

January 23, 2019

The Honorable Marc Veasey
United States House of Representatives
2348 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Richard Hudson
United States House of Representatives
2112 Rayburn House Office Building
Washington, D.C. 20515

RE: Consumer group opposition to legislation weakening the Federal Trade Commission's ability to protect consumers from pyramid schemes

Dear Congressman Veasey and Congressman Hudson,

In the 115th Congress, the undersigned consumer and civil rights organizations opposed the mis-named legislation, the Anti Pyramid Promotional Scheme Act (H.R. 3409). We are writing to request that you refrain from re-introducing this anti-consumer bill in the current Congress.

For over 40 years, the Federal Trade Commission (FTC) has protected consumers, on a bipartisan and unanimous basis, against pyramid schemes masquerading as business opportunities.¹ The reason for the FTC's focus on pyramid schemes is understandable. These scams lure would-be entrepreneurs into supposedly lucrative business opportunities that, by design, defraud the vast majority of "investors." Such schemes run

¹ Federal Trade Commission. "FTC Asks Court to Shut Down Illegal Pyramid Operation," press release, June 12, 2017, Online: <https://www.ftc.gov/news-events/press-releases/2007/06/ftc-asks-court-shut-down-illegal-pyramid-operation>

Federal Trade Commission. "FTC Acts to Halt Vemma as Alleged Pyramid Scheme," press release, August 26, 2015. Online: <https://www.ftc.gov/news-events/press-releases/2015/08/ftc-acts-halt-vemmas-alleged-pyramid-scheme>

Federal Trade Commission. "Herbalife Will Restructure Its Multi-level Marketing Operations and Pay \$200 Million For Consumer Redress to Settle FTC Charges," press release, July 15, 2016. Online: <https://www.ftc.gov/news-events/press-releases/2016/07/herbalife-will-restructure-its-multi-level-marketing-operations>

contrary to the entrepreneurial spirit that has empowered the American dream for decades.

After the 1979 *Amway* decision, the FTC's successful track record in prosecuting pyramid schemes shows just how careful the Commission has been in distinguishing blatant pyramid schemes from multi-level marketing (MLM) companies. Over the course of this enforcement history, the FTC and the courts have developed case law that provides clear guidance for how MLM businesses can avoid violating Section 5 of the FTC Act. Specifically, direct selling businesses must derive their revenue primarily from the verifiable sale of products and services to customers outside of the business opportunity, and must refrain from unsubstantiated product and income claims.

H.R. 3409 would have blocked the FTC's ability to protect consumers from all but the most blatant pyramid schemes. The legislation would have interfered with the FTC's authority in a number of ways, including:

1. Eliminating the need for direct selling operators to have genuine retail customers external to the people recruited into the business opportunity by re-defining an "ultimate user" in a way that runs counter to more than 40 years of case law, going back to the foundational *Koscot* decision in 1975.² Such a re-definition would relieve direct selling businesses of the obligation to operate a viable retail business as opposed to a fraudulent recruitment scheme.
2. Allowing direct selling companies to drive excessive inventory loading by their recruits, letting the operators profit off a churning base of recruits who are

² Federal Trade Commission. "In the Matter of Koscot Interplanetary inc., Et Al. Order, Opinion, etc., In Regard to the Alleged Violation of the Federal Trade Commission Act and Sec. 2 of the Clayton Act," November 18, 1975. Online: https://www.ftc.gov/sites/default/files/documents/commission_decision_volumes/volume-86/ftc_volume_decision_86_july_-_december_1975pages_1106-1202.pdf

continually incentivized to purchase more product in order to qualify for recruitment rewards rather than meeting legitimate retail demand for the product or service they offer.

3. Creating a safe harbor for direct selling operators that would allow pyramid schemes to evade FTC enforcement action through the use of a “bona fide inventory re-purchase program” (commonly known as a “buyback program”), regardless of whether such a re-purchase program actually reduces the risk to recruits of being stuck with unsold inventory.

The flaws in this bill have been recognized by a bipartisan group of former FTC directors, commissioners, and bureau chiefs who have all urged Members of Congress not to pursue it.^{3 4} Likewise, even leading members of the direct selling industry itself oppose this bill.^{5 6} Given these concerns, the undersigned consumer and civil rights groups urge you to not re-introduce the Anti Pyramid Promotional Scheme Act in the 116th Congress.

Sincerely,

Consumer Action

Consumer Federation of America

Consumer Reports

MANA, A National Latina Organization

National Association of Consumer Advocates

National Consumer Law Center (*on behalf of its low-income clients*)

³ McSweeney, Terrell. “Congress should crack down on predatory ‘pyramid schemes,’ not look away,” *The Hill*. August 3, 2017. Online: <http://thehill.com/blogs/pundits-blog/finance/345073-congress-should-crack-down-on-predatory-pyramid-schemes-not-look>

⁴ National Consumers League. “Former senior FTC officials call on Congress to oppose pyramid scheme promotion bill,” press release. September 13, 2017. Online: http://www.nclnet.org/ftc_alumni_moolenaar

⁵ Rosen, Eric. Letter from Herbalife to the Honorable Marsha Blackburn and the Honorable Marc Veasey. July 28, 2017. Online: <https://www.scribd.com/document/356458302/Blackburn-Veasey-072817>

⁶ Vandersloot, Frank. “Anti-pyramid measure is really a pro-pyramid bill,” *The Hill*. September 6, 2017. Online: <https://thehill.com/blogs/congress-blog/politics/349537-anti-pyramid-measure-is-a-step-in-the-wrong-direction-for>

National Consumers League

truthinadvertising.org

U.S. PIRG

William W. Keep, PhD, Interim Provost/VPAA, Professor of Marketing, The College of New Jersey

Peter J. Vander Nat, PhD, Senior Economist (retired), Federal Trade Commission

cc: Members of the Direct Sellers Caucus and Cosponsors of The Anti Pyramid Promotional Scheme Act of 2017