



## The College of New Jersey

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Ms. Edith Ramirez  
Chairwoman, Federal Trade Commission  
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Dear Madam Chairwoman:

I am writing about a consumer threat and industry-damaging problem described by the president of the Direct Selling Association as “pyramid schemes that like to disguise themselves as legitimate direct-selling companies.” Specifically, I ask the Federal Trade Commission to invest now in the long-term health of the direct selling industry, where pyramid schemes posing as legitimate multilevel marketing firms (MLMs) regularly victimize our citizens. The rule of caveat emptor cannot be the main line of protection for people who have fewer life-changing opportunities and are attracted to seemingly lucrative schemes that rely on asymmetric information and labyrinth-like compensation structures.

In 1995, I assisted the United States Department of Justice in a criminal prosecution of a pyramid scheme called Gold Unlimited. Since then I assisted the Securities and Exchange Commission in the International Heritage Inc. case, at the time its largest pyramid scheme prosecution to date, and worked with prosecutors in Florida and Kentucky. In 2002, I co-authored with Dr. Peter Vander Nat of your staff an academic paper on distinguishing between legitimate MLMs and pyramid schemes. I played no role in the current developments regarding Herbalife. Still, due to references to the Vander Nat and Keep article, I have spoken with, and written about, investors and their concerns on both sides of the matter. I have accepted no compensation. I do not hold a financial stake—short or long—in any MLM. My sole interest is to foster the development of a strong, appropriately regulated direct selling industry free of pyramid schemes.

Today, I argue that the growth of MLMs as the dominant form of direct selling and the persistence of pyramid schemes hiding in the same industry present a substantial threat to consumers. Industry data for the U.S. highlight the changing terrain: from 1990 to 2010 the number of direct selling salespeople (with the overwhelming majority in multilevel marketing) more than doubled, from 3.5% to 8.5%, as a percentage of all adults ages 20-64. During the same period, direct selling as a percentage of U.S. retail sales actually declined. As the number of direct selling salespeople in the U.S. increased from about five to fifteen million, revenue per salesperson also declined.

While the growth of multilevel marketing as a business form is undisputed, the claim that industry growth provides a corresponding growth of opportunities is far less obvious. At the firm level, for example, the 2011 average earnings of Herbalife and Nu Skin distributors were about

the same or less than those of Amway distributors in Wisconsin in 1979 (inflation adjusted), despite the significant financial success of the parent companies. Many MLMs and their top distributors also profit from the additional money spent by salespeople on training and development, often an investment with no documented impact on the probability of success.

Of course, flat distributor earnings and most compensation going to a small number of top distributors, and investors in the case of public companies, do not necessarily make an MLM a pyramid scheme. However, the lack of clear regulatory language and enforcement makes distinguishing one from the other very difficult. The recent FTC case of Fortune Hi-Tech Marketing (FHTM)—a firm that operated for more than ten years and had two former attorneys general on its advisory board—is one illustration of this point.

Unclear regulatory language and irregular enforcement prevent the development of a shared language between the industry and the FTC—language critical to identifying pyramid schemes. Since the 2004 FTC Staff Advisory Opinion, some industry members have interpreted the Advisory as different from the most relevant court decisions, as well as the FTC's position, recently expressed in FHTM. Yet, in response to these misinterpretations and related firm actions, the FTC has remained surprisingly silent. If, as is stated in the 2004 Advisory, the *critical question* for the FTC is the degree to which compensation to participants relies on recruitment (e.g., an endless chain), then I argue the FTC has not provided sufficient clarity nor induced sufficient industry transparency for protection against pyramid schemes.

For all practical purposes, the direct selling industry has become the MLM industry—again, an arena where pyramid schemes continue to hide. This evolution appears to have taken place with little oversight from the FTC. The relative ease with which very serious questions recently emerged about Herbalife, founded in 1983, underscores the confusion among American consumers, investors, and the industry about what constitutes a pyramid scheme. Consumers and investors deserve much better. A clarification of the 2004 Advisory is sorely needed. Equally so, an investigation by the FTC with clear public statements regarding the results—regardless of the outcome—would make pyramid schemes more identifiable, which is the key to their demise.

Educators are by nature optimists. The social impact of what we do in the classroom may not be felt for years. I am asking the FTC to invest the required resources now to create a stronger and more transparent direct selling industry, bringing increased consumer protection and lowering enforcement costs. Demanding transparency of the underlying business model, particularly the relationship between recruitment and participant compensation, would send a clear signal to the industry. Such effort would establish a much-needed regulatory investment in an industry that can provide consumer benefits and entrepreneurial opportunities.

Thank you for considering this important matter.

With regard,

A handwritten signature in dark ink, reading "William W. Keep PhD". The signature is fluid and cursive, with the first name "William" and last name "Keep" being more prominent, and "PhD" written in smaller letters at the end.

William W. Keep, PhD  
Dean