

UNFAIR BUSINESS PRACTICES

PS7621 - VEMMA ITALIA-PRODUCTS WITH MANGOSTEEN JUICE

Ruling no. 24784

THE COMPETITION AND MARKETS AUTHORITY
DURING THE MEETING of February 5, 2014;

HAVING REGARD to the report by Professor Piero Barucci;

HAVING REGARD to Part II, Title III, of Legislative Decree no. 206 of September 6, 2005, as amended by Legislative Decree no. 146 of August 2, 2007, 6 (hereinafter, the Consumer Code);

HAVING REGARD to the “Regulation concerning preliminary investigation procedures on unfair business practices”, adopted by resolution of the Authority of November 15, 2007, published in the Official Journal no. 283 of December 5, 2007, and entered into effect on December 6, 2007 (hereinafter, the Regulation);

HAVING REGARD to the Notice of Commencement of proceeding no. PS7621 dated June 10, 2013, aimed at ascertaining the existence of unfair business practices in violation of Articles 20, 21 § 1, letters *b)* and *c)*, and 23, letters *p)* and *s)*, of the Consumer Code, followed by the company Vemma Italia S.r.l.;

HAVING REGARD to the Authority's resolution dated September 11, 2013, which extended the final date for completion of the proceeding;

HAVING REGARD to the records of the proceeding;

I. THE PARTIES

1. The company Vemma Italia S.r.l. (hereinafter also referred to as Vemma) is a retailer of various products based on mangosteen juice, some of which are presented by a demonstrator or sales associate (door-to-door sales) as allegedly having special therapeutic properties.

In the financial year ended in 2012, the company recorded sales revenues of approximately [*less than 1 million*]¹ euro.

2. Two consumers who reported the facts.

II. THE BUSINESS PRACTICE

3. This proceeding was initiated following reports from two consumers, and concerns the conduct adopted by Vemma, as a manufacturer, i.e. the creation and management of a complex system for the promotion and marketing of mangosteen-based products. This system envisages, on the one hand, the involvement and participation of consumers in a scheme for the purchase and sale of said products, whereby they are incentivized to sponsor the joining of the Vemma network by a constantly increasing number of other consumers/sellers; and, on the other, the representation of the products (in messages posted on the web) as having certain beneficial properties.

4. Participation in the sales network, with the title of “brand partner”, requires registration with the Vemma company's website (www.vemma.com), registration of an order

¹ In this version some of the data have been omitted, as information confidentiality or secrecy considerations have been deemed to exist.

for automatic shipment, and the purchase at a significant cost of one of two differently priced enrollment packages (“Vemma Builder Pack Silver” for € 604, or “Vemma Builder Pack Gold” for € 1,007), which are the requirements to have access to the different bonuses/commissions indicated in a specific Compensation Plan (hereinafter also referred to as CP).

5. In the Vemma network, participants receive compensation according to the number of persons they succeed in enrolling, as well as commissions calculated on the volumes of sales they generate for Vemma, directly or indirectly, including those generated by participants that they have enrolled into the Vemma Scheme.

6. According to the Compensation Plan, access to the promised commissions and bonuses is limited by a series of requirements that reduce their amounts, and in any case make them not directly linked to the total volumes of sales each participant generates directly and indirectly. In particular, it is necessary to reach direct monthly orders for a minimum amount in terms of commissionable volume (CV); also, participants need to possess specific requirements.

7. In addition to these aspects, intended to be financially attractive, the manufacturer and his partners emphasize the special properties of Vemma mangosteen-based supplements, making them appear as functional in creating an image, with end customers, as particularly beneficial to their well-being and/or health.

8. Messages with a content focused on health are found in the manufacturer's website in connection with Vemma products, which - owing to mangosteen, one of its ingredients - are attributed outstanding antioxidant properties, and with the Vemma Nutrition Program, which should allegedly be considered as a sort of health insurance.

III. FINDINGS OF THE PROCEEDING

i) Course of the proceeding

9. On the basis of information acquired for the purpose of applying the Consumer Code, and of reports from consumers about a suspected unfair business practice followed by Vemma in marketing and selling dietary supplements, on June 10, 2013, the preliminary investigation proceeding no. PS7621 was initiated against Vemma, for alleged violation of Articles 20, 21, paragraph 1, letters *b)* and *c)*, and 23, letters *p)* and *s)*, of the Consumer Code.

10. On July 29, 2013, a letter was received from the manufacturer, in which the latter made commitments in response to the remarks contained in the Notice of Commencement of proceeding, and requested an extension of the final date to complete same.

11. On September 11, 2013 the Authority resolved to reject the commitments undertaken by the Party and to extend the final date for completion of the proceeding till January 7, 2014.

12. On October 23, 2013, a hearing of Vemma representatives was held at the office of the Authority; during the hearing, the Party requested an extension of the end date of the proceeding.

13. On November 15, 2013, the Party was notified that the last date for completion of the proceeding had been extended to February 6, 2014.

14. The subsequent notes dated November 27 and December 10, 2013 provided further information and clarifications on the new methods for calculation of compensation and the company's new regulations.

15. On December 12, 2013, the Parties were notified the date of completion of the preliminary investigation phase, scheduled on December 23, 2013.

16. On December 23, 2013, the manufacturer submitted a defense brief to which was attached a copy of the new Compensation Plan.

ii) Evidence acquired

a) Vemma's distribution business

17. Vemma's distribution and promotion business in Italy started in January 2011 with sales revenues of over [1-5] million euro in 2011 and approximately [less than 1 million] euro in 2012.

18. As to the size of the sales network, based on investigations conducted and information provided by the manufacturer, it was found that the distribution network involved, in 2013, [1,000-5,000] associates, of whom only [less than 500] were active,² equal to 27% of the total³. The title of active is obtained and maintained by periodically ordering products or submitting an order at wholesale price⁴.

19. Specifically, the number of participants who joined the network in the first half of 2013, with the promotional "Gold" and "Silver" packs, were [less than 100] and [less than 100] respectively, (or [omissis] of the total number of new participants), while the number of participants who joined the scheme with the same packages from July 1 to October 24, 2013 were [less than 100] and [100-150] respectively, (or [omissis] of the total number of new associates)⁵.

20. Data acquired during the inspection have shown that the number of new associates who joined the network in 2012 and in the first five months of 2013 was [501-1,000] and [501-1,000], respectively.

Additionally, among the [250-500] active participants who submitted orders in the period from September 2012 to June 2013, only [less than 100] on average achieve sales volumes of any significance, i.e. such as to generate six-monthly sales commissions higher than € 1,000, while nearly all the other associates receive quite low or even paltry compensation.

21. The data collected show that Vemma received approximately [2,500-5,000] orders in the period from September 2012 to June 2013, with an average value, deducted of the Builder Pack, of about [100-150] euro per order.

22. Additionally, based on product sales data, a significant portion of the orders consists of purchases made by associates themselves, presumably for their own consumption, which in the network are known as "autoship" sales. In the period from September 2012 to June 2013, the income generated by autoship sales amounted to [omissis], while income generated by non-autoship sales was considerably lower, amounting to [omissis] euro.

b) The enrollment phase

23. In the Vemma network, consumers register without incurring any initial cost, by signing a contract with the attached Compensation Plan, and have the possibility of buying one of the promotional packs offered (Builder Pack), to which participation in the Plan is linked.

² See doc. 9, paragraph 5.

³ See doc. 23, paragraph f).

⁴ See doc. 16, paragraph 6.

⁵ See doc. 23, paragraph a).

24. In particular, after registration, associates are required to submit an autoship order for at least 60 QVs (Qualifying Volumes) every month. Once activity is qualified through the registration of at least one Brand Partner in each of the right and left team (the title of active is obtained through an active Automatic Shipment order of at least 60 reward points), the associate acquires the right to earn income immediately.

25. The associate also has the possibility of buying one of the following Builder Packs: "Silver", for a price of € 599, or "Gold" for a price of € 999, in order to fully benefit from the compensation envisaged in the CP. With each of these Builder packs (Silver and Gold), the consumer/associate buys a different set of Vemma products, corresponding to a different value (expressed in QVs): specifically, the Silver pack corresponds to 400 QVs, and the Gold pack to 800 QVs.

Depending on the pack they buy, associates have different and greater "opportunities" to earn the commissions set out in the CP.

26. The data for the period from September 2012 to June 2013 show that a considerable portion of Vemma's sales revenues, around [omissis], is generated directly by the sale of Builder Packs to the associates.

c) Vemma's Compensation Plan

27. As mentioned above, sales associates sign an agreement with Vemma which governs the rather complex mechanisms for receiving the compensation set out in the CP.

In particular, associates receive compensation both for enrolling other associates sponsored by them, and for the sales volumes they generate for Vemma, directly and indirectly through the associates in their "downline".

28. Looking at the details of the Compensation Plan, compensation consists mainly of the following items: i) "Cycle Bonus", ii) "Enroller matching bonus"; iii) "Second tier matching bonus"; iv) "Momentum Bonus"; v) "Platinum Club Bonus".

29. The Cycle Bonus is awarded to active Brand Partners with an Automatic Shipment order of 120 reward points and two personally enrolled active Brand Partners, one for each team. At the end of each volume period (week), the Brand Partner can earn a Cycle Bonus of approximately US\$ 20 if he/she has 180 reward points in one team and 360 reward points in the other (the sides may alternate). The value of weekly cycles is calculated each week on the basis of total sales divided by the number of qualified cycles⁶.

30. To earn the Enroller Matching Bonus, the associate has to be active and qualified with a registered Automatic Shipment order of 120 reward points and four personally enrolled active Brand Partners, one in each team and the other two anywhere in either team. This bonus pays to the Enroller 10% of all Cycle Bonus amounts earned by the Brand Partners he/she enrolled personally. If a Brand Partner does not meet the qualifying criteria, the bonus is transferred to the first Enroller in the upline who meets the requirements.⁷

31. To earn the Second Tier Matching Bonus, the associate has to be active and qualified with a registered Automatic Shipment order of 120 reward points and six personally enrolled active Brand Partners

⁶ Earning levels for cycles: earning levels for cycles only apply to the Cycle Bonus and do not affect any of the other income areas in Vemma's Compensation Plan. Once he/she achieves the maximum earning level in Cycle for that position for four (4) consecutive weeks, the Brand Partner is assigned one (1) new position above that in which he/she has achieved the maximum earning level. This position will have the same earning limit, unless the Brand Partner advances to a higher rank as specified below. A Brand Partner may hold up to two (2) positions, four (4) positions for married couples.

⁷ A Brand Partner may not earn the Enroller Matching Bonus and the Second Tier Matching Bonus for the same Brand Partner in the downline. In case of transfer of the Enroller Matching Bonus because of ineligibility of the Enroller, the Second Tier Matching Bonus is also transferred.

one in each team and the other four anywhere in either team. Brand Partners may not only earn on the associates they enroll personally, but may also earn a 10% Matching Bonus on all the Cycle Bonus amounts received by the enrolled Brand Partners. If a Brand Partner does not meet the qualifying criteria, the Second Tier Matching Bonus is transferred to the first Enroller in the upline who meets the requirements.⁸

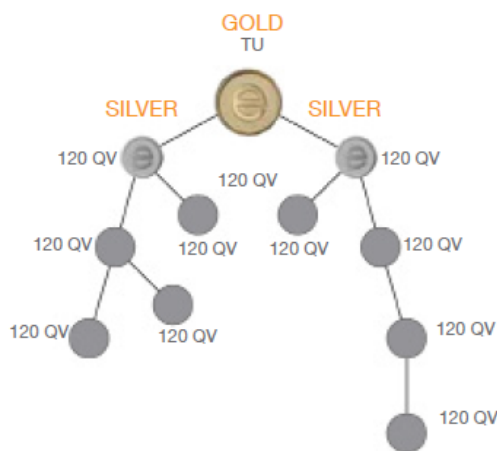
32. To earn the Momentum Bonus, the associate has to be active and qualified with a registered Automatic Shipment order of 120 reward points and one personally enrolled active Brand Partner, in each team. The additional requirements are shown in the table below⁹.

MOMENTUM BONUS

“PAYMENT LEVEL”: GOLD

Silver ** on each side of the enrollment line and 500 reward points consisting of Automatic Shipment orders and/or Builder Pack along the enrollment line on each side of their business.

Maximum payment per participation fee: Up to US\$ 300



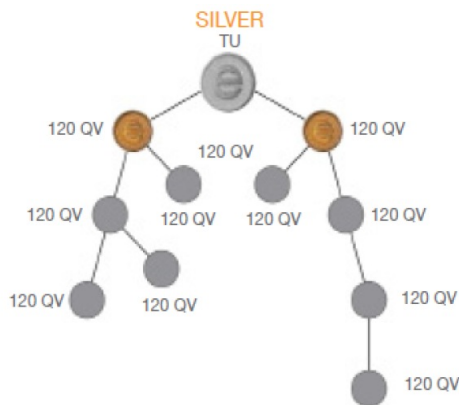
⁸ A Brand Partner may not earn the Enroller Matching Bonus and the Second Tier Matching Bonus for the same Brand Partner in the downline. In case of transfer of the Enroller Matching Bonus because of ineligibility of the Enroller, the Second Tier Matching Bonus is also transferred.

⁹ This bonus is a reward paid at the end of each four (4) week Rank Advancement, on the basis of the Payment Levels recognized during the current or the previous advancement period. The Momentum Bonus is equally subdivided among all participants who qualified on the basis of “Payment Level”. The Momentum Bonus Pool includes approximately three percent (3%) of the sales generated by the countries participating in the Momentum Bonus, and does not include orders on which a Fast Start Bonus was paid. The volume accumulated for the Momentum Bonus within a four (4) week rank advancement period is not transferred to the next four (4) week period. Compensation for each rank may vary from period to period. Brand Partners may participate in pools at each Momentum Pin rank for a period not exceeding twelve (12) months after the date on which they were recognized the Momentum Level Pin. Brand Partners who do not meet the requirements for the level that has been recognized may still participate in a lower pool for which they meet the requirements. All Brand Partners who achieve the Diamond Rank or higher and have a Gold “Payment Level” on each side of the enrollment line will pass from the Momentum Bonus to the Platinum Club Bonus.

“PAYMENT LEVEL”: SILVER

Bronze ** on each side of the enrollment line and 500 reward points consisting of Automatic Shipment orders and/or Builder Pack along the enrollment line on each side of their business.

Maximum payment per participation fee: Up to US\$ 200



33. Lastly, to earn the “Platinum Club Bonus” the brand partner must be active and qualified with an Automatic shipment order of 120 reward points. The Brand Partners must have purchased a Silver Builder or higher pack in the first 60 days after enrollment¹⁰.

34. A report by the Finance Police, who interviewed some of the network associates who earned the highest incomes documents the existence of a bonus called “frenzy bonus”. The interviewee stated that “each associate has two sales lines, the right and the left. When one line accumulates at least 180 points and the other at least 360 points, a “volume cycle” is generated producing a credit of approximately € 15. Income may also come from the so-called momentum bonuses and frenzy bonuses. The former, which may generate an income ranging from 75 to 225 euro, depending on the role one has in the network, is produced by the accumulation of at least 500 points per line over a one month period defined by Vemma. To earn the “frenzy bonus”, instead, one has to enroll three associates in a week, and is paid as a proportion of the latter’s purchases; this bonus can vary from 150 to 30 euro [sic]. Compensation is paid by bank wire transfer from abroad” (doc. 30, Exh. 8).

35. Additional requirements to access the commissions and bonuses set out in the Plan limit the amounts earned, and in any case result in their being not directly linked to the total sales volumes generated by associates, directly or indirectly (through their sponsored participants).

¹⁰ Brand Partners must achieve the Diamond “Payment Level” or higher and have a “Brand Partner paid as Gold” on each side of the enrollment line and 500 reward points consisting of Automatic Shipment orders and/or Builder Pack along the enrollment line on each side of their business, in a four week advancement period.

Once the Brand Partners are eligible for the Platinum Club, they may receive the bonus every time they meet the requirements during the four week rank advancement.

d) Vemma products

36. The manufacturer has produced all the dietary supplements distributed in the Italian market. All the supplements (Bode Burn, Bode E-cleans, Mangosteen Plus, Vemma Premium, Verve) are registered in the Ministry of Health's Register of Dietary Supplements. No health claim is contained in the labels.

37. In promotional materials acquired during the proceeding, some Vemma supplements were promoted claiming specifically their outstanding efficacy as antioxidants.

38. In view of the manufacturer's promotional messages boasting the health benefits of Vemma supplements, which are emphatically presented with expressions like "*arguably the most powerful antioxidant liquid*" or "*discovering the perfect supplement*"¹¹, the products' characteristics have been examined.

39. The descriptions of product properties provided by Vemma in regard to vitamins and minerals seem to comply with the provisions of EU Regulation no. 432 of May 16, 2012 (Claims).

iii) The manufacturer's defense arguments

a) On the pyramid nature of the Vemma network

40. Vemma pointed out that:

a) preliminarily, it does not recognize the role of consumer to the sales associates who join the Vemma network. The manufacturer - on the basis of the tax treatment applied, which benefits from reliefs and "[...] *is related to commercial intermediation operations*" and stating that an associate is comparable to a "*franchisee*" - maintains that "[...] *associates are financially independent from the principal company, are organizationally autonomous and conduct their business assuming all business risks*";

b) that a pyramid scheme exists if an associate earns on average more commissions "*... from other consumers joining the network*" than from the "*...sale or consumption of products*", and that Article 5, paragraph 1 of Law no. 173/05 makes no distinction between direct and indirect sales;

c) the so-called "fast start bonus" is not applicable in some European countries (including Italy), therefore the charge concerning the existence of a bonus payable immediately upon enrollment of a new associate is groundless.

d) "*The possible presence of incremental payments to associates linked to the forming of a team, and therefore to the involvement of other persons in the sales organization, certainly does not prove the prevalence of enrollment of new associates over the primary goal, which remains the generation of revenues from sales of products. [...] we do not believe that the presence of individual incentives to enrollment may of itself qualify the sales network as a pyramid scheme. [...] the network is not a pyramid scheme in that it does not reward mere enrollment in the absence of product sales*"¹². In fact, "*No compensation is paid for the enrollment of new associates, on the contrary, all compensation is linked to sales of products, in a spirit of*

¹¹ See doc. 9, Exh. 11.

¹² See doc. 9, paragraph 3.

*paying higher compensation to associates who demonstrate the ability to sell, directly or indirectly, greater volumes of products*¹³.

e) *“Autoship is an organizational mechanism the purpose of which is certainly not to impose anything, least of all the obligation to make periodic purchases. As such, the automatic shipment mechanism (autoship) is simply an order submission method and is neither mandatory nor irrevocable, as it may be canceled at any time”*¹⁴. In this regard the manufacturer specified that *“Joining the Vemma sales network does not entail any obligation to buy [...] Besides not requesting any payment at the time of registration, Vemma does not require the associates to purchase any promotional package to acquire the role of sales associate”*¹⁵ and that *“At the time of enrollment, no incentive exists - in law or in fact - for the new associate to make any purchases”*¹⁶. This is allegedly demonstrated by the percentage of associates who, at the time of joining, bought one of the Silver or Gold packs (equal to 22% in the second half of 2012 and the first ten months of 2013)

*“Until positive evidence exists that the associates are mainly compensated (meaning in a proportion of 50% + 1 of the bonuses and/or compensation actually received) on the exclusive basis of enrollment activities, in our opinion the compensation system is not to be censured in any manner”*¹⁷.

*“The possible presence of incremental payments to associates linked to the forming of a team, but in any case linked (as in the case at hand) to sales revenues generated by the new associates certainly does not prove the prevalence of enrollment of new associates over the primary goal, which remains the generation of revenues from sales of products. [...] the network is not a pyramid scheme in that it does not reward mere enrollment in the absence of product sales”*¹⁸.

b) On the health properties of the products

41. In regard to the messages that have been censured, the manufacturer points out that the properties attributed to the products correspond to the actual properties of said products. The descriptions of product properties provided by Vemma in regard to vitamins and minerals comply with the provisions of EU Regulation no. 432 of May 16, 2012 (Claims).

42. For the food products under comparison, the nutritional element values were derived from the database of the US Department of Agriculture¹⁹. Furthermore, with specific reference to the oxygen radical absorbance capacity, the latter was obtained using parameters and values developed by the Research Center of the aforesaid Department and applicable to fruit and vegetables.

c) Proposed changes to the Compensation Plan and to the promotional methods used for Vemma products

43. On July 29, November 26 and December 23, 2013 the manufacturer proposed changes to the adopted distribution model, specifically:

a) by making the Compensation Plan even more comprehensible;

¹³ See doc. 9, paragraph 3.

¹⁴ See doc. 34, paragraph 6.3

¹⁵ See doc. 34, paragraph 4.7

¹⁶ See doc. 34, paragraph 4.9

¹⁷ See doc. 34, paragraph 5.2.

¹⁸ See doc. 34, paragraph 6.1

¹⁹ See doc. 9, paragraph 4.

- b) by introducing a bonus called “retail bonus”, which will be clearly described in the new compensation plan as one of the main tools for generating revenues. This bonus will allow the Brand Partners to receive 5 to 40 euro in commissions on each order. The commission will be equal to the difference between Vemma products wholesale price (the “brand partner price”) and the recommended price to end consumers (“*recommended retail price*”). Within this framework, the brand partner invoices and receives payment for the product from the end consumer, acting as a professional distributor rather than as a sales associate. In essence, this bonus is compensation for intermediation of sales (those intermediated directly by the associate) and does not require the creation of any sales network for the associate to receive it²⁰;
- c) the so-called momentum bonus, which required sales volumes to be generated through the autoship mechanism or through the purchase of builder packs, is now awarded taking into account the volumes and the respective revenues generated by sales to consumers²¹;
- d) by removing the “Platinum Club bonus” (which required the purchase of a builder pack), thus eliminating the incentive to buy builder packs;
- e) the bonuses known as “enroller matching bonus” and “second tier matching bonus”, which required the presence of 4 and 6 associates, respectively, in the enroller's downline, are replaced by a single bonus (the “Team Bonus”), organized on two tiers, which requires a simple structure consisting of 2 to 4 associates in the downline;
- f) the bonus known as “Cycle bonus”, which required the enrollment of at least two associates in the downline, can be obtained simply by intermediating sales without being required to enroll any associates;
- g) changes to the internal procedures for the enrollment of new associates; enrollment can be completed free of charge and without the need to submit any initial order;
- h) removal of the mechanism called “*autoship*”. In order to remain active in the network, it will no longer be necessary to submit an autoship order (periodic product order) or a wholesale order. The associates will also have the possibility of using direct sales to their customers to remain active in the network, even without making personal purchases;
- i) the autoship mechanism has been eliminated altogether, both at the time of enrollment and as a method for activating associates into the sales system (for participation in the Compensation Plan), and as a requirement to receive any kind of bonus²²;
- l) Vemma will give even more visibility, at the time of enrollment of new associates, to their right to cancel orders or return the products within 30 days, thus exercising their unquestionable right of withdrawal. The enrollment procedure will not take place unless the associate has read and understood Vemma's return and withdrawal policies;
- m) Vemma undertakes to strengthen control over the advertising of its products by unauthorized parties, and to establish specific, stricter measures in case of violation of the provisions prohibiting misleading advertisements or those contained in the Consumer Code;
- n) a prospective associate will not be asked to sign the participation form without having carefully read and understood the Compensation Plan and the “Policies and Procedures” document, which expressly prohibits even mere emphasis on the earning opportunities involved

²⁰ See docs. 16 and 28

²¹ See doc. 28

²² See doc. 28

in participation on the Vemma network, so as to avoid creating expectations beyond what can reasonably be earned on the basis of the Compensation Plan²³.

44. Lastly, in regard to the promotional aspects, the manufacturer shall automatically terminate the agreement with the associate if the latter carries out advertising activities of whatever nature without the company's consent²⁴.

IV. OPINION OF THE COMMUNICATIONS REGULATORY AUTHORITY (AUTORITÀ PER LE GARANZIE NELLE COMUNICAZIONI - AGCOM)

45. As the business practice discussed in this ruling has been made known to the public through the press and broadcast media, on December 24, 2013 the Communications Regulatory Authority was requested to express an opinion in accordance with Article 27, paragraph 6 of the Consumer Code.

46. In the opinion submitted on January 23, 2014, the Authority found the business practice under examination to be unfair pursuant to Articles 20, 21, paragraph 1, letters *b*) and *c*), and 23, letters *p*) and *s*), of the Consumer Code, on the basis of the following considerations:

a) “based on ruling no. 20123 issued by the Competition and Markets Authority on July 22, 2009, “Waste Disposer”, the rationale of article 23, letter *p*), which establishes that any pyramid promotional scheme is deceitful, is - among other - (see paragraph 45) “to prevent the excessive expansion of distribution systems based on the progressive widening of the base of enrolled persons, detrimental to those who have invested in the pyramid once the chain expands exponentially”;

b) “even assuming that Vemma associates cannot be defined as “consumers”, they would then meet the definition of “microenterprises” under article 18, letter *d* bis) of the Consumer Code”;

c) additionally, “an average consumer would be induced to establish an improper relationship between constant consumption of the drinks and significant effects for the prevention of premature aging and weakening of the immune system, whereas no particular health properties have been demonstrated by scientific evidence, and “the information provided by the manufacturer in its commercial communications is unsuitable to inform the public on the actual characteristics of the product”.

V. FINAL CONSIDERATIONS

Introduction: Pyramid sales schemes

47. Law no. 173 of 2005, “Direct home selling and protection of consumers from pyramid sales schemes”, regulates the so-called “multilevel sales programs”, or direct home selling. In these systems, the participants are given the possibility not only of intermediating sales for a given company, but also of enrolling other people into the network, sponsoring them as new associates. The compensation received by each associate is directly linked to the sales he/she generates as well as to the sales volumes generated by the associates he/she sponsored, and these programs never impose²⁵ any constraints or prescriptions concerning the sales volumes that

²³ See doc. 34, paragraph 11.2.

²⁴ See doc. 34, paragraph 11.4.

²⁵ See among others the ruling issued by AGCM, no. 22299/2011, PS 6425 Xango.

must be achieved by the associate, together with his/her sponsored associates or otherwise, in a given time period.

48. By contrast, pyramid sales schemes - while sharing with multilevel schemes the structure that governs the intermediation of direct sales, are actually illegal, i.e. they are "sales organizations" where the primary economic incentive of the participant in the organization is based on the mere enrollment of new associates, rather than on their ability to sell or promote the sale of goods or services, directly or through other members of the organization"²⁶, and as such are strictly prohibited²⁷. The Consumer Code, in article 23, paragraph 1, letter *p*), also defines as unfair the conduct of a business organization that starts, manages or promotes "*a pyramid promotional scheme where consumers provide a contribution in exchange for the possibility of receiving payment mainly from the enrollment of other consumers into the scheme, rather than from the sale or consumption of products*"²⁸.

49. In particular, in pyramid sales schemes the sponsor's income does not depend only on the total sales volumes generated together with the associates he/she sponsors, (to which, moreover, they are not directly linked²⁹) but results mainly by the enrollment of other persons in the sales or promotional network, this being the primary aspect of this scheme, which determines the earnings level that will be recognized to sponsor. The mechanisms for the calculation of compensation, commissions and/or bonuses are extremely diversified, and the same can be said of the system for cashing the amounts that will then be returned as compensation (commissions) to the sponsors: in general, high participation fees are requested for this purpose from persons joining the sales network, and/or mandatory purchases of the products and/or services to be promoted or sold. Additionally, limitations are imposed on the payment of compensations through clauses introducing obligations relating to the specific characteristics of the organization formed by the sponsored associates: such characteristics must be achieved and maintained for a certain period of time, and/or requirements are set in connection with the associates' qualifications, and/or with the sales volumes to be achieved.

50. In other words, while a company that operates through multilevel direct selling pays its agents or sales representatives commissions that are always directly linked to the value or quantity of goods or services sold directly or through other associates that the agent/representative was able to enroll in the network, in a pyramid sales scheme the product or service to be sold becomes secondary, simply providing the pretext and opportunity to enroll other consumers to participate in the pyramid by making personal orders (purchases), thus artificially enabling the scheme to feed on itself. For this reason, newly enrolled sales representatives, as soon as they join the pyramid scheme, will pursue the primary objective to find other representatives and have them pay for the right

²⁶ Article 5, paragraph 1, Law no. 173 of August 17, 2005.

²⁷ Non-compliance with this prohibition is severely punished: under Article 7 of the above referenced law, anyone who starts or participates in pyramid sales schemes is punished with imprisonment from 6 months to one year or with a fine from € 100,000 to € 600,000.]

²⁸ Article 5 of the Code's final provision provides that "... Articles 5, paragraph 1, and 7 of Law no. 173 of August 17, 2005, n. 173, regulating direct home selling and the protection of consumers from pyramid sales schemes, are repealed in the part concerning pyramid sales schemes between consumers and business organizations as defined in Article 23, paragraph 1, letter *p*) of Legislative Decree no. 206 of September 6, 2005 (Consumer Code), where it envisages a possible contribution by a consumer as defined in article 18, paragraph 1, letter *a*), of said Code. The above mentioned articles 5, paragraph 1, and 7 shall therefore remain applicable to pyramid promotional schemes involving any individual or entity acting within the framework of their business, industrial, craft or professional activity".

²⁹ Whereas in multilevel schemes even a single unit of product sold entitles to compensation, pyramid schemes impose minimum volumes to be sold personally and/or as a group (together with the sponsored associates), and no compensation is paid unless these volumes are achieved.

to join or remain within the pyramid; the latter in turn will seek others, and so on.

51. The rationale underlying the regulation is to prevent the spreading of systems aimed not so much at selling goods or services, as at gaining economic benefits linked mainly to the progressive expansion of the associate base, through the deceitful representation of easy earnings³⁰. Those who last joined the pyramid scheme will only be able to earn the promised amounts - in some cases, to recover what they paid for participation - if a high number of participants join and make sales³¹, while there is a strong risk that the chain will break and that the new associates will never obtain any actual economic benefit³².

52. This possibility – the likelihood of which depends among other factors on the type and nature of the requirements set out in the compensation plans – is of course omitted at the time of enrolling new associates, to whom on the contrary the possible earnings are represented as immediate and rather significant, also through participation in meetings or events where the allegedly outstanding properties (e.g. health benefits) of the supplements are emphatically boasted.

i) On Vemma associates meeting the definition of consumers

53. Preliminarily, it should be noted that both in multilevel sales networks and in their degeneration, represented by pyramid schemes, what matters is not so much the formal title of the participants, i.e. sales associates, but rather the substantial fact of the activity they carry out, which normally ends up being an occasional activity. In the case of Vemma, according to the data provided by the manufacturer, only *[omissis]* of the associates have a VAT number, while all the others are occasional associates; moreover, only an extremely small number of associates received six-monthly commissions of more than € 1,000.

54. It should be added that, particularly in pyramid schemes, at the time of enrollment the new participants are subject to obligations and solicitations to buy products: these aspects undoubtedly qualify these individuals as consumers rather than professionals who carry out sales activities.

55. Further confirmation of this is provided, in the Vemma scheme, both by the small number of orders submitted by the associates (less than a quarter of the associates made at least one order) and by the implementation of the autoship mechanism, involving a considerable number of these orders. On the basis of the information provided by the Party, during the period from September 2012 and June 2013, the manufacturer's revenues were generated mainly by autoship sales, and to a much lesser extent by other sales (the former amounting to *[omissis]*, while the latter amount to *[omissis]* euro). In this case, the associate does not intermediate any sale to a third party external to the schema, but buys for him/herself, unless one is willing to assume that the purchased supplements may have been sold by the associates to others "on a retail basis".

56. Lastly, the same regulation referred to above (Law no. 173/2005), in defining the role of sales associates of individuals operating as part of a

³⁰ See ruling no. 19163 of November 20, 2008, PS121 – Telme telephone systems with VSIM-NGR, in Newsletter no. 44/08

³¹ Thus, the result in most cases is a purchase network rather than a sales network, where the buyers, however, are the associates/consumers themselves.

³² Indeed, in general only a very small number (a few dozens) of associates with high sales qualifications receive compensation of some significance (a few tens of thousands of euro per year), even for sales networks consisting of several tens of thousands of participants.

“multilevel marketing” scheme, identified the elements that characterize a sales organization as a pyramid scheme, going beyond the formal aspect related to the sales associate's role.

ii) On the pyramid nature of the Vemma network

57. Before analyzing the nature of the Vemma network, it should be noted that, in the documents presenting the Vemma network and specifically in the Compensation Plan distributed to consumers who are about to join, the earning opportunities are extensively emphasized (e.g.: “possible total earnings: US\$ 414,100” or “we have a strategic plan that will make you earn \$ 500, \$ 5,000 or even \$ 50,000 per month!” “If you are ready to make your financial dreams come true without limits, now is the perfect time to become a Vemma Brand Partner. Simply choose a Builder Pack to maximize your opportunities. As you will see, this small investment in your business is nothing compared to the potential income that this opportunity offers.”³³, while on the other hand the same completeness and/or clarity is not found in regard to the mechanisms for the calculation of compensation for each type of commission or bonus.

58. What emerges very clearly, instead, is that the network for the marketing and sale of Vemma supplements is structured according to rules that appear to be mainly aimed at acquiring new consumers within a complex compensation system. In particular, the presence of the so-called Builder Packs and of the periodic and automatic purchase order is undoubtedly anomalous in a multilevel sales network, whereas they constitute - as set out in the introduction - the typical elements of a pyramid system, in which the purpose of the manufacturer or business organization is to receive a significant contribution from consumers, both initially and in the form of subsequent purchases. Indeed, it is only through these enrollment methods that associates are able to benefit, to different extents, from all the commissions set out in the CP.

In particular, the purchase of autoship products is a requirement in order to be considered active, and therefore to be able to benefit from the different bonuses set out in the CP, which represent the real attraction for the new associates. Thus, it is clear that the purpose of the scheme is not to create a multilevel sales network, but a purchase network with consumers fictitiously enrolled as sales associates³⁴.

59. To appreciate the relevance of these aspects, it is enough to recall that in the period from September 2012 to June 2013, approximately 20% of the total income generated from product sales was obtained from the sale of the so-called Builder Packs, and over 60% was generated from autoship sales.

During the same period, only about 16% of the income was generated from the sale of products to third parties.

It is evident, therefore, that “personal” orders or purchases of Builder Pack products, as well as subsequent (“autoship”) purchases by associates play an absolutely predominant role in the scheme under examination.

60. Additionally, to recover the sums initially paid the associates need to sponsor other associates to join the network; specifically, the recovery occurs through payment of the compensation called “Enroller matching bonus” (whereby the enroller receives 10% of all the cycle bonus amounts earned by the associates he/she personally enrolled) and of the “second tier matching bonus” (equal to

³³ See doc. 12, page 14.

³⁴ This aspect confirms the anomalous nature of the Vemma sales network, making it more similar to a purchase network where the associates/consumers are primarily required to buy the manufacturer's products in order to remain within the scheme and earn indirect commissions.

10% of all the cycle bonus amounts earned by the associates in turn enrolled by those whom the enroller enrolled personally).

Based on this mechanism, the associate is induced, firstly, to enroll new consumers, also to recover the sum initially paid.

61. A particularly important element, for the purpose of determining that the Vemma network is in fact a pyramid scheme, is the requirements for earning the commissions/bonuses on the sales generated by the organization to which the associate belongs, as well as the presence of certain specific qualitative requirements of the sales organization and of the individual associate. While the mechanisms for commission calculation are characterized by a high level of complexity and confusion, it appears clear that the Compensation Plan involves the obligation of submitting monthly personal orders. Under the CP, the associates are under the obligation to produce monthly orders, and subsequently for a minimum amount, in order to participate in the distribution of the compensation and maintain the rank achieved.

62. It should also be noted that, in the Vemma network, the sales commissions provided by the CP are not granted in direct proportion to the total volume of generated sales, but only on a subset of the latter.

In particular, the volume calculation mechanism, based on only one of the created downlines, excludes sales for a volume amount equal to that generated by a single line.

63. In this regard it should be noted that, out of all the associates, only [less than 50] received (in the second half of 2012) six-monthly commission of any significance (2,000 to 5,000 euro) and [less than 50] received higher compensation amounts (more than 5,000 euro), while all the other associates received rather low if not paltry compensation; only 24% of the associates had a VAT number during that period.

64. Conversely, no relevance is to be attributed to the statement contained in the Party's defense brief of July 3, 2013 according to which it is possible for the associates, under Section 13 of the Distribution Agreement, to return the products through the Customer Service, as this action takes place after the effects of the mechanism (sponsoring the participation of other associates in the network) are already underway, and in any case the loss in product value (even if less than 10%) in case of return, combined with the onerous administrative procedures, undoubtedly act as a deterrent for returns to occur with any appreciable frequency.

65. In summary, the contested conducts were: the fact of setting up a sales network with the characteristics of a pyramid scheme, where the manufacturer makes a profit mainly from the enrollment of associates and the purchases of product made directly by the latter, and where the associates' promotional effort is aimed at constantly enrolling new associates and creating a purchase network (with purchases made by the participants themselves), rather than generating product sales.

66. Conversely, the changes introduced by Vemma in the Compensation Plan, described on July 29, November 26 and December 23, 2013 shall not be examined in this ruling. The reason is, on the one hand, that these measures cannot be accepted as commitments, considering the seriousness of the business practice under examination and the Authority's interest in investigating the matter. On the other hand the proposed measures, while they certainly address some of the more questionable aspects of the CP (elimination of the mandatory monthly orders and need for any type of purchase to be enrolled in the network; changes to some of the bonuses), still maintain certain elements of the old scheme - specifically, the calculation method, which considers the so-called "short leg" - and introduce new ones - e.g., the so-called "team bonus", which still requires, in order for

the associate to receive it, the presence in the latter's downline of a certain number of other associates. These changes require a new, complex review of the scheme, which is not part of the investigation into the subject conducts.

iii) On the nature and the health properties of the product

67. A synergistic role in enhancing the effectiveness of this pyramid scheme is generally the misleading representation of the supplements, so as to make them more attractive by attributing to them properties they do not possess.

68. In regard to the content of the health indications, however, it should be noted that the claims used are in line with the recent list contained in EC Regulation no. 432/2012; therefore, with respect to these provisions, the business practice adopted by Vemma, as set out in section II of this ruling, does not appear to constitute a violation.

VI. AMOUNT OF THE SANCTION

69. Pursuant to article 27, paragraph 9, of the Consumer Code, in issuing the ruling that prohibits the unfair business practice the Authority may provide for the application of an administrative sanction of € 5,000 to € 500,000, taking into account the seriousness and duration of the violation.

70. In regard to the amount of the sanction, the Authority should keep in mind, to the extent they are applicable, the criteria set out in article 11, Law no. 689/81, as referred to in article 27, paragraph 13, of the Consumer Code, and in particular: the seriousness of the violation, the efforts made by the company to eliminate or mitigate the violation, the personality of the agent, and the financial conditions of the company.

71. As to the seriousness of the practice, factors to be considered are the importance and size of the manufacturers, which in the case at hand is a company with large sales revenues, known in the specific sector as a company operating in some EU countries and in the United States, where the parent company Vemma Nutrition *has its place of business*.

72. The seriousness of the violation is also determined on the basis of the widespread nature of the practice, which involved a high number of consumers, approximately [1,000-5,000], and of the particular nature of the violations, i.e. the adoption of a pyramid distribution scheme.

73. In regard to the duration of the violation, according to the available information the business practice was first adopted in early 2011, also through the use of promotional materials dedicated to the products, and is still ongoing.

74. Based on these considerations, this Authority deems it appropriate to determine the amount of the administrative sanction applicable to the company Vemma Italia S.r.l. to be € 100,000 (one hundred thousand euro).

DEEMING, therefore, on the basis of the considerations set out above, that the business practice under examination is unfair because the complex system for the marketing and sales of products has the nature of a pyramid scheme, in violation of articles 20, 21 paragraph 1, letters *b*) and *c*), and 23, letter *p*), of the Consumer Code;

RESOLVES

a) that the business practice described in section II of this ruling, implemented by the company Vemma Italia S.r.l., constitutes, for the reasons and within the limits set out in the Grounds of the Ruling, an

unfair business practice pursuant to Articles 20, 21, paragraph 1, letters *b*) and *c*), and 23, letter *p*) of the Consumer Code, and prohibits its spreading or continuation;

b) to apply to Vemma Italia S.r.l. an administrative pecuniary sanction of € 100,000 (one hundred thousand);

c) that the manufacturer shall be required to communicate to the Authority, within sixty days after being served this ruling, the actions it has taken in compliance with the caution under paragraph a) above.

The administrative sanction set out in paragraph b) above shall be paid within thirty days after being served this ruling, using the attached Form F24 with identification information, in accordance with Legislative Decree no. 241/1997. The form can be submitted in paper format to any bank, Poste Italiane S.p.A. office, or Tax Collection Agent. Alternatively, the form can be submitted online and the amount be debited to the company's bank or postal account, through the home-banking and CBI services made available by banks or Poste Italiane S.p.A., or using the online services of Agenzia delle Entrate (Internal Revenue Agency), available at www.agenziaentrate.gov.it.

Pursuant to article 37, paragraph 49, of Law Decree no. 223/2006, individuals and entities having a VAT number are required to submit the F24 form through online channels.

After the period specified above expires, if the delay is less than six months, interest on late payment shall apply, according to legal rate, from the date following expiry of the payment period to the date of payment. If payment is further delayed, pursuant to article 27, paragraph 6, of Law no. 689/81, the sanction amount shall be increased by one tenth every six months, from the day after expiry of the payment period to that on which the roll is transmitted to the tax collection concessionaire; in this case, the increase absorbs interest on delayed payment accrued in the same period.

Once payment is made, notice of it must be immediately given to the Authority by transmitting a copy of the form documenting payment.

Pursuant to article 27, paragraph 12, of the Consumer Code, in case of non-compliance with this resolution the Authority shall apply an administrative pecuniary sanction of € 10,000 to € 150,000. In case of continued non-compliance, the Authority may order the suspension of the company's business activity for a period not exceeding thirty days.

This ruling shall be notified to the parties concerned and published in the Newsletter of the Competition and Markets Authority in consideration of the nature of the unlawful conduct and to ensure that the public is duly informed of its institutional activity.

The Party may file an appeal against this ruling with the Lazio Regional Administrative Court (TAR), in accordance with article 135, paragraph 1, letter *b*), of the Code of Administrative Proceeding (Legislative Decree no 104 of July 2, 2010), within sixty days after notification of this ruling, unless a longer period is granted under article 41, paragraph 5, of the Code of Administrative Proceeding, or may submit an extraordinary appeal to the President of the Republic in accordance with article 8 of Presidential Decree no. 1199 of November 24, 1971, within one hundred and twenty days after notification of the ruling.

THE SECRETARY GENERAL
Roberto Chiappa

THE PRESIDENT
Giovanni Pitruzzella
