

Delaware v. Ferro

©www.mlmllegal.com

Welcome to the MLMLegal.com Legal Cases Project. Here you will find hundreds of legal cases in the fields of MLM, Direct Selling, Network Marketing, Multilevel Marketing and Party Plan. The cases span federal and state courts as well as administrative cases from the FTC, FDA, IRS, SEC, worker's compensation, unemployment compensation, etc.

The intent of the MLMLegal.com Cases Project is strictly educational, and, to provide insight into the legal issues and cases for an industry that spans the globe in upwards of 150 countries with sales volume exceeding \$100 billion and distributor involvement in the tens of millions. MLMLegal.Com does not promote or endorse any company. MLMLegal.Com offers no value judgments, either pro or con, regarding the companies profiled in legal cases.

Jeffrey A. Babener, principal attorney in the Portland, Oregon, law firm Babener & Associates, and editor of www.mlmllegal.com, represents many of the leading direct selling companies in the United States and abroad.

www.mlmllegal.com www.mlmllegal.com www.mlmllegal.com www.mlmllegal.com

Delaware v. Ferro

Case: Delaware v. Ferro (1988)

Subject Category: Criminal

Agency Involved: Criminal Case

Court: Delaware Superior Court

Case Synopsis: The Delaware Superior court was asked to decide if an "airplane" sales scheme constituted a "pyramid or chain distribution scheme" the promotion of which was a violation of Delaware law.

Legal Issue: Is an airplane sales scheme a "pyramid or chain distribution scheme" the promotion of which was a violation of Delaware law?

Court Ruling: The court held that the statute prohibiting pyramid schemes was constitutional, and that an airplane scheme fell under the definitions within the statute because it was a "sales device" that transferred a "right" to perpetuate the scheme. Because the activity clearly fell under the statute, the defendant's motion to dismiss the charges was denied.

Practical Importance to Business of MLM/Direct Sales/Direct Selling/Network Marketing/Party Plan/Multilevel Marketing: Pyramid schemes can be regulated under securities laws, consumer

protection laws, and criminal laws. Where the law is clear on the subject, a motion to dismiss will not usually succeed

Delaware v. Ferro , 1988 WL 39996 (Del.Super. (1988) (Not Reported) : The court held that the statute prohibiting pyramid schemes was constitutional, and that an airplane scheme fell under the definitions within the statute because it was a "sales device" that transferred a "right" to perpetuate the scheme. Because the activity clearly fell under the statute, the defendant's motion to dismiss the charges was denied.

www.mlmlegal.com www.mlmlegal.com www.mlmlegal.com www.mlmlegal.com

1988 WL 39996 (Del.Super.)

STATE

v.

Daniel and John FERRO.

Superior Court of Delaware.

Submitted: April 6, 1988.

Decided: April 15, 1988.

BIFFERATO, Judge.

*1 The defendants in this case have been indicted for violations of 6 Del.C. s 2561 and a corresponding charge of Conspiracy in the Third Degree in violation of 11 Del.C. s 511. The defendants have filed two motions to dismiss claiming that: (1) the conduct alleged in the indictment is not prohibited by 6 Del.C. s 2563; and (2) the indictments, together with the underlying statute, 6 Del.C. s 2561, are unduly vague.

The defendants are alleged to have promoted participation in a pyramid scheme. In consideration for \$5,000, a consumer joins the investment group as a junior sales executive. Once recruiting two other individuals who are willing to pay \$5,000 to obtain a seat in the group, the original consumer moves up the ladder, becoming a senior sales executive and the two new investors become junior sales executives. When each new junior sales executive brings in two new investors, the original investor is promoted from senior sales executive to branch manager. The branch manager ultimately becomes a division manager and the eight new junior sales executives each pay him \$5,000 for a total payment of \$40,000. At that time, the original investor either leaves the investment group or starts over again as a junior sales executive.

The defendants are alleged to have promoted or granted participation in a pyramid scheme in violation of 6 Del.C. s 2563(a) which reads:

No person, either directly or through the use of agents or other intermediaries, shall promote, sell, attempt to sell, offer or grant participation in a pyramid or chain distribution scheme.

A pyramid scheme is defined in 6 Del.C. s 2561(1) as follows:

"Pyramid or chain distribution scheme" means a sales device whereby a person, upon a condition that he part with money, property, or any other thing of value, is granted a franchise license, distributorship or other right which person may further perpetuate the pyramid or chain of persons who are granted such franchise, license, distributorship or right upon such condition.

Thus, the initial issue before the Court is whether the alleged activity is a "sales device" as defined by s 2561(1).

The defendant argues that "sales" is undefined by the statute. Title 6 Del.C. s 2562 makes the use of a pyramid scheme an unlawful practice under s 2513 of this title. The definitions for s 2513 are found in s 2511 which defines "sale" as "any sale, offer for sale, or attempt to sell any merchandise for cash or credit." 6 Del.C. s 2511(4). "Merchandise" means any "objects, wares, goods, commodities, intangibles, real estate or services." 6 Del.C. s 2511(2). The word "device" is not defined in the subchapter prohibiting pyramid schemes. The common definition of "device", however, is found in Webster's New Collegiate Dictionary as "a scheme to devise."

Using the above definitions, s 2561 can be understood to mean that a pyramid scheme is a scheme or method of obtaining money from a person in exchange for granting that person the right to further perpetuate the chain the right to bring in more investors. It is generally held that if an individual is materially benefited by bringing in new members so that the emphasis is not on the sale of products, it is a pyramid scheme. See, *State v. Salem*, Minn.Supr., 222 N.W.2d 98 (1974); *State ex rel. Edmisten v. Challenge, Inc.*, N.C.App., 284 S.E.2d 333 (1981). The investment group, in the case sub judice, is a group primarily engaged in constructing a pyramid, using the sale of "seats" in the group as a front for its transactions. In exchange for the fee, the new investor or junior sales executive has the right to recruit others who would themselves have to pay a large sum of money to join the organization. The emphasis is on the sale of membership and not a product. The Court finds, therefore, that the investment plan is a pyramid scheme under 6 Del.C. s 2561(1).

The defendants argue further that the investment is not a "franchise, license, distributorship or other right" as required by s 2561. In response to the bill of particulars, the State indicated that the right granted in the pyramid scheme was an illegal right to bring other people into the pyramid scheme in order to receive money. Since a "right" is an enforceable claim and the investor has obtained no enforceable right or claim to anything, the defendant concludes that the conduct alleged in the indictment is not proscribed by s 2561.

*2 The defendants' argument is without merit. "Right" as used in the context of this chapter means an interest or privilege which is unenforceable at law. To suggest that the investor must acquire an enforceable claim before falling within the penal statute would be an illogical interpretation of s 2561.

Finally, the defendants have filed a separate motion to dismiss the indictment on the grounds that 6 Del.C. s 2561 and the indictment are unduly vague. As noted above, the defendants claim that the terms "sales device" and "right" are not defined in the statutory scheme and that the statute is unusually "labyrinthine."

Stripped to its adjectives, s 2561 reads:

Pyramid ... scheme means a sales device whereby a person, upon a condition that he part with money ... is granted a ... right which person may further perpetuate the ... right....

This is sufficiently defined that an individual of ordinary intelligence can understand what is prohibited. *Grayned v. City of Rockford*, 408 U.S. 104 (1972). In other words, recruiting investors to pay money for a seat in an investment program so that they may recruit others to pay money is an illegal pyramid scheme. The Court cannot say that the statute is so vague that men of ordinary intelligence must guess at its meaning. *State v. Green*, Del.Super., 376 A.2d 424 (1977).

For the foregoing reasons, the defendants' motions to dismiss are DENIED.

IT IS SO ORDERED.

www.mlmlegal.com www.mlmlegal.com www.mlmlegal.com www.mlmlegal.com

http://www.mlmlegal.com/legal-cases/Delaware_v_Ferro.php