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The Behavioral Economics of Multilevel Marketing

*Heidi Liu**

Abstract

Multilevel marketing companies (MLMs) — sales organizations that compensate independent consultants based on the sales and recruitment of other consultants — form a significant part of the American economy. Yet, MLMs provide little information to regulators and potential participants regarding potentially material information. Although MLMs are often compared to pyramid schemes, consultants argue that participation in a MLM allows them to make money outside of the traditional full-time labor force. This paper examines the law, economics, and psychology of MLMs, suggesting that MLMs may draw on prospective consultants’ cognitive biases in persuading consultants to join and continue a MLM. Consultants may be led to focus on unlikely benefits and to conform to notions of success that seem consistent with the “American dream” — even to their financial loss.

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Upon entering the homepage of American Communication Network, LLC (better known as ACN), you are greeted with one sentence: “Stop waiting for life to happen and create it — with ACN!”¹ You have three options to proceed:

1. A large arrow that says “Start Today”
2. The phrase “Learn More” at the bottom of the page
3. In small, nearly transparent letters, the word “Scroll” (i.e., scroll down)²

Clicking “Start Today” takes you immediately to a “convenient online form” with a \$499 application fee: A lengthy “ACN Independent Business Owner Agreement,” that is signed with the last four digits of your Social Security Number — without having provided your name.³ On the other hand, clicking the “Learn More” button leads you to a contact form with the caveat that “if you first heard about ACN from an Independent Business Owner, contact that person for more information.”⁴

Choosing to scroll down leads you to a segment that asks: “What if you got paid every time someone talked on the phone, watched television, sent text messages, surfed the internet, swiped a credit card, or used natural gas or electricity? ACN’s home-based business provides an opportunity to earn income on the services people are already using every day.”⁵

Finally, scrolling down further, you find a caption for a charity logo that states: “Every time someone becomes an ACN customer, a child gets fed”⁶ and another quote from an ACN consultant: “I try never to think of what I will do next week or next month, but always today. That has always helped me get closer to my long-term goals.”⁷ Alongside these quotes are links to other parts of the website — but no search function to find other information about the company.⁸

It took approximately twenty minutes exploring the website for this author to find a list of the services ACN provides.⁹ These services include telecommunications, home security, and energy utilities — a fairly broad

1. ACN, <http://www.acninc.com> [<https://perma.cc/W4BQ-EDEY>].

2. ACN, *supra* note 1.

3. ACN *Independent Business Owner Agreement*, ACN, <https://myacn2.acninc.com/OnlineRepAgreement/RepAgreementStart.do?init=false> [<https://perma.cc/73H3-YHU9>].

4. ACN *Contact Form*, ACN, http://acnreview.com/leads/?CO_LA=US_EN [<https://perma.cc/VUC9-FNMJ>].

5. ACN, *supra* note 1.

6. *Id.*

7. *Id.*

8. *See id.*

9. *See* ACN, <https://www.myacn.com/> [<https://perma.cc/4GEJ-JL2S>].

portfolio.¹⁰ It took another few minutes to find how Independent Business Owners earn money, as the Compensation Plan is only accessible within the Agreements. As an ACN Independent Business Owner — not a salesperson — you receive a portion of sales from customers. If an Owner recruits others to become Owners, he receives a portion of their sales from customers. The more customers Owners and their recruits have, the higher percentage of commissions you earn.¹¹

ACN, with revenues of \$800 million in 2016,¹² is just one example of a multilevel marketing company (called a “MLM”): A company that not only markets goods and services through direct sales, but also incentivizes its consultants to recruit other potential consultants.¹³ In a MLM, consultants are considered non-employees of the company,¹⁴ and the incentives may be aligned in such a way that it may be more profitable for consultants to recruit others than to sell products.¹⁵ In contrast, traditional salespeople are employed by companies and are paid a combination of a base salary and bonuses, based on how much inventory they or their team are able to sell.¹⁶ Perhaps it is for this reason that the websites of ACN and other prominent MLMs¹⁷ provide a similar emphasis on the opportunity to become a consultant rather than the products themselves.¹⁸

10. *See id.*

11. *North American Compensation Plan Overview*, ACN, <http://www2.acninc.com/join/301.pdf> [<https://perma.cc/FQB7-N2UT>].

12. *ACN, Inc. Ranked Among the Largest Direct Selling Companies in the World for 8th Straight Consecutive Year*, ACN, <http://acninc.com/news/press-releases/2016/04/28/acn-ranked-among-largest-direct-sellers> [<https://perma.cc/X6ES-NCJU>].

13. Participants involved with MLM companies may go by a variety of names — consultants, distributors, owners, or contractors. In this paper, I use the term consultants to refer to any participant. *See* Wesley K. Dagestad, Note, *Day's Pyramid Ignores Sturdy Severability Foundation, Builds off Granite Rock*, 2014 J. DISP. RESOL. 349, 349 n.2 (2014).

14. *See* Joel Busher, Sophie Bremner, and Paramita Muljono, *Freedom, Family, Hope and Rewards? Points of Departure for Development Studies Research on Direct Selling* (U. Anglia Sch. Int'l Dev., Working Paper No. 16, 2009).

15. *See* ACN, *supra* note 11. Consultants are paid a higher percentage of sales the more customer points they have. Customer points are based on the number of customers and recruits a consultant has. If you assume that a recruit has at least one customer, then it is in the consultant's interest to recruit rather than to sell to a customer.

16. *See, e.g.*, Thomas Steenburgh and Michael Ahearne, *Motivating Sales People: What Really Works*, HARV. BUS. REV., July-Aug. 2012, <https://hbr.org/2012/07/motivating-salespeople-what-really-works> [<https://perma.cc/R2CU-7N2L>].

17. *Compare* ACN, *supra* note 1, *with, e.g.*, AMWAY, <http://www.amway.com/> [<https://perma.cc/APH5-5ZLN>], *and* LULAROE, <http://www.lularoe.com/> [<https://perma.cc/YV6G-X755>].

18. *See, e.g.*, AMWAY, *supra* note 17 (where the first front page states “Build your knowledge, build your business”), SCENTSY, <http://www.scentsy.com> [<https://perma.cc/PP7R-46SZ>] (where a prominent arrow points to a consultant application).

As much as MLMs sell items (or people), they are also selling a distant opportunity. The majority of MLM consultants are likely to lose money from their participation. There is little public data regarding the MLM industry¹⁹ — much less MLM's per capita revenues — aside from what is disclosed in litigation.²⁰ However, 87.5% of Herbalife consultants earned a median annual income of \$637,²¹ and of all sellers that made *any* profit, median earnings in addition to retail profits, if any, were \$245 for the year.²² There appears to be no data regarding the share of income from recruitment (directly or indirectly), compared to sales;²³ however, in a 2013 appeal, the FTC argued that an emphasis on recruitment led to a net loss for 94% of consultants in one company.²⁴ Consultants' earnings are garnished by various expenses, further depreciating their income. In addition to pursuing prospective consultants, consultants often must purchase a training kit (which, in some cases, could run up to \$500²⁵). After training, they are expected to purchase ongoing promotional items (e.g., catalogs and display kits) or pay a subscription fee for their participation.²⁶ A back-of-the-envelope subtraction of these costs from the little revenue data we have suggests that a substantial number of consultants have a net loss.

19. See William W. Keep and Peter J. Vander Nat, *Multilevel Marketing and Pyramid Schemes in the U.S.: An Historical Analysis*, 6 J. HIST. RES. IN MARKETING 188, 203 (2014); Sergio Pareja, *Sales Gone Wild: Will the FTC's Business Opportunity Rule Put an End to Pyramid Marketing Schemes?*, 39 MCGEORGE L.REV. 85, 96 (2008).

20. See Keep, *supra* note 19, at 2034–55.

21. Melanie Hicken, *The Money Behind Herbalife, Mary Kay, and Others*, CNN (Jan. 10, 2013, 1:58 PM), <http://money.cnn.com/2013/01/09/pf/multilevel-marketing-industry/> [<https://perma.cc/6RZJ-QF2W>].

22. *What Should I Know About Herbalife Membership?*, HERBALIFE, <http://www.herbalife.com/Content/en-US/pdf/business-opportunity/statement-of-average-gross-compensation-usen.pdf> [<https://perma.cc/7FXR-4Y6D>].

23. Data comparing recruitment income to sales income would be useful information to have, as a large share of revenue from recruitment would help to distinguish MLMs from other sales opportunities.

24. Second Cross-Appeal and Answering Brief at 30–31, *FTC v. Burnlounge*, 753 F.3d 878 (9th Cir. 2013) (No. 12-55926, 12-56197, 12-56288 (consolidated)).

25. If the MLMs had a training kit over \$500, it would need to comply with the FTC's Franchise Rule. See Pareja, *supra* note 19, at 92. In my research, all kits were below \$500. Herbalife's kit was \$59.99.

26. See also Jayne O'Donnell, *Multilevel Marketing or 'Pyramid'? Sales People Find it Hard to Earn Much*, USA TODAY (Feb. 10, 2011, 8:48 PM), https://usatoday30.usatoday.com/money/industries/reta-il/2011-02-07-multilevelmarketing03_CV_N.htm/ [<https://perma.cc/SP7X-LYNY>]. I was unable to determine how much Herbalife promotional items would cost without signing up (it may vary across area). However, another MLM charges \$14.95 monthly for their subscription fee. See THIRTY-ONE GIFTS, <https://www.mythirtyone.com/info/join> [<https://perma.cc/NZ5P-YEL7>]. See part III *infra* for an extended discussion on this issue.

Indeed, accusations abound online that both prominent²⁷ and obscure²⁸ MLMs are scams;²⁹ both the FTC³⁰ and various states³¹ post collections of Frequently Asked Questions (FAQs) meant to help people discern if a MLM they are considering is worthwhile. Specifically, MLMs are compared to pyramid schemes given similarities in organizational structure (i.e., the incentive to recruit new people means that only a few people will make large profits). While not all MLM schemes are illegal pyramid schemes and vice versa, both MLMs and pyramid schemes may draw from the literature on influence in recruiting consultants that may override a rational actor's decision to participate.

Behavioral economics presents a potential explanation for why people might choose to enter a MLM despite the lack of information from both the industry and individual companies. This interdisciplinary approach drawing from law, psychology, and economics has been applied to a variety of domains³² and has a close relationship with advertising itself — as both of these fields draw inspiration from one another.³³ This paper seeks to examine the behavioral economics of multilevel marketing companies (“MLMs”). Part I serves as a brief overview of the structure and potential enforcement of these companies. Part II considers under what conditions a rational consumer might choose to participate in a MLM. Part III delineates how behavioral biases might cause someone to participate in a MLM in the face of incomplete information, drawing from examples from ACN, one of the largest MLMs by revenue,³⁴ as well as others. In particular, I suggest

27. See Roger Parloff, *Herbalife Deal Poses Challenges For the Industry*, FORTUNE MAG. (July 19, 2016), <http://fortune.com/2016/07/19/herbalife-deal-challenges-industry/> [<https://perma.cc/H7L5-TQYX>].

28. See *Reddit: MLM Scams*, REDDIT, <https://www.reddit.com/r/mlmscams/> [<https://perma.cc/EE7M-BC2K>].

29. See *infra*, Part III.

30. See FTC, *Multilevel Marketing* (July 2016), <https://www.ftc.gov/tips-advice/business-center/guidance/multilevel-marketing> [<https://perma.cc/Z3PW-BQJ7>].

31. See, e.g., Bill Schuette, Attorney General, *Consumer Alert: Multi-Level Marketing or Illegal Pyramid Scheme?*, STATE OF MICHIGAN, http://www.michigan.gov/ag/0,4534,7-164-17337_20942-208400--,00.html [<https://perma.cc/PS5W-G9ZA>].

32. See, e.g., RICHARD THALER AND CASS SUNSTEIN, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH AND HAPPINESS* (Yale Univ. Press 2008); OREN BAR-GILL, *SEDUCTION BY CONTRACT: LAW, ECONOMICS, AND PSYCHOLOGY IN CONSUMER MARKETS* (Oxford Univ. Press 2012). While NUDGE covers over ten different fields (including, e.g., health, environment, and financial markets), the ideas expressed in the book catalyzed innovation all over.

33. See, e.g., Matt Carmichael, *Making the Most of Our Irrationality*, ADVERTISING AGE (Sept. 21, 2010), <http://adage.com/article/adagestat/advertising-dan-ariely-behavioral-economics-marketing/146001/> [<https://perma.cc/5JGJ-KMV9>].

34. 2016 *DSN North America 50 List*, DIRECT SELLING NEWS (June 1, 2016), http://directsellingnews.c-om/index.php/view/2016_dsn_north_america_50_list1 [<https://perma.cc/9KT3-4C6H>].

that MLMs engage in both incomplete disclosure about expected economic benefits, while simultaneously deemphasizing the importance of economic benefits relative to a set of values that they believe consultants should develop. Both of these techniques rely on and exacerbate consultants' behavioral biases. Finally, Part IV concludes by considering existing regulatory policies and further areas of study.

I. BACKGROUND

A. DEFINING MLMs

Multilevel marketing companies ("MLMs") are defined as a subset of direct-sales companies.³⁵ The multilevel reference in the acronym comes from the fact that consultants proceed up levels associated with increased commissions as they acquire more customers and recruit more consultants.³⁶ MLMs sell a variety of goods and services, from health and beauty products,³⁷ to clothing,³⁸ and financial³⁹ services, with "an estimated \$34.47 billion in retail sales, and . . . 18.2 million direct selling distributors, in the U.S. in 2014."⁴⁰ The vast majority of distributors appear to be part-time⁴¹ and female.⁴²

35. Direct-sell companies are companies that directly sell products and services to the end-user without a retailer. See Peter J. Vander Nat and William W. Keep, *Marketing Fraud: An Approach for Differentiating Multilevel Marketing from Pyramid Schemes*, 21 J. PUB POL'Y & MARKETING 139, 140 (2002).

36. See *ibid.*

37. See, e.g., AMWAY, *supra* note 17; HERBALIFE, <http://www.herbalife.com/> [<https://perma.cc/M2TH-LLEC>], RODAN + FIELDS, <http://www.rodanandfields.com> [<https://perma.cc/YG5R-RTW8>].

38. See, e.g., LULAROE, *supra* note 17; CABI, <http://www.cabiclothing.com> [<https://perma.cc/9H7X-V3R4>].

39. See, e.g., PRIMERICA, <http://www.primerica.com> [<https://perma.cc/N5KA-UMCL>].

40. Anne T. Coughlan, *Multi-Level Marketing Business Opportunities: Analyzing Net Economic Return and Avoidable Economic Loss to Distributors*, 1 (July 15, 2016) (citing statistics from the Direct Sales Association's defunct link), <https://ssrn.com/abstract=2822402> [<https://perma.cc/UK69-LSSS>].

41. *Id.* at 2.

42. "Some 75% of U.S. MLM distributors in 2014 were women, and almost 90 percent worked only part-time on their businesses." *Id.* at 1. Indeed, the MLM industry appears consistently three-quarters feminine, based on earlier statistics. See John Bone, "The Longest Day": "Flexible" Contracts, *Performance-related Pay and Risk Shifting in the UK Direct Selling Sector*, 20 WORK, EMPLOYMENT AND SOCIETY 109, 111 (2006) (citing Nicole Woolsey Biggart, *CHARISMATIC CAPITALISM* (1989)).

B. COMPARISON TO PYRAMID SCHEMES

MLMs and pyramid schemes partially overlap: Some MLM companies are pyramid schemes and some pyramid schemes consist of MLM companies. The resemblance between the two is made salient by the organizational structure: Pyramid schemes ask those individuals at the base of the pyramid to contribute to the higher levels, with the promise of a reward provided entirely from those levels below the individual. Similarly, MLMs offer the promise of profits to its consultants, but those profits stem from two streams: Commissions from direct sales and commissions from recruiting new clients. Indeed, one early article attempting to distinguish pyramid schemes from MLM models pointed out that “the investor’s pecuniary benefit [of a pyramid scheme] derives primarily from his success in inducing additional persons to participate in the plan.”⁴³

C. ENFORCEMENT ACTIONS AND MLMS.

Enforcement against MLMs with problematic business tactics is primarily triggered through allegations that the MLMs employ pyramid sales schemes. Prosecution methods crosscut agencies (e.g., Department of Justice, Securities and Exchange Commission, Federal Trade Commission) and approaches. Overlaid on this framework are potential state law liabilities under each state’s lottery and consumer fraud acts.⁴⁴ The following is a general overview of three prosecution approaches categorized as (1) the lottery approach, pursued by the DOJ, (2) the securities approach, pursued by the SEC and state enforcement bodies, and (3) an assortment of consumer-directed approaches pursued by the FTC.

First, under the lottery approach, spearheaded by the DOJ, the investigation centers on three elements: Consideration, prize, and chance — that is, whether the victim has given funds to the company, how much the company benefits, and how much the victim may benefit from his or her consideration.⁴⁵ Historically, chance has been the most difficult element to

43. Donald Daniels, Note, *Toward a Uniform Approach to Multilevel Distributorships*, 8 U. MICH. J.L. REFORM 546, 547 (1975).

44. See *id.* at 559. As of 2010, more than half of states have enacted laws specifically targeting MLMs. See Adam Epstein, *Multi-Level Marketing and its Brethren: The Legal and Regulatory Environment in the Down Economy*, 12 ATLANTIC L.J. 91, 93 (2010). See also Keith Kanouse, *Business Opportunity Rule Means Less Disclosure, but by More Companies*, 26 FRANCHISE L.J. 125, 130 (2007).

45. See Daniels, *supra* note 43, at 552.

prove.⁴⁶ Another DOJ-driven approach includes prosecution under mail order fraud, although this strategy is less frequent.⁴⁷

Second, the securities approach utilizes federal and state securities laws that are violated when an MLM makes materially false or misleading statements in connection with a security — an infringing MLM is said to have sold a security in the form of an investment contract to its consultants. The Securities and Exchange Commission investigates MLMs by pursuing fraud claims under the Securities Act, Securities Exchange Act, and its associated regulations.⁴⁸ These claims depend on whether the scheme is construed to be a security (i.e., the customer “is not required to make significant efforts in the operation of the franchise in order to obtain the promised return.”⁴⁹) The four-prong test derived from *SEC v. W.J. Howey* delineates the Supreme Court’s definition of a security: When an individual “(1) invests his money (2) in a common enterprise and (3) is led to expect profits (4) solely from the efforts of a promoter or a third party.”⁵⁰ With regard to alleged pyramid schemes, the fourth prong is most relevant⁵¹ and, under *SEC v. Glenn W. Turner Enterprises*, the scheme’s profits must not substantially — rather than solely, as articulated in *Howey* — rely on recruitment.⁵²

Some states use a “risk capital test” to determine whether a MLM sells a security under state securities laws.⁵³ In such states, the four-prong test operates as follows:

- (1) An offeree furnishes initial value to an offeror, and (2) a portion of this initial value is subjected to the risks of the enterprise, and (3) the furnishing of the initial value is induced by the offeror’s promises or representations which give rise to a reasonable understanding that a valuable benefit of some kind, over and above the initial value, will accrue to the offeree as a result of the operation of the enterprise, and (4) the offeree does

46. See *ibid.* (citing generally *Zebelman v. United States*, 339 F.2d 484 (10th Cir. 1964)).

47. *Id.* at 553.

48. *Id.* at 554.

49. *Id.* (citing SEC, Securities Act Release No. 5211 (1971); SEC, Securities Exchange Act Release No. 9387 (1971)).

50. Douglas M. Fried, *General Partnership Interests as Securities Under the Federal Securities Laws: Substance Over Form*, 54 *FORDHAM L. REV.* 303, 309 (1985) (citing *SEC v. Howey*, 328 U.S. 293, 298–299 (1946)).

51. See Pareja, *supra* note 19 at 99.

52. *SEC v. Glenn W. Turner Enterprises*, 474 F.2d 476, 481–83 (9th Cir. 1973). See Daniels, *supra* note 43, at 555; Pareja, *supra* note 19, at 99–100.

53. Pareja, *supra* note 19, at 100.

not receive the right to exercise practical and actual control over the managerial decisions of the enterprise.⁵⁴

Ignoring both the *Howey* test and the “risk capital test,” the United States Court of Appeals for the Ninth Circuit has taken a third, more literal approach, holding that any pyramid structure should be construed as a security — this third test is known as a pyramid-scheme analysis, looking at whether the entity is or is not a pyramid scheme and thus a security.⁵⁵ Overall, despite the variations in the state and federal tests, whether something is a security is generally interpreted very broadly.⁵⁶

Third, the FTC has multiple pathways for enforcement against a MLM alleged to be a pyramid scheme. It may look to the Sherman Act in arguing that the distributor and the business essentially act as the same entity.⁵⁷ Alternatively, the FTC may challenge an alleged pyramid scheme under Section 5 of the FTC Act, which prohibits deceptive acts in commerce.⁵⁸ In the well-known case regarding MLM companies, *In re Amway Corp., Inc., et al.*,⁵⁹ the FTC ruled that Amway had “avoided the abuses of pyramid schemes” by requiring that a consultant must sell 70% of her inventory to 10 different customers each month in order to receive a performance bonus, and providing an opportunity for consultants to sell back inventory to Amway.⁶⁰ This trifecta of rules, known as the Amway Safeguards,⁶¹ provided a test for courts determining whether a MLM company is functionally acting as a pyramid scheme.⁶² In general, it appears that courts are quite deferential to this standard.⁶³ More recent cases add two indicia to whether a MLM business may be operating a pyramid scheme: Whether it provides “lump-sum payments for each new recruit”⁶⁴ and whether it provides “rewards based on volume purchased by recruits,” as these are unrelated to product

54. *Ibid.* (citing *Hawaii v. Hawaii Mkt. Ctr., Inc.*, 485 P.2d 105, 109 (Haw. 1971)).

55. *See ibid.* (citing *Webster v. Omnitrition International, Inc.*, 79 F.3d 776, 781–82 (9th Cir. 1996)).

56. Epstein, *supra* note 44, at 117.

57. Daniels, *supra* note 43, at 556–557.

58. *See* 15 U.S.C. § 45(a)(1); Daniels, *supra* note 43, at 557.

59. *In re Amway Corp., Inc., et al.*, 93 F.T.C. 618 (1979).

60. *Id.* at 668.

61. Pareja, *supra* note 19 at 95.

62. *See, e.g.*, *Whole Living, Inc. v. Tolman*, 344 F. Supp. 2d 739, 745–746 (D. Utah Nov. 9, 2004) (Judge Ted Stewart).

63. Epstein, *supra* note 44, at 104.

64. Keep, *supra* note 19, at 198 (citing generally *FTC et al. v. Fortune Hi-Tech Marketing et al.*, Civil No. 13 CV 578 (N.D. Ill. 2013)).

sales,⁶⁵ such that a consultant's compensation is largely derived from new recruits.⁶⁶

Altogether, under Amway and related decisions, a court will balance the following factors to determine whether a MLM enterprise is an illegal pyramid scheme:

1. Products have "no real world marketplace" and 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;
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.⁶⁷

II. A (POTENTIALLY) RATIONAL EXPLANATION.

One novel aspect of MLM companies is that the consultant is himself a good because his existence is a source of revenue to other consultants, either directly, through a recruitment fee, or indirectly, through his sales. This may mean that the incentives for MLMs and higher-status consultants (i.e., those who could have recruited others in an unsaturated market) are largely misaligned with those of lower-status consultants. Specifically, the former category would receive revenue from the lower-status consultants' recruitment-fee generation as well as through their inventory purchases, and it may be possible that the revenue from recruitment fees exceeds customer

65. See *ibid.* (citing generally *FTC v. Equinox Int'l. Corp.*, 1999 WL 1425373 (D. Nev. 1999); *FTC v. Trek Alliance*, 81 Fed.Appx. 118 (9th Cir. 2003)).

66. See *id.* at 199.

67. Epstein, *supra* note 44, at 105–106 (summarizing Jeffrey A. Babener, *FTC v. Equinox — Déjà Vu*, (1999) <http://www.mlmllegal.com/equinox.html> [<https://perma.cc/5CQZ-N3CG>]).

purchases. As one scholar points out: “[F]or MLM companies, there is no cost and, in some cases, failure still generates a profit.”⁶⁸

Altogether, a rational actor, i.e., a *homo economius*,⁶⁹ that is considering the entry into a MLM market would want to engage in a cost-benefit analysis, comparing the costs of entry relative to the benefits. Of course, an individual’s utility function differs from those of another, so I examine two situations: (a) Where the prospective consultant is only considering economic costs and benefits and (b) where the prospect is also incorporating certain noneconomic considerations into her decision.

In the first situation, the prospective consultant would calculate the costs of the startup package (e.g., training and inventory) against the anticipated benefits of sales. If the expected sales were greater than the startup package, and the sales were greater than her outside option (e.g., salary at another job or the value she places on leisure time), then she would enter the MLM.⁷⁰ Indeed, if she believed that the training that the MLM offered was non-company specific industry capital, she might value the training more highly. Even if she did not have full information about the MLM, she would need information about the risk or uncertainty involved.

In the second situation, the prospective consultant might enter the MLM if she valued certain aspects of the job differently. For instance, a stay-at-home mom might welcome the opportunity to stay involved in traditional market labor. In both of these situations, it would be economically rational for an individual to decide to enter the MLM.

As a potential *homo-economius* consultant weighs her options, she would probably value information about the average profits per consultant and the trajectory over time. As one economic model notes, even if a consultant is uninformed about how productive she will be (e.g., low vs. high productivity), knowing the average performance of a consultant can help her to make a calculated risk.⁷¹

68. Brian Bloch, *Multilevel Marketing: What’s the Catch?*, 13 J. CONSUMER MARKETING 18, 25 (1996).

69. See generally, Richard Thaler, *From Homo Economius to Homo Sapiens*, 14 J. ECON. PERSP. 133–141 (2000), for an example of this term in a behavioral economics context.

70. See Coughlan, *supra* note 40, at 12. It might also be possible that a distributor derives utility from consuming her own products, *see id.* at 2. For example, several consultants I know personally indicated that they became consultants because they wanted a discount on certain beauty products and clothing. However, if this were the case for all — or the majority of — consultants, then MLM companies would simply be termed “buyer’s clubs.” See Keep, *supra* note 19, at 204.

71. See Coughlan, *supra* note 40, at 13. The author notes that MLM companies could have low startup costs in order for potential consultants to try out the program and figure out whether they are low- or high-productivity type, *id.*

In addition, the prospective consultant might want to know how many consultants are in her networks. For instance, if everyone in her community was already a consultant, then her expected profits might be lower as there are fewer available people to recruit. She may also have prior beliefs about other consultants' rationality, either viewing the other surrounding consultants as largely rational or largely irrational (i.e., overly optimistic about earning a profit). If she believes the latter, then it seems possible that she plans to "ride a bubble" — making a profit from consultants she expects will fail.⁷² This plan, however, would likely constitute fraud and thus require the significant assumption that she is willing to defraud her targeted consultants.

That said, these beliefs may differ throughout the levels of a MLM. In particular, recruits that have recently joined may believe that other consultants are largely rational. After all, longtime consultants appear to be making money, they themselves are likely to believe that their own decision to join was rational,⁷³ and they must have some belief in the success of the consultants they recruit. (In legal MLMs, the portion of commissions and bonuses increase based on the number of individuals you recruit, but, the MLM cannot directly pay a consultant for recruiting new individuals.)⁷⁴ The MLM's marketing reinforces these beliefs.⁷⁵ At higher levels of a MLM, consultants may be more likely to believe that others are irrational, as they may have witnessed greater amounts of turnover or are more likely to recognize that at least some of their consultants will fail.

Compounding confusion, MLM companies appear resistant to providing additional information to customers or regulators about the industry. In 2006, the FTC attempted to establish the business opportunity rule, which appeared to be a response to pyramid schemes' exception from enforcement under the franchise rule.⁷⁶ For a company that solicited potential consultants,

72. See BAR-GILL, *supra* note 32, at 153 n. 84; Dilip Abreu & Markus K. Brunnermeier, *Bubbles and Crashes*, 71 *ECONOMETRICA* 173, 174–175 (2003).

73. *I.e.*, a post-hoc justification.

74. See FEDERAL TRADE COMMISSION, *Pyramid Schemes: International Monetary Funds Seminar on Current Legal Issues Affecting Central Banks* (May 13, 1998), <https://www.ftc.gov/public-statements/1998/05/pyramid-schemes> [<https://perma.cc/W9E5-GL9J>].

75. In Part III, I discuss how the idea of grit might double-down on consultants' beliefs on others' rationality — examples of failure are seen as lack of work ethic, not as bounded rationality revealed.

76. Business Opportunity Rule, 71 Fed. Reg. 19054 (proposed Apr. 12, 2006) (to be codified 16 C.F.R. pt. 437). Until the business opportunity rule was later implemented in 2012, MLMs could, in theory, have been forced to comply with the franchise rule, which states that businesses must provide material information to potential purchases (here, consultants) to provide them with an informed decision; this information includes "a statistical analysis of existing outlets of the business; whether company-owned or franchised." Pareja, *supra* note 19 at 92. However, MLM models often fell within the exceptions to the franchise rule, as the franchise rule has exceptions for business opportunities that do

required some form of consideration, and offered to “buy back ... any or all of the goods or services[,]”⁷⁷ the rule would have required the provision of a disclosure document to the prospective consultant.⁷⁸ That disclosure would include “information about the seller; the business background of the seller’s principals and their litigation and bankruptcy histories; [and] the terms and conditions of the offer.”⁷⁹ It would also require “statistical analyses of existing franchised and company-owned outlets.”⁸⁰

To simplify the process, the disclosure was to be limited to one page.⁸¹ Moreover, the company would be asked to simply check “yes” or “no” to whether it had made an earnings claim,⁸² “been the subject of any civil or criminal action for misrepresentation,”⁸³ or offered a cancellation policy.⁸⁴ If a company checked yes to any of these questions, it would have to attach additional information about the claims, legal actions, or cancellation policy.⁸⁵ These requirements and the design of the form itself could be interpreted as incorporating aspects of behavioral economics, with an eye towards how individuals might interpret large amounts of complex information.⁸⁶

During the notice and comment period, however, the FTC received thousands of form letters from MLM consultants.⁸⁷ Given the Amway Safeguards’ implication that legal MLMs should buy back their consultants’ unsold inventory,⁸⁸ the Business Opportunity Rule’s inclusion of companies that “buy back goods or services” appeared to bring all MLM companies under the umbrella of the Rule.⁸⁹ In 2008, the FTC chose to exclude MLMs from regulation by the Rule and to eliminate questions regarding legal actions against a company’s employees.⁹⁰

not, require immediate upfront costs of more than \$500, or if the costs relate to wholesale selling, training or returnable invento, *see ibid.* For instance, if registration fees were set at \$499, the franchise rule would not apply.

77. FTC Business Opportunity Rule, 71 Fed. Reg. at 19062.

78. Pareja, *supra* note 19, at 108–09.

79. FTC Business Opportunity Rule, 71 Fed. Reg. at 19055.

80. *Ibid.*

81. *Id.* at 19091.

82. *Id.* at 19058.

83. Or whether its affiliates had been the subject of legal action. *Id.* at 19088.

84. *Id.*

85. *Id.*

86. However, the disclosures could be written in a way to be confusing. Part IV briefly discusses the shortcomings of this approach.

87. FTC Business Opportunity Rule, Final Rule, 76 Fed. Reg. 76816, 76818 n.21 (Dec. 8, 2011) (to be codified at 16 C.F.R. pt. 437).

88. *See In re Amway Corp., Inc., et al.*, 93 F.T.C. 618, 669 (1979).

89. FTC Business Opportunity Rule, Final Rule, 76 Fed. Reg. at 76831.

90. *See id.* at 76819.

As scholars anticipated,⁹¹ it appears that industry lobbyists were part of this successful protest against extending enforcement under the Rule to MLMs.⁹² But the fact that short sellers in 2006 were prepared to sell stock from publicly held MLMs⁹³ suggests that experts might believe that disclosure of further information would hurt revenue, and in turn, consultant entry into the market, as well as earnings per consultant (given that product sales depend wholly on consultants). To better understand such beliefs and how disclosure policies like the proposed FTC rule would affect MLMs, a behavioral economics perspective provides a fruitful lens. Even if MLMs provided further information to prospective consultants, they are likely to do so in a way that shapes the preferences of the prospective consultant, especially with regard to how the prospect perceives the information (what I term imperfect disclosure). Additionally, the MLMs may exploit similar biases through a potential consultant's desire to conform to a particular religious or gender identity.

III. A BEHAVIORAL MODEL

In the following two sections, I look at how MLM disclosures to consultants exploit the consultants' underlying behavioral biases, as well as how MLMs target consultants' identities to exploit those same biases.

A. IMPERFECT DISCLOSURE

In this section, I define "imperfect disclosure" as the combination of (1) design choices by a MLM to influence prospective consultants into joining and (2) the cognitive biases that consumers might demonstrate in the process. Specifically, I suggest that at recruitment, MLMs strategically deploy design choices that appeal to emotion and engage in base-rate neglect (i.e., overreliance on successful but unlikely examples),⁹⁴ altogether appealing to "present bias," i.e., the behavioral economics concept that individuals strongly prefer rewards in the present.⁹⁵ Recall again the prominently displayed quote from an ACN consultant: "I try never to think of what I will

91. See Pareja, *supra* note 19, at 107.

92. See Herb Greenberg, *How Multi-Level Marketers Dodged a Bullet*, CNBC (Jan. 9, 2013, 4:25 PM), <http://www.cnbc.com/id/100360456> [<https://perma.cc/WP8K-WWMG>].

93. See Charles Duhigg, *Why Short Sellers Want to Crash the Tupperware Party*, N.Y. TIMES, Nov. 13, 2006, at C1.

94. See generally Amos Tversky and Daniel Kahneman, *Judgment under Uncertainty: Heuristics and Biases*, 185 SCIENCE 1124, 1124–1125 (1974).

95. See generally, e.g., David Laibson, *Golden Eggs and Hyperbolic Discounting*, 112 Q. J. ECON. 443–477 (1997).

do next week or next month, but always today. That has always helped me get closer to my long-term goals.”⁹⁶ After a prospective consultant signs a contract with the MLM company, the inertia bias and projected bias ensure her continued participation.

1. *During Recruitment*

A potential consultant may be recruited in multiple ways, including either through a friend who seeks to offer a new opportunity or through cold-call advertising.⁹⁷ It appears — likely due to the in-person nature of MLM — that generally, printed information is vaguely written on MLM websites.⁹⁸ For instance, on the ACN website, if you do not wish to sign the New Business Owner Agreement immediately, you are asked for your email and phone contact information so that a consultant may contact you.⁹⁹

MLM company events, with an ambiance similar to religious revivals, are a large part of recruiting.¹⁰⁰ These events play on the likelihood that people are often more present biased in highly charged situations¹⁰¹ due to cognitive overload.¹⁰² In particular, the emotional intensity of the event may heighten prospective consultants’ propensity to invest in a MLM.

At these company events, extremely successful consultants are brought on stage to discuss their experience with the company as a real-life parallel to testimonials found online. The focus on in-person testimonials of this sort is an example of base-rate neglect — when individuals focus on specific incidents rather than average, baseline data¹⁰³ — as enabled by the company. That is, only the most successful outcomes are shown and almost no information is distributed regarding the average or distribution of salaries.

Large samples of data seem to be specifically, not randomly, selected: During litigation, Herbalife reported gross earnings from a subset of “eligible” distributors, but did not disclose the eligibility requirements.¹⁰⁴ A full distribution of salary data, of course, would provide more valuable (and possibly different) information: One empirical study finds that “the bottom

96. ACN, *supra* note 7.

97. See Daniels, *supra* note 43, at 550.

98. See, e.g., LULAROE, *supra* note 17; CABI, *supra* note 38.

99. ACN, *supra* note 3.

100. *I.e.*, music, professional lighting and motivational speakers. See, e.g., ACN, *supra* note 1.

101. See generally David DeSteno et al., *Discrete Emotions and Persuasion: The Role of Emotion-Induced Expectancies*, 86 J. PERSONALITY & SOC. PSYCHOL. 43–56 (2004).

102. See generally ELDAR SHAFIR AND SENDHIL MULLAINATHAN, SCARCITY: WHY HAVING TOO LITTLE MEANS SO MUCH (Times Books 2013).

103. See generally Tversky, *supra* note 94.

104. See Keep, *supra* note 19, at 204.

99% of all Arbonne distributors earned an average income of \$87.36 annually whereas the top .04% earned an average income of \$330,516.”¹⁰⁵ Moreover, “99% of all sales representatives in [a sample of ten MLMs] . . . earned *less* than \$14 a week (on average) in commissions (from downline) while also earning less than ten dollars a week from their own sales.”¹⁰⁶ As one scholar notes:

[E]ven in the worst of the chain selling schemes . . . one can find participants who are making a lot of money at or near the top of their respective pyramids. The problem is not that the company misstates such a person's income. The problem is the company's intentional omissions and implications suggest that such an income is typical and attainable.¹⁰⁷

When the true distribution of statistics is referenced, representatives from a MLM may note that “[a]ny industry offering such substantial rewards and carrying with it such a low dollar cost of entry will obviously tend to attract some of the best and some of the worst entrepreneurs.”¹⁰⁸ Despite the sunny representations MLMs make to prospective clients, such push-back incidentally suggests that the true distribution suffers from selection bias or, alternatively, those consultants with lower incomes are working part time or not hard enough.¹⁰⁹

When numbers are cited by MLMs in their promotional materials, they relate to sales, not the probability of those sales or per capita sales. For example, one MLM informed its prospective consultants that “if they

105. Tiffany Lamoreaux, *Home is where the Work is: Women, Direct Sales, and Technologies of Gender* (Apr. 2013) (unpublished Ph.D. dissertation, Arizona State University) (on file with the Arizona State University Digital Repository)

106. *Id.* at 190.

107. Pareja, *supra* note 19, at 96.

108. Jeffrey A. Babener, *Network Marketing and the Law*, 24 VA. B. A. NEWS J. 12, 12 (1998).

109. Lamoreaux, *supra* note 105, at 198. *See, e.g.*, WILBUR CROSS, *AMWAY: THE TRUE STORY OF THE COMPANY THAT TRANSFORMED THE LIVES OF MILLIONS* xv (Berkeley Pub. Corp. 1999), provides a history of the company: “[I]t was clearly recorded, in surveys of the demographics of salespersons, that 99.9 percent were independent contractors rather than employees.” One apt analogy to the MLM industry might be fantasy sports, where only a few participants win large payouts at the expense of the pool, even though the sites appear to market fantasy sports as games that do not necessarily require experience. *See* N. Cameron Leishman, *Daily Fantasy Sports as Game of Chance: Distinction Without a Meaningful Difference?*, 2016 B.Y.U. L. REV. 1043, 1055 (2016); N.Y. State Office of the Att’y Gen., *A.G. Schneiderman Announces \$12 Million Settlement With Draftkings And Fanduel* (Oct. 25, 2016), <https://ag.ny.gov/press-release/ag-schneiderman-announces-12-million-settlement-draftkings-and-fanduel> [http://perma.cc/2HVZ-ENVM].

‘market[ed] just five memberships per week, [they would] receive \$500 per week!’ [yet] very few representatives . . . consistently sold five memberships a week” at that particular MLM.¹¹⁰

Overall, the recruitment methods of MLM firms engender optimism, rationally so — the theoretical economic model mentioned in Part II suggests that a consultant will only bear a loss where she thinks she would be a high performer but is actually a low performer. By highlighting only extremely successful examples and emphasizing that consultant effort necessarily leads to success,¹¹¹ the MLM company perpetuates this optimism without providing any information that might help the consultant determine her future performance.

While it should be expected that a profit-maximizing MLM would desire to highlight only success stories, in addition to highlighting benefits, at least some MLM companies ignore mentioning costs.¹¹² The omission of costs furthers present bias and hampers the consumer’s ability to make a rational cost-benefit calculation.

Ignorance of costs takes several hidden forms. *First*, it may mean not mentioning costs in the distribution of salaries. In Herbalife’s disclosure of consumer earnings, no consultant costs appear to have been mentioned — just gross revenue.¹¹³

Second, “from signing up to remaining active, direct selling may come with more costs than consultants realize.”¹¹⁴ MLM companies often stress that “direct selling requires no special training or skill, [with] ‘low’ start-up costs,”¹¹⁵ appealing to lower-income or otherwise frugal prospects. However, even if a company does not require inventory to be purchased, they may stress the purchase of “demonstration kits” (e.g., catalogs, sample products) to enhance one’s selling business.¹¹⁶ Frequently-updated demonstration kits obscure later-occurring costs,¹¹⁷ potentially holding less saliency to prospective consultants.¹¹⁸ Other fees may be mandatory but only noted in the boilerplate: At ACN, if a consultant does not request quickly enough that her sales revenue be sent to her, she may be charged an Account

110. Duhigg, *supra* note 93.

111. In the following Part, I argue that the MLM industry’s emphasis on grit makes it possible to assume high incomes are attainable.

112. See Vander Nat, *supra* note 35, at 141.

113. See Keep, *supra* note 19, at 204.

114. Lamoreaux, *supra* note 105, at 184.

115. *Id.* at 183.

116. The MLM may require you to sign a claim that demonstration kits are not required. See e.g., ACN, *supra* note 3.

117. Lamoreaux, *supra* note 105, at 183–184; see also O’Donnell, *supra* note 26.

118. See BAR-GILL, *supra* note 32, at 93.

Maintenance Fee to access where her revenue is stored.¹¹⁹ Legal disclaimers that indicate potential economic losses may also take the form of easily skimmed-over boilerplate language.¹²⁰ Even after the recruiting event, consultants are asked to “certify that no claims of guaranteed profits or representations of expected earnings that might result from [their] efforts as an IBO have been made by [the MLM] or [the] sponsor.”¹²¹

Finally, while the Amway Safeguards were meant to protect potential consultants, it may provide a sense of false security to a MLM’s business soundness. Recall that the *Amway* test suggests that a MLM company was not unlawful if it provides performance bonuses conditional on a certain amount of sales to a certain number of customers,¹²² and provides an opportunity for consultants to sell back inventory with a penalty.¹²³ However, corporations are allowed to buy back their inventory *at a discount* — a penalty or cost that is not highlighted in the recruitment materials.¹²⁴ Additionally, it is unclear who enforces the underlying conditions for bonuses, such that consultants may occasionally purchase their own inventory to maintain their discount or bonus levels.¹²⁵ Note that even if the consultant feels like this is forward-thinking behavior (i.e., contrary to present bias), she is likely overoptimistic about her prospects.

2. *At Signing of the Agreement*

Even if the MLM provides relevant information, it will be difficult to find. This is especially amplified in the agreements signed between consultants and MLMs, where the design of the contract may cause confusion. For example, take ACN’s Independent Business Owner Agreement, which asks the user to affirm that she “ha[s] read and agreed to be bound by all of the Terms and Conditions” of several agreements.¹²⁶ The

119. See ACN, *supra* note 3.

120. See Pareja, *supra* note 19, at 96. See also Daniels, *supra* note 43, at 548: “[I]t is not the act of recruitment which makes pyramid schemes suspect but the method of recruiting through unrealistic promises and mandatory investment.”

121. ACN, *supra* note 3.

122. *I.e.*, by requiring that a consultant must sell 70% of her inventory to 10 different customers each month in order to receive a performance bonus. See *In re Amway Corp., Inc., et al.*, 93 F.T.C. 618, 668 (1979).

123. See *ibid.*

124. ACN, for instance, buys back unsold inventory at 90% of the cost to the consultant. ACN, *supra* note 3.

125. See Lamoreaux, *supra* note 105, at 184.

126. ACN, *supra* note 3.

referenced materials, however, appear to be only viewable after the potential consultant has signed the agreement online.¹²⁷

While the FTC's Business Opportunity Rule now requires a cooling-off period — the opportunity to have seven business days to renege on a signed consultant contract¹²⁸ — for prospective consultants, recent research suggests that cooling-off periods may actually entrench consultants or other decision-makers in their decision.¹²⁹ For example, prospective consultants may fail to foresee how their lives may change with the time and money a MLM requires due to projection bias.¹³⁰ In some ways, people may have already thought ahead and envisioned their status as a successful consultant, such that revoking the contract may seem like a loss or a sunk cost of time.¹³¹

Finally, even if a consultant says that they plan to stay in the MLM industry for a certain amount of time or until they make a certain amount of revenue, their projection bias may not account for the fact that their attitudes towards the MLM industry may change, just as those attitudes may have already changed in the recruiting process.¹³² Coupled with the planning fallacy, in which people are prone to underestimate how much time their goals might take,¹³³ a consultant might spend longer in an MLM than they had originally planned.

B. PROMISES OF IDENTITY ENHANCEMENT.

Another practice of MLMs is to emphasize how the company may enhance a consultant's identity. For example, the official ACN website displays the following from a testimonial: "It's often said that ACN is a

127. *Id.*

128. FTC Business Opportunity Rule, Final Rule, 76 Fed. Reg. at 76859.

129. See Sven Hoeppe, *The Unintended Consequence of Doorstep Consumer Protection: Surprise, Reciprocation, and Consistency*, 38 EUR. J.L. & ECON. 247, 255 (2014) (citing George Loewenstein, Ted O'Donoghue & Matthew Rabin, *Projection Bias in Predicting Future Utility*, 118 Q. J. ECON. 1209, 1209–1248 (2003)).

130. See generally, e.g., Meghan R. Busse et al., *The Psychological Effect of Weather on Car Purchases*, 130 Q. J. ECON. 371, 371–414 (where car purchases are highly sensitive to weather suggesting that people are not properly anticipating the future).

131. See Courtenay Atwell, *The Franchisee as a Consumer: Determining the Optimal Duration of Pre-Contractual Disclosure*, 38 J. CONSUMER POL'Y 457, 482 (2015).

132. See generally George Loewenstein, Ted O'Donoghue & Matthew Rabin, *Projection Bias in Predicting Future Utility*, 118 Q. J. ECON. 1209, 1209–1248 (2003); Busse et al., *supra* note 130.

133. See generally, e.g., Roger Buehler, Dale Griffin & Michael Ross, *Exploring the "Planning Fallacy": Why People Underestimate Their Task Completion Times*, 67 J. PERSONALITY & SOC. PSYCHOL. 366, 366–81 (1994).

personal development program with a compensation plan attached[.]”¹³⁴ In doing so, MLMs play up the relative salience and benefits of non-financial considerations.¹³⁵

In particular, MLMs offer a narrative linked to American civil religion — the sociological proposition that nonsectarian religious symbols are often connected to American-exceptionalism values,¹³⁶ including “boundless faith in the [potential] of economic growth and prosperity.”¹³⁷ In MLM recruiting materials, both subtle and overt religious tones are often used, e.g., the word “blessing” is used frequently with regard to profits.¹³⁸ In an example of these overtones, the history of Amway starts with the following: “In this book you will find the same insights . . . that have served as a guiding light and a resource for millions of people around the earth to create a more rewarding life.”¹³⁹ Indeed, recruitment methods for at least some MLMs have often been compared to recruitment into religious organizations.¹⁴⁰

Altogether, the belief linked to American civil religion that “[b]oth God and the market should be left free . . . to reward correct behavior and punish the evil or lazy”¹⁴¹ plays into the mythology of the self-made man¹⁴² and can be translated into two mythical values removed from actual religious belief but tied to identity: (1) Grit (the idea that outcome is perfectly correlated with effort) and (2) independence. The first value sustains MLM consultants’ optimism in the face of potential losses, while the second value reduces the focus on economic losses altogether.

134. Danny Volonino, <http://acninc.com/news/company/2011/11/07/acn-and-personal-development-danny-volonino-svp> (last visited Mar. 21, 2018) (Note that I also saw this on the ACN website’s header with the same attribution; however, the website rotates through a series of quotes.); ACN, *supra* note 1.

135. See Keep, *supra* note 19, at 202.

136. See Robert N. Bellah, *Civil Religion in America*, 134 DAEDALUS 40, 42 (2005); see generally KATE BOWLER, *BLESSED: A HISTORY OF THE AMERICAN PROSPERITY GOSPEL* (2013).

137. Dick Anthony & Thomas Robbins, *Spiritual Innovation and the Crisis of American Civil Religion*, 111 DAEDALUS 215, 216 (1982).

138. See Epstein, *supra* note 44, at 98 (citing Pareja, *supra* note 19, at 119–20).

139. CROSS, *supra* note 109, at ix.

140. See generally Patralekha Bhattacharya & Krishna Kumar Mehta, *Socialization in Network Marketing Organizations: Is it Cult Behavior?*, 29 J. SOCIO-ECON. 361, 361–74 (2000).

141. Simon M. Coleman, *America Loves Sweden, Prosperity Theology and the Globalization of Civil Religion*, in RELIGION AND THE TRANSFORMATIONS OF CAPITALISM: COMPARATIVE APPROACHES (Richard H. Roberts ed., 1995).

142. Also known as the rags-to-riches tale; see generally Seymour Martin Lipset, *American Exceptionalism Reaffirmed*, 2 INT’L REV. SOC. 256 (1988).

In the social psychological literature, situations that emphasize particular identities (i.e., priming) may cause behavior changes among individuals.¹⁴³ As such, one could imagine a situation in which situations that stress particularly religious or gendered themes alongside MLM opportunities may cause potential consultants to engage further with MLMs. These contexts would serve as a social norm or reference point for what the consultant “should” do.

In turn, these norms might lead to a consultant staying on with her MLM even when she is losing money for three reasons. *First*, consultants who leave MLMs may not necessarily have plans for the next steps — MLM is a default path, and the people they work with have clear instructions for how to sell products. The logistical difficulty of starting something new creates inertia that ultimately keeps the consultant from exiting the MLM. *Second*, given that the majority of individuals are loss-averse, the consultant may want to continue working until she breaks even. The consultant may exhibit the sunk-cost fallacy here — if she believes that she has already put too much time in this endeavor to fail. *Third*, there is evidence that violating prescribed stereotypes about, for example, being American or female may result in social sanctions by others.¹⁴⁴ The consultant may not only view her work as a failure, but also herself.¹⁴⁵ MLMs’ emphasis on grit and independence may compound all of these beliefs.

1. *Grit*

Consider Amway, which one author described as “the most thoroughly American business in America . . . [i]n conception, in design, in basic economic philosophy, even in its very name itself.”¹⁴⁶ That same author describes one of Amway’s values as follows: “If people are to be held accountable, then it is necessary that their performances be evaluated and

143. See generally Daniel Benjamin, James Choi & Joshua Strickland, *Social Identity and Preferences*, 100 AM. ECON. REV. 1913, 1913–1928 (2010); Carol Dweck & Ellen Leggett, *A Social-Cognitive Approach to Motivation and Personality*, 95 PSYCHOL. REV. 256, 256–73 (1988).

144. See generally, e.g., Alice Eagly & Steven Karau, *Role Congruity Theory of Prejudice Toward Female Leaders*, 109 PSYCHOL. REV. 573, 573–598 (2002); Alice Eagly & Mary Kite, *Are Stereotypes of Nationalities Applied to Both Women and Men?*, 53 J. PERSONALITY & SOC. PSYCHOL. 451, 451–62 (1987).

145. See generally Paul Davies, Steven Spencer & Claude Steele, *Clearing the Air: Identity Safety Moderates the Effects of Stereotype Threat on Women’s Leadership Aspirations*, 88 J. PERSONALITY & SOC. PSYCHOL. 276, 276–87 (2005) (showing that an individual’s confidence in her identity reduces the psychological effect of stereotype threat, i.e., behaving more consistently with a particular stereotype).

146. See CHARLES PAUL CONN, *THE POSSIBLE DREAM: A CANDID LOOK AT AMWAY* 103 (Fleming H. Revell Co. 1977).

susceptible to judgment and the resulting rewards or penalties. People reap what they sow, and they must be taught in school, at home, on the job, and in all walks of life.”¹⁴⁷ Amway appears to use Biblical imagery¹⁴⁸ in this value to reinforce the belief that grit leads to success.

This belief appears consistently across MLM companies, where “success is considered to be a consequence of skill and attitude.”¹⁴⁹ Thus, consultants who are not currently experiencing success must have a positive attitude to obtain further success.¹⁵⁰ In contrast, “self-doubt is a sign of weakness and failure.”¹⁵¹ Failed consultants are considered the unmotivated majority: “Many simply do not have the stick-to-it attitude that characterizes the successful Amway distributor.”¹⁵² Yet, in one survey study of MLM consultants, job satisfaction was positively correlated with organizational commitment¹⁵³ but negatively correlated with job performance,¹⁵⁴ perhaps suggesting that optimism not only masks economic losses but may also prevent consultants from taking corrective steps earlier. Even the disclaimer ACN uses regarding potential economic loss emphasizes effort: “Success as an ACN Representative is not guaranteed, but rather influenced by an individual’s specific efforts. Not all ACN Independent Representatives make a profit and no one can be guaranteed success as an ACN Independent Representative.”¹⁵⁵

Recruiters often stress that “in contrast to traditional corporate employment, direct selling is a meritocratic industry [A]n individual’s race, class, age, and/or gender are meaningless in direct selling because success comes to those who simply work hard enough.”¹⁵⁶ This attitude reinforces the optimism shown in the recruiting materials, discussed later. However, it is likely that lower-income consultants will have networks with less disposable income,¹⁵⁷ MLMs ignore these structural realities.

147. CROSS, *supra* note 109, at 169.

148. See *Galatians* 6:7 (King James) (“[F]or whatsoever a man soweth, that shall he also reap.”)

149. Bone, *supra* note 42, at 116 (citing generally Peter Freund, *Social Performances and their Discontents: The Biopsychosocial Aspects of Dramaturgical Stress*, in *EMOTIONS IN SOCIAL LIFE* 268–94 (G. Bendelow & S. Williams eds., 1988)); ARLIE HOCHSCHILD, *THE MANAGED HEART: THE COMMERCIALIZATION OF HUMAN FEELING* (U.C. Press 1983)).

150. See Bone, *supra* note 42, at 116; see HOCHSCHILD, *supra* note 149.

151. *Ibid.*

152. CROSS, *supra* note 109, at 42.

153. See Pumela Msweli-Mbanga, *Predicting Turnover Behaviour of Direct Salespeople*, 8 S. AFR. BUS. REV. 14, 17 (2004).

154. See *id.* at 21.

155. ACN, *supra* note 3.

156. Lamoreaux, *supra* note 105, at 164–65.

157. See *id.* at 185.

Ultimately, the attitude of the disclaimer combines two biases: The fundamental attribution error and optimism. That is, a prospective consultant may view another consultant's failure due not only to the consultant's lack of talent but also due to their attitude — rather than the fact that the industry is relatively high risk. Because the failure is due to something that appears controllable, the prospective consultant may believe that regardless of how risky MLMs are, she is better than the average consultant.

Given that the attribution of success or failure falls squarely on consultants, it seems likely that unsuccessful consultants will engage the sunk cost fallacy.¹⁵⁸ Some consultants, as mentioned earlier, may continue in their MLMs because they feel as if they have given too much to end on a losing note. Alternatively, other consultants may engage with sunk costs in a novel — but still flawed — way. That is, the optimism of these consultants allows them to (mistakenly) *know* that they will recoup their investment; they are not afraid of having already lost some money because they *will* gain it back.

Even in the face of repeated failure, MLM consultants may find it difficult to remove themselves from MLMs altogether. As one reporter whose mother was a consultant noted, “[t]his business was different from the others, my mother insisted, and as long as she “worked it like a business” she could succeed It is hard to go to bat against a true believer.”¹⁵⁹

2. Independence

MLM companies also attempt to recast notions of success, shifting it away from how much a consultant makes to how she can participate in the workplace. MLM company origin stories often stress how they were founded as respectable, early 20th century alternatives¹⁶⁰ to “dangerous and [un]glamorous...labor in the domestic, manufacturing, or agriculture industry.”¹⁶¹ In particular, this idea that certain types of work were not respectable enough appears to be particularly gendered, aligning with the ideas of “middle-class evangelical Christian femininity.”¹⁶² Specifically,

158. “Some women left because of the debt they acquired while others held on to the belief that if they worked hard enough they would eventually succeed.” *Id.* at 188 (citing Virginia Sole-Smith, *The Pink Pyramid Scheme*, HARPER’S (July-Aug. 2009), 26–33).

159. *Id.* at 198.

160. See Lamoreaux, *supra* note 105 at 86.

161. *Id.* at 84. This was true in some cases — some of the most successful MLMs created opportunities for black women. See Kathy Peiss, “Vital Industry” and Women’s Ventures: Conceptualizing Gender in Twentieth Century Business History, 72 BUS. HIST. REV. 218, 233 (1998).

162. Lamoreaux, *supra* note 105, at 12 (citing Beth Kreydatus, “Enriching Women’s Lives”: The

one sociologist found in her fieldwork that MLMs “deliberately tap into women’s anxieties and desires to blend their perceived gender roles with their need for income.”¹⁶³

As mentioned earlier in this paper, the majority of MLM consultants are women.¹⁶⁴ It appears that “the most important and repeated motivation for entering into direct sales . . . was the desire to be stay-at-home mothers — to have *freedom*”¹⁶⁵ while still engaging in “meaningful employment . . . outside of waged labor.”¹⁶⁶ To that end, MLM companies are compared positively to profit-making “traditional corporate avenues.”¹⁶⁷ Recruiting materials may capitalize on gender stereotypes of women as “relationship oriented, caretakers, and socializers,”¹⁶⁸ suggesting that women are naturally more gifted at MLM skillsets.

Independence means many things to consultants — a flexible schedule, work-life balance, a way to provide goods and services that appear to align with their values,¹⁶⁹ and, in turn, a way to exercise their beliefs in a secular workforce.¹⁷⁰ But it also means a blurred boundary between work, home, and religion. For consultants inexperienced with the workforce, this can lead to underestimation of costs, as they may not account for the fact that they may ask their children to help with packages and setup,¹⁷¹ document the purchases they themselves made as business expenses,¹⁷² or count the hours they have been working, particularly if their office is the home. To that end,

Mary Kay Approach to Beauty, Business, and Feminism,” BUS. & ECON. HIST. ON-LINE 3 (2005)). See also *id.* at 95–100; see generally Katie Rose Sullivan and Helen Delaney, *A femininity that ‘giveth and taketh away’: The prosperity gospel and postfeminism in the neoliberal economy*, HUM. RELATIONS 1–24 (2016).

163. Lamoreaux, *supra* note 105, at 44.

164. But note that “men represent a majority of the executive leadership of the direct selling industry . . . and within direct selling affiliate [umbrella] organizations.” *Id.* at 162.

165. *Id.* at 102.

166. *Ibid.*

167. John R. Sparks & Joseph A. Schenk, *Explaining the Effects of Transformational Leadership: An Investigation of the Effects of Higher-Order Motives in Multilevel Marketing Organizations*, 22 J. ORG. BEHAV. 849, 852 (2001).

168. Lamoreaux, *supra* note 105, at 129; see also Pei-Chia Lan, *Networking Capitalism: Network Construction and Control Effects In Direct Selling*, 43 SOC. Q. 165–184 (2002).

169. Sparks & Schenk, *supra* note 167 at 852, provide some potential justifications: “[E]ducational toys advance the cause of children; weight management programmes enhance self-confidence.” To some extent, the blurring of religion and business is an encouragement to consultants: In one study, “being able to bring business together with private beliefs encouraged [a participant’s] recruitment” into a MLM business. Lamoreaux, *supra* note 105, at 97.

170. Busher, *supra* note 14, at 12. See also Cheris Shun-Ching Chan, *Reenchantment of the Workplace: The Interplay of Religiosity and Rationality*, 45 BERKELEY J. SOC. 42, 52–58 (2001).

171. See Lamoreaux, *supra* note 105, at 105–106 (finding that MLM consultants users view their office as home and vice versa).

172. See Vander Nat, *supra* note 35, at 141.

the blurred boundary “provides an effective means of exerting control over and eliciting affiliation from distributors.”¹⁷³ The consultant will be more committed to the organization¹⁷⁴ because of its mental association with her family.

Social interactions and social media also amplify the myth of independence. “The act of selling is transformed into an imaginary featuring making new friends, having fun, and caring about other people.”¹⁷⁵ Thus, the choice to enter a MLM feels less like an economic necessity and more of a choice.¹⁷⁶ At the same time, “MLMs establish elaborate systems of support through which members receive guidance and leadership from each other,”¹⁷⁷ as can be seen through numerous Facebook groups and teams of MLM sellers that advertise each other’s sales.¹⁷⁸ Moreover, successful consultants encourage others to “[t]rust the leadership and be coachable. If you want what successful people have, just do what successful people do.”¹⁷⁹ That is, consultants must still rely on the company to maintain their grit.

Finally, the benefits of independent employment leave the consultant with few tangible entitlements from their MLM. Unlike traditional full-time work, consultants do not receive health or retirement benefits.¹⁸⁰ Although some scholars argue that MLMs might personally empower low-income consumers,¹⁸¹ they may also render them ineligible for safety net provisions.¹⁸² Consultants must sign independent contractor agreements with indemnification and mandatory arbitration clauses.¹⁸³ Further, they are asked not to represent their relationship with the MLM company as more

173. Busher, *supra* note 14, at 12.

174. See generally Michael G. Pratt & José Antonio Rosa, *Transforming Work-Family Conflict into Commitment in Network Marketing Organizations*, 46 *ACAD. MGMT. J.* 395 (2003).

175. Lamoreaux, *supra* note 105, at 129.

176. Indeed, social satisfaction is suggested as a reason for a prospective consultant to participate in MLM. See Bhattacharya, *supra* note 140, at 369. However, it appears that excessive MLM activity by consultants may cause friendships to actually weaken, as people become irritated by solicitations. See Kent Grayson, *Friendship Versus Business in Marketing Relationships*, 71 *J. Marketing* 121, 132 (2007).

177. Sparks, *supra* note 169, at 851.

178. See, e.g., Lula Roe Down, FACEBOOK, <https://www.facebook.com/groups/lula.roedown/> [<https://perma.cc/N33B-RN8T>] (a website where clothes are sold by groups of consultants).

179. Spencer & Leanna Hunn — *Enjoying the Fruits of Their Labor*, ACN (Apr. 15, 2017), <http://theacnopportunity.shenellwhyte.com/acntelecomcanadamlm/acn-spencer-leanna-hunn.html> [<https://perma.cc/9C3Z-Z2XC>].

180. See Busher, *supra* note 14, at 18.

181. See *id.* at 19.

182. See *id.* at 18.

183. See ACN, *supra* note 3.

significant than it is¹⁸⁴ — even as ACN displays a blog post titled “10 Reasons Why ACN Can Change Your Life.”¹⁸⁵

IV. CONCLUSION

In this discussion of MLMs, I have noted several suggested policies, each with potentially mixed results or unanticipated consequences. *First*, cooling-off periods might allow time for consumers to justify their involvement in an MLM rather than question it. *Second*, other actions that are meant to lower costs once people join — for example, lowering upfront fees so that people can “try out” the MLM, or a more lenient buy-back policy so that customers are not stuck with inventory¹⁸⁶ — will not necessarily correct for consultants’ optimism, especially if the belief that grit is perfectly correlated with success is persistent. Moreover, these relatively generous policies might, like the Amway safeguards, make prospective consultants feel overly secure with their financial prospects. *Third*, regulating what and how information about a MLM is disclosed to consumers has proven somewhat politically unfeasible at the federal level,¹⁸⁷ especially given the ties between the MLM industry and the current administration.¹⁸⁸ When the final version of the Business Opportunity Rule was distributed in 2011, the FTC reiterated its stance, stating that it would be difficult for MLMs to craft an earnings disclosure given the heterogeneity of consultants (i.e., some work part time, some full time, and others intermittently), such that “disclosure would not provide prospective MLM participants with an accurate account of the MLM experience or with information necessary to make an informed purchasing decision.”¹⁸⁹

That said, simplifying disclosure has been done in other fields. It might be more politically feasible to pass enhanced consumer protection and disclosure laws at the state level. One could imagine, for example, a standardized handout (or website) accompanying each MLM that showed

184. *See id.* The relevant clause in the ACN Independent Business Owner Agreement states, “I agree to make no false or misleading statements regarding the ACN Products or about the various relationships between ACN, the ACN Provider(s) and me.”

185. Tracy Tippetts, *10 Reasons Why ACN Can Change Your Life*, ACN (Apr. 17, 2013), <http://acninc.co-m/news/company/2013/04/17/whyacn> [<https://perma.cc/N7W8-3TGH>].

186. Coughlan, *supra* note 40, at 13; Daryl Koehn, *Ethical Issues Connected with Multilevel Marketing Schemes*, 29 J. BUS. ETHICS 153, 156 (2001).

187. *See* discussion *supra* Part II.

188. In addition to the president’s endorsements of ACN, the current Secretary of Education, Betsy DeVos, is married to the son of Amway’s founder. Noam Scheiber, *Betsy DeVos, Trump’s Education Pick, Plays Hardball with Her Wealth*, N.Y. TIMES, Jan. 9, 2017, at A1.

189. FTC Business Opportunity Rule, Final Rule, 76 Fed. Reg. at 76823.

the average revenue, costs and hours worked, both nationally and in the metro area of the prospective consultant. At least one private-sector website has already attempted to provide standardized venues in which MLMs could be compared against one another; while the design is simple, the website uses metrics such as “expected payout after selling \$1,000” and “startup kit price.”¹⁹⁰ As mentioned previously, however, these metrics do not address the issues of how likely it is for a consultant to sell \$1,000 of product or the fact that a low startup kit price may make hidden fees less salient.¹⁹¹ Even if relevant information is provided to consumers, it may still be framed with an eye towards behavioral biases.¹⁹² The common shortcoming of these consumer-facing interventions is that they might create a cat-and-mouse game between marketers and regulators,¹⁹³ where marketers attempt to discover and exploit other behavioral biases. Nonetheless, it is not clear which behavioral interventions might succeed. Future research in the field should test these areas.

Even if regulating information disclosure to consumers does not necessarily change their behavior, due to the cat-and-mouse game, it is still important for MLMs to release more data on earnings and costs. In the same way the EEOC collects employee demographic and salary data, for example,¹⁹⁴ the FTC could collect MLM data for preliminary analysis and potential enforcement.¹⁹⁵ MLM companies might argue that they are so decentralized that it would be nearly impossible to aggregate this information, as they argued when the Business Opportunity Rule was being crafted, but that argument neglects the fact that costs and revenue data (in the form of inventory orders and sales data respectively) ultimately pass through their organizations. Furthermore, even if MLM consultants are considered independent contractors, the consulting agreements they sign require them to abide by the MLM’s policies. As such, the MLM is not prevented from implementing a policy where consultants must log the hours

190. See, e.g., CareerTrends, HERBALIFE, <http://work-at-home.careertrends.com/1/48/Herbalife> (last visited Apr. 20, 2017).

191. See *supra* Part III.

192. See, e.g., HERBALIFE, *supra* note 22, which does not clearly indicate that half of “active sellers” make no extra commission from Herbalife.

193. See Ryan Bubb & Richard H. Pildes, *How Behavioral Economics Trims Its Sails and Why*, 127 HARV. L. REV. 1593, 1648–1649 (2014).

194. See Pareja, *supra* note 19, at 89; Press Release, U.S. Equal Employment Opportunity Commission, EEOC to Collect Summary Pay Data (Sept. 29, 2016), <https://www.eeoc.gov/eeoc/newsroom/release/9-29-16.cfm> [<https://perma.cc/AXB5-A8M4>].

195. See Press Release, U.S. Equal Employment Opportunity Commission, *supra* note 194; Heidi Liu, *More Data, More Problems? Why the Proposed EEO-1 Data Collection is a Net Gain*, ON LABOR (Apr. 12, 2016), <https://onlabor.org/2016/04/12/more-data-more-problems-why-the-proposed-eeo-1-data-collection-is-a-net-gain/> [<https://perma.cc/QMN2-D9U7>].

they work. Because this data would not necessarily be used towards disclosures to individual consultants, concerns about coarsely estimated earnings serving as “inaccurate accounts of the MLM experience”¹⁹⁶ would be diminished.

Another suggested point of intervention is to equip trade associations to ensure that their members are acting ethically, such that membership in the association is an accurate signal of quality. There have been attempts to do this. For instance, one commentator notes that “MLMs who have joined the Direct Selling Association [the most prominent lobbying group in the industry¹⁹⁷], agree not to hide behind the ‘independent contractor’ status of their sales forces in an effort to avoid responsibility for what their sales force does.”¹⁹⁸ Still, it is unclear how the Direct Selling Association has enforced this and what incentive the organization would have for restraining its members.

In addition to studying the effects of potential behavioral interventions or regulations on MLM consultants, another important area of research is in the conditions under which MLMs (and potential interventions) exist. Changing these conditions could help make behavioral interventions efficacious and more specifically targeted. For example, one group of researchers suggests three areas of research: (1) “[T]he relative value of tangible and intangible rewards associated with becoming a MLM distributor,”¹⁹⁹ (2) the point when a distributor chooses to no longer participate, and (3) “the low level of complaints by victims of pyramid scheme fraud.”²⁰⁰

Differences among MLMs are also worth considering. For instance, there are several different ways in which MLMs distribute bonuses amongst consultants. These incentive structures may attract participants of different risk propensities, or shape risk propensities themselves. Alternatively, it is possible that the participant is not aware of these differences.²⁰¹ If some types of MLMs are more prone to unethical behavior than others, data from FTC settlements could help shed light on what types of MLMs undergo enforcement.

196. See FTC Business Opportunity Rule, Final Rule, 76 Fed. Reg. at 76823; discussion *supra* Part II.

197. See FTC Business Opportunity Rule, 73 Fed. Reg. 16110, 16114 (proposed Mar. 26, 2008) (to be codified at 16 C.F.R. pt. 437).

198. Koehn, *supra* note 186, at 158.

199. Keep, *supra* note 19, at 205.

200. *Ibid.*

201. See Rod Nichols, *Which Compensation Plan is the Best?*, BETTERNETWORKER (Sept. 24, 2010, 12:59 PM), <http://www.betternetworker.com/articles/view/sponsoring-and-recruiting/dealing-objections/which-compensation-plan-best> [<https://perma.cc/NB7F-Y6ZP>].

Research on existing legal and policy differences across states may also be helpful. For instance, various press articles seem to suggest that Utah is a hub for MLM incorporations due to a high level of trust in the community²⁰² — although this has rarely been supported with empirical data.²⁰³ It seems possible that the identity norms articulated in Part III might dovetail with Utah’s population, which is both highly religious and has a relatively high proportion of women outside the traditional labor force.²⁰⁴ Understanding the circumstances under which MLM-relevant policies form is important for understanding their potential consequences. Ultimately, given the lack of information around the industry itself, the legal landscape MLMs reside in is ripe for further study.

202. *See id.*

203. *See Pareja, supra* note 19, at 88 n.30; Alice Hines, How Utah Became a Bizarre, Blissful Epicenter for Get-Rich-Quick Schemes, TALKING POINTS MEMO (June 9, 2015), <http://talkingpointsmemo.com/theslice/mormon-utah-valley-multilevel-marketing-thrive-doterra> [<https://perma.cc/8MLU-HF8X>]; Daryl Lindsey, *Follow the Profit: How Mormon Culture Made Utah a Hotbed for Multi-Level Marketers*, KUTV (Sept. 8, 2016), <http://kutv.com/news/local/follow-the-profit-how-mormon-culture-made-utah-a-hotbed-for-multi-level-marketers> [<https://perma.cc/P876-FZA4>].

204. *See Lindsey, supra* note 203.
