



Pyramid Schemes

From the Office of Minnesota Attorney General Lori Swanson

Minnesota law prohibits all pyramid schemes because they deceive and cheat people. But promoters continue to hype pyramid schemes and recruit new people. con artists running the scams are looking for people who are vulnerable to get-rich-quick promises.

What is a Pyramid Scheme?

Pyramid schemes are illegal money-making ventures for individuals, businesses, and small groups of people. A typical pyramid scheme involves a few individuals at the top who recruit participants who, in turn, recruit other participants to offer something of value (usually money, but in some cases, time) to the organization. Recruits are offered the promise of large sums of money if they successfully bring in others to pay money to join the pyramid. Pyramid schemes focus on the exchange of money and recruitment. Usually, there is no legitimate product being sold.

How are Pyramids Disguised?

Pyramid schemes may be disguised as games, chain letters, buying clubs, motivational companies, mail order operations, or investment organizations. Some pyramid schemes call themselves multi-level marketing operations. The sale of legitimate products is what distinguishes multi-level operations from pyramids. When the emphasis is on recruiting new members rather than selling something of value the organization is probably an illegal pyramid.

How do Pyramids Work?

Basically, a pyramid scheme is formed when a single promoter (or small group of promoters) collects money from a certain number of “friends” and instructs them to collect more money from more of their “friends.” The cycle goes on from there. As the pyramid grows, the number of people involved becomes too large to sustain the pyramid. Some people will fail to send in their money, or recruit the required number of “friends,” and the pyramid crumbles. The majority of people end up on the “bottom” of the pyramid and inevitably will lose their initial “investment.” They won’t get their money back or earn their

promised fortune because no one is beneath them in the pyramid adding new money to the pot.

Why do Pyramids Fail?

Pyramid schemes collapse when a few people drop out or refuse to pay, and new members are not recruited in their place. In order for a pyramid scheme to profit, there would have to be a never-ending supply of potential (and willing) participants. In reality, however, the supply of participants is limited, and each new level of participants has less chance of recruiting others and a greater chance of losing money.

How is a Typical Pyramid Organized?

A simple pyramid — for example, a five level program built on recruitment by fours — might work like this:

- A new recruit would pay \$100 to “join” the organization.
- That money would then be disbursed at regular intervals by the company — \$25 to the recruiter, \$25 to the company, and \$50 to the recruiter’s “upline” in the form of \$10 payments to the recruiter’s recruiter, and so on through five levels.

continued

- The new recruit would recover the \$100 “fee” by recruiting four more people, each of whom would pay the recruiter \$25.
- From this point a participant is supposed to make money from all recruiting done by the four recruits and their recruits.

Pyramid Reality

- Pyramids are illegal. Because pyramid sales plans are by their very nature deceptive, they have been made illegal by the Minnesota legislature. There is a real risk that a pyramid operation will be closed down by police and the participants subject to fines and possible arrest.
- Pyramids are deceptive. Participants in a pyramid, whether they mean to or not, are deceiving those they recruit. Few would pay to join if the odds stacked against them were fully explained.
- Pyramids are losers. Pyramid Schemes are based on simple mathematics: many losers pay a few winners.

Why Would Anyone Pay to Join a Pyramid?

Pyramid promoters are masters of group psychology. At recruiting meetings they create a frenzied, enthusiastic atmosphere where group pressure and promises of easy money play upon people’s greed and fear of missing a good deal. It is difficult to resist this kind of appeal unless you recognize that the scheme is rigged against you.

Protect Yourself

- Take your time. Don’t be rushed into any business deal. Show your attorney any contracts you receive from the company. A legitimate business opportunity won’t disappear overnight.
- Ask questions about the competency and experience of the company and its officers; the products, including the potential market in your area; start-up fees; buy-back provisions; and actual earnings of current distributors.
- Get copies of all available company literature.
- Check with others who have experience with the company and its products. Find out if the products are actually being sold to customers.

Pyramids inevitably collapse because it is mathematically impossible to recruit the people required to support the pyramid.

A nine-level pyramid, which is built when each participant gets six “friends” to join, would involve over ten million people!

1. 6
2. 36
3. 216
4. 1,296
5. 7,776
6. 46,656
7. 279,936
8. 1,679,616
9. 10,077,696

- Investigate and verify all information. Contact the Minnesota Attorney General’s Office, the Minnesota Department of Commerce, your local Chamber of Commerce, or the Better Business Bureau if you suspect a company may be engaged in an illegal pyramid scheme.

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