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2010

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Available at: https://works.bepress.com/adam_epstein/5/
trade secret. In some circumstances, fortress-like barriers may be indeed called for. Absent real business purpose, protection policies can dilute the actual protection provided, and interfere with the ability of the firm to continue to generate valuable intellectual capital.

MULTI-LEVEL MARKETING AND ITS BRETHREN: THE LEGAL AND REGULATORY ENVIRONMENT IN THE DOWN ECONOMY

By

Adam Epstein*

This article explores the current legal environment surrounding the multi-level marketing business model also known as “network marketing” or simply MLM.291 MLM companies and the MLM model have generated legitimate direct selling business opportunities for non-salaried, independent business owners in the United States and around the world.292 Michigan-based Amway Global is often recognized as one of the most popular and

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291 See Grimes & Reese, P.L.L.C., Legal Principles of Multilevel Marketing, MLMLAW.COM, 2008, http://www.mlmlaw.com/library/guides/Primer.htm (Idaho-based law firm specializing in the direct selling industry and in-house counsel to direct selling company Melaleuca). Throughout this article, the acronym MLM may be used for “multi-level marketing organization or plan” for short. MLM is also referred to as direct selling and its members are often referred to as “distributors.”

292 See generally, Direct Selling Association, http://www.dsa.org/ (last visited Nov. 31, 2009). See also, Sergio Pareja, Sales Gone Wild: Will the FTC’s Business Opportunity Rule Put an End to Pyramid Marketing Schemes?, 39 McGeorge L. Rev. 83, 87-88 (2008) (thorough discussion of a variety of deceptive business opportunity schemes including pyramid schemes, Ponzi schemes, and MLMs, an analysis of a proposed modification to federal law with regard to the federal Franchise and Business Opportunity Rule at the time Pareja’s writing, and noting the steady increase in of “direct selling” participants in recent years).
successful MLMs and celebrated its 50th anniversary in 2009.\textsuperscript{293} Opportunities to work with an MLM such as Amway include the opportunity to start one’s own business and even work out of one’s own home.\textsuperscript{294} Published legal research in the area of MLM appears to be somewhat lacking, however.\textsuperscript{295}

Legitimate MLMs, though sometimes erroneously characterized as or confused with illegal pyramid or Ponzi schemes, have come under intense scrutiny due to the efforts of “rotten apples” which operated illegally and have been forced to pay hefty fines or terminate the operation altogether.\textsuperscript{296} A discussion of Ponzi schemes continues to be relevant today especially after the exposure of numerous Ponzi schemers in recent years beginning, of course, with a discussion and analysis of the downfall of financier Bernard Madoff’s scam, the largest Ponzi scheme in


\textsuperscript{299} See generally, Jeffrey A. Babener, MLM LEGAL, http://www.mlmlegal.com/ (Oregon-based attorney, editor, and member of Babener & Associates law firm) (last visited Nov. 1, 2009); See also, FitzPatrick, supra note 5, PYRAMID SCHEME ALERT, http://www.pyramidschemalert.org/ (Charlotte-based
Part I compares the MLM to pyramid schemes, Ponzi schemes and business opportunities. Part II explores the legislative authority and role that the administrative agencies have played in regulating MLMs with emphasis on the Federal Trade Commission (FTC) and the Securities and Exchange Commission (SEC). An exploration of a few state anti-pyramid and consumer protection statutes is presented demonstrating that MLMs are subject to governmental regulation and public critique from many angles. The author suggests that while MLMs will likely flourish in a down economy that it would be simple and appropriate to incorporate a three business day right-to-rescind (i.e., “cooling-off”) period for MLM enrollees within the various state consumer protection statutes mirroring the FTC’s current door-to-door sales rule.

Regardless of the statutory and regulatory landscape, information is readily available on the internet for consumers, prospective MLM members or anyone for that matter. Homepages of start-up and established MLM organizations, video postings on YouTube.com, MLM-related blogs and message boards provide ample access to MLMs. While MLM has had its share of legal challenges, the current regulatory environment in the internet era provides loads of information for prospects willing to assume personal responsibility for joining the MLM and to assist in differentiating the legitimate schemes from the scams.

I: THE MLM: LEGITIMATE BUSINESS OPPORTUNITY OR ILLEGAL PYRAMID SCHEME?

MLM is certainly big business in the United States, Canada and around the world involving millions of individual direct selling MLM members. MLMs offer opportunities to sell from a broad purchase price of $25 or more, whether under single or multiple contracts, in which the seller or his representative personally solicits the sale, including those in response to or following an invitation by the buyer, and the buyer’s agreement or offer to purchase is made at a place other than the place of business of the seller (e.g., sales at the buyer’s residence or at facilities rented on a temporary or short-term basis, such as hotel or motel rooms, convention centers, fairgrounds and restaurants, or sales at the buyer’s workplace or in dormitory lounges)...

See generally, Babener, supra note 7; See also, FitzPatrick, and Taylor, supra note 7; See also, James P. Nehf, Borderless Trade and the Consumer Interest: Protecting the Consumer in the Age of E-Commerce, 38 COLUM. J. TRANSNAT’L L. 457 (1999) (Review of book by John Dickie, INTERNET AND ELECTRONIC COMMERCE LAW IN THE EUROPEAN UNION, and noting that some of the most common online consumer complaints involve, inter alia, multi-level marketing (pyramid schemes, chain letters), bogus business opportunities, and ineffective health and diet products).

See Pareja, supra note 2 at 129 (refers to a three day “waiting” period); See also, FTC Rule Concerning Cooling-Off Period for Sales Made at Homes or Certain Other Locations, 16 C.F.R. § 429.0 et seq. (2009). (Door-to-Door Sale defined as “A sale, lease, or rental of consumer goods or services with a
spectrum of goods ranging from cosmetics to cleaning supplies to weight-loss pills to nutritional supplements to insurance.\footnote{See Jeffrey A. Babener, *MLM Company Profiles*, MLMLEGAL.COM, http://www.mlmlegal.com/profiles/index.html (lists of over one hundred links to MLM companies, divided alphabetically and by category) (last visited Nov. 1, 2009).}


stars, promote MLM products via endorsements as well.\footnote{See, e.g., Pareja, supra note 2, at 119-129 (critical discussion and analysis of ACN, an MLM company).}


MLMs, including their founding members, have drawn scrutiny for decades from federal and state regulators who have alleged violations of federal criminal statutes and questioned their legitimacy altogether more akin to a pyramid scheme.\footnote{Pareja, supra note 2, at 84-87, 96-97 (discussion of Charles Ponzi’s deceptive business scheme beginning in 1919, and noting a study demonstrated that 99.9 percent of investors in “business opportunities” lose money in the United States alone); Cf. Cabot Christianson, *You Can’t Cheat an Honest Man: Everything You Want to Know About Ponzi Schemes, 23 ALASKA B. RAG. Jan./Feb. 1999, (Review of book by James Walsh, noting that “Ponzi schemes have a strong-almost addictive-grasp on the people…”).}

MLM recruitment techniques can be extremely intense and sometimes misleading.\footnote{SEC v. Glenn W. Turner Enters., Inc., 474 F.2d 476, 479-80 (9th Cir. 1973) (These meetings are like an old time revival meeting...); See also, Robert T. Carroll, *Multi-Level Marketing (MLM) Harassment*, THE SKEPTIC’S DICTIONARY, http://www.skepdic.com/mlmhar.html (managers might unduly influence employee-subordinates to participate in an MLM) (last visited Nov. 1, 2009); Adam Hojnacki & Peter Scheck, *Get Rich Quick*, GENERATION,
It appears that some former members must seek post-separation assistance. Sometimes, a religious component might be used as part of the pep-rallies and sales pitches to new recruits or customers. As one MLM commentator notes, MLM sales and recruiting pitches make such outrageous claims as, “Make money like a gangster.” MLMs have required new members to buy into the scheme by paying a non-refundable initiation fee; this has drawn considerable and skeptical attention.

A. “Business Opportunity”

MLMs claim that they offer business opportunities for those who believe in their goods or services and wish to participate in selling them. However, the phrase “business opportunity” is actually a legal definition which has been legislated and interpreted at the federal and state levels as a matter of consumer protection.

http://www.subboard.com/generation/articles/116164656490688.asp (“Ponzi schemes have a strong - almost addictive - grasp on the people who perpetrate them and the people who invest in them”).


See Pareja, supra note 2, at 119-20 (Reference to ACN video quoting “This is a blessed company. We’re blessed people.”).


See Donna Fenn, Fast-Sinking Star, INC., Oct. 15, 2000, http://www.inc.com/magazine/20001015/20767.html (Equinox members were also expected to buy the products).


One of the first and most important legal issues involving an MLM is whether it has been established to sell anything or, instead, it is set up primarily to solicit others to join the group, the latter being considered an illegal pyramid scheme. Still, not all MLMs fall under the jurisdiction of state or federal “business opportunity” laws since the definition may contain specific exemptions or other ambiguities. Indeed, MLMs might even intentionally find and exploit loopholes in the statutes to avoid falling within the definition of a “business opportunity” from the get-go.

B. FTC’s Franchise and Business Opportunity Rule

In the name of consumer protection and in response to the prevalence of fraudulent pyramid schemes disguised as legitimate businesses, the FTC established its Franchise and Business Opportunity Rule (“Rule”) which appears to be undergoing consideration for modification. One of the hallmarks of the Rule is the requirement that if the minimum initial investment to participate in a business opportunity (such as an MLM) is $500.00 or more then it falls under the FTC’s federal jurisdictional umbrella and certain disclosure rules apply for potential buyers (participants). Indeed, many states have modeled their business opportunity statutes in the same way. Shady MLMs or fraudulent pyramid marketing schemes appear to have exploited the Rule with particular emphasis on avoiding the federal $500 minimum threshold.

In April, 2006, the FTC considered a proposal to adopt an amended version of its Rule which would have included all MLMs under its umbrella and to better stamp out unfair and deceptive practices such as illegal pyramiding. The FTC recognized that there was considerable input on the proposed Rule including ...
opinions from a variety of sources generating over 17,000 comments. As of the time of this writing, the FTC has decided to keep the status quo and to address MLMs under its current scheme which allows for jurisdiction involving unfair or deceptive practices and acts generally under Section 5 (a) of the FTC Act though it continued to advance a revised proposal generally. Though the current federal law related to business opportunities appears to be in flux, MLMs continue to press on.

C. The MLM’s Upline-Downline Structure

Key to any legitimately successful MLM is to understand the upline-downline structure in which the MLM member has someone “above” them and someone “below” them in the organizational hierarchy. MLMs compensate “upline” (i.e., vertical) members based upon actual sales of goods or services to customers from the “downline” members, theoretically ad infinitum in a pyramid-like structure. However, a structure that compensates its downline participants primarily based upon the recruitment of new downline participants rather than the actual sale of goods or services represents an illegal pyramid scheme. The distinguishing element between any MLM from its illegal adversary (i.e., the pyramid scheme) is that the legitimate MLM offers a third party (i.e., a third-party, retail consumer or any non-participant in the upline-downline structure) the chance to purchase an actual good or service. The illegal pyramid scheme only offers a promise of a positive return on an initial financial investment and only if additional members are recruited into the scheme.

To the ambitious MLM member, building a solid downline membership is vital and can be extremely exciting since residual income is earned from the continuous efforts and sales of the downline distribution network. An individual MLM member has a vested interest in the sustenance and success of the upline-downline structure, and this co-dependent upline-downline relationship can create an extreme synergistic-buzz of excitement for many MLM members who wish to benefit off the efforts of others. This creates a pyramid-like structure with more members below (less members above) as the MLM’s upline-downline organization grows. In that way, the downline generates multiple levels of possible commissions to the upline member as long as the


336 MLMs control the method and percentages of the commission structure, not individual members.


338 See Penn, supra note 30 (some Equinox meetings described as “high voltage” and cost up to $2,500).
downline distribution continues to sell. However, in order for the downline structure to expand, there must be the recruitment of new members as well which can be difficult to maintain. This pyramid shape alone, however, does not mean it is a pyramid scheme.

D. Pyramid Schemes

Pyramid schemes (and Ponzi schemes) are doomed to fail and MLM legal problems often begin when regulators pursue the organization as an illegal pyramid scheme disguised as an MLM. The FTC shed some light into how courts and governmental regulators might view the difference in a case in 1979 involving Amway. This significant decision, which held that Amway did, in fact, operate legally, seems to set the standard for all cases when addressing the difference between MLM and pyramid scheme.

For example, the Amway decision was given great deference twenty years later in U.S. v. Gold Unlimited, Inc., with the majority upholding a criminal conviction for a corporate “Get Rich Quick” scheme which focused more on pyramiding and less on retailing.341

Similarly, in Webster v. Omnitrion, Int'l Inc, the Ninth Circuit Court of Appeals, citing Amway as well, noted that pyramid schemes “are said to be inherently fraudulent.” Since the Amway decision in 1979 and its progeny, factors used to determine whether a business is a legitimate MLM or an illegitimate pyramid scheme, include:

1. Products have “no real world marketplace” and that the marketing program is a cover for a scam;

2. Products are sold at inflated prices;

3. That there is a substantial “buy-in” qualification also known as “inventory loading” or “front-loading” for the membership;

4. That there is an initial cash investment over $500;

5. That members must purchase ancillary products or services to remain in the program;

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342 In re Amway Corp., 93 F.T.C. 618, 715 (1979) (“a pyramid scheme is characterized by: The payment by participants of money to the company in return for which they receive (1) the right to sell a product and (2) the right to receive in return for recruiting other participants into the program rewards which are unrelated to sale of the product to ultimate users.”).

343 Webster v. Omnitrion Int'l, Inc., 79 F.3d 776 (9th Cir 1996); See also, Pareja, supra note 2, at 101-02 (noting that the Omnitrion case was the “seminal” Ninth Circuit case on pyramid schemes).

344 Webster at 781 (quoting In re Koscot Interplanetary, Inc., 86 F.T.C. 1106, 1181 (1975), aff'd mem. sub nom., Turner v. FTC, 580 F.2d 701 (D.C. Cir. 1978)); Compare Ger-Ro-Mar, Inc. v. FTC, 518 F.2d 33 (2d Cir. 1975) (FTC's claim that MLM business engaged in manufacture of brassieres, girdles, swimwear and lingerie constituted unfair practices failed though court found that some promotional materials were deceptive though not a pyramid scheme).

345 See Babener, supra note 5.

6. Whether the MLM has an inventory repurchase policy in the event that the member leaves the MLM;

7. That the emphasis is, or has become, more focused on rewards for recruiting than selling goods or services; and

8. Whether there are misrepresentations related to membership earnings claims or outright misrepresentations related to potential income by the member.347

E. Ponzi Schemes

A Ponzi scheme is named after Charles Ponzi, an Italian immigrant and already convicted who perpetrated a fraud on investors who were duped into thinking they could gain investment returns of 50 percent in less than two months.348 Unlike the legitimate MLM or the fraudulent pyramid scheme, a Ponzi scheme is an offer of a financial investment opportunity usually guaranteeing higher than average returns but without any further effort by the investor.349 While the terms “pyramid scheme” and “Ponzi scheme” are often used interchangeably, both are slightly different and they are illegal.350 In recent years, the number of Ponzi schemes that have been exposed has simply exploded.351 Anyone is susceptible to becoming a victim of a Ponzi scheme as demonstrated by the recent economic melt-down causing investors to withdraw their money from investment firms and banks.352

347 Id.; See, e.g., Fenn, supra note 30 (more than 80% of Equinox distributors made less than $1,000 a year and less than 2% earned more than $20,000); See also, Stephen Barrett, CASEWATCH, Quixtar Facing Class Action Lawsuit, http://www.casewatch.org/civil/amway/class_action_complaint.shtml (noting that Pyramid Scheme Alert’s Robert FitzPatrick submitted a declaration asserting that in 2001, 99.4% of all Quixtar distributors earned an average of $13.41 per week before product purchases, business expenses, and taxes, with the result that 99% of them made no profit) (last visited Nov. 2, 2009); See also, Kevin D. Grimes, Income and Earnings Representations, MLMSTARTUP.COM, 1996, http://www.mlmstartup.com/articles/incomereps.htm (last visited Nov. 2, 2009); But See MonaVie, Income Disclosure Statement Global 2008, http://media.monavie.com/pdf/corporate/income_disclosure_statement.pdf (last visited Nov. 2, 2009).


Unlike the pyramid scheme or legitimate MLM, the Ponzi scheme does not provide any upline-downline commission incentive arrangement in which participants share a vested interest in the scheme and does not reward for selling products or recruiting new members. Returns on investments are often marketed to the investor to be higher than the average and involve paying the early investors large dividends which entices others to join the con. From the outset of the initial investment, the promoter continually misrepresents how the investor's money is gaining financial returns. Ponzi promoters will send false financial statements to the investors stating bogus rates of returns comforting the investor who has no idea of the scam until it is too late. Then, to appear legitimate and to keep the scheme from collapsing altogether, the Ponzi promoter still must continue attract new investors especially if earlier investors scramble to cash out. However, the Ponzi scheme promoter has stolen the money, used it for themselves, lying to the investors all along. In some cases, the schemer files for bankruptcy itself to avoid paying creditors whose money has been stolen.

Since the Ponzi scheme involves an investment rather than the purchase or sale of goods, the SEC becomes involved when pursuing unfair and deceptive practices by the promoter. In 2009, Bernard Madoff pled guilty to the largest Ponzi scheme in history and countless others were charged with operating illegal Ponzi schemes as well. In the end, the Ponzi scheme bears no functional resemblance to an MLM or pyramid scheme other than that investors might, but are not required to, communicate and encourage others to join and even though no multi-level structure is involved.

F. Internet

Those who consider joining the MLM ranks now have virtually unlimited resources to explore more information about a particular MLM than ever before. Conducting diligent research via the internet from the home computer or public library can assist anyone in this decision-making process. Numerous websites provide a wealth of opportunity for the responsible decision-maker including the FTC website. YouTube.com serves as a seemingly endless conduit of postings by individuals for the serious prospect.

355 See Christianson, supra note 25.
357 See Pareja, supra note 2, at 102-04.
359 There are significant differences between an MLM and a business franchise for which this article does not address. See, e.g., Keith J. Kanouse, An Overview of Federal and State Business Opportunity Laws, 23 FRANCHISE L.J. 102 (2003); See also, See Melissa Ann Gauthier, The SJIC and Dunkin’ Donuts: Squeezing the Filling Out of the Small Franchisee, 41 NEW ENGL. L. REV. 757, 760-768 (2007); Debra Burke and E. Malcolm Abel II, Franchising Fraud: The Continuing Need for Reform, 40 AM. BUS. L.J. 355, 361-364 (2003); Pareja, supra note 2, at 91-93.
360 See Fitzpatrick, Hamblin, supra note 11.
or investigator on a particular MLM or MLMs generally. However, the internet has also opened up the opportunity for scams claiming to be legitimate MLMs.362 Social networking sites such as Facebook have recently changed their own policies to address concerns over schemes involving online incentivizing.363 Regardless of the model, name, structure or business opportunity, participation in an MLM involves various degrees of risk and personal responsibility, but the internet has leveled the playing field to preemptively gather information for the diligent prospect.

II: ANTI-PYRAMID REGULATION

Concerns over MLMs and pyramid schemes have caused the FTC and SEC to step up governmental regulation of business investments and opportunities. As mentioned, various states have enacted MLM statutes, also known as “anti-pyramid” statutes, to specifically address consumer protection concerns while other states rely on a broader consumer protection statute. Part II explores how the FTC, the SEC and state legislation have specifically addressed MLMs exposing how they have come under fire since the Amway decision.


A. Federal Trade Commission

The Federal Trade Commission (FTC) is considered an independent federal agency which works for the consumer to protect and prevent fraudulent, deceptive and unfair business practices in the interstate marketplace.364 Since 1914, it has had the legal authority to investigate a variety of consumer complaints under the Federal Trade Commission Act (the FTC Act).365 The FTC’s Bureau of Consumer Protection has seven divisions which work to protect consumers against unfair, deceptive, or fraudulent practices in the marketplace including the internet.366 The FTC is the leading federal administrative agency force behind protecting consumers from fraudulent MLMs, pyramid schemes and the like. The FTC has been involved in significant litigation or administrative settlements related to MLMs which have conducted illegal activities including, but not limited to actions involving Amway,367 JewelWay International, Inc.,368 Equinox

364 See generally, Federal Trade Commission, http://www.ftc.gov (last visited Nov. 3, 2009); See also, Pareja, supra note 2, at 89.


367 In re Amway Corp. 93 F.T.C. 618 (1979).

International, SkyBiz, Fortuna Alliance, and many others. Following an investigation, the FTC might initiate an enforcement action if it has "reason to believe" that the law is being or has been violated. Section 5(a) of the FTC Act is broad and powerful and provides that unfair or deceptive acts or practices in or affecting commerce are unlawful. The FTC may pursue federal district court proceedings to enjoin violations of the FTC Act and to secure equitable relief in each case including restitution and disgorgement.

In the 1979 Amway decision, the FTC ruled that Amway was not a pyramid scheme because it adopted and enforced certain rules that were intended to avoid the characteristics of a pyramid scheme. In sum, this decision held that a direct marketing business like Amway would not be considered a pyramid scheme if the sponsor of the business did not violate various rules including the Amway

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375 In re Amway Corp., 93 F.T.C. 618, 717 (1979). The 70 percent rule requires distributors to have sold 70 percent of previously purchased product before reordering (preventing "inventory loading").

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B. Securities and Exchange Commission

Like the FTC, the SEC is an independent governmental agency which has the authority to protect those who have been harmed by the fraudulent efforts of others. Created by section 4 of the Securities Exchange Act of 1934, the SEC is primarily responsible for enforcing the federal securities laws and regulating the securities industry. It was created by section 4 of the Securities Exchange Act of 1934. It enforces the Securities Act of 1933 among other acts and statutes.

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376 Known as the "Amway safeguards." See Jeffrey A. Babener, Network Marketing and the Law, 57 OR. ST. B. BULL. 23, 35 (1997); See also, Pareja, supra note 2, at 95.

377 See U.S. v. Gold Unlimited, Inc., 177 F.3d 472, 482 (6th Cir. 1999) ("the critical determination of the legality of [defendant's] operations will not be based on the written plan but on the actual practices of the company,"); quoting SEC v. Int'l Heritage, Inc., 4 F.Supp.2d 1378, 1384 (N.D. Ga. 1998); But see Webster v. Omnitrion Int'l, Inc., 79 F.3d 776, 783 (Amway safeguards are essentially meaningless if commissions are paid based on a distributor's wholesale sales, and not those sold at retail); See also, Valentine, supra note 24 (noting that at time the FTC had brought eight cases against pyramid schemes in two years alone).


With respect to MLMs, the SEC first asks whether there is a security involved and, if so, are there materially false or misleading statements. The SEC has asserted jurisdiction over allegations of Ponzi and pyramid schemes on the grounds that they constitute "investment contracts" subject to enforcement under federal securities laws. The SEC has also utilized temporary restraining orders, injunctions and "freeze orders" when Ponzi schemers have attempted to avoid returning investors' money by filing for bankruptcy protection.

Some MLMs may pretend to be product-based to avoid appearing as an investment, thereby avoiding SEC scrutiny. However, the SEC notes that the hallmark of pyramid schemes is "the promise of sky-high returns in a short period of time for doing nothing other than handing over your money and getting others to do the same." The SEC also points out that "fraudsters simply use money coming in from new recruits to pay off early state investors. But eventually the pyramid will collapse. At some point the schemes get too big, the promoter cannot raise enough money from new investors to pay earlier investors, and many people lose their money."

As mentioned, securities regulators examine MLMs, pyramid schemes, and Ponzi schemes for an investment contract, and therefore, securities, as defined by Section 2(1) of the Securities Act of 1933 and Section 3(a)(10) of the Securities Exchange Act of 1934. The SEC established that an MLM could be transformed into a security when the scheme looked more like a pyramid scheme in which the activity of a distributor was "passive" rather than "active," triggering its jurisdiction umbrella to open. Unfortunately for this agency, the SEC also was thrust into the spotlight during the discovery of Madoff's $50 billion Ponzi scheme, albeit in a negative light, as having failed miserably in its regulation and the failure to investigate Madoff's "curiously steady" annual returns, and ignoring the cries from whistleblowers exclaiming his operation was full of fraud.

C. The Howey Test

In 1946, the United States Supreme Court in SEC v. W.J. Howey Co. handed down a landmark decision related to securities...
regulation. According to the Court, key for purposes of SEC regulation are the existence and elements of an “investment contract” which include, (1) an investment (2) in a common enterprise (3) with a reasonable expectation of profits (4) to be derived solely from the entrepreneurial or managerial efforts of others. The Howey court stressed that the definition of “securities” is a flexible principle that is “capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.” It emphasized that the Howey test would serve the statutory policy of “affording broad protection to investors.”

The Howey test has had a broad interpretation in subsequent cases. In Tcherepnin v. Knight, decided over twenty years later, the court furthered a broader reading of the term “securities” by stating that “even a casual reading of . . . the 1934 Act reveals that Congress did not intend to adopt a narrow or restrictive concept of security in defining that term.” Wright also notes that in SEC v. Glenn W. Turner Enterprises the Ninth Circuit held that the word “solely,” as applied in the Howey test, should not be read as a strict limitation in defining what a security is. Wright notes that the “efforts” of the promoters in Turner satisfied the Howey test because they were the “undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.”

In SEC v. Koscot Interplanetary, Inc., Wright notes that the scheme was deemed to involve securities because the “investor’s realization of profits is inextricably tied to the success of the promotional scheme.” However, the appellate court in Koscot warned that the “Howey test is not possessed of the talismanic quality ascribed to it by the court below.” Thus, though the Koscot court used the Howey test, it stressed the importance for the test to be resilient enough to encompass egregious promotional schemes.

In sum, both the FTC and SEC have broad powers to regulate business opportunities such as MLMs and investment securities. With regard to actually what a “security” is, the Howey test appears to remain interpreted in the broadest light. As discussed, both the FTC and SEC have been involved in MLM litigation, but they are not the only government agencies who have the ability to pursue illegitimate schemers. Various states have specifically enacted statutes which address the actions of the schemers as well.

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392 Id. at 294-301. But see State v. Irons, 574 N.W.2d 144, 150 (Neb. 1998) (state MLM criminal case addressing whether investment profits must be derived “solely” from the efforts of others, citing Reves v. Ernst & Young, 494 U.S. 56 (1990)).
393 Id. at 299.
394 Id. at 301.
396 Wright, referencing SEC v. Glenn W. Turner Enters., Inc., supra note 93, at 481-482 (“the sticking point in the Howey definition is “solely,”...”).
397 SEC v. Glenn W. Turner Enters., Inc., supra note 93, at 482.
399 Id. at 481.
400 Id. at 486.
402 Attempts have been made to establish a federal anti-pyramiding bill which actually passed the United States Senate twice in the 1970s. See Valentine, supra, note 25; See also, Pareja, supra note 2, at 105 (noting that state laws are inadequate an unmanageable by state enforcement agencies especially when they cross state lines, all the more reason in support for a comprehensive federal rule with regard to pyramid schemes).
D. State Regulation

There is no federal anti-pyramid statute in the United States, but states have enacted laws directed specifically at MLM plans often referred to as “anti-pyramid” scheme legislation. Many of these state laws prohibit sales of business opportunities unless the seller gives potential purchasers a pre-sale disclosure document that has first been filed with a designated state agency. However, disclosures required by state business opportunity laws differ and might provide more abbreviated information than the FTC’s Rule requires.

Louisiana adopted its anti-pyramid statute in 1997 and defines a prohibited “pyramid promotional scheme” as: “Any plan or operation by which a participant gives consideration for the opportunity to receive compensation which is derived primarily from the person’s introduction of other persons into a plan or operation rather than from the sale of goods, services, or intangible property by the participant or other persons introduced into the plan or operation.” California defines pyramid schemes as “endless chains” and prohibits: “Any scheme for the disposal or distribution of property whereby a participant pays a valuable consideration for the chance to receive compensation for introducing one or more additional persons into participation in the

403 See Grimes & Reese, P.L.L.C., supra note 1 (noting that only a few states actual define MLM plans including Georgia, Louisiana, Maryland, Massachusetts, Puerto Rico, and Wyoming though many states use the term “pyramid,” “chain distributor” or “endless-chain” instead, including, for example North Carolina, New York, Texas, and others); See also, Grimes & Reese, P.L.L.C., Multi-level Marketing Cases, MLMLAW.COM, http://www.mlmlaw.com/mlmnstates.html (last visited Nov. 2, 2009).

404 See Grimes & Reese, P.L.L.C., supra note 1.

405 See Pareja, supra note 2, at 104-5.

406 L.A. R.S. §§51:361 et seq. (2009); See also, Howie, supra note 46, at 289.


408 “Endless chain” means any scheme for the disposal or distribution of property whereby a participant pays a valuable consideration for the chance to receive compensation for introducing one or more additional persons into participation in the scheme or for the chance to receive compensation when a person introduced by the participant introduces a new participant. V.T.C.A., PENAL CODE 32.48 (2009); Compare Illinois’ which classifies pyramid schemes as criminal acts of deception directed against property. 720 ILL. COMP. STAT. ANN. §§17-7 (2009).

participant introduces one or more additional persons into participation in the plan, each of whom receives the same or similar right, privilege, license, chance, or opportunity.

(2) A pyramid or chain promotion is declared to be illegal and against the public policy of the state. Any contract made in violation of this section is voidable at the sole option of the purchaser.

(3) The department shall not accept for filing a franchise which involves a pyramid or chain distribution contrary to the laws of this state. 410

It would be certainly wise to review all of these state laws for anyone involved with an MLM or those wishing to start one in a particular state. Unfortunately, state consumer protection statutes regarding pyramid schemes appear to have devolved into impotent provisions lacking an effective enforcement mechanism. 411

According to a 2009 report, almost all states' unfair deceptive acts and practices statutes have been undermined by significant gaps or court decisions. 412

412 Carter, supra note 121.

E. Future Consideration

As discussed, the regulatory environment for the MLM includes a combination of state and federal laws under a jurisdictional umbrella which includes federal administrative watchdog agencies such as the FTC and SEC. Still, many individuals might seek opportunities to generate income (such as by joining the MLM) even if it means relying more on the attraction of an initial revival-like excitement portrayed by its membership instead of a thorough analysis of the organization, its often non-refundable sign-up fees, the realistic (or average) earning potential of the enrollees, and the quality of its products or services. 413 With little hope for new jobs in this down economy, some might join the MLM ranks as a commission-based independent contractor in an act of desperation. 414

So, while some measure of personal responsibility must be expected when determining whether to join an MLM, is it realistic to assume that most MLM participants will take the initiative to research MLMs prior to agreeing to participate in them? Joining an MLM is a matter of personal choice, but it is possible that many enrollees could regret joining and suffer from buyer's remorse after they hype has subsided. Others may become disenchanted with the lack of income generated from the investment in the MLM after diligent efforts to produce.

413 See, e.g., Pareja, supra note 2, at 129 (“Prospective purchasers must also be given sufficient time to absorb the information. At a minimum, this means that an individual opportunity seller must provide the prospective recruit with a written disclosure of average and median net, not gross, income of all company representatives over a one year period.”).
This author supports a suggestion that the various states could include in their consumer protection statutes a three business day right-to-rescind (i.e., “cooling off”) period specifically to address MLM enrollees.\textsuperscript{415} State legislatures could modify state laws to mirror the FTC’s door-to-door sales rule and could allow for this three-day “cooling off” period after joining an MLM which would make the contract voidable during that time-frame for any reason even if the “sale” was not made in the home.\textsuperscript{416} In this way, those who decide to join the MLM could feel some measure of comfort in knowing at least they could remove themselves from the organization within three business days from the hype of signing up. Requiring a conspicuous disclosure of this three-day right to rescind period would also be consistent with other state consumer protection statutes as well.\textsuperscript{417}

\textsuperscript{415} See Pareja, supra note 2, at 104-05, 129 (Pareja’s discussion actually suggests that a contract to join could not even be offered until three days after the first meeting and calls for a federal rule focusing more on disclosure requirements at the federal level than at the state levels. Pareja recognizes the difficulties in attempting to administratively enforce state disclosure rules involving “pyramid marketing schemes” especially since MLMs are involved in interstate activity involving inconsistent state laws. However, this author suggests that a more localized approach to MLM regulation might be more appropriate (even with the lack of consistency among states), and that incorporating a three-day cooling-off period in a state consumer protection statute might be a less bureaucratic first step in the right direction mirroring and already accepted FTC rule).

\textsuperscript{416} See FTC Rule Concerning Cooling-Off Period for Sales Made at Homes or Certain Other Locations, 16 C.F.R. § 429.0 et seq. (2009), supra note 12; See also, Mike Cox, Attorney General, I Changed My Mind...Can I Cancel this Contract, Jan. 2009, http://www.michigan.gov/ag/0,1607,7-164-34739_20942-44718--,00.html (discussion of various Michigan provisions which address a right to cancellation) (last visited Apr. 12, 2010).


III. CONCLUSION

While legitimate MLMs, such as Amway, emphasize the selling goods or services (i.e., retailing) rather than signing-up recruits to join the organization’s ranks (i.e., pyramidising), this article has demonstrated that the legal environment in the MLM world is quite complex and involves a myriad of regulatory schemes emanating from FTC, SEC, and the various state anti-pyramid or consumer protection statutes. The revelation of swarms of numerous financial swindlers in recent years such as Bernard Madoff have certainly not helped those who support the MLM model even if Ponzi schemes or pyramids have little in common with legitimate MLMs.

The internet allows an MLM to share its vision and spread its message to anyone in the world via the computer. Potential MLM members are able to conduct thorough investigations of an MLM on their own time, in their own home, even before agreeing to attend “opportunity meetings” in order to make an informed, educated decision.\textsuperscript{418} Thus, MLM prospects must share some measure of personal responsibility for participating in any MLM venture today.\textsuperscript{419} One consideration to balance the concern

Freeway Mobile Home Sales, 521 P.2d 1119 (Ariz. 1974)); See also, e.g., Paul L. Reynolds, Chernick v. Fasig-Tipton: A Caeve to the Horse Trader, 74 KY. L.J. 889 (1985); Compare Anthony M. Balloon, From Wax Seals to Hypertext: Electronic Signatures, Contract Formation, and a New Model for Consumer Protection in Internet Transactions, 50 EMORY L.J. 905 (2001); See also generally, Pareja, supra note 2, (discussion of importance of disclosure requirements at the federal and state levels including the disclosure requirements under the revised proposed Rule).

\textsuperscript{418} See Pareja, supra note 2, at 119-20 (support of revised proposed Rule which would have mandated a waiting period after the occurrence of an “opportunity meeting” to allow for a cooling-off for potential MLM members to avoid the “pressure of the moment” before even being able to sign up).

\textsuperscript{419} The author notes that throughout this article he is not making any disparaging remark about or judgment related to the quality of any product
between personal responsibility and consumer protection generally
could be specifically to include MLMs under state consumer
protection statutes providing a three day right-to-rescind period
akin to the protections offered under FTC's door-to-door sales
rules even if the opportunity to join was not presented in one's
home.

It will be interesting to see in the coming years how many more
MLMs, pyramid schemes, Ponzi schemes and other business
opportunities will be exposed as illegitimate frauds in this world or
the virtual one. There appears to be a paucity of legal research in
the area of MLMs. Nonetheless, numerous websites, including the
homepages of MLMs, have loads of information for prospective
participants to help themselves in weeding out the good from the
bad, the reality of participation in an MLM from the fantasy.\textsuperscript{420}

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\textsuperscript{420} See Ger-Ro-Mar, Inc. v. FTC, \textit{supra} note 54 at 37 ("We find no flaw in the
mathematics...that the prospect of a quarter of a billion brassiere and girdle
hawkers is not only impossible but frightening to contemplate, particularly since
it is in excess of the present population of the Nation, only about half of whom
hopefully are prospective lingerie consumers. However, we live in a real world
and not fantasyland.").

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\textit{Gender Stereotyping: The EvC
Protections for Gender Non-
By
Bonnie L. Roach\textsuperscript{*}

I. INTRODUCTION

Consider the following situations: A woman who was told she
couldn't make partner because she didn't dress or act "femininely
enough"; a woman who was terminated because she was
considered "too masculine"; a man who was told he held his
serving tray "like a woman"; a male firefighter who experienced
adverse actions when he had to dress as a female for his sexual
reassignment surgery; a male police officer who decided to go
through with gender reassignment surgery and when he dressed as
a woman was told he did not possess a "command presence"; and a
male machine operator who was told he was "too flamboyant". All
of these individuals filed discrimination charges based on TVII sex
discrimination based on nonconformance to gender stereotype.

Since its inception, TVII has considered gender discrimination,
whether intentional or not, is a federal offense for employers with
15 or more employees. It has long been held that Title VII protects
men and women against intentional discrimination, known as
disparate treatment, and also protects individuals against disparate