The Case (for and) against Multi-level Marketing

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Chapter 7: MLM's ABYSMAL NUMBERS

Chapter summary

Is MLM a profitable business opportunity? And if so, for whom? Just do the math – the numbers don't lie. In this and preceding chapters, you will find the most rigorous and thorough analysis of MLM profitability ever done by an independent research firm. Questions about the viability and profitability of MLM as a business model and its many company manifestations are answered in this and prior chapters – based on 15 years' research, worldwide feedback, and analysis of the compensation plans of over 350 of the leading MLMs, as well as average earnings data, where available. The answers are not pretty.

Our studies, along with those done by other independent analysts (not connected to the MLM industry), clearly prove that MLM as a business model – with its endless chain of recruitment of participants as primary customers – is flawed, unfair, and deceptive. Worldwide feedback suggests it is also extremely viral, predatory and harmful to many participants. This conclusion does not apply just to a specific MLM company, but to the entire MLM industry. It is a systemic problem.

Of the 350 MLMs I have analyzed for which a complete compensation plan was available, 100% of them are recruitment-driven and top-weighted. In other words, the vast majority of commissions paid by MLM companies go to a tiny percentage of TOPPs (top-of-the-pyramid promoters) at the expense of a revolving door of recruits, 99% of whom lose money. This is after subtracting purchases they must make to qualify for commissions and advancement in the scheme, to say nothing of minimal operating expenses for conducting an aggressive recruitment campaign – which (based on the compensation plans) is essential to get into the profit column.

The claim by MLM promoters that many participants work for part-time or seasonal income is a bogus argument because without full-time and long-sustained effort, MLM participants cannot build and maintain a large enough downline to meet expenses, and therefore do not profit.

These conclusions were confirmed in the average earnings reports of all 30 MLMs for which we were able to obtain data published by the companies themselves. Such statistics are invaluable for analysts to debunk the many misrepresentations that are told to thousands of prospects every day.

Failure and loss rates for MLMs are not comparable with legitimate small businesses, which have been found to be profitable for 39% over the lifetime of the business; whereas less than 1% of MLM participants profit. MLM makes even gambling look like a safe bet in comparison.

MLM stocks are questionable investments at best. And like gambling, losses from MLM participation should not be allowed as a tax deduction – beyond the amount of actual income.

MLM as a business model is the epitome of an "unfair or deceptive acts or practice" that the FTC is pledged to protect against. It is even worse than classic, no-product pyramid schemes (for which the loss rate is only about 90%) and "pay to play" chain letters. For promoters to present MLM as a "business opportunity" or "income opportunity" is a misrepresentation.

Legal disclaimer

These reports, analytical tools, and opinions are intended purely to communicate information in accordance with the right of free speech. They do not constitute legal or tax advice. Anyone seeking such advice should consult a competent professional who has expertise on endless chain or pyramid selling schemes. Readers are specifically advised to obey all applicable laws, whether or not enforced in their area. Neither the Consumer Awareness Institute nor the author assumes any responsibility for the consequences of anyone acting according to the information in these reports.

Chapter contents

Assumptions and cautions needed to proceed with this analysis

In any analysis, especially on a controversial topic and using less than perfectly gathered and controlled data, the analyst must make certain assumptions and recognize certain cautions or potential pitfalls in order to proceed. So in order for me or anyone to do this analysis of profitability for MLM participants, certain assumptions will be identified - such as whether or not participants seek to optimize their gains, and what costs could be incurred (and therefore should be subtracted from earnings) in a successful recruitment campaign. Questionable reporting that could mislead those seeking to get at the truth must be guarded against, such as how numbers are reported and displayed.

What tax studies have revealed about MLM profitability for participants

The Wisconsin experience with Amway. In 1980, as part of a suit against Amway, an investigation was undertaken by the Office of Attorney General for the State of Wisconsin, led by Assistant AG Bruce Craig. Out of approximately 20,000 distributors operating in Wisconsin, state tax returns were obtained for all of the Amway "Direct" Distributors in Wisconsin, which numbered about 200, which represented approximately the top 1% of distributors in Wisconsin. Attached to the returns were the federal forms, which revealed a breakdown of revenue and expense information.

Though these were supposedly the top distributors in the state, with an average gross profit of about $12,500, *the average net income after subtracting operating expenses for these 200 top Amway distributors was about minus $900.* (Obviously those who profit must be much higher in the hierarchy of participants than the top 1% - and not living in Wisconsin) This information was reported on the nationally televised "60 Minutes" show.

It should be noted that had the costs of all Amway products that were consumed or given away as gifts – but which were required to qualify for commissions and advancement in the scheme –
been subtracted, the net losses could have been much higher.

Mr. Craig recalled that a couple of distributors may have grossed $50,000, with actual net income after expenses that would have exceeded a minimum wage for the time spent on their Amway "business" – but far below the income suggested at Amway "opportunity meetings." *Approximately two distributors who operated profitably out of 20,000 total distributors yields a one in 10,000 ratio – decidedly uneconomic.*

The Utah tax study. In 2004, I personally telephoned 99 tax preparers in four Utah counties, three of which were rural counties with no MLMs (MLM companies) headquartered in their boundaries. So I felt it was a safe assumption that few if any TOPPs (top-of-the-pyramid promoters), or "kingpins," would live in those counties. None of the 33 tax preparers could remember anyone reporting a profit on their income taxes from participating in MLM, for any length of time, even though an earlier randomized survey of Utah consumers showed that approximately 21% of the population had at some time been involved in MLM.

Then I called 33 CPAs who perform tax preparation in Utah County, in which is located the highest concentration of MLM company headquarters in the country – now over 25 MLMs. While they could not reveal specific amounts, collectively these CPAs could recall 35 clients who made large sums of money from MLM. These of course were TOPPs who lived close to company headquarters and (I assume) used CPAs because the income amounts were so large.

The average net income (after subtracting expenses) for the 200 top Amway distributors in Wisconsin was approximately <u>minus $900.</u>

I called another 33 tax preparers in Utah County who were not CPAs. From these, an additional five tax filers were reported to have very large incomes from MLM participation – likely also TOPPs. These results strongly support what the rest of this chapter will show – that most of the money goes to TOPPs at the expense of a revolving door of unwitting new downline recruits who try an MLM program and quit, only to enrich the TOPPs with commissions from the purchases they made in a vain effort to "succeed."

Disclosure of information supporting Income claims – so crucial for consumer protection – is vigorously resisted by the MLM industry.

Since the income claims of MLMs touted by their promoters are at the heart of the legitimacy of their programs, it is important to disclose the truth about average earnings so that prospective recruits can have valid information upon which to base their decisions on whether or not to participate.

So far, regulatory agencies have not required honest and understandable disclosure of essential information to MLM prospects. I have examined the compensation plans of hundreds of MLMs and found that virtually all hide the near-zero odds of making a profit, and in fact almost certain loss after subtracting purchases of products necessary to qualify for commissions and advancement in the pyramid of participants. It is no wonder that MLMs and their chief lobbyist, the DSA, vigorously resist transparency regarding income claims to protect consumers.

It is no surprise that recent efforts by the FTC (Federal Trade Commission) to get business opportunity sellers to disclose average earnings has been met with fierce resistance from MLMs and their primary lobby, the DSA (Direct Selling Association). This by itself should be a red flag signaling something very wrong with MLM as an *industry and/or as a fundamental business model.*

The DSA/MLM lobbyists argued that handing out a one-page disclosure of average earnings, criminal background of leaders, and references, etc. prepared by the company would be an "intolerable burden" for direct sellers. FTC personnel should have seen this as a blatant effort to avoid consumer protective transparency. It is actually quite absurd, especially since franchisors are required to furnish a disclosure document to prospects that is often hundreds of pages long.

Handing out a one-page disclosure document to prospects – an intolerable burden?

It should also be noted that the average earnings data that has been disclosed by a select few MLMs (whether mandated or not) appears to have been cleverly designed to mislead prospects and regulators. So in my opinion, it is imperative that the deceptions be identified and a more true portrayal of average earnings be made available. I will also endeavor in this chapter to provide a set of procedures for any qualified analyst to use to replicate my findings.

MLM compensation plans assume an infinite market and a virgin market, neither of which exists. MLM is therefore inherently flawed, unfair, and deceptive. MLMs are also extremely viral, predatory, and harmful.

Inherent flaws in MLM

In prior chapters, the flaws in the MLM as a business model were discussed. In a nutshell, MLM is predicated on the recruitment of an endless chain of participants as primary customers. *MLM compensation plans assume an infinite market and a virgin market, neither of which exists in the real world. MLM is therefore inherently flawed, unfair, and deceptive.*

From analyses of the compensation plans of hundreds of MLMs, I have found a consistent pattern of pay plans that are recruitment-driven and top-weighted, meaning they are driven by incentives to recruit, with company payout of commissions going primarily to founders and a select few "TOPPs" (top-of-the pyramid promoters) who are usually those who were positioned at the beginning of the recruitment chain.

The fundamental flaw in MLM is the endless chain of recruitment of participants as primary customers. MLM pay plans assume infinite markets and virgin markets – neither of which exists in the real world.

Worldwide feedback suggests that MLMs are also extremely viral and predatory. They feed on the product investments of a revolving door of new recruits, each subscribing to product purchases to qualify for commissions or advancement in the pyramid of participants. But for almost all newcomers, they are being sold a ticket on a flight that has already left the ground. MLMs can be extremely harmful, causing huge losses for those who invest the most in the schemes.

Assuming all this were true, we would expect to see it reflected in the average earnings of participants in MLM programs. And that is precisely what I will examine in detail.

How can the odds of profiting from an MLM be calculated?

Statistics of average earnings that have been provided by MLMs are laden with obfuscation and deception, apparently to avoid revealing the abysmal odds of success for new recruits. But careful analysis can lead to a more accurate picture of profitability (or loss rate) for those considering a particular MLM. I have found that by following the steps outlined here a more truthful assessment can be made. Here is how I would advise persons being recruited into an MLM to estimate the true odds of their being successful, regardless of effort:

Step 1: Obtain average earnings statistics

Obtain from the MLM recruiter the average earnings statistics for the MLM you are examining, showing the average amount of money paid by the company in commissions and bonuses to participants at the various levels in the compensation plan.

Caution: If the MLM won't provide statistics of average earnings, you should consider that a red flag, as it would for anything promoted as a “business opportunity” or “income opportunity.”

Step 2: Determine total incentivized or “pay to play” expenses – and other purchases expected of participants.

From the compensation plan, determine the minimum incentivized or “pay to play” purchase requirements. In other words, how much in products and services will you be expected to purchase (even if supposedly for resale) in order to qualify for commissions and bonuses, and to advance up the various levels in the pay plan.

TOPPs for many MLMs expect downline participants to pay for training, conferences - and books, recordings, sales literature, and other “tools” needed to be successful.

For the MLMs I examined, incentivized or “pay-to-play” purchases ranged from $50-$500 a month. I usually discover at least “$100 a month as a minimum figure for incentivized purchases.

Caution: Avoid falling for the ruse that you don’t have to purchase anything, or that you can sign up just to get the products at a discount. If you listen carefully to the pitch of the MLM recruiter, it should soon become clear whether they are selling the products, or the opportunity. If the latter, it is deceptive to sell you on signing up so you can buy products. Ask this question: “Is this a buyers’ club - or an opportunity chain?”

Step 3: Try to find out the average total amount of money paid to the company by participants.

If the company will provide it, you should also get the average of the total amount of money paid to the company by participants at each level for products and services purchased from the company. I have found this to be an important piece of information that MLMs have been unwilling to provide, though it is crucial information, since prospects have a right to know the likelihood they will lose money or come out ahead. Even if – as MLM promoters claim – it was not possible to get total operating expenses, average amounts of money paid in to the company per participant should be readily available.

Determine as much as possible what other costs may be involved, such as training meetings, “tools” (books, web site, CD.s etc.) sold by TOPPs (or upline promoters) that they are selling to assure the “success” of downline participants.

Caution: Avoid falling for the line that purchases that you make for their own use are purchases you would have made anyway and therefore should not count. Typically, similar products can be purchased for a small fraction of the price from alternative sources. And purchases are seldom continued after participants terminate.

The point that you want to determine is how many people come out ahead financially from their participation. The formula for profitability is very simple – money paid by the MLM to participants less money paid to the MLM by participants. As will be seen, our calculations show the balance is nearly always negative, meaning a net loss for participants. And it is even worse if you subtract operating expenses. More on that later.

Caution: You should not assume you can sell the products at a heightened “retail” price to others, as promoters claim is possible. Our extensive research and feedback leads to the firm conclusion that such re-selling by MLM participants is only a very minor portion of product sales. Typically, MLM products are far too expensive to compete with products purchased from standard retail outlets. (See Chapter 4.) “Direct selling” by MLM participants to non-participants in significant volume is a myth promoted by well-paid MLM company and industry communicators. Exceptions to this are “sympathy buyers” – friends and family that may purchase the overpriced products out of sympathy for participants. As with participants, such purchases usually cease when the participant leaves the MLM.

However, if an MLM promoter insists that significant retail selling is going on, ask for proof in the form of receipts. If it were a legitimate direct selling operation, sales to non-participants would be many times the amount of sales to participants.

Caution: Avoid accepting uncritically the MLM promoter’s claims that the products have magical properties that will heal or prevent every disease on the planet and that they can only be obtained through this particular MLM. Many MLM promoters claim to have the latest and greatest “pills, potions, and lotions” – or the best and most unique of some other products or services. Note the ingredients and shop around for at least comparable products through other outlets – you will be surprised at what you can save. (Again – see Chapter 4.)

Step 4: Obtain – or estimate – the company’s attrition/retention rate

Prospects should ask their recruiter to furnish the company’s attrition (dropout) rate; i.e., the percentage of recruits who sign up only to drop out within a year – and over a five or ten-year period. If they can’t or won’t furnish it, you can assume that it exceeds the minimum of 50% per year, which we have found where such data is available. Over a five-year period, at least 95% typically have left the company; and usually after ten years, nearly all but those at or near the top of their respective pyramids will have dropped out.

At the very least, you can assume that 90% of participants will terminate within five years, and at least 95% within ten years. This is useful to know, since MLM's published average earnings reports will often include top-level participants who were there from the beginning – which may be ten years or more. To be statistically valid, all dropouts and terminations should be included for the same period as for those participants included at the top levels.

If any company challenges the assumption of attrition of 90% for five years, and 95% for ten years (or retention rates of 10% and 5% respectively), ask company officials for data to prove otherwise. To my knowledge, no recruitment-driven MLM has been able to show less unfavorable attrition statistics than these. (For important information on attrition rates, see Chapter 6.)

Caution: Don't accept an MLM’s statistic for the total number of "active" distributors or participants as the base used for calculating what percentage of participants succeeded in rising to the various levels. Again, if the "successful" participants who have been with the MLM for ten years are counted, then every person who signed on with the program during that same ten-year time period. should be counted in calculating success rates - whether they are active, inactive, or terminated. *The MLM practice (endorsed by the DSA) of comparing only currently "active" participants (most of whom have been there only a short time) with "successful" participants who have been there for many years, greatly skews the numbers in their favor - a <u>huge</u> deception.*

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Step 5: Obtain – or estimate – minimum operating expenses needed to conduct a successful recruitment campaign.

Estimate minimum operating expenses necessary to successfully recruit. It is true that most MLM participants purchase a few products, find recruiting and selling very tough, and then quit without spending much money. But my analysis of hundreds of MLM compensation plans convinces me that *participants rarely – if ever – move into the profit column without an aggressive recruitment campaign carried out over a period of time.*

In 1994-5, I put Nu Skin, a leading MLM program, to the test for a year, devoting all my time to climb to the top 1% of participants (counting ALL participants, including dropouts). During that year I kept careful records of my spending and wound up with expenses of over $1,500 per month including products and services from the company, plus all operating expenses, such as travel, telephone, computer supplies, advertising, meeting rooms, etc. My commissions totaled only about $250 a month, netting an annual loss of approximately $15,000.

I included incentivized purchases in the amount spent on products and services, even though some or most were personally consumed or given away. This is because these are purchases necessary to qualify for commissions or advance-ment in the scheme. Some may not be treated as a deduction for tax purposes, but they should be considered as a cost of doing business for analytical purposes – especially if the participant would not have made the purchases were he/she not intending to advance in the scheme in some way.

Important note: The $18,000 ($1,500/mo.) operating expense figure would be equivalent to well over $25,000 in 2008 dollars (the year for the report in Exhibit 1). So as a reasonable assumption based on my experience, in typically saturated U.S. markets I would estimate a bare minimum of $25,000 in total expenses to mount an effective recruitment campaign today, which is essential for any hope of success in a typical recruitment-focused, top-weighted MLM program. This is a conservative figure, and the figure could be several times that for TOPPs who must frequently travel, rent meeting facilities, etc., in order to recruit sufficient new recruits to replace those who are continually dropping out. Also, many costs have increased since 1994, along with new recruitment resources, such as maintaining a web site.

Caution: *MLM promoters and the DSA, often claim that many or most participants just work part time for a little cash to supplement income, to meet Christmas expenses, etc. This is one of their biggest deceptions. Profitability in MLM does not come cheaply or easily*. It's very costly and time-consuming, and compensation plans require consistent effort over time to advance in any MLM scheme. Based on the foregoing, I feel confident in my conclusion that part-timers and seasonal participants are not profiting, but are merely contributing to the coffers of the company, founders, and TOPP's.

Part-timers and seasonal participants are not profiting, but are merely contributing to the coffers of the company, founders, and TOPP's.

Tax studies and analyses of reports of average incomes (assuming minimal expen-ses are subtracted) show that few ever earn a profit from MLM participation, with the notable exception of those who arrive at or near the top of their respective pyramids – who may make a lot of money, often millions of dollars – harvesting commissions from purchases of hopeful new recruits beneath them.

Caution: Don't accept the argument by promoters that success in MLM recruitment costs little or nothing. New MLM recruiters will soon start getting the cold shoulder from friends and relatives and have to recruit elsewhere. Again, anyone who climbs the ladder in the compensation plan must spend not only a great deal of time, but a considerable amount of money to be successful.

Step 6: Calculate the profit/loss rate

Now put it all together. This means debunking the figures supplied by the company by including ALL who signed up during the same period during which those who "succeeded" are counted – and then subtracting expenses as explained above. Even if you just go back five years, you can multiply the MLM company's published success rate by a factor of 0.10 (retention rate with 0.90 attrition rate) to get a success rate much closer to the truth. Then select all distributors who earned enough to have exceeded the break-even point; i.e., incentivized or "pay to play" purchases plus estimated operating costs. Again, don't assume resale of products at heightened retail prices unless they can show you the actual sales receipts to prove it.

The case of Nu Skin – responding to an FTC Order to cease its misrepresentations

Exhibit 1 is extracted from a report of 57,998 "active distributors" in the U.S. for Nu Skin Enterprises[1], a leading MLM company which was ordered to cease its misrepresentations of distributor earnings in 1994 – and has since then periodically provided average earnings data. We will show you how to interpret these numbers and then apply the same procedures to other MLMs.

Cautions: Great care must be taken in reading these numbers in this report. Note these deceptive techniques used to mislead readers:

➤ Quarterly commissions are given and then the figures are annualized. Since many terminate before a year is over, this *annualized* number could be much higher than *annual* figures. But we'll give them the benefit of the doubt.

➤ Percentages are presented in a way to make the odds appear much higher than they are, especially if we assume 90% dropout rate over 5 years, or 95% over ten years - an optimistic assumption, based on actual statements by Nu Skin. Since the company was 24 years old when these 2008 statistics were reported, and the top earners (Blue Diamonds) in the U.S.A. have been there for well over ten years, it is reasonable to use the ten-year figure. *Using these assumptions, the number of people achieving Blue Diamond status would then be 0.14%, or 0.0014. Then, 0.0014x 0.05 (5% remaining after 10 years) equals 0.00007 – which looks a lot less than the reported ".14%".*

➤ Minimum pay-to-play in this program is $100 a month, or 1,200 a year – in order to qualify for commissions. This is not included in the report, as it should be. Only a small percentage of distributors would earn enough in commissions to exceed this amount.

➤ Add to the $1,200 the operating expenses needed to conduct a successful recruitment campaign, which the author found to be absolutely essential to climb the hierarchy of distributors. In my one-year test of the Nu Skin program, the minimum total expenses to recruit successfully was over $18,000 per year (well over $25,000 in 2008 dollars), including products and services from the company, travel and telephone expenses, home office and rooms for opportunity meetings, printing and duplicating expenses, advertising, telephone and computer expenses, and miscellaneous supplies. (For a more complete account of my Nu Skin experience, read Chapter 1.)

Sample calculations, using Nu Skin data:

Step 1: Average earnings statistics are published by Nu Skin, as shown in the table in Exhibit 1 and labeled "2008 Distributor Compensation Summary."

Step 2: "Pay to play" purchases have for years been at least $100, with many times that amount (in group volume) required to qualify for Executive status, the

[1] "2008 Distributor Compensation Summary" published by Nu Skin, which is posted on the Nu Skin web site. The report is updated periodically, but for each year we see the same pattern of extreme concentration of payout to Blue Diamonds at the top.

lowest “pin level” in the pay plan. In addition, the company and its “Blue Diamonds” (“TOPPs”) encourage partici-pants to make additional purchases of a wide range of products and services – and to pay for training and opportunity meetings to enhance their “success.”

With the odds of profiting being about one in 3,922, it is more appropriate to call MLM programs like Nu Skin a “loss certainty” than an “income opportunity.”

Step 3: Data on average amounts of money paid by participants to Nu Skin is not provided.

Step 4: Nu Skin has been in business since 1994, and several of the Blue Diamonds included in the report have been with the company for more than ten years. So – based on the information in Chapter 6 – we can use 95% as the attrition rate.

Step 5: I found from my one-year test of the Nu Skin program that to conduct a successful recruitment campaign is expensive. Including products and services from Nu Skin, I spent over $18,000 (at least $25,000 in 2008 dollars), and others at higher levels were spending considerably more than that.

Of course, Blue Diamonds at Nu Skin claim that good money can be made just selling products to friends, neighbors, etc. This deceptive claim has been discussed in chapter 4. The compensation plan for Nu Skin, like for the hundreds of other MLMs I have analyzed, is heavily weighted towards building a huge downline in order to get to where profits are even possible after expenses, including pur-chases from Nu Skin.

So I am completely comfortable placing the breakeven bar (the amount above which profits are possible after subtracting costs) at $25,000 per year, allowing for cost of living adjustments (Chapter 5).

Step 6: Based on the above, only those achieving status of Ruby and above were likely (on average) to have risen from a net loss to actual net profits, since all those beneath do not earn enough in commissions to meet expenses of $25,000 a year. In actual fact, however, since these are only averages, it is highly likely that many below Diamond

Exhibit 1: Average earnings statistics for Nu Skin Enterprises, Inc. – Extracted from Nu Skin's "2008 Distributor Compensation Summary"

Average number of "Active Distributors" in the United States during 2008 – 75,710

Commissions paid to distributors in the United States in 2008 – approximately $107,686,324

Average commissions paid to U.S. Active Distributors $1,421.75 on an annualized basis.

On a monthly basis, an average of 13.11% of U.S. Active Distributors earned a commission check.[2]

Active Distributors represented an average of 40.71% of total distributors" [of record][3]

How data are presented by Nu Skin Enterprises, Inc.

	Monthly Average Commission Income at Each Level for 2008	Annualized Commissions[4]	Average Percentage of Active Distributors[5]	Average Percentage of Executive and above level distributors
Active Distributor earning a check (non-Executive)	$62.00	$744.00	7.89%	N/A%
Qualifying Executives	228.00	2,736.00	1.29	N/A
Executives	441.00	5,292.00	2.96	59.9
Gold Executives	800.00	9,600.00	.93	18.9
Lapis Executives	1,405.00	16,860.00	.53	10.8
Ruby Executives	2,860.00	34,320.00	.19	3.8
Emerald Executives	5,634.00	67,608.00	.09	1.8
Diamond Executives	9,520.00	114,240.00	.08	1.7
Blue Diamond Executives	42,710.00	512,520.00	.15	3.1

[2] This number is calculated by adding the average percentage of Active Distributors in the above table.
[3] This percentage is obtained by taking the total average of monthly actives and dividing it by the total average of Distributors on a monthly basis. "Total Distributors" includes all U.S. Distributor accounts currently on file, irrespective of their purchasing products,
promotional materials or services or earning commissions. "Distributor" numbers do not include customer or Preferred Customer accounts.
[4] These numbers are calculated by taking the monthly average commissions and multiplying by twelve. The column labeled "Monthly Average Commission Income at Each Level for 2008" has been deleted, as it is irrelevant to this analysis.
[5] These percentages are calculated by taking the total monthly Distributor/Executive count and dividing it by the total number of monthly Active Distributors. One must then add the average percentage of Active Distributors at each level for each month during 2008 and divide by twelve. The column labeled "Average Percentage of Executive-and above level Distributors" has been deleted, as it is irrelevant to this analysis.

Exhibit 2: Data with highlighted information that is important for prospects to know, but which is not disclosed in Nu Skin's report

Title	Annualized Commissions[6]	Average % of Active Distributors[7]	Number of Distributors at that Level	Company Payout by Level[8]	% of Co. Payout by Level[9]
Active Distributors not earning a check	**$0**	**85.89%**	**65,027**	**0**	**0%**
Active Distributors earning a check (non-Executive)	$744	7.89%	5,974	$4,444,298	4.15%
Qualifying Executives	$2,736	1.29%	977	$2,672,139	2.49%
Executives	$5,292	2.96%	2,241	$11,859,457	11.07%
Gold Executives	$9,600	0.93%	704	$6,759,389	6.31%
Lapis Executives	$16,860	0.53%	401	$6,765,294	6.31%
Ruby Executives	$34,320	0.19%	144	$4,936,898	4.61%
Emerald Executives	$67,608	0.09%	68	$4,606,742	4.30%
Diamond Exec's	$114,240	0.08%	61	$6,919,288	6.46%
Blue Diamonds	$512,520	**0.15%**	**114**	$58,204,334	**54.31%**

Actually, it is even far worse than these numbers show, because dropouts are not included for the same period as the period of activity for those at the higher levels who have stayed with the company. We will address this issue below.

Ruby and above – 0.51%, or .0051 could have profited after expenses – not counting dropouts
Corrected for 5% retention – .0051 x 0.05 = 0.000255, or 0.0255%, or **1 in 3,922 recruits who could have profited.**

Thus, the loss rate is 1- 0.000255, or 99.997%. Rounded off, virtually 100% of recruits lose money.
Subtract Blue Diamonds, and the loss rate for everyone else is calculated as follows:
Ruby to Diamond – 0.36%, or .0036 x 0.05 = 0.000165, or 0.0165%, or **1 in 6,061 recruits could have profited. A much smaller percent could have achieved significant profits (well above minimum wage).**

114 Blue Diamonds x 512,520 = $58,427,280
$58,427,280/$107,686,324 = **54.3% of total company payout is paid to the Blue Diamonds** (TOPPs), who comprise only a very tiny percentage of distributors (0.000075, or 0.0075%)

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[6] These numbers are calculated by taking the monthly average commissions and multiplying by twelve. The column labeled "Monthly Average Commission Income at Each Level for 2008" has been deleted, as it is irrelevant to this analysis.

[7] These percentages are calculated by taking the total monthly Distributor/Executive count and dividing it by the total number of monthly Active Distributors. One must then add the average percentage of Active Distributors at each level for each month during 2008 and divide by twelve. The column labeled "Average Percentage of Executive-and above level Distributors" has been deleted, as it is irrelevant to this analysis.

[8] Calculated by multiplying the "Average Percentage of Active Distributors" (first column) by 75,710 (total U.S. distributors), then multiplying that number by Annualized Commissions" (first column). Added to table by author.

[9] Calculated by dividing number from prior column by total commissions paid by Nu Skin in 2008. Added Added to table by author.

Additional conclusions that could be extracted from Nu Skin data

Eliminate TOPPs from the calculations of average earnings. In the fourth column of Exhibit 2, I have calculated the total payout by the company to all participants at each level, and in the fifth column is shown the percentage of total payout paid to each level. The average for this column reveals a startling fact – 54.3% of company payout goes to only 114 Blue Diamonds – out of 75,710 current distributors, not including over a million who dropped out in the past ten years.

Because over half of company payout to Nu Skin participants goes to Blue Diamonds, or TOPPs (top-of-the-pyramid promoters), the results for averaging purposes are extremely skewed to make averages appear larger than they really are for the vast majority of participants. A more useful calculation of average income would exclude these TOPPs
from the calculation.

Assuming you subtract only $1,200 minimum "pay to play" purchases is substracted for each "active Blue Diamond distributor (not counting operating expenses), *the average net income/loss per participant for the year is figured as follows:*

$107,686,324 total distributor payout less $58,204,334 to Blue Diamonds = $47,658,648

75,710 – 114 Blue Diamonds = 75,596 distributors

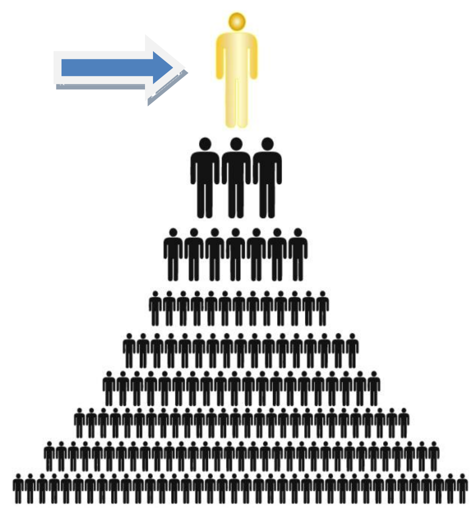
$47,658,648 / *75,596* = $630.44 average com-missions per distributor.

– (subtract) $1,200 "pay-to-play" purchases = average of *minus $559.66 per distributor – and a far greater loss if you subtract operating expenses.*

"**Residual income" far more elusive than just "profits."** But how many earn the large "residual income" bragged about by Nu Skin promoters? (Minimum operating expenses would be much higher for levels higher than Executives.) We could speculate what level would pay enough after heavy recruiting expenses to constitute a significant income as TOPPs often suggest can be earned.

My close observation of Nu Skin's top promoters when I was involved tells me that no one below Diamond level would be netting enough to qualify as significant income, and they constitute only 0.0008 of Active Distributors, or 0.00004 of all distributors over a ten-year period. Therefore, after eliminating Blue Diamonds, or TOPPs, at best *only one out of every 25,000 recruits could have received the "residual income" touted by Nu Skin promoters.*

Most of the incentives are paid to Blue Diamonds, or TOPPs (top-of-the-pyramid promoters.) I'd color him blue if I could.



Eliminating Blue Diamonds, or TOPPs (top-of-the-pyramid promoters), from the calculation removes some of the statistical skewing, since most of the money paid by Nu Skin to hundreds of thousands of (present and past) distributors goes to just 114 Blue Diamonds. (This visual is used only to illustrate a point, not to show the details of Nu Skin's pay plan.)

All three statistical measures of averages are abysmal for Nu Skin (and other MLMs). There are three statistical measures of averages:

(1) the <u>arithmetic mean</u>, which would be the total amount divided by the number of participants,

(2) the <u>mode,</u> which is the number that appears most often, and

(3) the <u>median</u>, which is the figure that falls in the middle of the entire range of participants.

It is clear from a careful study of Nu Skin's own data that <u>the mode and the median are zero, and the arithmetic mean is a large minus figure</u>. To call Nu Skin (or any other MLM) an "income opportunity" or "business opportunity" is a major misrepresentation.

. . . the mode and the median are zero, and the arithmetic mean is a large minus figure. To call an MLM like Nu Skin an "income opportunity" or "business opportunity" is a major misrepresentation.

Results when backing off on assumptions. Even if an analyst accepts the MLM/DSA arguments that costs of participation and rate of attrition is far less than those used in this analysis, the results are not favorable for Nu Skin participation.

Let us assume that recruitment is much easier than I experienced (in a more virgin market, for example) and that total costs of incentivized purchases and of the recruitment campaign were only half of $25,000, or $12,500.

We might also assume that attrition was only 90% over ten years (a highly unlikely assumption and one that could easily be debunked if honest attrition data from Nu Skin was made available). Even with these assumptions, the loss rate would be high.

Lapis distributors and above exceed $12,500 in commissions. Total percentage of distributors at levels of Lapis and above is 1.04%. And if 10-year attrition is 90%, retention is 10%.. Therefore, 0.0104 x 0.10 = <u>*0.00104, or 0.104%.*</u> *This means that less than 1/10 of 1% of distributors would have earned a profit – even with such liberal assumptions in Nu Skin's favor!*

. . . less than1/10 of 1% of distributors would have earned a profit – even with such liberal assumptions in Nu Skin's favor!

I should remind readers that I rose to Executive status and almost to the level of Gold Executive, placing me well in the top 1% of distributors (assuming all recruits for a given time period are included). Yet I was losing over $1,000 a month. Based on my personal experience and observations, as well as the Utah tax study (Utah is where Nu Skin is based) I seriously doubt that anyone below Emerald Executives were reporting a profit on their taxes from participation in the Nu Skin program.

:

My personal experience with Nu Skin. As I mentioned above, in 1994 I was heavily recruited into Nu Skin and finally decided to join and give it my all for a year to test its validity. Obviously, I would never have joined had I any idea these numbers were so abysmal – and neither would anyone else who had a rudimentary math background.

On the other hand, my Nu Skin experience was the beginning of a journey of discovery into the deceptive world of multi-level marketing. It has taken me years to fully debunk the many deceptions inherent in these schemes. Fortunately, my wide experience as a home entrepreneur, graduate business education, analytical and research skills, and desire to get at the truth have yielded this rich outpouring of key information which can be used to provide some consumer awareness where law enforcement agencies have failed to meet this challenge.

Perform your own calculations.

Of course, anyone is welcome to challenge my calculations, although I believe they are as accurate as could be performed, given the deceptively presented reports of the MLMs I was able to gather. For obvious reasons, none presented their information in a format that made it easy to see how unprofitable their programs were.

A person considering an MLM program would be wise to take the information furnished by the company and perform the same calculations as those done here with Nu Skin. If the company is unwilling to disclose average income data and percentages for the various levels, consider this a red flag in itself.

These conclusions on abysmal loss rates apply to all recruitment-driven MLMs for which we were able to obtain data.

Proponents of some MLM programs will likely argue that “while the numbers for Nu Skin (and other MLMs) are horrible, our particular MLM is “different. In fact, we offer one of the most generous compensation plans in the industry.” I have heard this type of argument so often, that it seemed important that I and those assisting me spend considerable time gathering average earnings data from as many MLMs as would provide such data, however skewed (as explained above). The 30 MLMs for which we have obtained sufficient data for income analysis is included in Appendix 7A.

W*ith every MLM, where such data was available, and after debunking the deceptions in their reporting, the loss rate was at least 99%, using liberal assumptions relating to retention and cost of participation, as explained in subsequent sections of this chapter. The average loss rate for the 30 MLMs reported here was 99.6%.*

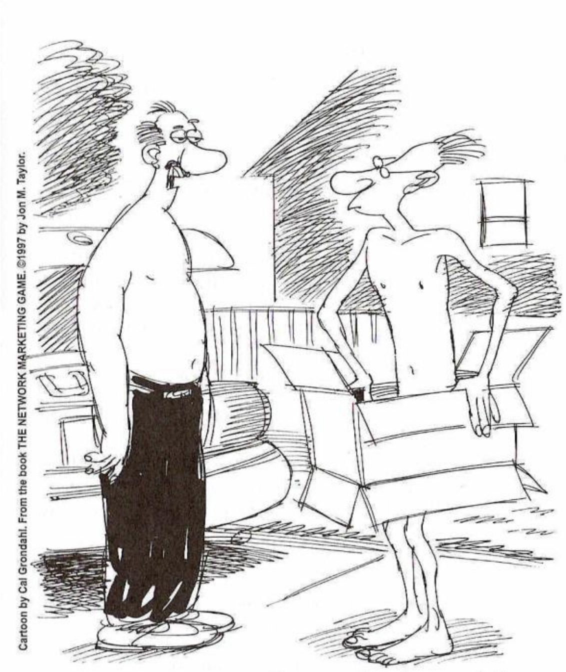
I believe it is safe to assume that MLMs for which promoters do not provide such data are not likely to be more profitable because if they were, at least some would have provided data for competitive advantage. So it is highly likely that others of the 350 MLMs that I have also found to be recruitment-driven and top-weighted would have similar loss rates.

Carrying this logic a step further, since all (100%) of the MLMs for which I have been able to obtain an explicit compensation plan have at least four of the causative and defining characteristics (CDCs) of a recruitment-driven MLM, hundreds of additional MLMs would have these same basic characteristics. This provides conclusive support for considering MLM a fundamentally flawed system.

From all my research and from worldwide feedback, I can say confidently that as a general rule, the more a new recruit invests in an MLM program, the more he or she loses. This, of course, is true of most any scam.

Even though MLM defenders may challenge these figures and assumptions, I have done my best to remove the deceptions in MLM reporting, and I firmly believe my conclusions drawn from this analysis to be as close to the truth as is possible.

As a general rule, the more a new recruit invests in an MLM program, the more he or she loses. This, of course, is true of most any scam.



" I went to Las Vegas and lost my shirt. How's your Network Marketing going?"

Exhibit 3:

Analysis of recruitment-driven MLMs for which we have received earnings data

Based on my analysis of their compensation plans, using the four causal and defining characteristics ("red flags")[10] as a checklist, ALL (100%) of the 30 MLMs included in this analysis are recruitment driven and top-weighted. This means that rewards are paid primarily for the aggressive recruitment of a large downline, not for retailing products; and most of the money paid by the company goes to participants at the highest levels. I have analyzed the compensation plans of over 350 MLMs and found that ALL (100%) are recruitment-driven and top-weighted, so it seems justifiable to assume that the same results could be expected for other MLMs.[11]

NOTE: These calculations are based on actual company reports and the best independent analyses used by the author, as explained in the preceding chapters. Of course, anyone is welcome to perform their own calculations, but calculations using assumptions by those in the industry should be questioned. As in other reports I have prepared, the same legal disclaimer applies. *Note also that I am giving these MLMs the extreme benefit of the doubt, using only 10% of the amount of total costs of purchases and operating expenses in my one year test and doubling the retention rate for 10 years and increasing by 50% the retention rate for five years.*

MLM company and year of average earn-ings report[12]	**Estimated min. annual costs for effective recruitment campaign.**[13]	**Level at and above which net profits possible**[14]	**Approx. % of active participants at that level or above** [15]	**Maximum retention rate** [16]	**Approx. % of all partic's that could have profited from participation**[17]	**Approx. % of all partic's who lost money**[18]
Advocare (2009)[19]	$2,545	Silver	9.23%	10%	0.92% (0.009) – or **1 in 111 profits**	**99.1% lost money**
Ameriplan (2008)[20]	$2,545	SRSD	7.5%	10%	0.75% (0.0075) **– or 1 in 133 profits**	**99.25% lost money**
Amway/Quixtar (2001)[21]	$2,090	Platinum (no "pins" below)	1.02%	10%	0.1% (0.001) – **or 1 in 1,000 profits**	**99.9% lost money**

For the full table of 30 recruitment-driven MLMs that were analyzed, go to Appendix 7A.

10 See Chapter 2 for these characteristics ("red flags") – also the full report on web site – mlm-thetruth.com
11 We have average income data for other MLMs besides these 29, but without adequate data to do this analysis.
12 The most recent report available to the author at the time of the analysis.
13 Minimum costs of conducting a successful recruitment campaign, based on the author's one-year test of a leading MLM. Costs includes incentivized purchases plus minimum operating expenses, corrected by COL (cost of living adjustment, based on Consumer Price Index) since the MLM's founding – See chapter 5. Here we use the extremely liberal assumption that total costs were only 10% of those of the author.
14 Estimated average net profits assume all expenses (including incentivized purchases and minimum operating expenses) are subtracted from income. This is the "pin level" at and above which profits would be possible.
15 Referring to the level in the previous column – per MLM company reports
16 See chapter 6 for how approximate attrition (and retention) rates for MLMs are estimated. The inverse of attrition is retention, which is used to estimate the percentage who could profit. Retention is estimated to be a maximum of 10% if in business for four to nine years, 5% for ten or more years. However, for this report, we use the liberal assumption of15% for four to nine years and 10% for ten or more years.
17 Average income exceeding all expenses for conducting a successful recruitment campaign.
18 In calculating percentage who lost money, those who dropped out are included. This is assuming that participants who had arrived at such a high "pin level" that they were profiting would stay in the program – since they enjoy the "residual income" that promoters imply at opportunity meetings is possible and a highly prized goal.
19 "2009 Income Disclosure Statement" - published by Advocare
20 "AmeriPlan Independent Business Owner Income Disclosure Statement for 2008" - published by AmeriPlan
21 "Average Annual Income for IBO's in North America, 2001 Average Annual Earnings in U.S. Dollars." ©2002 Quixtar, Inc.

Why the breakeven point for expenses is so high before MLM participants can net any profits

Recruitment expenses are significant. In the above and subsequent analyses, the minimum operating expenses – about $25,000 – for MLM participation assume that the person is conducting an aggressive recruitment campaign such as I found necessary to climb the hierarchy of distributors at Nu Skin. Of course, MLM defenders will argue that it is not necessary to do this and that it is a matter of choice whether or not one elects to be a "business builder," to just sell products to meet more modest goals, or even to merely be a customer of the products because they love them so much.

Review of rationale for high breakeven figure. In case a reader missed some critical information in this and prior chapters, I will reiterate some important findings in my research that justify such a high breakeven bar for those seeking to calculate the percentage of participants who gain or lose money – and average amounts of profits or losses at the various levels. Let's review these findings.

First, based on extensive comparative research, I identified the four causative and defining characteristics of recruitment-driven MLMs, or product-based pyramid schemes.[22] (A fifth characteristic applies to most, but not all.) These are characteristics (or "red flags") that clearly separate recruitment-driven MLMs from legitimate direct selling programs or any other business format or model. Coincidentally, these are the very same characteristics that lead to such huge loss rates for the continuing stream of new recruits who iinvest in the program and drop out, only to further enrich those at the top.

Second, I was able to establish an amount of minimum operating expenses for conducting a successful recruitment campaign[23] from my one-year test of the Nu Skin program. Unless one were recruiting in a virgin market (outside the U.S.), I can assert that it would not be possible to recruit successfully for much less than that, and in fact it is likely much more expensive for those at the higher levels in the hierarchy of distributors.

Third, using these defining characteristics, I was able to analyze the compensation plans of over 350 MLMs. (See Appendix 7B.) In every case, I found that the plans reward primarily those who recruit large downlines of participants; i.e., the "TOPPs" (top-of-the-pyramid promoters). All of the MLMs could be said to be recruitment-driven and top-weighted.

(The only class of MLMs that may be exceptions are in-home demonstration programs, or "party plans," which may reward enough for sales to non-participants to be profitable. I left them out of the analysis, as they are quite different in their approach, and I have not been able to obtain either detailed compensation plans for all levels or average com-missions and overrides paid to participants by the companies. This is not to recommend or excuse such programs. To evaluate a party plan, one would have to obtain a detailed compensation plan and go through the same analysis, factoring in actual validated sales to non-participants.)

Fourth, the MLM compensation plans do not reward those working part-time, seasonally, or with minimal commitment. Except for those initiating the endless chain of recruitment, participants who profit have to climb to a level where commissions and bonuses from the company exceed expenses. This requires aggressive and long-term recruitment, using the deceptive dialog necessary to get prospects to go along with them.[24] Only a tiny few manage to recruit enough people to build a profitable downline.

And finally, the oft-repeated claim by MLM defenders that most new recruits join to get the products wholesale rings hollow if one objectively looks at the prices for MLM products. Comparisons of products sold through MLMs and through retail outlets show huge differentials – often several

22 See Chapter 2
23 See Chapter 5

24 A whole litany of these deceptions are listed in Chapter 8.

times as much.[25] It is an insult to the intelligence of MLM recruits to assume that all those who don't build a downline are merely "customers" because they are sold on the products and don't want to be "business builders." True, some fall for the "unique value of the products" hype of the MLM promoters, and others are buying from friends or relatives out of sympathy for them. But we cannot assume all "inactives" are so naïve as to pay exorbitant prices for products with no connection to the "opportunity."

Based on my analysis of all the MLMs in my research, at best only one in 1,000 achieve a level at or near the top of the pyramid of participants where they could report a significant profit (more than a minimum wage) on their income taxes. And far less earn the amounts of money that are thrown out to prospects at opportunity meetings as possible to attain. Of course, they protect themselves by saying there are no guarantees the new recruits will earn than much. *They would be much more honest saying that it is virtually guaranteed that they will* <u>*not*</u> *earn those huge paychecks – but will in fact* <u>*lose money.*</u>

Even if we assume lower expenses and attrition, loss rates are abysmal.

Even though MLM defenders may argue that in my calculations I exaggerate estimated expenses and attrition rates, when one assumes much lower expenses – even 10% of what I spent - and far higher retention rates of 15% for four to nine years (or 10% for ten years or more, the resulting loss rates are still over 99%. (See Appendix 7A.) And the percentage of participants that achieve the large incomes shown as possible in opportunity meetings are but a tiny fraction of one percent. Probably less than one in 25,000 new recruits will ever achieve the substantial "residual income" touted at opportunity meetings.

25 See Chapter 4

MLM loss rates are not comparable to those for legitimate small businesses, including franchises.

MLM promoters often claim that the failure rates of small businesses is in the range of 90-95%. They say this to excuse the widely recognized failure rate in MLMs. What they fail to do is quote statistics from reliable organizations not affiliated in any way with MLM. So let's debug that myth once and for all.

For example, the SBA (Small Business Administration) found that *44% of small businesses survive at least four years, and 31% at least seven years*[26]*.* Also*, according to the NFIB (*National Federation of Independent Business), *one nationwide survey of small businesses*[27] *showed that over the lifetime of a business, 39% are profitable, 30% break even, and 30% lose money. Cumulatively, according to this study, 64.2% of businesses failed in a 10-year period.*

The following quote from an article in *Journal of Small Business Management*[28] is highly relevant here:

> When aspiring business owners compare the options of franchise versus independent business ownership, an important consideration is the relative risk of business failure. To date, the primary referent for examining franchise failure rates has been surveys conducted by Andrew Kostecka (1988)(1) under the auspices of the U.S. Department of Commerce, which indicate that less than 4 percent of all franchises fail each year. This figure compares favorably with various estimates of independent small business failures (e.g., Dun and Bradstreet 1989).

If only 64.2% of businesses failed (or terminated) in ten years, this totally refutes

26 "Frequently Asked Questions. SBA, Sept. 2008. U.S. Dept. of Commerce, Bureau of the Census.

27 William Dennis, Nat'l Federation of Independent Businesses, reported by Karen E. Klein in Business Week, September 30, 1999.

28 Franchise failure rates: an assessment of magnitude and influencing factors. By Castrogiovanni, Gary J., Justis, Robert T., and Julian, Scott C. (April 1, 1993)

the argument of MLM defenders that "MLM is just like any business. Those who work at it succeed. Most fail because they didn't really try."

My research – and that of other non-MLM analysts – leads to the conclusion that MLM does not qualify as a legitimate business. If less than 1% profit and 95% or more quit in ten years across the entire MLM industry, there must be something fundamentally wrong with MLM as a business model. Incidentally, it should be noted that MLM participants do not qualify for SBA loans, SCORE assistance, or other small business funding and assistance programs.[29]

The fundamental deception of MLM is that of selling it as an "income opportunity" In fact, it is misleading to call MLM a "business opportunity."

For a graphical depiction of how loss rates for small businesses, direct selling, no-product pyramid schemes, and gambling compare with MLM, see Appendix 7C and 7E. Appendix 7E is especially revealing.

While none (of the tax clients) reported profits from MLM participation, over 300 clients reported profits from gambling.

MLM does not offer a part-time or seasonal income option. MLM/DSA defenders, often justify small payments to participants by claiming they are merely seeking part-time income or a little spending money for Christmas or to pay off some debts, etc. But because the rewards in any of the hundreds of MLM compensation plans I have analyzed are heavily stacked in favor of building huge downlines, it is not realistic or even possible to earn part-time or seasonal income from any of them. Again, *part-timers and seasonal participants are not profiting, but are merely contributing to the coffers of the company, founders, and TOPP's*.

How does MLM participation compare with gambling? Comparisons of odds of profiting from gambling with participation in MLM have shown conclusively that participants in many games of chance fare far better.[30] For example, in an earlier analysis, I found the odds of winning from **a single spin of the wheel in a game of roulette** in Las Vegas[31]

- **286 times** as great as the odds of profiting after enrolling as an Amway "distributor."
- **48 times** as great as the odds of profiting after enrolling as a Nu Skin "distributor."
- **22 times** as great as the odds of profiting after enrolling as a Melaleuca "distributor"

Referring to the Utah tax study discussed above, an interesting fact emerged. Wendover, Nevada, is on the border between the two states and a gambling mecca for some Utahns visiting there. I called 16 tax preparers in Tooele County, Utah, which borders Nevada. While *none of them had any clients who reported profits from MLM participation* (6% were active in MLM), they reported *over 300 clients who reported profits from gambling!*

BUSINESS OPPORTUNITY?

29 From SBA (SCORE), banking, and Internet sources.

30 See "Shocking Statistics" report on our web site – www.mlm-thetruth.com

31 Statistics published for Caesar's Palace in Las Vegas, April 6, 2001. Calculations are based on MLM average earnings statistics at the time.

MLM does not qualify as a legitimate business any more than gambling, and in fact gambling is more honest because gambling establishments do not promote participation at gaming tables as a "business opportunity." See Appendix 7 F for a very revealing chart comparing MLM with gambling and with legitimate income options.[32]

Does MLM participation qualify for tax write-offs?

Many MLM promoters tout MLM participation as an opportunity to write off many household and travel expenses as business expenses. But expenses from a business that does not produce profits for more than three years may not qualify for business expense deductions, but are more likely classified not as business losses, but as "hobby losses."[33]

As suggested above, MLM is far less profitable than some games of chance at gambling casinos. Gamblers can only deduct expenses from winnings in any given year.[34]

If MLM losses were treated as "hobby losses" – or in the same way as gambling for tax purposes – the IRS could gain billions in tax revenues it is now losing. Actually, in this sense all of us as taxpayers are paying for this abuse of our tax system promoted by the MLM industry.

Do MLM company stocks make good investments?

Those MLMs that are publicly traded often draw attention to periods of rapid growth unlike other typical stocks for legitimate companies traded on the stock market. Properly understood, this hyper-growth is to be expected of any company using a multi-level or pyramid selling scheme featuring an endless chain of recruitment. They can be extremely viral at the outset, as is true of most pyramid schemes, whether product-based or not. Then they level out or decline as their market becomes saturated. (See Chapter 3.)

This chart (not an MLM) illustrates the typical growth pattern of MLM stock prices – a sharp rise during the momentum phase, followed by a leveling off or decrease.

All of this reminds me of a consultant for a hedge fund who reviewed the data I had gathered on the MLM industry and was astounded at what he discovered. As I drove him back to the airport, he was shaking his head all the way, as he exclaimed something like this:

> Now let's see. This is an industry with few if any real customers (other than participants) and that is totally dependent on a network of tens of thousands of distributors, 99% of whom lose money! How is it possible for such an industry to exist in America?

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[32] Separate pdf file

[33] "Instructions for Schedule C: Profit or Loss from Business"

[34] Ibid

The Network Marketing Payout Distribution Study

In 1999, I gathered the data I had, together with feedback I was receiving from tax accountants, and issued a challenge that continues to this day. I wrote the presidents of 60 of the most prominent MLMs at the time, challenging them to prove me wrong in my conclusions – that network marketing companies were in fact pyramid schemes, with most of the money paid to participants going to those at the highest levels, and everyone else losing money, after subtracting incentivized purchases and minimal operating expenses.

These presidents were supplied forms that could be used to break down money paid out to partici-pants in various percentiles with money they paid in to the company for products and services in order to conduct their "business." My challenge to these executives was to "Prove me wrong" by furnishing this data as requested.

The response from most of these company presidents was interesting. Most did not bother – or dare – to respond. Company communicators from about a half dozen of the MLMs said they would get back to me with a response, but when they ran the challenge by their superiors, the answer in every case was negative. They apparently did not want the truth to get out – which is no surprise, given the damning reality of the numbers, as reported here.

This challenge has been posted since that time on either my web site or on the Pyramid Scheme Alert web site. To this day, no company president has met the challenge. Details of the *Network Marketing Payout Distribution Study* can be found in Appendix 7F (separate pdf file).

These conclusions about MLM are confirmed in other studies.

I am not alone in coming up with these abysmal odds of success for MLM programs. I have already mentioned the Wisconsin study of Amway tax returns. Another revealing study is the "*The Myth of 'Income Opportunity' in Multi-level Marketing*," by Robert FitzPatrick, sponsor of the web site pyramidschemealert.org. He used different assumptions than those used here - not attempting to correct the deceptions in the reporting of the 11 MLM companies he analyzed. But he still concluded – based on the companies' own reports – as follows:

> A statistical analysis of income disclosures made by 11 major multi-level marketing (MLM) companies and the largest of all MLMs, Amway/Quixtar, reveals that, on average, 99% of all participants received less than $10 a week in commissions, before all expenses. Additionally, the report shows that on average no net income is earned by MLM distributors from door to door "retail" sales. . .
>
> The data analyses prove that virtually all MLM participants never earn a profit and that MLM claims of a broad-based MLM "income opportunity" are false. The report reveals that the majority of all commission payments are awarded only to a small group of promoters at the top. More than 50% of all commission payments were transferred to the top one-percent in ten of the eleven companies. In several cases, more than 70% of all commissions were paid to the top one percent. The top-loaded pay plans of the MLM companies are based on "endless chain" recruiting in which the investments of the latest recruits are transferred to the earliest ones, and the vast majority of all participants are always situated at the bottom levels of the chain, where profit is impossible.[35]

Comparing MLM to other options, it is safe to say that that *MLM is the most unfair and deceptive, and the most viral and predatory of all business practices and should be illegal per se, as are pay-to-play chain letters and no-product pyramid schemes.*

Therefore, to promote as a "business opportunity" an endless chain or pyramid selling activity (MLM) that in fact leads to almost certain loss for all but the founders and primary promoters (who are enriched from the purchases of victims/recruits), is a misrepresentation of the facts, and can lead to the defrauding of large numbers of participants. MLM is the epitome of the type of business activity the FTC) is pledged to protect against – "unfair and deceptive acts or practices."

[35] Fitzpatrick, Robert, *The Myth of "Income Opportunity" in Multi-level Marketing,* 2008.

MLM's candlestick income distribution. When I first became interested in the abysmal numbers associated with MLM profit/loss rates, I was struck with a phenomenon I had never seen in decades of analysis of financial and entrepreneurial business models. When I spoke at conferences and workshops for law enforcement personnel, I attempted to display on a graph the distribution of income across the entire spectrum of MLM participants.

On the left of an income distribution chart I would show a tiny few making huge sums of money on the left of the horizontal axis and the balance losing money on the right side. The problem was that no display media was wide enough to display the huge disparity between winners and losers. Those who made money would be less than a half inch in width, while those who lost money (after incentivized purchases and expenses) would spread across the length of the entire building in which we were meeting – if not the whole block.

In the UK's case against Amway[36], this extremely unfair income distribution was aptly described as a "candle stick." The following description by the finder of fact is very revealing. If you have the patience to read it and the statistical background to understand it, you will be rewarded with some very useful insights in just how incredibly unfair MLMs can be. (Conversions from pounds to dollars will vary, but you can still grasp the comparisons from relative size of the numbers.)

> Having set out the structure I turn to my findings of fact as to what, in truth, this structure produces for individual IBOs. The case for the Secretary of State is that the reality of the Amway business is that the nature and rewards of becoming an IBO and participating in that business are such that only a very small number of IBOs make any significant money from their participation. In fact, *the substantial majority of IBOs make no money and indeed by reason of their payment of the registration fee and the annual renewal fees, lose money from their participation.*
>
> In its Points of Defense Amway does not assert that this is not so, nor does it run any positive case. It merely puts the Secretary of State to proof. The Secretary of State proves the case by statistical analysis. For the period from 2001 to 2006 (a) 95% of all bonus income was earned by just 6% of the IBOs; and (b) 75% of all bonus income was earned by less than 1.5% of IBOs. In 2005-2006 there were 39,316 IBOs who shared a bonus pot of £3,427 million. But of this total, 27,906 IBOs (71%) earned no bonus at all, and 101 IBOs (0.25%) shared £1,954 million between them. That leaves a group of 11,309 IBOs to share a bonus pot of £1,473 million. Within that category there was a group of 7,492 IBOs (earning 3% commission) who between them shared £101,400. This gave them an average annual bonus income of just over £13.50, a sum less than the annual renewal fee of £18.00.
>
> (I do not, of course, overlook the "retail margin" earned on product purchased. from Amway and not self-consumed: but *the 3% commission is earned when the monthly points value is 200 PV, so the total retail margin, allowing for self consumption, and even assuming full-price sales, will be low*).
>
> If one were to represent this bonus distribution on a graph with, a central vertical axis containing the commission bands (with 0% at the base and 21% at the top), and the horizontal axis calibrating the number of people in the class, then *the bar graph would resemble not a pyramid but a candle stick, with a large solid base of IBOs who earned nothing or virtually nothing and a thin column of lBOs arising out of it who earned 6 to 2l% commission.*
>
> A feature of that graph would be that the group at the top of the candle would be those who had been IBOs longest. So, Trevor and Jackie Lowe earned a total bonus of £141,000 (having been IBOs since 1979). Of that bonus only £1,788 related to commission on their personal volume (which suggests that they had personally purchased about £8500 worth of product in a year for on-sale to their own customers). £30,000 was attributable to the differential bonus earned on sales made by their down line, and the rest was attributable to the higher awards scheme to which I have referred. The Stranneys earned a total bonus of £59,142. They too

[36] Approved Judgment: The Secretary of State for Business Enterprise and Regulatory Reform v. Amway (UK) Limited May 14, 2008. §42-43

> had joined in 1979. The bonus payable on their personal purchases was £ 1,963. The differential bonus earned on sales by their down line was £15,660. The balance was made up of the higher awards to which I have referred. The Melvilles earned a total bonus of £32,058. They joined in 1980. The bonus earned on their personal volume was £788. The differential bonus earned on sales by their down line was £20,078. The balance was made up of the higher awards. On the other hand *at the base of the candle stick are almost all the recent joiners together with a very considerable number of people who have been IBOs for years, but not made a financial success out of their business.*
>
> The picture can be presented in a variety of ways: but it is consistent. Between 2001 and 2006 the proportion of IBOs not earning any bonus income varied between 69% and 78%. In year 2004/5 only 74 out of 25,342 IBOs earned over £10,000 by way of bonus. In that year only 4,076 IBOs earned enough bonus to cover the annual renewal fee: 21,266 did not even cover
> their most basic running cost from bonus payments (though there may be retail margin).
>
> If very modest business expenses are factored in (say £1 00 on petrol or the purchase of BSM) the picture is even starker, with only 1,820 IBOs making sufficient from bonus payments to cover those expenses and 23,521 IBOs failing to do so. In the period from 2000 to 2005 Chris and Sharon Farrier's bonus-income ranged from £21,495 to £7,971 and averaged £12,850 Over the same period the income of Dr. Anup Biswas ranged from £137 to £433 and averaged £306. *These are the people whose testimonials said respectively that they were earning "the equivalent of good executive size income", or was deriving an income that "continue[d] to climb to replace my full professional salary".*

I would add that – as bad as these numbers are – they do not account for <u>all</u> expenses. So the loss rate is actually far worse than described above. I would also like to emphasize that the extremely unfair distribution of income described above does not apply just to Amway, but to all MLMs for which I have been able to obtain data on average earnings of participants. It is not just a few MLMs that are conducting unfair and deceptive marketing practices, but virtually all of them, as all MLMs are built on a fundamentally flawed system of endless chain recruitment of participants as primary customers.

MLMs are the most unfair and deceptive of all business opportunities, and of all pyramid schemes.

In the original FTC v. Amway ruling in 1979, the “retail rules” supposedly used by Amway to assure that products were sold and not just stockpiled are based on the questionable assumption that even though Amway was structured as a pyramid scheme, retail sales would serve as a mitigating factor to minimize the harm. But since the loss rate is so much higher for product-based pyramid schemes (MLMs) than for classic, no-product schemes, this assumption should be challenged as totally untenable.

In a classic 8-ball (1-2-4-8) no-product pyramid scheme all the money from 14 downline participants goes to the person at the top. Assuming the pyramid schemes continues, that person would leave and recruit another pyramid of participants. Those on the second level of the original pyramid would move up to the number one position, and those on the bottom level would each move up a level in the new pyramid and recruit another two persons for the bottom level. Those at the top would cash out and go on to form other pyramids, in an endless chain of recruitment of new participants into an ever growing number of pyramids. [See Appendix 7C for profit and loss rates for classic, no-product pyramid schemes.]

The inevitable result of such pyramid schemes is that eventually recruitment will dry up as the market becomes saturated or law enforcement steps in and stops it. In any event, when the pyramid ceases, the vast majority of participants are guaranteed be in a losing position at the bottom.

In a typical product-based scheme, or MLM, like Amway or Nu Skin, investments are disguised or laundered through product purchases. Revenues from product sales are channeled through a large infrastructure, with not even half of the money going back to those who generated it. And instead of going to the top person of the 14 participants in a no-product scheme, company payout must be shared with tens of thousands, or even hundreds of thousands of participants – most of it going to those at or near the top levels; i.e., the TOPPs who are the driving force behind product-based pyramid schemes. So only a tiny amount is paid back to lower level participants – almost all of whom lose money.

The loss rate for MLMs is at least 99%. This means that less than one in 100 MLM participants make a clear profit, and at least 99 out of 100 participants actually lose money! In fact, classic no-product pyramid schemes are ten to one hundred times as likely to result in profits as are product-based pyramid schemes, or MLMs.

Thus the loss rates for MLM participants (averaging at least 99.6% as shown in Appendix 7A) is far greater than for participants in classic pyramid schemes, which is approximately 90%.

Put another way, *the odds of profiting from a classic 8-ball no-product pyramid scheme (close to 10% depending on how many continue) is in the range of ten to 100 times as great as the likelihood of profiting from a typical MLM program (less than 1%). MLM is the worst of all classes of pyramid schemes by any measure – loss rate, aggregate losses, or number of victims.* (For a chart comparing no-product with product-based pyramid schemes (MLMs) – and with legitimate income options, see 7F.)

MLM is a mathematical trick played on the unwary. MLM promises significant rewards to those who invest time and money in an MLM program, but delivers losses to all but those at or near the top of a large pyramid (or beginning of the chain) of participants - who profit from the failed investments of those beneath them in the pyramid. As discussed above, MLM's, or product-based pyramid schemes, cause far more harm than other types of pyramid schemes by any measure – loss rates, aggregate losses, number of victims, etc.

Based on figures released by the Direct Selling Association, aggregate losses amount to tens of billions of dollars and are suffered annually by tens of millions of victims worldwide. Of course, the DSA refers to MLM revenues as "sales," when in fact with a 99% loss rate, such "sales" represent losses for the vast majority of participants.

In this regard, the following comment from the trier of fact in the UK's case against Amway[37] is instructive:

> . . . In my survey of the evidence I have recorded some instances of those who did have some success. But *they are the equivalent of one in many thousands. If* the reality of an opportunity is fairly presented, members of the public are free to try and free to fail; and the mere fact that some do fail would not compel the conclusion that the opportunity was not being fairly presented. But if *almost all* do not achieve then I think the inference is fairly raised that the disparity between expectation and experience is arises from a failure to make a fair presentation of the actual (as opposed to the theoretical or exceptional) chance of success.

All of the foregoing supports the obvious conclusion with which any rational analyst would agree. There exists a critical need for adequate disclosure of information crucial to an informed decision by an MLM prospect on whether or not to participate. This will be the topic of the next section.

[37] Approved Judgment: The Secretary of State for Business Enterprise and Regulatory Reform v. Amway (UK) Limited May 14, 2008. §54 (c)

The critical need for adequate disclosure is herein under-scored.

Persons who are considering buying into an MLM are surprised to learn that the numbers are so abysmal. A typical reaction is “I knew that few people make any money, but I had no idea MLM was *that* bad.” Even consumer advocates say that it is far worse than they imagined. And of course, those who have already invested money in MLM are sickened by the awareness of the scam they have fallen into. “If I had only known,” they say.

While the DSA/MLM lobby has mounted a fierce resistance to providing transparency in MLM reporting that could provide some protection for consumers, it should be clear from these studies that adequate disclosure is absolutely essential. The argument the FTC used for exempting MLM in its Revised Business Opportunity Rule was that it would be “too much of a burden” for participants to hand out a one-page document of disclosures to prospects. Apparently anticipating the outcry of consumer advocates, they pledged to deal with MLM abuses by using Section 5 of the FTC Act. The problem is that the FTC admitted to prosecuting only 14 MLM companies in the preceding ten years. Since virtually all MLMs are violating Section 5, as clearly demonstrated here, this would require that the FTC increase its staff at least twenty-fold just to handle the MLMs just commencing, not to mention the hundreds that are still operating.

To present MLM as an “income” or “business opportunity” is misleading.” However, it may be acceptable to sell it as a “buyer’s club,” where participants get to pay *more* for some good – and some highly questionable – products.

A rule requiring adequate disclosure is the only cost effective way for the FTC to handle the hundreds of deceptive MLM programs. This problem was magnified when an FTC administrative judge ruled that Amway was not a pyramid scheme in 1979, assuming compliance with some exculpatory “retail rules,” which have never been adequately enforced – and probably never could be, as they only address behavior of participants, not underlying flaws in the business model - or the compensation plans which actually discourage a retail emphasis.

In one of my many comments to the FTC, I suggested a disclosure form that could be very helpful in making more transparent to consumers what the MLM opportunity was – or was not. For the form I proposed (revised some), see Appendix 7D.

MLMs as “pay more” buyers’ clubs

Perhaps I am too harsh in my judgment of MLM as an unprofitable – even fraudulent – system. Actually, I would be all right with any MLM continuing to operate, so long as its promoters do not present it as an “income opportunity” or as a “business opportunity.” If they want to call it a “buyer’s club,” where participants are told they get to pay *more* for some good – and some highly questionable – products, and that they won’t make any money doing so, that would be fine with me.

Note to persons being recruited by an MLM participant:

If someone tries to recruit you into an MLM, you can save yourself the trouble of researching the MLM and doing all this debugging and calculating by asking the person who is recruiting you to show you his tax returns for the past year. Then ask that others he has recruited in the past couple of years show their tax returns – or some proof that they have earned the promised rewards (less expenses). Be prepared for some blank stares and evasive answers.

Conclusions

This book – especially this chapter – presents the most thoroughly researched independent analysis ever done of the viability and profitability of MLM as a business model. It has been long overdue, as it is information that is vital for consumer awareness and for regulatory rule-making. This would have to include the FTC's Business Opportunity Rule, for which comments received by MLM spokesmen and participants (with the encouragement of MLM promoters) were full of the misrepresentations discussed in this and preceding chapters.

With every MLM, where such data was available, and after debunking the deceptions in their reporting, the loss rate was at least 99%, using liberal assumptions relating to retention and cost of participation. The average loss rate for the 30 reported here was 99.6%. And I believe it safe to assume that the hundreds of MLMs (with the four causative and defining characteristics in their compensation plan)[38] *that do not provide such data are not likely to be more profitable because if they were, at least some would have provided data for competitive advantage.*

This means that at best less than one in 100 participants in all MLMs make a clear profit, and at least 99 out of 100 participants actually lose money! And a much smaller percentage realize the earnings held out as possible at opportunity meetings – which is usually those who joined very early in the chain of recruitment. Newer recruits are being sold a ticket for a flight that has already left the ground.

As indicated above, one can do much better at the gaming tables in Las Vegas. And a person need not risk his or her social capital – treasured relationships with friends and family one has spent a lifetime cultivating. (NOTE: I am not promoting gambling.)

The fundamental flaws discussed in this and prior chapters are confirmed with this analysis. At the very least, it is safe to conclude that MLMs are not legitimate income opportunities. Recruitment-driven MLMs are truly scams.

As a business model, MLM is likely the most successful con game of all time. The very people who are out recruiting are themselves victims until they run out of money and quit. And because victims seldom file complaints, law enforcement rarely acts. It is a vicious cycle, No complaints, no law enforcement action; no law enforcement action, no complaints. So the game goes on.

[38] See Chapter 2.

Appendix 7A: Analysis of loss rates of recruitment-driven MLMs for which we have received earnings data

Based on our analysis of their compensation plans, using the four causal and defining characteristics ("red flags")[39] as a checklist, ALL (100%) of the 29 listed below are recruitment driven and top-weighted programs. This means that rewards are paid primarily for the aggressive recruitment of a large downline, not for retailing products; and most of the money paid by the company goes to participants at the highest levels. We have analyzed the compensation plans of over 350 MLMs and determined that ALL (100%) are recruitment-driven and top-weighted, so it seems justifiable to assume that the same results could be expected for other MLMs.[40]

NOTE: These calculations are based on actual company reports and the best independent analyses available to the author, as explained in the preceding chapters. Of course, anyone is welcome to perform their own calculations, but we should question any calculations using assumptions by those in the industry. As in other reports we have prepared, the same legal disclaimer applies.[41]

MLM company and year of average earn-ings report [42]	**Estim. min. annual costs for effective recruitment campaign.[43]**	**Level at and above which net profits possible [44]**	**Approx. % of active participants at that level or above [45]**	**Maxi-mum Reten-tion rate [46]**	**Approx. % of all partic's that could have profited from participation [47]**	**Approx. % of all partic's who lost money [48]**
Advocare (2009)[49]	$2,545	Silver	4.61%	10%	0.46% (0.0046)– or **1 in 217 profits**	**99.54% lost money**
Ameriplan (2008)[50]	$2,545	SRSD	7.46%	10%	0.75% (0.0075) **– or 1 in 133 profits**	**99.25% lost money**

[39] See Chapter 2 for these characteristics ("red flags") – also available as a full report or summary at – mlm-thetruth.com

[40] We have received average income statements for several other MLMs, but without adequate data to do this analysis.

[41] It is important that you make your own decision on whether or not to participate in an MLM based on your own evaluation. These reports, lists, and opinions are intended purely as a communication of information in accordance with the right of free speech. They do not constitute legal or tax advice. Anyone seeking such advice should consult a competent professional who has some expertise on endless chain or pyramid selling schemes. Readers are specifically advised to obey all applicable laws, whether or not enforced in their area. Neither the Consumer Awareness Institute nor the author assumes any responsibility for the consequences of anyone acting according to the information in these reports.

[42] The most recent report available to the author at the time of the analysis.

[43] Estimated minimum costs of conducting a successful recruitment campaign, based on the author's one-year test of a leading MLM. Costs includes incentivized purchases plus minimum operating expenses, corrected by COL (cost of living adjustment, based on Consumer Price Index) since founding – See chapter 5. Here we use the extremely liberal assumption that total costs were only 10% of those of the author.

[44] Estimated average net profits assume all expenses (including incentivized purchases and minimum operating expenses) are subtracted from income. This is the "pin level" at and above which profits would be possible.

[45] Referring to the level in the previous column – per MLM company reports. If only "Active" participants ("Distributors," "Associates," etc.) were counted, we can safely assume that the numbers on the report represent no more than half of the total. If the requirement to be listed as Active is very restrictive, a factor of 25% is used instead.

[46] See chapter 6 for how approximate attrition (and retention) rates for MLMs are estimated. The inverse of attrition is retention, which is used to estimate the percentage who could profit. Retention is estimated to be a maximum of 10% if in business for four to nine years, 5% for ten or more years. However, for this report, we use the liberal assumption of15% for four to nine years and 10% for ten or more years. Newer MLMs are not included, as data to establish long-term retention rates has not yet been established.

[47] Average income exceeding all expenses (second column) for conducting a successful recruitment campaign.

[48] In calculating percentage who lost money, those who dropped out are included. This is using the assumption that participants who had arrived at such a high "pin level" that they were profiting would stay in the program – since the enjoy the "residual income" that promoters imply at opportunity meetings is possible.

[49] "2009 Income Disclosure Statement" - published by Advocare

MLM company and year of average earnings report	Estim. min. annual costs for effective recruitment campaign.	Level at and above which net profits possible	Approx. % of active participants at that level or above	Max. Retention rate	Approx. % of <u>all</u> partic's that could have profited from participation	Approx. % of all partic's who lost money
Amway/ Quixtar (2001)[51]	$2,090	Platinum	0.60%	10%	0.06% (0.0006) – **or 1 in 1,667 profits**	**99.94% lost money**
Arbonne Int'l (2007)[52]	$2,450	Area Managers	0.59%	10%	0.059% (0.0006) **– or 1 in 1,659 profits**	**99.94% lost money**
Cyberwize (2006-2007)[53]	$2,381	Director	5.75%	10%	0.57% (0.0057) **– or 1 in 175 profits**	**99.43% lost money**
Ecoquest (2005 - now Vollara)[54]	$2,306	Fast Start Distributor	1.46%	Since 2000 - -278,024 Dealers[55]	0.44% (0.0044) – **or 1 in 227 profits**	**99.56% lost money**
FHTM (2009)[56]	$2,545	Executive Sales Manager	5.19%	15%	0.78% (0.0078) – **or 1 in 128 profits**	**99.22% lost money**
FreeLife Int'l (2008)[57]	$2,545	Ambassador	4.18%	15%	0.63% (0.0063) – **or 1 in 159 profits**	**99.37% lost money**
Herbalife (2008)[58]	$2,545	World Team	5.71%	10%	0.571% (0.0057) **– or 1 in 175 profits**	**99.43% lost money**
Ignite –Stream Energy (2009)[59]	$2,306	Senior Director	1.77%	15%	0.27%, (0.0027) or **1 in 370 profits**	**99.73% lost money**
Immunotec (2007)[60]	$2,450	Silver	0.71%	10%	0.071% (0.00071) – or **1 in 1,408 profits**	**99.93% lost money**
iNetGlobal (2009)[61]	$2,545	Diamond Executive	2.9%	15%	0.87% (0.0087) – or **1 in 115 profits**	**99.57% lost money**
Isagenix (2007)[62]	$2,450+	Star Consultant	2.1%	10%	0.21% (0.0021) – **or 1 in 476 profits**	**99.79% lost money**
Mannatech (2007) [63]	$2,450	Regional Director	7.16%	10%	0.72% (0.0072) **– or 1 in 139 profits**	**99.28% lost money**
Melaleuca (2008)[64]	$2,545	Director III/IV	2.9%	10%	0.29% (0.0029) – or **1 in 345 profits**	**99.71% lost money**

50 "AmeriPlan Independent Business Owner Income Disclosure Statement for 2008" - published by AmeriPlan
51 "Average Annual Income for IBO's in North America, 2001 Average Annual Earnings in U.S. Dollars." ©2002 Quixtar, Inc.
52 Independent Consultant Compensation Summary – U.S. " (2007), published by Arbone, Int'l
53 "Cyberwize Income Disclosure Statement for 2006-2007" - published by Cyberwize
54 "Income Disclosure Statement" - provided by Ecoquest Int'l (now Vollara)
55 Ecoquest reported what all MLMs should report – the total population base of recruits since the company's founding, or the year during which the first TOPPs (that are included in the report) joined the system. So we did not need to estimate attrition rate.
56 "Income Disclosure Statement," January 23,2009 – January 20, 2010. In business since 2006.
57 "2008 Annual Income Statistics" - published by FreeLife Int'l
58 Herbalife: "Statement of Average Gross Compensation of U.S. Supervisors in 2008" – published by Herbalife
59 "Income Disclosure" July 2008 – June 30, 2009" - published by Ignite
60 "Immunotec: INCOME DISCLOSURE REPORT – 2007" – published by Immunotec
61 "INCOME DISCLOSURE STATEMENT FOR INETGLOBAL.COM" 1 Jan 2009 – 31 Dec 2009
62 "Annual 2007 Isagenix Independent Associate Earnings Statement" - published by Isagenix
63 "2007 U.S. Income Averages: 2007 Annualized Income Averages by Status" – published by Mannatech
64 "2008 Annual Income Statistics" – published by Melaleuca. This Melaleuca report is one of the most obfuscated reports I have analyzed. All buyers are designated "customers." A certain percentage are deemed "business builderfs," and percentages of these are in turn percentages of all customers, and a percentage of these are in "development" or "leader" status. Thus, those who are in the profit category are made to appear a much larger

MLM company and year of average earnings report	Estim. min. annual costs for effective recruitment campaign.	Level at and above which net profits possible	Approx. % of active participants at that level or above	Max. Retention rate	Approx. % of all partic's that could have profited from participation	Approx. % of all partic's who lost money
Mona Vie (2008)[65]	$2,306	Star 500	1.95%	15%	0.29% (0.0029) – **or 1 in 345 profit**	**99.71% lost money**
MXI Corp[66] **(Xocai - 2009)**	$2,232	Silver Executive	3.75%[67]	15%	0.56% (0.0056) – or **1 in 179 profits**	**99.44% lost money**
Nikken (2007)[68]	$2,450	Gold	0.82%	10%	0.082% (0.00082) – **or 1 in 1,216 profits**	**99.12% lost money**
Nu Skin (2008)[69]	$2,545	Qualifying Executive[70]	6.22%	10%	0.62% (0.0062) **– or 1 in 161 profits**	**99.38% lost money**
Reliv (2005)[71]	$2,306	Key Director[72]	3.12%	10%	0.312% (0.0031) **– or 1 in 321 profits**	**99.69% lost money**
SendOutCards (2009)[73]	$2,232[74]	Senior Manager	4.22%	15%	0.35% (0.0035) - **or 1 in 286 profits**	**99.65% lost money**
Sunrider (2007)[75]	$2,450	Business Leader	11.19%	10%	1.12% (0.0112) – **or 1 in 89 profits**	**98.9% lost money**
Symmetry (2003)[76]	$2,175	$201-500/mo. income level	3.3%	10%	0.33% (0.0033) – **or 1 in 303 profits**	**99.67% lost money**
Tahitian Noni Int'l (2007)[77]	$2,306	Jade	3.59%	10%	0.36% (0.0036)– or **1 in 278 profits**	**99.64% lost money**
Tupperware (2008)[78]	$2,545	Manager	2.85%[79]	10%	0.285% (0.0028) – or **1 in 351 profits**	**99.71% lost money**
USANA (2005)[80]	$2,545	Achiever	4.7%	10%	0.47% (0.0047) – or **1 in 213 profits**	**99.53% lost money**

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percentage than would appear in the report. I doubt that anyone looking at the numbers to decide on participation could get the true likelihood of profiting from the information provided.

65 "Income Disclosure Statement Global 2008" – published by Mona Vie. Mona Vie calls those who made a purchase in the past 12 months but failed to meet four criteria are classified "wholesale customers," lessening the percentage of distributors who would otherwise be considered customers.

66 Xocai 2009 "Income Disclosure statement" – published by MXI Corp.

67 The percentage of Associates who did not qualify under strict standards as "Active Associates" is not disclosed. A liberal assumption of 50% of all Associates being "Active" is used here.

68 "Average Consultant Income Sheet" – published by Nikken. Nikken has two sets of income statistics, one for sponsoring levels and one for leadership levels. I assumed that leadership levels come out of and do not exceed the top sponsoring level (Bronze).

69 "Nu Skin Enterprises, Inc.: 2008 Distributor Compensation Summary" – published by Nu Skin

70 This illustrates how these assumptions are extreme in favor of the MLMs in this table. In my own personal experience withNu Skin, I was losing $1,250 per month even at Executive level – almost to Gold level.

71 "2005 Earnings Statisics" – published by Reliv

72 Reliv only lists earnings for Director and above, with six levels below all essentially losing money

73 "2009 Income Disclosure" – published by SendOutCards

74 Still in hypergrowth stage typical of any new MLM, or product-based pyramid scheme

75 " Income Disclosure Statement: January – December 2007" – published by Sunrider

76 "Vision: Earnings Matrix Based on 2003" – published by Symmetry

77 "Average Incomes of U.S. IPCs" – published by TNI

78 "2008 Income Disclosure Summary" – published by Tupperware – which appears to have changed their compensation plan in April of 2005 to provide greater rewards for high level participants ("Directors"). Reported in Presentation Summary, S2Sales Force Structure.Earnings Conference Call, Jan. 31, 2007.

79 This number is likely inflated because Tupperware did not report the plan participants who received no commissions.

80 "2005 Average Income of Associates" – published by USANA. I would have used their 2008 report, but they began selectively reporting only the most active of participants ("Associates") and suggested their numbers represented average total earnings – a huge deception. Apparently the 2005 numbers did not look good enough, so they changed

MLM company and year of average earnings report	Estim. min. annual costs for effective recruitment campaign.	Level at and above which net profits possible	Approx. % of active participants at that level or above	Maximum Retention rate	Approx. % of all partic's that could have profited from participation	Approx. % of all partic's who lost money
World Ventures (2008) [81]	$2,306	Senior Representative	0.2%	15%	0.03% (0.0003) – **or 1 in 3,333 profits**	**99.97% lost money**
Xango (2007)[82]	$2,545	5K	1.22%	15%	0.18% (0.0018) – or **1 in 556 profits**	**99.82% lost money**
Yor Health (2010)[83]	$2,545	Copper	2.52%[84]	15%	0.378% (0.0038) – **or 1 in 263 profits**	**99.62% lost money**
Your Travel Biz (YTB-2007)[85]	$2,545	$2,500-5,000 per month	N/A (only total since 2001)	N/A	0.207% (0.002067) – or **1 in 484 profits**	**99.79% lost money**
Approx. average profit and loss rates of participants	N/A	N/A	N/A	N/A	0.4.2% (0.0042) – or **1 in 238 profits**	**99.6% lost money**

Observation from Appendix 7A:

In every case, using the analytical framework described above, the loss rate for all of these MLMs ranged from 99.12% to 99.97%, with an average of 99.6% of participants losing money. On average, **one in 238 actually profited after subtracting expenses, and 996 out of 1,000 lost money – to say nothing of the time invested**.

The most liberal assumptions that could reasonably be used in favor of the MLMs were applied to this table of MLM loss rates. **Using the more realistic assumptions discussed in prior chapters, the average loss rate for these MLMs would have averaged no better than 99.9% - with less than one in 1,000 profiting significantly.**

Also, I would estimate that the number of new recruits who wind up receiving the promised substantial "residual income" held out at MLM opportunity meetings is no better than one in 25,000 recruits!

As a general rule, the more a new recruit invests in an MLM program, the more he or she loses. This, of course, is true of most any scam.

their reporting to make them look better. For more on USANA's deceptive reporting, search "USANA" in The Fraud Files at – www.sequenceinc.com

[81] "World Ventures Marketing. LLC: Annual Income Disclosure Statement" – published by World Ventures

[82] "Income Disclosure Statement: 2007 Average Monthly Earnings by Rank for All Markets" – published by Xango

[83] "YOR Income Disclosure Statement"

[84] Total population of reps from beginning of company was reported to be 224,440 - which is what was needed for the calculations.

[85] "Rep Earnings Report July 2007"

Appendix 7B: List of MLMs for which compensation plans have been evaluated by Jon M. Taylor, MBA, Ph.D. (as of January 1, 2011)

1Cellnet
4Life Int'l
5Linx
A. L. Williams
Acai Plus
Achievers Unlimited
ACN
Adcalls
Advantage Conferences
Advantage Marketing Systems
Advantage Neutraceuticals
Advocare
Affordable Energy
Agel
AIM
AliveMax
All-star Entrepreneur
Amazon Herb
Ambit Energy
American Longevity
Ameriplan USA
Amerisciences
Amkey
Amsoil
Amway-Quixtar
American Marketing Systems
American Petroleum Promotions
Amigo Health
Annasa
Apeus
Arbonne
Ardyss International
Ascend Technologies
Ascential Bioscience
At Home America
Avalla-Distributes Nutrimetrics
Avon
Baby Crazy
Beach Body
BeautiControl Cosmetics
Bel'Air
Better Universe
Beyond Freedom Seminars
bHIPGlobal
Big Planet (Nu Skin)
Biogen
Biometrics
Bioperformance
BioPro
Bodywise
Bookwise Books
Brain Garden
Business in Motion (BIM)
Celebrating Home
Cell Tech
Cell Wireless
Ceres Living
Champion Communications
Cie Aura
Citizenre
Cleur
Cognigen
Conklin
Cookie Lee Jewelry
Creative Memories
Cyberwize
Daisy Blue
Digital Crown Holdings Ltd. (DHCL)
Direct from Vatican City
DoTERRA
Drink ACT
DSX
Dubli
Dynasty of Diamonds
E. Excel
Earth Essence
Easy Daily Cash (2-up)
Ebiz.com
Ecoquest
eFoods Global
eFusion (acai)
Eido
Eiro
Elur
Emerald Passport (Profit Masters)
Empire Dreams
Empower Net
Enagic (Kangen water)
Enfinitia
Eniva Gold Marketing
Enliven
EnvisionCC
Epic Network
Escape International
Essante
Essentially Yours
Evolution International
Excel Telecommunications
eXfuse
Extreme Research
EZ Wealth by Design
First Financial Security
First Fitness International
Fuel Freedom International
FFSI
FM Group World
For You
Forever Green
Forever Int'l
Forever Living
Formor Int'l
Forte Builder (New Vision)
Fortune Hi-tech Marketing
Free Life International
Freedom Rocks
Fruda Vida International
Frutaigo
Fuller Brush
Fun Unlimited
Gano Excel
GBG
Gemcap
Gem Lifestyle
Genewize Life Sciences
GDI - Global Domain Int'l
Global Equity Marketing and Global Equity Lending (World Leadership Group)
Global Health Trax
Global Research Network (1-up)
Global Resorts Network
Global Travel Trends (PRT Travel)
Global Wealth Trade
GNLD
GoHFT
Gold Mine International
Golden Neo-life Diamite
GoldQuest
Goldshield Elite
Good Life International
Goyin
Great Life Int'l
HBW Insurance and Financial
Herbalife
Heritage Health Products
Heritage Makers/li>
Hsin Ten Enterprise USA
iBuzzPro
Ignite/Stream of Energy
Igonet
Immunotec
iNet Global
Inner Light
Integris Global
IDN (Nu Skin)
International Galleries, Inc. (IGI)
Isagenix
ITV Ventures
It Works
IV-7 Direct
Jafra
Jewelry by Park Lane
Jus International
K-Link
Kaire
Kangivity Global
Kanosis
Karemore
Kleeneze
Kyani
Ky-Ani Sun
Learning Global USA
Leaving Prints
Legacy for Life
Lexxus
Liberty International
Liberty League Int'l (LLI)
Life Force International
Life Max
Life Plus
LifeWave
Life without Debt
Lifestyles USA
Lightyear Alliance
The Limu Company

Livinity
Longevity Network
Mandura
Mannatech
Market America
Mary Kay Cosmetics
Matol Botanical
Mavericks (World Health Card)
Max GXL
Max International
Maxxis 2000
Me2Everyone
Melaleuca
Menage International
ML International
MMOGULS
Mona Vie
Monarch Health Sciences
Mona Vie
Morinda (Tahitian Noni Int'l)
Moxxor
MPB Today
Multi-pure
MXI-Xocai
My4Life
My7Diamonds
My Leisure Business
Narc that Car
NAA - National Agents Alliance
National Lending Corp.
Native American Nutritionals
Natural Air Products
Nature's Own
Nature's Sunshine
NeutroGenesis
Neways
New Quest International
New Vision USA
NextFit
Nexx
NHT Global
Nikken
Noevir
Nouveau Cosmeceuticals
Nouveau Riche University
NSA (Juice Plus)
Nucerity
Numis Network (coins)
NuLegacy Rx card
NuMed
Nu Skin/Pharmanex/Big Planet
Nussentials
Nutronix
Nuvante
Ohana Health
Omegatrends
Ominex
Omnitrition
One24
Online Exchange
OnPoint Direct
Orender International
Organo Gold
Orovo
Our World Network
Oxyfresh
Palmary
Passport LLC
Petromagic
Pharmanex (Nu Skin)
PhotoMax (Nu Skin)
Plexus Pink
PM International AG
Power2Marketing (P2M)
Power Mall
Prepaid Legal
Primerica Financial Services
Prixdale Ventures
The Profit Masters (Emerald Passport)
Pureworks
Purse Party
Qing Mei (cards)
Quixtar (Amway/Alticore)
Questnet
RBC Life Sciences
RMP Infotech
Refer Life
Reliv
The Right Solution
Rodan & FIelds - Victoria
SkinCare
Royal Body Care
Saraha of India (Saraha Conserve & Comosale)
Scent-sations
Sendoutcards.com
Sene Gence Int'l
Sensaria
Sevea
Shaklee
Share the Wealth
Sibu
Silver Cache
Slender Now
Soteria/ It Works Marketing
Southern Living at HOME
Sportron
Spring Wellness
Stampin' Up!
Stem Tech Health Sciences
Stimulife
Success University
Sunrider
Supralife
Sweet Living
Swiss Just
Symmetry
Synergy Worldwide
Syntec
Tahitian Noni Juice (Morinda)
Talk Fusion
Take Shape for Life
Team Everest
Team LIfe Changes (Nutraburst)
Team National
The Traveling Vineyard
Tiens Biotech Group
Tianshi
Transcend Mktng Int'l, Inc. (TMII)
Tomboy Tools
Tom Danley's Tape of the Month
Top Line Creations (TLC)
Traverus Travel
Trilogy
Triunity Int'l
Trivani
Trivita
Tupperware
TVI Express
Ubifone
UltraStore
Unicity
Univera Life Sciences
USANA Health Sciences
Vemma
Visalis
Vision for Life
Vision Travel
Vitagenesis
Viva Life Science
VM Direct (Hello world)
Votre Vu
Xyngular
Waiora
Watkins
Wealth Pools Int'l
Wellness International Network (WIN)
Woosh
World Financial Group
World Group Securities
World Leadership Group
World Lending Group
World Marketing Alliance (WMA)
World Ventures
Wowgreen
Wynlife Healthcare
Xango
XELR8
Xocai
Xooma
XOWii
Xzotto
Yoli
YOR Health
Young Living Essential Oils
Youngevity
Your Travel Biz (YTB Travel Network)
Zamu
Zamzuu
Zermat International
Zija
Zrii
Zu-B
Zulian
Zurvita

Appendix 7C: Winners and losers in a classic no-product 8-ball (1-2-4-8) pyramid scheme

Cycle	Number of pyramids	Total number of participants*	Number who profit**	Percentage who profit***	Percentage who lose
1	1	15	1	6.67%	93.99%
2	3	31	3	9.68%	90.32%
3	7	63	7	11.11%	88.89%
4	15	127	15	11.81%	88.19%
5	31	255	31	12.10%	87.84%
6	63	511	63	12.33%	87.67%
7	127	4123	127	12.41%	87.59%
8	255	2047	255	12.46%	87.54%
9	511	4095	511	12.48%	87.52%
10	1023	8191	1023	12.49%	87.51%

Profits broken down in a classic no-product 8-ball (1-2-4-8) pyramid scheme:

Order of participants' entry into the scheme	Revenues to each participant at that level	Number of participants at that level
Initiator	$140,000	1
2nd participants entering the system	$120,000	2
3rd “ “ “ “	$112,000	4
4th “ “ “ “	$98,000	8
5th “ “ “ “	$84,000	16
6th “ “ “ “	$70,000	32
7th “ “ “ “	$56,000	64
8th “ “ “ “	$42,000	128
9th “ “ “ “	$28,000	256
10th “ “ “ “	$14,000	512

Total number of participants who would profit	1,023
Number of participants at the lower levels who would lose money	7,168
Total of all participants in the scheme	8,191
Per cent who profit (assuming all those who profit reinvest in new cycles of the pryamid	12.49%
Percent who lose money at the 10th level	87.51%

* This includes all who participated, regardless of how many times.
** This is the number of participants who have cashed in at least once and some multiple times.
*** This assumes every profiting participant keeps investing in new pyramid cycles. The percentage profiting would be slightly higher or lower depending on how many participants dropped out and when.

Appendix 7D: A simple form that would disclose crucial information to prospects

Average payments to – and purchases from – all WealthPlus[1] participants who had enrolled[2] within the past three years

Total number of participants[3] recruited during the three-year period of the report	100,000
Total of all purchases[4] of products and services for the past year from WealthPlus by (the same group of) participants who were enrolled and authorized to recruit other participants within the past three years	$87,835,000
Total payments in commissions to these participants for the past year	$25,390,000
Percentage of distributor-generated revenue rebated to these distributors (payout)	28.9%
Average purchases of products and services[5] by these participants from WealthPlus	$878.35
Average commissions and bonuses paid by WealthPlus to each of these participants	$253.90
Average income/loss of participants in this group of participants	– ***(minus) 624.45***

Range of annual Commissions[6] received by participants from WealthPlus	**Average purchases from company for each level**	**% of total participants***	**Number of participants**	**Total commissions paid by company to distributors at each level**
Over $500,000	$20,000	0.001%	1	$1,500,000
$250,000-$499,999	$18,000	0.005%	5	$3,500,000
$100,000-$249,999	$16,000	0.01%	10	$3,000,000
$50,000-$99,999	$14,000	0.05%	50	$3,500,000
$25,000-$49,999	$12,000	0.01%	100	$3,000,000
$10,000-$24,999	$10,000	0.03%	300	$3,600,000
$5,000-$9,999	$8,000	0.05%	500	$3,500,000
$1,000-$4,999	$3,400	2.0%	2,000	$3,000,000
$1-$999	$1,200	7.0%	7,000	$700,000
$0 – participants who made purchases but did not qualify for commissions[6]	$400	80%	80,000	0
$0 – participants who enrolled but made no Purchases[7] since enrolling	$0	10% (approx.)	10,000	(approx.) 0
Totals	$87,835,000	100%	100,000	$25,300,000

See "Explanatory Reference Notes for FTC Officials" on the following page.

Explanatory Reference Notes for FTC Officials:

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

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

[3] These statistics include ALL persons who contracted with the company as participants within the past three years (or other designated time period). This is to correct the typical deceptive reporting practice of MLM firms of counting only "active distributors" in the past year (or other limited time period). They eliminate the recruits that dropped out. Their base for comparison thus represents only a small slice of the total recruits. Note that while eliminating participants that contracted to join and then dropped out, this small base of participants is compared with participants who may have been with the company for five to twenty years at a certain level – often from the beginning of the chain of recruitment. The statistical results are extremely skewed, making the MLM "opportunity" appear to be profitable for more recruits than is actually the case. The above form would help correct these deceptions. Those that had been with the company for longer than three years would not be included in this disclosure.

[4] This number must include ALL purchases from the company, including products, training, sales aids, telecommunications and other electronic aids, etc. This makes it possible for recruits to see if it is likely that more money will be received from the company than is paid to it. It also will help determine if the company is a legitimate business opportunity or merely uses the "business opportunity" as a ruse to get participants to buy products – with few real customers outside the network of participants. NOTE: Because only participants recruited in the past three years are counted, the percentage payout is unusually low, even for an MLM. This is because the early entrants, who joined at or near the beginning of the recruitment chain and who are harvesting a disproportionate portion of the commissions, are not included in this figure.

[5] Additional expenses would include any "sales tools" sold by upline participants – and normal operating expenses, such as travel and telephone and Internet costs

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

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

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

APPENDIX 7F: Network Marketing Payout Distribution Study – Letter to Presidents of 60 Prominent MLM* Companies

May 13, 1999

ATTN: ___________, President
Company name & address

Dear Mr./Ms.______________:

For the past two years I have researched the field of network marketing (a.k.a. multi-level marketing or "MLM"*) and have interviewed hundreds of people who had been involved in a wide variety of programs. My research, while initially positive, uncovered more and more very unsettling problems with MLM.

When speaking on the subject of MLM to local groups I have received much feedback from participants and critics of MLM. One tax accountant who was a principal of H&R Block in northern Utah stated that over the years he and his staff had prepared thousands of tax returns, and of the several hundred of these who he knew had been involved in MLM, <u>he could remember only one who had ever reported a net profit on his return.</u>

Though I already knew that the actual success stories were far less than one would be led to believe from attending a typical MLM opportunity meeting, this tax man's report was shocking to those of us who heard it. So I called tax accountants and preparers in other areas to see if their experience was the same. Each of them claimed similar experiences with their clients over the years. Others who work with peoples' money, such as certified financial planners, insurance underwriters, and bankers, have relayed similar feedback.

I will soon be publishing this information for the benefit of consumers, educators, legislators, and regulatory agencies who have an interest in this topic. The page that follows presents the essence of my conclusions, which unfortunately are not favorable for the MLM industry. So <u>I felt it only fair to allow for rebuttal from you and others who may have an interest in seeing a balanced treatment of the subject. So I am offering you that opportunity and the format for doing so.</u>

Your assistance in gathering objective information will be greatly appreciated. I am not interested in anecdotal material, which may be no more valid than stories of persons who won a lottery or a sweepstakes. And vigorous arguments to the contrary will not help – I believe I've heard them all. What will carry weight is data which breaks down the distribution of payouts to your distributors, extracted from your data base of distributors. The information you provide must be verifiable by independent audit, as consumer protection agencies and legislators may choose to validate this material. Following this letter are instructions for providing the information.

<u>You should be able to access this information readily from your database.</u> However, if you prefer not to provide this information because it won't reflect well on your program, I can certainly understand your reluctance. But such refusal will be interpreted to be an answer in itself. I shall be looking forward to your response.

Appreciatively,

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

* Originally, "NWM" (for network marketing) was used in the letters, instead of "MLM" (rev. 6-30-06

Network marketing has wide appeal.

Network marketing (aka "multi-level marketing," or "MLM" for short) offers the opportunity for an individual to conduct a business without having to bother with expensive resources such as physical plant or retail storefront, warehousing, employees, advertising, or other costs typically associated with running a business.

MLM promoters claim that with MLM, large (leveraged) incomes can be produced by recruiting a downline (network) of multiple layers of distributors upon which a distributor can draw commissions and bonuses, the amount depending on the type of compensation plan and the size and character of one's "downline." Such an organization can be built from one's own home without the expenses and complications typically associated with other types of businesses.

MLM promoters claim that MLM offers not only financial independence with minimal investment, but a level playing field in which anyone can participate, regardless of sex, age, education, or financial resources. Other advantages include the social benefits and recognition of building one's own organization and the backing of a MLM company that provides the products and infrastructure necessary for success.

Network marketing poses problems for most participants, resulting from pyramidal concept, motivation, and effects.

When the Federal Trade Commission ruled in 1979 that Amway was not an illegal pyramid scheme—mainly because legitimate products were offered, the floodgates were opened and multi-level marketing programs began to proliferate. But what is often ignored is the fact that MLM programs are still pyramid schemes, modified by a variety of compensation systems that change the character of the pyramid, but **not the essential pyramidal concept, motivation, and effects.**

The pyramid concept in MLM is seen in multiple layers of distributors, with lower level distributors contributing income to an "upline" who may have little to do with a given sale. This is distinguished from the typical retail scenario in which a retailer may get two or three times the return per sale as the wholesaler, whereas with MLM the upline distributor may get as much or more of a return per sale (in commissions and bonuses paid by the company) as the front line distributor who actually sells the product.

Because MLM compensation systems reward front line distributors only a small commission (usually less than 10% - not counting assumed resale of expensive products at retail markup) for selling products, recruiting to gain income from downline distributors is vital to earning a significant income. This is distinguished from other direct sales programs, in which the person selling and servicing the product typically is paid commissions from the company of from 20% to 50% of the sale – enough incentive to concentrate on the end user as a valued customer.

The motivation of most MLM is the opportunity to make large amounts of income for a minimal investment of time and money. One of the primary appeals of MLM is the concept (touted at MLM opportunity meetings) of "time freedom" or "leveraged income," which allows a person to gain an income flow from the efforts of others without having to work directly for one's own income. But because of MLM compensation systems, this requires success at recruiting a downline, more than on selling the products directly.

Critics complain that many MLM distributors place too much emphasis on the "opportunity" as opposed to the product, thus blurring the distinction between the product and the opportunity. As I mentioned, this can be accounted for by the reward structure of MLM compensation systems, which benefits primarily top upline distributors – who may receive extremely large commissions from their aggregate downline. An inordinate appeal to greed often becomes the primary motivation.

A most troubling aspect of MLM is its effects on people. Because the compensation plans are heavily weighted to reward upline distributors for their recruitment efforts and because of the pyramidal nature of these systems, extraordinary income differentials are created between upline and downline distributors. In fact, after deducting expenses for building and maintaining a network, only a tiny fraction of MLM distributors ever report a positive income on their income taxes.

Letter to MLM Presidents, page 3

And if products purchased from the company (that likely would not have been purchased were they not participants in the program) are subtracted, far less than one out of 100 distributors earns more than a minimum wage for their efforts. A high percentage of distributors lose money – much higher than most other legitimate business and income pursuits.

Careful examination of most MLM programs reveals a pattern of exorbitant incomes accruing to relatively few top distributors at the expense of hundreds and even thousands of downline distributors who – even with diligent effort – come away empty-handed. In this respect MLM is akin to illegal (no-product) pyramid schemes.

It is interesting to compare the odds of success of MLM schemes with legalized gambling in Nevada. It appears that on average one could do better at most any of the gaming tables or slot machines in Las Vegas – without investing all that time and placing valued relationships at risk.

Some zealous MLM distributors will mortgage their homes or max out their credit cards (buying MLM products and other expenses) to finance their ambition to achieve top levels in their organization—which is seldom achieved. Others focus so much on recruiting to meet escalating volume requirements for higher distributor levels that they ignore the needs of spouse and family members.

Sometimes the recruiting practices of MLM distributors are deceptive and overbearing. Often MLM distributors will alienate friends and family members they endeavor to recruit for what seems to them a self-centered pursuit of a vaporous dream.

Summary and invitation for rebuttal

In summary, with network marketing, what appears on the surface to be a fair and enabling marketing system for participants is in reality a pyramid scheme with characteristics of concept, motivation, and effects similar to those of clearly illegal no-product pyramid schemes.

You are invited to prove me wrong—at least for your company. This can best be done by providing full disclosure on payout distribution to your distributors on the attached form. For the purposes of this study, this information must be broken down by percentiles, not by distributor level.

Please note that I am not asking you to reveal sensitive information, such as individual distributor incomes or even your annual profits, which you may wish to keep confidential. It is average payout to distributors by percentiles (as indicated on the attached form) that will satisfy the objectives of this study for the benefit of consumers.

Please also note that I am offering two options for your response – an easy one (Option A) and a more comprehensive one (Option B). It is assumed that Option A could be competed quickly and easily from your existing accounting system. **Option B requires a more extensive breakdown, but would offer to those interested more conclusive evidence that your company does or does not base its compensation to distributors on a pyramidal structure, as discussed above. For the purposes of this study, Option B would be much preferred, if you can return such data to us within a month or so.**

We are not making any assumptions about how much effort was put into any given MLM program or compensation system, as it relates to success of failure of any specific distributor or program. So it is important that <u>all</u> participants in your MLM program for the year be included, even those who only bought a distributor starter kit or set of samples—whether or not they have done anything with it.

Please mail completed form to:

Network Marketing Payout Distribution Study
Consumer Awareness Institute

OPTION A: Distribution of Payout to Distributors for the Most Recent Fiscal Year Beginning____________ and Ending ___________

Company name______________________ Address____

City, state, zip__________________________________ Contact person_________________ Tel. no. (_____)_______

Please check (□) one:
___a. We are willing to provide the information below and have it made available to the public.
___b. We are providing the information below with the understanding that it may be used for compiling industry statistics but not identified with our company in published reports.
___c. We are not willing to provide the information requested. We realize that in refusing to do so we may be tacitly conceding the conclusions drawn in the preliminary two-page report, entitled, "Network Marketing Payout Distribution Study."

If you are interested in receiving information on the completed report when it is done, please check here_____ (This research report is to be sold for a reasonable price—yet to be determined—to recover costs.)

Important instructions: For purposes of analysis, distributors are to be broken down by distributor payout percentiles, <u>not</u> company-established distributor levels. Also, it is important that <u>every</u> person who has enrolled as a distributor (i.e., purchased starter kit or samples, or signed a distributor agreement) be included in these statistics, including those who have not sold anything or quit, even after one day.

Percentile break-down in payouts to distributors (by percentile, <u>not</u> <u>distributor level)</u>	**Total number of <u>all</u> of your distributors <u>at this payout level</u>**	**Average total company payout per distributor (all commissions <u>and</u> <u>bonuses</u> paid by the company, but <u>excluding</u> <u>retail margins)</u>**	**Less: average total dollar amount per distributor of purchases of goods and services <u>from your company</u>**	**Average net payout* per distributor – deduct total products & services distributors purchased from your company, from total commissions <u>you paid them</u>**
Top 1/10 of the top 1% of distributors	_________________	$____________________	$_______________	$________________
Bottom 9/10 of the top 1% of distributors	_________________	$____________________	$_______________	$________________
Next 9/10 of the top 10% of distributors (the 2nd to the 10th percentiles)	_________________	$_____________________	$_______________	$________________
Bottom 90% of distributors	___________________ (Total 100%)	$_____________________	$_______________	$________________

*It is recognized that net income reported here does not take into account operating costs to distributors for conducting their MLM business. Such costs may include, travel, postage and shipping, long distance and other telephone costs, advertising, rental of meeting rooms and/or office space, fees for company conferences or retreats, supplies, sales materials, and other expenses.

THANK YOU FOR YOUR HELP!

OPTION B: Distribution of Payout to Distributors for the Most Recent Fiscal Year Beginning____________ and Ending ___________

Company name______________________ Address____

City, state, zip_____________________________Contact person______________Tel. no. (____)________

Please check (□) one:

___a. We are willing to provide the information below and have it made available to the public.

___b. We are providing the information below with the understanding that it may be used for compiling industry statistics but not identified with our company in published reports.

___c. We are not willing to provide the information requested. We realize that in refusing to do so we may be tacitly conceding the conclusions drawn in the preliminary two-page report, entitled, "Network Marketing Payout Distribution Study."

If you are interested in receiving information on the completed report when it is done, please check here_____ (This research report is to be sold for a reasonable price—yet to be determined—to recover costs.)

Important instructions: For purposes of analysis, distributors are to be broken down by distributor payout percentiles, not company-established distributor levels. Also, it is important that every person who has enrolled as a distributor (i.e., purchased starter kit or samples, or signed a distributor agreement) be included in these statistics, including those who have not sold anything or quit, even after one day.

Percentile break-down in payouts to distributors (by percentile, not distributor level)	**Total no. of all of your distrib's at this payout level**	**Aver. total company payout per distrib. all commissions and bonuses paid by the company –excluding retail margins)**	**Less: average total dollar amount per distributor of purchases of goods and services from your company**	**Average net payout* per distrib. – deduct total products & services distrib's purchased from your company, from total comissions you paid them**
Top 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Second 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Third 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Fourth 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Fifth 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Sixth 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Seventh 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Eighth 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Ninth 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________
Bottom 1/10 of the top 1%	_____________	$_____________________	$_______________	$_______________

—continued—

After breaking down average payout per distributor for the top 1% by tenths of a percent, please break down the next 10% by whole percentiles:

Percentile breakdown in payouts to distributors (by percentile, not distributor level)	**Total no. of all of your distrib's at this payout level**	**Aver. total company payout per distrib. all commissions and bonuses paid by the company –excluding retail margins)**	**Less: average total dollar amount per distributor of purchases of goods and services from your company**	**Average net payout* per distrib. – deduct total products & services distrib's purchased from your company, from total commissions you paid them**
Second 1%	_______________	$____________________	$______________	$______________
Fourth 1%	_______________	$____________________	$______________	$______________
Fifth 1%	_______________	$____________________	$______________	$_______________
Sixth 1%	______________	$____________________	$______________	$_______________
Seventh 1%	______________	$____________________	$______________	$______________
Eighth 1%	______________	$____________________	$______________	$______________
Ninth 1%	______________	$____________________	$______________	$_______________
Tenth 1%	_______________	$____________________	$______________	$_______________

After breaking down average payout per distributor for the top 10% by whole percentiles, please break down the next 90% in groups of 10% each:

Second 10%	_______________	$____________________	$______________	$_______________
Third 10%	_______________	$____________________	$______________	$_______________
Fourth 10%	_____ _________	$____________________	$______________	$_______________
Fifth 10%	_______________	$____________________	$______________	$_______________
Sixth 10%	_______________	$____________________	$______________	$_______________
Seventh 10%	______________	$____________________	$______________	$_______________
Eighth 10%	_______________	$____________________	$______________	$_______________
Ninth 10%	_______________	$____________________	$______________	$_______________
Bottom 10%	_____ _________	$____________________	$______________	$_______________
	(Total 100%)			

*It is recognized that net income reported here does not take into account costs to distributors for conducting their MLM business. Such costs may include, travel, postage and shipping, long distance and other telephone costs, advertising, rental of meeting rooms and/or office space, fees for company conferences or retreats, supplies, sales materials, and other expenses.

THANK YOU FOR YOUR HELP!