HERBALIFE: WHAT SHORT SELLERS MISSED ON THE WAY TO THE PRESS CONFERENCE…

The Personal Use Issue in Pyramid Analysis

Who is an Ultimate User?

By Jeffrey Babener © 2013

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Déjà vu, all over again … Yogi Berra

History repeats itself.

The 2012 billion dollar short seller attack on Herbalife, a 32 year old NYSE listed direct seller of nutritional products in 80 plus countries with annual sales in excess of $3 billion, is akin to a replay of seminal challenge to the MLM/Direct Selling model, won by Amway in 1979. In the Matter of Amway, 93 F.T.C. 618 (1979).

In the 1970's FTC challenge, the criticism went to whether or not the core of the MLM referral selling model was a "deceptive" way to market. In the 2012 short seller attack, along with other criticisms, a principal complaint is that evidence of "substantial personal use and consumption" of company products by distributors themselves, renders an MLM/Direct Selling model inherently deceptive and an illegal pyramid scheme. **Armed with multi-hour slide presentations, short sellers and financial bloggers predicted that a direct selling program, in which substantial product is purchased by distributors for personal use, is doomed to collapse as an illegal pyramid scheme; and that federal agencies should step in to hasten that demise. Is this legal analysis correct and is the call to federal action justified or predictable in light of the 40-year legal history of direct selling?**

Does the answer lie in the follow-up and prolific financial blogging that focuses on algorithms, multiple regression analysis and economist "speak" about "who uses the product?" **Perhaps not.** Rather, the answer as to whether or not an MLM/Direct Selling program is a pyramid, for which federal prosecution is justified and predicted, may be driven by a case by case fact scenario that answers a "gut instinct," as noted by Justice Potter Stewart (on pornography) … **I can't define it, but I know it when I see it.** In the case of direct selling, the operative question appears to be: Is this program an "inherently deceptive" and an "egregious abuse" of consumers and is the driving force behind payment of money for products the desire to qualify in an MLM plan, i.e., **are distributor purchases and payments incidental to the business opportunity or are payments made merely as a "gateway" to a business opportunity? … as opposed to the question of the amount of internal consumption or personal use by distributors, even**

if it is incentivized by a compensation plan. And do today's established multi-direct sellers deserve to be placed in the same gene pool as companies that have been the target of federal prosecutions?

Memo to short sellers and algorithmic financial bloggers:

It may be time to reassess.

Some very salient facts and cases may well have been missed in the rush to challenge direct sellers.

1. A survey of FTC, SEC and Justice Department leading pyramid cases during the last two decades is instructive. Interestingly, in massive releases of the Herbalife short seller and the prolific financial blogging "call to action" that Herbalife is a pyramid that should and will be prosecuted by the FTC, NO ONE has bothered to actually examine the facts of leading FTC, SEC and Justice Department pyramid prosecutions of the last two decades … if they had done so, they might observe a significant chasm that exists between inherently deceptive and egregiously abusive pyramid schemes and the practices of leading direct selling companies.

2. They also may have missed the FTC's own statements on personal use, as well as the trending legislation **in more than a dozen states**, recognizing the validity of personal use as a legitimate end destination of product.

Some Background

The MLM/Direct Selling/Network Marketing business model was off to a robust start in the 1950's with the success of Amway, Mary Kay and Shaklee. Not long thereafter, imposters and inherently deceptive pyramid headhunting recruitment schemes came along, emphasizing recruitment of participants to pay money and find others to do the same.

Two promotions founded by Glenn W. Turner, Dare to Be Great (motivational seminars and materials) and Koscot Interplanetary (cosmetics), prompted major prosecutions for pyramiding. Virtually every state had residents who were impacted by this and other programs which officials successfully argued were mere "headhunting" schemes.

The FTC established the earliest guidelines regulating illegal pyramids and other unlawful entrepreneurial chains: In *In Re Koscot Interplanetary Inc.*, 86 F.T.C. 11106 (1975) (inventory loading of cosmetics), the FTC was highly critical of:

1. Large membership fees,

2. Front-end loading and inventory loading,

3. Programs in which distributors were misled as to the amount of commissions they might reasonably earn, and

4. Programs in which commissions were not based on the sale of product to the ultimate users.

In fact, the *Koscot* case established the legal standard, for pyramid analysis, that has threaded its way intact from the 1975 *FTC Koscot* case to the 1979 *FTC Amway* case to the 2012 *FTC BurnLounge* case (*FTC v. BurnLounge*, U.S. District Court, Central District California, Case CV 07- 3654-GW(FMOx) (2012): ***Are there rewards earned unrelated to sale of product to ultimate users?*** *[At the core of short seller accusation is that purchases for personal use by distributors (internal consumption) cannot be considered to be a sale to an ultimate user … a standard, if adopted, which would cast a cloud over many well-established direct selling companies, particularly those that sell consumable products such as health, home and personal care.]*

The Securities and Exchange Commission (SEC) also stepped into the Dare To Be Great picture, demonstrating that securities statutes also apply to the industry. In *SEC v. Glenn W. Turner Enterprises*, 474 F.2d 476 (1973), the U.S. Ninth Circuit Court of Appeals reaffirmed that the securities acts were "designed to protect the American public from speculative or fraudulent schemes of promoters. Like other pyramid schemes, the only "commodity" that moved through this program was money. There were no viable goods or services, sold at fair market value, accompanying the recruiting activities. Basically, individuals were invited to pay money to attend motivational seminars where they were trained to go find others to do the same, and so on. The Dare To Be Great program was ruled to be an "investment contract" under the securities laws and thus subject to regulation by the SEC. This was a landmark ruling in establishing the distinction between "speculative or fraudulent schemes" and legitimate direct sales activities. It also helped establish the SEC's role in upholding the rights of legally operating companies and the right to prosecute offenders.

The *Koscot, Dare To Be Great*, and other pyramid cases left a sour taste in the mouth of the American public. And so, the legitimate MLM industry had a close call in the 1970's when the FTC accused Amway of being an illegal pyramid scheme rather than a legitimate business opportunity. Fortunately for Amway and the industry, a 1979 administrative law decision declared the Amway MLM business model to be legitimate and applauded various consumer safeguards, including buy-back policy for unsold inventory, curbs on inventory loading and stress on moving product to the ultimate user. *In the Matter of Amway*, 93 F.T.C. 618 (1979).

And so it went for the next 40 years and to this day. Federal agencies, such as the FTC or SEC or the U.S. Justice Department, did not chase after well-established MLM firms, but rather they sought out inherently deceptive schemes that defrauded the consumer of business opportunities. Hard hit were offerings with large upfront investments of cash or inventory loading, nonrefundable fees, bogus products used as an excuse to move money, etc.

Time Travel 40 years to 2012 Hedge Fund Battles

A man hears what he wants to hear and disregards the rest … Simon and Garfunkel

And now, flash forward 40 years and the attack on the Direct Selling model is launched against leading companies in a mature direct selling industry with worldwide sales in excess of $150 billion in more than 100 countries, an industry led by the likes of publicly traded NYSE companies such as Herbalife, NuSkin, Avon, USANA, Primerica and Tupperware, as well as decades old venerable brands such as Mary Kay, Shaklee and Amway.

The attack comes, not from federal agencies, but from short sellers who stand to gain billions from precipitous drops in stock prices. In one such publicized attack, a billion dollar short bet was made on Herbalife in December 2012. In a dramatic public presentation, the 32 year old company was labeled a "well run" pyramid scheme, destined to fail and whose stock should be valued at zero. The public accusation took its toll and set off gyrations in the stock market as to direct seller stocks, ultimately resulting in a battle of hedge funds that bet "short" or bet "long." This play is destined to go on for some time to come.

And so, what may be a possible strategy of a short seller in this situation. To borrow a war time analogy, the best strategy may be "shock and awe." Hold a public conference and announce that Company A is a "pyramid scheme" destined for collapse. Inspire the financial press and blogs to pile on. Hope that the accusations will undermine public confidence in products and the opportunity and that fleeing distributors will result in a self-fulfilling prophecy of collapse. If this doesn't work, urge a federal agency such as the FTC to prosecute the company, again to usher in a self-fulfilling prophecy. If that doesn't work, urge the federal government to pass legislation to negatively impact the business model. If that doesn't work, continue to attack the company and inspire more financial press and blog debate.

And the ensuing result ... is it to look out for the average "Joe" investor and low income participants of sinister direct selling companies; or conversely, is it to create substantial profits for Wall Street hedge funds? Whatever the answer, one thing is agreed upon by financial pundits: when the pros are playing, the tumultuous gyrations in the stock market are not for the faint of heart.

Says Jeremy Phillips and Austin Smith of the **Motley Fool**:

> *I'll say this is the worst way to invest and what we've seen happen the last few years is that there has been this drama and this sort of sensationalism that's been brought to investing. You see hedge funds literally going public and rolling out 300 slide decks … in the sort of obvious intention of trying to move the market with their news instead of being quiet about their short. So, what you see is … you see a lot of drama unfolding that's getting people's interest, but it, in no way, is associated with the fundamentals of investing. … It's all drama. It's people getting interested in this and we see these hedge-funders who have so much money and so much ego on the line that it becomes a game. It's a market manipulation thing, right?*

(March 17, 2013) http://www.dailyfinance.com/2013/03/17/these-billionaires-are-destroying-the-stock-market/

The "I know it when I see it" Pyramid Spectrum

Toward one end: *Established direct selling companies that offer financial incentives for personal use, product promotion and sales force expansion. In such programs, the primary revenue source and primary funding source for commissions derive, not from upfront purchases, but from ongoing and deliberate* *sales of products and/or services to outside customers or, in reasonable amounts, to distributors for personal or family use.*

At the other end: *Inherently deceptive egregiously abusive schemes where recruits are urged to pay money or purchase product as a "gateway" to qualify for rewards in a business opportunity … where payments are incidental to the business opportunity … and where schemes are often characterized by upfront investments for inventory, training, administrative services or bogus products to "buy in" to the opportunity for rewards. In such programs, the primary revenue source and primary funding source for commissions are the gateway purchases upon entry to the opportunity.*

The Practices of Established Direct Sellers…

Should decades old direct selling companies be re-confronted by federal regulatory agencies such as the FTC, SEC or U.S. Justice Department? After all, they clearly offer a financial incentive to consumers to use their products and services and to recommend those products and services to their neighbors.

However, have not financial incentives been one arrow in the quiver of the shaping of consumer spending behavior forever? Witness: all frequent flyer programs; credit card reward programs; cash back loyalty programs; and every loyalty and referral program from every mom and pop diner and donut shop in America. Also witness Fortune 500 companies embracing their customers as referrers who receive rewards for finding other customers: MCI Friends and Family; United Airlines Mileage Program that rewards members for referrals; American Express Referral Membership Rewards; and Amazon.com Affiliate Rewards, etc.

In fact, the direct selling industry merely takes the referral rewards program one step further. Often pitching the positive experience of customers, companies offer a 1099 independent contractor business opportunity to those motivated to refer friends, family, co-workers and neighbors to patronize products that they themselves typically have used and enjoyed. The result: in the U.S. a $30 billion industry with more than 15 million individuals involved and worldwide a $150 billion dollar industry with 90 million individuals involved.

And, along the way, over the last 50 years, the direct selling model has produced many multi-billion dollar companies, with household names, operating in more than 100 countries, with publicly traded NYSE leaders such as Avon, Herbalife, Primerica, USANA, NuSkin and Tupperware, etc.

Such companies, including the "short sale" target, Herbalife, populate the 100 year old Direct Selling Association, an organization that demands adherence to a longstanding Code of Ethics, http://www.dsa.org/ethics/code/, that among other things:

1. Prohibits deceptive behavior in recruiting and selling;
2. Mandates a 90% 12-month inventory and sales aids refund to terminating distributors;
3. Prohibits unsubstantiated earnings claims; and

4. Prohibits "inventory loading" or purchases of inventory in other than reasonably commercial quantities.

And virtually all of these well-established companies mandate as the only cost to become a distributor, the purchase of a modestly priced "at cost" refundable sales kit … typically $50-$100.

Of course, these companies can't guarantee success and it is widely recognized that, for most direct sellers, buying at discount may be the primary reward. Such companies are not bashful about providing extremely detailed disclosures of earnings histories of their distributors. And by and large, "disclosure" is the primary expectation of a U.S. federal agency such as the FTC. The FTC does not mandate earnings success; but it does mandate earnings disclosure if a company references earnings or income potentials. After all, these programs are entrepreneur programs, not entitlement programs … and "entrepreneur" is the French word for "risk taker." For its part, the FTC, in a 2004 statement on direct selling lauded the benefits of "buyers clubs" with "multi-level rewards" as a legitimate business model. *(See detailed discussion below.)*

And, notwithstanding the fondest dream of short sellers of NYSE direct selling companies to drive down stock prices by allegations of pyramid, the odds are diminished by the fact that, **since the landmark approval of the multilevel marketing model in the 1979 seminal administrative law decision, In the matter of Amway, no federal prosecutions have been aimed at multi-decade established direct sellers.** In fact, attend a legal day symposium at the Direct Selling Association, and one is likely to find a representative of the FTC praising the work of the DSA and the contributions of member companies to the American economy and U.S. business expansion abroad. On behalf of these established companies, the DSA is in continuing contact and consultation with the FTC. In fact, when China sought membership to the World Trade Organization, it was the U.S. government, at the request of leading direct sellers (who now boast billions of dollars of sales in China), to condition admission on a gradual legalization of direct selling activity in China.

The Other End of "I know it when I see it" Spectrum: Inherently Deceptive Schemes

What the short sellers and financial bloggers missed...

And so, in urging federal prosecution of Herbalife and similar direct sellers, what have such proponents, along with their financial blogger surrogates and self-described MLM experts (many of whom have carved out a cottage expert witness industry with anti-MLM websites and frequent court and legislative appearances) missed in their condemnatory conclusion that a direct selling company occasioned by substantial distributor personal is afortiori a pyramid scheme, doomed to failure and destined for federal prosecution?

What did they miss? … They failed to look at the reality of federal prosecutions over the last two decades. If they had bothered to spend some time, they might see that such prosecutions, by the FTC, SEC and U.S. Justice Department, were aimed at what federal regulators believed to be inherently

deceptive pyramid schemes and egregiously abusive programs that fit the "I know it when I see it" analysis.

So, for the sake of edifying the conversation, below are the leading federal prosecutions over the last two decades, all of which regulators alleged some **inherently deceptive component(s)** that differentiates the prosecuted companies from long time established direct selling companies:

ZeekRewards (2012). *SEC vs. Rex Venture Group, LLC, dba ZeekRewards.com, et al.*, U.S. District Court, Western District, North Carolina, Civil Action 3:12 CV 519 (2012). The SEC shut down a program that enticed $600 million from two million individuals worldwide. Assets were seized and a Receiver appointed to consolidate assets, pursue claims and make distributions to victims. Said critics, the veneer of a penny auction promotion attracted participants, but the real money to be made was paying large cash sums for "bid credits" and recruiting others to do the same.

Gold Unlimited (1996). *U.S. v. Gold Unlimited, Inc.*, U.S. District Court, Western District of Kentucky, No. 95-00013 (1996), Appellate Case, U.S. Court of Appeals, Sixth Circuit, 177 F.3rd 472 (1999). The U.S. Justice Department, U.S. Attorney for the Western District of Kentucky, criminally prosecuted a purported MLM in which participants made down payments on gold contracts, recruited others to do the same and received commissions on down payments of recruits. Funds were often plowed into further down payments without gold necessarily being delivered. The individual owner promoters were each sentenced to more than 10 years.

International Loan Network (1991). *SEC v. International Loan Network,* U.S. District Court, District of Columbia, Civ. No. 91-1102, 770 F.Supp.678 (1991). The SEC shuttered International Loan Network. International Loan Network provided financial products that advertised significant returns. Prospective members would buy into one of the plans with a membership fee, payable to the company, and an investment, which would be apportioned, to the company and the prospective member's sponsoring member. The court concluded that ILN sold "investment contracts" within the meaning of federal securities laws because the efforts of others in recruiting new members was undeniably significant in the success of the group.

Equinox (2000). *FTC v Equinox International Corp.*, U.S. District Court, District of Nevada, Case CV-S-99-0969-JBR-RLH (2000). The FTC successfully shut down Equinox, an MLM marketer of health-related products. Among the principal accusations: (1) Prospective recruits were lured by advertising for promises of job or employment interviews, which turned out to be opportunity pitches. (2) New recruits were front-loaded with thousands of dollars of inventory purchases by being encouraged to "buy-in" at the managerial level to qualify for higher commissions.

BurnLounge (2012). *FTC v. BurnLounge*, U.S. District Court, Central District California, Case CV 07- 3654-GW(FMOx) (2012) (appeal pending). The FTC successfully shut down the company. BurnLounge was envisioned as a seller of music through on-line digital music stores of participants. Distributors purchased web packages to facilitate downloads of music and recruited others to do the same. Commissions were paid on the web package purchases. The court found that the overwhelming income and commissions came from the sale of web packages (which the court found to be tools) rather than from sale of products, i.e., downloaded music to consumers, and that the upfront purchases were incidental to the business opportunity.

Bigsmart (2001). *FTC v. Bigsmart.com L.L.C., et al*., U.S. District Court, District of Arizona, Civil Action No. CIV01 0466 PHX ROS (2001). The FTC successfully enjoined Bigsmart practices. The business model for Bigsmart was somewhat different than other MLM web malls that were accused of frontloading multiple websites on distributors and paying commissions based upon purchase of multiple websites. In the Bigsmart model, the FTC accused Bigsmart of encouraging distributors to purchase multiple websites and qualify those website "shopping malls" by purchasing overpriced products of questionable value and price, which were accorded high points in the qualification system, as opposed to purchases of well-known third party vendors that were accorded very low point value in the system. They were then entitled to receive commissions on similar purchases of downline mall operators that they recruited.

Trek Alliance (2005). *FTC v. Trek Alliance, Inc.*, U.S. District Court, Central District California, Case CV-02-9270 DSF (AJWx) (2005). Widely criticized by industry observers as a "thin" FTC action, the FTC linked practices of Trek, a marketer of water filtration, home care and nutritional products, to those criticized in the earlier FTC v. Equinox case. The FTC alleged that Trek distributors ran classified ads in the "Help Wanted" sections of newspapers that implied that they were offering salaried positions. According to the FTC, people who responded to the ads were instead given a sales presentation designed to recruit new distributors. The FTC alleged that Trek told recruits that they could earn money by selling products or recruiting, but emphasized that more money could be made through recruiting. The recruits were expected to attend training seminars around the country, purchase hundreds of dollars worth of products so they could enter the program at a higher level, rent desk space in regional offices, and subscribe to phone lines so they could begin recruiting others, all at their own expense. The FTC contended that the company promised monthly incomes ranging from $2,000 to $20,000, and the FTC complaint alleged that the vast majority of consumers made less money than they had paid for front-end expenses, and that many made little or nothing.

SkyBiz (2003). *FTC v. SkyBiz.com, Inc.*, U.S. District Court, Northern District Oklahoma, Case 01CV0396K(E) (2003). The FTC shut down SkyBiz, charging it as an operation that purported to sell online tutorials on web-based products, but was actually a massive illegal pyramid scheme which bilked consumers in 200 countries around the world of approximately $175,000,000. Participants bought the web tutorial packages and then recruited others to do the same. The cost to join the SkyBiz Program was $125, ostensibly used to buy an "e-Commerce Web Pak," but in reality was to purchase the right to receive compensation for recruiting additional participants. Participants were urged to invest in more than one "Web Pak," to maximize their earning potential and to recruit others to do the same.

FutureNet (1998). *FTC v. FutureNet, Inc., et al.*, U.S. District Court, Central District of California, Civil No. 98-1113 GHK (BQRx) (1998). The FTC halted an operation by which consumers paid up to $700 plus for packages to be internet consultants with the idea that they would make money on sales to consumers of products and services. In fact, the money to be made and upon which commissions were paid was for payments by participants to be internet consultants and recruiting others to do the same.

Fortuna Alliance (1996). *FTC v. Fortuna Alliance, L.L.C., et al.*, U.S. District Court, Western District of Washington; Civil Action No. C96-799M (1996). The FTC shut down Fortuna Alliance. The FTC charged that Fortuna Alliance marketed the pyramid scheme through a home page on the World Wide Web and with printed promotional materials. Using extraordinary earnings claims, they induced tens of thousands of consumers in over 60 countries around the world to pay between $250 and $1,750 to join their pyramid scheme, claiming that members would receive over $5,000 per month in "profits" as others were induced to "enroll" and so on.

2Extreme (2001). *FTC v. 2Extreme, et al.*, U. S. District Court, Northern District of Maryland, Civil No. JFM99CV3679 (2001). The FTC shut down an operator that sold nutritional products, but which opportunity was overlaid with required commission qualifying purchases of up to $1,300 in training materials, sales of $3,000 in day trading computer software, up to $7,300 in computer equipment and the sale of pre-filled distributor positions for up to $5,000 and "business in a box" tools and lead recruiting systems for up to $4,000. Distributors were then encouraged to find others to do the same.

Five Star Auto Club (2000). *FTC v. Five Star Auto Club, Inc., et al.*, U.S. District Court, Southern District of New York, Civil Action No. CIV.99-1693 (McMahon) (2000). The FTC shut down a program that promised participants auto lease and cash awards if they purchased auto club memberships of up to a $395 annual fee and $100 per month, and then recruited other members to do the same and so on.

World Class Network (1997). *FTC v World Class Network, Inc.*, U.S. District Court, Civil No. SACV-97-162 AHS EEx (1997). The FTC shut down World Class Network after alleging that the defendants offered a travel tutorial kit that purportedly would allow purchasers to receive the professional courtesy discounts and upgrades traditionally available to travel agents on their own travel accommodations, and to operate and achieve specified earnings in an at-home travel business. Distributors also could receive commissions by recruiting new distributors and reselling the tutorial to these recruits. In fact, the FTC charged, purchasers could not obtain the promised discounts and upgrades for personal travel because many travel industry service providers did not recognize World Class Network's proprietary I.D. and the travel tutorials were inadequate to allow purchasers to open and operate a functioning business.

Mall Ventures, 2x2.net (2005). *FTC v. Mall Ventures, Inc., d/b/a 2by2.net, et al.*, U.S. District Court, Central District of California, Civil Action No. 04-cv-0463 (2005). The FTC shut down Mall Ventures, 2x2.net. The FTC charged that the company recruited investors into their pyramid as "eCommerce Consultants" for $300 to $420 per spot. According to the FTC's complaint, the defendants touted 2by2.net as a lucrative business opportunity in which consumers could earn over $1,000 per month if they were just "1% successful," and up to $117,000 per month after five years of effort. Many consumers were persuaded to pay up to $2,940 for multiple spots and to spend thousands of dollars more in their attempts to make money through 2by2.net. Internet malls contained links to retail websites maintained by third-party merchants. The FTC alleged that 2by2.net falsely represented to its eCommerce Consultants that they could make substantial commissions on purchases made through these 2by2.net Internet malls, as well as by selling Internet access, vitamins, and prepaid long distance telephone cards. The FTC charged in its complaint, the few eCommerce Consultants who made money through 2by2.net did so by recruiting others into the program, and the vast majority of eCommerce Consultants made very little or no money, regardless of the effort expended.

AdSurf Daily (2012). *U.S. v Thomas Anderson Bowdoin, Jr.*, U.S. District Court, District of Columbia, CR 10-320 (2012). U.S. Justice Department, U.S. Attorney for District of Columbia succeeded in the criminal prosecution. ASD's business model promised members the opportunity to earn 125 percent (initially 150 percent) on each dollar paid into ASD, as long as the members viewed other members' websites for a few minutes each day on ASD's Internet page, commonly referred to as the ASD "rotator." ASD also promised members commissions for recruiting other members into the program. In addition, the civil forfeiture was $80 million.

NexGen3000 (2003). *FTC v. NexGen3000, et al*., U.S. District Court, District of Arizona, Case CIV 03 120TUCWDB (2003). The FTC shut down this MLM mall operator. The FTC alleged that NexGen marketed Internet "shopping malls" that it claimed would enable investors to earn substantial income and commissions on products purchased through the Internet. The malls contained a collection of links to retail websites maintained by merchants. The defendants allegedly advertised their business opportunity through the NexGen website, live presentations, and telemarketing calls, and maintained a network of affiliates to help promote and sell the malls. Participants paid a registration fee to join the NexGen program, and most also purchased a "WebSuite" including the Internet mall and related goods and services. A "Basic WebSuite" cost $185, including the registration fee, and a "Power Pack WebSuite" cost $555. The FTC's complaint stated that NexGen assured consumers that buying the "WebSuite" qualified them to earn significant commissions for every "WebSuite" sold. NexGen allegedly claimed that "each activated business center had the potential to earn up to $60,000 per week."

Prosperity Network (2006). *SEC v. William M. Osterhout, Prosperity Network, Inc.*, U.S. District Court, Northern District of Georgia, Civil Action No. 1:06-CV-2318 (2006). The SEC shut down an operator that sold memberships in "passive income" generating web portals to participants, who in turn, received income from recruiting others to do the same and so on. The SEC charged, "that in order to purchase a PAS membership, prospective investors submit their personal information into an existing PAS website and agree to be contacted by a PAS team leader, who then directly solicits the investor. Investors who choose to purchase PAS memberships receive the following: (1) their own unique replicated PAS website that automatically offers PAS memberships to additional prospective investors; and (2) the services of PAS team leaders to solicit new prospective investors. The proceeds from an investor's first sale of a PAS membership must be paid to an earlier investor; thereafter, PAS investors retain commissions for each subsequent sale of PAS memberships to new investors while directing part of the sales proceeds to PNI. Although PAS can purportedly be used to market goods and services in addition to PAS memberships, PAS is designed to generate returns for existing investors based almost entirely upon the sales of new PAS memberships to downline investors. As there are a finite number of prospective investors who could ultimately choose to invest in PAS by purchasing a membership, PAS is a pyramid-scheme that will collapse when there are no further investors, leaving the majority of downline investors with losses."

Fortune Hi-Tech Marketing (2013). *FTC v. Fortune Hi-Tech Marketing, Inc.*, U.S. District Court, Northern District of Illinois, Civil N. 13 CV 578 (2013). The FTC filed this case in 2013. It is highly contested and a preliminary injunction hearing is scheduled in the near term. Therefore, no conclusions can be drawn one way or the other. The FTC's primary allegation is that participants pay upfront fees ranging into the hundreds of dollars and, that, it is those upfront fees, rather than the slight revenue paid from third party vendors that is used to fuel distributor commissions in the program. 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. Says the FTC in its press release, 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 nonparticipants, 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 the litigation, FHTM contends that its program is primarily driven by sale of products and services. Until this case is adjudicated or resolved, no lessons are to be learned.

JewelWay (1997). *FTC v JewelWay International, Inc.*, U.S. District Court, District of Arizona, Case CV-97-383 TUC JMR (1997). The FTC successfully prosecuted and closed JewelWay International, Inc., a jewelry company that enlisted independent representatives to sell to the public. In reality, minimal attention was paid to ongoing sales of jewelry from inventory, but instead, participants were encouraged to purchase $750 packages of jewelry and find others to do the same and so on. Primary revenue to the company and to fund commissions came from initial wholesale package purchases by distributors who were urged to buy these larger packages to advance to higher earnings levels. The FTC argued that the primary promotional activities focused on recruitment of participants to buy quantities of product rather than on selling inventory on to customers.

In summary, short sellers and critics seemed to miss the clear dividing line here. As a general matter, the facts of these federal prosecutions look nothing like the programs of established leading direct selling companies. They are often "inherently fraudulent" and often represent "egregious" abuse. Prosecuted programs are often characterized by bogus products, bogus services, bogus programs, purposefully misleading recruitment and sales activity, earnings misrepresentations, payment of commissions on sales tools and training, investment schemes and out and out fraud. Their fact patterns are far afield from the more innocuous issue of personal use of products by distributors by leading established direct selling companies.

If such cases are predictors for short sellers that federal agencies will seek the death of leading established direct selling companies, they may wish to revisit their "bets." On the pyramid spectrum of

"I know it when I see it," although there may be an occasional blurring of facts, it is not that hard to put programs in one camp or the other.

Additionally, Short Sellers missed a 40-year trend recognizing Personal Use as a legitimate end destination for product.

Leading direct sellers are the first to recognize that many of their distributors join for the purpose of becoming discount buyers and for their own personal use of products. In fact, an early study by the Direct Selling Association as to why direct sellers join companies, revealed that the number one reason individuals join is that they like and believe in the product. Short Sellers have focused on "personal use" by distributors, as a major factor in criticizing leading direct selling companies as pyramids. From their perspective, if usage of product is not dominated by non-distributor retail customers, then, *a fortiori*, a program is a pyramid scheme. This criticism is followed by a prediction that federal authorities will shut down such programs and, if they are publicly traded, their stock price should be valued at zero.

As with a miscalculation as to where programs may fit on the pyramid spectrum of "I know it when I see it," short sellers have missed a 40-year legal trend line which focuses, not on the existence of sales to nonparticipant retail customers, **but rather on whether product is purchased by and used by the "ultimate user,"** whether or not that individual is a distributor or non-distributor. Beyond that issue, as noted above, prosecutions are driven by factors of "inherently deceptive and egregious abuse."

A look at the earliest of the pyramid cases supports this thesis.

A good summary of the earliest thinking appears in the landmark 1979 FTC administrative law decision, *In the Matter of Amway* (93 F.T.C. 618), which validated Amway's multilevel marketing program. As noted in the administrative law decision:

> *Such schemes are characterized by the payment by participants of money to the company in return for which they receive (1) the right to sell the product and (2) the right to receive in return for recruiting other participants into the program rewards* ***which are unrelated to sale of the product to ultimate users.*** *(emphasis added). In general such recruitment is facilitated by promising all participants the same 'lucrative' rights to recruit.*
>
> *Participants in the Koscot marketing plan paid an initial amount up to $5,000 to the company for inventory and the right to recruit others. The distributors who recruited others received $2,650 of the recruit's $5,000 payment. 86 F.T.C. at 1179. The only way a Koscot distributor could get the payment back was to recruit more distributors. 86 F.T.C. at 1131. Koscot and its distributors were primarily in the business of selling distributorships. 86 F.T.C. at 1140.*
>
> *Participants in the GerRoMar, Inc. marketing plan bought nonreturnable inventory for up to $1,950. 84 F.T.C. at 10810. Recruiters received compensation based on the fact of recruiting regardless of whether products were sold to the consumers. 84 F.T.C. at 148.*

The pyramid marketing program in Holiday Magic, Inc., 84 F.T.C. 748 (1974) required distributors to buy in at various levels for up to $4,500. At the highest level, distributors received $2,500 of the $4,500 for recruiting another distributor at the same level. 84 F.T.C. at 1032. The inventory purchased in this manner was nonreturnable and the company paid little attention to consumers. 84 F.T.C. at 1035.

The FTC Amway decision went on to cite salutary consumer protection features of Amway, which, have since been adopted by leading direct selling companies and cited in almost every court decision as the "Amway safeguards": (1) an inventory buyback policy for terminating distributors; (2) a 70% rule which is an anti-inventory loading rule that prohibits reordering unless 70% of previously ordered product has been sold or used; a mandated customer rule that emphasized moving product to the ultimate user.

Amway has traditionally recognized personal use of product for commission purposes and the FTC Amway decision specifically recognized what it meant by sales to the "ultimate user":

... This multilevel wholesaling network ends with those distributors who have not sponsored any new distributors, and ***who make purchases from their sponsors solely for their own use or for resale to consumers.*** *… (emphasis added)*

… Specifically, the Amway Plan is not a plan where participants purchase the right to earn profits by recruiting other participants, who themselves are interested in recruitment fees rather than the sale of products.

Jump forward 40 years to the most recent comprehensive federal court opinion on an FTC prosecution, *FTC v. BurnLounge,* U.S. District Court, Central District California, Case CV 07- 3654-GW(FMOx) (2012), and the target and pyramid acid test analysis of the U.S. District Judge is not "personal use" by distributors; but, rather whether the motivation for "first purchases" was really as a "buy in" gateway to the opportunity.

In fact, the thrust of the opinion was not based on criticism of the sort of "personal use" by distributors so common in many leading direct selling companies. Instead, the thrust of the opinion was that the motivation for distributor purchases of "packages" was incidental to creating a market for company product or services; i.e. the true purpose for purchases was to buy into qualification for commissions in the opportunity ... a classic allegation in pyramid schemes.

In fact, the Court's own observations even seemed to ratify distributor personal use, for the right reasons, as a favorable factor in legal analysis, but noting that products, purchased as sales tools, as in the BurnLounge program, do not fit properly in the analysis:

The bundled products had at least some minor value in and of themselves, and a consumer who had primarily in mind that value when he/she purchased them could not have been harmed by the scheme. The Court therefore finds the fact that the products had some value is relevant to the calculation of consumer harm, but only insofar as those products were purchased for their value as ultimate user products, and not for the conjoined business opportunity. ***To individuals***

> ***who considered the bundled products as merely incidental to the business opportunity, the Court finds the products were of no relevant value.*** *(emphasis added).*
>
> *BurnLounge argues that the sale of the Basic Package (i.e. the sale of an individual BurnPage and its required software) is the sale of a product to an ultimate user.37 See Whole Living, Inc., 344 F. Supp. 2d at 745-46 ("A structure that allows commission on downline purchases by other distributors does not, by itself, render a multi-level marketing scheme an illegal pyramid.").* ***While it is true that the BurnPage could be considered a 'product' and a Retailer to be the 'user' of that product, this argument ignores the nature of the use itself. That is as a tool for sales and (more importantly) for recruitment, as demonstrated by a review of the BurnLounge promotional materials, the presentations of its spokespersons, and the statistics as to the participants who bought into the enterprise.*** *(emphasis added)*

Real Confusion Created by the *Omnitrition* Decision

In between *Amway* and *BurnLounge*, an odd decision created havoc for the industry on the issue of personal use. A private class action had charged a company, Omnitrition, as a pyramid. Actually, Omnitrition prevailed at the trial court and summary judgment was entered for Omnitrition. The case was appealed to the U.S. Court of Appeals for the Ninth Circuit. The court ruled that material issues of fact remained to be reviewed and, therefore, the summary judgment, in favor of Omnitrition, should be reversed and the case remanded for further proceedings. *Webster v. Omnitrition International*, 79 F.3d 776 (1996). Shortly thereafter, the case settled and, therefore, no final trial or adjudication occurred.

In actuality, it was not necessary for the appellate court to address the substantive issue of what is and what is not a pyramid. But it did, in what industry observers referenced as ***dicta***, language not necessary to the decision; as the issue before the court was whether or not there was a material issue of fact as to whether or not Omnitrition actually implemented anti-pyramiding rules beyond the mere adoption of the written Amway safeguards rules.

For the next decade, the Omnitrition dicta created confusion as to whether distributors, who were also ultimate users, could be a legitimate destination for purposes of pyramid analysis. And that confusion, to this day, has been seized upon by critics (and today's short sellers) that leading direct selling companies (particularly those that sell personal consumables products such as nutrition) were pyramid schemes.

In reality, critics of MLM and the 2012 short sellers seemed to have missed the point of the Omnitrition court. In its analysis, the court applied principles of Koscot and Amway, which demanded "no rewards unless sales related to ultimate users." The message of the appellate court to the trial court was that Omnitrition could not be said to be promoting "retail sales" nor sales to the "ultimate consumer" if it allowed a climate of ***pervasive inventory loading***, i.e., purchases of large stocks of inventory and payment of commissions on such sales hardly insured that product was moving on to the **ultimate user**.

In particular, the court was critical that distributors were urged to advance to the "supervisor" level to make meaningful commissions through initial purchases and ongoing purchases of thousands of dollars of product. In the words of the court, "people buy exorbitant amounts of products that normally would not be sold in an average market." The court's message was that "adopting a 10 retail customer" rule from Amway, would be ineffective, even with personal use, to rid oneself of thousands of dollars of mandated inventory purchases. **In other words, this case was not really about "retail sales," nor "personal use," it was about inventory loading that defeated the goal of sales to the ultimate user.** Any other reading, as by MLM critics and short sellers, would be to miss the entire factual context of the case.

Getting it Right...

In the absence of the actual context of the Omnitrition facts, industry critics and short sellers have cited the Omnitrition dicta as standing for a precedent that personal use or internal consumption should not be credited in the pyramid/legitimacy analysis. **However, given a long line of precedent and follow-up cases, state legislation and FTC statements, as well as the true "objectionable facts" of Omnitrition, their pyramid accusation is not warranted.**

In 2004, the FTC, in an FTC Staff Advisory Opinion and Pyramid Schemes Analysis, responded to an inquiry from the Direct Selling Association, intending to clarify that the FTC did not view "personal use" as the primary determinant of illegality, but rather whether purchases of goods and services were "merely incidental" to "buying in" to the opportunity. In fact, its major cases have focused on this point.

In its 2004 "clarification letter," the FTC noted:

> *Internal Consumption*
>
> *Much has been made of the personal, or internal, consumption issue in recent years. In fact, the amount of internal consumption in any multi-level compensation business does not determine whether or not the FTC will consider the plan a pyramid scheme, The critical question for the FTC is whether the revenues that primarily support the commissions paid to all participants are generated from purchases of goods and services that are not simply incidental to the purchase of the right to participate in a money-making venture.*
>
> *It is important to distinguish an illegal pyramid scheme from a legitimate buyers club. A buyers club confers the right to purchase goods and services at a discount. If a buyers club is organized as a multi-level reward system, the purchase of goods and services by one's downline could defray the cost of one's own purchases (i.e., the greater the downline purchases, the greater the volume discounts that the club receives from its suppliers, the greater the discount that can be apportioned to participants through the multi-level system). The purchase of goods and services within such a system can, therefore, be distinguished from a pyramid scheme on two grounds. First, purchases by the club's members can actually reduce costs for everyone (the goal of the club in the first place). Second, the purchase of goods and services is not merely incidental to the right to participate in a money-making venture, but rather the very reason participants join the program. Therefore, the plan does not simply transfer money from winners to losers, leaving the majority of participants with financial losses.*

FTC Consent Orders and Final Orders: Why the Overreach?

And so, why the overreaching and unnecessary language on "personal use" that finds its way into the formal court briefs, attached expert witness declarations and final orders of FTC cases? The FTC noted, in the clarification 2004 letter, that it did not mean such language to be applicable to the direct selling industry in general, but rather to specific inherently deceptive and abusive pyramid schemes. And, although understanding that such overreaching might place a cloud of uncertainty over mainstream companies, the FTC indicated that it consciously promoted such overreaching language (sometimes referred to as "fencing in" language) to give it more enforcement flexibility in future prosecutions.

Said the FTC:

> *With regard to your second question, the Federal Trade Commission often enters into consent orders with individuals and companies that the Commission has determined have violated the FTC Act. To protect the public from those who have demonstrated unwillingness to follow the law, these orders often contain provisions that place extra constraints upon a wrongdoer that do not apply to the general public. These 'fencing-in' provisions only apply to the defendant signing the order and anyone with whom the defendant is acting in concert. They do not represent the general state of the law.*
>
> *For example, when the Commission brings a pyramid scheme action, the case often concludes with a consent order. The scope and severity of the order will depend upon the facts of the case; however, most such orders contain definitions that exclude any sale to a participant in the business from the calculation of the venture's legitimacy. These definitions draw very clear lines for those who have demonstrated a willingness to violate the law, but are not intended to represent the state of the law for the general public.*

Why does the FTC overreach? Does the FTC really envision, as short sellers might urge, chasing after long-established "consumables" MLM companies, where "internal consumption" or "purchases for personal and family use" are quite usual? **Probably not.**

Rather, the FTC is looking for maximum negotiating strength as it chases after what it perceives as egregious, abusive and inherently fraudulent pyramid schemes. In multiple cases, its formal posture has strengthened its ability to achieve temporary restraining orders, receiverships and other mechanisms to **immediately** cut off a pyramid scheme that is in "full stride." From this perspective, “over playing” the hand may be inconsistent, but it is also understandable.

And even the FDA’s primary expert economist in many of its pyramid prosecutions, Dr. Peter Vander Nat, has been quite equivocal on the issue of "internal consumption." In declarations in a number of cases, he misinterprets the Omnitrition precedent for pyramid analysis arising from Koscot’s demand of "sales to ultimate users" as, instead, demanding "sales to non-participant retail customers." No doubt, such declarations have been helpful in a "rushed" environment to help the FTC achieve temporary restraining orders and receiverships in front of courts that may have never adjudicated pyramid cases.

But, not only is this overreaching and misinterpretation expedient for attaining a result, it actually does not reflect Dr. Vander Nat's opinion, in a more reflective moment, on the role of internal consumption in pyramid analysis.

Below is an excerpt from Dr. Vander Nat's deposition in the BurnLounge case:

Vander Nat *BurnLounge* deposition on issue of internal consumption ... November 12, 2008:

> *218-219*
>
> *Q. Under the heading internal consumption, the second sentence. "In fact the amount of internal consumption in any multilevel compensation business does not determine whether or not the FTC will consider the plan a pyramid scheme." Do you agree with that sentence?*
>
> *A. I think so. Yes. I think that that is consistent with what I said this morning on this point.*
>
> *Q. What if the sentence read a little differently? What if the sentence read the amount of internal consumption in any multilevel compensation business is not a factor in the analysis of the FTC's determination of whether or not a plan is a pyramid? Would you still agree with the sentence?*
>
> *A. I think I would. I said this morning, when I think back on this testimony, that I expect there to be internal consumption in the organization and the fact that it's there is itself not determinative one way or another. I think I said that*
>
> *220*
>
> *Q. And that is the sales that you consider in your analysis. And you exclude from that sales within the distribution network.*
>
> *A. I said I exclude from it those purchases that people are required to make in order to enter the business opportunity. That's exactly what I said about it.*
>
> *Q. And isn't that at least some of what internal consumption is?*
>
> *A. No. I don't think that that's what's being referred to here. I mean, normally when you're talking about internal consumption, if you just use the word generally, it means people wanting to use the product for their own use just because they like the product. I mean, that's normally what the phrase refers to. And I simply made this other qualifier about it. Whatever you are required to purchase of consumable goods in order to enter the business opportunity, I count that as part of your business investment because you're required to buy it as part of the investment*
>
> *228*
>
> *Q. And are you involved in the negotiation or drafting of terms of those consent decrees when they're entered or negotiated?*

A. Usually not. I'm only sometimes tangentially involved in that somebody might ask my opinion. But not in actually drafting the terms, no.

Q. Are you aware that many of those orders contain provisions regarding the percentage of permitted sales within the distribution network?

A. No. I'm not -- I don't recall any discussion about that. I was not part of that formulation.

Q. Do you have any opinion as to a percentage of sales within a distribution network of a company that would not make it more likely that there be a finding of pyramid?

A. No. As I've said, internal consumption doesn't count one way or another with me. I've given all the factors that I use. Internal consumption is itself not one of the factors.

And notwithstanding his declarations in many FTC pyramid prosecutions that "retail sales" are the dividing line, Dr. Vander Nat cuts to the chase in his *BurnLounge* deposition that, in fact, the acid test is whether or not distributors are making payments as a gateway to the business opportunity, i.e. purchases incidental to the business opportunity. In this regard, he is on the same wavelength as both the case law, 2004 FTC Advisory opinion and the position of the direct selling industry. He is not on the same wavelength as the MLM industry critics and short sellers that decry recognition for personal use by distributors.

Page 130 of the Vander Nat BurnLounge deposition:

I believe in the Mogul program people are buying the product for the sake of a business opportunity. That's why they're buying it. So the VIP package has a certain business value which is distinct from the exclusive package as a business value which is again distinguished from the basic package as a business value. I am basing the analysis on this basic premise in the Mogul program people are buying into a business opportunity. They're paying what in essence is a business investment for them. The fact that it has some consumable items in it, that may be beneficial to them, but they're buying it for the sake of the business opportunity. Therefore the issue of whether they're harmed is for me they went into a business in the hopes of making money but in fact they have a business loss. So for me the business loss is the harm.

In reality, it appears that the dividing line between pyramid and legitimacy is probably the same for both the FTC and the established direct selling industry. On true substance, they are on the same wavelength even if at odds on the best path to support their core convictions. Opposition is clear for programs in which distributor payments are merely made as "gateways to the business opportunity" or are "purchases incidental to the business opportunity." On the other hand, the long-established consumables MLM companies that are characterized by purchases of product for resale to consumers or purchases for personal or family use in reasonable amounts and which are made in a deliberate and orderly fashion (as opposed to upfront inventory loading at the inception of the opportunity), are viewed as legitimate "machines" of distribution.

And so, in the end, short sellers and financial bloggers may have mistakenly relied on misreading of case authority, the FTC's chief expert witness and the FTC's actual position on the issue of "personal use" or "internal consumption" to forecast government prosecution or ultimate demise of companies they short sell.

Many States Step in to Recognize Personal Use

In the aftermath of uncertainty created by Omnitrition and "fencing in" FTC actions, no less than a dozen states, including Louisiana, Texas, Oklahoma, Montana, Idaho, Utah, Washington, South Dakota, Kentucky, Indiana, Virginia, Nebraska and Georgia (with more states considering such amendments) sought to clarify the issue, amending pyramid and MLM statutes to recognize internal consumption and personal use in reasonable amounts as basis for paying commissions:

A typical provision of such legislation from the state of Washington:

> *'Compensation' means payment, regardless of how it is characterized, of money, financial benefit, or thing of value. 'Compensation' does not include payment based on the sale of goods or services to anyone who is purchasing the goods or services for actual use or consumption.*

And so, the state legislative trend on "personal use" is very clear.

Herbalife Gets its Marching Orders on Personal Use from our Largest State

And lest industry critics or short sellers think that companies like Herbalife created the "defining line" on the "I know it when I see it" pyramid analysis, it should be noted that Herbalife actually took its marching orders (more than a decade before the Omnitrition *dicta* on personal use) from one of the most respected Attorney General Consumer Protection Divisions and the largest consumer state in the country, California.

Almost 30 years ago, in the infancy of Herbalife, the State of California provided precise direction to Herbalife on how it should account for personal use by its distributors … it should count it the same way as other sales to nonparticipants. In other words, Herbalife didn't invent this standard in 2013, it has operated under this standard, as have leading direct selling companies for almost 30 years.

In 1986, the State of California focused the essential factor to use for determining whether a direct selling company was a pyramid and at what end of the "I know it when I see it" spectrum it should lie. *People of the State of California v. Herbalife International Inc.*, Superior Court, Santa Cruz County, Case No. 92767 (1986).

The State of California entered into a Stipulated Judgment Order with Herbalife that provides good direction on this subject. The Stipulated Judgment Order provided:

> *5(c). The term retail sale as used in this Section 5 means a sale at defendants' product(s) in any of the following situations: (1) to persons who are not part of defendant's marketing program or*

> *distribution system; or, (2) to persons who are not buying to become part of defendants marketing program or distribution system; or, **(3) to persons who, although desirous of becoming or who are a part of defendants' marketing plan or distribution system are buying for their own personal or family use.***

In fact, this stipulated order was an inspiration to the many states that have amended their pyramid/MLM statutes to recognize legitimacy of personal use, and also likely to subsequent court decisions and, even the FTC, in recognizing personal use in its 2004 Advisory Opinion on Pyramid Schemes Analysis.

A Modest Suggestion for Model Federal Legislation

In fact, it is submitted that the following model pyramid language, relating to personal use, might serve as a synthesis of trending state legislation, FTC staff advisory and reasoning set forth in various federal and state court opinions:

> *Prohibited Marketing Scheme means an illegal pyramid sales scheme, Ponzi scheme, chain marketing scheme, or other marketing plan or program in which participants pay money or valuable consideration in return for which they obtain the right to receive rewards for recruiting other participants into the program, and those rewards are unrelated to the sale of products or services to ultimate users. Prohibited payment or consideration does not include payment for non-commissionable not for profit or at cost sales and marketing materials support. **For purposes of this definition, sale of products or services to ultimate users include sales to participants, in reasonable amounts, for actual personal or family use.***

The adoption of such language would provide a great service to the direct selling industry and its distributors and customers to avoid the continuing rehash of whether or not such businesses are legitimate or pyramid schemes. And such model legislation would also drown the cacophony of direct selling critics who wreak havoc and turbulence on financial markets with respect to publicly traded direct selling companies.

In Summary...

And so, coming full circle on the "I know it when I see it" pyramid analysis:

Given,

1. A survey of FTC, SEC and Justice Department leading pyramid cases during the last two decades which seem to focus on inherently deceptive, abusive and egregious schemes that are radically different than the marketing programs of well-established and decades old direct selling companies , and

2. The FTC's own statements on personal use, as well as the trending legislation at the state level, recognizing the validity of personal use as a legitimate end destination of product,

The recent short seller attack strategy on established direct sellers, may, itself be worthy of self-reexamination. A few cogent facts and legal precedent may have been missed on the way to the press conference.

And, how will all this turn out. Well, the fat lady hasn't sung … stay tuned.

For more information on this subject and other important issues in the area of MLM, Direct Selling and Network Marketing, please visit http://www.mlmlegal.com.

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On any given day you can catch Jeffrey Babener lecturing on Network Marketing at the University of Texas or the University of Illinois, addressing thousands of distributors in Los Angeles, Bangkok, Tokyo and Russia, or writing a new book on Network Marketing, an article for Entrepreneur Magazine or a chapter for a University textbook. Over two decades he has served as marketing and legal advisor to some of the world's largest direct selling companies, the likes of Avon, Nikken, Melaleuca, Discovery Toys, NuSkin, and he has provided counsel to the most successful telecom network marketing companies...Excel, ACN, World Connect, ITI, AOL Select and Network 2000. An active spokesperson for the industry, he has assisted in new legislation and served on the Lawyer's Council, Government Relations Committee and Internet Task Force of the Direct Selling Association (DSA) as well as serving as General Counsel for the Multilevel Marketing International Association.   He is an MLM attorney supplier member of the DSA and has served as legal counsel and MLM consultant on MLM law issues for many DSA companies.

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