



DIRECT SELLING ASSOCIATION

DIRECT SELLING MYTH VS. FACT

MYTH: Direct selling companies are pyramid schemes.

FACT: Direct selling companies and pyramid schemes are not the same.

Bad actors in the marketplace sometimes masquerade as direct sellers, harming consumers and legitimate direct selling companies. There are a number of important differences between direct selling companies and pyramid schemes. First, an important difference is that direct selling companies offer protections and guarantees to those that interact with them so their sellers and customers can be confident they are safeguarded. Also, member companies of the Direct Selling Association (DSA) adhere to a rigorous set of standards as part of its Code of Ethics, including requirements that member companies buy back unused inventory at no less than 90% of the original purchase price.

Pyramid schemes are illegal and should be prosecuted to the fullest extent of the law. At this time there is no set definition of a pyramid scheme in federal law. For this reason, the Direct Selling Association (DSA) supports H.R. 5230, the Anti-Pyramid Promotional Scheme Act of 2016, bipartisan consumer protection legislation that would clearly define a pyramid scheme in federal statute for the first time.

None of the key provisions of H.R. 5230 are new or outlandish. The legislation is based on the widely-accepted principle that a scheme exists when compensation is based primarily on recruitment rather than retail sales, and that personal use is a legitimate business practice in direct selling. DSA has long been working to codify consumer protection law at the state level. Forty-nine states have codified laws banning pyramid schemes, and numerous court decisions have used the same definition of a scheme that H.R. 5230 seeks to enact at the federal level. This pro-consumer measure mitigates confusion and extends protection of consumers and direct sellers at the federal level as a natural next step.

MYTH: Purchasing products from a direct selling company at a discount isn't a legitimate business practice.

FACT: There are many reasons why independent contractors become involved with and stay in the direct selling industry, including the ability to buy products and services they love for their personal use at a discounted price.

In fact, this is one of the reasons why many people decide to get into direct selling in the first place. And in many cases, it's an entry point for people to then go into selling to others.

MYTH: All direct sellers are required to purchase inventory themselves to start selling.

FACT: This is simply not true. Every company is different, but many direct selling companies allow independent consultants to take orders from customers without requiring them to purchase inventory themselves. Typically, independent consultants also decide to purchase products for their own use because they love what's offered or want to familiarize themselves with various product and service lines.

While some individuals in direct selling may purchase inventory to sell, members of DSA abide by a Code of Ethics with key provisions that protect direct sellers against financial loss. This includes requirements that all companies purchase unused inventory from independent consultants at 90% or more of the original cost.

In contrast, bad actors may engage in the practice of inventory loading – where individuals

are convinced to buy large amounts of products or services that cannot be easily sold to others or returned. This practice is unethical and harms direct sellers. It is also a warning sign of a pyramid scheme.

MYTH: The direct selling model involves high financial risks for those involved.

FACT: One of the many reasons why direct selling is appealing is its low cost of entry and relatively low financial risk. While the average cost of entry in direct sales is \$106.40, the cost to other types of independent consultants in other industries, such as realtors and restaurant franchise owners, may be anywhere from \$1,000 to well over \$100,000.

Most direct selling companies offer protections and guarantees to their customers and independent consultants, many of which exceed Federal Trade Commission (FTC) regulations, as well as federal and state law. The members of DSA also adhere to a rigorous set of standards as part of its Code of Ethics, including requirements that member companies buy back unused inventory at no less than 90% of the original purchase price.

MYTH: Direct selling takes advantage of vulnerable populations, such as certain Hispanic American communities.

FACT: This is simply not true. Hispanic Americans represent 20% of the more than 20 million people involved in direct selling, and for whom direct selling represents a key entry point to join the growing ranks of Latino business owners.

The low cost of entry and low risk of direct selling makes it appealing to many Americans looking to empower themselves and their families. The typical start-up cost is \$100 or less – as opposed to the thousands or even millions associated with franchises or other types of small businesses. In addition, direct sellers have protections against financial risk through DSA's Code of Ethics, which requires its member companies to buy back unused inventory at no less than 90% of the original purchase price.

However, there are bad actors in the marketplace that sometimes masquerade as direct sellers and target vulnerable populations. That is why it is critical that safeguards are put in place to educate consumers and sellers and to guard against pyramid schemes. For that reason, DSA supports H.R. 5230, the Anti-Pyramid Promotional Scheme Act of 2016, a bipartisan legislation that protects the financial security of Latinos and all Americans by clearly defining the difference between a direct selling company and pyramid scheme. This pro-consumer legislation helps consumers avoid pyramid schemes and preserves the integrity of the direct selling model – a vehicle of economic opportunity for millions of Hispanic Americans and many others.

MYTH: The primary reason people get involved in direct selling is to make a large income.

FACT: Direct sellers become involved and stay in the business for a wide variety of reasons. These include being able to buy products and services they like at a discounted price, flexibility and work-life balance or the entrepreneurial opportunity to earn supplemental income, among others.

For most Americans involved in direct sales, the revenue they earn is not their primary income but the way to a family vacation, presents for the holidays or just extra spending money. In fact, most independent contractors only work part time in direct sales, and many have other jobs.

MYTH: A majority of people involved in direct selling never make a profit.

FACT: People involved in direct selling are motivated by and have different metrics of success. They may be interested in the flexibility provided by direct selling, or look to supplement their existing income.

In 2015, people involved in direct selling made more revenue than any previous year. However, a majority do not use direct sales as their primary source of income. Instead, they look to use the supplemental income they earn from direct selling for family vacations, presents for the holidays, or just extra spending money. In fact, most independent contractors only work part time in direct sales, and many have other jobs.

MYTH: The Anti-Pyramid Promotional Scheme Act (H.R. 5230) will weaken the government's ability to prosecute pyramid schemes.

FACT: H.R. 5230 does nothing to change the FTC's existing enforcement authority against illegal pyramid schemes.

This bipartisan legislation would clearly define a pyramid scheme in federal statute for the first time.

None of the key provisions of H.R. 5230 are new or outlandish – that a scheme exists when compensation is based primarily on recruitment rather than retail sales, and that personal use is a legitimate business practice in direct selling.

Forty-nine states have codified laws banning pyramid schemes, and numerous court decisions have used the same definition of a scheme that H.R. 5230 seeks to enact at the federal level. This pro-consumer measure extends protection of consumers and direct selling independent consultants at the federal level as a natural next step.

MYTH: DSA is solely responsible for H.R. 5230.

FACT: This bipartisan legislation is sponsored by U.S. Reps. Marsha Blackburn (R-TN) and Marc Veasey (D-TX), and has currently garnered support from more than 30 members of the Congressional Hispanic Caucus, Congressional Black Caucus, Direct Selling Caucus and Energy & Commerce Committee, as well as a variety of industry and non-profit organizations.

As the voice of direct selling in the U.S., DSA has long worked to promote strong consumer protection legislation, including supporting laws banning pyramid schemes that have been codified in almost every state. Supporting legislation to define pyramid schemes at the federal level is a natural next step.

Forty-nine states have codified laws banning pyramid schemes, and numerous court decisions have used the same definition of a scheme that H.R. 5230 seeks to enact at the federal level. In addition, more than a third of the states have anti-pyramid statutes that explicitly sanction personal use. This pro-consumer measure extends protection of consumers and direct sellers at the federal level as a natural next step.

MYTH: Herbalife's settlement agreement with FTC serves as guidance for the entire direct selling industry.

FACT: The settlement agreement of FTC's enquiry into Herbalife applies only to that company. However, it reinforces the importance of the principles and requirements of DSA's self-regulatory Code of Ethics for all DSA members.

Similar to Amway's action with the FTC in 1979, the remedies set forth in the Herbalife matter apply only to that company, and not the entire industry. While this settlement gives us

insight into the FTC's thinking regarding business practices associated with direct selling, it would be a mistake to apply facts and remedies specific to one company to an entire industry.

Nevertheless, we continue to review the settlement and examine various issues raised by the FTC's settlement with Herbalife.