So no complaints – no action by law enforcement; and conversely, no action - no complaints. It’s a vicious cycle.

Amount of MLM damage underestimated. To be on the safe side, multiply 17,858 complaints by 500 to get the minimum number of victims, and you get 8,929,000 victims per year – almost nine million who bought MLM products based on at least some of the typical misrepresentations. Almost nine million! I believe this is not an exaggeration, since the DSA reported 15.2 million persons engaged in “direct sales” in 2006, most of them doing MLM and nearly all exposed to similar deceptions when recruited.

Then multiply the \$46 million dollars in damages reported by the FTC in 2005 by a factor of at least 500, and you get \$23 billion in participant losses per year, which I feel is a realistic minimum since the DSA reported \$32 billion in “direct sales” in 2006 (most from MLM). Multiply a more conservative average of \$10 billion by 20 years, and you have a minimum of over \$200 billion in MLM participant losses worldwide just in the last 20 years. These estimates (or even a tenth of them) would easily place MLM fraud far above all classes of business opportunity fraud combined.

History of FTC use of Section 5. As to the FTC assurance that officials can use Section 5 to deal with unfair and deceptive practices, let’s look at the history. Those of us who have studied MLMs for many years know that the number of MLMs that have come and gone number in the thousands. This means that less than 1% of product-based pyramid schemes have been prosecuted by the FTC. Does the FTC have the resources to go after thousands of fraudulent MLMs? Even the several hundred that have managed to survive?

A proven model for differentiating legitimate direct selling from fraudulent recruiting MLMs. After years of research, including consultation with the top experts in the field (not financed by the MLM industry), I developed a model for differentiating legitimate direct selling programs from clearly exploitive recruiting MLMs (that reward recruitment over retail sales) or product-based pyramid schemes. A summary version of the report – “FIVE RED FLAGS: five causative and defining characteristics of recruiting MLMs, or product-based pyramid schemes” – was presented to the Economic Crime Summit Conferences in 2002 and 2004.

This model has been tested by applying it to all the MLMs for which data on average income of participants was available. In every case, when all five red flags was found in an MLM compensation plan (and is found in nearly all MLMs), the percentage of participants losing money is approximately 99%. When ALL participants were counted and costs of required purchases (to qualify for commissions and advancement up the pay levels) and minimal operating expenses were subtracted, the loss rate is closer to 99.9%. This kind of information should be disclosed. If a disclosure rule were needed for anything, this is it.

Can Section 5 be used for hundreds of MLMs? I have studied the compensation plans of over 250 MLMs (see the list in Appendix C) and find that all of them display these five factors that cause the harm and that clearly separate them from legitimate business opportunities. All of these should either be regulated by a Rule requiring disclosure of crucial information for making a decision, including average income data and attrition rates, or they should be investigated by the FTC. Officials should not wait for a large number of complaints to come in, as by that time enormous damage will be suffered by participants.

Does the FTC have the resources to investigate 250 MLM programs that can be alleged to be illegal pyramid schemes? Not if FTC enforcement history is any indication. A Business Opportunity Rule that requires meaningful disclosure would be far more manageable.

The revised Rule is meaningless. So to what does the revised Business Opportunity Rule apply, if MLM is exempt? Vending machines? Work from home envelope stuffing? Car wash packages? These kinds of opportunities may have been a problem decades ago, but as one who has followed the business opportunity field for 35 years, I can tell you that these kinds of activities are all trivial compared to fraudulent MLM schemes today.

Better to scrap the Rule altogether than have a rule exempting MLM. Based on the foregoing, my strong recommendation would be that if MLM is exempt from the Rule it would be best to scrap the proposed Business Opportunity Rule altogether. A bad rule or an empty rule is worse than no rule at all. Here’s why:

Based on observing their prior behavior, MLM promoters, including DSA spokesmen, will find ways to turn this revised Rule to their advantage. They will likely say that MLM was not included in the Business Opportunity Rule because MLM is legal and that their programs are not pyramid schemes, but legitimate “direct selling” opportunities. And they will continue to defraud a revolving door of victims in an endless chain of recruitment

For more information backing up these claims, I would refer the reader both to the law enforcement page of my web site (www.mlm-thetruth.com), that summarizes thousands of pages of research and feedback from all over the world, and to my [rebuttal comments](#) on the FTC web site. For a more updated list of misrepresentations used in MLM recruitment, read Chapter 8 of my book *Multi-level Marketing Unmasked*, and for an updated discussion of the “5 Red Flags,” read Chapter 2.

Received: 5/27/2008 6:14:08 PM
Organization: CONSUMER AWARENESS INSTITUTE - & PSA
Commenter: Jon Taylor
State: UT
Agency: Federal Trade Commission
Rule: Business Opportunity Rule
Attachments: [535221-00057.pdf](#) [Download Adobe Reader](#)

Comments:

Please read the attached statistics and reasons for setting aside the Revised Business Opportunity Rule.

WHY THE FTC'S REVISED PROPOSED BUSINESS OPPORTUNITY RULE SHOULD BE SET ASIDE

By Jon M. Taylor, MBA, PhD, President, Consumer Awareness Institute
and Advisor, Pyramid Scheme Alert

Response to the Initial Proposed Business Opportunity Rule (IPBOR). The Direct Selling Association (DSA), which has been taken over by multi-level marketing companies (MLMs), responded to the IPBOR by sending appeals with content suggestions or form letters that could be accessed by at least 17 million participants (what they call “direct sellers”) in MLMs’ endless chains and recruitment pyramids. However, only 17,000 responded, or less than 1 in 1,000! Those who commented claimed the Rule would impose an unnecessary burden upon them, which of course is not true, as the MLMs could with the press of a few keys on their computers access that data and circulate it to the participants in their respective schemes. MLM participants also claimed the Rule would threaten their livelihoods, although we have evidence that less than 1% of all participants (including dropouts) in MLM earn a profit (after subtracting purchases necessary to qualify for commissions, minimal operating expenses, etc.)

Also, the DSA was able to get 86 Senators and Congressmen to parrot their objections to the Rule on behalf of their “constituents.” I lack the time to check the contribution records of all the candidates, but I do know that candidates in Utah have received substantial political contributions from MLM companies and officials, not to mention implied votes from a huge population of participants. The millions of dollars in aggregate campaign dollars donated by these MLMs may have been their best investment yet. Had the Rule gone through, requiring MLMs to disclose information on abysmal average earnings (high loss rates) by participants, heavy attrition rates, etc., many MLMs would have folded due to lack of recruits, who were their primary customers – though most would likely find ways to obfuscate the information to confuse and mislead consumers.

And even more incredible are the comments from former high level FTC officials objecting to the Rule on behalf of MLMs –

- Timothy Muris, former FTC Chairman, for Primerica;
- J. Howard Beales III, former Director of the Div. of Consumer Enforcement, also for Primerica; and
- Jodie Bernstein, former Director of Consumer Protection, for Quixtar (Amway).

One can only imagine what they are paid to lobby or write on behalf of these MLMs. It is disturbing to us consumer advocates to see such officials move so readily from consumer protection to fraud protection by opposing rules to protect consumers!

The IBOR was supported by consumer advocates who, with no financial stake in the outcome and lacking funds to influence politicians, were hopelessly outnumbered by MLM defenders. So the FTC yielded to the DSA/MLM lobby and exempted MLM from its proposed Rule – a huge setback for consumers looking to the FTC for protection.

So what would the Revised Rule cover? The March 18 FTC announcement suggested the Rule would now apply to such business opportunities as vending machine routes, rack display operations, and medical billing opportunities. While such programs may have been a problem 20 or 30 years ago when I was following such options, today they are miniscule in comparison to MLM fraud. An advanced Google search pairing “fraud” with “MLM” and then compared with these options turned up 223 times as many web sites for MLM fraud as for these other packaged business opportunities combined. All other classes of business opportunity fraud fade into insignificance compared to MLM fraud, which easily exceeds all the rest combined. In other words, by far the top category of business opportunity fraud would be exempt from the Revised Business Opportunity Rule – which begs the question: Why have a Business Opportunity Rule at all, if MLM is excluded?

Can the FTC afford to fall back on Section 5 for MLM fraud? The revised Rule announcement includes the statement: “The Commission, therefore, has determined that at this point, it will continue to use Section 5 to challenge unfair and deceptive acts or practices in the MLM industry.” However, it appears that since 1990, the FTC has prosecuted only 14 MLM cases and investigated several more – less than 50 overall. This is out of well over 2,000 MLM companies that have sprouted up since the 1979 Amway decision – many of them now defunct – but having left behind literally tens of millions of victims and hundreds of billions in participant losses worldwide. These numbers assume that nearly all MLM participants fall prey to at least some of the 30 typical misrepresentations used in MLM recruitment campaigns –and are to that extent classified as “victims.”

The MLM model of infinite expansion in finite markets is inherently flawed, uneconomic, and fraudulent. As can be demonstrated by recent research, the fundamental nature of the MLM business model leads them to engage in a complex set of deceptions. Yet several hundred MLMs exist today. At the present time, my research shows that at least 250 MLMs are engaging in unfair and deceptive acts or practices, as they must if they are to survive and grow. This is the real reason for the extreme reaction against IPBOR by MLM defenders, who have a lot to lose if true information about them were disclosed. They have everything to gain by concealing the truth.

But based on history of FTC actions over the past three decades, reliance upon Section 5 offers no real assurance of protection for consumers. If a minimum of 250 MLMs are simultaneously engaging in similar patterns of unfair and deceptive acts or practices (which our evidence shows), is it fair to single out two or three to go after? On the other hand, does the FTC have the resources in time, manpower, funds, and prosecutorial will to take on hundreds and perhaps thousands of MLMs simultaneously? A uniform disclosure rule would be much more cost effective.

MLM is the biggest scam facing consumers today. Because of its endless chain of recruitment, MLM is predatory and viral, like a fast-growing cancer. For details on MLM’s inherent flaws, see my comments #535221-00006 (dated 5-15-8), as well as my rebuttal comments for IPBOR. Or go to the Law Enforcement page at our web sites at www.mlm-thetruth.com, where you will find details on why MLM victims remain silent and why MLM is under-regulated and its fraudulent practices

underestimated by the FTC and by the states that harbor MLMs. See also www.pyramidschemealert.org.

Terrible unintended worldwide consequences of inaction against MLM. One of the saddest consequences from the FTC's caving in to the MLM/DSA lobby is that states are left without the national leadership they sorely need. The DSA/MLM lobby has been going from state to state to systematically weaken their statutes protecting consumers against predatory pyramid and chain selling schemes.

In Utah, for example, the DSA crafted a bill exempting "direct selling" programs from prosecution as pyramid schemes, provided the program offered consumable products "to anyone." I testified that there must be sales to "non-participants" for it not to be a pyramid scheme. Both DSA and MLM representatives blatantly lied about the purpose of the bill (calling it the "Direct Sales Amendment" when it was clearly written to allow unmitigated chain selling) and the position of the FTC about "internal consumption." At the hearings, the legislators asked the Attorney General, Mark Shurtleff, what he thought. He said the bill was designed to protect "against the worst schemes – those without legitimate products." I testified that product-based pyramid schemes were the worst by any measure – loss rates, aggregate losses, and number of victims. His testimony as the state's top law enforcement officer prevailed, but he failed to disclose that his top corporate campaign contributors were the very MLMs who would benefit. Since 2002, he has received at least \$231,000 from various MLMs (including \$110,000 from one MLM) – plus additional money from MLM founders.

Our appeal to Utah's *Governor Huntsman to veto the bill was ignored; he too had received substantial donations from some of the many MLMs based in Utah. Governor Huntsman even used his Chinese contacts (having been a trade representative for the White House) to campaign for the relaxing of the ban on MLM in China.* No wonder Utah is so soft on MLM.

As if that weren't enough, we have received feedback from concerned consumers and officials in countries in Asia and throughout the world, of US-based MLMs that are literally plundering the most vulnerable of their people of their precious resources. Many of these people can barely afford food, and when they purchase the expensive products they must subscribe to on a monthly basis in order to participate in what is presented as their "passport to financial freedom," they are nearly always left more impoverished than before they joined the "opportunity." Law enforcement in most of these countries is even less prepared to deal with this class of fraud than are officials and legislators in the U.S. Many lean on the FTC, assuming that as our national consumer protection agency, the FTC would not allow outright scams to proliferate and expand beyond our borders.

Should the FTC initiate a Rule that is specific to MLM? Obviously, this would be the ideal solution. It should require average income information (including average money paid to the MLM, compared with average money rebated to participants, using comparable percentiles), terminations or dropouts as well as "successes" within the same time period, and other information essential to a good decision on whether or not to participate. The horrible loss rates for participants in all these "recruiting MLMs" could be a warning to every thinking person to avoid them like a plague. But considering what just happened with IPBOR, one should not be optimistic that such could ever occur. MLM promoters would again scream bloody murder – all the arguments thrown up against IPBOR – and then some. One can picture as many as 50,000 comments objecting to an MLM-specific Rule and letters from 100 Congressmen and Senators, even if the DSA and MLMs had to pony up several million dollars more in campaign contributions. Plus one would expect fat offers to additional departing FTC officials to lobby against such honest disclosure.

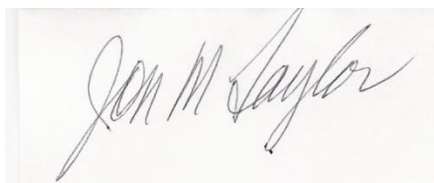
What is the best course of action for the FTC now? In retrospect, had the FTC in 1979 been privy to the analytical research based on data available today (assuming an impartial trial), Amway would certainly have been adjudged to be an illegal pyramid scheme, and pyramid and chain selling (a.k.a., MLM) could have been stopped or severely limited. But Amway was given a pass, and recruiting MLMs, or product-based pyramid schemes, have proliferated to a total of thousands of such schemes, hundreds still thriving. It may be too late to restore integrity to the direct sales marketplace. Legitimate direct selling can scarcely compete with such blatant fraud, as many consumers lack the sophistication to discern the difference between legitimate direct selling and pyramid or chain selling.

Going ahead with a Revised Business Opportunity Rule (exempting MLM) would be a grave disservice to consumers. Knowing the mentality of MLM and DSA spokesmen, such a Rule would play right into their hands. The new mantra in MLM recruitment would be as follows:

“MLM is a legitimate business opportunity, which is obviously why the FTC exempted it from its new Business Opportunity Rule. You can be perfectly safe investing in our program – merely pay the \$30 entry fee – with no profit to the company (followed by a carefully crafted pitch to subscribe to a minimum of \$100 a month in products and services to qualify for commissions, advancement, etc., etc., etc.).”

With this kind of appeal, these MLMs could defraud additional millions of consumers out of additional hundreds of billions of dollars worldwide. Does this jibe with the FTC’s mission to challenge unfair and deceptive acts or practices? This one’s a no-brainer. With MLM exempted, the proposed Business Opportunity Rule should be set aside.

Sincerely,

A handwritten signature in black ink that reads "Jon M. Taylor". The signature is written in a cursive, flowing style.

Jon M. Taylor, Ph.D., President, Consumer Awareness

Institute
and Advisor, Pyramid Scheme Alert
E-mail: jonmtaylor@juno.com

Cogent comments criticizing RPBOR by Robert FitzPatrick (PSA)

For an excellent letter on the fallacies underlying the decision to exempt MLM, read the full report to FTC commissioners, which follows.

Comment Number: 535221-00040
Received: 5/27/2008 3:58:30 PM
Organization: Pyramid Scheme Alert.org
Commenter: Robert FitzPatrick
State: NC
Agency: Federal Trade Commission
Rule: Business Opportunity Rule
Attachments: [535221-00040.pdf](#) [Download Adobe Reader](#)

Comments:

May 27, 2008 To: Members of US Federal Trade Commission From: Robert L. FitzPatrick, Pres. Pyramid Scheme Alert.org As president of Pyramid Scheme Alert, a consumer organization that investigates, analyzes and seeks to prevent pyramid schemes, I urge the FTC to cancel plans to enact the “business opportunity rule” as it is presently proposed. (<http://www.ftc.gov/opa/2008/03/busrule.shtm>). The proposed rule - which now effectively excludes multi-level marketing (MLM) schemes - would be meaningless, a waste of tax money, and useless in its stated purpose of protecting consumers. Whatever value such a rule might have provided the public was eradicated by the Commissioners’ decision to effectively exempt multi-level marketing schemes from its coverage MLM is, by every measure, the largest and most pervasive of all the types of business opportunity schemes. The remaining types that the rule would cover “envelope stuffing, vending machine routes, etc,” are insignificant, uncommon, and have little financial impact. The endless chain scam, sometimes called a Ponzi scheme or pyramid scheme, is the most common and most harmful form of fraud facing consumers today when they seek new business or income opportunities. Multi-level marketing is the most common – almost exclusive – disguise used by Ponzi perpetrators. Consumer losses in the US from these types of business opportunity scams are in the billions each year. There is hardly an American household today that does not have a member who has been solicited or who has lost money and time in a multi-level marketing “business opportunity” scheme that turned out to be an endless chain recruiting/investment scam. The effective exclusion of MLM serves to bolster and protect the worst and most common type of business opportunity fraud. Rather than protecting the public, the revised rule literally provides a safe haven for business opportunity frauds. It may even drive those scams that use other models to now adopt a MLM pay plan in order to gain protection under the rule. The Commission statement that MLMs will be covered by Section 5 of the FTC Act governing “unfair and deceptive practices” is equally meaningless, since the FTC’s record since 2001 in responding to consumer claims and requests for law enforcement against MLM scams reveals a political agenda to shield MLMs from federal law enforcement (see attachment). Respectfully submitted, Robert L. FitzPatrick, Pres. PYRAMID SCHEME ALERT 1800 Camden Rd. Ste. 107, No. 101 Charlotte, NC 28203 rfitzpatrick@pyramidschemealert.org



Robert L. FitzPatrick, Pres.
 PYRAMID SCHEME ALERT
 1800 Camden Rd. Ste. 107 #101
 Charlotte, NC 28203
 704-334-2047

May 26, 2008

Members of the United States Federal Trade Commission:

William E. Kovacic, Chairman
 Pamela Jones Harbour, Commissioner
 Jon Leibowitz, Commissioner
 J. Thomas Rosch, Commissioner

600 Pennsylvania Avenue, NW
 Washington, DC 20580

An Open Letter to the Members of the United States Federal Trade Commission

Re: Decision to Exempt “Multi-Level Marketing” from Proposed Rule to Combat Fraud in “Business Opportunity” Schemes.

Dear Commissioners:

This letter supports my submitted comment that the proposed businesses opportunity rule –which effectively excludes multi-level marketing (MLM) schemes – is meaningless, a waste of tax money, and useless in its stated purpose of protecting consumers. Whatever value such a rule would have provided the public was eradicated by the Commissioners’ decision to exempt multilevel marketing schemes from its coverage (<http://www.ftc.gov/opa/2008/03/busrule.shtm>).

MLM is, by every measure, the largest and most pervasive of all the types of business opportunity schemes. The remaining types that the proposed rule would cover – envelope stuffing, vending machine routes, etc, –are insignificant, uncommon, and have little financial impact. The exclusion of MLM serves to bolster and protect the worst and most common type of business opportunity fraud. Rather than protecting the public, the revised rule literally provides a safe haven for business opportunity schemes. It may even drive those scams that use other models to now adopt a MLM pay plan in order to gain protection under the rule.

An Open Letter to the Members of the US Federal Trade Commission

The Commission stated that MLMs will be covered by Section 5 of the FTC Act governing “unfair and deceptive practices.” It is to this point – the Commissioners’ record and willingness to enforce Section 5 in cases of MLM fraud – that the rest of this letter is addressed.

When confronting widespread and persistent crimes, frauds, or other anti-social conditions, experience may force citizens to make a critical decision. They may decide to no longer alert and seek the support of proper regulatory agencies. Instead, they may be forced to raise awareness about the negligence and complicity of regulatory agencies themselves in allowing the frauds to continue. Persistent failure of a duly appointed regulatory agency to protect consumers makes the public even more vulnerable and emboldens and aids perpetrators of fraud.

This point in time has been reached with the FTC regarding the Commissioners’ failure – and apparent refusal – to enforce the law against the most common and pernicious form of business opportunity fraud: the use of the “endless chain” in selling business opportunities as “multi-level marketing.” In an era when millions of people are forced to seek new income opportunities through self-employment or independent sales, this type of fraud is insidious and tragic. That it is protected by the Commission through refusal to enforce Section 5 of the FTC act is indefensible.

While the FTC has many dedicated and knowledgeable staff on whom the public can still rely, the policies and actions of you, the Commissioners, make you a party to the escalating fraud now being inflicted on the American public and worldwide in “MLM- business opportunity” frauds.

The reality which led to this position can be stated briefly:

1. The “endless chain” is the most common and most harmful form of fraud facing consumers today when they seek new business or income opportunities. There is hardly an American household today that does not have a member who has been solicited or who has lost money and time in a multi-level marketing scheme that turned out to be an endless chain recruiting/investment scam.
2. Multi-level marketing is overwhelmingly – almost exclusively – the primary disguise used for the epidemic of endless chain frauds. The scale of losses is in the billions each year.
3. In the MLM scams, a closed system of money transfer is disguised as “direct selling;” participants are authorized as independent sales representatives, but in fact, the nature of the products, their high prices, the top loaded and recruitment-based pay plans and other market conditions make actual “direct selling” unfeasible; the “consideration” paid by investors to participate is laundered through required inventory purchases and other “fees”; rewards are tied to endless chain recruiting of new participants, not retailing; the perpetrators conceal key information about the flawed model and the extent of losses it has caused.
4. Few people can discern the true nature of such scams. This public vulnerability is exacerbated when the frauds are allowed to operate openly, without regulation, and the public sees no government interest in investigating them. In that circumstance, the government serves as endorser and supporter of these known scams. The perpetrators repeatedly point to the regulators’ inaction as evidence of the schemes’ “legality.”

2 An Open Letter to the Members of the US Federal Trade Commission

1. In the mid-to late 1990’s, the FTC was systematically prosecuting MLMs that operated as pyramid scheme frauds. It had gained experience in analysis; developed a proven method for

distinguishing such scams from legitimate sales companies; had the legal foundation of three federal court rulings to support prosecution of MLM scams in which there is little actual retailing of goods and recruiting new participants is the primary means to recoup investments and gain promised profits.

2. Since 2001 the FTC virtually stopped all investigations and prosecution of MLM endless chain scams; it moved key personnel out of this area of investigation; and the FTC has ignored repeated consumer requests for investigations of these schemes (e.g. <http://www.ftc.gov/os/comments/businessopprule/522418-70047.pdf>)
3. The timing of this abrupt change in policy coincides with the 2001 FTC Chairmanship appointment by President Bush of Timothy Muris, an attorney whose law firm at that time represented the largest of all multi-level marketing companies, Amway. Though Mr. Muris has left the FTC, the endless chain safe haven policies have continued.
4. With nearly seven years of government protection, endless chain schemes have proliferated; consumers are now harassed or sued who dare to question their legitimacy; with great risk and at their own expense, consumers have battled these scams with publicity, research and lawsuits.
5. In 2008, the FTC went beyond providing endless chain sales scheme immunity from investigation. It voted to exclude these types of schemes from a proposed rule aimed at combating business opportunity fraud. This action reinforces the protection provided to fraud. It renders whatever rule may be finally adopted meaningless and useless, since the largest form of business opportunity fraud is specifically excluded.

The improper influence of an appointment to the FTC Chair of an individual from a law firm that represented the world's largest multi-level marketing company might be disconnected from the FTC's immediate moratorium on prosecutions of MLMs, except that other facts also make the political influence-buying connection impossible to ignore.

- The subsequent appointment by Mr. Muris of David Scheffman as the FTC's Chief Economist. When the large and notorious multi-level marketing company, Equinox International, was prosecuted and shut down by the FTC in the late 1990's, David Scheffman testified as a consultant/expert for Equinox *against the FTC*. He argued that the Equinox business model – based on recruiting, not retailing – was legitimate, not a pyramid scheme. His claim was largely based on the assertion that Equinox operated just like Amway.
- The “soft money” donation of \$2.5 million from the Amway Corporation to the Republican Party in 1994.
- Amway's and affiliated donors' soft money contributions to the Republican National Committee totaling \$4,147,000 between January 1, 1991 and June 30, 1999, according to the consumer watchdog group Common Cause,
- Amway's 1996 donation of \$1.3 million to San Diego's host committee “to defer convention costs” for the Republican Party's national convention.

An Open Letter to the Members of the US Federal Trade Commission

- The 1997 gift of \$1 million to the Republican Party, one of the largest single donations on record from an individual, by Amway founder, Richard DeVos, a former finance chairman of the Republican National Committee.
- The campaign status with the Bush/Cheney campaign of Betsy DeVos, daughter-in-law of the Amway co-founder Richard DeVos, as a "Pioneer" after raising \$100,000 for the Bush/Cheney campaign.
- Contributions of \$2 million each from Amway founders Richard DeVos and Jay Van Andel in 2004 to the Republican "527" *Progress for America*.
- The use of the Amway yacht in Philadelphia and New York at the 2000 and 2004 Republican Conventions to host parties for lobbyists and insiders.
- The use of the DeVos family yacht in 1999 by the "Republican Majority Issues Committee" (RMIC), for its inaugural fundraising event. RMIC is a "527" organization founded by Rep. Tom DeLay (R-Texas).

Every day, our organization receives the same basic questions from consumers worldwide. They ask whether one of the hundreds of US-based MLMs is a fraud due to their programs of endless chain recruiting and lack of retail sales; and, from those who have already been harmed, they ask why the FTC is not prosecuting or at least formally investigating the schemes.

Part of this consumer confusion is attributed to the FTC's near 30-year policy of identifying "non-retailing" MLMs as inherent frauds. The sudden reversal of that policy in 2001 toward allowing such scams to operate is inexplicable to many Americans.

Secondly, the FTC's own double-speak on the matter has confused citizens. On your own website (<http://www.ftc.gov/bcp/online/pubs/alerts/pyrdalrt.shtm>), the FTC warns consumers away from endless chain schemes, which it identifies as "illegal", while it takes no action to prosecute them. The FTC website states:

"However, others (MLMs) are illegal pyramid schemes. In pyramids, commissions are based on the number of distributors recruited. Most of the product sales are made to these distributors – not to consumers in general. The underlying goods and services, which vary from vitamins to car leases, serve only to make the schemes look legitimate."

This "FTC Alert" shows that the FTC is fully aware of the fraudulence of an MLM that operates as a closed system ("Most of the product sales are made to these distributors - not to consumers in general... commissions are based on the number of distributors recruited.") The FTC even lists, in question form, the key factors that identify MLM frauds:

- Does it sell products to the public-at-large?
- Is the product competitively priced?
- Is it likely to appeal to a large customer base?
- Is there a minimum monthly sales commitment to earn a commission?
- Will you be required to recruit new distributors to earn your commission?

Most of the largest and best known MLMs fail this questionnaire.

4 An Open Letter to the Members of the US Federal Trade Commission

- The products are ultimately purchased almost exclusively by the salespeople, not the public at large. A recent class action suit brought against the largest MLM, Amway, by a group of its top insider sales people, asserts that only 4% of Amway's goods are ever retailed. Amway itself has admitted that less than 20% of its product are ever sold to the "public-at-large."
- The products are exorbitantly priced, sometimes 3 to 10 times the price of similar products. Recent reports in the *Wall Street Journal* reported the extraordinary pricing of a large MLM, Usana Health Sciences, and a recent government prosecution of Amway in England also confirmed the absurdly uncompetitive prices of Amway goods.
- Detached from their "income proposition" MLM products have little or no market value and the great majority of all who do purchase them stop doing so within a year. Recent controversies about the MLM, Herbalife, revealed that 80% of all Herbalife "sales people" quit the scheme within a year and stop buying the goods. Many of MLM product are for sale on EBay at fractions of their so called wholesale prices.
- To earn a commission each new recruit must continue to purchase goods at a specified level. The monthly "auto order", employed by Usana, Amway, Nu Skin, and others in which the purchases are automatically charged to the consumer's credit card is a standard in the MLM business. =
- MLM payments are based on recruiting new distributors and the pay plans escalate payment rates the higher one moves up the recruiting chain. In nearly every MLM studied, more than 50% of all payments are transferred to the top 1% of the sales chain and 99% of all sales people earn less than their costs. Recruiting is the only viable way to earn a profit and in the closed systems, profit from recruiting is mathematically limited to a tiny few at the top of the chain.
- The extraordinary consumer losses that the MLM endless chain system requires and inflicts are concealed or denied by the perpetrators.

On its website, the FTC admonishes consumers about their liability in joining a fraudulent MLM scheme and urges "common sense." It remains silent about its own responsibilities to enforce the law against the schemes and its own liability for not doing so. The time has come for consumers to no longer ask the FTC to investigate MLM frauds, but rather to ask Congress to investigate the FTC for politically protecting them.

Signed



Robert FitzPatrick, President
PYRAMID SCHEME ALERT

Former FTC Chairman-turned-lobbyist Timothy Muris continues his effort to influence his former employees on behalf of Primerica and the MLM industry – to make absolutely sure they are shielded from having to provide transparency to protect consumers. In so doing, he was supporting the dialogue of deception upon which the MLM industry depends. His introduction follows, with comments by Jon Taylor inserted in the text and highlighted.

#58 [Primerica Financial Services, Inc.](#) (Muris, Timothy J.) (5/27/2008) #535221-00056

FEDERAL TRADE COMMISSION Project No. R511993

COMMENT of PRIMERICA FINANCIAL SERVICES, INC. on the REVISED NOTICE OF PROPOSED RULEMAKING on the BUSINESS OPPORTUNITY RULE R511993

FILED MAY 27, 2008

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I. INTRODUCTION

Primerica Financial Services, Inc. (“Primerica”) submits this comment on the Commission’s Revised Notice of Proposed Rulemaking (“NPRM”). First, we congratulate the Commission for its decision to exclude multi-level marketing opportunities from the proposed Rule. As staff’s analysis of the very large number of comments received in response to the original Proposed Business Opportunity Rule makes clear, the decision to exclude multi-level marketing from the Revised Proposed Business Opportunity Rule (“RPBOR”) is well-grounded. The comments make an overwhelming case that the costs of covering multi-level marketing arrangements far exceed any possible benefit. The small number of comments supporting application of the rule to multi-level marketers simply did not provide persuasive arguments or evidence to the contrary. Indeed, the record lacks any real evidence of a need for such a rule in the multi-level marketing context, and, as the revised NPRM recognizes, the Commission has an effective tool to prosecute any instance of fraud that may occur under Section 5 of the Federal Trade Commission (“FTC”) Act. The lack of any need for a new rule, particularly when weighed against the extreme cost to the vast number of individuals whose livelihoods depend on multi-level marketing opportunities, amply justifies, and indeed compels, the Commission’s decision to modify its proposal to exclude multi-level marketing, thereby better aligning benefits and costs.

[Muris might as well have said, “Thank you for bowing to our will. No matter how unjustified – and even absurd – were some of our arguments (the DSA/MLM lobby), your decision protected our industry. Forget consumer protection!]

Second, Primerica suggests three modifications to the RPBOR, to better assure that the regulatory language actually achieves the clear intent of the Revised Notice that the Rule exclude multi-level marketing opportunities like those offered by Primerica and by many members of the Direct Selling Association. Primerica believes that each of these changes retains the Proposed Rule’s efficacy against the types of arrangements intended to be covered by the RPBOR, while making it clear that multi-level marketing opportunities are not covered by the Proposed Rule.

[Muris is wanting to make absolutely sure that Primerica and the MLM industry are not having to provide transparency to consumers at the expense of the MLM industry. He is an effective proxy spokesman for the DSA/MLM lobby.]

It is important for the Rule’s text be clear in this regard, because a variety of actors within both the federal and state governments will have the opportunity to interpret the Rule once it becomes final. Federal courts play an obvious role in the interpretation and application of federal laws, including the Commission’s regulations. Moreover, because the Commission’s regulations are frequently relevant under state unfair and deceptive trade practices statutes, state courts and state regulatory agencies also may have the opportunity to interpret and apply the final rule. Although the message in the Revised Notice is loud and clear that the Commission does not intend to cover multi-level marketing opportunities, the text of the RPBOR itself leaves some room for argument to the contrary. ***[Uh-oh. We wouldn’t want that, would we?]***

The Commission specifically requested comment on this issue (*see* Revised Notice, 73 Federal Register 16110 at 16133 (March 26, 2008) (requesting comment on the definition of assistance: “Will it result in the inclusion of multi-level marketing relationships that would otherwise not be covered?”)).

Primerica believes that several small adjustments to the RPBOR will make it clear that multi-level opportunities are not covered by the Rule without interfering with the applicability of the Rule to the types of schemes that the RPBOR seeks to cover, such as work-at-home schemes, vending machine schemes, and the like.

[Muris is implying that with a little fine-tuning, the FTC will be fully captured by the DSA/MLM lobby to the benefit of the MLM industry.]

RPBOR rebuttals – 17 out of the 31 rebuttals were from Dr. Jon Taylor.

These can be accessed from the links below. The first is included after this list, which is a rebuttal of DSA comments, since the DSA is the lobbyist that manipulated the FTC into granting the MLM exemption. Most comments parroted the arguments of the DSA, which lobbies for the MLM industry. (NOTE: On the pro-consumer side, comments by Gail Aird, Heather Dobrott, and Nicole Lopez are well worth reading. To access them, go to –www.ftc.gov/os/comments/bizoprevised/index.shtm Scroll to # 243)

1. [Aird, Gail \(6/16/2008\) #535221-00081](#)
2. [Aird, Gail \(6/24/2008\) #535221-00086](#)
3. [Aird, Gail \(6/27/2008\) #535221-00088](#)
4. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. \(Taylor, Jon\) \(6/30/2008\) #535221-00091](#)
5. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. \(Taylor, Jon\) \(6/30/2008\) #535221-00092](#)
6. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, j\) \(6/30/2008\) #535221-00105](#)
7. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, j\) \(6/30/2008\) #535221-00107](#)
8. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00093](#)
9. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00095](#)
10. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00096](#)
11. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00097](#)
12. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00098](#)
13. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00099](#)
14. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00100](#)
15. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00101](#)
16. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00102](#)
17. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00103](#)
18. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00104](#)
19. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(6/30/2008\) #535221-00106](#)
20. [CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO. - and advisor, Pyramid Scheme Alert \(Taylor, Jon\) \(7/3/2008\) #535221-00115](#)
21. [Dobrott, Heather \(6/30/2008\) #535221-00090](#)
22. [Integrative Health Concepts, LLC \(Harkenrider, Lawrence\) \(6/30/2008\) #535221-00094](#)
23. [Johnson, \(6/21/2008\) #535221-00084](#)
24. [Lewitt, Hackman, Shapiro, Marshall & Harlan \(Gurnick, David\) \(7/1/2008\) #535221-00113](#)
25. [Lopez, Nicole \(6/26/2008\) #535221-00087](#)
26. [MarketWave, Inc. \(Clements, Len\) \(7/14/2008\) #535221-00119](#)
27. [MarketWave, Inc. \(Clements, Len\) \(7/14/2008\) #535221-00120](#)
28. [MarketWave, Inc. \(Clements, Len\) \(7/14/2008\) #535221-00121](#)
29. [MarketWave, Inc. \(Clements, Len\) \(7/14/2008\) #535221-00122](#)
30. [Parrington, Reid \(6/12/2008\) #535221-00079](#)
31. [Venable LLP \(Hailey, Gary\) \(6/24/2008\) #535221-00085](#)

Rebuttal of DSA comments by Dr. Jon Taylor

Comment Number: 535221-00091
Received: 6/30/2008 2:39:37 PM
Organization: CONSUMER AWARENESS INSTITUTE - and JON TAYLOR & CO.
Commenter: Jon Taylor
State: UT
Agency: Federal Trade Commission
Rule: Business Opportunity Rule
Attachments: [535221-00091.pdf](#) [Download Adobe Reader](#)

Comments:

In this **rebuttal of comments by the Direct Selling Association** (DSA- comment #535221-00050), I propose a resolution to the mess created by the FTC's caving in to the intense lobbying by the DSA to exempt MLM (multi-level marketing) from the Proposed Revised Business Opportunity Rule (RPBOR). All informed independent consumer advocates are appalled by this exemption, since extensive research and feedback we have received from tens of thousands of inquirers and victims prove that MLM is by far the most fraudulent of all classes of business opportunity fraud today. World wide, hundreds of MLMs are causing millions of victims to lose tens of billions of dollars every year. Included in this set of comments are the "Top ten reasons for the FTC to be highly suspicious of any comments or lobbying initiatives by the DSA." Also included is a list of 81 members of the DSA that merit immediate investigation under Section 5, in the event the FTC goes ahead with a Business Opportunity rule exempting MLM – and powerful reasons for investigating these companies for pyramid scheme abuse. These 81 are just the beginning; there are hundreds of others not in the DSA that are just as fraudulent. (See attachment). Respectfully submitted, Jon M. Taylor, MBA, Ph.D., Pres. CONSUMER AWARENESS INSTITUTE, and Pres., Jon Taylor & Co., Email: jonmtaylor@juno.com

June 11, 2008
Via Electronic Submission

Mr. Donald S. Clark, Secretary, and Commissioners
 of the Federal Trade Commission
 Room H-135 (Annex S)
 600 Pennsylvania Avenue, N.W.
 Washington, D.C. 20580

Re: REBUTTAL of Comments from the Direct Selling Association regarding the Revised Proposed Business Opportunity Rule, R511993

Dear Secretary Clark and Commissioners:

Thank you for the opportunity to comment in efforts to restore some integrity to the proposed Business Opportunity Rule. In the opening paragraph of the comments by the Direct Selling Association (DSA) is this statement:

The thoroughness and thoughtfulness of the FTC's analysis regarding the revised proposed Business Opportunity Rule ("RPBOR") and the preceding April 2006 Notice of Proposed Rulemaking ("NPR") demonstrate the seriousness with which the FTC considered the views of legitimate direct sellers who were concerned about the scope of the original proposed rule. This well-reasoned conclusion was premised not only on sound analysis but also by the fact that the FTC already possesses authority under Section 5 of the FTC Act to prosecute business Opportunity fraud in any area in which it may arise.

In its comments #535221-00050, the DSA deftly references MLMs (multi-level marketing companies) as “legitimate direct sellers.” In truth, our research proves that most MLMs (including members in the DSA) are not “direct sellers,” but pyramid or endless chain sellers, though they position themselves as direct sellers to mislead law enforcement. However, in MLM opportunity rallies, they often refer to their programs as “business opportunities” or “investments” to get prospects to part with their money. New recruits are incentivized to subscribe to regular monthly product purchases to qualify for commissions and/or advancement to higher levels in the pyramidal compensation plan where potential profits can be realized. “You have to invest in your business if you expect it to grow,” they are told. This type of deception is just one of over 30 typical misrepresentations I have identified that are used in MLM recruitment campaigns. (For the full list, see RNBOR comment #535221-00006, Appendix A).

The DSA flatters FTC officials with compliments that the Revised Rule was “well-reasoned.” Let’s be honest here. The FTC capitulated to extraordinary pressure and influence peddling by MLMs and their lobby, the DSA, which has recently come under the control of a fraudulent MLM industry. This pressure and corrupt influence was detailed in my May 27 comments #535221-00057 and in comments by Robert Fitzpatrick #535221-00040.

The DSA assertion that “the FTC already possesses authority under Section 5 of the FTC Act to prosecute business opportunity fraud in any area in which it may arise” ignores an essential fact: Section 5 only provides for case-by case action – which is not cost effective or even possible for hundreds of fraudulent operating MLM/pyramid/chain selling schemes – at least 81 of which are represented by the DSA (as will be discussed later). This is proven by the history of FTC actions against MLMs over the past several years. Out of several hundred MLM/pyramid/ chain selling schemes, including over 250 I have analyzed (See May 15 comment #535221-00006), the FTC has acted against less than 1% of these schemes using Section 5. For more information on the research that led to these conclusions, go to the research and law enforcement pages at – www.mlm-thetruth.com.

On page 3, the DSA includes among “DSA Suggested Clarifications” the following:

Business Opportunity Definition

As proposed, several elements within the §437.1 RNPR definitions may unintentionally include non-business opportunity activities. The proposed RNPR definition of business opportunity has three elements:

- 1) a solicitation to enter into a new business;*
- 2) a "required payment" made to the seller; and*
- 3) a representation that the seller will provide assistance in the form of locations, outlets, security accounts, or buying back certain materials.*

Of paramount concern to DSA is the possibility that "required payment" might be construed inappropriately to include payments for the purchase of certain materials on a not-for-profit basis. Additional concerns relate to the lack of clarity regarding what might constitute representations about providing locations, outlets, accounts, and customers; and the use of the term "provides" regarding buybacks of materials.

MLMs most certainly satisfy at least two of the three elements of the business opportunity definition of RNPR, except that instead of providing locations and outlets, it sells an unlimited chain of participants with no territorial protection, all in competition with each other – an unfair trade practice in itself.

Also, on page 4, the DSA states:

*A "business opportunity" as defined by the proposed rule requires a prospective purchaser to "make a required payment." Notably, this definition of required payment expressly excludes "payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices for resale or lease." However, the required payment element of the business opportunity definition could still inadvertently sweep in certain direct selling relationships that are clearly not intended to be covered by the revised rule. Direct sellers routinely purchase - on a not-for-profit basis - certain materials for demonstration, display, or otherwise to be used to encourage or facilitate the sale of products to consumers. The not-for-profit sale by the company of these materials is another feature that distinguishes direct selling from business opportunities and business opportunity frauds that seek up-front investments on a for-profit basis. Therefore, the exclusion for the purchase of reasonable amounts of inventory sold at bona fide wholesale prices should be amended to also include payments for the purchase of business materials on a not-for-profit basis. To that end, DSA recommends modifying the required payment exclusion as follows: payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices for resale or lease, **or payments for business materials, supplies and equipment sold on a not-for-profit basis.** (Suggested new language in **boldface**)*

"not-for-profit"?? "bona fide wholesale prices"?? Who do DSA spokesmen think they are fooling? Hopefully not responsible FTC officials. If I were an FTC official reading their comments, I would be insulted at such assumed stupidity.

No informed independent analyst would agree with the "bona fide wholesale prices" charged by MLM companies for their overpriced products (usually potions and lotions) and services. In one study I reported on my web site (www.mlm-thetruth.com/PRODUCTS-MLMprices.htm), *prices for multi-vitamins of ten MLM companies averaged over five times as much as those sold in ten health food stores.* Even wholesale prices did not compete with retail prices for comparable products elsewhere. Of course, each of the MLM companies had a proprietary formula with secret ingredients that they claimed earned the high prices, but independent laboratory that have been done have failed to show such superiority. Just because apples have blue stripes painted on them does not make them worth five times as much as apples without stripes.

Exempting MLM from the proposed Business Opportunity Rule for the reasons given by the DSA makes about as much sense as exempting fast food restaurants from the Franchise Rule because some people might go hungry. Somehow it seems appropriate at this point to do a take-off on David Letterman's "Top Ten" series as it relates to the DSA. See Exhibit 1: *"Top ten reasons for the FTC to be highly suspicious of any comments or lobbying initiatives by the DSA"*

To FTC Officials: Please do not allow yourselves to be duped by the convoluted DSA/MLM arguments in their comments on the Revised Rule. MLM typically consists of recruitment of an endless chain of recruits as primary (or only) customers. The small signup fee for most MLMs, which may include a starter kit, is merely a ruse. If you study MLM compensation plans carefully, you will find that no one qualifies for significant commissions or advancement up the various levels in the pyramidal pay plan without meeting minimum purchase requirements. Typically, these purchases are expensive "potions and lotions," touted to help cure or prevent all manner of diseases and aging.

Add to this the various sales aids, training, leads, web sites, etc. that new recruits are told is essential to “growing your business,” and you have significant ongoing expenses needed to “play the game.” These purchases amount to camouflaged or laundered investments over several months in a product-based pyramid scheme. If you doubt this, assign some of your staff as undercover investigators to attend some MLM opportunity meetings. You will find many of them presented not as “direct selling” opportunities, but as “businesses opportunities” or “investments.”

It is interesting to observe what happens in MLM opportunity meetings. Prospects are given a hard sell on the value of their unique products – the modern version of the snake oil pitch. Then they are encouraged to subscribe to these overpriced products on a monthly basis – to meet the minimum qualification for commissions and advancement. The small signup fee is merely a ruse.

Before going ahead with a Revised Rule that exempts MLM, FTC officials need to spend several months investigating these MLMs by actual attendance at their meetings, as some of us who are advocating for consumers have done. The MLM (“direct selling”) exemption almost totally negates the value of the Rule, as MLM is by far the leading category of fraud in the business opportunity field. I know this from 40 years of work with sales and business opportunities (including review or categorization of thousands of business opportunities), teaching entrepreneurship as adjunct college instructor, wide experience in entrepreneurship (having initiated over 40 business startups), extensive direct sales experience, and decades of advocacy for consumers. So please set aside any Business Opportunity Rule pending further research – by qualified independent researchers NOT funded in any way by the DSA or MLM industry.

Or more realistically, *considering the power exercised by the DSA with its millions of participants sucked into these pyramid/chain selling schemes (and who will fight to preserve the hope of some day realizing a profit), it may be best to cancel RPBOR altogether.* Any effort to protect consumers against these schemes with a new or revised Rule specifically directed to MLM abuse is likely to be met with similar fierce pressure by the DSA to dilute its effectiveness. The DSA will use all its massive resources and political influence to defeat any Rule that would protect consumers against some of the worst “business opportunity” schemes in history – many of which are MLMs included in DSA’s membership.

The Direct Selling Association has everything to gain by blocking the FTC’s efforts to protect consumers from unfair and deceptive trade practices because at least 81 of their members are currently rewarding such practices. (See Exhibit 2.)

This is a bold statement and deserves explanation. *When analyzing any human behavior, some background in psychology is helpful. Behaviorists learned decades ago that you get the behavior you reward.* While working on my Ph.D., I shared office space with “rat psychologists” who trained rats to do amazing feats simply by manipulating rewards. This is not rocket science, yet many in law enforcement have ignored this principle and depend exclusively on complaints to signal problems.

In its attempts to protect consumers, some in law enforcement have acted on complaints about behavior that could be described as “unfair and deceptive trade practices.” But

complaint-driven enforcement simply does not work with MLM/pyramid/chain selling schemes. I have evidence that less than one victim in 500 of MLM endless chains ever files a complaint. They blame themselves, and they fear self-incrimination or consequences from or to their upline or downline. For more on the silence of victims, go to comment #535221-00006.

The surest signal of pyramid scheme or chain selling abuse is the underlying reward system, or compensation plan, which 14 years of research and consumer advocacy convinces me is at the root of all the unfair and deceptive trade practices associated with all MLM/pyramid/chain selling schemes. After years of review and analysis of several dozen factors that contribute to victimization of participants in such schemes, I was able to identify five factors in the compensation plan (reward system) of an MLM that clearly cause the harm – extremely high loss rates and transfer of investment from a multitude of participants at the bottom of the pyramid to a handful of founders and TOPPs (top of the pyramid promoters), making it an unfair trade practice. Taken together, these five factors also clearly separate a legitimate direct selling program or home business from what I call a “recruiting MLM” (dependent on recruitment of an endless chain of participants), or “product-based pyramid scheme.”

Summary of the five causative and defining factors of a recruiting MLM or product-based pyramid scheme:

- 1. *Recruiting of participants is unlimited in an endless chain of empowered and motivated recruiters recruiting recruiters, without regard to (de facto) market saturation.*
- 2. *Advancement in a hierarchy of multiple levels of participants is achieved by recruitment and purchases, rather than by appointment.*
- 3. *“Pay to play” requirements are satisfied by ongoing “incentivized purchases,” with participants the primary customers.*
- 4. *The company pays commissions and/or bonuses to five or more levels of participants.*
- 5. *Company payout per sale for the person actually selling the product is less than the total of all upline participants, creating inadequate incentive to retail and excessive incentive to recruit – and an extreme concentration of income at the top.*

What should be compelling evidence for FTC officials is that in every case where data was available, when these five factors were found in an MLM compensation plan (true of nearly all MLMs), approximately 99% of participants lost money – only to enrich the TOPPs. Even more compelling is the fact that when ALL participants who signed up during a given time period were counted and ALL expenses (including incentivized purchases and minimal operating expenses) were subtracted, closer to 99.9% lost money. For the full 40-page report on how these five causative and defining factors were derived and their consequences in specific MLM programs, go to our research link at – www.mlm-thetruth.com.

Any MLM/pyramid/chain selling program that promises infinite expansion in a finite marketplace is inherently flawed, uneconomic, and fraudulent. Yet we have observed extreme self-deception among founders and executives, who are in profound denial about the harm caused by their schemes.

It is possible for a few persons to profit from MLM participation (as from the lottery). However, to succeed, one must not only work hard, but must also (1) be deceived, (2) maintain a high level

of self-deception, (3) aggressively recruit and deceive a large downline, or revolving door, of recruits, and (4) maintain a high level of deception. (Again, for the full list of 30 typical misrepresentations, go to <http://www.mlm-thetruth.com/30typicalMLMmisrepresentations.htm>).

This dependence on a bevy of deceptions by MLM companies is the very reason the DSA is so aggressive in (1) exempting MLM (“direct selling”) from any Business Opportunity Rule requiring meaningful disclosure essential for consumer protection, and (2) attempting to influence the language in RPBOR (comment #535221-00050) to exclude all present and potential members from having to truthfully disclose such information. Though good for consumers, such disclosures could greatly limit the success of MLM/pyramid/chain selling promoters at recruiting victims into their respective schemes.

Here is the crux of the whole matter for the FTC in evaluating any DSA input: According to the five causative and defining factors (above), a total of 81 of its members are recruiting MLMs, or product-based pyramid schemes (see Exhibit 2). They engage in unfair and deceptive trade practices because they MUST in order to survive. If the full truth were told about these recruiting MLMs, no one in their right mind would join, and they would collapse like a house of cards. Who would sign up to spend \$100 or more a month to qualify for bonuses and advancement if they knew their chances were less than one in a hundred that they would realize a profit (and 99% lose money), even with their best efforts?

So if an effective Business Opportunity Rule – requiring meaningful disclosure by MLMs – were implemented, many MLMs would pass out of existence. Instead of wringing their hands over this outcome, FTC officials should rejoice. Consumers would benefit, and the integrity and effectiveness of the FTC would be restored. Some MLM founders and executives may even gravitate to honest enterprises.

If, on the other hand, the FTC were to rely upon Section 5 to go after fraudulent MLMs, the DSA has 81 MLMs (Exhibit 2) that deserve immediate attention, since the DSA would be responsible for rendering the Business Opportunity Rule impotent in protecting consumers against the worst scams. It would not be fair to single out one or two of the members of the DSA for investigation, as all 81 are rewarding unfair and deceptive trade practices. But as Gail Aird clearly explains (RPBOR comment #535221-00081), even Section 5 would not be effective if the DSA language and recommendations were to be incorporated in the final Rule. It would be much more cost effective to have a Business Opportunity Rule that includes MLM than to go after the hundreds of abusive MLMs one by one – or simultaneously (including those in the DSA).

The next step for consumer advocates on this issue.

It is time for this issue to come before the more capable investigative journalists and/or TV program analysts who like to expose corruption in government. And if a Business Opportunity Rule is enacted that excludes MLM, it is certainly time to insist on a Congressional investigation of the FTC and its rulemaking. After all, the mission of the FTC is to protect consumers from unfair and deceptive trade practices, rather than to protect those committing such practices – which is what RPBOR does.

Questions for FTC officials:

- Do you want to uphold the mission of the FTC to protect consumers from unfair and deceptive trade practices – or those, such as the DSA, which is attempting to emasculate the FTC in its ability to perform this function?
- Do you really want your career and your legacy to be tainted by caving in to deceptive and self-serving DSA initiatives?
- If the RPBOR wound up merely aiding and abetting MLM fraud (by exempting MLM), as it easily could, would you be comfortable with that?
- Can you picture yourselves testifying before a Congressional Committee and defending a Business Opportunity Rule that exempts MLM/pyramid/chain selling from having to make disclosures to protect consumers from what are likely the worst scams in history?
- Or will you hold your head high because you stood up to DSA's deceptive devices and its "cartel of chain selling chicanery?"

Conclusion:

No rule is better than a bad rule – one that misleads consumers into believing the FTC offers some protection, when in fact they are terribly exposed. MLM promoters would take advantage of the exemption to tout their supposed legitimacy. Other shady business opportunities not excluded would move towards an MLM model to become exempt. And action under Section 5 could not possibly keep up with the hundreds of present and future MLM scams dotting the landscape.

A Revised Business Opportunity Rule that exempts MLMs as "direct sellers," would place the FTC in the position of inadvertent complicity in massive MLM/pyramid/chain selling fraud. MLM promoters would claim that MLM was not included in the Rule because their MLM members are "legitimate direct sellers." Nothing could be further from the truth. Collectively, fraudulent MLM schemes represent the greatest "business opportunity" scams of all time. RPBOR, in the current milieu, must be set aside.

Up with consumers and with the mission of the FTC in protecting them from "unfair or deceptive acts or practices." Down with MLM/pyramid/chain selling fraudsters and their highly deceptive lobbying organization, the DSA!

Sincerely,



Jon M. Taylor, MBA, Ph.D.,
 President, Consumer Awareness Institute
 Advisor, Pyramid Scheme Alert
 and President, Jon Taylor & Co. (consulting)

Exhibit 1: “Top ten reasons for the FTC to be highly suspicious of any comments or lobbying initiatives by the Direct Selling Association”

- ➡ 1. The Direct Selling Association (DSA) has gradually evolved from a representative of legitimate direct selling companies to aggressive lobbyist for pyramid and chain selling schemes.
- ➡ 2. The DSA seeks to define what “direct selling” IS without excluding what legitimate direct selling is NOT – recruitment of an endless chain of participants who are the primary buyers of the products and are organized into layers in a pyramid of participants, with founders and those at the top (or beginning of the chain of recruitment) benefiting from the losses of a huge downline of victims beneath them.
- ➡ 3. The DSA has a “Code of Ethics” which its members routinely violate. In spite of its supposed ban on “Deceptive or Unlawful Consumer or Recruiting Practices,” DSA member firms use as many as 30 typical deceptions in every recruitment campaign. (See comment #535221-00006, Appendix A). DSA spokes persons also twist of the intent and application of FTC guidelines regarding internal consumption as legitimate sales.
- ➡ 4. Using these deceptions, pyramid/chain selling schemes that are members of the DSA have defrauded *tens of millions of victims* out of *hundreds of billions of dollars worldwide* since the 1979 Amway decision by the FTC that Amway was not a pyramid scheme – subject to specific “retail rules.” These retail rules have been increasingly ignored, even to the point that many MLMs in the DSA thumb their noses at these retail requirements. (See *Pyramid Nation*, by Robert FitzPatrick, available from www.falseprofits.com. And for statistics supporting these claims of extraordinary losses by MLM victims, review the statistics page of my web site at – www.mlm-thetruth.com)
- ➡ 5. DSA members harass with lawsuits and personal attacks on the Internet upon individuals who donate their time trying to provide consumer awareness to protect against the worst scams. Read the appeal at the “Merchants of Deception” web site - www.merchantsofdeception.com/legalhelp.html
- ➡ 6. The DSA and its members use deception and corrupt influence peddling to weaken state and federal laws against product-based pyramid schemes. (A prime example can be found in Utah as described on the Utah page of my web site at – www.mlm-thetruth.com/Utah-pyramidSchemesNowLegal.htm
- ➡ 7. DSA members donate heavily to political parties and candidates, including elective law enforcement officers. For examples, read the comments by Robert Fitzpatrick of Pyramid Scheme Alert in RBOR comment #535221-00040. Also, in 2006 Utah legislative hearings, Utah Attorney General Mark Shurtleff spoke in favor of the DSA-written bill exempting MLM companies from prosecution as pyramid schemes. Mr. Shurtleff has received substantial contributions from DSA members since 2002.
- ➡ 8. The DSA has engaged in the web version of identity theft by buying up alternative domain name extensions of critics and then deceptively re-directing web surfers to the DSA’s convoluted definition of what is a pyramid scheme. They did this with “pyramidschemealert.org” – only recently taking down their “pyramidschemealert.com” website when they got criticism for such deceptive web tactics. Yet they still own several domain name extensions for Pyramid Scheme Alert and for my Consumer Awareness Institute.
- ➡ 9. By appealing to millions of participants in MLM/pyramid and chain selling schemes that make up much of its membership and by blatant influence peddling (providing campaign funds and promising jobs and votes, and by hiring former high-level FTC officials to lobby for them), the DSA succeeded in exempting MLM (“direct selling”) from the FTC’s proposed Business Opportunity Rule – even though MLM misrepresentations are by far the leading category of deceptive marketing practices among business opportunity sellers. Of course, MLMs only refer to their programs as “business opportunities” or “investments” at opportunity events. They are careful not to use those terms when communicating with regulators - calling it “direct selling” instead.
- ➡ 10. The DSA is now attempting to define what the FTC can and cannot do to protect consumers, using highly deceptive verbal maneuvers that would effectively render the FTC impotent to act against the most egregious sales and business opportunity schemes. Consumer advocate Gail Aird provides an excellent but lengthy treatise on these maneuvers in her comments numbered 535221-00089 and 535221-00086, so I will not attempt to discuss them here.
- For these ten reasons, the FTC should stop allowing the DSA to influence its rules and policies.

Exhibit 2: DSA Member Firms that Qualify as Recruiting MLMs, or Product-based Pyramid Schemes – and therefore powerfully motivated to avoid transparency

Out of 212 members (June, 2008), at least 81 qualify as recruitment-driven MLMs, or product-based pyramid schemes, based on their compensation plans*. All those listed below are practicing unfair and deceptive trade practices and merit immediate investigation under Section 5.

4Life Research, LC , Sandy, Utah
 5LINX Enterprises, Inc., Rochester, New York
 ACN, Inc., Farmington Hills, Michigan
 Advocare, International, LP, Carrollton, Texas
 Agel Enterprises, LLC, Provo, Utah
 Amazon Herb Co., Jupiter, Florida
 Ameriplan USA, Plano, Texas
 AMS Health Sciences, Inc., Oklahoma City, OK
 Amway Corp., Ada, Michigan
 Arbonne Int'l., Irvine, California
 Avalla, Houston, Texas
 Avon Products, Inc. (*Avon is marginal as a product-based pyramid scheme, but according to experienced participants, Avon has recently moved towards channel stuffing and/or internal consumption for increased volume.*)
 Body Wise Int'l, LLC, Tustin, California
 Cleur, Camarillo, California
 Creative Memories, St. Cloud, Minnesota
 CyberWize, Sarasota, Florida
 Essentially Yours Industries, Burnaby, B.C., Canada
 First Fitness Int'l, Carrollton, Texas
 Forever Green Int'l, Orem, Utah
 FreeLife Int'l, Phoenix, Arizona
 Frutaiga, Carlsbad, California
 Gano Excel USA, Inc., Irwindale, California
 Global Health Trax, Vista, California
 GNLD Int'l, Fremont, California
 Goldshield Elite, West Palm Beach, Florida
 Herbalife Int'l of America, Inc., Los Angeles, California
 Heritage Makers, Provo, Utah
 Hsin Ten Enterprise USA, Inc., Plainview, New York
 Immunotec Research, Vaudreuil-Dorion, Quebec, Can.
 Integris Global, LP, Irving, Texas
 Life Force Int'l, Poway, California
 Lifestyles USA, Cheekowaga, New York
 The Limu Company, Lake Mary, Florida
 Livinity, Inc., Russell, Kansas
 Mannatech, Inc., Coppell, Texas

Market America, Inc., Greensboro, North Carolina
 Mary Kay, Inc, Dallas, Texas (*According to experienced participants, Mary Kay has recently moved towards channel stuffing and/or internal consumption for increased volume.*)
 Max Int'l, Salt Lake City, Utah
 Melaleuca, Inc., Idaho Falls, Idaho
 Nature's Sunshine Products, Provo, Utah
 New Vision USA, Inc., City of Industry, California
 Neways Int'l, Springville, Utah
 NHT Global, Inc., Dallas, Texas
 Nikken, Inc., Irvine, California
 Noevir USA, Inc., Irvine, California
 NSA, Collierville, Tennessee
 Nu Skin Enterprises, Provo, Utah
 PM Int'l Nutrition and Cosmetics, Export, Pennsylvania
 Primerica Financial Services, Duluth, Georgia
 Reliv Int'l, Inc., Redmond, Washington
 Sentsy, Inc., Meridian, Idaho
 Shaklee Corporation, Pleasanton, California
 Sportron Int'l, Inc., McKinney, Texas
 Stampin' Up, Riverton, Utah
 Stemtech Health Sciences, Inc., San Clemente, Calif.
 Sunrider Int'l, Torrance, California
 Symmetry Corporation, Milpitas, California
 Synergy Worldwide, Provo, Utah
 Tahitian Noni Int'l, Provo, Utah
 Take Shape for Life – Medifast, Owings Mills, Maryland
 Tianshi Health Products, Inc., Markham, Ontario, Can.
 Tomboy Tools, Denver, Colorado
 Unicity Int'l, Inc., Orem, Utah
 Univera Life Sciences, Lacey, Washington
 USANA, Health Sciences, Inc., Salt Lake City, Utah
 Vision for Life Int'l, Oklahoma City, Oklahoma
 VIVA Life Science, Inc., Costa Mesa, California
 Wynlife Healthcare, Inc., San Diego, California
 XanGo, LLC, Lehi, Utah
 YTB Int'l, Wood River, Illinois

*For a complete analysis of how the compensation plan is at the core of pyramid scheme abuse, read the report, a summary of which was prepared for the National White Collar Crime Center - and for the Economic Crime Summit Conferences (in 2002 and 2004), entitled: *"THE 5 RED FLAGS: Five Causal and Defining Characteristics of PRODUCT-BASED PYRAMID SCHEMES or RECRUITING MLM's"* – linked from our web site at – www.mlm-thetruth.com

PUBLIC WORKSHOP ON PROPOSED BOR CHANGES

Held in Conference Room at FTC offices, June 1, 2009 (Reference: Public Comments #291)

For Release: 04/21/2009

FTC to Hold Public Workshop on Proposed Business Opportunity Rule Changes

The Federal Trade Commission will hold a day-long public workshop on June 1, 2009 in Washington, DC, to explore proposed changes to the FTC's Business Opportunity Rule. The workshop, which is free and open to the public, will examine possible changes to the rule that were outlined in a Revised Notice of Proposed Rulemaking (RNPR) on March 26, 2008.

The workshop will primarily explore issues relating to the effectiveness of a proposed one-page Business Opportunities Disclosure Form that sellers of business opportunities would be required to provide to prospective purchasers. The proposed Disclosure Form is intended to provide prospective purchasers with information they can use to make an informed decision about the potential business opportunity, including information about earnings claims, legal actions, existence of cancellation or refund policies, and references. The workshop also will address general issues raised in comments that have been submitted to the FTC in response to the proposed rulemaking. A more detailed agenda will be published at a later date, before the scheduled workshop.

Business opportunity ventures include vending machine routes, rack display operations, and medical billing ventures. The FTC's new proposed rule is aimed at protecting consumers from bogus business opportunities while minimizing compliance costs for legitimate businesses.

The workshop will be held from 9 a.m. to 5 p.m. at the FTC's satellite building conference center, located at 601 New Jersey Avenue, N.W., Washington, DC. All attendees will be required to display a current driver's license or other form of photo identification for entry.

The Commission will be accepting comments on the topics to be covered at the workshop until June 15, 2009. The FTC staff also invites interested parties to submit requests to be panelists by May 4, 2009. Interested parties should include a statement detailing their expertise on the issues to be addressed at the workshop and their complete contact information. Requests to participate filed in an electronic form should be sent to: businessopportunityworkshop@ftc.gov.

Reasonable accommodations for people with disabilities are available upon request. Requests for such accommodations should be submitted via e-mail to: cmcglothin@ftc.gov or by calling Carrie McGlothin at 202-326-3388. Such requests should include a detailed description of the accommodations needed and a way to contact you if we need more information. Please provide advance notice.

The Commission vote approving publication of the Federal Register Notice announcing the workshop was 4-0.

The Federal Trade Commission works for consumers to prevent fraudulent, deceptive, and unfair business practices and to provide information to help spot, stop, and avoid them. To file a complaint in English or Spanish, visit the FTC's online [Complaint Assistant](#) or call 1-877-FTC-HELP (1-877-382-4357). The FTC enters complaints into Consumer Sentinel, a secure, online database available to more than 1,500 civil and criminal law enforcement agencies in the U.S. and abroad. The FTC's Web site provides free information on a variety of [consumer topics](#).

MEDIA CONTACT:

Peter Kaplan
Office of Public Affairs
202-326-2334

STAFF CONTACT:

Kathleen Benway
Division of Marketing Practices
202-326-2024

(FTC File No. R511993)
(BizOppWorkshop)

- [Text of the Federal Register Notice](#)
- [Text of the Design and Testing of Business Opportunity Disclosures Report](#)

Highly relevant comments include those by Bruce Craig, Douglas Brooks, Jon Taylor (CAI), the DSA, and Tupperware as a DSA (non-member) plant. (See below.) The letter from Doug Brooks follows this listing. Then my letter to the FTC in conjunction with the workshop he attended is quoted in full.

291; 16 CFR Part 437; FTC Matter No.: P084405: Business Opportunity Rule: Public Workshop Analyzing Business Opportunity Disclosure Form and Other Proposed Changes to the Business Opportunity Rule

Public Comments

1. [Consumer Awareness Institute](#) (Taylor, Jon) (6/02/2009) # 541181-00001
2. [Consumer Awareness Institute](#) (Taylor, Jon) (6/15/2009) # 541181-00006
3. [Consumer Awareness Institute](#) (Taylor, Jon) (6/29/2009) # 541181-00008
4. [Craig, Bruce](#) (10/20/2009) # 541181-00009
5. [Direct Selling Association](#) (Mariano, Joseph) (6/15/2009) # 541181-00003
6. [Martland & Brooks, LLP](#) (Brooks, Douglas) (6/29/2009) # 541181-00007
7. [Planet Antares](#) (MacLeod, William) (6/15/2009) # 541181-00004
8. [Tupperware Brands Corporation](#) (Morrissey, Maureen) (6/04/2009) # 541181-00002

Behavior of FTC staff and DSA attendees at workshop

Since I had submitted the most comments in opposition to DSA/MLM arguments and influence over the whole rulemaking process, I was invited to participate in a workshop on the final form for BOR. I travelled at my own expense to Washington, D.C. for the workshop held at a conference room at the FTC headquarters. What happened there – from a consumer protection standpoint – seemed most unusual, if not bizarre and biased – but not towards consumers. I realize some of my observations may seem subjective, but I believe they are relevant and generally correct in showing the influence over the rulemaking by the DSA/MLM lobby.

- The room was packed with DSA/MLM supporters. I was the only participant representing consumers nationwide – who were to be affected by the Rule – in a panel discussion on the actual form that was to be used in implementing the Rule.
- I was sought out and greeted not only politely, but very warmly, by DSA officials in attendance. While I appreciated their courtesy, it seemed strange, since they had reacted to my rebuttals of their arguments with such hostility during the various stages of the rulemaking. They may have assumed that it would not help to appear hostile, as they did not want me to be too vigorous in opposing the DSA position in my comments. They may have concluded that this was not a time to challenge me or to make waves.
- DSA/MLM officials were strangely silent for most of the workshop – even during question and answer periods – again apparently not wanting to stir up any controversy that might upset the victory they had achieved in getting their MLM member firms exempted from having to comply with the Rule.
- During a break, I walked out into a hallway and noticed a group of DSA/MLM officials huddled and conversing in hushed tones in a caucus atmosphere at the side of the hallway. When they saw me looking at them, they quickly shushed one another. I excused myself for interrupting them, but they just smiled and remained silent.
- No DSA officials were represented on the panel, though they had been the most

influential in getting their wishes implemented in the Revised Rule.

- The Tupperware spokesperson on the panel, Maureen Morrissey, presented essentially the same deceptive arguments used in the DSA/MLM comments submitted during the BOR rulemaking. Tupperware is not a member of the DSA, which seems strange since it is certainly in their interest to be a member. I don't believe it would be too great a stretch to conclude that keeping Tupperware as an ally, rather than as a member, is a deliberate part of a DSA strategy to help promote DSA interests from a position outside of their membership when necessary. Ms. Morrissey appeared to be deliberately planted on the panel so she could protect the views of the DSA without directly representing the DSA – since most of the wishes of the DSA had already been implemented in the Revised Rule. She could dispute any challenge I might make to the MLM exemption.
- In preparing my opening remarks for the panel, I wrote the staff asking how much time I could have to present my arguments. I was warned that there would be very little time to do so, as the purpose of the workshop was to focus on the form to be used in implementing the Rule. So my opening remarks were very brief. However, Ms. Morrissey was allowed to give a long prepared speech praising “direct selling” and praising the FTC for exempting “direct selling” (MLM) companies from the Rule.
- At one point during the workshop, when Ms. Morrissey was introduced by Lois Greisman, the FTC official conducting the workshop, she asked Ms. Morrissey to comment on the lead system used by Tupperware, which obviously impressed Ms. Greisman. This seemed altogether inappropriate for the objective of the workshop. I noticed that Ms. Greisman's request was expunged from the transcript of the workshop that was later released.

Douglas M. Brooks weighs in again with highly relevant comments

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DOUGLAS M. BROOKS

June 29, 2009

Via Electronic Submission

Mr. Donald S. Clark
Secretary
Federal Trade Commission
Room H-135 (Annex S)
600 Pennsylvania Avenue, N.W.
Washington, D.C. 20580

Re: Business Opportunity Rule Workshop
Comment, Project No. P084405

Dear Secretary Clark

I am submitting the following comments in reference to the public workshop held on June 1, 2009 in the rule-making proceeding regarding the Business Opportunity Rule.

Over the past 14 years I have submitted comments to the Commission in reference to the need to protect consumers from unfair or deceptive practices in the multilevel marketing (MLM) industry. These include a comment in response to the Commission's April 7, 1995 Request for Comment on the Franchise Rule, a comment dated July 16, 2006, in response to the Commission's Notice of Proposed Rulemaking regarding the Business Opportunity Rule, and a rebuttal comment dated July 1, 2008, regarding the Revised Proposed Business Opportunity Rule. I respectfully refer the Commission to my prior comments, which provide a more detailed discussion of my background and experience, as well as the basis for my views on the need for regulation in this area to avoid further the substantial and devastating harm suffered by the vast majority of participants in MLM "opportunities," *whether or not* they can be characterized as pyramid schemes.

I appreciate that the public workshop had the relatively narrow purpose of addressing the format of the proposed pre-sale disclosure document. It is my understanding that the Commission anticipates that a staff report will be issued in the Fall of 2009, and that there will be a further opportunity for public comment at that time. I will therefore restrict my comments in this letter to the issues discussed at the public workshop relative to the disclosure document.

I note that the representative from Tupperware raised the issue of whether, despite the efforts of the MLM industry's lobbying efforts, the proposed rule might still be broad enough to cover MLM opportunities. I will not repeat here the many compelling reasons why the rule should cover MLM opportunities, which are detailed in my prior submissions.

The bankruptcy history of the company, promoters and key persons should definitely be included in the legal actions section. The burden of including such information is slight, while the value to consumers – who are only being provided with a one-page disclosure – is substantial. If nothing else, disclosure of a prior bankruptcy will prompt the consumer to investigate the offering more thoroughly. Mr. Macleod suggests (Transcript pp. 33-34) that there may be bankruptcy filings unrelated to fraudulent conduct, implying that consumers may misunderstand the significance of the filing. Such a misunderstanding is a consequence of using a simplified, stream-lined form – which is something that Mr. Macleod's client – a business opportunity seller – would otherwise prefer.

Disclosure of the company's refund policy should include a "black box" warning (similar to that required for certain adverse side effects of prescription drugs) that the refund will not cover all of the business losses typically incurred by participants in business opportunities. I would refer to my previous submissions, which address this subject in detail. I am not aware of any MLM refund policy that provides for the recovery of such losses. There should also be bold print disclosure of any applicable deadlines, and any other limitations, such as that goods must be in their original packaging. Finally, disclosure of the number and percentage of persons who request and receive refunds should be required, as this is extremely significant information for persons attempting to evaluate a business opportunity.

As to earnings claims, I do not believe that promoters should have the option to state that no earnings claims are made. In the real world, no business opportunity is sold without some sort of earnings claim. A disclosure form which permits the promoter to disclaim making such claims (by checking the "no" box) simply gives the promoter a defense, based on "unreasonable reliance" that they would not otherwise have in a subsequent fraud action by the purchaser. Thus, the existence of a disclosure form which is intended to assist the consumer actually makes the consumer worse off. Alternatively, if a company expressly disclaims making earnings claims, there ought to be a black box warning to the effect that any suggestion that the consumer will make money at the proposed venture is a lie, and that any supposed opportunity for which the promoter declines to provide earnings information should be treated with extreme caution. However, simply providing the promoter with the option of checking the "no" box on the form is an invitation to fraud.

Thank you for the opportunity to submit my comments.

Respectfully,



Douglas M. Brooks

DMB/s

This is the letter Dr. Jon Taylor wrote to the FTC and which was distributed to those attending the workshop at the FTC in Wash. D.C. – to which I travelled at my own expense. The ex parte DSA seminar featuring FTC staff – and possible violation of FTC rulemaking procedures – is discussed. Supporting Appendices are available by special request from the author.



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COMMENTS ON FTC'S RPBOR WORKSHOP – JUNE 1, 2009

The Revised Business Opportunity Rule Is Invalid and Must be Vacated.

By Jon M. Taylor, MBA, Ph.D.

Consumer Awareness Institute
 (web site – mlm-thetruth.com)

What began as a consumer-friendly Business Opportunity Rule (IPBOR) quickly degenerated into a corrupt rulemaking procedure, manipulated by the DSA (Direct Selling Association), a lobbying organization now dominated by MLMs (multi-level marketing companies). As a result, the Revised Rule (RPBOR) is invalid and will provide little consumer protection, thanks to the DSA and complicit FTC officials. Below are some of the reasons for this conclusion:

1. False and misleading statements of material facts

Below is just one crucial and glaring example among many of falsehood with the imprint of the DSA. Either A or B below is true, but not both.

- A. In the text of the Federal Register Notice for the Workshop, and for the Revised Rule, the following is noted about the Revised Rule:
- 1) (RPBOR) narrows the scope of the proposed Rule to avoid broadly sweeping in sellers of multi-level marketing opportunities. (Workshop Notice, Footnote 7)
 - 2) In addition, the revised proposal does not attempt to cover MLMs. (In Section C. Scope of the Proposed Rule – 1st paragraph)

- 3) The Commission does not believe it is practicable or sufficiently beneficial to consumers to attempt to apply the proposals advanced in this rulemaking against multi-level marketing companies. (In Section C-2 The MLM Industry: Scope of the Proposed Rule)
- 4) The Commission takes MLM companies out of the ambit of the Rule.
- 5) The MLM industry articulated concerns peculiar to its business model, but these provisions would no longer apply to *MLM companies* inasmuch as these companies, and their representatives, *are excluded from the ambit of the RPBOR*. (Section D-2-d)

B. In stark contrast to the above, the following is found in Footnote 7 on page 3:

The RNPR did not exempt MLMs from coverage of the RPBOR. Instead, it narrowed the scope of the IPBOR by significantly revising Section 437.1 by redefining the term “business opportunity.” The RNPR noted that while some MLMs do engage in unfair or deceptive acts or practices, including the operation of pyramid schemes or unsubstantiated earnings claims that cause consumer harm, [MLM] commenters generally agreed that the IPBOR’s required disclosures would not help consumers identify a fraudulent pyramid scheme. In the RNPR, the Commission stated its belief that consumer harm flowing from deceptive practices in the MLM industry could be more effectively addressed through the use of Section 5 of the FTC Act. . .

If A (above) is true, the opening statement for B is false. If B is true, A is false. Either way, one or the other is false and misleading to the public.

2. In all of the Rulemaking procedures, from the original IPBOR announcement to the June 1 Workshop, I was struck with how much the FTC has underestimated the scope of and the harm done by MLM schemes, which may (or may not) be excluded from the Rule.

The DSA claims that the vast majority (98.2%) of direct sellers are now using a multi-level pay structure and that there are over 15 million people selling over \$30 billion in products and services using a direct selling model²⁷. If we assume these DSA figures are correct, and if we use figures on MLM loss rates from analyses from qualified independent analysts of approximately 99%²⁸, the losses to consumers are staggering. **In the aggregate, millions of MLM participants are losing tens of billions of dollars every year in the U.S. alone. To exempt this leading class of business opportunity fraud from the Business Opportunity Rule is unthinkable to any informed consumer advocate.**

Those familiar with the harm done by MLMs, including DSA members, often ask why law enforcement at both state and federal levels seem unaware of the extent of the losses. My answer from having worked with victims worldwide is not the obvious one often given out – embarrassment at having not succeeded at “making the plan work.” Most are not aware that they have been scammed unless and until they have gone through some deprogramming, similar to what is done with victims of cults.

Perhaps the strongest explanation for the lack of law enforcement action against MLMs is that victims of endless chain business opportunity schemes rarely file complaints. This is because nearly every major victim has of necessity become a perpetrator – having recruited some of his close friends and family in the hope of eventually recouping enough in commissions to meet their ongoing purchases necessary to qualify for commissions and/or advancement in the scheme. So they fear going public for fear of consequences from or to those who they recruited or persons who recruited them – often close family or friends.

MLM is perhaps the cleverest con game of all time. The very people who are perpetrators are themselves victims until they run out of money and drop off the vine. And since they don’t complain, law enforcement does nothing. So the game goes on.

²⁷ DSA Industry statistics – www.dsa.org

²⁸ Available for download at www.mlm-thetruth.com and www.pyramidschemealert.org

3. The Revised Rule will apply to no one and will therefore provide no consumer protection against unfair and deceptive practices, which the FTC is pledged to protect.

In her closing comments, Ms. Morrissey applauded the Commission and Staff for narrowing the scope of the proposed Business Opportunity Rule. Other DSA members present were obviously please with this apparent exclusion. (I say apparent advisedly, given #1, above)

However, according to the Revised Rule²⁹, all Business Opportunities that pay commissions to two or more individuals as the result of a sale of the company's products or services are MLMs for purposes of the proposed MLM exemption. Given the facts that (1) there are few, if any, business opportunities sellers ("direct sellers") that do not currently engage in this practice and that (2) the minuscule number of sellers that do not engage in same will do so to gain exemption from the ambit of a final Rule, **the end result, if the MLM exemption is included in a final rule, will be a Business Opportunity Rule that will exclude virtually every single business opportunity in the US from the ambit of the Rule.**

As explained in earlier comments and in FTC announcements regarding both IPBOR and RPBOR, fraudulent practices are common in business opportunity schemes. By exempting virtually all such schemes through RPBOR, the FTC could thereby be complicit in aiding and abetting massive consumer fraud by direct sellers of "business opportunities" -- many of them members of the DSA, which is the lobbying group primarily responsible for the MLM exemption. With RPBOR, the FTC is clearly siding with the DSA in direct contradiction to its responsibility to protect consumers from unfair and deceptive practices.

4. The RPBOR and the whole rulemaking process for a Business Opportunity Rule have been corrupted by ex parte communications between FTC officials and the DSA.

After the comment period closed for RPBOR, I and other parties sought to give additional input to correct facts regarding interpretation of prior comments. Such communications were refused on the grounds that they would be ex parte communications. However, **in a DSA revenue generating event after the close of the comment period, certain FTC officials met with DSA members on October 23-24, 2008, in Alexandria, Virginia.** Details of these ex parte communications are included in the Notice of Corruption at the end of these comments. It should also be noted that **no transcript has been provided by the FTC of such ex parte communications where the Business Opportunity Rule was discussed.**

These ex parte communications are just one of many strong pieces of evidence of collusion between certain present and former FTC officials and the DSA. Another revealing example is the attempt to influence the IPBOR by comments on behalf of DSA members from former high level FTC officials, including Timothy Muris, Howard Beales III, and Jodi Bernstein. It is very disturbing to us as consumer advocates to see this radical transformation by these officials we once trusted from consumer protection to fraud protection.

This also raises the question of what direct or implied enticements DSA members have offered to current officials for supporting the MLM exemption in promises of lucrative consulting jobs, etc., following FTC employment. This and related corruption of the rulemaking procedure deserve Congressional investigation. **At the very least, the Commissioners should be asking how it is that certain FTC officials have allowed the DSA to roam so unbridled over the rulemaking process.**

²⁹ Footnote 34 of the RPBOR announcement:

"Multi-level marketing is one form of direct selling, and refers to a business model in which a company distributes products through a network of distributors who earn income from their own retail sales of the product and from retail sales made by the distributors' direct and indirect recruits. Because they earn a commission from the sales their recruits make, each member in the MLM network has an incentive to continue recruiting additional sales representatives into their 'down lines.' "• See Peter J. Vander Nat and William W. Keep, *Marketing Fraud: An Approach to Differentiating Multilevel Marketing from Pyramid Schemes*, 21 J. of Pub. Policy & Marketing (Spring 2002), ("Vander Nat and Keep") at 140. See also rebuttal to DSA Comments,

Part 1: www.ftc.gov/os/comments/bizoprevised/rebuttals/535221-00081.pdf

5. Other rulemaking irregularities include refusal to answer one key question at the Workshop, while responding to others.

At the June 1 Workshop, Ms. Benway answered Mr. Hailey's question about the legal action section of the form – and even discussed Tupperware's lead generation system with Ms. Morrissey (to whom was shown great deference and who was allowed to pitch both Tupperware and the DSA), as well as defending her use of the DSA Code of Ethics, but refused to answer my question about the obvious contradiction discussed in #1 above.

6. The cost effectiveness of a Rule promoting transparency – vs. utilizing Section 5 on a case-by-case basis – was ignored in RPBOR. Without hugely increasing the personnel at the FTC, it would be impossible to keep up with the MLMs that are forming every year, many if not most of them violating Section 5.

In the April 24 announcement of the Workshop, the FTC also stated in Footnote 7:

. . . In the RPBOR, the Commission stated its belief that consumer harm flowing from deceptive practices in the MLM industry could be more effectively addressed through the use of Section 5 of the FTC Act.

As a business model predicated upon infinite expansion (endless chain of recruitment) in a finite marketplace, MLMs are inherently flawed, uneconomic, and fraudulent. In spite of this mathematical reality, the FTC admitted in the RPBOR announcement that the FTC had used Section 5 in actions against only 14 MLMs in the past ten years. However, FTC officials were in a position to know of the research I cited in my comments showing evidence that at least 250 MLMs (out of over 1,000 extant, according to some industry observers), are currently violating Section 5 and that at least 81 of these are members of the DSA, which has so vigorously objected to a rule requiring their members to provide greater transparency to protect consumers against unfair and deceptive practices.

Extensive research I and others have performed (reported on mlm-thetruth.com) has demonstrated that the compensation plan of an MLM can determine the extent to which a program depends upon aggressive recruitment by new recruits of a large downline of self-consuming participants in order to profit from the scheme. When this is the case, the MLM is merely a money transfer scheme. (See FTC Staff Advisory letter dated January 14, 2004, from James Kohm to DSA president Neil H. Offen). In other words, they are structured to transfer money from those at the bottom to founders and TOPPs (Top-of-the-pyramid promoters). They accomplish this by using purchases of (usually overpriced) products to disguise or launder their investments in a product-based pyramid scheme.

Such emphasis on revenues from “internal consumption” is positive proof that an MLM is conducting an unfair and deceptive practice in violation of Section 5. Please review the speech on “Pyramid Schemes” by Debra Valentine, General Counsel of the FTC, delivered May 13, 1998, sponsored by the International Monetary Fund. Note the section titled: “What is a Pyramid Scheme and What is Legitimate Marketing?” *Note that she asked “What is legitimate marketing? – not legitimate multi-level marketing – an oxymoron to those who understand how sales and recruiting are incentivized in typical MLMs.*

In every MLM for which I could obtain the compensation plan, I found five causative and defining characteristics of a recruiting MLM, or product-based pyramid scheme. Please read my “*5 Red Flags: Five Causative and Defining Characteristics of Recruiting MLMs, or Product-based Pyramid Schemes*” on my web site – mlm-thetruth.com. This report is a summary of literally thousands of pages of research and feedback from all over the world. In every case where data was available on MLMs with these five red flags, the percentage of people losing money was about 99%. Robert Fitzpatrick of Pyramid Scheme Alert found essentially the same thing in his report “*The Myth of ‘Income Opportunity’ in Multi-level Marketing*”

(pyramidschemealert.org). The FTC is in possession of this information as recorded in prior comments by myself and Mr. Fitzpatrick.

Since nearly every MLM I have studied (by now over 300) has these five characteristics, it can be assumed that the vast majority of all MLMs will also have these characteristics, making them likewise unfair and deceptive practices. Army Diller lists over 1,000 past and present MLMs at - www.armydiller.com/financial-scam/links.htm#complaintsmmlm

Even if we assume that the number of MLMs with compensation plans that make them merely money transfer schemes – or product-based pyramid schemes – totaled only 500, with at least 50 new schemes originating every year (I personally encounter about one new MLM every week), it would be impossible for the FTC to keep up with them using Section 5 on a case-by-case basis. At the rate of 14 cases every ten years, **applying Section 5 would require 357 years for the FTC to act against the existing base of MLMs, and the FTC would have to increase its staff at least tenfold just to keep up with fraudulent new MLMs forming every year. The DSA recognizes that it is in its members' best interest to get the FTC to exclude them from having to make meaningful disclosures, and to instead fall back on Section 5, since it would make the threat that any of their many members (violating Section 5) would have to deal with FTC regulation rare to non-existent. By the time the FTC finally got around to investigating any given MLM using Section 5, all the principals would likely be long dead.**

The Business Opportunity Rule requiring meaningful disclosure by ALL sellers of business opportunities would be far more cost effective than exempting MLMs from the Rule – and instead relying upon section 5 to protect against unfair and deceptive practices. I seriously doubt that had the Commissioners been informed of this reality, they would have voted 4-0 in favor of RPBOR. The exemption of MLMs is not consistent with the FTC's practice of using industry-wide rules to more efficiently discourage unfair and deceptive practices than relying on case-by-case enforcement.

7. The FTC may have exceeded its authority in defining “business opportunity” so narrowly by excluding MLM in RPBOR.

In the announcement of the Workshop, the FTC also states:

... It [the RNBOR] narrowed the scope of the IPBOR by significantly revising Section 437.1 by redefining the term “business opportunity.” (April 24 Federal Register, Footnote 7)

The DSA is a lobbying and trade organization representing direct sellers in the United States, many of whom – especially MLMs – could be classified as business opportunity sellers. In 2007, according to the DSA, 98.2% of all individual sellers in the United States were compensated under an MLM compensation plan, leaving only 1.8% compensated under a single level compensation plan.

(<http://www.dsa.org/pubs/numbers/07gofactsheet.pdf>) And in 2007 the DSA claimed to have 285 MLM direct sellers whose collective MLM sales forces total 15 million distributors. This would suggest that DSA members comprise by far the largest group of business opportunity sellers in the United States. The FTC notice states: “Business opportunity ventures include vending machine routes, rack display operations, and medical billing ventures.” To anyone familiar with the business opportunity market, complaints about these three represent only a tiny percentage of problems needing consumer protection.

There is a real question as to whether or not the FTC even has the authority to define business opportunity so narrowly as to limit the Rule to such a miniscule portion of the marketplace of business opportunities; i.e., non-MLM sellers. This makes about as much sense as a Franchise Rule exempting all food services because requiring them to disclose information might contribute to world hunger.

8. The acceptance of the “too great a burden” argument against a one-page disclosure form by MLMs is such an obvious absurdity that only FTC officials partial to the DSA/MLM lobby or those unaware of other disclosure requirements, such as franchises or securities, would have accepted it.

Several panel members at the workshop referred to the issue of the burden of disclosing certain information on a one-page form to those being sold Business Opportunities. However, the FTC requires a Franchise Disclosure Document by franchisors be supplied to prospective franchisees that can be hundreds of pages in length. The IPBOR would have required only a single page disclosure form (plus any supporting information of average earnings, etc.) be provided by business opportunity sellers. But the DSA/MLM and their minions protested it would be “too great a burden” to supply each prospect with only a couple pieces of paper provided by the company. This makes about as much sense as the FTC not requiring franchisors to provide a Franchise Disclosure Document – or the SEC exempting all private corporations from having to publish annual and quarterly reports because it would place “too great a burden” on them to comply.

The “too great a burden” argument is just one of many put forth by the DSA and its many minions and accepted by the FTC. The “too great a burden” argument is so absurd as to not require further comment, yet the RPBOR clearly shows FTC officials accepting it, again raising serious questions about the motivation behind such cooperation between certain FTC officials and the DSA/MLM lobby. Two and two do not equal five, even if 17,000 commenters claim it is so.

9. The suggestion in the Workshop announcement that disclosures by MLMs would not help consumers is a manifestly bogus argument – as are other arguments for exempting MLM from the Rule. Two and two do not equal five, even if 17,000 commenters claim it is so.

In the April 24 announcement of the Workshop, the FTC stated in Footnote 7:

. . . The RNPR noted that while some MLMs do engage in unfair or deceptive acts or practices, including the operation of pyramid schemes or unsubstantiated earnings claims that cause consumer harm, commenters generally agreed that the IPBORs required disclosures would not help consumers identify a fraudulent pyramid scheme.

In my comments regarding IPBOR, I suggested that MLMs would attempt to circumvent honest disclosure in such a Rule, such as Nu Skin has done in its compliance with the 1994 Order for Nu Skin to cease its misrepresentations of earnings of distributors³⁰. When MLMs do disclose earnings, they do everything they can to report in such a way as to disguise the truth; viz., that it is extremely rare for anyone to realize a net profit from their pay plan. However, I was in no way suggesting that such disclosures could not help any consumers identify a fraudulent scheme. Some sophisticated consumers may understand the statistics. And such data could be analyzed, debunked, reported by independent analysts, and then conveyed to consumers in print or online. This would not be possible if no data were made available.

Of course, nearly all the DSA/MLM commenters “generally agreed that the IPBOR’s required disclosures would not help consumers identify a fraudulent pyramid scheme.” This response from MLM parties should have been expected, as the last thing MLM promoters want is for the truth to be made obvious – that they are unprofitable for all but the founders and a few TOPPs (top-of-the-pyramid promoters). But regardless of the number of MLM proponents who agreed that disclosure would not help consumers, this should not be accepted by the FTC as fact, but recognized for what it is – desire by MLMs to protect their capability to continue defrauding consumers without regulatory scrutiny.

Other typical DSA arguments that were used to gain an exemption for its member MLM firms (many of which were reiterated by Ms. Morrissey and others at the workshop) include:

- Multi-level marketing is equated to legitimate direct selling. My analysis of over 300 MLM programs reveals that MLMs rarely incentivize direct selling to the public sufficiently to outweigh the enormous incentives to recruit a huge downline, which is where any profits are realized. Participants are primarily incentivized to do pyramid or chain selling, not direct selling.

³⁰ See REPORT OF VIOLATIONS of the FTC Order for Nu Skin to cease its misrepresentations of distributor earnings, linked from the Law Enforcement page of my web site – www.mlm-thetruth.com

- MLM is presented as a business with little risk, as the signup fee is small. But this is merely a ruse, as major ongoing incentivized purchases (often \$50 to \$300 a month) are required in nearly all MLMs in order to qualify for commissions or advancement in the scheme. And those who invest the most tend to lose the most – some many thousands of dollars.
- MLM companies who are members of the DSA are subject to its Code of Ethics. But members who were found guilty of conducting illegal pyramid schemes were members of the DSA in good standing at the time³¹. And it is clear from its Code of Ethics that the DSA allows pyramid or endless chains schemes among its membership.³²
- Many MLM participants merely work part-time or seasonally to earn enough for Christmas or to meet other temporary needs. Only a person unfamiliar with the compensation plans of MLM companies would accept such a claim. All of the MLMs who are members of the DSA use compensation plans that require enormous full-time and long-term commitment to building and maintaining large downlines before they can realize significant profits. The only way a person could earn enough in commissions to exceed incentivized purchases and minimal operating expenses is if products were priced competitively to make possible sales to the general public. But my studies and those of other independent analysts has shown prices anywhere from two to six times as much as products sold through more standard outlets.
- For the same reason, the DSA argument that many join one of their MLMs just to get the products at retail just does not hold water. Even at wholesale, the products cannot compete with alternative outlets.

Refer to my previous comments in IPBOR and RPBOR for other weak arguments put forth by the DSA and apparently accepted by the FTC to gain the MLM exemption. FTC personnel had access to all of the information rebutting with irrefutable evidence the fallacy of DSA arguments. If you take away these bogus arguments, there is no justification - for any informed official or analyst not sponsored by the MLM industry - for exempting MLM from the Rule. So this again calls into question the motivation of those FTC personnel who used these bogus arguments as justification for exempting MLM from the ambit of the Rule.

10. For the RPBOR form, the most important disclosure a business opportunity seller can provide is breakdown of earnings of participants. False earnings claims are typical of MLM sellers, so MLMs must not be excluded from the Rule.

After reading IPBOR, RPBOR, the consultant's report on the BOR form, and related materials, one can safely conclude the following:

- a) The making of false earnings claims is the most prevalent problem in the offer and sale of business opportunities.
- b) The making of false earnings claims underlies virtually all fraudulent business opportunity schemes.
- c) Earnings claims lie at the heart of business opportunity fraud, and are typically the enticement that persuades consumers to invest their money.
- d) Earnings claims are highly relevant to consumers in making their investment decisions and typically are the single most decisive factor in such decisions.
- e) Earnings claims are the most salient feature of sales (and recruiting) presentations made by business opportunity sellers.

³¹ Equinox, Trek Alliance, etc.

³² **Pyramid Schemes (DSA Code of Ethics #6)** For the purpose of this Code, pyramid or endless chain schemes shall be considered consumer transactions actionable under this Code. **The Code Administrator shall determine whether such pyramid or endless chain schemes constitute a violation of this Code** in accordance with applicable federal, state and/or local law or regulation.

- f) MLMs as business opportunities, often deceive consumers with the promise of large potential income and are thereby highly successful in attracting prospective investors.
- g) By far, the most frequent allegations in business opportunity cases pertain to false or unsubstantiated earnings claims.

The FTC has brought over 140 cases against a multitude of business opportunities and related schemes (including MLMs and pyramid schemes), each of which lured unsuspecting consumers through false or deceptive earnings representations.

Narrowing the definition of “earnings claims” could weaken protections regarding the most salient feature of the sales presentation by allowing sellers to avoid disclosing the average incomes of participants at ascending levels in the pay plan.

For MLMs, the impetus for making false income claims is the compensation plan which incentivizes promising whatever will entice prospects to join one’s downline.

According to the FTC, the catalyst for making false earnings claims is the MLM compensation model “because they earn a commission from the sales their recruits make, each member in the MLM network has an incentive to continue recruiting additional sales representatives into their “down lines.” (Revised Rule, p. 15)

As independent analysts, both Robert Fitzpatrick³³ and I³⁴ have done extensive analyses based on the actual reports of average incomes of participants in MLM programs for which data is available to prove that 99-99.9% of participants in their programs lose money. Even promoting such MLMs as income or business opportunities, when the odds of profiting are far greater for gambling in Las Vegas, is deceptive.

This all adds up to the necessity, not just advisability, to include MLMs in the Rule, primarily to assure meaningful disclosure of average earnings of participants at the different levels in the pay plan. This is essential to protect against unfair and deceptive practices, especially false earnings claims.

11. If the Revised Rule (RPBOR) were enacted, consumers would be misled into believing that the FTC’s Business Opportunity Rule provides protection against fraudulent, unfair, and deceptive practices, when in fact it will do just the opposite.

Since any business opportunity seller can easily qualify as an MLM and thereby gain exemption from the Rule, they will likely do so, leaving virtually no business opportunity sellers covered by the Rule. Also, it is not difficult to envision MLM promoters emboldened in their deceptive recruiting practices and saying to prospective recruits: “Our MLM is a legitimate business model. If it were not, it would certainly come under scrutiny by the FTC or other regulatory agencies set up to protect against unfair and deceptive practices.”

While a Business Opportunity rule is certainly needed, this Revised Rule is not the answer, but could have extremely harmful unintended consequences for consumers. It would be far better for the FTC to scrap the Rule altogether than to let it go forward with the MLM exemption.

This is one of those cases in which **no rule is better than a bad rule.**

12. Considering the above, the Workshop was a sham, and the form is irrelevant. In exempting MLM from the Rule to satisfy the DSA, the FTC is abandoning its mission to protect consumers from unfair and deceptive practices.

³³ “The Myth of Income Opportunity in Multi-level Marketing” is available for downloading from the web site – www.pyramidschemealert.org.

³⁴ Several reports on MLM loss rates are linked from the Statistics page on my web site – www.mlm-thetruth.com.

As an analyst and advocate for the tens of thousands of victims and their families who have visited my web site (www.mlm-thetruth.com, as well as www.pyramidschemealert.org – for which I am an advisor), there is ample reason for the DSA to so vigorously object to requiring transparency among its members. Those reasons are all tied to the FTC's role to “prevent fraudulent, deceptive, and unfair business practices and to provide information to help spot, stop, and avoid them.” The DSA thereby presents a direct challenge to all that the FTC is about.

As one who has by now studied the compensation plans of over 300 MLMs, I can testify that **virtually all MLMs employ a business model that assumes infinite expansion in finite markets, which makes them inherently flawed, uneconomic, and fraudulent.** What should surprise FTC officials is that there were only 17,000 comments out of approximately 30 million participants (according to the DSA) in several hundred MLMs, some with gigantic pyramids of participants – all hoping to eventually earn a profit, but with less than 1% ever receiving enough to exceed their expenses; i.e., meeting quotas of product purchases, training costs, and minimal operating expenses. In other words, for those MLMs for which reliable data is available, approximately 99 out of every 100 participants lose money. And yet these same MLMs are promoted by sellers as the answer to consumers' financial woes. **MLM is almost by definition (infinite expansion within finite markets) an unfair and deceptive practice,** and in addition is both **viral** (all are built up by an endless chain of aggressive recruitment) and **predatory** – taking advantage of the most vulnerable populations among us. If FTC staff were to attend (unannounced) very many MLM recruitment rallies, as I have, they would see the truth of all that I am saying – and reporting on my web site. With 99% doomed to financial loss, why would FTC officials cave to the DSA's demand that MLMs be excluded from the RPBOR? Their motivation must be examined.

It is my hope that the FTC will stop pursuing a disastrous course in abandoning its mission to protect consumers by yielding to the enormous pressure placed upon certain FTC officials by the DSA. Relying on Section 5, rather than the Rule for MLMs would be allowing consumers to be victimized by endless chains of MLM recruiters, and then left like sheep wandering without protection in an enclosure full of wolves.

IMPORTANT NOTE TO FTC STAFF:

Inasmuch as the transcript of the Workshop was not made available until one working day before this June 15 deadline, I reserve the right to comment further after more thoroughly analyzing the transcript.

NOTICE OF CORRUPTION of the Proposed Business Opportunity Rule

By Jon M. Taylor, MBA, Ph.D., Consumer Awareness Institute,
and Advisor, Pyramid Scheme Alert

In April, 2006, in an effort to curtail false earnings representations and other abuses of business opportunity sellers, the FTC proposed a Business Opportunity Rule and invited comments from the public. However, a serious corruption of the rule-making process has occurred with respect to the original and a Revised Business Opportunity Rule³⁵, as outlined below.

1. The initial Proposed Business Opportunity Rule led to over 17,000 comment letters, the vast majority of them from MLMs (multi-level marketing companies) and participants in MLM/pyramid/chain selling schemes. They claimed the rule would threaten their livelihood. This is not surprising, since extensive research shows that 99% of participants in such schemes lose money, and disclosure of meaningful information such as average earnings (or losses) of participants, would discourage prospective recruits from joining and buying into their programs. *It could dash any hope by participants in these schemes of recovering their*

³⁵ In a press release posted on the FTC web site in April 2006, the FTC proposed –

... a rule to protect consumers from bogus business opportunities and further enhance law enforcement efforts in this area. The rule would cover business opportunities commonly touted by fraudsters, while minimizing compliance costs for legitimate businesses. Currently, the FTC brings law enforcement actions against fraudulent business opportunities under two laws, the Franchise Rule and the FTC Act. Neither is specifically designed for the unique scams that occur frequently with business opportunities. . .

The FTC concluded its press release by asserting its mission: “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.”

investments and of eventually reaping a profit.

2. *Yielding to extraordinary pressure*³⁶, in March, 2008, the FTC altered the proposed Rule to a Revised Business Opportunity Rule (RBOR) that would exempt MLMs³⁷.

³⁶ *At least three of these letters came from former high level FTC officials who at one time worked in important position related to consumer protection. To those of us advocating on behalf of consumers, this turnabout from consumer protection to fraud protection is incredible, since MLM clearly is at the forefront of a business model which is clearly an unfair and deceptive trade practice (Section 5), costing tens of millions of victims worldwide tens of billions of dollars in losses every year.*

The FTC also received letters from 85 Congressmen, who had been successfully lobbied by MLMs to object to the inclusion of MLM in the proposed business opportunity rule. I have not checked their records of campaign contributions to see how much was donated to their campaigns by MLMs and the DSA (Direct Selling Association), *the organization that has aggressively lobbied for the weakening of statutes that protect consumers against pyramid schemes.* This happened in Utah, where I live, when DSA member firms donated extensively to key political figures to assure exemption of MLM from prosecution as pyramid schemes. *Whether or not they paid money to these Congressmen to assure their support, because of their huge numbers of participants in their endless chains of recruitment, their promises of jobs and votes can be very compelling.*

³⁷ After intense lobbying by the DSA (which claims to have 285 MLM members and 13.3 million MLM distributors) to have MLM exempted from the Rule, the FTC proposed a Revised Business Opportunity Rule. In a press release posted on the FTC web site in April 2006, these changes were noted:

After evaluating the comments received on the April 2006 notice, the Commission has decided to issue an RNPR [Revised Notice of Proposed Rulemaking] that is more narrowly focused than the April 2006 proposal. As proposed now, the Business Opportunity Rule would still cover those schemes currently covered by the interim Business Opportunity Rule, and it would expand coverage to include work-at-home schemes. The revised

To independent consumer advocates who are aware of the research (not funded by MLM), this is ludicrous, since non-MLM business opportunity promoters that would be covered are relatively insignificant in comparison, and they do not have the reputation for massive fraud that is characteristic of the hundreds of MLM programs now operating.

3. The FTC proposed instead to use Section 5 to prosecute MLMs on a case-by-case basis. Based on prior experience with FTC inaction against hundreds of product-based pyramid schemes, we see this as totally unworkable. I have personally analyzed over 250 MLM programs and can assert that *virtually all of them are violating Section 5*. The FTC only has sufficient personnel to go after a small sample (less than 1-2%) of them, as in the past. To take one at a time would not only be impractical, but would facilitate the defrauding of millions of persons while waiting for the FTC to get to all the programs. In the meantime, hundreds of additional MLMs would have sprung up, as they are now doing, and millions of additional consumers would be victimized in the interim. No rule would be better than a bad rule, such as this one.
4. After the comment period for rebuttals of comments on RBOR) was closed, I twice emailed Monica Vaca at the FTC, who was at that time administering RBOR. I expressed some concerns about FTC interpretations of my earlier comments and about some unjustified attacks against me personally by an MLM proponent in his comments. Ms. Vaca responded by saying *“it would be inappropriate for staff to consider material that is not part of the rulemaking record.”* My letters are quoted as Appendix A, and her letter

proposal, however, would not reach multi-level marketing companies or certain companies that may have been swept inadvertently into scope of the April 2006 proposal.

is quoted as Appendix B.

5. An informant alerted me to an ex parte communication with at a “Legal Issues of the Day” seminar sponsored October 23-24 in Alexandria, Virginia – by the DSA³⁸. One of the presenters was Lois Greisman, Associate Director of the Division of Marketing Practices at the FTC. Another was Lem Dowdy, FTC Attorney. As indicated in the DSA press release (Appendix C), this was not merely a one-way presentation. Note the following statement:

“Attendees will have the opportunity to ask questions and engage in an open dialogue with these representatives, encouraging understanding between our industry and this important government regulator.”

Note: *The ex parte meeting was a revenue-generating event for the DSA. Specifically, the DSA charged Active DSA members \$575, Direct Selling Non-Members \$2,975, and Supplier Non-Members \$2,600. In an effort to ensure that individuals or entities that opposed the DSA position (in connection with the Rule) from gaining access to this event, the DSA did not allow the media or the public to attend the event.*

6. I wrote Monica Vaca, protesting this ex parte communication – which is clearly forbidden – as indicated in her July 23 letter to me (and as outlined in U.S.C. Title 5, governing, among other things, the conduct of employees of federal agencies to protect against abuses of the rule-making process such as this). My letter is in Appendix D and is followed by Ms. Vaca’s response in Appendix E.

³⁸ **DSA press release, program, and registration costs and restrictions.** See Appendix A for the DSA press release confirming the above. For the official announcement on the DSA web site, go to –

http://www.dsa.org/press/press_releases/index.cfm?fuseaction=show_release&Document_id=1928

The full program can be accessed at –

<http://www.dsa.org/press/misc/index.cfm?documentID=1808>

Registration information can be accessed at –

<http://www.dsa.org/forms/meeting/MeetingFormPublic/view?id=2C1DD00000076>

7. In addition, based on personal information and belief, other individuals advocating for consumers were told they could not communicate with FTC personnel about this matter pending the rule's promulgation. Therefore, apparently *the FTC gave preferential treatment, to the exclusion of other interested parties, to the DSA by the FTC's participation in the DSA ex parte meetings.*
8. In her response, Ms. Vaca attempted to persuade me that the DSA ex parte meeting (which she admitted was attended by Ms. Greisman) was "consistent with our [FTC] rule making procedures." In an attempt to further convince me that the DSA ex parte meeting was appropriate (in compliance with applicable law), Ms. Vaca stated that "FTC staff regularly speaks with . . . trade organizations . . . to provide information about activities going on at the agency that may be of interest to such groups, including our (FTC) regulatory initiatives."³⁹

the Rule. Others believe that Chairman Kovacic, who was appointed to his post by President Bush, allowed the FTC to abandon its duty to consumers as the ultimate "thank you" to the DSA and its members for their financial support of Republican lawmakers.

Whether these beliefs are real or perceived, the significant amount of contributions to Republican lawmakers, at the very least, gives rise to the appearance that these contributions have influenced the decision of the FTC in connection with the Rule – to the great detriment of consumers.

I have no basis on which to rely that Chairman Kovacic, Secretary Clark, or the Commissioners will take the appropriate action to Notice the public that the rulemaking process (in connection with the Rule) has been terminated for the reasons that gave rise to this event; i.e., corruption of the rulemaking process. If the Commission attempts to enact a rule under these circumstances, this information – along with additional information withheld from this writing – will be transmitted to certain interested individuals who have the power and authority to address this issue, with a view to protecting consumers; as opposed to protecting the financial interests of the DSA and its members.

CONCLUSIONS

The FTC had information at least four months before it participated in the DSA ex parte meeting that would have caused a reasonable person, not intent on protecting the DSA's 285 MLM members and their 13.3 million MLM distributors, to question the legality of the practices of DSA member firms.

By participating in the ex parte meeting with DSA members, FTC employees have corrupted the Rule and compromised the integrity and mission of the Federal Trade Commission. As you are well aware, as a matter of law, once a rulemaking process has been corrupted, any final Rule will be invalid.

There are individuals who believe that the FTC abandoned its duty to consumers – in favor of protecting the financial interests of the DSA and its members – because of substantial donations DSA member firms have given to Republican lawmakers; including Republican lawmakers who wrote letters to the FTC in support of the DSA position in connection with

The only reference book of research on MLM as a business model and as an industry by qualified independent experts who volunteer resources advocating for consumers was dismissed by FTC staff handling BOR

Towards the end of the BOR rulemaking process, I completed the first edition of a reference book in which I compiled the research that had been done on the profitability (or lack thereof) of MLM as an industry. The inherent flaws in MLM as a business model were examined. These include the assumption of an infinite market, which does not exist in the real world. It also assumes a virgin market, which doesn't exist for long. In all of the compensation plans of the approximately 500 MLMs I have examined, they are built up by unlimited recruitment of a whole network of endless chains of participants. So it is logical to conclude that MLM as a business model is inherently flawed, unfair and deceptive.

But rather than form our conclusions from mere logic, I gathered promotional material and data on average incomes of participants from every MLM company that had released such data. Then using conservative assumptions on expenses and attrition rates in the MLMs' favor, I was able to come up with an average loss rate of 99.7%. This is all spelled out in my later comments sent to the FTC.

These numbers and quotes from MLM promotional materials on which this research was based were not manufactured, but obtained directly from company sources. The evidence of massive fraud in fundamentally flawed MLM systems is explained in earlier chapters of my book.⁴⁰ In the Introduction are letters from financial experts who validate the methodology and the calculations underlying the abysmal loss rates (averaging 99.7%), billions of dollars in aggregate losses, and millions of victims of MLM programs worldwide.

Although my research data (and others cited) was gathered from the MLM companies' official web sites and other publications and my methodology and calculations of MLM loss rates were validated by the financial experts quoted above, the FTC staff chose to dismiss it as "not approved by the FTC." How convenient. They could then save the trouble of reading the voluminous evidence that I and others had compiled, and they could act in accordance with the wishes of the DSA/MLM lobby, which had put tremendous pressure on them to exempt MLM from the ambit of the Rule.

At any rate, the FTC staff chose to ignore this evidence to avoid coping with the disapproval of a powerful DSA lobby. (And there is the possibility of an implied promise of a profitable position after leaving the DSA, as with other high level officials who left the agency.)

It is also possible that the staff simply lacked the background in business math and statistics to understand the validity and significance of our reports. If so, they should have hired someone who did. (They hired a consulting firm to design a simple form.) See the letter that follows from FTC staffer Christine Todaro to another staff member – whose name is blocked out in the documents we received in response to an FOIA request

⁴⁰ *Multi-level Marketing Unmasked* (formerly *The Case against Multi-level Marketing – an Unfair and Deceptive Practice*).

From: Todaro, Christine <ctodaro@ftcexchange.com>
Sent: Friday, October 7, 2011 5:12 PM
To: (b)(6)
Subject: Re: Asking about Consumer Awareness Institute

Mr. (b)(6)

Thank you for your question.

When the FTC engages in rulemaking pursuant to its authority under 15 U.S.C. Section 57a, the FTC solicits comments from interested parties. For the Business Opportunity Rule, the FTC solicited comments throughout the rulemaking proceedings. The comments received are not approved by the FTC. Those comments, however, do become part of the rulemaking record.

Last November, the FTC asked interested parties to comment on the recommendations announced by the Staff Report on the Business Opportunity Rule. See 75 FR 68559. The Staff Report on the Business Opportunity Rule is available here: <http://www.ftc.gov/os/fedreg/2010/october/101028businessopportunitiesstaffreport.pdf>. Mr. Taylor submitted comments on the Staff Report on the Business Opportunity Rule. His comments referred to the publication, "THE CASE (FOR AND) AGAINST MULTI-LEVEL MARKETING: The Complete Guide to Understanding and Countering the Effects of Endless Chain Selling and Product-based Pyramid Schemes" by Jon M. Taylor, MBA, Ph.D. This publication has not been approved by the FTC. Nor has the research discussed in the publication been approved by the FTC. As with the other comments submitted, Mr. Taylor's comments are now part of the rulemaking record.

Comments received by the FTC are publicly available on the FTC Website, to the extent practicable. Mr. Taylor's comments, along with the comments from various other individuals and entities who submitted comments on the Staff Report on the Business Opportunity Rule, are available at <http://www.ftc.gov/os/comments/bizoppstaffreport/>.

Thank you,

Christine M. Todaro
Federal Trade Commission
600 Pennsylvania Ave., N.W.
Washington DC 20580
(202)326-3711 (p)
(202)326-3395 (f)

The Final BOR was issued in December of 2011.

Federal Register – 16 CFR Part 437 Business Opportunity Rule

For a complete copy of the FTC Final Business Opportunity Rule, together with extensive FTC staff commentary, go to – www.mlmllegal.com/images/FTC_Final_Bus_Opp_Rule_Dec_2011.pdf

For Release: 11/22/2011

FTC Adds New Protections for Consumers Seeking to Work from Home

The Federal Trade Commission has approved changes to its Business Opportunity Rule that will ensure that consumers have the information they need when considering buying a work-at-home program or any other business opportunity. The changes simplify the disclosures that business opportunity sellers must provide to prospective buyers. The simplified disclosures will help prospective purchasers assess the risks of buying a business opportunity, while minimizing compliance burdens on businesses.

In addition, the [Final Rule](#), which will be effective on March 1, 2012, applies to business opportunities previously covered under the Rule, as well as work-at-home offers such as envelope stuffing and craft assembly opportunities. The final Rule requires business opportunity sellers to give consumers specific information to help them evaluate a business opportunity. Sellers must disclose five key items of information in a simple, one-page document:

- the seller's identifying information;
- whether the seller makes a claim about the purchaser's likely earnings (and, if the seller checks the "yes" box, the seller must provide information supporting any such claims);
- whether the seller, its affiliates or key personnel have been involved in certain legal actions (and, if yes, a separate list of those actions);
- whether the seller has a cancellation or refund policy (and, if yes, a separate document stating the material terms of such policies); and
- a list of persons who bought the business opportunity within the previous three years.

Misrepresentations and omissions are prohibited under the Rule, and for sales conducted in languages other than English, all disclosures must be provided in the language in which the sale is conducted.

Consumers should use the disclosure document and supplementary information to fact-check sellers' sales pitches. This information will be helpful to consumers like Teresa Yeast, a stay-at-home mother who purchased a craft-assembly work-at-home program from a company called Darling Angel Pin Creations. The FTC filed a law enforcement action against that company in February 2010 for allegedly claiming that consumers could make hundreds of dollars assembling angel pins at home. "It's important to be skeptical and to be cautionary when you're approached with ... a business opportunity," Mrs. Yeast said. "I saw an opportunity that looked great, and took it. They took my money."

The announcement of a final Business Opportunity Rule completes the process that started when the Commission published an Initial Notice of Proposed Rulemaking and proposed creating a Business Opportunity Rule separate from the Franchise Rule. The FTC issued a Revised Proposed Business Opportunity Rule and conducted a public workshop, and the staff issued a Staff Report. At every stage of the Rule amendment proceeding, the Commission solicited comment on the economic impact of the Rule, as well as the costs and benefits of each proposed amendment. In issuing the final Rule, the Commission has carefully considered the comments received and the costs and benefits of each amendment.

To find out more about business opportunity sellers' compliance obligations, read [Selling a Work-at-Home or Other Business Opportunity? Revised Rule May Apply to You](#) or watch this new [video](#). Consumers thinking about buying a business opportunity should read [Looking to Earn Extra Income? Rule Helps You Avoid Bogus Business Opportunity Offers](#) to learn more about the final Rule.

The Commission vote approving the final amendments to the Business Opportunity Rule was 4-0.

The Federal Trade Commission works for consumers to prevent fraudulent, deceptive, and unfair business practices and to provide information to help spot, stop, and avoid them. To file a complaint in English or Spanish, visit the FTC's online [Complaint Assistant](#) or call 1-877-FTC-HELP (1-877-382-4357). The FTC enters complaints into Consumer Sentinel, a secure, online database available to more than 2,000 civil and criminal law enforcement agencies in the U.S. and abroad. The FTC's website provides free information on a variety of [consumer topics](#). Like the FTC on [Facebook](#) and follow us on [Twitter](#).

MEDIA CONTACT: Office of Public Affairs 202-326-2180 (Bus Opp Rule)

The 17,000 pro-industry comments were given greater weight than the united voice of unpaid consumer advocates who objected to the MLM exemption.

Is rulemaking merely a numbers game? Should the FTC staff have been impressed that 17,000 commenters complained about the Rule including MLM, when the FTC/MLM lobby sent an appeal to as many as 1,000 times that many to comment? (And as we learned from our telephone survey, most of those commenters were in favor of the disclosures in IPBOR when it was explained to them, and some of them did not send the comments themselves.)

I am quoting here some excerpts relating to the MLM exemption, as the rest of the 46-page statement in the Federal Register is essentially irrelevant. In effect, with the MLM exemption, the Rule becomes a non-rule. Packaged business opportunities are incentivized to convert to an MLM format, even though it is deeply flawed, in order to escape having to comply with the Rule.

(Footnotes are excluded in these excerpts.
Comments by Dr. Jon Taylor are in brackets and emphases are his.)

76816 Federal Register / Vol. 76, No. 236 / Thursday, December 8, 2011 / Rules and Regulations

**FEDERAL TRADE COMMISSION
16 CFR Part 437
RIN 3084-AB04
Business Opportunity Rule**

AGENCY: Federal Trade Commission
(FTC or Commission).
ACTION: Final rule.

Revised Notice of Proposed Rulemaking (“RNPR”), a public workshop, a Staff Report, and other information discussed herein. This document also contains the text of the final Rule and the Rule’s Statement of Basis and Purpose (“SBP”), including a Regulatory Analysis.
DATES: The provisions of the final Rule will become effective on March 1, 2012.

SUMMARY: The Commission is adopting final amendments to its Trade Regulation Rule entitled “Disclosure Requirements and Prohibitions Concerning Business Opportunities” (“Business Opportunity Rule” or “Rule”). Among other things, the Business Opportunity Rule has been amended to broaden its scope to cover business opportunity sellers not covered by the interim Business Opportunity Rule, such as sellers of work-at-home opportunities, and to streamline and simplify the disclosures that sellers must provide to prospective purchasers. The final Rule is based upon the comments received in response to an Advance Notice of Proposed Rulemaking (“ANPR”), an Initial Notice of Proposed Rulemaking (“INPR”), a

(I) B. Rule Amendment Proceedings

1. Initial Notice of Proposed Rulemaking and Initial Proposed Business Opportunity Rule

In 2006, having determined that a separate business opportunity rule was necessary, the Commission published an Initial Notice of Proposed Rulemaking (“INPR”), announcing its intention to proceed with its proposal for a separate Business Opportunity Rule (the “initial proposed Business Opportunity Rule” or “IPBOR”). The INPR proposed to amend the interim Business Opportunity Rule by updating it, streamlining it, and expanding its

scope of coverage. *The IPBOR contained an expansive definition of “business opportunity” that encompassed business opportunities previously covered by the Original Franchise Rule as well as work-at home, medical billing, and multi-level marketing (MLM) operations. It also eliminated the \$500 threshold for Rule coverage.*

In response to the INPR, the Commission received more than 17,000 comments, the overwhelming majority of which came from individuals active in the MLM industry. MLM companies, their representatives and trade associations, as well as individual participants in various MLM plans, expressed grave concern about the burdens the IPBOR would impose on them and urged the Commission to exclude them from the scope of the IPBOR, to implement various safe harbor provisions, and to reduce the required disclosures. The Commission also received approximately 187 comments, primarily from individual consumers or consumer groups, in favor of the IPBOR. Only a handful of comments came from non-MLM companies and industry groups, expressing various concerns about obligations that the IPBOR would impose upon them. None of the comments addressed the form of the initial proposed disclosure document.

2. The Revised Notice of Proposed Rulemaking and Revised Proposed Business Opportunity Rule

Second, the Commission determined that the IPBOR was unworkable with respect to MLMs and would have imposed greater burdens on the MLM industry than other types of business opportunity sellers without sufficient countervailing benefits to consumers. After careful consideration of the record, the Commission decided to narrow the scope of the RPBOR to avoid broadly sweeping in all sellers of MLM opportunities. This decision was based on the overwhelming majority of the

approximately 17,000 comments that argued that the IPBOR failed to differentiate between unlawful pyramid schemes – which the Commission intended to cover – and legitimate companies using an MLM model.

[As discussed above, this is a distinction without a difference, except that of no-product vs. product-based pyramid schemes. In fact, of the two, product-based schemes, or MLMs, are far worse by any measure – loss rate, aggregate losses, and number of victims. – JMT]

The RNPR sought public comment on issues relevant to the Commission’s consideration of the RPBOR, including whether the RPBOR would adequately accomplish the Commission’s stated purpose of protecting consumers against fraud and, if it did not, what alternatives the Commission could consider. ***In contrast to the INPR, which generated more than 17,000 comments, the Commission received fewer than 125 comments and rebuttal comments in response to the RNPR. Again, however, the vast majority of commenters were from the MLM industry, but this time they supported the Commission’s proposal to narrow the scope of the Business Opportunity Rule, albeit with suggestions for finetuning. It is noteworthy that only one comment came from a business opportunity seller. The Commission also received comments from two consumer groups and approximately twelve individuals who expressed their disappointment that the FTC’s proposed rule would exclude MLMs from coverage.***

2. The Revised Notice of Proposed Rulemaking and Revised Proposed Business Opportunity Rule

Based on an extensive review of the comments received in response to the INPR and the Commission’s law enforcement history, the Commission issued a revised Notice of Proposed Rulemaking (“RNPR”) on March 28, 2008, that set forth a revised proposed Rule (the “Revised Proposed Business

Opportunity Rule” or “RPBOR”) that was more narrowly tailored than the IPBOR.

In the RNPR, the Commission recognized that there were two main problems with the IPBOR’s breadth of coverage. First, the IPBOR would have unintentionally swept in numerous commercial arrangements, including retail product distribution, training and/or educational organizations, where there was little or no evidence that fraud was occurring. Recognizing this legitimate concern, the Commission, in the RNPR, proposed to narrow the definition of “business opportunity.” Specifically, the RPBOR provided that the “required payment” prong of the business opportunity definition would not include payments for the purchase of reasonable amounts of inventory at bona fide wholesale prices; eliminated as an element of the business opportunity definition the making of an earnings claim; and narrowed the types of “business assistance” that would trigger the business opportunity definition to just those types of assistance that are the hallmark of business opportunity fraud: Location, account, and “buy-back” assistance.

3. Consumer Testing of Disclosure Document and Public Workshop

In the RNPR, the Commission announced that it had retained a consultant to assess the proposed disclosure document, with the objective of achieving the proper format and content for communicating material information to consumers. Following publication of the RNPR, Macro International, Inc. (“Macro”), the FTC’s consultant, conducted extensive consumer testing of the initial proposed disclosure document that resulted in substantial improvement to both the layout and the wording of the form.

[It would be interesting to know how much was paid to Macro for this exercise in futility – a waste of taxpayer dollars – as was the whole rulemaking process, considering the dismal outcome for consumers. – JMT]

The Commission made Macro’s report as well as the revised proposed Business Opportunity Disclosure Document

(“revised proposed disclosure document”) public in a Federal Register Notice (“Workshop Notice”) that also announced a one-day public workshop in Washington, DC. The Workshop Notice focused on whether the revised proposed disclosure document was an effective means of conveying material information to prospective purchasers of business opportunities. The Workshop Notice also sought comment to further develop the public record on issues that had been raised in the comments received in response to the RNPR. *Five individuals who represented a range of interests in the proposed Rule were chosen to participate as panelists, including a federal law enforcer, a state law enforcer, a consumer advocate [just one representing consumers nationwide – JMT], the general counsel of a national multi-level marketing company, and a former director of the FTC’s Bureau of Consumer Protection.* Staff convened the public workshop with these five panelists in Washington, DC, on June 1, 2009. At the conclusion of the workshop discussion of the revised proposed disclosure document, panelists and audience members were invited to express their views about other issues related to the RPBOR. Following robust discussion on various topics, the Commission received follow-up written comment from six individuals and entities.

4. Staff Report

Pursuant to the Rule amendment process announced in the INPR, the Commission’s Bureau of Consumer Protection issued a Staff Report on the Business Opportunity Rule in November 2010. The Staff Report explained in detail the history of the Rule amendment proceeding and summarized the issues raised during the various notice and comment periods, particularly those raised in response to the RNPR. It also addressed the public workshop discussion and subsequent comments, as well as additional issues that the staff raised on its own initiative, based on the Commission’s law enforcement experience.

Twenty-seven comments were submitted in response to the Staff

Report, including eleven comments submitted by consumer group Consumer Awareness Institute (“CAI”). The Commission also received comments from the Department of Justice (“DOJ”), the Direct Selling Association (“DSA”), MLM companies,⁴⁵ one franchise lead generator, a consumer group named Pyramid Scheme Alert (“PSA”), and ten individuals. A few commenters suggested changes to some of the Rule’s definitions and the scope of coverage,⁴⁶ while others encouraged the Commission to adopt the Rule as recommended in the Staff Report. The majority of comments submitted by individuals, and the comments submitted by CAI and PSA, opposed the Commission’s decision to narrow the scope of the Rule to avoid broadly sweeping in MLMs. In crafting the final Rule, the Commission has carefully considered the comments received in response to the Staff Report and throughout the Rule amendment proceeding.

[Carefully? Perhaps someone scanned the comments of consumer advocates, but they dismissed our research, which showed indisputable proof of widespread fraud in the MLM industry. Or perhaps they just did not have the background in elementary statistics to understand its significance, and did not want to admit it. – JMT]

C. Overview of the Final Rule

c. The Final Rule Avoids Broadly Sweeping in MLMs

The final Rule’s definition of business opportunity avoids broadly sweeping in all sellers of MLM opportunities.⁶¹ The decision in the RPBOR to exclude MLMs from the scope of the Rule’s coverage was based on the overwhelming majority of the approximately 17,000 comments that argued that the IPBOR failed to differentiate between unlawful pyramid schemes—which the Commission intended to cover—and legitimate companies using an MLM model.

As detailed more fully in the RNPR, several common themes emerged from the numerous comments submitted by

the MLM industry. Many commenters suggested that the low economic risks of participating in a typical MLM do not justify imposing burdensome regulations that would threaten to strangle the MLM industry. These commenters focused on the low fees—often less than \$100—that top MLM companies charge prospective distributors for the right to sell their products, and on the relatively low risk that consumers would lose money on large purchases of inventory. In addition, industry commenters contended that the various disclosure requirements were ill-suited for the MLM business model and that many of the disclosure obligations would show direct selling companies in a distorting negative light. For example, according to one commenter, the requirement to disclose prior legal actions would cast successful and long-established companies in a worse light than fly-by-night frauds simply because larger companies with more sales representatives and more years of operation are likely to get involved in a larger number of lawsuits. Moreover, industry commenters uniformly asserted that the cost of compliance with the IPBOR would be extremely high for them—first, from the burden of developing, providing and keeping records of proposed disclosures, and second, from the impaired ability to recruit prospective distributors. Finally, industry commenters argued that unlike traditional business opportunities, the MLM industry is not permeated with fraud.

[Does any informed person expect MLM spokespersons to tell the truth about MLM? Actually, fraud is inherent in MLM as a business model, dependent as it is on unlimited recruitment of endless chains of participants as primary customers. All MLMs assume infinite markets and virgin markets, neither of which exists in the real world. Thus, a “good MLM” may be an oxymoron. See Chapters 2 and 7-9 of my book Multi-level Marketing Unmasked – JMT]

In contrast to the overwhelming majority of comments that opposed regulating MLMs through the Business Opportunity Rule, only a small minority of commenters were in favor of a rule that would cover MLMs.

[What did the FTC staff expect? Did they honestly expect MLM promoters and participants to want to be regulated – especially if they knew that if the truth were known about these schemes, very few prospects they were seeking to recruit would join? – JMT]

These commenters included two consumer groups, CAI and PSA, a few consumer advocates, individuals who regretted becoming involved in MLMs, and other MLM participants. Many of the consumer advocates contended that the MLM industry is comprised primarily of pyramid schemes masquerading as legitimate companies. The commenters also asserted that MLMs deceptively market their distributorships as a low-risk opportunity with high earnings potential, when in fact, the costs of participating in an MLM can be high and the earnings comparatively small.

In the RNPR, the Commission concluded that although there is significant concern that some pyramid schemes may masquerade as legitimate MLMs, assessing the incidence of such practices is difficult and indeed, determining whether an MLM is a pyramid scheme requires a fact intensive, case-by-case analysis.

[Not so. If you read Chapter 2 of the aforementioned book and understand the fundamental flaws in all endless chain marketing schemes, all such programs are inherently unfair and deceptive. And it does not matter whether or not you label an MLM as a pyramid scheme, if it is manifestly unfair and deceptive (as research shows them to be), consumers deserve transparency in considering any given MLM program.]

Further, the record developed was insufficient as a basis for crafting MLM disclosures that would effectively help consumers make an informed decision about the risks of joining a particular MLM.

Based on the record and the Commission's law enforcement experience, the RNPR announced the Commission's determination that it would not be practicable to apply the requirements of the proposed Rule to MLM companies. Drawing on its law

enforcement experience, the Commission acknowledged that some MLMs do engage in unfair or deceptive acts or practices, including operating pyramid schemes or making unsubstantiated earnings claims that cause consumer harm. The Commission, however, was not persuaded that workable, meaningful disclosures could be devised that would help consumers identify a fraudulent pyramid scheme. This being the case, the Commission decided that the proposed Rule was too blunt an instrument to alleviate fraud in the sale of MLMs. The Commission therefore determined to continue to challenge unfair or deceptive practices in the MLM industry through law enforcement actions alleging violations of Section 5 of the FTC Act and not through the Business Opportunity Rule. The Staff Report's recommendations were consistent with this decision.

[In our research we have uncovered over 400 MLMs where there is plenty of evidence that they are violating Section 5. The FTC has prosecuted only about 14 in ten years. At that rate, they would have to increase their staff at least 35 times just to handle the current cases, not ot mention the continual spawning of new MLMs. – JMT]

In response to the Staff Report, the Commission received 24 comments addressing the Commission's decision to narrow the scope of the Rule to avoid broadly sweeping in MLMs. Specifically, 19 comments opposed the Commission's decision, one commenter agreed with the decision to narrow the scope of the Rule, but suggested modifying the Rule to contain bright line exemptions and to clarify the definition of "required payment," and two commenters advocated that the Commission adopt the Rule as recommended.

Commenters opposing the decision to avoid sweeping MLMs within the scope of the Rule's coverage set forth the same basic premise – that MLMs frequently misrepresent the level of earnings achieved by their distributors and therefore, should be subject to regulation. More specifically, many of the commenters advocated that the MLM industry should be required to disclose the average income of their

participants. The Commission has carefully considered the comments submitted in response to the Staff Report on the issue of MLMs. While some of the commenters provided an analysis of the MLM industry with concrete examples of the types of problems that exist within that industry, many did not. Instead, many commenters expressed in general terms their low opinion of MLMs and their general opinion that MLMs should be regulated. More to the point, none of the commenters provided persuasive arguments for why the Business Opportunity Rule is the proper vehicle to address the problems they identified within the MLM industry.

Before discussing the comments in further detail, however, one point in the rulemaking record requires clarification. Several comments focused on the following language contained in the Staff Report:

“Two key problems emerged with the IPBOR’s breadth of coverage. First, the IPBOR would have unintentionally swept in numerous commercial arrangements where there is little or no evidence that fraud is occurring.” The commenters suggest, incorrectly, that the quoted language reveals a finding by the Commission that there is little or no evidence of fraud occurring within the MLM industry. This language, however, referred to a passage from the RNPR that addressed traditional product distribution arrangements, not MLMs. *The Commission has not made a finding that there is little or no evidence of fraud within the MLM industry; to the contrary, it has specifically recognized, through its own law enforcement experience, that some MLMs may be pyramid schemes in masquerade and may make false and unsubstantiated earnings claims.*

In any event, the comments submitted in response to the Staff Report do not persuade the Commission that the Business Opportunity Rule is the proper tool to address these problems. Two of the affirmative disclosure requirements illustrate the difficulty in applying the Rule to MLMs: (1) The disclosure of substantiation for earnings claims; and (2) the disclosure of references.

First, as the Commission has acknowledged, the varied and complex

structure of MLMs makes it exceedingly difficult to make an accurate earnings disclosure and likely would require different disclosures for different levels of participation in the company. For instance, it would be difficult to craft an accurate earnings disclosure that would account for “inactive” participants that use their distributorship as a “buyers club” and are interested only in purchasing goods at a wholesale price for their own use. This problem appears to be unique to MLMs and, so far as the Commission is aware, does not arise in other forms of business opportunities.

Furthermore, it may be difficult to determine retail income if the MLM is not in a position to verify the extent to which a distributor has resold the product at retail, is warehousing the product, or bought the product for his or her own personal consumption. Even where the MLM has policies in place purportedly to ensure that a portion of its distributors’ income is derived from retail sales, these policies could go unenforced, or even where ostensibly enforced, could be circumvented by distributors who may have an incentive to “inflate” their retail sales by “certifying” that such sales occurred in order to qualify for higher levels of commissions. In light of these difficulties, and because the comments submitted in response to the Staff Report did not refute these findings, the Commission continues to believe that developing a standard, useful, and understandable earnings disclosure that would apply to both the MLM industry and the other business opportunities covered by the Rule remains elusive.

Second, the reference disclosure required under the final Rule would make little sense in the MLM context. As the Commission has previously recognized, those prior purchasers appearing on the reference list likely would stand to receive a financial benefit if they could convince a prospect to enroll into their downline. Under these circumstances, information provided by such a reference might not be a reliable indicator of the potential risk and rewards of enrollment in the MLM.

In response to the Staff Report, the Commission received one comment

attempting to refute this reasoning. The commenter argued that, contrary to the Commission's view, prior purchasers would have little incentive to misrepresent the success of the MLM because that incentive would exist only if the prospective purchaser would become part of the prior purchaser's downline, which the commenter implies would not always be the case. The commenter further argued that the fact that the prospective purchaser had received the disclosure document would indicate that the prospective purchaser had already been recruited, and therefore would be unlikely to face further recruitment by the prior purchaser.

The Commission finds these arguments unpersuasive. To the extent there is any financial incentive for a reference to puff or exaggerate the benefits of buying into a business, that reference obviously cannot provide a disinterested opinion to the prospect. The MLM model is inherently structured to create financial incentives for distributors to recruit prospects into their downlines. Thus, those financial incentives are present whenever a potential recruit enquires into the business. To illustrate the point, even dissatisfied distributors have an incentive to refrain from disparaging the MLM because any losses they have suffered could potentially be recouped by the recruitment of the prospect into their downline. Whether they are ultimately successful in their attempt to woo a recruit from another distributor is immaterial; they have every incentive to try.

Thus, the Commission continues to believe that the final Rule's reference disclosure would not provide prospective MLM participants with an accurate account of the MLM experience or with information necessary to make an informed purchasing decision. Moreover, these challenges appear to be unique to MLMs, and as far as the Commission is aware, are not inherent in the other types of business opportunities addressed by the final Rule.

Accordingly, while the Commission recognizes that problems may exist within the MLM industry, it continues to find that the Business Opportunity

Rule is not the appropriate vehicle through which to address them. Rather, the Commission will continue to challenge unfair or deceptive practices in the MLM industry through Section 5 of the FTC Act. Thus, the final Rule has been crafted to avoid broadly sweeping in MLMs.

NOTE: The rest of the 49-page notice in the Federal Register is essentially irrelevant. With MLM exempted, at least 90% of packaged business opportunity sellers fall outside the ambit of the Rule, and those remaining will have a strong incentive to meet the FTC's easily satisfied definition of a multi-level marketing program.

Thus, with the MLM exemption, the Rule has become a non-rule – a terrible waste of public resources and of the opportunity for the FTC to accomplish something significant for consumers. In following through with this action, the FTC is failing in its duty to protect consumers from the most prevalent and the most unfair and deceptive of all classes of business opportunities. With its endless chains of recruitment, MLM as a business model is also extremely viral and predatory. In adhering to the wishes of the DSA/MLM lobby, the FTC has placed itself in the position of aiding and abetting worldwide MLM fraud.

For a brief account of what happened from the DSA/MLM perspective, see the report below by MLM attorney Jeffrey Babener, which praises the success of DSA/MLM lobbying efforts, but also warns of areas of vulnerability that remain for the MLM industry.

Plus – at the end of the article, see quote from another article.

[Though the article is copyrighted, under the doctrine of "fair use" for the sharing of important information very much in the public interest, I am quoting extensive portions to help the reader understand what the DSA/MLM lobby is boasting about – and admitting to – in this article. I have highlighted important passages and have added some notes in brackets – JMT]

THE FTC FINAL BUSINESS OPPORTUNITY RULE: TILL WORK TO DO FOR MLM/DIRECT SELLING/NETWORK MARKETING

By Jeffrey A. Babener © 2012

“The Mills of the Gods grind slowly, yet exceedingly fine.”
Greek philosopher, Sextus Empiricus

On March 1, 2012, a three decade rulemaking process of the FTC (Federal Trade Commission) will result in the implementation of the final FTC Business Opportunity Rule. Although the FTC’s summary of the Rule explicitly states that it is not the intent of the Rule to apply to companies that offer opportunities in the channel of distribution alternatively referred to as MLM/Multilevel Marketing/Direct Selling/Network Marketing, the actual Rule seemingly covers many areas of support provided by MLM companies, leaving the FTC rhetoric at odds with the actual Rule that has been adopted. *The quasi-assurance of MLM industry exemption, granted in the summary text of the Final Business Opportunity Rule, is unfortunately taken back in the "footnotes" to the Rule and the Rule itself.*

The application of onerous disclosure and regulatory coverage leaves the industry in an uncertain position, seemingly at risk of enforcement at the discretion of future FTC

staff, notwithstanding the FTC’s specific statement that it believes that proper enforcement against deceptive pyramid schemes should be pursued under its Section 5 rule that prohibits "unfair and deceptive practices." For the present, the goodwill and current enforcement plans of the FTC toward the MLM industry is readily apparent. The actual Rule, in the absence of the industry seeking adjustments in the Rule or Congressional exemption, creates an ambiguous future for the MLM/Direct Selling/Network Marketing industry.

In 1978, the FTC (Federal Trade Commission) issued a combined rule regulating disclosures for sellers of franchises and business opportunities. It was principally aimed at the franchise industry to require extensive disclosures to purchasers of franchises. In 1999, the FTC decided to embark on a process to create a stand-alone Business Opportunity Rule. In 2006, the first draft was published for public comment. In 2008, the FTC published an interim Rule followed by a 2011 release of the Final Rule, which would be effective in March, 2012.

The MLM/Direct Selling/Network Marketing Industry is Heard Loud and Clear ... Almost

In April 2006, the FTC released a sweeping proposed change in its FTC Business Opportunity Rule. During the following two-year period, the FTC received more than 17,000 comments on its proposed rule, the majority of which were from companies, representatives and distributors in the MLM industry. The vast majority of comments raised serious concerns regarding the onerous and burdensome nature of the proposed rule, as well as extending the scope of the Rule to the MLM /Direct Selling industry. In addition, scores of members of Congress weighed in with concerns about the impact on a well-established industry that involved millions of home-based businesses.

On March 18, 2008, the FTC responded favorably to constructive criticism, and announced that it was seeking to modify the Proposed Business Opportunity Rule to exempt MLM companies. The FTC issued a Revised Proposed Business Opportunity Rule for comment. At the very least, the FTC was unequivocal in its stated intent to exempt the MLM industry, noting in its public statement:

On balance, based on this record and its law enforcement experience, the Commission does not believe it is practicable or sufficiently beneficial to consumers to attempt to apply the proposals advanced in this rulemaking against multi-level marketing companies, particularly when considering the burdens upon industry. The Commission, therefore, has determined that at this point, it will continue to use Section 5 to challenge unfair and deceptive acts or practices in the MLM Industry.

In fact, *no less than ten references are set forth by the FTC with respect to its intent to exclude application of the RPBOR to MLM/Direct Selling companies.* Those comments are couched in such terms as:

*The [Rule] has been pared back to exclude MLMs;
The Commission takes MLM companies out of the ambit of the Rule;*

*... these provisions would no longer apply to MLM companies;
... they [MLM Companies] are excluded from the scope of the [Rule].*

Unfortunately, the actual Revised Proposed Rule was silent on the exemption for MLM/Direct Selling.

The revised draft, announced with the intent of exempting MLM companies, was unfortunately still flawed in that its wording may still inadvertently create applicability to many leading MLM companies because proposed "definitions" section 437.1(c)(3)(ii) may mistakenly include MLM/Direct Selling companies that assist in customer gathering on the web, in print, institutional or co-op advertising campaigns or other customer lead generation programs. However, industry commentators noted that the proposed rule represents a good faith start to narrow the scope of the Proposed FTC Business Opportunity Rule and invite comments from the public to assist in this process.

The response of the industry was one of appreciation and concern, all at once. It was noted that the expressed intentions of the FTC were much appreciated by the MLM/Direct Selling Industry. Unfortunately, the industry could take very limited comfort in the FTC comments, in that, at no place in the Revised Proposed Business Opportunity Rule is the MLM/Direct Selling exemption "called out," nor was it even addressed. If adopted, as is, future statutory interpretation within the "four corners" of the actual Rule, will find no guidance as to the FTC intention to exempt MLM/Direct Sellers from the Rule. . . .

And there the matter stood from 2008 to 2011, awaiting publication of the FTC Final Business Opportunity Rule.

Close, But No Cigar – The FTC Heard the MLM/Direct Selling/Network Marketing Industry ... Almost

And so, the industry waited patiently, with the hope that the FTC's Final Business Opportunity Rule would match exemption intent with actual exemption language.

In 2011, the FTC released the Final Business Opportunity Rule, to be effective March 1, 2012.

In its 200 page release, the FTC rhetoric, time and time again, clearly indicated its intent to exempt the MLM industry from broad sweeping coverage of the new Rule. Its position was succinctly expressed at page 33 of the Release:

Accordingly, while the Commission recognizes that problems may exist within the MLM industry, it continues to find that the Business Opportunity Rule is not the appropriate vehicle through which to address them. Rather, the Commission will continue to challenge unfair or deceptive practices in the MLM industry through Section 5 of the FTC Act. Thus, the final Rule has been crafted to avoid broadly sweeping in MLMs.

As applied to MLM/Direct Selling/Network Marketing Companies, the FTC Final Business Opportunity Rule, under section 437.1 (c) offered a definition of a "business opportunity" that required three prongs to trigger applicability:

1. Solicitation to enter a new business;
2. A required payment of any amount (whether "at cost" or not);
3. Providing assistance in acquiring customers or accounts.

The problem: Almost all federal and state franchise, business opportunity and MLM legislation exempt, from coverage, offerings with entry fees below threshold amounts (typically \$500) as well as "not for profit" or "at cost materials." The Final Rule contains no such exemptions.

Thus, absent an exemption for entry fees below a threshold amount, or for "at cost" materials, under the Final Rule, MLM/Direct Selling/Network Marketing Companies clearly trigger the first and second prongs. Thus, unless the FTC reconsiders number two, the third prong was the only possible "out" for MLM/Direct Selling/Network Marketing companies. The industry sought relief and exemption here for both prongs two and three, but it was unsuccessful ... and notwithstanding the FTC's good faith intent to not pull MLM companies into enforcement of the new Rule, in reality, they are "pulled in."

Unfortunately, the goodwill exemption so clearly offered in the FTC's generalized discussion, was effectively retracted in footnotes and rejection of the MLM/Direct Selling/Network Marketing industry's constructive comments and request for a specific called out exemption that matched the FTC's stated goals.

In one clear, but somewhat buried, footnote, (footnote 91, page 33) the FTC effectively took back what it had granted in its text:

91 The final Rule, however, does not explicitly exempt MLMs from coverage, but instead contains a narrow definition of "business opportunity."

In all fairness to the FTC, it clearly improved its earlier draft, at the request of the industry to narrow the scope of "business assistance" that forms an important third prong required to trigger application of the Rule to MLM. It specifically removed as examples of business assistance both generalized business training and tracking and paying commission ... also noted in footnote 91, page 33:

As discussed in Section III.A.3 infra, the final Rule's definition of "business opportunity" eliminates two types of business assistance that previously would have triggered the Rule's coverage of MLMs:

- (1) tracking or paying commissions or other compensation for recruitment or sales; and
- (2) providing generalized training or advice for the business. The final Rule is thus more narrowly tailored to those types of deceptive business assistance representations that are the hallmark of fraudulent business opportunity schemes: location, account, and "buy back" assistance.

73 FR at 16123.

And true to its word, the FTC's Final Business Opportunity Rule provided for a specific exemption from the triggering third prong of a "business opportunity" in which a company provides outlets, accounts or customers to those involved in the opportunity ... going a long way, but not far enough to encompass the services provided to MLM distributors:

*Section 437.1(m)
Providing locations, outlets, accounts, or customers means furnishing the prospective purchaser with existing or potential locations, outlets, accounts, or customers; requiring, recommending, or suggesting one or more locators or lead generating companies; providing a list of locator or lead generating companies; collecting a fee on behalf of one or more locators or lead generating companies; offering to furnish a list of locations; or otherwise assisting the prospective purchaser in obtaining his or her own locations, outlets, accounts, or customers, provided, however, that advertising and general advice about business development and training shall not be considered as "providing locations, outlets, accounts, or customers."*

However, the FTC specifically rejected requests by the industry to extend the exemption to otherwise typical assistance provided by almost all leading MLM/Direct Selling/Network Marketing Companies, including replicated websites, referral of customers, lead generation, etc. In failing to call out in the Rule its intent to not cover MLM opportunities or to further exempt typical MLM Company assistance, prong three is triggered, and the industry is left vulnerable. . . .

[So there may be some hope for prospect protection? JMT]

In the end, the FTC did not grant the exemption relief that the MLM/Direct Selling/Network Marketing industry was seeking.

In the future, enforcement will clearly be in the discretion of FTC staff and not in the control of the industry. If any comfort was to be offered by the FTC, it was to be found in the FTC discussion of the standard it may choose to enforce or not enforce its new Rule against MLM/Direct Selling/Network Marketing companies that offer typical non-exempted business assistance to distributors, i.e., the significance of assistance in inducing a potential distributor to enter the business:

*The Staff Report noted a concern with narrowing the definition in the ways the commenters suggested, because it would allow promoters of fraudulent schemes to craft their sales pitches carefully to evade the Rule. The staff disagreed with commenters who recommended excising the word "customers" from the definition or diluting it in some fashion. **Instead, the Staff Report recommended that the Commission continue its longstanding policy of analyzing the significance of assistance in the context of the specific business opportunity, focusing on whether the seller's offer is "reasonably likely to have the effect of inducing reliance on [the seller] to provide a prepackaged business."** (at page 85.)*

Time to Go to Work: The MLM/Direct Selling/Network Marketing Industry: Operation: Get it Right ... Put it to Bed

The industry clearly has the goodwill of the FTC at a time when the Final Business Opportunity Rule is launching, March, 2012. But it enters a new era with a shadow of uncertainty over its head and an enforcement that is subject to the

discretionary decision making of future FTC staff. If it is looking for some ultimate peace and security, the industry, through leading companies, leading commentators and legal experts and associations, such as the DSA or MLMIA, should continue the good and respectful fight for changes to the FTC Final Rule or Congressional legislation to memorialize the exemption. It will not be the first time; in 1982, Congress amended the Internal Revenue Code to recognize independent contractor status of direct sellers ... sending a clear message on enforcement and interpretation to the IRS.

Five recommendations are respectfully suggested to achieve the intent of the FTC that will further FTC objectives, create consistency with a long-standing state tradition of regulation of business opportunities, and finally, address the goals and needs of the MLM/Direct Selling industry:

- (1) Specifically call out the exemption for MLM/Direct Selling/Network Marketing in the Final Business Opportunity Rule. (*A total exemption consistent with FTC implied intent*);
- (2) Adopt a threshold exemption for required payments in the first six months, preferably \$500, but perhaps as low as \$200. (*Eliminates the "required payment" prong of the Rule's definition of a "business opportunity"*);
- (3) Adopt an exemption from the definition of "required payment" for the purchase of "at cost" or "not for profit" sales kits and marketing support materials and marketing systems support such as replicating websites or "back office" distributor systems for analyzing commissions, productivity and communication. (*Eliminates the "required payment" prong of the Rule's definition of a "business opportunity"*);
- (4) In the alternative, adopt a specific exemption for MLM/Direct Selling companies as follows:
MLM/Direct Selling companies are exempted from this Rule so long as any required payment during the first six months of distributor participation is below \$_____, and so long as the required purchase is for "at cost" or systems support such as replicating websites or lead referral or "back office" distributor systems for analyzing commissions, productivity and communication. (*Eliminates the "required payment" prong of the Rule's definition of a "business opportunity"*);

(5) Expand the MLM exemption from the business assistance prong of "providing locations, outlets, accounts or customers" as follows:

Providing locations, outlets, accounts, or customers means furnishing the prospective purchaser with existing or potential locations, outlets, accounts, or customers; requiring, recommending, or suggesting one or more locators or lead generating companies; providing a list of locator or lead generating companies; collecting a fee on behalf of one or more locators or lead generating companies; offering to furnish a list of locations; or otherwise assisting the prospective purchaser in obtaining his or her own locations, outlets, accounts, or customers, provided, however, that for MLM/Direct Selling/Network marketing companies, advertising and general advice about business development and training, replicated websites, back office support, customer or distributor referral programs and lead generation programs, shall not be considered as "providing locations, outlets, accounts, or customers."

In a later article⁴¹, Babener boasts of the success of the DSA's lobbying efforts with this introduction:

The Direct Selling Industry Scores a Win
[Highlighting emphasis by JMT]

In March 2012, the direct selling industry has occasion to celebrate what a united industry, companies and distributors, can achieve if everyone pulls oars together in the same direction. ***The fruits of their labor are apparent in a newly-forged positive relationship with the primary federal agency that regulates a channel distribution, alternately referred to as direct selling, network marketing and multilevel marketing. In its final FTC Business Opportunity Rule, the FTC stated its clear intention to relieve***

companies and distributors from what might have been very onerous conditions of recruitment that would have dramatically impaired the ability of distributors to build their businesses.

In Conclusion ...

In conclusion, the MLM/Direct Selling/Network Marketing industry is certainly entitled to celebrate a continuing positive dialogue and cooperation with the Nation's top consumer protection agency, the FTC. In its commentary on the Final Business Opportunity Rule, the FTC could not have been more clear that it did not intend to apply its new Rule to the MLM channel of distribution. Instead, the commentary opined that the current regimen of prohibition on "deceptive" practices should be the appropriate vehicle for enforcement.

Unfortunately, the new Final Rule language does not match the "staff" commentary. And unfortunately, staffs come and go ... and administrations come and go. And commentaries are just that ... commentaries. In the end, it is the actual Rule that reigns. And the actual language of the Final Business Opportunity rule opens the door to significant enforcement of the Rule to the MLM/Direct Selling/Network Marketing industry should a future staff so choose. In that regard, the Industry, in the absence of clarification of the Rule, should not sleep quite as peacefully as it would like. And it may take limited comfort in the FTC staff commentary and good rapport that exists between the Industry and the FTC at the time of adoption of the Final Business Opportunity Rule.

In other words, there is work to be done.

⁴¹ "THE NEW FTC BUSINESS OPPORTUNITY RULE: MLM/Direct Selling Exemption Recognized"
By Jeffrey A. Babener (from JD Supra Law News, © 2012

Some communications between DSA and FTC officials not disclosed in response to FOIA (Freedom of Information Act) requests

Commencing in February of 2012, a group of us consumer advocates who had donated a considerable amount of time and personal funds to educate and warn the public about MLM abuse decided to seek answers to questions about the FTC's decision to enact BOR with the MLM exemption. Dr. Jon Taylor acted as agent for the group.

The response to our first request was to challenge us to explain why we should not be charged for the costs of retrieving and copying the documents requested. With a letter drafted by Douglas Brooks, we responded with our motives in acting on behalf of consumers nationwide and the ability to disseminate the information nationwide with our web sites. Willard K. Tom, the FTC's general counsel finally wrote that they accepted our explanation and would grant our fee waiver request.

We had several additional communications with FTC-FOIA personnel, including an appeal after the first denial, but *our request for identifying information for the 17,000 commenters was eventually denied*. The reasons given seemed weak, but as it turned out, it would have made little difference. Only the name and state was required for each comment. Those submissions that were sent by the company or upline without authorization of the submitter – and we know from discussions with some of them that this happened in some cases – would not likely have provided more identifying information.

To answer our questions, I then hired some assistants to do a Yahoo people search to identify a few hundred commenters that we could survey by telephone. The results were reported in the section above on the 17,000 submissions to IPBOR.

We then requested information from the FTC's FOIA office on the persons responsible for writing reports favorable to the MLM industry (next page), but the copies of emails that were sent between officials had the content and many of the names blocked out. Their justifications for such a weak response seemed weak and defensive.

Our request should have yielded some communications between DSA officials and FTC officials, but none were forthcoming. However, in a DSA article, it is clear that the government relations committee of the DSA met with FTC officials. No record from or communication

regarding such meeting were disclosed in response to our FOIA request. Below are excerpts from the article:

(Under the heading "Strategic Alliances")

Mills describes the work accomplished by the DSA staff and government relations committee. "The government relations committee visited with the FTC to discuss its intent, what led to such a proposal and why it felt such a proposal was necessary," she says. . .

[Note also the following expert retained by the DSA, which would have to include Former FTC Chairman-turned lobbyist Timothy Muris.– JMT]

"Mariano says the DSA and certain industry companies retained experts on "substantive areas of the rulemaking process and procedure"– including former FTC commissioners. "These rulemaking experts also helped us develop arguments that would be the most helpful to the FTC in accomplishing their goals of dealing with business opportunity fraud while protecting our interests as legitimate direct sellers," he says.

NOTE: Three of the letters we wrote to the FTC's FOIA office are reproduced on the next seven pages. While several documents were supplied, most of them we already had or were irrelevant to our request. And those communications that would have been useful had either names or content – or both – blocked out.



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Research, education, and advocacy for consumers

June 7, 2011

ATTN: Richard Gold, Freedom of Information Act Request,
 Office of General Counsel
 Federal Trade Commission
 600 Pennsylvania Avenue, N.W.
 Washington, D.C. 20580

RE: Request for records of communications between FTC personnel and representatives of the DSA (Direct Selling Association) and MLM (multi-level marketing) industry

Dear Sir/Madam:

This is a request under the Freedom of Information Act for documents concerning communications between the Federal Trade Commission and representatives of the Multi-Level Marketing (MLM) and/or Direct Selling Industry concerning the proposed Business Opportunity Rule. Specifically, I request that copies of the following documents be provided to me:

All communications, including emails, electronic communications and printed correspondence, and all documents in written or electronic form which refer or relate to oral communications, from April 7, 1995 to the present, between or among the Federal Trade Commission, including but not limited to the following individuals:

- Kathleen Benway, Division of Marketing Practices,
- Lois C. Greisman, Division of Marketing Practices,
- Allyson Himelfarb, Division of Marketing Practices,
- David Vladek, Director, Bureau of Consumer Protection,
- John Liebowitz, Chairman,
- William E. Kovacic, Commissioner,
- J. Thomas Rosch, Commissioner,
- Edith Ramirez, Commissioner,
- Julie Brill, Commissioner, and
- Donald S. Clark, Secretary to the Commission;

And/or any and all of the following individuals or organizations:

- a. **Direct Selling Association (DSA)**, 1667 K Street, NW, Suite 1100, Washington, D.C. 20006,
- b. **Neil H. Offen**, DSA President,
- c. **Joseph N. Mariano**, DSA Secretary and Legal Counsel,
- d. **Amy Robinson**, DSA Senior Vice President and Marketing Officer,
- e. **John W. Webb**, DSA Associate Legal Counsel & Senior Director, Government Relations, and other members of the DSA Board of Directors and staff,

Request for records between FTC personnel and DSA/MLM representatives, page 2

- f. **Timothy J. Muris, J. Howard Beales, III, and O'Melveny & Meyers, LLP**, 1625 Eye Street, NW, Washington, D.C., 20006,
- g. **Joan (Jodie) Z. Bernstein and Bryan Cave, LLP**, 700 Thirteenth Street, NW, Washington, D.C. 20005-3960, and
- h. **Maureen M. (Morrissey) Fries**, Assistant General Counsel, Tupperware Brands Corporation, 14901 S. Orange Blossom Trl, Orlando, FL 32837;

which relate or refer to the proposed regulation of the multi-level marketing and/or direct selling industries or the proposed Business Opportunity Rule, including but not limited to the Franchise Rule Review, 60 FR 17656 (April 7, 1995), the Advance Notice of Proposed Rulemaking, 62 FR 9115 (Feb. 28, 1997), the Notice of Proposed Rulemaking, 71 FR 19056 (April 12, 2006) and the Revised Notice of Proposed Rulemaking, 73 FR 16,110 (Mar. 28, 2008).

Excluded from this request are any and all documents which were posted on the Federal Trade Commission's publicly available website, <http://www.ftc.gov/os/publiccomments.shtm>.

In making this request I am acting on behalf of myself and as agent for the following persons:

- Jon M. Taylor, MBA, Ph.D., President, Consumer Awareness Institute, author – *The Network Marketing Game* and *The Case (for and) against Multi-level Marketing(MLM)*, and operator of the web site www.MLM-thetruth.com,
- Robert Fitzpatrick, Robert L. Fitzpatrick, President, Pyramid Scheme Alert, author – *False Profits* and operator of the web site www.pyramidschemealert.org,
- Bruce Craig, former Assistant Attorney General, State of Wisconsin – litigated landmark cases against Koscot Interplanetary, Amway, and other MLM companies
- Stephen Barrett, M.D., publisher of Consumer Health Digest, operator of anti-quackery websites and the web site www.mlmwatch.org,
- Douglas M. Brooks, Martland & Brooks, LLP, attorney, franchise, distribution and consumer protection litigation, including cases involving MLM firms
- Eric Scheibeler, former federal auditor, author – *Merchants of Deception*

As consumer advocates, we have donated many years of time and expertise, as well as personal funds, to educate and warn consumers against unfair, deceptive, and injurious practices in the marketplace by the MLM and Direct Selling Industry. The materials we are requesting will further our goals of consumer education and protection, and we intend to publish them, or representative portions of them, on some or all of the above-referenced web sites.

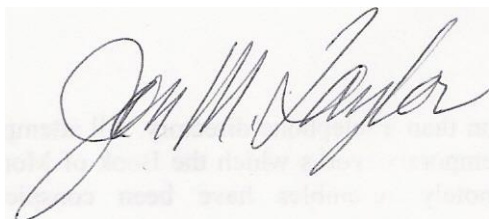
Release of these materials is in the public interest as it will contribute significantly to the public's understanding of the Federal Trade Commission's rule-making process, including the influence of industry and trade groups on the rule-making process in general, and upon the proposed Business Opportunity Rule in particular. We have no commercial purpose in making this request. We are therefore requesting a waiver of fees incurred in responding to this request.

We expect a timely response to this request which complies with FOIA guidelines as posted on the FTC web site. It appears from a careful review that none of the nine FOIA exemptions listed on the FOIA page of the FTC web site applies to this request.

Request for records between FTC personnel and DSA/MLM representatives, page 3

I, Jon M. Taylor, am acting as agent for the above-listed group and am coordinating this request and the processing of information you provide in your response. If you need to discuss this with me, I can be reached at (801) 298-2425, or at (801) 671-1870. Please respond to the address below. Thank you in advance for your prompt consideration of our request.

Sincerely,

A handwritten signature in black ink that reads "Jon M. Taylor". The signature is written in a cursive style with a large, looping initial "J".

Jon M. Taylor, MBA, Ph.D., President, Consumer Awareness institute
291 E. 1850 South, Bountiful, UT 84010



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Research, education, and advocacy for consumers

September 15, 2011

Freedom of Information Act Appeal, Office of General Counsel
 Federal Trade Commission
 600 Pennsylvania Avenue, N.W.
 Washington, D.C. 20580

RE: Appeal from Response to FOIA Request

Dear Sir/Madam:

This is an appeal from the response dated August 22, 2011 to our June 7, 2011 request under the Freedom of Information Act, copies of which are enclosed herewith.

I. Identification of Withheld Documents

The Commission's response states that there are 18 pages of responsive documents which are being withheld pursuant to FOIA Exemption 5 because they are "deliberative and pre-decisional and are an integral part of the agency's decision making process." The Commission fails, however, to identify or describe these documents in such a way that we (or a reviewing Court) can assess the validity of the claimed exemption. We call upon the Commission to provide an index and itemization of the withheld documents sufficient to demonstrate the applicability of Exemption 5, and to assess whether any portions of the withheld documents are not subject to Exemption 5. *See Mead Data Central, Inc. v. U.S. Dept. of the Air Force*, 566 F.2d 242, 248-252 (D.C.Cir. 1977); *Vaughn v. Rosen*, 484 F.2d 820, 826-28 (D.C.Cir. 1973), *cert. den.* 415 U.S. 977 (1974).

We also note that it is highly doubtful that Exemption 5 could possibly apply to any documents which are responsive to our request. We requested communications between the Commission and various parties (e.g., the Direct Selling Association and a number of so-called direct selling firms) concerning the proposed Business Opportunity Rule. The parties identified in our request were all interested in the regulation; they were certainly not the sort of independent, disinterested third parties with whom the Commission might conceivably assert the deliberative process privilege. *See generally Department of the Interior v. Klamath Water Users Protective Association*, 532 U.S. 1 (2001). Finally, the Commission's response states that there were a total of 50 pages of responsive documents, of which 18 were withheld as noted above. Presumably this left 32 pages of documents which the Commission intended to produce. We only received 29 pages. We call upon the Commission to review its response and confirm that it has produced all of the responsive documents.

Appeal from Response to FOIA Request, page 2

II. Documents Related to the 2008 Direct Selling Association Seminar

The Commission produced documents indicating that two staff members attended and made presentations at a seminar held by the Direct Selling Association (a lobbying organization for the multi-level marketing industry), entitled “Legal Issues of the Day,” which was held in September of 2008 and concerned the Commission’s proposed Business Opportunity Rule. The documents indicate that the seminar was audio-taped, and that the Commissions’ staff members provided handouts to attendees. Under the authorities referenced above, these audio tapes and handout materials are clearly not subject to any exemption from FOIA, are responsive to our request, and should be produced.

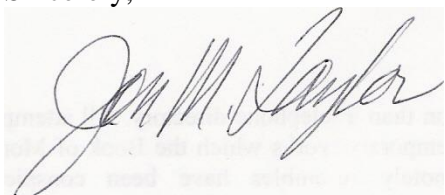
III. Request for Discretionary Production of Exempt Documents

In the event that you determine that the documents withheld by the Commission are in fact subject to Exemption 5, we respectfully request that the Commission produce those documents as a matter of discretion.

The purpose of our FOIA request is to learn – and then explain to the public – how the multi-level marketing industry (MLM industry – sometimes referred to as the “direct selling industry”) was exempted from the Commission’s pending Business Opportunity Rule (the “Rule”). The original version of the Rule – as set forth in the April 12, 2006 Notice of Proposed Rulemaking, 71 Fed.Reg. at 19054 (“NPR”) – was expressly drafted to encompass multi-level marketing. The NPR provided ample justification for regulation of the MLM industry based on thousands of consumer complaints and many millions of dollars in documented consumer losses. (NPR, 71 Fed.Reg. at 19061). Indeed, several of the consumer advocates who submitted comments in the rulemaking proceeding – including those making this FOIA request – demonstrated the existence of substantial consumer losses caused by the MLM industry, two of whom gave evidence of *tens of billions of dollars* in aggregate losses suffered by MLM participants. These calculated loss rates have been validated by a CPA, an actuary, a statistician, and a certified financial planner.

Two years later, despite the urgent need for consumer protection against deceptive MLM schemes, the Commission issued a Revised Notice of Proposed Rulemaking which would exempt the MLM industry from the Rule. *See* March 26, 2008 Revised Notice of Proposed Rulemaking (“RNPR”), 73 Fed.Reg. at 16110. It is our belief that the Commission’s dramatic change in position was caused by a sophisticated, multi-pronged lobbying effort by the MLM industry, costing over \$4 million (April 2008 Direct Selling News). The purpose of this FOIA request is to enable us to fully understand all of the factors that led to the Commission’s change in position and to present and explain those factors to the general public. Accordingly, it would be in the public interest to release all of the requested documents.

Sincerely,

A handwritten signature in black ink, appearing to read "Jon M. Taylor", is written over a light-colored rectangular background.

Jon M. Taylor, MBA, Ph.D., President, Consumer Awareness institute
291 E. 1850 South, Bountiful, UT 84010

CONSUMER
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March 22, 2012

Sarah M. Mathias, Associate General Counsel, FOIA
 Federal Trade Commission
 600 Pennsylvania Avenue, N.W.
 Washington, D.C. 20580

RE: Request for authorship of staff reports related to Business Opportunity Rule

Dear Ms. Mathias:

This is a request under the Freedom of Information Act for documents concerning the identity of the staff officials who drafted the Business Opportunity Rule.

We have reviewed the last set of documents you sent us in response to our FOIA request dated October 26, 2011. Included was a memo from Lois Greisman to Regina Williams, dated July 20, 2006, including an original message from Steven Toporoff to three staff members: Allen Hile, Lois Greisman, and Karen Hobbs, also dated July 20, 2006. (4th page of the pdf file you sent). In the letter, Mr. Toporoff states:

“I was able to find Muris’ comment among the 13,000 comments posted on commentworks. Attached is a copy. I also printed it out, in the event you want a hard copy.”

This raises serious questions for those of us trying to identify the real reasons the FTC granted an exemption to multi-level marketing companies (MLMs) from having to comply with the final BOR. A careful study of the revised proposed BOR on 2008 and the final BOR issued last December exposes the inordinate influence of Timothy Muris upon the staff report justifying the MLM exemption – in what he wrote in his comments. Rather than take the time to read our comments, referencing reports of our independent research (not funded by the MLM industry), the staff reflected and in some sections parroted some of Muris’ arguments almost word for word. This included Muris’ denigration of my research – covering 15 years research on over 300 MLMs (now over 400). and feedback from thousands of MLM victims and their families worldwide.

Timothy Muris was a lead attorney with Amway when he was appointed by President Bush as Chairman of the FTC. After his appointment, virtually all new prosecutions of product-based pyramid schemes ground to a halt – a huge setback for consumers which has continued to this day.

The memo I refer to above suggests his influence continued after his departure from the FTC, as he lobbied for Primerica (and apparently for the Direct Selling Association, the lobby for the MLM industry) in his comments on their behalf – as referenced in this memo. So here we have what appears to be a former FTC Chairman coming from fraud protection to consumer protection and back to fraud protection. And unfortunately for consumers (which the FTC is pledged to protect against unfair and deceptive practices), the staff handling BOR were comfortable just parroting his arguments in favor of MLMs and against the interests of consumers – which I and a few other consumer experts were laboring pro bono to defend. Our time and extensive research was donated

on behalf of consumers, while Muris was likely paid very well to lobby on behalf of what our independent research proves to be a flawed, unfair, deceptive, and predatory business model – MLM.

We know that Lois Greisman was Muris' Chief of Staff prior to working as Associate Director of the Div. of Marketing Practices. For some reason, she remained under his influence, having given credence to his arguments as a lobbyist over the arguments of consumer advocates – which were based on solid research evidence. Clearly, the MLM industry benefitted at the expense of consumers.

What we need to know now is the following:

- 1. Were the three individuals to whom the aforementioned memo from Steven Toporoff was addressed involved in the drafting of the staff report for the final Rule proposed in 2008? If not, what was their role, as related to the final BOR?**
- 2. What are the names of all the staff members who had a primary role in drafting the staff report for the final BOR in 2008 and for drafting the final BOR in 2011?**

In making this request I am acting on behalf of myself and as agent for the following persons:

- Jon M. Taylor, MBA, Ph.D., President, Consumer Awareness Institute, author – *The Network Marketing Game* and *The Case for and against Multi-level Marketing(MLM)*, and operator of the web site www.MLM-thetruth.com,
- Robert Fitzpatrick, Robert L. Fitzpatrick, President, Pyramid Scheme Alert, author – *False Profits* and operator of the web site www.pyramidschemealert.org,
- Stephen Barrett, M.D., publisher of Consumer Health Digest, sponsor of anti-quackery websites and the web site www.mlmwatch.org,
- Douglas M. Brooks, Martland & Brooks, LLP, attorney, franchise, distribution and consumer protection litigation, including cases involving MLM firms
- Eric Scheibeler, former federal auditor, author – *Merchants of Deception*

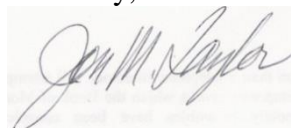
As consumer advocates, we have donated many years of time and expertise to educate and warn consumers against unfair, deceptive, and injurious practices in the marketplace by the MLM and Direct Selling Industry. Disclosure of this information is in the public interest as it will contribute significantly to the public's understanding of the Federal Trade Commission's rule-making process, including the influence of industry and trade groups on the rule-making process in general, and upon the proposed Business Opportunity Rule in particular. We have no commercial purpose in making this request.

We expect a timely response to this request which complies with FOIA guidelines as posted on the FTC web site. It appears from a careful review that none of the nine FOIA exemptions listed on the FOIA page of the FTC web site applies to this request.

This request should be satisfied through a simple phone call or memo to Lois Greisman. Then, a prompt email response to me would seem to be most appropriate.

I, Jon M. Taylor, am acting as agent for the above-listed group and am coordinating this request and the processing of information you provide in your response. If you need to discuss this with me, I can be reached at (801) 298-2425, or at (801) 671-1870. Please respond to the address below. Thank you in advance for your prompt consideration of our request.

Sincerely,



Jon M. Taylor, MBA, Ph.D., President, Consumer Awareness institute
291 E. 1850 South, Bountiful, UT 84010

FTC Press Conference

FTC Negligence of Pyramid Scams Moves to *Denial* Stage?

From End-of-Year Report by Robert FitzPatrick of Pyramid Scheme Alert, November 2012



The stealthy hand of the political lobbyist and the influence-buyer is apparently pushing the United State Federal Trade Commission (FTC) from silently avoiding MLM prosecution to, now, carefully avoiding any *mention* of pyramid scheme fraud, i.e., *denial*. In *1984ish* fashion, the FTC seems to have adopted a specially crafted language to make pyramid fraud disappear when speaking about "business opportunity fraud." MLMs are, in fact, the most common and most harmful form of such fraud.

The *NewSpeak* language that covers up the MLM "endless chain" fraud that plagues Main Street was put on display at a [Nov. 16 press conference](#) in which the FTC announced a "crackdown" on "business opportunity" frauds. The harms and evils of selling bogus "income opportunities", fake "jobs" and false "work-at-home" schemes - especially during a Recession - were eloquently described by the chief of the FTC Bureau of Consumer Protection, David Vladeck. Also the "tricks" used by "income opportunity" scammers to lure consumers into worthless "business opportunities" were described, *minus one trick*. That trick is the one that consumers are *most likely* to encounter and to be fooled by. It is the trick of offering an income based on recruiting of other seekers of the income who do the same. This is the classic "[endless chain](#)" trick that can promise "unlimited" income based on "endless" expansion of the chain of "distributors, coaches, IBOs, associates" or whatever pseudo-name is used to describe those who pay to join the income plan. The "endless chain" scams spread *virally*, reaching far more people more quickly, and they can defraud the public of much more money. They debauch the marketplace by disguising the frauds as legitimate "direct selling." And by claiming the ability to provide the utopian goal of unlimited wealth to followers, they can gain the persuasive and destructive power of cults.

The FTC did not acknowledge this trick or make any reference to the dominant role of [pyramid schemes](#) in "business opportunity" fraud because - under pressure from MLM influence-buyers and the MLM industry lobbyist, the Direct Selling Association - the FTC adopted a new [rule that specially exempts MLMs](#) from the rule's regulations.

Revealing how absurd such an FTC exemption is, the SEC recently shut down the fastest growing MLM in America, called [Zeek Rewards](#), for operating a pyramid scheme. That one MLM scam pulled in \$600 million from more than one-million victims in just 18 months! Yet the FTC has declared MLMs "exempt" from even being required to make disclosures about their "income" claims. During the Nov. 16 press conference, the terms, "pyramid scheme", "endless chain" and "multi-level marketing" were never uttered even once.

Reference: See "Media Advisory" (11/15/12) on next page, copied from the FTC web site at – http://www.ftc.gov/opa/2012/11/lostopp_ma.shtm

For an excellent separate account of regulatory capture of the FTC by the "pyramid lobby," read the report by Robert FitzPatrick titled: "*The Main Street Bubble: A Whistleblower's Guide to Business Opportunity Fraud. How the FTC Ignored and Now Protects It*" - included at the end of this report.

Media Advisory: 11/15/2012

FTC Announces Expanded Fight to Stop Deceptive Business Opportunity Schemes

More Than 70 Actions Brought By FTC and Its Law Enforcement Partners

The Federal Trade Commission will host a **press conference in Washington, DC, on Thursday, November 15, 2012, at 11 a.m. ET** to announce a major federal-state law enforcement crackdown on [scams that falsely promise jobs and opportunities to “be your own boss” to people who are unemployed or underemployed.](#)

David C. Vladeck, Director of the FTC’s Bureau of Consumer Protection, will be available to answer reporters’ questions, as well as Stuart Delery, Principal Deputy Assistant Attorney General for the Civil Division, U.S. Department of Justice; Teresa Thome, Deputy Chief Inspector, U.S. Postal Inspection Service; and Indiana Attorney General Greg Zoeller.



WHO: David C. Vladeck, Director, Bureau of Consumer Protection, FTC

Stuart Delery, Principal Deputy Assistant Attorney General for the Civil Division, U.S. Department of Justice

Teresa Thome, Deputy Chief Inspector, U.S. Postal Inspection Service

Greg Zoeller, Indiana Attorney General

WHERE: Federal Trade Commission
Room 432, 600 Pennsylvania Avenue NW
Washington, DC

CALL-IN: Reporters unable to attend the event can call in. The phone number is 800-398-9389, the confirmation ID number is 271344. The lines, which are only for news media, will open at 10:45 a.m. The conference leader is Bruce Jennings.

WEBCAST: The event will be [webcast live](#).

SOCIAL Join FTC staff online 2-3 p.m. ET to discuss the crackdown and get tips on

CHATS: avoiding job scams on Twitter. Follow [@FTC](#) and tweet questions/comments with the hashtag [#FTCbcp](#). Staff will also host a chat on the [FTC Facebook page](#) from 3-3:30 p.m. ET.

MEDIA Office of Public Affairs

CONTACT: 202-326-2180

A sampling of recent articles and media relevant to the FTC's Business Opportunity Rule and the MLM business model

“Pyramid Insurance,” by Jeff Ernsthausen, *Harper's Magazine*, October 2012

The author researched the funding of elected law enforcement officials (state AGs) and legislators who would have responsibility for MLM laws and regulations and found that the DSA had donated heavily to the political campaigns of these persons, even to Congressmen who might hold hearings about FTC action against MLM.

<http://harpers.org/blog/2012/08/pyramid-insurance/>

“The pink pyramid scheme – How Mary Kay cosmetics preys on desperate housewives”

The article explains how the ladies in pink become ladies in the red.

By Virginia Sole-Smith, *Harper's Magazine*, August 2012 issue

<http://harpers.org/archive/2012/08/the-pink-pyramid-scheme/>

“How Direct Sellers Dodged FTC Regulation”

By Karen E. Klein, *Business Week*, April 16, 2012

The article discusses BOR and quotes advocates for and against exempting MLM, as well as FTC staff justifications for their actions.

<http://www.businessweek.com/articles/2012-04-16/the-multibillion-dollar-direct-selling-industry-dodges-the-ftc#p1>

“Selling A Better Life,” by Donald Frazier, *Forbes Asia*, November 25, 2012

In the rough-and-tumble business of direct sales, Malaysia's Vijay Eswaran Learns from Mistakes and Builds a Movement. *This article demonstrates how desperate and vulnerable populations are prime pickings for MLM programs like Qnet.*

<http://www.forbes.com/sites/donaldfrazier/2012/10/24/selling-a-better-life/>

Complaint Review: Herbalife

Ripoff Report, Submitted: Wednesday, October 24, 2012, Reported By: Mary — Connecticut USA
Powerful account of how manipulative, deceptive, and degrading an MLM like Herbalife can be.

<http://www.ripoffreport.com/ehome-iooffice-bridge/weightloss-programs/internet-arizona-4F1F6.htm>

“Nu Skin and the short-sellers,” CNN report about an article by Peter Elkind with Doris Burke, *Fortune Magazine*, October 2012

The \$2 billion multilevel marketer in Utah -- with ties to Mitt Romney -- says its skin-care and nutritional products can delay aging. But short-sellers and a couple of angry ex-husbands are taking the company on, and they're not being quiet about it.

http://management.fortune.cnn.com/2012/10/26/nu-skin-short-sellers/?source=yahoo_quote

Video from Justice Department “Summit On Consumer Protection Issues”

Business Opportunity Scams, reported by C-Span, March 9, 2012

Panelists talked about specific types of financial fraud schemes. Topics included enforcement measures and recommendations for improved consumer protection programs.

Lois Greisman, former assistant to (former) chairman-turned-MLM-lobbyist timothy Muris and later a central figure in the BOR rulemaking, speaks of the Rule’s application to Business Opportunity fraud – like vending machines and envelope stuffing. Seriously!

<http://www.c-spanvideo.org/program/304838-4>

“For Romney, Ties That Bind,” by Joe Nocera, *New York Times*, October 26, 2012

Romney’s ties to Nu Skin go back to the days when he needed help financing the 2002 Winter Olympics in Salt Lake City. The problems with the FTC are reviewed, as is the exemption from the new Business Opportunity Rule.

“Herbalife Information Disputes Pyramid Allegations,” by G. Hudson, *Seeking Alpha* (for investors), September 13, 2012. This is one of many articles that followed a challenge by prominent short seller David Einhorn at a May 1 investor conference in which he asked some simple questions about the amount of sales were made to non-participants in the Herbalife network. <http://seekingalpha.com/article/865761-herbalife-information-disputes-pyramid-allegations>

G. Hudson later wrote “Is Herbalife A Fraud? That Is The Question.” proving the fraudulence in Herbalife’s promotion of its “business opportunity,” *Seeking Alpha*, August 8, 2013, http://seekingalpha.com/article/1618122-is-herbalife-a-fraud-that-is-the-question?source=email_rt_mc_focus_0

“An Investor's Guide to Identifying Pyramid Schemes,” by Bruce Craig (former assistant to Wisconsin AG), *Seeking Alpha*, Oct 11 2012. Craig cites and analyzes the relevant court decisions that clearly outlaw endless chain financial propositions as "inherently" fraudulent. Craig also notes that several state statutes outlaw "endless chain" income propositions regardless of the presence of some retail sales. (See the statutes of NC, WI, CA, ME, VT, and PR – Chapter 10 in my book.) <http://seekingalpha.com/article/918831-an-investors-guide-to-identifying-pyramid-schemes>

Ackman *It should also be noted that a great deal of publicity, including many articles in [Seeking Alpha](#), followed a 3-hour Sohn conference presentation by hedge fund manager William Ackman on December 20, 2012. bet a billion dollars shorting Herbalife, calling it a pyramid scheme and claiming he will see the stock drop to zero. <http://factsabouth Herbalife.com/> Others, including Dan Loeb of Third Point Capital and Carl Icahn took major positions against him. I weighed in with an article (January 24, 2012) titled **“Ackman Was Too Kind in his Attack on Herbalife,”** in which I expressed my doubts that any significant action would be taken by the FTC, in spite of extensive evidence amassed by Ackman. (full text on following pages) (http://seekingalpha.com/article/1130981-ackman-was-too-kind-in-his-attack-on-herbalife?source=google_news) Numerous other articles (many on *Seeking Alpha*) on the unfolding drama can be found with a Google search, using the search terms “Herbalife” and “Ackman.” Here a just a few examples:*

“Ackman Outlines Bet Against Herbalife,” by William Alden, *NY Times*, December 20, 2012. “From the perspective of Herbalife’s executives, the company is built on a sound model that

benefits its participants.” But “from the perspective of the hedge fund manager William A. Ackman, Herbalife is a pyramid scheme — and an attractive short-selling opportunity.”

“**CEO insists Herbalife is no pyramid scheme**,” by Irfan Khan, *Los Angeles Times*, December 21, 2012. Herbalife Ltd. CEO Michael Johnson assembled top company officials to prepare a point-by-point response to hedge fund manager Bill Ackman's assertions that Herbalife is a “sophisticated pyramid scheme.”

“**Ackman Is Right About Herbalife: It's Ripe for Investigation**,” by Janet Tavakoli, President, Tavakoli Structured Finance, *Huffington Post Blog* - Posted: December 23, 2012. “Bill Ackman, founder of hedge fund Pershing Square Capital Management, often claims his public analyses of companies in which his fund has investment positions are ‘for the good of the country.’ Ackman claims his latest idea, a short position in Herbalife, is a ‘patriotic short.’ . . . His patriotism seems to flare up when there's money to be made by his fund.”

“**Salve for Shorts**,” by Michelle Celarier, *NY Post*, February 3, 2013. The Los Angeles-based distributor of nutritional products is the subject of a law enforcement investigation, *The Post* has learned. The existence of the probe emerged after the Federal Trade Commission, responding to a Freedom of Information Law request by *The Post*, released 192 complaints filed against Herbalife over the past seven years.

http://www.nypost.com/p/news/business/salve_for_shorts_zBEIXePUI1oSoeMkv4WFQK

More Seeking Alpha articles:

“**Ackman's Short Of Herbalife Highlights Lack Of Adequate Information From Federal Agencies**,” by Bruce Craig, *Seeking Alpha*, Jan 2 2013. Provides an extensive analysis of how multi-level marketing programs, such as Herbalife, are vulnerable to regulatory action, though the applicable agencies have failed to provide a legally sufficient examination of the issues he raises and a clear legal standard.

“**Herbalife's Problem With Deceptive Earnings Claims**,” by Douglas Brooks, *Seeking Alpha*, Jan 17, 2013. Brooks believes Herbalife failed to address a key issue in its presentation defending its practices. That issue is the repeated use of deceptive earnings claims by high-level Herbalife distributors in their Herbalife promotional materials. He explains why most, if not all, of these earnings claims are deceptive, and that whatever course of action Herbalife chooses to deal with these claims will prove to be extremely disruptive to its army of distributors.

“**The Herbalife Controversy: A Historical Perspective**,” by Robert FitzPatrick, *Seeking Alpha*, Feb 1 2013. Looks at Herbalife and the latest chapter in a 90-year pyramid debate and unfinished regulation.

“**One Of Herbalife's Greatest Risks**,” by Douglas Brooks, *Seeking Alpha*, Mar 13 2013.

http://seekingalpha.com/article/1269591-one-of-herbalife-s-greatest-risks?source=email_rt_article_readmore

Brooks discusses how Herbalife has stopped allowing some fraudulent lead generation systems sponsored by high level distributors to continue. He had challenged these systems in a Seeking Alpha article published January 17, 2013..

The Salt Lake Tribune published a series of articles on MLM. In addition, they published articles on two of the ex-husbands of one of the founders, which are not relevant here.

“FTC drops direct sellers as target,” by Matt Canham, *The Salt Lake Tribune*, February 18, 2011 (See below) How the FTC’s proposed Biz Opp Rule was met with fierce lobbying by the DSA, who succeeded in getting MLM exempted. *This article deserves to be printed in full (see next page), as it describes the FTC’s BOR rulemaking prior to the final Rule in December of 2011. Monica Vaca describes the “change of heart” (caving to DSA pressure) the staff had leading to the MLM exemption.*
<http://www.sltrib.com/sltrib/home/51207514-76/business-companies-direct-earnings.html.csp>

– also from Salt Lake Tribune –

“Elusive Wealth, Strong lure,” by Steven Oberbeck *The Salt Lake Tribune*, February 22, 2011 Lured by the promise of wealth, thousands of Utahns every year become "distributors" of the pills, potions and lotions multilevel marketing companies in the state make. *Nearly all will fail, with their money flowing into the pockets of an elite few top-level distributors — men and women who typically get into the game early and make a fortune off those who try but fail to duplicate their successes.*
<http://www.sltrib.com/sltrib/home/51183138-76/average-companies-distributors-earn.html.csp>

“Multilevel marketers’ influence growing in Utah,” by Steven Oberbeck , *The Salt Lake Tribune*, Oct 23 2011

Nu Skin is among the Utah MLMs whose influence is visibly growing in the community- *especially since the DSA bought the support of AG Mark Shurtleff, Governor Jon Huntsman, and a host of state legislators. In 2006, the legislature passed a bill exempting MLMs with consumable products from prosecution as pyramid schemes – and Governor Huntsman signed it over the objections of consumer advocates.*
<http://www.sltrib.com/sltrib/home2/52706578-183/state-utah-companies-industry.html.csp>

“Utah’s Nu Skin expanding in China” – *The Salt Lake Tribune*, Sep 21 2012

Provo company adding stores, sales support for personal-care products. This frenetic expansion is part of a desperate effort to “re-pyramid” into other areas to prevent market collapse, since there is little substantive customer base except for its own distributors, as explained in my book *Multi-level Marketing Unmasked*.
<http://www.sltrib.com/sltrib/money/54941601-79/china-skin-company-distributors.html.csp>

“Debt and defeat at the bottom of the sales pyramid. Amid riches for a few, most in multilevel marketing lose out,”. by Steven Oberbeck, *The Salt Lake Tribune*, May 27 2011

Using stories of victims, Oberbeck paints a picture of defeat and loss that most in MLM experience, even after enormous effort. Those who may be on the verge of profiting are encouraged to put on appearances of success to lure others into their programs.
<http://www.sltrib.com/sltrib/money/51831477-79/companies-company-distributors-kay.html.csp?page=1>

“Mona Vie’s top guy: the richest multilevel marketer of all,” by Tom Harvey, *The Salt Lake Tribune*, May 27, 2011 Richest networker for the fruit juice company gives thanks to God. Brig Hart left Amway to build a huge and profitable downline at Utah-based Mona Vie. While a few succeed, the vast majority leave empty handed. So recruitment to replace dropouts is constant.
<http://www.sltrib.com/sltrib/money/51831930-79/amway-brig-company-distributors.html.csp>

“FTC Drops Direct Sellers as Target”

By Matt Canham, *The Salt Lake Tribune*, February 18, 2011

For federal regulators, the idea seemed like a no-brainer.

People thinking of selling Avon, Utah-based Nu Skin or some other multilevel marketing (MLM) products should know how likely they are to make a profit. They should know about any lawsuits against the company and the number of independent sellers who ended up demanding a refund.

After years of study, the Federal Trade Commission in 2006 formally proposed a "business opportunity rule" to protect people from fraud by requiring such disclosures of MLMs, also known as direct sellers, along with companies pitching vending machine routes and letter-stuffing campaigns.

Then regulators asked the public to comment. And they did. First by the hundreds, then by the thousands, almost all of which were sent by direct selling companies or their distributors clamoring that the rule would hurt their home-to-home business, if not kill it all together.

Two years later the FTC dropped any reference to MLMs and forged ahead with its proposal. The commission expects to finalize the business opportunity rule sometime later this year.

So what happened? That depends on your vantage point.

The direct selling industry says it demonstrated that the proposal was unnecessarily onerous and persuaded federal regulators to back off.

The FTC's staff say they decided the rule wouldn't help consumers determine if a MLM was a good bet.

And then there's a small group of critics who believes the FTC caved to political pressure from a questionable industry.

"It defies reason and the experience of millions of people to take the most common form of business opportunity solicitation and exclude it," said Robert FitzPatrick, president of Pyramid Scheme Alert, based in Charlotte, N.C. "This rule was snuffed out with a political lobbying campaign."

That campaign was waged largely by the Direct Selling Association (DSA), which counts 16 Utah businesses as members. And the group doesn't hide that it helped direct most of the 17,000 comments the FTC received.

"We certainly facilitated those communications. I'm not abashed about that at all," said Joseph Mariano, the incoming

president of the DSA. "We felt that the regulatory burdens they were going to place on legitimate businesses in an effort to weed out the scams were just too high."

The drawn-out debate over the business opportunity rule shows how aggressive direct sellers respond to regulations they find threatening, but also how the government has struggled to fashion rules for an industry that regulators regard skeptically.

Such regulatory dust-ups are of particular interest for Utah, which has more MLM companies per capita than anywhere else in the nation. Companies like Nu Skin, USANA and XanGo employ thousands and rack up annual revenues of \$4 billion. They also enjoy the support of Utah's political elite. Sen. Orrin Hatch, Reps. Jim Matheson and Rob Bishop and former Rep. Chris Cannon sent letters to the FTC questioning the business opportunity rule and how it applies to direct sellers.

The thousands of comments, including those from Utah political leaders, almost exclusively focused on three areas: a seven-day waiting period to sign up, the financial and legal disclosures, and a required list of references.

The companies felt a week-long waiting period would zap the excitement of potential distributors, making it harder to recruit new people into their sales force. They also felt the earnings and lawsuit disclosures would make it look like the company was sketchy.

"There is sort of a feeling like 'Why do you have to do this? Have you done something wrong?'" said James Bramble, general counsel for USANA Health Sciences, based in Salt Lake City.

As for the list of references, their complaints covered both privacy concerns and issues unique to the MLM world.

Distributors get more money when they add new distributors to their "downline," so encouraging someone to call independent sellers to check on the validity of the business could start a recruitment war.

"We were ultimately able to persuade the FTC that the direct sellers should not be covered," said Nu Skin General Counsel Rich Hartvigsen. "There are several million independent direct sellers in the U.S. When they get involved in an issue that impacts their business, they have a fairly loud voice."

Monica Vaca of the FTC's Bureau of Consumer Protection said the 17,000 comments were far more than the commission normally receives on a proposed rule, but she didn't believe the industry arguments resulted in the policy change.

"At its core what the business opportunity rule does is provide prospective purchasers with disclosures. Things we think are important for people to know before they invest money," said Vaca. "Some of those disclosures are going to be more difficult to apply in the MLM context."

She said the big one is the earnings disclosure. According to Vaca, MLM companies and even their distributors have an incentive to exaggerate annual earnings, making it easier to recruit others into the business.

"If they are engaged in some kind of collusion to inflate these earnings, then the earnings disclosure is not going to be really that useful," she said.

Vaca did agree that providing references to other MLM distributors could be counterproductive.

"If they have an incentive to recruit you into their downline, then you don't have somebody who is necessarily giving you the full, honest picture," she said.

Beyond the details of the regulation, Vaca said the commission had a change in heart through the rule-making process.

"Initially, we felt like there was really quite a lot of evidence there, that there are some bad practices in this industry. However, identifying bad practices of 14 companies is a little bit different than identifying that as a prevalent problem affecting the entire industry," she said, referring to past FTC lawsuits against 14 direct selling companies, none of which was from Utah.

[NOTE: Ms. Vaca refers to the 14 MLM companies the FTC has recently prosecuted as lack of evidence of widespread fraud in the industry. It is evidence, to be sure – but of an inept agency that has allowed thousands of MLMs to regularly fleece the public. – JMT]

The FTC decided that it would continue its case-by-case approach to rooting out the bad companies from the legitimate ones, focusing on how much of the money is made by recruiting others rather than selling products.

FitzPatrick, the vocal MLM critic, called that "absurd."

"The original rule was not to prove that each scheme was a fraud," he said. "The point of the rule was to provide disclosure so the consumer could know if it was a viable business opportunity."

He said the biggest need is for more information on potential earnings, because he said people envision making big money selling the products and recruiting other distributors, but the overwhelming majority makes little or no money at all. He thinks the FTC should have tried to tweak the disclosure, not jettison it entirely.

FitzPatrick also lamented the political involvement in the rule making, including a direct selling company in Georgia that hired past FTC Chairman Timothy Muris and former Consumer Protection Bureau Director Howard Beales to argue on its behalf.

Vaca rebuffed the claim that the FTC caved to industry pressure, saying: "I think our report really stands on its own. We talk about all the reasons why it was not a good fit."

But she also promised that the FTC would keep a vigilant eye on direct sellers.

"We are going to be active in the MLM world for a long time," she said. "The two main issues are the potential for a possible pyramid scheme, and the making of false or unsubstantiated earnings claims."

The FTC's proposal was a play off the already established franchise rule, which requires chains to provide lengthy disclosures to a prospective buyer. This time, the FTC wanted to target much less expensive ventures such as at-home work companies and multilevel marketing.

- Disclosures required:
- Any earnings claim made by the company
- A list of lawsuits concerning fraud or deceptive practices
- Description of any refund policy
- The number of purchasers in the past two years and the number who sought a refund
- A list of references, usually the 10 geographically closest to the new recruit

mcanham@sltrib.com Business opportunities
www.sltrib.com/sltrib/home/51183138-76/average-companies-distributors-earn.html.csp

Unprecedented Wall Street saga of the bet by William Ackman against Herbalife – his \$1 billion short sale of Herbalife stock – and those who bet against him

A great deal of publicity⁴² followed a 3-hour Sohn conference presentation by hedge fund manager William Ackman of Pershing Square Capital Management on December 20, 2012. Ackman bet a billion dollars shorting Herbalife, calling it a pyramid scheme and claiming he will see the stock drop to zero⁴³. Others, including Dan Loeb of Third Point Capital and the legendary Carl Icahn took major positions against him.

I weighed in with an article (January 24, 2013) titled “Ackman Was Too Kind in his Attack on Herbalife” (below). in which I presented evidence that Ackman’s calculations of harm done by Herbalife were conservative and that the entire MLM industry is flawed, unfair, and deceptive. I also expressed my doubts that any significant action would be taken by the FTC, in spite of extensive evidence amassed by Ackman. Numerous other articles on the unfolding drama can be found with a Google search, using the search terms “Herbalife” and “Ackman.”

Ackman was too kind in his attack on Herbalife

By Jon M. Taylor, MBA, PhD

With the hedge fund battle initiated by Bill Ackman's December 20 Sohn Conference presentation - calling Herbalife ([HLF](#)) a "pyramid scheme" - one point has been overlooked. He was way too kind in his criticisms of the company and of the multi-level marketing (MLM) industry, of which Herbalife is a top player.

As a consumer advocate with four decades of teaching, writing, entrepreneurship, and consulting related to the field of home business opportunities, I have analyzed approximately 500 MLMs (multi-level marketing programs) over the past 18 years and written three books on the subject. I would have to rank Herbalife near the top of the list of questionable MLMs.

Ackman concluded his presentation by charging that 1.9 million Sales Leaders for Herbalife have lost \$3.8 billion since the company's founding in 1980. In my opinion, this is a gross underestimate. Let's look more closely at the numbers.

Calculating the harm done by Herbalife

I agree with Ackman that the products are too expensive to be competitive with retail alternatives and that little selling occurs to persons who are not participating in the program. And no one makes the "residual income" held out to prospects without building a sizable downline of distributors beneath them. Careful study of the compensation plan confirms this. And why would anyone attempt to sell overpriced products, when they can be bought much cheaper online and

⁴² Many articles about the Ackman vs. Herbalife fracas were posted in the web site seekingalpha.com.

⁴³ The entire 34-page Power Point slide presentation is available online at - <http://factsaboutheralife.com/>

when the plan offers huge rewards for recruiting, compared to a pittance for selling direct to non-participants?

To build a downline is expensive and getting more so, as hundreds of MLMs are saturating U.S. and overseas markets. So Herbalife must "re-pyramid" (rebuild new pyramids) into market after market to compensate for what Ackman calls the "pop and drop" phenomenon, as each market reaches saturation and impending collapse - with no sustainable retail base of non-participating customers. The company's entries into obscure markets does not represent real growth, but merely re-pyramiding to replace declining markets for its bogus "income opportunity." Herbalife's nutrition clubs and ubiquitous "work from home" ads are merely efforts to maintain its income stream by recruiting a revolving door of new recruits, each investing their hard-earned dollars before giving up.

Ackman cites evidence that the cost of becoming a Sales Leader is at least \$10,000, and my own one-year test of a similar program (Nu Skin) suggests that the cost of conducting a successful MLM recruitment campaign is actually much more. A review of Herbalife's "Statement of Average Gross Compensation of U.S. Supervisors - 2011" shows that only 3.5% of "Total Leaders" are paid commissions exceeding \$10,000, making it possible for them to realize a net profit after expenses. These are at earnings levels labeled "Get Team," "Millionaire Team," and "President's Team."

The Statement claims that 25% of Distributors reach the level of "Supervisor and above" ("Leader"). Dropouts are not counted in its statistics, which hugely skews the calculations of average incomes to appear to suggest a far more favorable success rate. The company also claims that it has improved its retention rate, bringing it from approximately 43% to 48.9% in 2011. If we (1) assume a 50% dropout rate, (2) include the 75% of distributors who did not reach Leader status, (3) project the 50% dropout rate over a ten-year period, and (4) subtract costs of recruiting a downline, we get a loss rate of approximately 99.88%. In other words, about one distributor out of 813 realizes a significant profit after expenses. And if we exclude those few who hold the top spots in the pyramid of distributors (which also hugely skews the averages), the odds of new distributors earning significant profits is less than one in 10,000 - essentially zero. Recruits are being sold a ticket on a flight that has already left the ground.

Now let's look at the number of Herbalife distributors that have been recruited (and victimized) since the company's founding in 1980. By 1996, the company reported sales of \$1 billion, and by 2011, it reported 3.15 million distributors selling a total of \$4.3 billion. If we conservatively estimate an average of at least one million distributors and average sales of at least \$1 billion per year since 1980 (allowing for a minimal amount of sales to non-distributors), the total number of distributors cycled through the program during those 32 years would be roughly 32 million, with a total of about \$32 billion dollars in sales. Since 99.88% lose money, the total recorded as sales for the company could be considered an estimate of the losses for the downline distributors who provide the vast majority of the company's revenue from their failed investments. This is roughly eight times the losses reported by Ackman.

NOTE: My methodology and calculations were validated by five financial experts, but readers can examine this for themselves by reading chapter 7 of my free eBook [*The Case \(for and\) Against Multi-Level Marketing*](#).

So what is a pyramid scheme - and are all MLMs pyramid schemes?

Ask ten regulators (from the FTC, SEC, and state AG offices) to define a pyramid scheme, and you get ten different answers. About the only thing they (and Ackman) agree upon is that if revenues are derived primarily from recruitment, rather than from product sales, it's a pyramid. But even then, some would say that most sales must be to non-participants, while others would not even make that distinction. In fact, it is hard to get agreement on a good definition of "multi-level marketing."

The problem with most definitions of pyramid schemes is that they focus on *behavioral characteristics*, rather than on the underlying *structure* of the scheme. Ackman posits six "indicia of pyramids" - all behavioral::

- exaggerated earnings claims
- Inflated prices and need to sell to other members
- Emotional sales pitch - the "Dream"
- A history of lawsuits
- Targeting the financially unsophisticated
- Complex compensation plans

Note that none of these address the fundamental structural flaws in all MLM programs. Let me try to summarize an entire chapter in my eBook in which I define what is and what is not MLM and on what constitutes a pyramid scheme.

To gain a good grasp of this definitional issue, one can benefit from looking at the features of a classic, 1-2-4-8 no-product pyramid scheme, such as the "Airplane Game," which was active in the late 1980s. The nomenclature of the various levels of the game involve participatory levels such as 'passenger', 'flight attendant', 'co-pilot' and at the top, 'pilot'. Typically, a new recruit would pay \$1,000 to enter at the level of passenger, in the hopes of receiving an \$8,000 payout when one 'piloted out' at the top of the scheme. When the downline of participants at the bottom level have each paid their money to the pilot at the top, the pyramid matures and the pilot departs with his booty, allowing the next person to move up to his spot and those at the bottom to continue the recruiting process in hopes of each reaching the top and receiving the cash reward. Because of the endless chain of recruitment, the pyramid ultimately saturates a given market, and those at the bottom levels (93.3% of participants) are caught in a losing position. The loss rate of participants averages about 90% (between 87.7% and 93.3%, depending on the percentage of pilots who have continued to initiate new pyramids after reaping the reward).

The fundamental flaw in all pyramid schemes is the assumption of an infinite market, since they are structurally built up on an endless chain of recruitment. It is assumed that they will inevitably reach market saturation and collapse. The only way to get to the top is to recruit others into the scheme. There is a requirement for an investment ("pay to play") in order to participate. And all the money goes to the top.

MLMs, which evolved from classic, no-product pyramid schemes (and chain letters) are what I call "product-based pyramid schemes." They operate structurally on exactly the same principle, except that they disguise or launder the investment in the pyramid with the purchase of products (usually "pills, potions, and lotions"), and the pyramid may be many more levels deep, as with

Herbalife. Typically, they spread rapidly through recruitment of a whole network of endless chains of participants (a.k.a, distributors, associates, agents, etc), with thousands, or even millions of participants in an ever expanding mega-pyramid of participants. And instead of a loss rate of approximately 90% as with classic 1-2-4-8 pyramid schemes, the loss rate for MLMs is closer to 99.9% So participants in a classic, no-product pyramid scheme are 100 times more likely to profit as are participants in a product-based pyramid scheme/[MLM](#). And in fact the likelihood of receiving the promised rewards by getting to the top of a classic, no-product scheme are at least 1,000 times as great as in a product-based scheme/[MLM](#).

MLMs are not even shaped like a classic 1-2-4-8 pyramid scheme – which is so named because it looks like pyramid scheme with one, then two, then four, then eight participants stacked atop each other in the four levels of the pyramid. But most MLMs have far more levels, and by the time a 6th or 7th level in an MLM is reached, the number of participants is extremely wide, making the structure look more like a pancake (with a bump in the middle of the "upline") than a pyramid. An MLM like Herbalife could more appropriately be called a "pancake scheme," with a much larger base at the bottom losing money.

So I conclude that Ackman's claim that Herbalife is a pyramid scheme is an extreme understatement - way too kind. My research convinces me that MLMs like Herbalife are a form of white collar crime that is far more damaging than are classic no-product pyramid schemes, by any measure - loss rate, aggregate losses, or number of victims.

As a flawed business model, MLM is unfair, deceptive, viral, and predatory.

As if Herbalife by itself did not do enough harm to consumers struggling to stay afloat, it should be noted that Herbalife is one of hundreds of similar MLM programs with a loss rate I calculate to be upwards of 99%, several of which are publicly traded - Nu Skin ([NUS](#)), Medifast ([MED](#)), PrePaid Legal ([PPD](#)), USANA ([USNA](#)), Mannatech ([MTEX](#)), Tupperware ([TUP](#)) etc.). In the aggregate, *tens of millions of MLM victims worldwide suffer losses of tens of billions of dollars every year.*

In my opinion, Ackman errs in suggesting that Herbalife stands out as a "bad MLM," choosing to compare it to Avon. While it is true that Avon was once a legitimate direct selling company, they recently changed their program and are much more recruitment-driven, like other MLMs. I will grant that some MLMs like Herbalife and Nu Skin are worse than others, in that they are more highly leveraged; i.e., leveraging the losses of a huge downline of participants (victims) to the benefit of a few at the top of the pyramid. Looking at the industry as a whole, there are hundreds of MLMs with compensation plans (the root of all the problems) that are built on the same flawed assumptions that drive Herbalife.

Of approximately 500 MLMs I have analyzed, ALL assume an infinite market, which does not exist in the real world. ALL assume a virgin market, which does not exist for long. ALL suspend the laws of supply and demand, rewarding unlimited recruitment of a whole network of endless chains of participants - who are the primary customers. ALL hold out a false hope of income that is only possible for those at or near the top, who are usually the first ones in. And I have identified over 110 typical misrepresentations that are used in MLM recruitment campaigns. In fact, ALL of the MLMs I have studied are extremely unfair and deceptive and (as endless chain "opportunity" recruitment schemes) both viral and predatory as well.

Ackman is right in concluding that society would be better off without Herbalife. But Herbalife could be included in a multitude of MLMs that sap the most vulnerable among us of much-needed resources, and I would argue that that society would be far better off without all MLMs that follow the same endless chain recruitment model.

Most MLM recruits spend a few hundred dollars but find the selling of overpriced products and the pressure to recruit too formidable, so they drop out. They are the lucky ones. Others believe the MLM hype and become more committed, spending the family fortune or going deep in debt. Prospective MLM recruits should be given the warning: "the more you spend, the more you lose" - which is true of any scam.

Don't join Herbalife - gamble!

Let's look at it another way. Using the calculations above, you are 24 times more likely to profit from a single bet on snake eyes in a roll of the dice in a game of Craps in Las Vegas as you are to profit as a Distributor for Herbalife. And this is without risking one's social capital - the friends and family that resent your efforts to recruit them and may even shun you as loved-one-turned-recruiter.

It should also be noted that the personal losses from MLM participation often far exceed financial losses. From reports we have received, I conclude there are many thousands of divorces, estranged extended families, bankruptcies, lost homes, diverted careers, and even suicides. Some become addicted to the "easy money" allure of MLM to the point that they can no longer work at an honest job, but keep moving from one MLM to another in hopes of finding "the right program" for them. We refer to these victims as "MLM junkies."

So where is law enforcement in all this?

The Federal Trade Commission is supposedly the nation's consumer watchdog, charged with protecting consumers against "unfair and deceptive acts or practices in the marketplace." (Section 5 of the FTC Act.) Unfortunately, investigators working for the agency have assumed that any pyramid will reach saturation and collapse. They also assume that if MLM fraud was widespread, it would be reflected in a large number of complaints. They are wrong on both counts.

Let's look at the first issue. The assumption that pyramid schemes ultimately lead to saturation and collapse misled prosecutors involved in the 1979 FTC v. Amway case. Amway attorneys argued that though the company had been active for 20 years, it had not even captured 1% of the market - far from a saturated market - and therefore was not a pyramid scheme (assuming certain "retail rules" were enforced). But no distinction was made between *total saturation* and *market saturation*. Why would a city of 100,000 people need 100,000 distributors? Five may be plenty, with each new distributor finding it more difficult to get customers. So total saturation is absurd. It is *market saturation* that is at issue, and that happens very quickly. No MLM market can sustain itself, since there is no significant base of actual customers who are not participating in the scheme. MLMs like Herbalife get around this problem by "re-pyramiding" into new markets and/or by introducing new products and programs. Ackman's presentation of the "pop-and-drop" syndrome in one country after another demonstrated the need for such aggressive re-pyramiding in order to survive and grow.

And why do victims remain silent?

This is one of the most insidious facets of the MLM problem. Even MLM victims who have lost thousands of dollars almost never file complaints with either state or federal authorities. They blame themselves for their "failure" since MLM promoters claim that their programs are perfectly legitimate and that success is assured for those who work hard. But worldwide feedback from victims and their families convinces me that a greater factor for the silence of victims is *fear*. Since all MLMs are endless chains, every major victim is of necessity a perpetrator, having recruited as many people as they could in hopes of covering their expenses and eventually profiting. They fear self-incrimination, and they fear consequences from or to those they recruited, which likely includes close family and friends. So they remain silent. And since in law enforcement, the squeaky wheel gets the grease, nothing gets done.

Of course, one could complain to the Better Business Bureau. But the BBB includes among its "corporate sponsors" some leading MLM companies. In fact, the BBB gives an A+ rating to Amway - which says more about the BBB than it says about Amway.

The FTC caves to the DSA/MLM lobby.

In 2006, the FTC proposed a "Business Opportunity Rule" which would have required that business opportunity sellers disclose average incomes, any legal actions against the company, refund provisions, a list of references, and that a 7-day waiting period be required before investing in the program. The Direct Selling Association (DSA), the lobby for the MLM industry, appealed to millions of MLM participants and got over 15,000 MLM participants and 84 congressmen (influenced by money and votes) to write in and complain that MLM (rebranded "direct selling") be exempted. The FTC officials caved and exempted MLMs from compliance! What is needed to tackle the MLM issue are a cadre of Eliot Spitzer-style regulators, with the skill and the will and the resources to stand up to the DSA/MLM lobby (a.k.a. "the pyramid lobby").

The influence of the powerful DSA/MLM lobby over the FTC is detailed in a 200-page report I just completed titled: *REGULATORY CAPTURE: The FTC's Flawed Business Opportunity Rule*, which can also be downloaded free of charge from my web site.

Conclusion

Where Ackman's short attack on Herbalife will wind up, no one knows. But I do know this. Daniel Loeb, Carl Icahn, and others who bet long on the stock either don't understand the business model, or they don't care that millions of struggling families are impoverished by its tentacles, and our society is worse for allowing such unfair and deceptive practices to sap our resources and corrupt our markets. Bernie Madoff was a stain on Wall Street and the SEC. MLMs like Herbalife are a stain on Main Street and the FTC.

In January of 2013, the FTC actually took action against an MLM – Fortune Hi-Tech Marketing (FHTM)

Soon after the Ackman challenge, the FTC announced that it was taking action against an MLM company, and there was speculation that the company targeted would be Herbalife – considering the compelling evidence that Ackman’s team had uncovered and reported. But to the dismay of Ackman supporters, the company in question was not Herbalife, but Fortune Hi-tech Marketing, which had been investigated by the state offices of Attorney General in three states for flagrant abuses. However, it should be noted that the complaints against FHTM could apply to virtually the entire MLM industry.

At the request of the FTC, a federal court shut down FHTM, as explained in the notice below. But it has yet to be seen if the FTC is turning over a new regulatory leaf or just bowing to public pressure and the urging of the states of Illinois, Kentucky, and North Carolina, which worked together with the FTC to bring down FHTM.

For Release: 01/28/2013

FTC Action Leads Court to Halt Alleged Pyramid Scheme

FHTM Promoted Itself as a Path to Financial Independence, But Most People Made Little or No Money

At the request of the Federal Trade Commission and the states of Illinois, Kentucky, and North Carolina, a federal court has halted an allegedly illegal pyramid scheme pending trial. The FTC and the state attorneys general seek to stop the allegedly illegal practices of the Fortune Hi-Tech Marketing (FHTM) operation, which claimed consumers would make substantial income by joining the scheme. The operation affected more than 100,000 consumers throughout the United States, including Puerto Rico, and Canada. In some areas, including Chicago, the scheme targeted Spanish-speaking consumers.

“Pyramid schemes are more like icebergs,” said C. Steven Baker, Director of the FTC’s Midwest Region. “At any point most people must and will be underwater financially. These defendants were promising people that if they worked hard they could make lots of money. But it was a rigged game, and the vast majority of people lost money.”

According to the complaint filed by the FTC and the state attorneys general, the defendants falsely claimed consumers would earn significant income for selling the products and services of companies such as Dish Network, Frontpoint Home Security, and various cell phone providers, and for selling FHTM’s line of health and beauty products. Despite FHTM’s claims, nearly all consumers who signed up with the scheme lost more money than they ever made. To the extent that consumers could make any income, however, it was mainly for recruiting other consumers, and FHTM’s compensation plan ensured that most consumers made little or no money, the complaint alleged.

“This is the beginning of the end for one of the most prolific pyramid schemes operating in North America,” Kentucky Attorney General Jack Conway said. “This is a classic pyramid scheme in every sense of the word. The vast majority of people, more than 90 percent, who bought in to FHTM lost their money.”

As alleged in the complaint, FHTM promoted itself as a way for average people to achieve financial independence. Some FHTM representatives claimed they earned more than 10 times as much as their previous earnings in their second and subsequent years with FHTM. One person claimed that another representative earned more than \$50,000 in his sixth month and millions of dollars in subsequent years. Another person promoted a recruitment meeting on her Twitter account, stating, “Bring ur friends & learn how 2 make \$120K aYR.” At its 2012 national convention in Dallas, FHTM called its top 30 earners to the stage to present them with a mock-up of a \$64 million check, which several of them shared as a photo on social networking websites.

To participate in the scheme, consumers paid annual fees ranging from \$100 to \$300. To qualify for sales commissions and recruiting bonuses, they had to pay an extra \$130 to \$400 per month and agree to a continuity plan that billed them monthly for products unless they canceled the plan. Those who signed up more consumers and maintained certain sales levels could earn promotions and greater compensation, but contrary to FHTM’s claims, the complaint alleged, its compensation plan ensured that, at any given time, most participants would spend more money than they would earn.

According to the complaint, recruits were told they could earn high commissions by selling products to people outside the operation, but instead only minimal compensation was paid for sales to non-participants, and few products were ever sold to anyone other than participants. The scheme provided much larger rewards for recruiting people than for selling products, and more than 85 percent of the money consumers made was for recruitment.

In addition to charging the defendants with operating an illegal pyramid scheme and making false earnings claims, the FTC charged them with furnishing consumers with false and misleading materials for recruiting more participants. The attorneys general offices of Illinois, Kentucky and North Carolina joined the FTC complaint, as well as alleging violations of their respective state laws.

The defendants are Paul C. Orberon, Thomas A. Mills, Fortune Hi-Tech Marketing Inc., FHTM Inc., Alan Clark Holdings LLC, FHTM Canada Inc., and Fortune Network Marketing (UK) Limited. On January 24, 2013, the court halted the deceptive practices, froze the defendants’ assets, and appointed a temporary receiver over the corporations pending a trial.

The Commission vote, including Commissioner J. Thomas Rosch, authorizing the staff to file the complaint was 5-0. The complaint was filed in the U.S. District Court for the Northern District of Illinois, Eastern Division.

For more information about the case, in English and Spanish, consumers can call 202-326-2643. To learn more about multi-level marketing, read the FTC’s [Multilevel Marketing](#) and [Business Opportunity Scams](#) ([Estafas de Oportunidades de Negocio](#)).

NOTE: The Commission files a complaint when it has “reason to believe” that the law has been or is being violated and it appears to the Commission that a proceeding is in the public interest. The complaint is not a finding or ruling that the defendant has actually violated the law. The case will be decided by the court.

The DSA manipulation of the FTC's BOR rulemaking is the very embodiment of "regulatory capture."

Definition of 'Regulatory Capture'⁴⁴

Investopedia.com suggests a simple explanation of the term:

Regulatory capture is a theory associated with George Stigler, a Nobel laureate economist. It is the process by which regulatory agencies eventually come to be dominated by the very industries they were charged with regulating. Regulatory capture happens when a regulatory agency, formed to act in the public's interest, eventually acts in ways that benefit the industry it is supposed to be regulating, rather than the public.

Public interest agencies that come to be controlled by the industry they were charged with regulating are known as captured agencies. Regulatory capture is an example of gamekeeper turns poacher; in other words, the interests the agency set out to protect are ignored in favor of the regulated industry's interests.

This is precisely what has happened with the FTC and its Business Opportunity Rule. Weak officials allowed themselves to be manipulated by a powerful industry that regularly defrauds the public. This is amply proven, based on analyses of published, information provided by MLM companies in the book *Multi-level Marketing Unmasked* (formerly *The Case against Multi-level Marketing – an Unfair and Deceptive Practice*).

As explained at the outset, a compelling case for regulatory capture of the FTC by the DSA/MLM lobby has been presented here, with 21 "smoking guns" highlighted, which show the FTC staff favoring paid DSA/MLM lobbyists over unpaid consumer advocates. While none of these pieces of evidence are conclusive in and of themselves, the eighteen taken together demonstrate a clear pattern of "regulatory capture," in which a seriously flawed industry – which the FTC should be regulating – has manipulated the FTC to protect its interests, rather than the interests of consumers

Whether or not agency officials can be expected to withstand such a powerful assault on their core mission as occurred with BOR is a good question. It may be necessary to set up additional firewall protections against such agency capture. Some economists and public policy researchers are developing tools to accomplish this. A good example is a new book by two Harvard professors, Daniel Carpenter and David Moss, titled: *Preventing Capture: Special Interest Influence in Regulation, and How to Limit it*.⁴⁵

NOTE: For an excellent separate account of the influence of the "pyramid lobby" on the FTC, read the report in the Appendix by Robert FitzPatrick titled: *"The Main Street Bubble: A Whistleblower's Guide to Business Opportunity Fraud. How the FTC Ignored and Now Protects It"*⁴⁶

⁴⁴ Investopedia – www.investopedia.com/terms/r/regulatory-capture.asp#axzz2C8QNDdab There are also many other articles from peer-reviewed journals, such as "Regulatory Capture: A Review," by Ernesto dal, published in *Oxford Review of Economic Policy*, Vol. 32, Issue 3.

⁴⁵ See The Tobin Project: www.tobinproject.org/

⁴⁶ Included at the end of this report

Letter sent to three top FTC officials and to the director of CFPB, with a copy of this report and a copy of the book *The Case (for and) against Multi-level Marketing – over 600 pages of research and analysis*



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 Web site: www.mlm-thetruth.com
 December 19, 2012

Research, education, and advocacy for consumers

ATTN: Jon Leibowitz, Chairman
 Federal Trade Commission
 600 Pennsylvania Avenue, NW
 Washington, DC 20580

RE: Regulatory Capture of the FTC by the DSA/MLM lobby

Dear Mr. Leibowitz:

This letter is serious and deserves your personal and immediate attention. When you were appointed Chairman, those of us advocating for consumers were hopeful you would use the resources of the agency to stand up against unfair or deceptive acts or practices, as the FTC is charged to do. But unfortunately, *the agency has recently become a pawn of the most fraudulent of all the industries it should be regulating. The FTC has become a victim of “regulatory capture.”*

I am referring to endless chain recruitment schemes, a.k.a. pyramid marketing schemes, product-based pyramid schemes, or multi-level marketing programs (MLMs). We have presented evidence to your staff of not only widespread, but inherent and universal fraud in the entire industry. Having analyzed over 400 active MLMs (plus about 100 shut down or terminated), I can say with authority that all MLMs assume infinite and virgin markets, which don't exist in the real world. *All depend on unlimited recruitment of a network of endless chains of participants as primary customers. MLMs are therefore inherently flawed, unfair and deceptive. World-wide feedback demonstrates that they are also extremely viral and predatory. And they are by far the most prevalent (covering at least 90%) of all purported “business opportunities.”*

Because of these inherent flaws in the MLM business model, a “good MLM” is likely an oxymoron. There are not “good MLMs” and “bad MLMs,” as the FTC staff assumes. Some may be worse than others, but by design all are endless chain recruitment schemes. *Those joining after the first ones in are being sold a ticket on a flight that has already left the ground. Their chances of earning the “residual income” touted by promoters is virtually ZERO!*

Based on data published by the MLMs themselves, approximately 99.7% of all MLM participants lose money (after expenses). MLMs, or product-based pyramid schemes, are far worse than classic no-product pyramid schemes by any measure – loss rate, aggregate losses, and number of victims. *Using the company's own reports and calculations validated by financial experts, we calculate that **tens of millions of victims lose tens of billions of dollars every year.***

Regulatory Capture of the FTC, page 2

Over 18 years of research has culminated in my 400-page report (enclosed) – ***THE CASE (FOR AND) AGAINST MULTI-LEVEL MARKETING: The complete research-based guide to understanding the flaws – and proving and countering the effects – of endless chain “opportunity” recruitment, or product-based pyramid schemes (MLMs).*** The report documents indisputable evidence of not only massive, but universal, fraud in this flawed industry. This information (in less developed form) was made available to your staff during the Business Opportunity Rule (BOR) rulemaking proceedings. Yet the staff handling BOR was persuaded by a lobby for the MLM industry – the Direct Selling Assn (DSA) – to exempt MLM from having to disclose information that could help consumers (as prospects) make wise decisions – which could also help prevent huge losses. The staff dismissed the most extensive research ever done on the subject in favor of self-serving arguments by the DSA/MLM lobby, which acts as a cartel to control MLM’s dialogue of deception.

The FTC staff posts praise for its BOR on its web site and has spoken of its benefits at a recent consumer seminar. FTC staff members should not be boasting of the new Rule, but should instead be hanging their heads in shame. *Their praise for BOR is hollow, as over 95% of packaged business opportunities – and by far the worst of them – are MLMs, which are exempt!*

Tragically, an unintended consequences of BOR is that all packaged business opportunities will be incentivized to convert to an MLM model to avoid having to comply with the Rule. So with BOR, the FTC is actually in the position of aiding and abetting “unfair and deceptive acts or practices (UDAP) in the marketplace.”

The staff argued that MLM abuse could be handled on a case-by-case basis using Section 5 of the FTC Act. The absurdity of this position is demonstrated in the evidence in the report, which strongly suggests that several hundred MLMs are currently violating Section 5 – and in fact, with their inherent flaws, virtually all of them are. Yet the FTC staff admits to having prosecuted only about 14 MLM cases in the past ten years, out of hundreds that follow the same endless chain recruitment formula. *Relying on Section 5 (instead of a good protective Rule) is like placing a hearse at the bottom of a cliff instead of a fence at the top to keep people from falling off in the first place.*

The rulemaking process for BOR was a tragic waste of taxpayer dollars and of agency resources. With BOR, the FTC has utterly failed in what has likely been its greatest test. Your staff misled you in their recommendations, and you apparently were too busy to validate their conclusions, which amounted to “regulatory capture” by the very industry you should be regulating – or banning outright.

In my original 181-page report titled ***REGULATORY CAPTURE: The FTC’s Flawed Business Opportunity Rule*** (enclosed), I highlighted 21 “smoking guns” that – taken together – show a clear pattern of regulatory capture of the FTC staff by the DSA/MLM lobby. It is not a pretty picture of your agency’s performance.

In working with your FOIA office for the latter report, I have been acting as agent for the following top MLM experts, besides myself:

- Bruce Craig, former Assistant Attorney General, State of Wisconsin, who litigated some of the earliest cases against MLM companies
- Douglas M. Brooks, LLP, attorney, franchise, distribution and consumer protection litigation, including cases involving MLM firms,

Regulatory Capture of the FTC, page 3

- Robert Fitzpatrick, President, Pyramid Scheme Alert, author – *False Profits* and operator of the web site www.pyramidschemealert.org,
- Stephen Barrett, M.D., publisher of Consumer Health Digest, sponsor of anti-quackery websites and the web site www.mlmwatch.org,
- Eric Scheibeler, former federal auditor, author – *Merchants of Deception*

Though the reports are lengthy, you can begin by reading the summary and descriptive table of contents to get the gist of what the research reveals. And you can print out more (or access the links) from my web site at – mlm-thetruth.com. One knowledgeable expert on the subject commented that my reports show that *I have been doing the very research that the FTC should have been doing all along.*

These reports will also be distributed or made available to the following:

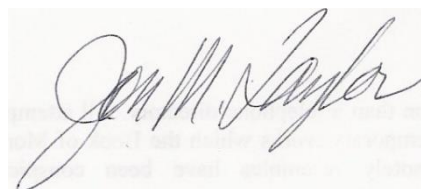
- Scott Wilson, Inspector General
- Charles Harwood, new Acting Director of the Bureau of Consumer Protection
- Richard Cordray, Director, Consumer Financial Protection Bureau
- Investigative reporters of some of the more important national media
- Members of Congress with oversight responsibility for the FTC
- Other appropriate federal agencies that deal with these or similar issues
- State Attorneys General and Consumer Protection Bureaus
- Libraries for business and law schools, as well as public libraries
- Other consumer advocacy experts

The regulatory capture of the FTC by the “DSA/MLM cartel” (my term) will be a topic to be debated for years to come.

Mr. Leibowitz, is this the legacy for which you want to be remembered as a Chairman of the FTC – *abject failure of the agency to protect against what is likely the most unfair and deceptive – and the most viral and predatory – practice it has ever confronted?*

Please give this matter serious attention and take corrective action to protect consumers, as well as your own reputation. *Either revise the Business Opportunity Rule to include MLM – by far the most egregious and prevalent of all purported “business opportunities,” or vacate the Rule altogether so that consumers are not misled into thinking they have significant consumer protection with BOR, when they don’t. This will also help to minimize the unintended consequence of incentivizing all business opportunity sponsors to adopt the flawed MLM model to avoid having to comply with the Rule, thus corrupting much of the home business marketplace. Considering the consequences of this matter for consumers, you can responsibly do nothing less.*

Sincerely,



Jon M. Taylor, MBA, Ph.D.
Research-based web site: www.mlm-thetruth.com

Form letter received in response to the above letter and over 600 pages and 18 years of research, including analyses of approximately 500 MLMs) sent to three top FTC officials and to the CFPB Director.

This is a less-than-responsible response to the most extensive industry-wide analysis ever done of a flawed business practice (MLM) that defrauds tens of millions of participants of tens of billions of dollars every year! The fact that victims of endless chain recruitment schemes seldom file complaints should not be the only determining factor in FTC investigations.



UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

Consumer Response Center

January 10, 2013

Jon Taylor
291 E. 1850 South
Bountiful, UT 84010

RE: FTC Ref. No. 42926881

Dear Jon Taylor:

Your correspondence to the Office of the Bureau Director regarding multi-level marketing was referred to the Consumer Response Center for reply.

Multilevel Marketing plans are subject to Section 5 of the FTC Act which prohibits unfair and deceptive business practices. Promoters of multilevel marketing plans may misrepresent the earnings of distributors touting the substantial earnings of a few top distributors as typical, violating Section 5 of the FTC Act. Pyramid schemes, in which distributors receive a substantial amount of compensation from recruiting and not from the sale of goods or services to ultimate users, are almost always characterized by promises of high earnings. The same can be said for Ponzi schemes where there is no product sold just "earnings" from cash paid in by new investors.

Multilevel marketing plans may misrepresent important characteristics of those goods or services that are sold as part of the program. Consumers should be especially wary of plans that offer miracle products, especially medical products. Frequently these programs sell weight loss products or miracle cures for which there is no scientific support.

Most states have laws that specifically prohibit "pyramid" programs. Although the laws vary from state to state, they most often prohibit plans that require distributors to pay an entry fee (or purchase required inventory) from which commissions are paid to existing distributors. As a result of these laws, most lawful plans do not require distributors to pay any fees (other than perhaps a distributor kit of minimal cost) or purchase any inventory. Consumers should beware of plans where it is suggested that they purchase a large initial inventory, even if not required, because such plans may be disguised pyramids. They may wish to ask a representative from the office of their state attorney general if the plan complies with state law.

The Federal Trade Commission cannot provide consumers with assessments of the merits of the many multilevel marketing plans operating at any one time. However, pyramids or other illegal plans often carry warning signs. Unlawful pyramids almost always promise rapid income opportunities from recruiting new distributors. Some even suggest that no sales are necessary and that they will build a "downline" for the investor. The earnings and product claims are usually amazing, and may be delivered in a pep rally style, such as a seminar, where people are encouraged to join immediately. Prospective recruits should be wary of such tactics, and contact their local Better Business Bureau or state attorney general prior to paying money or signing a contract.

The Federal Trade Commission acts in the public interest to stop business practices that violate the laws it enforces. Letters from consumers and businesses are very important to the work of the Commission. They are often the first indication of a problem in the marketplace and may provide the initial evidence to begin an investigation. The Commission is not authorized by Congress to resolve individual complaints. The Commission can, however, act when it sees a pattern of possible violations developing. The decision to open up an investigative action depends on how widespread the practice is, how many consumers are hurt, how much harm is done, and how much evidence we have. We must also determine how much staff time and effort we can put into each case, and we must concentrate on the most urgent.

We appreciate your taking the time to write. We hope the above information has been useful to your situation.

Sincerely Yours,
Consumer Response Center



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 March 9, 2013

Research, education, and advocacy for consumers

ATTN: Edith Ramirez, Chairperson
 Federal Trade Commission
 600 Pennsylvania Avenue, NW
 Washington, DC 20580

**Open letter to new FTC Chairperson Edith Ramirez:
 Please uphold the FTC's consumer protection role that was severely compromised
 in the MLM exemption to the Business Opportunity Rule**

Dear Ms. Ramirez:

This letter is serious and deserves your personal and immediate attention. With your appointment as FTC Chairperson, those of us advocating for consumers are hoping that you will use the resources of your agency to stand up against unfair or deceptive acts or practices, as the FTC is charged to do. But unfortunately, *the agency has recently become a pawn of what is likely the most fraudulent of all the industries it should be regulating. The FTC has become a victim of "regulatory capture."*

I am referring to endless chain "opportunity" recruitment schemes, or multi-level marketing programs (MLMs). During the rulemaking for the Business Opportunity Rule (BOR), we presented evidence to your staff of inherent and widespread fraud in the entire MLM industry. Having analyzed approximately 500 MLMs, I can without reservation state that all MLMs depend on unlimited recruitment of a network of endless chains of participants as primary customers. All MLMs assume infinite and virgin markets, which don't exist in the real world. MLMs are therefore inherently flawed, unfair and deceptive. World-wide feedback demonstrates that many are also extremely viral and predatory. And they are by far the most prevalent (at least 90%) of all purported "business opportunities."

Because of the inherent flaws in the MLM business model, a "good MLM" is likely an oxymoron. *There are not "good MLMs" and "bad MLMs," as the FTC staff assumes. Some are obviously worse than others, but by design all are endless chain recruitment schemes. Those joining after the first ones in are being sold a ticket on a flight that has already left the ground. The chance of earning the "residual income" deceptively touted by MLM promoters is virtually ZERO! Led on by false promises, virtually all MLM recruits could be classified as victims, even if they don't complain.*

In exempting MLMs from the recently enacted Business Opportunity Rule, the FTC staff was misled by the fact that the agency receives relatively few complaints against MLMs. This shows the staff's naiveté about the business model, as MLM victims almost never file complaints with law enforcement. One reason is fear – because in the endless chain of recruitment, every major victim is of necessity a perpetrator – having to recruit friends and family and others to have any hope of recouping their ongoing incentivized purchases and other expenses. They fear self-incrimination, as well as consequences from or to those they recruited – which could be best friends or relatives. They also have been taught that if they fail it is their fault for not "working the system." And the fact that some MLMs have lasted for decades is cited as evidence of their legitimacy.

Please restore the FTC's consumer protection role, page 2

From calculations based on data published by MLMs and the DSA (Direct Selling Association), we found that approximately 99.7% of all MLM participants lose money (after expenses). MLMs, or product-based pyramid schemes, are far worse than classic no-product pyramid schemes by any measure – loss rate, aggregate losses, and number of victims. Using methodology and calculations validated by financial experts, I estimate that tens of millions of MLM victims worldwide lose tens of billions of dollars every year.

Over 18 years of research – mine and that of others – has culminated in my eBook – *THE CASE (FOR AND) AGAINST MULTI-LEVEL MARKETING: The Complete Research-Based Guide to Understanding the Flaws – and Proving and Countering the Effects – of Endless Chain “Opportunity” Recruitment, or Product-Based Pyramid Schemes (MLMs)* – available for free download from my web site at – mlm-thetruth.com. *The book documents indisputable evidence of massive, industry-wide fraud, stemming from this flawed business model. This information (in less complete earlier versions) was made available to your staff in comments we filed during the BOR rulemaking process. Yet the staff handling BOR was persuaded by the DSA/MLM lobby to exempt MLM from having to disclose information that could help consumers (as prospects) make wise decisions and to help prevent inevitable losses from participation.*

The staff dismissed the most extensive expert research ever done on MLM in favor of self-serving comments by the DSA/MLM lobby, which acts as a cartel to orchestrate MLM's dialogue of deception. The staff was overly impressed by 17,000 comments – many of questionable validity or based on misrepresentations about the purpose of the Rule – as we discovered in a telephone survey. Less than 1/10 of 1% of MLM participants wrote on their own volition to protest the disclosure requirements, while 100% of those advocating for consumers – and even most commenters surveyed – favored the disclosures. Yet the staff chose industry appeasement over consumer protection. We also discovered a revolving door from consumer protection to fraud protection among former high level MLM officials, who assisted the lobbying effort in favor of the MLM industry.

The FTC staff posts praise for its BOR on its web site and has spoken of its benefits at a recent consumer seminar. Actually, FTC staff should not be boasting of the new Rule, but should instead be hanging their heads in shame. *Their praise for BOR is hollow, as likely over 95% of purported “business opportunities” – and by far the worst of them – are MLMs, which are exempt from the Rule!*

Tragically, an unintended consequence of BOR is that all sponsors of business opportunities will be incentivized to convert to the flawed, unfair and deceptive MLM model to avoid having to comply with the Rule. So with BOR, the FTC is inadvertently in the position of aiding and abetting “unfair and deceptive acts or practices (UDAP) in the marketplace” – when in fact, it's mission is to protect against such practices.

The staff argued that MLM abuse could be handled on a case-by-case basis using Section 5 of the FTC Act. The absurdity of this position is demonstrated by indisputable evidence that – with their inherent flaws – virtually all MLMs are violating Section 5, at least to some degree. Yet the FTC staff admits to having prosecuted only about 14 MLM cases in the past ten years, out of hundreds that follow the same endless chain recruitment formula. Relying on Section 5 with MLMs is like placing a hearse at the bottom of a cliff instead of a fence at the top to keep people from falling off in the first place.

The rulemaking for BOR was corrupt and a tragic waste of taxpayer dollars and agency resources. With BOR, the FTC failed one of its greatest tests. The BOR staff misled Commissioners in their recommendations, which amounted to “regulatory capture” by the very industry the FTC should be regulating – or banning outright. Industry spokesmen openly boasted that the FTC gave them just about everything they wanted.

Please restore the FTC's consumer protection role, page 3

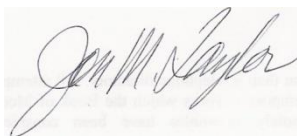
In my report titled “*REGULATORY CAPTURE: The FTC's Flawed Business Opportunity Rule*” (also available from my web site), I highlighted 21 “smoking guns” that – taken together – show a clear pattern of regulatory capture of the FTC staff by the DSA/MLM lobby. It is not a pretty picture of the FTC's performance in this arena.

You can begin by reading the summary and Descriptive Table of Contents to get the gist of what the research reveals. And you can access other research reports and related links from my web site at – mlm-thetruth.com. One knowledgeable expert commented that *these independent research reports represent the very type of research that the FTC should have been doing all along*.

Ms. Ramirez, you can make a great contribution to consumer protection by reversing the course of the FTC in its abject failure to protect against probably the most unfair and deceptive – and the most viral and predatory – practice it has ever confronted – MLMs, or endless chain opportunity recruitment schemes. Please give this matter serious attention and take corrective action to protect consumers. This may require “cleaning house” by re-assigning personnel responsible for the BOR's MLM exemption and for allowing the DSA/MLM lobby to bypass the consumer protection function of the FTC to accommodate an inherently flawed industry. Corrupted staff should be replaced with personnel who have the skill and the will to stand up to special interests like the DSA.

And please either revise the Business Opportunity Rule to include MLM – by far the largest and most egregious class of all purported “business opportunities,” – or vacate the Rule altogether, so that consumers are not misled into thinking they have consumer protection with BOR, when they don't. This will also help to minimize the unintended consequence of incentivizing all business opportunity sponsors to adopt the flawed MLM model to avoid having to comply with the Rule – corrupting much of the home business market. Considering the consequences for consumers, you can responsibly do nothing less.

Sincerely,



Jon M. Taylor, MBA, Ph.D.

NOTE: In working with your FOIA office for the aforementioned report, I have been acting as agent for the following top MLM experts, besides myself (with legal counsel):

- Bruce Craig, former Assistant Attorney General, State of Wisconsin, who litigated some of the earliest cases against MLM companies
- Robert Fitzpatrick, President, Pyramid Scheme Alert, author – *False Profits* and operator of the web site www.pyramidschemealert.org,
- Stephen Barrett, M.D., publisher of Consumer Health Digest, sponsor of anti-quackery websites and the web site www.mlmwatch.org,
- Eric Scheibeler, former federal auditor, author – *Merchants of Deception*

Copies of this letter are also being made available to the following:

- Scott Wilson, FTC Inspector General, with copies to the other Commissioners
- Charles Harwood, new Acting Director of the Bureau of Consumer Protection
- Richard Cordray, Director, Consumer Financial Protection Bureau
- The SEC, which may be responding to charges against Herbalife and Nu Skin
- Investigative reporters of some of the more important national media
- Members of Congress with oversight responsibility for the FTC
- State Attorneys General and Consumer Protection Bureaus

In response to this request for action, I received the same form letter as that sent Jan. 10 (in response to my prior letter to FTC leaders) from the “Consumer Response Center.”

Addendum: October 2014 Update

Complaints filed with FTC against MLMs

In a report on complaints filed with the FTC against MLMs during the year 2013, victims gave some very interesting feedback to FTC officials. Note especially the observations in Part III, which show clearly the pattern of unfair and deceptive practices throughout the MLM industry. (Download full pdf file by clicking the link at the bottom of the page at – www.mlm-thetruth.com/research/complaints-against-mlms-filed-ftc/ .) Quoting from a letter to the FTC's Director of Consumer Protection dated July 11, 2014:

A group of ICCA associates have spent months processing complaints filed against MLMs during the year 2013. They were supplied in response to an FOIA request from our coalition. We found them in an almost indecipherable form that made it virtually impossible to fully grasp patterns in what the complainants were actually saying. The spreadsheet was about 100 columns wide, and over half of those in the MLM category were not MLM at all, but complaints against payday loans, banks, and other irrelevant topics. Also, many of the complaints against business opportunities should have been classified as MLMs. It is little wonder that public statements by some of your staff may indicate a lack of understanding of the unfair and deceptive acts and practices that characterize multi-level marketing and therefore misled the FTC in its granting an exemption to MLMs from having to comply with the Business Opportunity Rule.

This lack of understanding, coupled with the obscuring of relevant data from consumers, led the previous FTC Consumer Protection Chief, David Vladeck to recommend to the FTC that no disclosures of any kind be required of multi-level marketing companies. In a report to the FTC, during deliberations of the Business Opportunity Rule, he wrote:

As the Commission noted in the RNPR, identifying a pyramid scheme (or, at least, one that attempts to disguise itself as a

legitimate business opportunity) entails a complex economic analysis including an in-depth examination of the compensation structure and the actual manner in which compensation flows within an organization. There is no bright line disclosure that would help consumers identify a fraudulent pyramid from a legitimate MLM.

The consumer complaint data, actually show multiple "bright lines" identified by the consumers themselves in recognizing signs of unfair and deceptive practices, or product-based pyramid schemes. The analysis reveals a sweeping pattern of abuse expressed in consumer complaints and, a large body of complaints, contradicting claims by staff of consumer silence about MLM abuse.

When properly sorted out, alphabetized, and reformatted into a Word document so that they can be read and analyzed, one finds clear patterns of widespread abuse – and cries for help from consumers that are being ignored, overlooked, or misread by FTC staff. The data show that the FTC has erroneously based its policy actions on a position that few consumers complain about MLM losses, deceptions, and pyramid schemes disguised as "direct selling" or that their losses and complaints constitute consumer harm. The misreading or failure to respond to consumer pleas for help may have led the previous director, David Vladeck, to make an unfounded and erroneous statement on a 2013 CNBC documentary (<http://www.cnbc.com/id/100359541>) on multi-level marketing, Herbalife and pyramid schemes, in which correspondent Herb Greenberg interviewed David Vladeck:

HERB GREENBERG: *Well, if 90% of the distributors are failing, what does that say? If -*

DAVID VLADECK: *It doesn't mat--*

HERB GREENBERG: *What kind of a business is it if 90% of 2.7 million every year-*

- right now we're talking 2.7 million distributors for one company.

DAVID VLADECK: *It doesn't mean that-- that-- that doesn't mean that the company made misrepresentations. And it doesn't mean that the people who-- who bought these-- franchises or participated in these schemes necessarily feel that they were injured.*

The study of complaints we completed show 930 complaints filed against 210 MLMs, plus 63 complaints filed against no-product pyramid schemes, Ponzi schemes, and pay-to-play chain letters. They are easy to read, as irrelevant complaints and non-essential information is excluded.

The conclusion of this study is that consumers have expressed anger at the unfair and deceptive practices they experienced in multi-level marketing; they have appealed to the FTC for relief and for investigations; they have provided a large body of evidence and specific areas in which

the FTC could take action to prevent abuse. Yet, due to an unwieldy data collection and classification system, FTC staff may be unaware of the public's experiences, needs, and requests. The cumbersome data format may have contributed to the false reading of consumer silence or lack of widespread abuses.

While the staff may have given some attention to individual cases, the patterns that this report reveals have been largely ignored, such as in the granting of an exemption to MLMs from having to comply with the Business Opportunity Rule. The failure of the FTC to respond to the consumer complaints and pleas across the MLM industry may also indicate a lack of knowledge among some staff members about the methodology and characteristics of "endless chain" and recruiting scams disguised as direct-selling companies.

More articles on the topic of MLM abuses – and DSA maintains cozy relationship with FTC officials

Numerous articles have continued to appear in Seeking Alpha and other media attacking and defending the practices of MLM since this report was sent to FTC officials. One that appeared in BusinessWeek.com⁴⁷ has the president of the DSA painting a picture of a cozy ongoing relationship with the FTC:

Industry representative Mariano says his organization meets regularly with lawmakers and the FTC to discuss the industry's self-regulation standards and the contributions that MLMs make to the U.S. and the international economy.

"I'm confident that the FTC, as well as other law enforcement agencies, understand the contributions that direct selling makes. We create a better life for all Americans, and the FTC has always recognized that," he says. Industry critics are "trying to turn around a positive thing for people and translate it into something bad."

My response to that statement is simply this:

A pig is still a pig, no matter how much money and effort is spent trying to position it as a horse.

⁴⁷ "New Efforts to Get the FTC to Regulate Direct Sellers," by Karen Klein, Businessweek.com, November 11, 2013

Addendum #2: January 2015 Update

The DSA scores again with the FTC's "Cooling Off Period" rule changed to favor MLMs

According to an FTC press release dated January 6, 2015:

The Federal Trade Commission has approved a [final amendment to its Cooling-Off Rule](#) that increases the exclusionary limit for certain "door-to-door" sales. The Cooling-Off Rule previously provided that it is unfair and deceptive for sellers engaged in "door-to-door" sales valued at more than \$25 to fail to provide consumers with disclosures regarding their right to cancel the sales contract within three business days of the transaction.

Under the final rule, the revised definition of "door-to-door sales" distinguishes between sales at a buyer's residence and those at other locations. The revised definition retains coverage for sales made at a buyer's residence that have a purchase price of \$25 or more, and *it increases the purchase price to \$130 or more for all other covered sales at temporary locations.*

In retaining the \$25 limit for in-home sales, the Commission stated that the rulemaking record reflected significant concern about high-pressure sales tactics and deception that can occur during in-home solicitations. Because the sellers' practices did not appear to be as problematic when sales were made away from consumers' homes, the Commission concluded that raising the value to \$130 for those sales would reduce compliance burdens for sellers while still protecting consumers who make purchases from sellers located in temporary locations.

The final rule amendment follows [the Commission's December 2012 notice proposing to increase the \\$25 limit to \\$130 to account for inflation.](#)⁴⁸

While comments regarding the proposed rule from consumer groups favored this protection against unscrupulous door-to-door salesmen, nearly all of them vigorously objected to raising the limit for sales at temporary locations away from home.⁴⁹

Knowing that most MLM recruitment occurs at temporary meeting rooms, the DSA praised the ruling, especially the \$130 limit. This allows for signup fees up to \$129 at hotels and other facilities, which are soon followed up with incentives to buy products and services to qualify for commissions and for rank advancement. As one commenter noted:

... Inflation formulas are irrelevant and rendered meaningless in the face of these often sophisticated solicitations. The initial payment is, in all cases, only a first step toward further solicitations, financial requirements, and other costs that a consumer is likely to incur upon initially paying. Further payments that the consumer may be subjected to after signing the initial sales contract may include monthly inventory purchase requirements, fee-paid seminars, marketing tools, travel costs, or purchases of sales leads.⁵⁰

Douglas M. Brooks, who has acted as plaintiff attorney for several MLM cases and done much pro bono work for consumer advocates, summarized the views and experience of other consumer advocates with these comments:

At first glance, the Commission's proposal to increase the exclusionary limit from \$25 to \$130 to account for the effects of inflation since 1972 appears to be reasonable. However, the increase would have the unintended consequence of exempting most multi-level marketing (MLM) plans from coverage under the Cooling Off Rule. Most MLM plans call for prospective "distributors" to purchase a "start-up kit," including product samples, in conjunction with enrolling in the plan. MLM recruitment generally does not occur at fixed retail locations; therefore the

⁴⁸ Go to - <http://www.ftc.gov/news-events/press-releases/2015/01/ftc-approves-changes-cooling-rule>)

⁴⁹ To read these comments, go to - <http://www.ftc.gov/policy/public-comments/initiative-461>

⁵⁰ Submission no. 563691-00038 by Robert FitzPatrick, founder of Pyramid Scheme Alert, March 2, 2013

solicitation and sale of MLM start-up kits is within the scope of the Rule. The Direct Selling Association (DSA), most of whose members employ MLM compensation plans, states that "the median cost for the start-up kit is \$99 ." See <http://www.dsa.org/ethics/legitirnatecompanies.pdf>. Accordingly, most MLM start-up kits (i.e., all such kits costing over \$25) are subject to the Cooling Off Rule. Increasing the exclusionary amount will have the effect of exempting most MLM start-up kits. The DSA's comment in support of changing the Rule fails to mention these facts or the impact the increase will have on its members. In fact, the proposed increase would benefit most of the DSA's members by exempting start-up kit purchases costing less than \$130, and it will harm consumers who will lose the protections of the Rule when they are recruited to join MLM sales organizations. Moreover, if the increase becomes effective, those few MLM companies which currently charge more than \$130 for a start-up kit will lower their prices to take advantage of the exclusionary amount, while those which currently charge less will be free to raise their start-up kit price to \$129.

The consumer's purchase of an MLM start-up kit is a critical event in the MLM recruitment process. As explained in the comment submitted by economist Stacey Bosley,⁵¹ the cooling off period is vital for consumers, given the importance of "urgency" in MLM recruitment. Once committed to the MLM company via the start-up kit purchase, the consumer will be more likely to continue making qualifying purchases in order to advance in the scheme, and will suffer losses well in excess of the exclusionary amount. It is well established that the vast majority of participants in MLM schemes lose their investments. See Fitzpatrick, Robert The Myth of the MLM Income Opportunity, <http://pyramidschemealert.org/PSAMain/resources/MythReport.html> and Taylor, Jon, *The Case (For and) Against Multi-level Marketing*, <http://mlm-thetruth.com/research/case4and-against-mlm/>. Since the Commission has seen fit to exempt MLM plans from its Business Opportunity Rule, the Cooling Off Rule is one of the few protections consumers have against being pressured into joining deceptive MLM business opportunities.

In addition, the inflation justification is itself suspect. As explained by economist William Keep in his comment, the poorest U.S. households have barely kept up with inflation since 1972. These are the households which are most susceptible to the typical MLM pitch, which promises financial independence and job security while making deceptive earnings claims.

I urge the Commission to keep the exclusionary amount at \$25.⁵²

We might echo the response of one consumer expert that with this rule change the FTC is "defending the sanctity of the home against invading scam artists wearing gold and bad suits, long after the "direct selling" tricksters stopped operating in living rooms and moved into hotel ballrooms, nutrition clubs, and infomercials."⁵³

The FTC press release closed with its usual claim:

The Federal Trade Commission works for consumers to *prevent fraudulent, deceptive, and unfair business practices and to provide information to help spot, stop, and avoid them.*⁵⁴

Oh really? Unwittingly (or intentionally), by this *change the FTC has facilitated – not prevented – fraudulent, deceptive, and unfair business (MLM) practices*. And having in 2012 granted MLMs an exemption to the Business Opportunity Rule, *the FTC allows masking, rather than disclosing information to spot, stop, and avoid such practices*.

The DSA/MLM lobby has good reason to celebrate its influence over the FTC. Conversely, consumer advocates have reason for sorrow that "the nation's consumer watchdog" caved to the DSA once again, *leaving consumers with little or no protection against the most unfair and deceptive (and often the most viral and predatory) of business practices – multi-level marketing*.

⁵¹ Submission no. 563691-00032, by Stacie Bosley, dated March 1, 2013

⁵² Submission no. 563691-00033 by attorney Douglas M. Brooks, March 3, 2013

⁵³ Letter dated January 7, 2015, from Robert FitzPatrick, president of Pyramid Scheme Alert, to members of the International Coalition of Consumer Advocates, an ad hoc group of consumer advocates.

⁵⁴ Op. cit.

— CONCLUSIONS —

The only research-based definition, together with the effects of multi-level marketing for practical (not legal) purposes is explained in Chapter 2 of my book *Multi-level Marketing Unmasked (updated)*. This definition of MLM really requires some explanation of its effects. Both the definition and effects provide a true and complete picture of MLM, which has been confirmed in analyses of over 500 MLMs:

Definition of multi-level marketing, confirmed by analysis of over 500 MLM programs:

Multi-level marketing (MLM) is a purported income opportunity, in which persons are recruited and incentivized to buy products and to recruit others in endless chains of recruits, all of whom must buy products and/or recruit others in order to qualify for commissions and to advance upward through multiple levels in company-sponsored pyramids of participants – with the majority of commissions paid to those at the top, based primarily on purchases of their “downline” (those beneath them). Such programs can appropriately be labeled “product-based pyramid schemes.”

The fundamental structure of product-based pyramid schemes is identical to classic, no-product pyramid schemes, except that in lieu of cash exchanged directly between participants, products are supplied and commissions processed through an MLM company infrastructure.

MLMs’ features and effects, confirmed by research and worldwide feedback:

As a business model incentivizing unlimited recruitment, MLM assumes an infinite market, which does not exist in the real world. MLMs (MLM programs) also assume virgin markets, which cannot exist for long. Also, since MLM compensation plans are heavily weighted towards recruitment, stable retail markets never materialize. Consequently, MLMs must expand (“re-pyramid”) into new markets to compensate for saturation of existing markets. MLMs are therefore inherently flawed and are the most

unfair and deceptive of all purported business opportunities. As recruitment-driven systems, MLMs can also be extremely viral and predatory. MLMs, or product-based pyramid schemes, do far more damage than classic, no-product pyramid schemes by any measure – loss rates, aggregate losses, and number of victims.

While financial losses can be significant, adverse effects can also sometimes be seen in bizarre or cultish behavior, divorces, loss of “social capital” or ruined relationships with family and friends, and even addiction to MLM’s empty promises. Some sacrifice careers or education to pursue MLM’s vaporish promises of easy wealth, “time freedom” to do what one wants, “residual income,” and a mystique of personal and spiritual fulfillment. Also, some MLM recruiters sell books, lead generation systems, and other “tools” to assure success, but which wind up increasing costs and eventual losses.

Prospects are typically lured into MLM with exaggerated product and income claims. Rewards are stacked in favor of those at the top of the pyramid, who are typically the first ones to join. Since approximately 99% of participants lose money, most eventually drop out, to be replaced by a continual supply of new recruits, who are likewise destined for loss and disappointment.

This definition is strengthened by information from subsequent chapters in the book. MLM is dependent on aggressive recruitment of new recruits as primary customers. Products are overpriced to accommodate large downlines. The loss rate and attrition rates are extremely high, and a myriad of misrepresentations are necessary to lure new prospects. And because victims seldom file complaints with law enforcement, there is little incentive for law enforcement to act against them or for legislators to enact better laws to protect against MLM fraud.

Though MLM is a fundamentally flawed business model manifested in bogus “business opportunities,” it is now protected by the FTC with its exemption from having to comply with its recently enacted Business Opportunity Rule (BOR) – which was

originally intended to protect the public from such practices. As an unintended consequence, other “business opportunities” will be incentivized to adopt the same flawed MLM model to avoid having to comply with the Rule – hurting rather than helping those they target.

As in the past, tens of millions of MLM victims will continue to suffer tens of billions of dollars in losses every year – likely the greatest consumer fraud in history.⁵⁵ With the Rule’s MLM exemption, the FTC is facilitating the perpetuation and spread of fraudulent endless chain recruitment schemes, in direct conflict with its mission to protect against “unfair and deceptive practices in or affecting commerce.”

The FTC countered its critics by insisting it can use Section 5 of the FTC Act to prosecute violators on a case-by-case basis. But as the research in my book demonstrates, to act against violators would require at least a 50-fold increase in staff just to prosecute current violators, which research shows could number in the hundreds. At least one FTC staff member who worked on BOR admits that the FTC has acted against only 14 MLMs in the last ten years⁵⁶ – at most 1% of likely offenders.

A startling statement by DSA president

FTC officials were skillfully manipulated by the \$4 million campaign by the Direct Selling Association and its minions. Neil Offen, who was Association president at the time, was quoted as saying⁵⁷:

“It is almost unprecedented what the FTC has done. . . The commission has tried to accommodate our industry completely.”

⁵⁵ This was expressed to me December 6, 2012, by Bruce Craig, former assistant to the Wisconsin Attorney General, who led the prosecution against some of the earliest cases against MLMs.

⁵⁶ “FTC Drops Direct Sellers as Target” by Matt Canham, *The Salt Lake Tribune*, Feb. 18, 2011

⁵⁷ Statement in DSA article: “A United Industry Makes Its Case: FTC Revises Proposed Rule,” by Brittany Glenn. Published about April 2008. Quoted later by Karen Klein in her article “New Efforts to Get the FTC to Regulate Direct Sellers,” *Bloomberg Business Week*, Nov. 11, 2013.

Taxpaying citizens deserve better.

The BOR rulemaking that transpired is a powerful demonstration of the need to appoint public officials with both the skill and the will to stand up against powerful special interests in order to protect the public from unfair and deceptive practices. In the case of BOR, the staff that advised the Commission clearly lacked both the competence and the determination to meet the agency’s primary obligation to the public – that of protecting against “unfair and deceptive practices in or affecting commerce.”

As mentioned at the beginning of this report, an unintended consequence of the final Rule is that all packaged business opportunities will have an incentive to convert to a multi-level format to avoid having to comply with the Rule. This means that the FTC will have actually facilitated the spread of unfair and deceptive practices – the very thing the FTC was established to protect against.

After all our work, there is not much more we can say, except that the FTC has been a huge disappointment to our group of volunteer experts and communicators who are united in working on behalf of consumers – and were all in favor of the original Rule which included “pyramid marketing schemes.” The FTC should have been working with us – not against us.

However, with a \$4 million lobbying effort and an appeal to millions of MLM participants, the DSA/lobby has succeeded in protecting the interests of its industry by gaining an exemption from a Rule that could have provided some protection for consumers against massive worldwide MLM fraud. It is worth repeating that widespread (inherent) MLM fraud causes tens of millions of victims to lose tens of billions of dollars every year. But because few victims complain, little action is taken by law enforcement, including the FTC.

In granting the MLM exemption to BOR, the FTC is not only avoiding its responsibility to protect against unfair and deceptive practices, but has also used precious resources in its rulemaking – a tragic waste of taxpayer dollars.

The FTC’s Business Opportunity Rule is a perfect example of “regulatory capture” where a regulatory agency allows itself to be manipulated, influenced, and eventually

controlled by the very entities it should be regulating. Voluntary consumer advocacy groups and researchers with limited resources – with whom the agency should be cooperating – find themselves opposing not only the companies scamming consumers, but also the very agencies that should be preventing abuses.

It is worth noting that those of us who have done the most independent research on MLM commented that the Initial Proposed BOR was inadequate and should have required that more information be disclosed, such as attrition rates and average amounts of purchases from the companies; i.e., net revenue from the company after subtracting purchases from the company (not even counting other business expenses). That was denied.

This raises a key question about the MLM industry: What kind of business would so vigorously oppose disclosure of references, legal actions against the company, average income (or lack thereof) for participants – or a brief waiting period – as did the MLM industry? This level of opposition to reasonable transparency requirements should by itself be a red flag supporting our claim that MLM is a fundamentally flawed business model.

So – the DSA/MLM lobby has been successful in capturing the cooperation and support of the FTC, to the point that the FTC is now protecting the MLM industry, which is guilty of the very type of unfair and deceptive acts or practices (UDAP) that the FTC was created to protect against. As citizens and as taxpayers, we deserve better.

Appendix

*Memorandum to President Barack Obama and Members
of Congress Overseeing the Federal Trade Commission and the newly created Consumer
Financial Protection Bureau:*

The Main Street Bubble

A Whistle Blower's Guide to

Business Opportunity Fraud

How the FTC Ignored and Now Protects It
by Robert L. FitzPatrick, Pres., Pyramid Scheme Alert

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Date: October 7, 2010
To: President Barack Obama and Appropriate Members of Congress
From: Robert L. FitzPatrick
Re: Main Street Bubble

We recently witnessed shocking revelations of how our Securities & Exchange Commission (SEC) failed America in the regulation and prevention of financial Ponzi schemes on *Wall Street*.

I urgently bring to your attention a parallel pattern that has prevailed for ten years at the Federal Trade Commission (FTC), a failure to protect Americans from Ponzis and pyramids on *Main Street*. These Ponzis are spread not as investment plans, loans or credit offerings but as “business opportunity” solicitations that promise extraordinary income potential. They are now the most common form of financial fraud that citizens fall victim to. During this recent period of regulatory immunity, the schemes have collectively and over time inflicted losses on Main Street consumers that dwarf those of Bernard Madoff’s Wall Street investors. The recent Recession has given the schemes additional predatory momentum as millions more people have become unemployed, face foreclosure and are in desperate need of income.

Oversight is immediately needed at the FTC. Additionally, the new Consumer Financial Protection Bureau must include these Main Street schemes in its coverage of “financial products.” The financial products sold to consumers in Main Street Ponzis entail consumers paying fees and related costs, signing a complex and lengthy legal contract, surrendering many legal rights otherwise available to consumers, restrictions on pricing that result in price gouging, and incurring longer term financial and legal liabilities or restrictions. Additionally, as further evidence that these schemes primarily sell a common *financial product*, not their advertised consumer items, most of them have strict non-compete clauses in their contracts prohibiting the consumers from investing or working with all other schemes of the same type, *regardless of the product they offer*. The purveyors of these financial products are, therefore, a clearly identifiable business sector.

The sales of “business opportunities,” are most frequently disguised as “direct selling” and referred to as “multi-level marketing” (MLM), “home-based” sales, network marketing or pyramid selling schemes. They are egregious violations of Section 5 of the FTC Act as “unfair and deceptive trade practices.” Yet, in 2001, the FTC virtually stopped investigating and prosecuting – and therefore *de facto* legalized – these types of scams. Consequently, they have multiplied in number, spread globally and become more aggressive in their solicitations.

For purposes of this report, they will be referenced by the name commonly used by regulators – Biz Op frauds. Collectively, they represent an enormous and highly manipulated financial bubble – billions of dollars invested in worthless or grossly overvalued assets – the Main Street Bubble.

The Main Street Bubble is inflated by hundreds of pyramid selling schemes and a related network of “cash gifting schemes.” Each year it expands with billions in investment dollars and the futile hopes, efforts and manipulated dreams of millions of Americans who are lured into them. Like all bubbles, the hoped-for returns are based on the deceptive and deluded projection of *endless expansion*. And, as in all bubbles, the losers are left with largely worthless assets, lost funds, squandered time and, frequently, more debt. Many people are financially ruined. The overpriced purchases and payments made by participants, along with costly, time-consuming and futile promotional efforts on behalf of the pyramid company, are revealed, in retrospect, to have been motivated by their *perceived future value*, which had been falsely advertised as “unlimited.”

Wall Street bubbles typically inflate rapidly and then collapse suddenly and totally. They may later re-emerge over a number of years in a new form, shifting in appearance but not substance, from stocks to real estate or some other commodity or from one security to another.

The Main Street Bubble, in contrast, inflates, collapses and re-inflates *continuously*, year after year. The majority of the “losers” are cycled out *annually* and the bubble is sustained with the concurrent recruitment of new investors and those reinvesting. The bubble is maintained and allowed to grow each year under the current protective policies of the Federal Trade Commission. With political protection allowing it to continuously reconstitute, the Main Street Bubble enjoys a *permanent* bailout. It functions as a constant drain of funds and energy at the Main Street level. Money from 99% of consumer investors (the proverbial *last ones in*) is systematically transferred to the scheme’s owners and 1% of the promoters, the equivalent to Wall Street’s Ponzi operators and feeder funds.

After years of no regulation, ubiquitous solicitations, publicized “success stories,” and orchestrated lobbying in which pyramid selling schemes are falsely depicted as viable income opportunities for millions of consumers or a unique business sector that produces a disproportionate percentage of millionaires, some consumers *and legislators* dismiss news of a 99% loss rate among all consumers who join the schemes. Reality clashes jarringly with myth. The scale of government neglect, the scope of the deception and consequent public harm are too much for many people to accept. It is indeed an “uncomfortable truth.” Yet, the truth of these loss rates has been known and statistically verified for many years.

- In the early 1980s former Wisconsin Assistant Attorney General, Bruce Craig, brought fraud charges against Amway, the largest MLM operating in that state. During the case, he obtained and reviewed tax returns of *all of Amway’s active distributors in Wisconsin*. The losses revealed by the tax returns were shocking even to the prosecutors. The “active” direct distributors constituted the company's top representatives in income. Yet this group’s tax returns showed an average net income of *minus \$900*. Those earning a net profit were *far less than 1%* of the total consumer participants. Asst. Attorney General Craig was later interviewed on the 1982 *CBS 60 Minutes* exposé of Amway entitled “Soap and Hope” where the findings were reported.⁵⁸
- In England in 2007, the Department for Business Enterprise and Regulatory Reform charged that Amway is “inherently objectionable” and must be “wound down” (closed down in USA-English). The government claimed that Amway violated England's Fair Trading Act 1973 among other laws. The Fair Trading Act 1973 addresses “Get rich quick schemes [operating]

⁵⁸ From the transcript of the *60 Minutes* show:

CRAIG: We're charging them with deceptive business practices because of the use of those hypotheticals because they so vary from what we feel is REALITY.

WALLACE: [voice over] Bruce Craig investigated some examples used in Amway literature. Examples that said that Amway distributors could make in excess of \$1200 a month. Money that some Amway distributors could be earned with just a few hours a week. But after looking at the average income of the 20,000 Amway distributors in Wisconsin, Craig came to the conclusion that such a claim was outlandish.

[to Craig] Surely, SOMEbody's making that kind of money.

BRUCE CRAIG: Yes. That's correct.

WALLACE: How many? Percentage wise.

BRUCE CRAIG: About one percent.

WALLACE: [voice over] Amway DID make the disclaimer that \$1200 a month was ONLY hypothetical but that still doesn't convince Bruce Craig.

BRUCE CRAIG: If the figure of successful distributors was 1 out of 5 as opposed to 1 out of 100 we wouldn't be in court right now.

WALLACE: [voice over] And, Craig says that even the distributors who, on paper, earn an average of \$14,000 dollars a year in Wisconsin actually earn a lot LESS. How much do they actually make?

BRUCE CRAIG: After business expenses, a net income of minus \$918.

WALLACE: WAAAAIT a MINute! The direct distributors who make a gross income on average of over \$14,000 wind up losing almost \$1000 after business expenses?

BRUCE CRAIG: On average. Yes.

on the same basis as chain letters...” The government based its action largely on its documented findings that more than 99% of all UK Amway distributors had lost money. This 99% loss rate held true from more than three decades of Amway UK operations and had inflicted financial harm on tens of thousands of UK consumer/investors.

- A huge database of consumers who have lost money as Amway distributors has been compiled by whistle-blower, Eric Scheibeler, author of *Merchants of Deception*, a book about deception in Amway’s solicitation campaigns. Scheibeler was involved in Amway for nearly a decade and reached the upper level of Amway’s pyramid hierarchy. When he presented direct evidence of deception and massive consumers losses to Amway officials he was driven from the company, vilified and sued. His database now has thousands of verified and documented reports of losses from consumers all over the world, including more than 200 from Australia and, increasingly, many coming in from China.⁵⁹
- The 99% rate is by no means limited to Amway, but rather occurs among *all* MLM companies that employ Amway’s “endless chain” pay plan and in which few distributors earn profits from retail selling. The pyramid structure, lack of sustainable retail sales and “top loaded” pay plans (the majority of commission – per sale – is transferred to the top levels of the recruitment chain) *guarantee* these loss rates. Most MLM companies employ the Amway-type pay plan and fit this description. *Pyramid Scheme Alert* compiled statistical data on commission payouts disclosed by 11 of the largest and better known multi-level marketing companies, including Amway. The data revealed that the 99% loss rate held true for *all of them*.⁶⁰

Collectively and over time the Main Street Bubble far exceeds Bernard Madoff’s Wall Street fraud in scale of financial harm. An estimated \$10 billion *per year* are lost by US consumers. Worldwide, the figure is far higher, with most losses inflicted by US-based companies.

As in Bernard Madoff’s “hedge fund,” the value of the consumer investments in the “direct selling” schemes depends on the continuous enlargement of an investor base. When Madoff’s bubble suddenly burst most investors realized their losses immediately. But, as prosecutors and whistle blowers revealed, the investments of nearly all were actually lost the day they were placed with Madoff. This is because his investment fund operated as a Ponzi scheme. It was only *disguised* as a hedge fund. Returns were not generated from profitable trades but from a money transfer of later to earlier investors. Such a money transfer plan dooms most investors *by design*.

Similarly, the Main Street Bubble is composed of investments ranging from hundreds to tens of thousands of dollars from millions of consumers seeking the “income opportunity” that the schemes dramatically portray and aggressively solicit investors to join. This income opportunity is disguised as a “direct selling distributorship.” In reality, the “business opportunities” are pyramid schemes. The investors are told they are investing in “distributorships.” In fact, returns are not generated from profitable and sustainable retail selling, which real distributors do, but from each distributor recruiting many new distributors.⁶¹ Effectively, the same unprofitable

⁵⁹ See <http://www.merchantsofdeception.com/>

⁶⁰ The data supporting the 99% loss rate and the concentration of commission rewards to the top 1% is available in the report “The Myth of MLM Income Opportunity” which examined payout data on eleven MLMs. See <http://www.pyramidschemealert.org/PSAMain/news/MythofIncomeReport.html>

⁶¹ It is important to grasp that the absence of retail sales in a “direct selling” business opportunity scheme is not an infraction or an excess or an abuse. Rather, it fundamentally alters the business from legitimate direct selling to a “closed market” in which the vast majority of participants *cannot succeed*, since endless expansion of “distributors” is *impossible*. It is this type of “non-retailing” multi-level marketing scheme, that prevails among the members of the Direct Selling Association (DSA).

distributorship is simply resold continuously. The money transfer is laundered through sign-up fees, costly “marketing tools” and induced or mandatory purchases of often absurdly inflated products. *This system, advertised as a “business opportunity,” inflicts documented financial losses on 99% of all consumer/investors each year.*

Each consumer/investor in the Main Street Bubble experiences the inevitable financial loss *individually*, not as part of a group of victims such as in the Madoff Ponzi. No group awareness develops, which might help warn future investors. Main Street victims seldom learn the nature of the fraud that harmed them, which at least the Madoff victims understood. Though most suffer enough loss in the first year to quit the schemes, some may continue to pursue the “dream” for years in a futile effort to solicit new consumer investors or they move from one scheme to another. These believers suffer far larger losses. Yet, as in the Madoff scheme, their investments are actually doomed from the day the consumers join the schemes because of the pyramid structure, impossible recruitment requirements and the unsustainable money transfer system that siphons funds to a handful of promoters at the top.

The Main Street Bubble is not hidden. Indeed, the schemes operate in plain sight. As many as ten million Americans are lured to invest in them annually. Solicitations to join them are everywhere now – in churches, at the office, in the neighborhood. They inundate the Internet. *USA Today* recently reported that *YouTube* now features nearly 23,000 “cash gifting” videos. The *London Times* has referred to America’s Biz Op Pyramid schemes as the “poor man’s Ponzi scheme.”⁶² Others compare them to a form of economic cancer. The schemes multiply in number each year, financially devouring savings and investments of millions of consumers. Participants are induced to prey upon their very own friends and family to recoup their investments from their *recruits’* lost investments. Tragically, for millions of Americans the pursuit of these direct selling schemes is now viewed as a pursuit of the American Dream, which the Main Street Bubble has hijacked.

The multi-level marketing Biz Op schemes gain little media attention because they have enjoyed *de facto* government endorsement over the last ten years. The news media is faced with a dilemma of *accusing*, not exposing, them. Journalists routinely raise the *question* of fraudulence and economic harm when reporting the schemes, but they have few authoritative sources to reference. Many investigative writers fall back on anecdotes of consumer losses but also inevitably include, for “balance,” the rare instance of one who made a great deal of money in the scheme.⁶³

Consequently, the American public is left largely in the dark and sadly misled. The prevailing media and government message is the myth that MLM is a viable, legal and perhaps, as the promoters claim, the consumer’s *best* chance for income in troubled economic times. Those who do confront reality after being harmed are mostly silenced by shame or fear into accepting losses. If they overcome these obstacles they still have limited recourse for restitution. Private lawsuits are beyond the means of most. Regulators routinely ignore complaints. Independent whistle blowers, at great cost to themselves, have provided facts and analysis to the media and, in vain, to the FTC. Other consumers have sought justice in class action lawsuits.⁶⁴ Some fraud

⁶² See full *London Times* article, “Pyramid Swindlers Unmasked,” February 1, 2009, in the Appendix.

⁶³ The rare “winners” in MLM are not the result of their special talent, ambition or persistence as MLM schemes routinely claim. Nor are they the outcome of mathematical odds in open market competition. Rather, they are intrinsic to the *design*. 99% of consumer/investors *must* lose for a tiny group at the pyramid’s peak to gain as “commissions and profits.” Their “success” is not evidence of the scheme’s potential opportunity for the others but the impossibility of that opportunity. The system is closed. Value is not exchanged. Money is merely transferred.

⁶⁴ In the past, the FTC utilized class action lawsuits to support prosecutions and as reasonable cause to open investigations. Today, though numerous class action suits have been filed against major MLMs such as Amway, Herbalife, Usana, Pre-Paid Legal, and others – all making the same charges of pyramid

investigators and financial analysts have also warned investors, the FTC and the SEC about the pyramid selling schemes that sell securities on major stock exchanges.

The FTC has direct federal regulatory oversight over multi-level marketing. This oversight was effectively abandoned in 2001 following President George W. Bush's appointment of Timothy Muris to chair the FTC. At that time, Muris was an anti-trust lawyer whose largest client was the multi-level marketing company, the Amway Corporation. In addition to being the icon and business prototype of nearly all other multi-level marketing companies, Amway is one of the most politically influential corporations in America with powerful ties to the previous George W. Bush administration and to the National Republican Party. Amway's paramount lobbying goal is to shield itself and other schemes of its type from FTC fraud investigation. To prevent prosecution it has engaged in influence-buying on an extraordinary level (details of Amway's and the "pyramid lobby's" influence-buying are included later in this memorandum).

Under Timothy Muris, the FTC went beyond what the SEC did in terms of lax law enforcement and regulatory negligence of Wall Street. It effectively *legalized* this form of Main Street business fraud. This was achieved, not by vote of FTC Commissioners, some of whom may have been unaware of the policy change, but primarily by staff actions under the chairmanship of Muris and continues to date. These have included:

- Effectively halting investigations and prosecutions of pyramid selling schemes.
- Consistently failing to monitor companies that had been issued enforcement orders by earlier FTC Commissions and are blatantly violating these orders.
- Issuing a widely circulated letter that obscured and appeared to permit practices – paying rewards for “endless chain” recruiting without retail sales as a revenue source – that the courts, and 30 years of earlier FTC policy have declared are illegal.⁶⁵ The letter was used by

fraud – the FTC has not even opened investigations. In one previously settled class action lawsuit brought by consumers against Herbalife, 2,700 former distributors filed claims with aggregate losses totaling approximately \$19 million. The suit charged Herbalife with operating a pyramid scheme and using false and misleading claims about income to lure investors. (Nancy Jacobs, Individually on behalf of herself and all others similarly situated, and on behalf of the General Public, Plaintiff, vs. Herbalife International, Inc., et. al., Class Action Complaint, Feb.15, 2002 filed before the US District Court for the Central District of California, Los Angeles Division).

Even state prosecutions do not prompt FTC action against MLMs. The Attorney General of California brought suit against a large MLM, Your Travel Biz.com (YTB), which is a member of the Direct Selling Association. The Attorney General called YTB “a gigantic pyramid scheme.” The FTC has not responded. See <http://pyramidschemealert.org/PSAMain/news/YTBProsecuted.html>

⁶⁵ The judicial foundation for the FTC to prosecute MLM endless chain schemes is clear and well established. It was cited in one of the last significant prosecutions that the FTC undertook, before the Bush administration placed a protective canopy over them with the appointment of former Amway attorney, Timothy Muris, as FTC Chair.

Count 5 of FTC Complaint against the large MLM, Equinox International, filed in the United States District Court, District Of Nevada, August, 1999, stated, “the Equinox program is an inherently unlawful scheme whose essential element is the payment by participants of money to the company in return for which they receive (1) the right to sell a product, and (2) the right to receive in return for recruiting other participants into the program rewards which are unrelated to the sale of the product to the ultimate users.... The result of the structure and operation of the program is that financial gains to Equinox participants are primarily dependent upon the continued, successive recruitment of other participants... This type of scheme is often referred to as a pyramid.”

In his formal declaration that concluded Equinox was a pyramid scheme, FTC pyramid expert, Dr. Peter Vandernat wrote at that time, “In distinguishing between a pyramid scheme and a legitimate business, the critical issue is whether rewards paid in connection with recruitment are tied to, or are derived from, the sales of goods and services to the general public (i.e. retail sales)...The Koscot case affirmed the stated

MLM companies to persuade millions of consumers that previous FTC policies and court actions that defined pyramid selling fraud were no longer valid.

- Consistently ignoring consumer requests, complaints, class action lawsuits, international regulatory actions and media exposures concerning fraudulent business practices of US-based multi-level marketing companies.
- After taking public comment on a proposed FTC rule, which had been years in the making, to protect consumers from fraudulent “business opportunity” schemes, the staff rejected further comments from whistleblowers but at the same time held an *ex-parte* meeting with the MLM lobbying organization, the Direct Selling Association, which was seeking to exempt all MLM companies from the rule.
- Following the meeting, the FTC staff recommended that MLM companies would be *exempted* from any new rule to regulate business opportunity frauds. This ruling was made even though multi-level marketing schemes overwhelmingly constitute the most common form of “business opportunity” frauds that consumers encounter and MLM schemes have been the source of numerous FTC prosecutions.
- In recent years, a new pattern of revolving door work has developed between the FTC staff and MLM lobbyists. Key FTC staff have taken jobs with law firms that represent the multi-level marketing schemes. The former chairman of the FTC, Timothy Muris and the former head of Consumer Protection, J. Howard Beales (appointed by Timothy Muris while he was FTC Chairman) worked as MLM lobbyists to influence the FTC against regulation of multi-level marketing. Another Director of Consumer Protection, Jodie Bernstein, subsequently became a lobbyist for the Amway Corporation, and has urged the FTC to exempt Amway and similar schemes from any new rules over business opportunity frauds.

Business opportunity frauds, structured as multi-level marketing schemes, are insidious as well as financially destructive because they lure consumers to spread financial harm among close friends and relatives, the “warm list” of recruits, as they are termed. The schemes operate by exciting misguided dreams and false hopes of a secure financial future through financial investments in the schemes. These deceptive promises lead many consumers to forego jobs and education, to incur additional debt, and to commit months or even years of time in what are carefully crafted financial traps.

Most, but not all, members of the Washington, DC-based lobbying group, the Direct Selling Association, now operate under the Amway “business model.” The Amway model, under FTC protection, has come to dominate and corrupt the direct selling industry.

Endless chain frauds are illegal under many state statutes and in some countries. Lacking FTC support, few states can prosecute the large schemes, due to limited resources. The schemes now operate with relative immunity from prosecution.

The true effect of these Main Street frauds is even more destructive since \$10 billion is filched from the middle class, least able to afford losses. The schemes claim perfect legality and, just as Bernard Madoff did, they cite the lack of federal prosecutions as proof of their legitimacy.

issue to be the critical factor. Later, cases such as *Webster v Omnitrition* and *Gold Unlimited* affirmed *Koscot*. In *Webster* the court also found that for pyramid analysis the sales that are made to a distributor’s downline do not count as retail sales. A “retail sale” refers to a sales of product to general consumer, i.e., someone who is not a member of the organization.”

While our government seeks to repair America's tarnished reputation abroad, the FTC's policy has resulted in US-based pyramid schemes damaging US credibility internationally. Most MLM companies operating worldwide are US-based.

- In 2005, China, America's largest economic competitor, banned this US-sanctioned MLM business model entirely.⁶⁶
- In 2006, England sought to close down the Amway Corporation, the largest US MLM operating in that country, on the grounds that it harmed the public.⁶⁷
- Sri Lanka recently passed new anti-pyramid scheme laws aimed at curbing the exploitation of its poor citizens by MLM schemes, most of which are from the USA.
- Government officials in India have raided Amway offices and now brought criminal charges against Amway for operating a pyramid scheme.⁶⁸
- Other MLMs that operate under the model that the FTC now allows, have been prosecuted in others countries for fraud.⁶⁹

While this memo may be read as alarmist, I ask you to consider that SEC whistle-blower, Harry Markopolos, was viewed similarly. And, just as a charge of fraud against prominent, politically-connected figures may seem far fetched to some, I ask you to remember that Bernard Madoff was viewed as above reproach by many in the government, media and investor community. I also ask you to recall that, using fraudulent accounting, Enron grew to become our 7th largest company and its CEO, Kenneth Lay, held celebrated business credentials and political connections at the very highest level.

Ferretting out and confronting fraud that is imbedded within the fabric of the legitimate marketplace and affiliated with elected leadership requires courage and will. Revealing fraud inevitably triggers collapse, loss and outrage. However, as the Madoff debacle has shown, lack of action leads to even greater harm.

While the government works to rescue our economy from Recession and financial chaos, the spread of false "income opportunity" schemes subverts the economy, misleads and confuses the public, obstructs the goal of renewed productivity and entrepreneurship and impoverishes millions of people.

Two actions are immediately needed:

1. Congress needs to direct the FTC to renew investigation and law enforcement against Main Street Ponzis, disguised as "direct selling" and "multi-level marketing."
2. The newly established Consumer Financial Protection Bureau should be empowered to investigate pyramid selling schemes as purveyors of "financial products."

I ask you to please review this outline of facts and events that reveals the tragedy of the Main Street Bubble, in which millions of Americans are taken advantage of by business opportunity frauds.

Sincerely,

Robert L. FitzPatrick, Pres.
PYRAMID SCHEME ALERT

⁶⁶ <http://pyramidschemealert.org/PSAMain/news/ChinaoutlawsMLM.html>

⁶⁷ <http://pyramidschemealert.org/PSAMain/news/AmwayOnTrialinEngland.html>

⁶⁸ <http://pyramidschemealert.org/PSAMain/news/AmwayinIndia.html>

⁶⁹ <http://pyramidschemealert.org/PSAMain/news/GoldQuest-QuestNetinIndia.html>

I. The FTC's Role in Promoting and Protecting Biz Op Pyramids

1. Background and Overview

It is a sad but true fact that there is nothing new about a regulatory agency cooperating or colluding with an industry it regulates. Regulators have bent laws, loosened rules or granted favors. Experience has repeatedly revealed this kind of corruption and the consequences have also been repeatedly demonstrated. When the corrupting behavior passes certain thresholds of abuse, enormous harm follows. The SEC's lax oversight of Wall Street is the clearest example.

The FTC's collusion with business opportunity schemes between 2001 and 2009, however, is in another category. The FTC's actions since 2001 have been to *legalize* activities and business practices that the courts, the states and previous FTC policy have consistently understood to be illegal. A pyramid scheme is not "abuse" by a legitimate business, or an "excess" of a basically legal business practice, or just a violation of rules. It is a *per se* fraud, defined as an "unfair and deceptive trade practice" in the FTC Act. It is a device *constructed* to deceive and to harm. This is what the FTC's policies and action in recent years have protected.

Prior to 1980, pyramid schemes, as a major force in the market, were not widespread. When they began to appear in the mid 1960s, pyramid selling schemes were widely understood to be classic frauds and were prosecuted. In 1968, California passed its famous "endless chain" statute, which has been a model for other states.⁷⁰ The endless chain was understood to be not only a fraud for inducing "business opportunity" investment but also for illicitly driving purchases. Some states bolster anti-pyramid selling scheme laws with anti-referral discounts statutes. These laws prevent discount plans that require the customers to recruit new customers in order to gain the advertised price. In both scenarios the endless chain places the vast majority of all participants at the end of the chain where profit or discounts cannot be gained. In short, the endless chain was understood to be a menace to an open and fair marketplace, a corruption of business and a new form of swindle in the annals of capitalism.

Multi-level marketing schemes combine an endless chain pay plan with a referral-based discount. Recognizing the impossibility of its income plan, in 1975, the FTC sued to close down Amway, the first pyramid selling scheme that showed significant growth nationally. FTC attorneys saw that Amway's endless chain pay plan, by design, doomed most consumers to losses and it therefore would cause widespread harm. It followed that the promotion of the plan was inherently deceptive.

In 1980, a fundamental shift occurred in America that enabled pyramid selling frauds to proliferate and begin to spread worldwide. It occurred with the coincidence of two events:

- 1) The FTC lost its court effort to close down Amway as an *inherent* fraud. While winning on its charges that Amway fixed prices and engaged in false income claims, the FTC was unsuccessful in its effort to prove its case of a *per se* pyramid scheme. After a four-year legal

⁷⁰ § 327. "Endless chain" schemes

Every person who contrives, prepares, or operates any endless chain is guilty of a public offense, and is punishable by imprisonment in the county jail not exceeding one year or in state prison for 16 months, two, or three years.

As used in this section, an "endless chain" means any scheme for the disposal or distribution of property whereby a participant pays a valuable consideration for the chance to receive compensation for introducing one or more additional persons into participation in the scheme or for the chance to receive compensation when a person introduced by the participant introduces a new participant. Compensation, as used in this section, does not mean or include payment based upon sales made to persons who are not participants in the scheme and who are not purchasing in order to participate in the scheme.

battle, an FTC Administrative Law Judge's ruled in 1979 that Amway, under certain conditions (commissions are to be paid primarily from retail sales revenue, not from investments of new salespeople), could continue to operate.

- 2) Then, Ronald Reagan's administration took office whose official policy was "de-regulation." The oversight of MLM that was required in the Amway court outcome *was not carried out*. New staffers with a de-regulation ideology came to the agency. In the new climate of de-regulation, the MLM business quickly devolved from the retail selling of products to the calculated selling of *distributorships*. The distributorships' value depended upon an endless chain reward system. Little or no profits were gained from retail selling but from the investments of future distributorship.⁷¹

An MLM "industry" developed that operated exactly as the FTC case against Amway had tried to prevent. Under FTC de-regulation, the requirement of the 1979 decision of the Administrative Law Judge linking commissions to retail sales was ignored. Retail sales virtually disappeared. "Direct selling" became the official disguise of a newly invented and distinctly *American* business scam. Its chief protagonist was even called "American Way." Product purchases with inflated prices became the standard M.O. for laundering pyramid money transfers. Each new distributor was induced to purchase goods each month as part of the "investment." Then, 40-50% of the price was transferred to as many as 12 levels of recruiters above, with nearly all of it concentrating in the top tier. Each newly recruited "distributor" was told that he/she too could recruit an "endless chain" of levels of distributors below them. The opportunity was said to be "unlimited" and the market potential to be "infinite."

The new pyramid "business model" spread to all 50 states and expanded to 60 other countries. This was an American scam on a scale far larger than Nigeria's famous export.⁷²

Some negative media coverage about consumer losses, false income promises and the operation of obvious pyramid recruiting led the larger MLMs such as Herbalife and Amway to focus their businesses outside the USA where there were even fewer restrictions. Without the spread to new territories, the schemes would have collapsed even without regulation. The schemes have no repeat "customers". They churn through 50-80% of victims annually, replacing them with new ones. The influx of new cash from abroad continued the illusion of sustainability, thus enabling them to continue recruiting new USA residents, long after markets were saturated.

Today, more than 80% of Amway's and Herbalife's revenue comes from consumers outside the USA. The global expansion hit a major obstacle in 2005, when China banned the MLM recruitment model. Effectively, China achieved in 2005 within its borders what the FTC had sought to do for US consumers 30 years earlier – to protect its citizens from the orchestrated, well funded, and disguised "direct selling" frauds.

⁷¹ In the prepared statement on "pyramid schemes" presented at the International Monetary Fund's Seminar on Current Legal Issues Affecting Central Banks, Washington, D.C., May 13, 1998, Debra A. Valentine, General Counsel for the U.S. Federal Trade Commission stated, "Pyramid schemes now come in so many forms that they may be difficult to recognize immediately. However, they all share one overriding characteristic. They promise consumers or investors large profits based primarily on recruiting others to join their program, not based on profits from any real investment or real sale of goods to the public. Some schemes may purport to sell a product, but they often simply use the product to hide their pyramid structure... A lack of retail sales is also a red flag that a pyramid exists. Many pyramid schemes will claim that their product is selling like hot cakes. However, on closer examination, the sales occur only between people inside the pyramid structure or to new recruits joining the structure, not to consumers out in the general public." (<http://www.ftc.gov/speeches/other/dvimmf16.htm>)

⁷² For a comparison of the Nigerian scam with America's version of MLM (now banned in China) see <http://www.falseprofits.com/Americanscam.html>

In the mid-1990s through 2000, the FTC began to reassert law enforcement over pyramid selling schemes. It relied on common sense tests for recognizing endless chain schemes, federal court rulings and it cooperated with states in identifying and prosecuting them. Nearly 20 cases were prosecuted.

In these prosecutions, one fundamental factor was reconfirmed repeatedly as a criterion for identifying and defining the pyramid selling scams that masquerade as “multi-level marketing.” This was the same factor identified in the Amway case: *retail sales*.

Despite the impossible proposition of income based on endless chain recruiting, the Amway decision of 1979 had allowed the pyramid *structure* to stand. Regulation and prosecution, therefore, had to go below the structure and examine *how the MLMs operate*. The fundamental role of retail selling became a key qualifier. This approach goes to the heart of the question addressed in all pyramid and Ponzi investigations: *Where does the money for commissions come from?*

Without sustainable and profitable retail sales opportunity for the distributors, the reward money can only come from one place: *the investments of later recruits*. Without significant numbers of distributors earning profits from retail sales, the only way to be profitable in such a scheme is to engage in hopeless (for nearly all) recruiting. Only by examining this key factor, can the perverse workings of a pyramid scheme be revealed behind the façade of “direct selling.”

During the 1990’s resumption of FTC oversight and prosecutions, FTC Senior Economist, Dr. Peter Vandernat, became an internationally recognized expert in explaining and analyzing pyramid frauds disguised as multi-level marketing. He provided declarations and expert witness testimony on most FTC cases to show how a classic pyramid fraud can be dressed up as “direct selling.” He assisted state Attorneys General cases, explained the analysis to the news media and assisted consumer watchdog groups that had begun to spring up in support of FTC enforcement. His declarations and depositions have been widely quoted.

Of special importance, Dr. Vandernat developed a simple “test” for determining the legitimacy of most MLMs (the test had some limitations but was applicable in much of the MLM industry). It measured how much retail sales (outside revenue) would have to occur for an MLM to pay legitimate commissions rather than rewards for illegal pyramid recruiting. The test enabled the FTC to enforce Section 5 of the FTC Act on multi-level marketing with minimal research and discovery. Only a few key financial data points were needed to perform the test. In general, in a typical MLM pay plan, the test usually revealed that at least 70% of all purchases by MLM “distributors” would have to be resold to retail customers at full retail price in order to generate legitimate commissions.⁷³ Dr. Vandernat also co-authored the only academic paper that explains how to distinguish a legitimate MLM from a disguised pyramid scheme. In this paper, he fully presented the legal and mathematical basis for applying the “retail test” to multi-level marketing.⁷⁴

⁷³ The state of North Carolina imposed a 70% standard in four pyramid scheme cases that it prosecuted in 1999. Indicating the vast reach of MLM pyramid frauds, the four relatively small MLM companies, Club Atlanta Travel, Destiny Telecomm International, Inc., Tele-Card International, and International Heritage, Inc., had enrolled 40,000 distributors in that one state alone. The settlement agreement with Destiny Telcomm International stated: “...at least 70% of all North Carolina sales shall be retail sales to persons who are not connected in any way to the Destiny sales force.” The ruling also excluded from the 70% portion, sales to individuals who subsequently became Destiny representatives.”

A more recent application of the retail sales standard was applied by the California Attorney General. In a May, 2009 settlement with the MLM scheme, Your Travel Biz.com (YTB), the ruling requires that at least 60% of sales by YTB representatives must come from non-representatives (retail customers). The ruling also stripped YTB of much of its “pay to play” revenue in which participants paid monthly fees for “websites.” See <http://www.pyramidschemealert.org/PSAMain/news/CA.AG.YTB.Judgment.pdf>

⁷⁴ Peter J. Vandernat and William W. Keep, *Marketing Fraud: An Approach to Differentiating Multilevel Marketing from Pyramid Schemes*, 21 *Journal of Public Policy & Marketing* (Spring 2002), at 139– 151.

2. FTC Protection of Pyramid Selling Schemes

When Timothy Muris, a former attorney for Amway, was named by President George W. Bush as head of the FTC, a series of actions unfolded to roll back FTC oversight of Amway and other pyramid selling schemes and to halt prosecutions and enforcement. The shift in policy was critical for Amway, which Muris' law firm previously represented. Amway's own "SA4400" document, which it provided to new recruits, stated that less than 20% of all sales to distributors led to retail sales. Later class action lawsuits by top Amway insiders asserted that less than 4% of all Amway "sales" were ever made on a retail basis. Virtually all Amway revenue was sourced ultimately and only from the investments of the "salespeople."

Retail sales were unprofitable and unfeasible due to high prices, no consumer demand, and low retail profit margin available to the distributors. If FTC policies were maintained and Dr. Vandernat's test and analysis were applied to Amway, it would fail and would become a target of prosecution and with it many others would follow. The Main Street Bubble would burst in which hundreds of MLMs leveraged the investments of millions of consumers, who could never gain returns. The MLM house of cards was in jeopardy of imminent collapse.

1) Reassignment of FTC's Internal Expert on Pyramid Schemes

One of the first actions taken that resulted in protection of Biz Op Pyramids from future prosecutions was to move Dr. Vandernat out of the area of MLM fraud investigation and analysis. He was reassigned to an unrelated area of examining the accuracy of credit ratings. Dr. Vandernat's extensive expertise and enormously valuable experience and international reputation in pyramid scheme analysis were largely furloughed and no longer put to use on behalf of US consumers.

2) Official Policy of No More Pyramid Scheme Prosecutions

Sources inside the FTC, who must remain anonymous, have verified that Dr. Vandernat's reassignment was an early signal of an unstated but nonetheless official FTC policy in which pyramid selling schemes would no longer be prosecuted to any significant degree. In fact, this occurred. Over the next eight years, FTC prosecutions virtually stopped. One prosecution of the MLM scheme, Burnlounge, was conducted but was initiated by the state of South Carolina and arose from many complaints within the music industry (Burnlounge used an endless chain income promise to sell downloaded music and entice musicians to place their music in its library.)

The FTC imposed this virtual moratorium on MLM investigations despite increased consumer activism against multi-level marketing schemes in the United States and dramatic international prosecutions against them.

- √ Class action cases were brought against large MLMs, Amway, Herbalife, Usana, and Pre-Paid Legal, among others. All the cases made the same claim – that the MLMs are pyramid schemes in violation of Section 5 of the FTC Act and other state statutes against endless chain frauds.
- √ Another new and fast growing MLM and members of the DSA, Your Travel Biz.com, was sued by the Attorney General of California as a "gigantic pyramid scheme."
- √ The state of Texas prosecuted the MLM company, Mannatech. The Attorney General of Texas, where the scheme is based, charged that Mannatech falsely claimed that its food supplements cured Down syndrome, cystic fibrosis, cancer and other serious diseases. The company was subsequently fined \$6 million and its founder required to pay \$1

million to settle. Mannatech is a member of the Direct Selling Association and is publicly traded on the Nasdaq stock exchange.

- √ The nation of China banned the MLM payment model in 2005 as an inherent pyramid fraud.
- √ The government of England sought to close down the largest MLM, Amway, after discovering that less than 1% of all English consumers who had invested in Amway's "business opportunity" had ever earned a profit.

The FTC protection of MLMs had a wider effect also on *states*. Without FTC resources and support, state prosecutions, which had limited prosecution and investigation budgets, were cut back. Large MLMs, with significant legal defense funds, were effectively granted immunity from the FTC Act Section 5.

3) No Enforcement of Past FTC Orders against MLMs

Not only were virtually no prosecutions initiated over the last eight years, but orders from past prosecutions were not enforced. Representatives of *Pyramid Scheme Alert* met with and repeatedly notified FTC officials concerning the violations of past enforcement orders against the MLM, Nuskin.⁷⁵ This company had been fined two times for more than \$1 million each for making false claims about its products and about its claims of "income potential."

Similar consumer requests were made to reopen the Amway case in which the FTC was to enforce court rulings regarding retail sales. In 2004, *NBC Dateline* aired a documentary showing Amway distributors misleading consumers about income and the sources of the money of Amway promoters. Consumer requests to the FTC, based on the airing of that national news show, to reopen an investigation of Amway and enforce past orders were ignored.⁷⁶

4) Obscuring the Longstanding Interpretation of Section 5 of the FTC Act that a Multi-Level Marketing Scheme without Significant Retail Sales Is a *Per Se* Fraud

On January 14, 2004, James A. Kohm, Acting Director of Marketing Practices, Federal Trade Commission, wrote a highly publicized letter to Neil H. Offen, President, Direct Selling Association, that, according to many in the MLM industry and the DSA, repudiated all past FTC interpretations of Section 5 of the FTC Act and federal court rulings regarding the fundamental requirement of retail sales (external revenue source). The letter is entitled: "Staff Advisory Opinion - Pyramid Scheme Analysis."⁷⁷

This letter was cited twice by the former FTC Chairman, Timothy Muris, after he left the FTC and served as a lobbyist for an MLM company. Mr. Muris referenced the letter to support his arguments that the FTC should not impose disclosure regulations on MLM companies.⁷⁸

⁷⁵ *Pyramid Scheme Alert* sent consumer petitions to the FTC asking for enforcement of its orders against Nuskin and cited many instances of violation. The petitions were ignored. See <http://www.pyramidschemealert.org/psamain/action/nuskinpet.html>

⁷⁶ The *NBC Dateline* show can be seen in full on YouTube at <http://video.google.com/videoplay?docid=-215989802739458876&>. The formal letter from *Pyramid Scheme Alert* to the FTC asking for an investigation can be read at <http://www.pyramidschemealert.org/psamain/action/FTCCommissLtr.html>

⁷⁷ The full text of the letter can be read at <http://www.pyramidschemealert.org/PSAMain/resources/FTC.Kohm.Letter.pdf>

⁷⁸ Timothy Muris' July 17, 2006 letter to the FTC as a MLM lobbyist can be seen at

Kohm's letter has been widely circulated by MLM recruiters to persuade consumers that product purchases made by MLM distributors can count as retail sales, i.e., no external revenue is required for legitimacy. Kohm's letter refers to "fees" as the primary payment made by pyramid participants and obscures the far larger role of the product purchases. In those purchases, which are effectively required by the pay plans prices are inflated 50-250% and then 40-50% of the exorbitant price is transferred directly to the top of multiple levels of recruiters through "top-loaded" [top-weighted⁷⁹] pay formulas.

5) Colluding with Pyramid Lobbyists

While still in deliberations over rules to regulate the MLM industry, FTC officials, arguably, held at last one *ex parte* meeting with lobbyists of the MLM industry in possible violation of the Administrative Procedure Act ("APA"), 5 U.S.C.⁸⁰

Complying with the requests of the Pyramid Lobby, the FTC staff has recommended that all multi-level marketing companies be exempted from its proposed new rule that was to require more income disclosure on "business opportunity" schemes. This extraordinary recommendation reversed the earlier FTC statements about the proposed rule in which "pyramid selling schemes" were featured as a major source of "business opportunity" fraud. The Direct Selling Association (DSA) lobbied to exempt its member companies.

In the case of one DSA member, Pre-Paid Legal, an MLM that has been the target of more class action and private lawsuits for fraud than any others, the company argued that nearly 500,000 North American consumers "depended" on it for "income." In fact, 80% of Pre-Paid Legal's "salespeople" never make even one sale and only 2% make 10 sales. The mean average "income" of the salespeople is about \$5 a week. In short, the DSA presented a false claim that disclosure rules would harm rather than protect the public. The FTC staff accepted the arguments and recommended that MLMs be exempted.

6) Influence Peddling

In recent years, the FTC has experienced a pattern in which staff and even Commissioners have been able to market their roles within the FTC to multi-level marketing companies, which lobby against regulation and law enforcement, and MLM lobbyists have been brought in as FTC staff to oversee MLM.

- √ George W. Bush appointed Timothy Muris to head the FTC. Muris' last job before chairing the federal agency that regulates multi-level marketing was as an attorney with the antitrust

<http://www.ftc.gov/os/comments/businessopprule/522418-11929.pdf>

⁷⁹ Insertion by Jon Taylor, who prefers the term "top-weighted" to avoid confusion with the concept of "front-end loading."

⁸⁰ In the fall of 2008, the DSA issued a press release announcing the attendance of Lois Greisman, Associate Director of the Division of Marketing Practices at the FTC, and Lem Dowdy, FTC Attorney, to a closed DSA seminar October 23-24 in Alexandria, Va with DSA members. This was during the period of deliberations on a new rule to regulate income disclosures of MLMs. The release stated that "attendees will have the opportunity to ask questions and engage in an open dialogue with these (FTC) representatives, The general public had no opportunity for rebuttal and at the same time was not even allowed the chance to offer further comment as the comment period had ended. See http://www.dsa.org/press/press_releases/index.cfm?fuseaction=show_release&Document_id=1928

division of the firm Howrey, Simon, Arnold and White, LLP. The antitrust division of Howrey counted among its largest clients the Amway Corporation.

- √ As the new chairman of the FTC, Timothy Muris appointed David Scheffman as the FTC's new Chief Economist. Only a year earlier, Scheffman worked as an expert for the multi-level marketing company, Equinox International, a member of the Direct Selling Association that was prosecuted by the FTC for violating Section 5 of the FTC Act. David Scheffman testified against the FTC and on behalf of the scheme. Scheffman argued that the Equinox business model was legitimate, not a pyramid scheme. His claim was largely based on the assertion that Equinox operated just like Amway. The FTC ultimately succeeded in shutting down Equinox and recovering about \$50 million for consumers. However, the FTC estimated that consumer losses at the hands of Equinox exceeded \$330 million.
- √ After leaving the FTC in 2004, Timothy Muris joined the Washington DC law firm, O'Melveny & Myers. The website of O'Melveny & Myers lists Mr. Muris as "representing Primerica Financial Services... in the Federal Trade Commission's Business Opportunity Rulemaking proceeding." Primerica is a member of the Direct Selling Association and a multi-level marketing company that, like all MLMs, could be negatively affected by a new rule proposed by the FTC to regulate any business that sell a "business opportunity." A 2006 letter sent to the FTC on behalf of Primerica argued against the proposed FTC rule. The letter was signed by Timothy Muris.
- √ While head of the FTC, Timothy Muris appointed J. Howard Beales III, as Director of the Bureau of Consumer Protection. He had previously served at the Commission in the 1980s during the "de-regulation" era. After leaving the FTC, Beales co-signed the letter to the FTC with Timothy Muris on behalf of the MLM, Primerica, that argued against regulation of multi-level marketing. Howard Beales was also known for his consulting work for Reynolds Tobacco and his public defense of the Joe Camel advertising campaign.
- √ Jodie Bernstein after serving as Director of Consumer Protection at the FTC from 1997 to 2002 joined the law firm, Bryan Cave. In that capacity she lobbied the FTC on behalf of the MLM, the Amway Corporation, arguing against regulation.

The law firm, Bryan Cave, has considerable experience in representing companies accused of operating as pyramid schemes. It defended the notorious Ponzi operator Reed Slatkin and previously represented Michael C. Cooper, president and chief executive officer of the MLM company, Renaissance the Tax People, which was shut down by the state of Kansas as a pyramid scheme.⁸¹

⁸¹ The firm of Bryan Cave, which lobbies for and represents Amway, also counts among its newer attorneys:

- Frank Gorman, formerly legal advisor to the director of the Federal Trade Commission's Bureau of Consumer Protection. Gorman left the FTC and joined the firm in 2003 when Ms. Bernstein also came over from the FTC and began lobbying for Amway.
- Dana Rosenfeld, who served as the assistant director of the Federal Trade Commission's Bureau of Consumer Protection and was senior legal advisor to Jodie Bernstein.

II. The Political Influence of the Pyramid Lobby

This memorandum cannot conclude without addressing the question of *why* the FTC reversed policy and protected companies that violate Section 5 of the FTC Act. The answer is plainly *political*. Influence was purchased.

While many people are somewhat aware of large lobbying forces in Washington such as Tobacco, Guns and Pharmaceuticals, few are aware of the powerful political influence of the MLM industry which constitutes a Pyramid Lobby. Like the stealth marketing of MLM companies, which is mostly carried out without national media, the Pyramid Lobby's work is similarly low profile. This is partly due to its extraordinary purpose. MLM's top priority is not just to curry favoritism or receive income at the public trough, but to *prevent its extinction*. This requires *thwarting law enforcement and foiling consumer protection*. Only the tobacco industry has as much at stake in its political lobbying and its public marketing campaign.

Much of the influence is carried out at the state level where legislatures and state Attorneys General are lobbied to change or not enforce clearly worded statutes that ban business opportunity frauds and endless chain schemes. One notable example is the state of Utah, which has more MLM headquarters per capita than any other state. MLM brings more money into that state than its famed skiing industry. While Utah has no lottery, it is the beneficiary of an industry based on endless chain speculating. *The actual odds of winning are significantly better at a Las Vegas craps table than joining at the end of an MLM recruitment chain.*⁸² The Attorney General of Utah, Mark Shurtleff, recently supported a "safe haven" amendment (SB 182) to Utah's anti-fraud law that exempts multi-level marketing schemes. Shurtleff's largest political contributors are MLM companies. He has been a featured speaker at MLM meetings, giving every appearance of commercial endorsement.

But it is on the *national* level where the FTC is directly influenced. Here, the Pyramid Lobby has focused virtually all its resources on the National Republican Party. Democrats are largely absent from lists of recipients of MLM money.

In 2003, the Pyramid Lobby made its boldest and most overt move. It sought a national law that would protect the industry, once and for all, from FTC and state law enforcement. A bill was written by the Direct Selling Association and introduced in the House by Texas Republican, Joe Barton. The bill, HR1220,⁸³ would have exempted endless chain schemes in which the money transfer was laundered with product purchases. HR1220 was essentially a replica of the bill that Utah adopted with Attorney General Shurtleff's endorsement, as have several other states, such as Texas, where the DSA has held sway.

Co-sponsors of HR1220 were all Republicans, including Congresswoman Sue Myrick of Charlotte, NC, whose main campaign funds were raised by Amway's largest distributor, Dexter Yager who is based in the Charlotte area. Myrick was herself an Amway distributor. Other co-sponsors included Vernon J. Ehlers of Michigan (from Amway's home district with Amway as 2nd largest campaign contributor in 2006) and three Republican Congressional representatives from Texas, among others.

A brief overview of the political activities, influence-buying and financial contributions of the MLM industry, led by its largest member, the Amway Corporation, readily answers the question

⁸² <http://www.mlm-thetruth.com/ShockingMLMstats.htm>

⁸³ Full details about HR1220 can be found at http://pyramidschemealert.org/PSAMain/news/DSABill/DSAbill_analysis.html - Behind DSA

of why the FTC, under President Bush's appointee, Timothy Muris, undertook a policy of protecting illegal business practices. The answer is plain and simple. Protection of business opportunity frauds was *purchased*.

- According to the consumer watchdog group Common Cause, Amway and affiliated donors made soft money contributions to the Republican National Committee totaling \$4,147,000 between January 1, 1991 and June 30, 1997. In April 1997, the co-founder of Amway Corp. gave \$1 million to the Republican Party, one of the largest single donations on record from an individual. Federal Election Commission records show that Richard DeVos, said to be worth \$3.2 billion, and his wife, Helen, wrote two \$500,000 checks on April 2, 1997 from their personal accounts. DeVos is the former finance chairman of the Republican National Committee.
- In 2000, Amway "soft money" contributions to the Republican National Party totaled \$1,138,500. A publication of the Brookings Institute lists Amway among the top ten "soft money" contributors to the Republican Party in 2000, just below and – only \$500 less than – Enron.⁸⁴
- In 2004, the 527 "Progress for America" received major contributions from Amway. "The latest crop of donors includes Amway founders Richard DeVos and Jay Van Andel, who each chipped in \$2 million." (*Newsweek*, "The Secret Money War," September 20, 2004.) This 527 subsequently poured \$28.8 million into supporting George W. Bush in 2004.⁸⁵
- Dick DeVos, the son of the founder of Amway is married to Betsy Prince, sister of Erik Prince, the founder of the politically powerful military contracting firm of Blackwater (recently renamed Xe). The Prince/DeVos marriage, which links Blackwater and Amway, both based in Michigan, created what has been called the most politically influential family in the Republican Party. Erik Prince has been a steady contributor to the Republican National Committee.
- In 2006, Dick DeVos ran unsuccessfully for the governorship of Michigan. Had he won, some analysts speculated he would have been a viable candidate for President.
- The above referenced wife of Dick Devos (sister of Erik Prince), Betsy DeVos, served as chair of the Michigan Republican Party. In 2000 she won special status as a so-called "Pioneer" after raising \$100,000 for the Bush/Cheney campaign.
- In 1999, the inaugural fundraising event for the Republican Majority Issues Committee (RMIC) was held aboard the DeVos family yacht. The RMIC, a "527" organization, was founded by Rep. Tom DeLay (R-Texas). The committee declared its intention to "identify, educate, and mobilize conservative voters in key House races."
(http://www.motherjones.com/news/special_reports/mojo_400/12_devos.html)
- Describing the events at the 2000 Republican Convention in Philadelphia, the *New York Times* wrote, "For the party's top underwriters, there will be an array of gold-plated events in Philadelphia, including cocktails with Gen. Colin L. Powell and an evening cruise on the Delaware River aboard the 'Enterprise,' the yacht owned by Richard M. DeVos, the Amway founder.
- In the 2000 national election, the George W. Bush campaign used Amway's voicemail network to broadcast its message to tens of thousands of Amway/Quixtar distributors with a "personal voicemail message" from Mr. Bush.

⁸⁴ <http://www.brookings.edu/gs/cf/Financing2000/ch06.pdf>

⁸⁵ http://www.sourcewatch.org/index.php?title=Progress_for_America_Voter_Fund

- For large speaking fees, former Presidents George Bush, Ronald Reagan, Gerald Ford and former Vice Presidents Bob Dole and Dan Quayle have spoken at Amway-related functions, as have former Republican heavyweights Newt Gingrich, Oliver North, and the SE Regional Chairman for Bush-Cheney '04, Ralph Reed, among others.
- Regarding Amway's formidable political lobbying power in Congress, syndicated columnist Molly Ivins wrote in 1997, "Amway has its own caucus in Congress. Yes, the Amway caucus. Five Republican House members are also Amway distributors: Reps. Sue Myrick of North Carolina, Jon Christensen of Nebraska, Dick Chrysler of Michigan, Richard Rombo of California and John Ensign of Nevada. Their informal caucus meets several times a year with Amway bigwigs to discuss policy matters affecting the company, including China's trade status." (Amway lobbied to get the US Dept. of Commerce to back its efforts to get China to legalize the Amway pyramid pay plan. In 2005, this effort failed as China banned MLMs.) Ivins also noted, "House Majority Whip Tom DeLay, a onetime Amway salesman, also remains close to the company."
- Sen. Rick Santorum of Pennsylvania was a favored speaker at large meetings held by Amway "kingpin" Fred Harteis, and received financial support from the Harteis family, their recruits, and other Amway kingpins.
- A close personal friend and "spiritual advisor" to George W. Bush is a former high ranking (Diamond) distributor with Amway and regular Amway convention speaker, evangelist Doug Wead. Wead was President George H.W. Bush's liaison to the Christian Right. During the early 1988 George Bush presidential campaign, Wead reported to son, George W. Bush. He later served as Special Assistant to the President in the Bush Senior, White House. *Time* magazine referred to him as "the man who coined the phrase the compassionate conservative." The phrase, "compassionate conservative" is closely related to a Rich DeVos book title, "Compassionate Capitalism." Wead also researched and wrote about the children of presidents, at the request of George W. Bush.
- At the 2004 Republican National Convention in New York insiders were feted aboard Dick and Betsy DeVos' yacht, as well as Jay Van Andel's lavish 169-footer." (Kathleen Gray, *Detroit Free Press*, 9/2/04)
- In a 1997 article, nationally syndicated columnist, Molly Ivins, reported that the budget package passed by Congress that year provided a tax break "worth \$283 million to one corporation: Amway."

Ivins noted, "The company and its top leaders have contributed at least \$4 million to the Republican Party during the past four years, so that's a \$4 million investment in campaign contributions with a \$283 million payoff for Amway."

"The payoff for Amway was not in the original House or the Senate version of the tax bill," she wrote. "House Speaker Newt Gingrich intervened at the last minute to help get the special tax break inserted in the bill."
- Describing this special tax break, Common Cause reported: "Buried in the 1997 budget and tax deal is Provision C, Section XI. The provision... reads: 'Modification of passive foreign investment company provisions to eliminate overlap with subpart F and to allow market-to-market election, and to modify asset measurement rule.' In other words... the provision primarily benefits Amway Corp. and could be worth millions of dollars to (Amway)."

III. Conclusion:

Business Opportunity Scams, the Cruellest of Frauds

Today, millions lose their jobs; life savings are wiped out in the 401K meltdown; and many suffer the disaster of home foreclosure. The government pours in money for “stimulus” and “rescue.” Legitimate businesses reorganize; citizens struggle to survive.

In this climate, the “product” in most demand – and in least supply – is an *income opportunity*. This is what more than 10 million Americans and many more worldwide think they are buying *each year* when they invest in a multi-level marketing business opportunity scheme. The “opportunity” that is offered is, in fact, to sell the opportunity to someone else, a classic Ponzi. Unwittingly, the consumer investors have been lured into the Main Street Bubble. Their investments in fees and inventory were worthless or absurdly inflated in price. Collapse for the *new investors, one at a time*, is inevitable as they each “fail” to recruit enough new investors.

The cruelty of the fraud extends beyond causing a financial loss. The schemes induce the victims to spread the loss to their very own friends and relatives. Social and personal harm may exceed the financial losses.

In violation of Section 5 of the FTC Act, business opportunity frauds have an enormous, corrupting influence on the marketplace. They promote a predatory and deceptive reward system in which one person’s gain is based on many others’ losses. They incorporate deception into the model to conceal the inevitable fate of those solicited to join.

The scale on which MLMs promote and teach these predatory practices cannot be understated. To take the example of only two of the hundreds of multi-level marketing schemes, as many as 10 million Americans have become Amway distributors over the last 20 years; 1.6 million Americans have signed up as sales representatives of the MLM, Pre-Paid Legal (NYSE:PPD). Virtually all of these investors quit these schemes after suffering losses. There are hundreds of smaller versions of these two. There are very few families that have not been hit.

Each recruit is subjected to a powerful “message machine” in which gainful employment, corporate America, and legitimate careers or businesses are derided, Government regulation is portrayed as dictatorial and safety net services are reviled as socialism while the MLM pyramid plans are presented as a last refuge for the average person. Covering up and diverting attention from the massive consumer loss rates, the schemes’ leaders indict the “failures” as quitters, “pathetic losers” or as consumers who (despite their quitting the scheme within a year and never buying the goods again) joined only out of love of the high priced products, not to earn an income.

Multi-level marketing is an Enron waiting to be exposed. Like Enron it claims to be the “business model of the future”, hides its actual operations from the public and regulators and globally generates funds illegitimately, using some of that money to buy protection from regulation or oversight.

Unless Congress intercedes and restores the FTC to its lawful duty of enforcing Section 5 of the FTC Act against frauds of this type, they will continue to multiply, harm millions more consumers each year and further strengthen their hold on the marketplace.