

# TOP TEN THINGS I LEARNED FROM TEN YEARS' RESEARCH ON MLM/NETWORK MARKETING (Multi-level or "Consumer Direct" Marketing, etc.)

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## RESEARCH NOTE:

These conclusions are supported [by rigorous independent research](#). These analyses and conclusions are more than mere opinions. They are supported by—

- extensive comparative research on MLM compensation plans and alternative business models to clarify differences
- evaluations of over 200 MLM programs, looking for the “5 Red Flags” in their compensation plan (See below.)
- interviews with and feedback from thousands of MLM distributors and ex-distributors world-wide in a wide variety of MLM programs
- interviews with the top experts in the field
- surveys of hundreds of tax professionals where MLM is concentrated, representing thousands of MLM's tax returns
- court records in MLM cases (including IRS income tax records of top distributors in one state)
- involvement as consultant and expert witness in several public and private court cases against MLM companies
- household consumer surveys regarding MLM participation
- surveys of leading MLM company presidents
- private and public financial disclosures by MLM companies
- communications with law enforcement officials at all levels
- direct experience with prominent MLM companies.

## 1. MLM PROGRAMS APPEAR INNOCENT, BUT MOST MLM'S RESULT IN 99% OF PARTICIPANTS' LOSING MONEY.

“Multi-level marketing” (a.k.a., “MLM,” or “network marketing”) programs have great appeal to vulnerable consumers seeking to improve their lot in life. Some people are drawn to MLM's by their apparent low cost of initial participation, by the need to be part of a group dedicated to a common purpose, by the appeal of products with magical properties, and by the promise of “residual” second income or early retirement. MLM is often **insidious** in its apparent innocence – and at the same time **pernicious** in its inevitable impoverishment of nearly all participants to the degree of their investments in time and money. While losses (mostly from unused product purchases) are minimal for many participants, harm to some can be great, including heavy debt, home foreclosures, career disruptions, and bankruptcy. Other harmful effects often include inordinate focus on materialism, exploitation of valued friendships, obsessive focus on MLM contributing to divorce, and damage to self-esteem.

Most MLM participants are not seeking an “opportunity,” but are recruited by someone close to them. It


is sold as a legitimate home business to “earn a little extra money,” to pay bills or college costs, to donate to worthy causes, etc. The reality is far different. By promoting infinite (endless chain) recruitment in finite markets, they mathematically doom the vast majority of participants to financial loss. The loss rate for “recruiting MLM's” (See #2 below) exceeds 99%, with many approximating 99.9%; i.e., about 999 out of 1,000 participants lose money! Such odds are far worse than for no-product pyramid schemes and even worse than for many games of chance in gambling centers like Las Vegas. World wide, millions of MLM participants lose an aggregate total of tens of billions of dollars annually.


(See ["Which Does the Greater Harm?"](#) and ["Who Profits from Multi-Level Marketing? Preparers of Utah Tax Returns Have the Answer."](#))


## 2. ALMOST ALL MLM'S ARE RECRUITING MLM'S, OR PRODUCT-BASED PYRAMID SCHEMES.


Nearly all MLM programs can be considered “product-based pyramid schemes,” or “recruiting MLM's” – because they thrive on recruitment of new “distributors” – who are the actual customers. Here the term “recruiting MLM” – or “MLM” for short – refers to schemes that are characterized *by multi-level endless chain recruitment of distributors as their primary customers.*

Recruiting MLM's incorporate these “Five Red Flags” in their compensation plans:

 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.

 Ongoing purchases (products, sales “tools,” etc.) by “distributors” are encouraged in order for them to be eligible for commissions and to advance in the business (“pay to play”).

 4. The company pays commissions and/or bonuses to more than five levels of “distributors.”



5. For each sale, company payout for each upline participant 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.

**WARNING:** Where data has become available for MLM companies with these 5 red flags in their compensation plans (which is most MLM's), approximately 99.9% of participants lose money – after subtracting purchases from the company. Consumers would be wise to avoid participating—regardless of how great the products, how many "respectable" people manage it or endorse it, and whether or not law enforcement has taken any action against them. A person's odds of profiting from gambling in Las Vegas are far better. (See "Which Does the Greater Harm," posted at [www.mlm-thetruth.com](http://www.mlm-thetruth.com))

### **3. A FAIR AND PROFITABLE "RETAIL MLM" WOULD NOT LOOK AT ALL LIKE THE TYPICAL MLM.**

It is conceivable that an MLM could be created which is both fair and legitimate. For example, the emphasis on direct sales at retail would be reflected in a compensation plan in which most of the commissions - over 50% - paid by the company would be paid to distributors selling the product. Override commissions would be paid on no more than three or four levels in one's upline, each of whom would receive a very small (perhaps 3-6% at most) override from the sales of front-line participants doing the selling. Purchases would not be required or "incentivized" to qualify for commissions or advancement. Such a plan could be called a "retail MLM." "Retail MLM's" that might be considered legitimate would be acceptable only to the degree that they are not like typical MLM's, as characterized by the "5 Red Flags" above.

### **4. PROPERLY UNDERSTOOD, EVEN LEADING MLM'S ARE LIKELY TO BE FRAUDULENT AND TECHNICALLY ILLEGAL.**

Nearly all MLM's are inherently fraudulent endless chain recruitment schemes, promising substantial ongoing income, but leading to losses for the vast majority of participants. However, a few at the top profit hugely from product purchases of downline participants who stock up on or subscribe to products to "play the game."

In fact, 30 typical misrepresentations that are routinely used in MLM recruitment have been identified. As such, recruiting MLM's could be considered engaged in theft by misrepresentation.

And investors in publicly traded MLM companies would be upset if they learned that in their MLM, there are few if any bone fide customers (see # 10) and that the MLM is

dependent for its success on a network of distributors, 99.9% of whom lose money.

These schemes are technically illegal in almost all jurisdictions because they violate statutes against pyramid schemes and deceptive sales practices – or simple fraud. Based on available data, **the vast majority of MLM's are not income opportunities, but loss opportunities instead – and not legitimate businesses by any reasonable measure.**

### **5. MLM VICTIMS SELDOM FILE COMPLAINTS – WHICH CONTRIBUTES TO THE PROBLEM.**

In law enforcement, the squeaky wheel gets the grease. So a primary reason for lack of enforcement against fraudulent MLM's is the lack of public outcry. Even victims suffering huge losses seldom file complaints with law enforcement, having been conditioned to blame themselves for their "failure." They may also avoid filing complaints because they fear consequences from or to their upline, which are often close friends and relatives. And they may fear the consequences of reporting fraud, or self-incrimination, when they themselves were at one time defrauding others, albeit unwittingly. So with few if any complaints, there is little pressure for regulators to act against MLM's. And when law enforcement agencies fail to act against a fraudulent MLM company, prospects assume it must be legal.

### **6. LAW ENFORCEMENT AGENCIES GENERALLY LACK STATUTORY AUTHORITY, THE RESOURCES, AND/OR THE WILL TO PROTECT CONSUMERS AGAINST MLM ABUSES.**

Except in rare instances, **law enforcement at both federal and state levels is not likely to act on the innumerable violations of state and federal laws by MLM firms.** These officials are often overwhelmed with cases, few of them as complicated as MLM. Agency officials often work long, hard hours; but they simply lack the resources to stand up to these schemes – which one important law enforcement official told me would take 20 times the resources as the typical case brought before them.

Also, few regulators understand the fraud inherent in complex MLM compensation plans that are obfuscated by their complexity. MLM companies merely put on the façade of complying with the "Amway rules," which were initiated by the FTC to assure that some legitimate selling to non-distributors is taking place. These rules are typically ignored, since it would be impractical to enforce them. So law enforcement is not likely to act without a significant number of complaints filed by consumers – which seldom happens, especially with established MLM's.

State legislation is often weak and inconsistent over jurisdictions; since MLM's rapidly transcend jurisdictional boundaries, they quickly become unmanageable by local

authorities. And the legislatures of some states are being lobbied by the Direct Selling Association (DSA, which has become an arm of the MLM industry) to pass "improved" legislation against pyramid schemes, but that would exempt product-based pyramid schemes from prosecution. And such legislation has been accepted in several states by unwitting legislators. In these states, the most damaging pyramid schemes of all (those with the highest loss rates) are exempt from prosecution, and the least damaging carry criminal penalties. (See [The NUMBERS – the Odds of Success](#). More on the perverse legislation promoted by the DSA can be found on the following web sites — [www.mlm-thetruth.com](http://www.mlm-thetruth.com) and [www.pyramidchemealert.org](http://www.pyramidchemealert.org))

Federal agencies, particularly the FTC, find other classes of consumer abuse much easier to deal with and more publicly acceptable to prosecute.

There are the occasional exceptions. A handful of MLM's (product-based pyramid schemes) have been stopped by authorities, but this is but a drop in the bucket, compared to the hundreds of MLM's which defraud new recruits every day – with new ones cropping up regularly to replace those which collapse. To be effective, law enforcement agencies would have to be less focused on merely reacting to complaints and more proactive in educating and warning the public and in taking action while the MLM programs are small and the endless chain of recruitment of a pyramid of participants has not become too powerful to stop.

Unfortunately, many of the larger MLM's are compensating for declining acceptance in the U.S. by finding populations in Asia and other parts of the world who are highly vulnerable to their recruitment. In this respect, "recruiting MLM's" evolve into Ponzi schemes in order to survive and grow – recruiting in new countries or with new divisions to repay earlier investors in its "opportunity."

Officials from foreign countries are no more savvy on this issue than are U.S. officials, and in fact U.S. trade representatives have yielded to lobbying pressure from the DSA (see below) to accept MLM (in the guise of "direct selling") overseas. As a result, millions of unsuspecting victims overseas are suffering billions of dollars in losses from these US-based companies. This type of plundering of countries whose good will we have been trying to cultivate is bound to have adverse consequences to our foreign relations down the road.

There is one bright spot in all of this, which helps to offset the inaction of law enforcement. Many participants and those close to them have seen enough of the harmful consequences of MLM participation that they have become immune to recruitment appeals. And some victims have developed web sites to warn others of the costs and harm done by these programs. (See [Highly recommended WEB SITES on MLM](#)) Any one who does a diligent search on the Internet with an open mind is not likely to participate in MLM, regardless of whether or not law enforcement acts against it.

## **7. MLM PROMOTERS RATIONALIZE MLM/PYRAMID SCHEME FRAUD.**

I have seen MLM company officials come up with very clever rationalizations for what they do. Those with whom I have communicated have shown extreme denial of the harm done by their MLM's. They interact primarily with those at the top of recruiting pyramids and are oblivious to the extent of the damages to those lower in the hierarchy, the vast majority of whom lose money and drop out, never to be heard from.

MLM promoters misrepresent because they MUST in order to survive and grow. Deception, including self-deception, becomes a way of life. If the truth were known about their abysmal odds of success, these programs would collapse like a house of cards. Who would join up if they knew that only one out of 1,000 participants earned a profit – after subtracting expenses, including sales helps and purchases from the company to qualify for commissions and for advancement in the scheme? In fact, the deceptions in MLM provide fodder for much [humor and satire on MLM](#).

Informed law enforcement officials and concerned consumer activists have observed religious overtones and even cult-like behavior of the "true believers" in MLM's or product-based pyramid schemes. For example: Cult expert, founder of "Resource Center for Freedom of Mind," counselor and author Steven Hassan looks at MLM/network marketing, such as Amway/Quixtar, as exhibiting many of the destructive traits of a cult. –

<http://www.freedomofmind.com/resourcecenter/groups/a/amway/index.htm>.

You can download the revealing experiences of a former federal auditor who was caught up in the Amway dream and then went public with what he found at – <http://www.merchantsofdeception.com/> Also, check out "Amway world wide dream builders and 'the things they will say' to profit from your dreams." Potential Amway recruits will be inoculated against their program after reading "the things they will say." –

<http://www.angelfire.com/or/amwaydreamers/index.html>

I have written on the impact of MLM on members of the Church of Jesus Christ of Latter-day Saints, who seem particularly vulnerable to these schemes, due at least in part to very trusting relationships cultivated in their ranks. My book [The Network Marketing Game: Gospel Perspectives in Multi-level Marketing](#) addresses the ethics of MLM for Latter-day Saints, and in fact for all persons with a Judeo-Christian code of ethics.

## **8. THE VILLAIN IN MLM IS AN EXPLOITATIVE AND DECEPTIVE COMPENSATION PLAN – OR "SYSTEM FRAUD."**

It would be difficult to point to individuals as villains. **The primary cause of MLM fraud is neither the leaders nor the products they sell, but a compensation plan or system, that rewards multi-level endless chain**

recruitment of “distributors” as primary customers. Thus, it could be termed “system fraud.”

MLM is the perfect con game. Many of the very persons who are out promoting the scheme are themselves victims – eventually running out of money and dropping out. They just absorb their losses – often substantial. And since they seldom complain to authorities, the game goes on!

MLM is all about deception. Ten years’ research and experience has taught me that in order to succeed in MLM, one must (1) be deceived, (2) maintain a high degree of self-deception, and (3) aggressively go about deceiving others.

## **9. THOUGH MOST MLM PROGRAMS ARE PRODUCT-BASED PYRAMID SCHEMES, MLM’S CAN DISPLAY REMARKABLE ENDURANCE – OFTEN EXPANDING PONZI-STYLE TO FOREIGN COUNTRIES TO KEEP THE CHAIN OF RECRUITMENT GOING.**

One would think that if almost all MLM’s were merely disguised pyramid schemes or endless chain recruitment schemes, they would collapse on their own. However, recruiting MLM’s are the most durable of all types of pyramid schemes. Complex compensation plans obfuscate the fraud so that only the most sophisticated of analysts can see through the maze of deceptions, making it possible for the programs to defraud on a massive scale without being recognized or stopped by authorities. (For more on MLM durability, see the aforementioned *5 Red Flags* report.)

As explained in #6 above, when recruitment in a given area dries up, top recruiters in an MLM move on to other areas. Recruits in each area are told that the real opportunity lies in \_\_\_ (the next fresh market, often a 2<sup>nd</sup> world country). When the market world-wide peaks and begins to slide, the company may open a new product division and begins the same cycle all over again, as Amway has done with Quixtar and Nu Skin with its Big Planet and Pharmanex divisions. Thus, durable MLM’s evolve into Ponzi schemes, with earlier investors profiting from the investments of new recruits.

As endless chain recruitment schemes, powerful incentives are in place to continue MLM recruiting – even when the “opportunity” is proven unprofitable. And since so few complaints are received by enforcement agencies, this class of fraud continues virtually unchecked.

## **10. MLM COMPENSATION PLANS REWARD RECRUITING OVER DIRECT SELLING.**

The Direct Selling Association (DSA), which is now dominated by the MLM industry and therefore promotes MLM’s agenda, defines direct selling as “the sale of a

consumer product or service, person-to-person, away from a fixed retail location.” On the bases of this definition, MLM’s claim to be direct sales programs. But the definition fails to specify what legitimate direct sales programs are NOT.

**Legitimate direct sales programs do not—**

- (1) recruit participants in an endless chain of recruiters recruiting recruiters,**
- (2) specify advancement by recruitment, rather than by appointment,**
- (3) require or use powerful incentives for ongoing purchases in order to qualify for commissions and to advance in the scheme,**
- (4) pay overrides on more levels of managers than are functionally justified (most corporations have found the entire country can be covered in four levels of sales managers),**
- and (5) offer excessive incentive to recruit, combined with inadequate incentive to sell products to bona fide customers. In nearly all MLM’s, there are few legitimate customers outside the network of “distributors.”**

I am confident that any qualified person willing to examine the evidence with an open mind will agree with the above conclusions. For the serious researcher, reports expanding on this research are available from the author.

**Ten years have gone into these reports. As a result of reading this information, you may be spared losses of hundreds or even thousands of dollars. Please show your appreciation by sharing this information with five people. Then ask each of them to share it with five more, and each of them with five more, etc. You can thereby participate in an endless chain of truth-telling.**

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