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

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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 from100 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,

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For more information backing up these claims, I would refer the reader both to the law enforcement and research pages of my web site (www.mlm-thetruth.com), that summarizes thousands of pages of research and feedback from all over the world, or to my rebuttal comments from the original Rule on the FTC web site.