Dismantling a pyramid: Lessons from the Vemma settlement

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Promoting a "Young People's Revolution," multi-level marketer Vemma pitched its business opportunity to college students and other young adults as a big-money, fast-lane alternative to "the traditional 9-to-5." In 2015, the FTC sued Vemma and related parties, alleging that its smoke-and-mirrors earnings claims were obscuring the true nature of what Vemma was up to. As a result of an FTC settlement, there's a revolution underway all right. But it's dismantling the alleged pyramid at the center of Vemma's operation.

According to the FTC's complaint, rather than marketing the company's health drinks to the general public, the defendants encouraged participants to qualify for bonuses by buying products themselves and recruiting others to do the same. The result, the FTC charged, was a classic pyramid scheme that compensated participants mainly for enrolling others in the network, rather than for retail sales based on legitimate consumer demand for Vemma's beverages.

But what about the fancy cars, jets, and earnings of "$50,000 per month"? The FTC also alleged that Vemma used deceptive income claims to recruit people into its affiliate network, when – truth be told – the vast majority of participants lost money.

The court-enforceable settlement includes provisions designed to change the shape of Vemma's structure from pyramid to "on the level." To protect consumers in the future, Vemma and CEO B.K. Boreyko are prohibited from:

compensating participants for enrolling new recruits;

tying compensation to participants' own product purchases; and

paying any compensation for a pay period unless the majority of the revenue generated during that time – both by the participant and others he or she has recruited – comes from sales to non-participants.

That last provision is key. It shifts the focus away from signing up new recruits and puts it back where it belongs: on selling products to people who aren't part of the network structure. By doing this, the company incentivizes sales over recruitment. The settlement also bars the defendants from making deceptive income claims and unproven health representations. The $238 million judgment against Vemma and Boreyko will be partially suspended upon payment of $470,136 and the surrender of certain real estate and business assets.

A separate settlement with Vemma affiliate Tom Alkazin and Bethany Alkazin puts similar provisions in place and imposes a judgment of more than $6.7 million, which will be partially suspended when they pay more than $1.2 million and surrender certain assets.

Are the Vemma settlements, the FTC's $200 million Herbalife order, and the recent action against Fortune Hi-Tech Marketing (FHTM) striking a familiar chord? They should because they all reinforce two fundamental legal principles:

1. The *raison d'être* for any legitimate business is to sell products to people who aren't affiliated with the company. This isn't just a theoretical point. An MLM's compensation plan should reward real sales to customers outside the network. That's not how Vemma and Herbalife operated, and the FTC alleged that both companies ran afoul of the law in different ways. The FTC orders require Vemma and Herbalife to change their business models to comply with the law, and given their different business structures, use different remedies to reach that result. What other MLMs do will depend on their structure and circumstance. But here are two key features that the Vemma and Herbalife orders have in common. Both companies will have to distinguish between the people who join just to buy the product vs. participants who

join to make money – and they must track those sales separately. And both will have compensation schemes that incentivize sales to people outside the network instead of recruitment of new participants.

2. Using misleading earnings claims and convoluted compensation schemes to deceive consumers is illegal. Established truth-in-advertising principles apply in the MLM world, and the FTC remains committed to combating questionable practices.