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Ministry of Commerce People's Republic of China
Department of Foreign Investment Administration
No.2 Dong Chang'an Avenue,
Beijing China (100731)
Phone: (010)65284671
Fax: (010)65599340

Mr. Wang Zhongfu - Director
State Administration for Industry and Commerce
8 Sanlihe Donglu, Xicheng District, Beijing 100820, China
Tel: (86-10) 6803-2233
Fax: (86-10) 6802-0848

Dear Respected Government Officials;

The Fraud Discovery Institute, Inc. has been filming a documentary titled “**Doomed by Design**” to be released internationally in the 4th quarter of 2007.¹ This documentary is focused on the business opportunity and practices of two companies, one of which is Herbalife, LTD (hereafter referred to as Herbalife). **Doomed by Design** contains footage obtained from (by)

1. An undercover investigation², that legally obtained video footage of various opportunity meetings held by Herbalife.
2. Former employee(s) (not to be confused with distributors) of Herbalife never before seen on film telling their stories.
3. Interviews with victims of Herbalife who spent thousands of dollars on tools, product, leads or lead generation products, and were, according to their interviews, financially ruined as the result of these entities.
4. Interviews with a variety of experts ranging from the former assistant chief of enforcement at the Securities and Exchange Commission's New York regional office, to nutraceutical experts from Columbia University's Department of Nutrition and Applied Physiology, political experts, a PhD mathematician, former and current law enforcement, stock analysts and other contributing experts.
5. Extensive investigation of Herbalife's operation in China using primary source research which included in-person visits and interviews at two different locations³

¹ In the interest of full disclosure, the documentary “Doomed by Design” will also be used by agents representing certain participants for a proposed weekly television show dealing with issues of fraud tentatively titled “America's Frauds Most Wanted.” The information included in this report could be the basis for an upcoming television show which would financially benefit Mr. Minkow and others who have produced the documentary.

² All undercover footage was done in one-party consent states.

in the country of China, as well legally obtained taped phone calls and video footage of Herbalife employees (not to be confused with distributors) in the countries of China, Singapore and Taiwan.

Cheating in China is “Material”⁴

While researching for this documentary, the Fraud Discovery Institute came across evidence of apparent material impropriety by Herbalife in China.⁵ It is material in part because of a recent statement found on page 7 of the Company’s latest 10-K Annual Report (a “10-K” is an annual report which is filed with the US Securities and Exchange Commission):

While we plan to expand into new markets each year, expanding in China represents a significant growth opportunity for us. We believe that China could become one of the largest direct-selling markets in the world over the next several years. To address this opportunity, we have assembled a management team with direct selling experience.

Moreover, according to the company’s latest 10-Q (a “10-Q” is a quarterly report that is filed with the US Securities and Exchange Commission), they have achieved an almost 70% year over year growth in China.⁶ In fact, the company currently has 47 retail stores and 37 service centers in 28 provinces⁷ and consistently touts China⁸ as their next

³ One location was on October 11th, 2007 at One layer No.4# Building, Weipeng Garden, Zhenzhong Road, Futain District, SZ (深圳市福田区振中路玮鹏花园4栋首层) which is confirmed to be an official Herbalife location from the company website (please see <http://www.herbalife.cn/english/branchFollow.action?pageIndex=3&query.type=3>) and the other location is shown on the business card of the Herbalife employee contained in our last addendum and it took place on October 15th and 16th, 2007.

⁴ The laws governing each employee of Herbalife in China, which are equivalent to distributors in other countries, are summarized in the following link http://www.iibulletin.com/kmclaw/10_04/article2.html. Although these employees have strict guidelines mandated by the Chinese government, for the purposes of comparison they perform the function of a distributor minus the ability to develop a downline as in typical multi-level marketing structures. In their official website <http://www.herbalife.cn/english/newsDetailFollow.action?id=278>, the company claims that they will abide by these laws.

⁵ The reason for the emphasis on materiality is based upon Herbalife previously underplaying the seriousness of fraud allegations in Belgium. The company was accused of fraud there, but Herbalife noted that sales in Belgium were negligible and therefore win, lose or draw, it was really much ado about nothing. (Please see Herbalife’s 2006 10-K, page 30.) In the case of China, this issue cannot be dismissed because of materiality. Furthermore, the problem in China is both internal (Chinese nationals participating in multi-level marketing within the country) and external (Chinese nationals placed in downlines outside of China).

⁶ Please see page 22 <http://yahoo.brand.edgar-online.com/fetchFilingFrameset.aspx?dcn=0000950124-07-003991&Type=HTML>.

⁷ Please see July 9th, 2007 press release, http://www.herbalife.com/global/investor_relations_frset.jsp?irhome&, 3rd paragraph.

greatest growth market.⁹ Additionally, the company *never* hesitates to announce publicly to Wall Street when they succeed in securing any new license in *any* province or city in China. If the “good news” of obtaining those licenses is newsworthy, then any bad news relating to the entire Chinese operation (or the sum of its parts) is equally as newsworthy.¹⁰

Instead of distributors, Herbalife has “employees” in China, as the laws of that country prohibit multi-level marketing and only allow a model of single level direct selling with a commission cap of 30.¹¹ According to the most recent 10-K:

*In China, as of December 31, 2006, we also had labor contracts with approximately 2,011 sales representatives.*¹²

However, those employee numbers are not at all consistent with what our investigation appears to have uncovered through recorded in-person meetings in China. In fact, our operatives were told that the current employee count in China was considerably higher as the tape reveals:

*We and the staff members working in the plants total 10,000.*¹³

Finally, and perhaps most importantly, as it relates to the issue of whether or not the subject of China is material to a company with 3 billion in sales, is the fact that downlines *outside* of China would not be reflected in segregated sales for China (or Hong Kong and Taiwan, which the Company separates as the Greater China area). Those sales would inflate the revenues of other countries through the placement of Chinese nationals in downlines in regions such as Singapore, Malaysia and the US (just to name a few). This means that the true number of Chinese nationals in downlines *outside* of China

⁸ Please see addendum 4 for sample of publicity.

⁹ Approximately 82% of Herbalife’s net sales for the year ended December 31, 2006 were generated outside the United States; therefore, Herbalife has significant risk associated with its foreign operations. Herbalife has already engaged in acts that have come to the attention of one foreign consumer protection agency. Specifically, Herbalife is a defendant in a lawsuit brought by a Belgian Consumer Protection Organization alleging Herbalife is engaging in pyramid selling. The plaintiffs filed their initial brief on September 27, 2006 and Herbalife filed its reply brief on May 9, 2007.

¹⁰ Please see addendum 5 as a sample announcement of a new China license announced on the news wire.

¹¹ Please see <http://translate.google.com/translate?hl=en&sl=zh-CN&u=http://english.mofcom.gov.cn/aarticle/policyrelease/domesticpolicy/200511/20051100893874.html&sa=X&oi=translate&resnum=2&ct=result&prev=/search%3Fq%3DChina%2527s%2BPublic%2BSecurity%2BMinistry%2BMLM%26hl%3Den%26sa%3DG%26ie%3DUTF-8>.

¹² Please see <http://yahoo.brand.edgar-online.com/fetchFilingFrameset.aspx?dcn=0000950137-07-002811&Type=HTML>, page 25.

¹³ Please see addendum 6. That this does, in the context, refer to China is confirmed (by process of elimination) by the fact that the 10,000 figure could not mean distributors outside of China as they number some 1.5 million, nor could it mean employees outside of China as the company states on page 25 of their 10-K that they have 3,644 employees not counting China. Thus, the 10,000 figure clearly appears to refer to China personnel.

make this a material issue, as the amount of revenue they currently bring to various downlines is clearly significant. The existence of Chinese nationals in downlines outside of restrictive China can be seen with a cursory examination of certain Herbalife distributor websites that blatantly appear to solicit Chinese nationals to join Herbalife *through them!* But for what reason?

In China, the law explicitly states no multi-level marketing is allowed and no products are allowed to flow into or out of China (they must be made and sold there). Also, no revenue or commissions can be paid to those living in China. In other words, China is a closed system - nothing in or out. Even the products sold in China by Herbalife, according to the law, must be manufactured in China, sold at prices comparable to those of similar products, and have a capped retail profit of 30%. Yet despite this, U.S.-based Herbalife distributor Danny Castello's site www.goshape.com states:¹⁴

IF YOU ARE RESIDENT ANYWHERE ELSE IN THE WORLD

I truly am an INTERNATIONAL Herbalife distributor, and I am always searching for people that have some very specific skills (like local language skills: Spanish, Swedish, Dutch, French, Italian, German, Chinese, Japanese etc).

In my own team of distributors, I have people that live in the UK, Ireland, Italy, France, Spain, Mexico, Australia, China, Greece and South Africa.

So, if you are not resident in the US, that's no problem.

I can teach you how to be successfull (sic) in your own local market.

Just drop me an email at admin@goshape.com and I will be happy to show you how you can become an Herbalife distributor and we can start working TOGETHER.

I will send you the exact price of your local distributor kit (for example, if you are from Mexico, it will cost you 650 pesos and it will include 1 Formula 1 shake (flavor vanilla), 1 aloe vera drink and 1 herbal tea (natural flavor).

Don't delay. Start your lifestyle business now and let ME teach you how to work (HARD) but from WHEREVER you want, at the time of the day YOU want.

Danny Castello

Founder and President of GoShape.com

¹⁴ Please see <http://goshape.com/inbupa.html>.

Other distributor website examples exist,¹⁵ but this one raises a specific question. How can Mr. Castello have distributors in China when the law prevents such a model? What possible reason would any Herbalife distributor in the U.S. have for establishing a business relationship with anyone residing in China when there is no financial incentive to do so, based on the Chinese laws that prohibit multi-level marketing and downlines?

Moreover, why would this Herbalife distributor appear to be recruiting people who speak Chinese and live in China? Our investigation appears to answer the question, and that is to illegally recruit and conceal the presence of Chinese nationals in downlines of Herbalife distributors outside of China. Herbalife distributors in China appear to be regularly placed in downlines outside of China which pad sales numbers in markets other than just greater China.

Four foundational points established within this report

First, Herbalife is keenly aware of the potential for the problem of fraud and abuse in the China. On page 32 of their most recent 10-K, they state:

Chinese regulations prevent persons who are not Chinese nationals from engaging in direct selling in China. We cannot guarantee that any of our distributors living outside of China or any of our independent sales representatives or employed sales management personnel in China have not engaged or will not engage in activities that violate our policies in this market, or that violate Chinese law or other applicable law, and therefore result in regulatory action and adverse publicity.

This disclosure does not excuse illegal activity of Herbalife employees in China but merely expresses a concern that if it occurs, the company may suffer negative publicity from it and investors cannot complain because they have been warned that there could be such a problem. However, the problem with this disclosure is seen in the analogy of a factory owner who discloses to potential investors that if the dam upstream breaks, the factory may be washed away and investors would therefore lose their money. That disclosure sounds fine, except if the factory owner *knew* the dam **had already broken** when he made the disclosure it would constitute a material fraud.

In the case of Herbalife, the evidence within this report and upcoming documentary appears to confirm that the company has an intricate knowledge of fraud in the

¹⁵ Please see <http://us-chinabusiness.com/getstarted.htm> and http://www.herbal-team.com/herbalife_chinese.php and note the “We welcome all Chinese speaking customers and will happily assist with your Herbalife order as well as inquiries for our business opportunity here in the USA and in China.” This statement comes from a U.S. resident and confirms the recruitment efforts of Chinese nationals in the U.S.

provinces of China. Their own employees demonstrate that they “knew the dam was broken” when they made the above disclosure.

The company cannot cite the above “we told you it could happen” disclosure as a defense against the wrongdoing in China when the company’s **employees (not just distributors¹⁶) outside of China demonstrate a working knowledge** of the structuring involved in its perpetration.¹⁷ These Herbalife customer service employees (again, employees not just in China) in Singapore and Taiwan appear to demonstrate a working knowledge of how payments to Chinese nationals that exceed the legal limit allowed by Chinese law are made, as well as how Chinese nationals can be placed in countries outside of China without detection. This structured concealment by employees outside of China demonstrates a commonly understood (amongst various employees) method of doing business in various Herbalife international offices.

Second, Herbalife knows the laws of China¹⁸ and the restrictions associated with those laws, as both Chinese regulators and the media in and around China have recently provided fair warning about the potential of fraud and abuse in the region. One such news article is dated October 4th 2007 from the Hong Kong Sun News and titled *“Massive Recruitment during Golden Week Holiday Hong Kong becoming the Headquarter of China’s Multi-Level Marketing Activities.”*¹⁹ The article outlines the massive problem faced by Chinese law enforcement as they seek to keep law-breaking multi-level marketers from circumventing Chinese law through the recruitment of Chinese nationals into various multi-level marketing schemes both from within the country and outside the country in neighboring areas like Hong Kong.²⁰

¹⁶ In the past, Herbalife has maintained a “rogue distributor” or a “law of averages says that with 1.5 million distributors, some violation of company policy is inevitable and outside of our control” defense to evidence that distributors have violated laws.

¹⁷ Taped phone calls from employees in Herbalife offices in Singapore and Taiwan as well as an Herbalife office in Guangzhou. In these calls customer service representatives demonstrated a working knowledge of how Chinese laws were regularly broken by the company.

¹⁸ For the actual laws of China, please see <http://translate.google.com/translate?hl=en&sl=zh-CN&u=http://english.mofcom.gov.cn/article/policyrelease/domesticpolicy/200511/20051100893874.html&sa=X&oi=translate&resnum=2&ct=result&prev=/search%3Fq%3DChina%2527s%2BPublic%2BSecurity%2BMinistry%2BMLM%26hl%3Den%26sa%3DG%26ie%3DUTF-8>. The point being made here is that Herbalife’s public filings confirm a clear understanding of how these laws specifically restrict their activities.

¹⁹ Please see addendum 7 for the actual article from the Hong Kong Sun News. Also, that addendum contains other obvious public news stories that clearly convey the problem of multi-level marketing occurring illegally in China and the government’s commitment to prosecuting offenders who break that law.

²⁰ This point and the accompanying articles are included because of the “China knows and does not care” argument that inevitably arises whenever accusations of impropriety are made in regard to a foreign country. However, in the case of multi-level marketing, the country of China is focused on abuse and actively pursues and prosecutes offenders. Moreover, for a public company in the US to state in their SEC filings that they know Chinese law and then willfully break it or intentionally turn the other cheek through a “don’t ask, don’t tell” approach, is most certainly an unacceptable practice in a post-Sarbanes-Oxley environment.

Also to be considered are the assurances from Herbalife on their official website promising the world that they will comply with the laws of China when they state:

We can clearly see, through the law, that the government attaches importance to the direct selling industry and has made great efforts to regulate the market. We respect the efforts and will conduct our business in accordance with the law.²¹

Based on the above, it would seem that the company should err on the side of having more internal controls in these fraud prone areas, rather than less.

Third, stock analysts²² have placed the very future of the success of the multi-level marketing industry on their ability to secure additional licensing (in the case of Herbalife) and penetrate the market of China with its 1.2 billion people. This rapid Chinese expansion can be seen in Herbalife's most recent 10-Q where they state:

Net sales in China increased by \$11.2 million, or 187.9% and \$18.6 million, or 181.9%, for the three and six months ended June 30, 2007, as compared to the same periods of 2006. Since March of 2005, we have opened 47 stores and 37 service centers in 28 provinces throughout China.²³

The ultimate goal for Herbalife, the largest of the multi-level marketing companies in the U.S., is to eventually have the current restrictive laws of China changed to legalize the retailing of products through multiple levels. Based on the potential growth that they believe will inevitably come from China, investors have relied upon this forward-looking statement when purchasing the company's stock. Any attempt to dismiss China as a small or immaterial market that does not adversely affect Herbalife's \$3 billion in company-wide distributor purchases is not feasible for two reasons.

First, according to page 10 of Herbalife's most recent 10-Q, approximately 80% of sales come from outside the U.S. making any problem in a foreign market material - especially the market that carries with it the most promise for future earnings (China). Secondly, the company by its own admission²⁴ "may" have Chinese nationals residing in China but signed up in other countries as Herbalife distributors attempt to take advantage of the multi-level marketing structure not readily available in China or "employee" distributors in

²¹ Please see <http://www.herbalife.cn/english/newsDetailFollow.action?id=278>

²² Please see http://www.directsellingnews.com/article_app.php?articleid=151 and section "Where is the light at the end of the tunnel?" One analyst put it this way: "The direct selling stock slide and weaker results experienced over the last year go hand in hand. **However, the prospect of China licenses** for additional direct sellers beyond Avon is still the most significant catalyst we see for the direct selling stocks." (emphasis mine)

²³ Please see <http://yahoo.brand.edgar-online.com/fetchFilingFrameset.aspx?dcn=0000950124-07-003991&Type=HTML> page 26.

²⁴ Page 32 2006 10-K.

China promulgating a multi-level marketing plan despite the laws against such activities within the country. Our investigation appears to corroborate that both points are true.

Moreover, since all of Herbalife's income is derived from distributors, how do the outside auditors test Herbalife downlines to determine which contain Chinese nationals who ought not to be there? How do the auditors determine which revenue is being generated through illegal means? It would appear the audit committee and outside auditors cannot rely upon the company's internal controls because this report establishes the existence of a widespread (confirmed by taped calls, in person meetings, and other corroborative evidence) practice of Herbalife employees regularly aiding and abetting the massive conspiracy to illegally recruit and pay commissions in China.

Fourth, employees²⁵ (not just distributors, although we have evidence of both) who have no motive to lie, appear to be knowingly and willingly breaking these laws. Although seldom disciplined, rogue distributors are often blamed for misrepresentations made about Herbalife. In the past, the company has successfully fought off accusations of misrepresentation and fraud due largely in part to their ability to successfully make analogies similar to the following: "With 1.5 million distributors worldwide, few rogue distributors breaking the law in China or anywhere else is really not that bad, when one considers the percentage of the rogue distributors to the vast majority who are not breaking the laws."

However, despite Herbalife's attempt at "preemptive disclosures,"²⁶ our investigation reveals a pattern of behavior prevalent in multiple markets by both distributors and employees. They clearly demonstrate a working knowledge of how this wrongdoing and law violation is carried out. The company could try to dismiss these allegations by saying that an hourly employee in Singapore who confirms fraud in China does not hold a position of authority or speak for on behalf of the company. Yet such statements about fraud from this lower-level employee are even more damaging than if they came from the company's CFO. Why? Because an hourly employee has no stock options and no motive or reason to lie. These lower-level employees state what they know to be the way Herbalife does business in China and conceals Chinese nationals in downlines outside of China. So the fact that they do not necessarily hold positions of prominence lends credibility for, not against, our obtained evidence.

As it relates to the gathering of the evidence, no "cherry picking" was done. That is, the Fraud Discovery Institute did not interview 50 or 100 employees of Herbalife of which a small percentage were "cheating in China" and that percentage found its way into our report. On the contrary, as almost every single phone or in person visit with employees of Herbalife and then their distributors revealed a well known conspiracy to conceal the

²⁵ Please see <http://www.secinfo.com/d11MXs.zrHx.htm> where the company notes "Herbalife Ltd. is filing a copy of its current form of Stock Option Agreement, Non-Employee Director Stock Option Agreement, Stock Option Agreement for Employees in China." Thus, these are employees and if they can earn stock options they can also be held accountable for what they do and say on behalf of the company.

²⁶ These disclosures were addressed through the analogy of the factory owner and the downstream dam.

infiltration of Chinese nationals into Herbalife down lines both outside and inside the country of China.

If...Then

Addendum One is a 24 page report prepared for the Fraud Discovery Institute, Inc. by government-recognized expert on multi-level marketing, Robert Fitzpatrick. Mr. Fitzpatrick has a particular expertise in the implications of multi-level marketing on China, as he was a consultant hired in 2005 by the People's Republic of China to help them analyze whether or not China should allow multi-level marketing in that country.

In November of 2005, China passed a law prohibiting multi-level marketing in that country. Direct selling, where companies like Avon and Tupperware provide point of sales commissions to the person making the sale are allowed in China but the retailing of products through more than a single level is against the law. This is a law that Robert Fitzpatrick helped the Chinese government understand.²⁷ By including these findings which appear to provide more than adequate "cause" for law enforcement in the US and China to take immediate action as an addendum instead of in the body of the report, it should not be viewed as a depreciation of their impact or importance. In fact, the findings constitute motive for the offenses in China and also eliminate the dismissal of the pertinent arguments by apologists for the MLM industry as "old, tired, anti MLM zealots rehashing the same old troubling facts about the entire sales force being in a constant state of collapse because of attrition." On the contrary, the arguments contained in Mr. Fitzpatrick's analysis of Herbalife are devastating and should be viewed as the basis for the motive for the Company's regular abuses of Chinese law.

In this report, Mr. Fitzpatrick proves that 82% of the compensation Herbalife pays to its distributor sales force goes to **less than 1%** of its 1.5 million distributors. This leaves the other 18% of compensation to be divided between the other 1,450,000 distributors. Mr. FitzPatrick notes:

Unknown to most participants, the pyramid design of the plan and the extreme requirement for ongoing investments result in only a small fraction, less than 1% of all distributors, ever being able to gain revenue even minimally. The prime incentive employed by Herbalife is the mirage of the "endless chain". For those in the top three levels of the pyramid, Herbalife pays commissions based on investments from "infinite levels" of the (endless) chain. Herbalife's distribution chain is potentially "endless" since each new recruit is authorized and rewarded to recruit others who can do the same ad infinitum. Millions of new people are

²⁷ One of the saddest things about this industry is that detractors are labeled everything from pathetic losers to anti-MLM zealots, all in an attempt to dismiss their irrefutable findings by giving them an insulting label and dismissing them. To China's credit, they did not do this with Mr. FitzPatrick and used his expertise to develop a law that would protect the people for business opportunity fraud.

thereby lured into the scheme by Herbalife and its promoters that are positioned in the top 1% of the chain. These promoters have advance knowledge that virtually all new recruits are doomed to losses and that nearly every new investor will quit the “opportunity” in less than a year after suffering losses.²⁸

This, of course leads to the distributors, who bring in all of the Herbalife income, quitting at astronomical rates. According to Mr. FitzPatrick,

unless someone understood Herbalife’s actual income data – for example, that there were 1.5 million people in the chain and that each year, perhaps as many as 99% of all who join during one year will quit within that same, and that each year 98.5% of all distributors earn less than \$10.50 a week on average, then the disclaimer note has little meaning. The advisory that “some” of the testimonials come from distributors in the top 1% would mean nothing unless one could understand what it would take and what the odds would be of getting into that tier.

How well do the Supervisors actually do financially compared to that promotional video? According to Herbalife disclosure document 97% would not earn in commission on average even the amount needed to pay for qualifying inventory purchases. The odds of making a profit for those below the Supervisory level are so low they could not be meaningfully charted.²⁹

This is where the “if-then” scenario begins. **If** the above failure and collapse rates are true, and Herbalife is faced with rebuilding a sales force that is in a constant state of collapse, **then** the only solution to sustaining the current distributor sales force of 1.5 million people involves two things. First, the company must crank up the deception machine in countries like the U.S. This includes sales of “lead generation” to distributors, in which the distributors are able to purchase lists of names of people who are said to be “ready to sign up under your down line,” as well as sales of advertisements on the internet promising “work from home and earn big dollars.”³⁰

Secondly, Herbalife must find a pool of *potential* distributors who, in general, have not yet fallen prey to other doomed by design, multi-level marketing plans. China solves all kinds of problems for Herbalife because it has over one billion people who have little or

²⁸ Please see addendum 1 pages 1 and 10 where Mr. FitzPatrick actually states the figure is more like 84% of the compensation goes to less than one percent of the Herbalife distributors.

²⁹ Ibid page 10.

³⁰ ***Doomed by Design*** will contain eye witness testimony from several U.S.-based Herbalife distributors who will confirm the lead generation sales pressure placed on them by their upline. In one instance, a distributor spent close to \$4,000 per month just buying leads that supposedly contained future downline members for their businesses.

no experience with multi-level marketing and seems to have little regulation or enforcement of certain business opportunities.³¹

What is being stated is that every “crime” has a motive. **If** the above “doomed by design” endless chain business model does, in fact, churn distributors at an annual rate exceeding 90%, **then** Herbalife must tap into China’s resources - at any cost. This report appears to show that the reason for the fraud and abuse by Herbalife in downlines outside of China and multi-level marketing occurring within China is out of necessity. In order for Herbalife to draw even every year, the recruitment task of this company is not just an uphill climb; it is like scaling Mount Everest in tennis shoes.

Don’t focus on China enforcement, but follow the money instead

Views vary on what China may or may not do with violators of their laws against multi-level marketing,³² but endangering public company investors with illegal activities designed to inflate sales (and reward actors with performance-based compensation like stock options) is actionable under Sarbanes-Oxley in the U.S. To illustrate how serious this is, we can examine the stock activity of the company and insiders. In 2007 alone, Herbalife repurchased 3,233,900 shares in May and 266,100 in June of 2007, for a total of about 3.5 million shares at approximately \$138.8 million.³³ During the same time period in 2007, insiders of the company sold over \$115 million of stock on the open market.³⁴ Obviously, the insiders receive a better price for those shares if earnings and the promise of future earnings (China) are substantive. Therein lies another motive for concealing problems in China and problems with Chinese nationals in downlines outside of China.

The U.S. cannot be viewed as a safe haven for companies that aid and abet Chinese nationals to commit crimes against other Chinese nationals with a “doomed by design” and a multi-level marketing business model rightfully banned in that country. The cost of being a public company in the U.S. is being held accountable by the SEC for required filings relied upon by investors. In this instance, those SEC filings clearly illustrate knowledge of the laws in China. The Company then apparently promptly breaks those laws and hedges against future negative consequences by disclosing in advance a defense of “it may happen and I didn’t do it.”

Finally, in the case of Usana Health Sciences, Inc (please see www.cheatinginchina.com) that company had no license to conduct any kind of business

³¹ However, our investigation proves that China, for whatever reason, has been very zealous at enforcing its laws against multi-level marketing.

³² Recent articles from the regions of China and Hong Kong appear to reveal that the Chinese authorities are interested in prosecuting violators of their strict, multi-level marketing laws.

³³ Source: Insider Cow 9/04/2007.

³⁴ Ibid.

in China but since Herbalife does have the licensing to direct sell in the country, by violating those laws they are also violating a position of trust granted to them by the government. That is, they have various “salespeople” licensed in that country who know first hand what is not allowed and yet they appear to it anyway and in so doing violate a position of trust.

The obtained evidence reveals three things about Herbalife

Issue One

Company says sales fell in certain areas because of focus on China

On page 55 of the company’s most recent 10-K, Herbalife indicates:

...net sales in Taiwan decreased \$3.6 million, or 4.0%, for the year ended December 31, 2006, as compared to 2005...The decrease in net sales was primarily attributable to the loss of focus of local distributor leadership and some of their key members. In 2006, their attention was primarily directed towards the opening of Malaysia and the emerging business opportunity in China.

A similar statement about Hong Kong states:

Net sales in Hong Kong decreased \$4.8 million, or 28.8%, for the year ended December 31, 2006, as compared to 2005. The decline in net sales was primarily the result of a loss of momentum, attributable to the focus on the emerging opportunity in China, resulting in a decrease in supervisors, down 24.4% at December 31, 2006, as compared to December 31, 2005.

The problem here is the reason given for the decline in sales in Taiwan and Hong Kong. Apparently those who reside in Taiwan or Hong Kong have shifted their focus to China, or, in the case of Taiwan, Malaysia, so that they can build their multi-level marketing businesses in these areas instead of at home. However, it has already been clearly established that this type of business-building through downlines is strictly prohibited by Chinese law. Still, Herbalife’s own prospectus accounts for a drop in sales in the regions of Hong Kong and Taiwan so that residents of those countries can build downlines in the closed system of China.

It appears the Company is basically saying that business is down in Hong Kong and Taiwan where they are freely allowed to use a multi-level marketing approach in favor of doing business in the more restrictive, closed system in China. Why would they focus on doing business in China, where they cannot receive commissions?

What possible explanation can be given for the above? The intention is to set investors’ minds at ease and explain away sales decreases in two major markets. How is that done? By citing “greener pastures” in Malaysia (understandable), and China (without

qualification)? Why is that done when China and Malaysia aren't really even comparable due to differences in laws?

Herbalife appears to be explaining this apparent contradiction by with a "pre launch" method of doing business, which is the saturation of a market before its official opening. This is untenable because Herbalife has been in China for years and the Chinese laws against multi-level marketing are relatively new (November of 2005). To say that this activity in China (instead of Taiwan or Hong Kong) is being generated in advance of the inevitable opening of China when multi-level marketing is legalized³⁵ is also a pipedream.

Regarding the above, blatant justification for fallen sales in Taiwan and Hong Kong because of a distributor preoccupation of building a business in China, expert Robert Fitzpatrick notes:

In its "Terms of Use" web page (http://www.herbalife.com/global/terms_of_use.jsp), which serves as its agreement with distributors, Herbalife states:

3. ELIGIBILITY

You represent and warrant that you are at least 18 years old. Herbalife products and the Herbalife business opportunity cannot be offered, shipped into or sold in any country outside of those countries that are previously authorized by Herbalife. For a list of such countries, please click here: [Authorized Countries](#). Herbalife is expanding its sales into other markets, accordingly please check for updates periodically.

The link to the "authorized countries" (http://www.herbalife.com/global/about-herbalife/hl_worldwide.jsp?requestid=2578) includes China in the list.

However, Herbalife's 2006 10K states:

To become a distributor, a person must be sponsored by an existing distributor, except in China where no sponsorship is allowed, and must purchase an International Business Pack from us, except in South Korea, where there is no charge for a distributor kit.

In its 10-Q for the 2nd quarter of this year, Herbalife states,

³⁵ For years the multi level marketing industry has insinuated that the WTO will eventually pressure China into the legalization of multi-level marketing in China. This is unlikely considering how long and hard China thought about and researched their very recent decision to ban multi-level marketing in that country. Although I am most certainly not an expert on the Chinese culture, they do appear to be a proud people and definitive decision makers who seldom retract recent rulings they spent years on formulating.

Chinese regulations prevent persons who are not Chinese nationals from engaging in direct selling in China. We cannot guarantee that any of our distributors living outside of China or any of our independent sales representatives or employed sales management personnel in China have not engaged or will not engage in activities that violate our policies in this market, or that violate Chinese law or other applicable law, and therefore result in regulatory action and adverse publicity.

Even if a HK or Taiwanese distributor could recruit a Chinese distributor, it would not be very useful, since the Chinese distributor cannot recruit further. The only benefit would be volume from retail sales --- assuming the rules are followed. As we know, it is largely a waste of a distributor's time to retail or to recruit a retailer.

If, however, the rules were violated and one Chinese national could recruit another, the opportunity would be huge, given the market's size. I suspect that is what is happening.

Attorney Douglas Brooks, who is currently suing Herbalife on behalf of a class of victimized distributors, states this about the aforementioned:

The question I have is -- what benefit does "local [Taiwan or Hong Kong] distributor leadership" expect to gain from "the emerging business opportunity in China." Taiwan or Hong Kong distributors are not going to focus on China unless they can earn something by doing so. I can think of three ways: (1) selling products to Chinese distributors; (2) recruiting Chinese distributors and earning commissions and bonuses based on their sales; or (3) personally going to China and becoming a distributor there. Based on my (limited) understanding of Chinese law, (1) and (2) are illegal, while (3) seems unlikely. What is more likely is that, as your investigation suggests, Taiwanese and Hong Kong distributors have developed various means to evade Chinese legal restrictions against multi-level marketing and selling. The quoted statements which you forwarded leave no doubt that company executives are aware that their Hong Kong and Taiwanese distributors are "doing something" in China, despite the fact that there does not seem to be any legal way for them to benefit from this activity. At the very least, Herbalife has a duty to investigate. Is there is a legal way for non-Chinese distributors to benefit from doing business in China? If there is, then the quoted disclosures may be innocuous. If not, they demonstrate (at the very least) that Herbalife has knowledge of malfeasance by its Hong Kong and Taiwanese "leadership" level distributors.

That these Hong Kong distributors are focusing on China to conduct multi level marketing can be seen from one Hong Kong based Herbalife distributor's website that openly asks prospective distributors:

Who do you know that lives in these countries?

Argentina, Australia, Austria, Belgium, Botswana, Brazil, Canada, Chile, China, Costa Rica, Cyprus, Czech Republic, Denmark, Dominican Republic, Eire, Finland, France, Germany, Greece, Hong Kong, Hungary, Iceland, India, Indonesia, Ireland, Israel, Italy, Japan, Jamaica, Korea, Lesotho, Malaysia, Mexico, Namibia, Netherlands, New Zealand, Norway, Panama, Philippines, Poland, Portugal, Puerto Rico, Romania, Russia, Singapore, Slovak Republic, South Africa, Spain, Sweden, Swaziland, Switzerland, Taiwan, Thailand, Turkey, United Kingdom, United States, Venezuela.³⁶

What is most interesting is what is not present on this website - specifically a distinction of appeals from China and every other country listed. The apparent context of the appeal (similar to the explanation given by the company in SEC filings placing China and Malaysia together without distinction) is for potential distributors who know people in any of these countries (including China) who may help build their downlines. Remember, this website is posted by a current Herbalife distributor based in Hong Kong, and the laws strictly prohibit outsiders from Hong Kong or anywhere to engage in multi-level marketing sales and recruiting activities in China.

Other evidence secured through taped phone calls confirms the clear intention to recruit Chinese nationals into downlines when, during one call, the Herbalife distributor instructed our operative to not “...mention the policy of HK (Hong Kong) Herbalife in China. Coz it's not allowed.”³⁷ When a return call was made to the same Hong Kong based distributor, our operative was once again reminded to “...remember don't tell anybody about your HK Herbalife plans or rules, otherwise somebody will accuse you.”

Issue Two³⁸

Evidence of widespread abuse of Chinese laws with international consequences

To highlight some of the evidence of this massive external and internal infiltration of China, we have assembled portions of evidence obtained during meetings, phone calls, emails and other legal means. This paints a clear picture of what is understood as the way Herbalife conducts business in and through China. Although not an exhaustive list of the alleged violations of Chinese and US laws, the below excerpts do make for a compelling, cumulative case.

It is important to note that all persons involved in the meeting in China were Chinese nationals living in China. The potential prospect is presented with the Herbalife international pay plan, multi-level structure based on recruiting, downline purchase volume requirements, and income projections based on rising to top “levels.” Yet this prospect lives and works in China.

³⁶ <http://www.feelgoodnutrition.biz/work-from-home-business-opportunity-start-Hong-Kong.htm>.

³⁷ Please see addendum 3, taped phone calls of various Herbalife employees and distributors.

³⁸ It should be stated that when the documentary airs, additional evidence will be revealed.

What Herbalife says to the Public about China

Herbalife's Limited Legal Authority To Conduct Business is summarized in a press release from the company dated July 9th, 2007:

Herbalife Receives Additional Access in China

LOS ANGELES--(BUSINESS WIRE)--July 9, 2007--Herbalife Ltd. (NYSE:HLF), a global nutrition direct-selling company, announced today that it has received a direct-selling license from China's Ministry of Commerce to conduct business throughout the entire Jiangsu province. In March 2007, the company received permission to conduct business in just two cities, Suzhou and Nanjing.

Located on China's east coast, the Jiangsu province, consisting of 13 cities with 61 counties, has a permanent and transient population of approximately 85 to 90 million people. Cities approved are Nanjing, Suzhou, Xuzhou, Lianyungang, Suqian, Huan'an, Yancheng, Yangzhou, Taizhou, Nantong, Zhenjiang, Changzhou, and Wuxi.

Herbalife currently operates 47 stores and 37 service centers in 28 provinces in China. The company operates a unique direct-selling model in China in accordance with local regulations, where our supervisor-level distributors are employed by, and conduct their business, in retail locations owned by Herbalife China. Consumers and other distributors come into the store to buy product and learn more about the business opportunity. In areas where the company is licensed, distributors will be allowed to conduct business outside of the store.³⁹

How Herbalife *really* does business in China⁴⁰

China's law prohibits any entity from enrolling any Chinese national into a business venture or program wherein they are compensated [for participation in the Company's business] by and through a multi-level compensation system or program. Under China law, a multi-level compensation system or program is one that provides for the payment of monies to multiple individuals as the result of a purchase made by a distributor, agent or employee of the Company.

The fact that Herbalife has been granted licenses as presented above, does not exempt the company from conducting business in accordance with all applicable China law; including without limitation, China's law that prohibits Herbalife from enrolling any Chinese national into its multi-level compensation program. In fact, that China draws a

³⁹ For entire release please see addendum 9. Please also note that the phrase "outside the store" does not mean that multi-level marketing can be done "outside a retail store in China" but merely a door-to-door, single level retailing.

⁴⁰ The statement "in China" does not limit the problem to just China as previously indicated in the report.

distinction between legal direct selling within the country and illegal multi-level marketing can be seen by their recent law enforcement “stings” where enforcement was made on abusers of this law.⁴¹

In light of the above, the below comments are very troubling.⁴² The first quote is from a meeting in China. Our operative is a Chinese national and the husband and wife team are employees of Herbalife and carry the title “Mendy Xi Business Manager License Number: 24112151.”⁴³

The transcript of the meeting⁴⁴ appears to corroborate the belief that Herbalife allows Chinese nationals to join the multi-level compensation program in direct violation of China law. Although we found numerous admissions that support these beliefs, only a handful are presented to avoid redundancy. To make it easy to follow the abbreviations used for the names in the transcripts, they are listed as:

- A : Xiao Tang’s boyfriend (our operative)
- M : Mandy (female) is the wife of Peter (Herbalife employee in China)
- B : Peter (male Herbalife Employee in China)
- C : Xiao Tang (female our operative)
- Z : Sister Jane (female associate of Peter and Mandy)

First quote page 9 of the transcript:

A : It’s impossible.

B : You should look at risks and you should have a unique point of view. To view it from a different angle. No company will make money if they perform business in accordance with the Chinese laws.

Explanation: No truer words were ever said. This is why the Company’s explanation about Taiwan and Hong Kong defies logic. Doing business in China as a multi-level marketing company cannot be nearly as profitable (by their own admission) as it could be if they were allowed by law to multi-level market. They cannot so they obtain licenses

⁴¹ Please see addendum 7 article of recent arrests made in China for pyramid scheme payment posing as multi-level marketing.

⁴² Please see addendums 3 and 6 where all of the recorded, in-person meetings cited in this section and the phone calls are included. For unabridged versions of the employee and distributor calls (not to be confused with the unabridged, in-person meeting), please see our website www.doomedbydesign.com.

⁴³ The salesperson for a direct selling company must have a salesperson certificate. To obtain the certificate, the salesperson must take and pass a national test prepared and administered by the government (as quoted by).

⁴⁴ Please see addendum 8 which is the English translation of the business card of the Herbalife employee. To see the actual business card front and back please see the last addendum.

that allow them into the country, promise they will be good and obey the laws, and in all of the meetings we went to in China, they encouraged law breaking and sold prospective distributors a multi-level marketing structure.

A : That is to say, all PV is reduced to zero before being promoted to the position of director?

B : Right. That's it. The lowest level is the business representative.

A : Unless you are promoted to the position of business director.

M : Generally speaking, the director is also eligible to obtain 5% management bonus of three generations apart from 30% profits.

Explanation: The plan of 5% paid on three levels of supervisors, quoted here, is the exact same pay plan Herbalife uses around the world.

A : That is to say that even you have been promoted to the position of director, you are still required to gain 2500 points of PV, the primary requirement for the business representative, right?

M : Right. It is approximately RMB30,000. This point is not the point done by you alone, rather it is done by you and the business representatives below you.

Explanation: This is a critical confirmation of the "group volume," proving that Herbalife is using multi-level marketing downlines.

B : The persons recruited by you?

A : Yes. The person recruited by me. That is to say that I recruited three of you. If the points gained by three of you total 2500 points, full points have been gained. Then I do not need to contribute any points.

M : Yes.

B : Yes, provided that three of us are all business representatives.

Explanation: This shows that recruiting is being done. Volume alone does not result in payment. The people producing the volume must be salespeople, so recruiting is required.

B: Wrong, Wrong, Wrong. I feel that Herbalife is special in one aspect. Each one wants to sell goods and he should know how to sell goods. It is crucial. Even if you have been promoted to the position of president, you have to have the record of retail in order to obtain bonus each month.

Explanation: There is a sudden assertion of retail sales requirements. Previously there was no mention of retail, just Volume Points and potential income.

A : Actually if he is promoted to the position of president and the business achievement is supported by the team, he does not need performing retail.

B : Yes. Yes.

Explanation: There is a sudden assertion of retail sales requirements. Previously there was no mention of retail, just Volume Points and potential income.

Affirmation that retailing is not necessary, just volume of the “team”

A : In fact in theory retail is required, but in reality if he is promoted to that level, he does not need performing retail.

B : But the junior manager of ours is required to make this business achievement each month. Each month. You are required to make the business achievement of RMB30,000 absolutely.

Explanation: This is the equivalent of \$4,000 to qualify, which is the same multi-level compensation plan used in the US.

The transcript contains further corroboration that this multi-level structure is exactly what is being promulgated in China. Moreover, similar results of the “*promotion through volume points in Herbalife’s Chinese business opportunity and not management skill*” were duplicated from another, videotaped meeting in China at an official Herbalife location. To avoid redundancy, we had the meeting translated from Mandarin to English and then summarized and analyzed.⁴⁵

Meeting at Herbalife China One location was One layer No.4# Building, Weipeng Garden, Zhenzhong Road, Futain District, SZ

This audio records the conversation among three gentlemen. One is a business representative, who introduces his business products, operation, and structure to the other two gentlemen. He tells them the company was started in 1980. The company’s stock was offered on New York Stock Exchange in December 2004 with its current value at \$46 per share. The company has over 90 stores in China and two stores in every province. The company has two stores in Guangzhou, two stores in Wuhan, one store in Chengdu.

The company sells health-related products and has its own factory. The investor of one of the products is David Haibo (translated phonetically), who won Nobel Prize in 1998. The company sells products that can prevent heart problems,

⁴⁵ Since this entire meeting is on videotape, a summarization was not a problem as the evidence of multi-level marketing is undeniable and widespread. The entire meeting will be posted on www.doomedbydesign.com shortly. The complete transcript from Mandarin to English will be forwarded to law enforcement in China and the U.S.

hypertension, diabetes, cancer, hypotension, anemia and also products used for weight loss, weight gain, and facial care. The products are safe and made from plants. The products are certified by the Ministry of Commerce of China. Everyone can use their products, including the elderly, children, and pregnant women.

A person who wants to join the company is required to have an ID, full-time working card from his/her factory, personal account, and 100 yuan to buy the company information material. After the person fills the application, the company issues a certificate to the applicant, who then becomes the company's business representative. The company is structured on a multilevel basis. The entry level is a business representative, followed by business director, senior director, manager, senior manager, and executive. There are 8 executives, 40 senior managers, over 100 managers in China. A senior director is required to have 10,000 points. A manager is required to have a total sale of 200,000 yuan for three consecutive months. A senior manager is required to have a total sale of 800,000 yuan for three consecutive months. An executive is required to have a total sale of 2 million yuan.

After analyzing the transcript, Robert FitzPatrick corroborates and explains that this is, in fact, a pitch for multi-level marketing:⁴⁶

The commentary appears to describe a classic multi-tiered business model but it does not offer enough detail to say definitively that this person is describing Herbalife's "international" pay plan.

Herbalife's Chinese (in English) website,⁴⁷ under "business opportunity" shows an escalating commission schedule. It does not offer names of the levels associated with commission rates.

The narrative describing the levels does not state that commissions are paid to upper levels from the purchases of lower levels, which would be illegal. It also does not state that each level can recruit other levels and be paid a portion of their investment.

However, the yuan requirements would only be possible if "downline" volumes are being counted. I think 7.5 yuans equal a dollar. So a senior manager would need a volume of more than \$100,000, hardly a one-person retail sales figure. Moreover, it says the person must maintain this level for three months running. The executive needs \$267,000 (2 million yuans) a month in revenue! The narrative says there are 8 of these "executives" in China > 8 executives x \$267,000 revenue per month x 12 Months = \$25.6 million. According to the 10-Q, China revenue in the first six months was \$28.8 million.

⁴⁶ Please see addendum 2 for translation summary of video.

⁴⁷ Please see <http://www.herbalife.cn/english/careerFollow.action?query.type=1>

The 2 million yuan a month requirement for the "executive" is the minimum required. So these figures might correlate. In any event, clearly these "levels" are based on downline volume, not management promotion, as in a normal corporation. Volume has to be tied to recruiting.

So, in summary, it is a multi-tiered program based on recruiting. Rising on the ladder is tied not to management skills but purely on volume production. This level of production can only be developed from recruiting. Hence payments is tied to recruiting.

Finally, there are the various Herbalife employees and certain distributors who confirm the widespread nature of Chinese nationals in downlines inside and outside of China. One of the most specific statements comes from Ms. Hon, an employee in the Taiwan office of Herbalife. Her statement was made during a recorded conversation, and she gave specific details that could not be dismissed as a "mistake" because of the structuring.⁴⁸

C: Ok, if I join Herbalife in Taiwan, but my down line is from HK & China, is it ok?

H: Yes.

C: How can I get the commission?

H: If you are taking HK ID, then our office in HK will transfer money to your bank account directly.

In Taiwan area, we all pay in US dollar.

C: um

H: If you earn money out of Hong Kong area, then you will get US.

C: They will bank in to my Hong Kong bank account?

H: Yes.

C: Is it possible to bank in to Taiwan bank account?

H: First, you have to provide Taiwan address and you have to pay tax if bank into your Taiwan bank account.

⁴⁸ The conversation took place October 5th, 2007.

C: I see. How about my friends in China?

H: Our China office will send them money. Not from Taiwan.

The question was how would someone living in Taiwan could be an Herbalife distributor with downline members in Hong Kong and China. The answer was first, yes that is a tenable business model (although illegal). When pressed about commissions paid to potential downline members in China, the employee stated the “China office will send them money. Not from Taiwan.”

A similar result occurred when we called Zen at the Herbalife office in Singapore⁴⁹ During the interchange with Herbalife employee “Zen,” our operative asked:

I also want to ask, some of my friends who is living in China. They can be my down line after I join?

The Herbalife representative first responds with:

For China, they can only do the business in China, join in China, cannot make purchasing in other countries.

The Chinese national asks a follow-up question:

So they can be my down line?

The Herbalife representative states:

They can still be your down line.

The Chinese national prospect then asks the obvious question:

How about my friend in China? How to get the commission?

The Herbalife representative responds:

They will get the check from China office.

But such activities are not allowed in China. A China resident is not permitted to be in a Singapore downline and receive a commission payment from Herbalife.

Yet another recorded conversation with an Herbalife distributor based in Hong Kong revealed that there is even a specified bank from which Chinese payments originate:

⁴⁹ The call took place on October 8th, 2007.

C: How about my friend in China? (our operative asked).

M: They must to open an account in ICBC, the only bank that we accept.⁵⁰

More audio and video footage with similar admissions has been secured and will be seen in the “Doomed by Design” documentary. The examples here are provided as an offer of proof of a widespread violation of Chinese law by Herbalife. These examples show that this violation of law is commonly understood by both employees and distributors inside and outside of China.

Issue Three

Two contradictory disclosures about the same event at the same time

A funny thing appears to have happened to Herbalife on the way to the SEC in November of 2006. Herbalife filed a late form 10-Q in 2006, but the reason for that late filing seems to have changed between Thursday night and Monday morning:

Filing date 11/13/2006, sent Thursday November 9th, 2006

PART III — NARRATIVE

State below in reasonable detail why Forms 10-K, 20-F, 11-K, 10-Q, 10-D, N-SAR, N-CSR, or the transition report or portion thereof, could not be filed within the prescribed time period.

Herbalife Ltd. (the “Company”) hereby requests an extension of time to file its Quarterly Report on Form 10-Q for the period ended September 30, 2006 (the “Form 10-Q”). Despite diligent efforts, the Company was unable to file the Form 10-Q by November 9, 2006, without unreasonable effort or expense, primarily because the Company was unable to finalize review procedures which are necessary to complete the Company’s financial reporting requirements for the fiscal quarter ended September 30, 2006. The Company currently expects that it will be able to conclude the remaining work necessary to complete the review procedures in time for the Company to file the Form 10-Q within the five calendar day extension provided by Rule 12b-25.

Filing date 11/13/2006, sent Monday November 13th, 2006

From time to time, the results of these internal audits may necessitate that we conduct further investigations into aspects of our business or operations. At the time of the filing of this Quarterly Report on Form 10-Q, one such investigation was pending. This investigation concerns certain activities related to one of our foreign subsidiaries and related matters, and may involve violations of applicable law. The then pending review of this investigation necessitated our filing of a

⁵⁰ Please see addendum 3 conversation 1 with Hong Kong Herbalife distributor recorded. There were two parts and this quote is from part one.

request for extension on Form 12b-25 with the Securities and Exchange Commission. While we currently believe the likelihood is remote that the results of this investigation will have a material adverse effect on our financial condition or results of operations, no such assurances can be given at this time. In addition, our business practices and operations may periodically be investigated by one or more of the many governmental authorities with jurisdiction over our worldwide operations. In the event that these investigations produce unfavorable results, we may be subjected to fines, penalties or loss of licenses or permits needed to operate in certain jurisdictions, any one of which could have a material adverse effect on our financial condition or results of operations.

Our investigation appears to have found that the foreign subsidiary referenced in the second filing above is the country of China.⁵¹ Two questions emerge. First, why are there two separate explanations for the same event? Second, why does the earlier filing cite the reason for delay as only an inability to “finalized review procedures,” while the next filing only a few days later cites a more serious-sounding investigation into a foreign subsidiary and potential violations of law?

Of course, since the first disclosure was the weaker of the two (by far), it would appear that that someone questioned the adequacy of the disclosure. If management made an incomplete disclosure in this instance, it raises the issue of what else might not be disclosed by senior management.

If this disclosure does indeed deal with China, it calls into question how dependent Herbalife really is on their presence in China. That is, if the company has more Chinese nationals, either by illegally engaging in multi-level marketing in China or by putting Chinese nationals in downlines outside of China, even more revenue is at risk and the company is in greater jeopardy than the average investor could know.

Conclusion

The information in this report does not constitute everything there is to know about Herbalife and the company’s presence in China. However, it is everything that both the Chinese and U.S. government officials need to know to investigate the claims contained in this report.

To confirm our findings and eliminate the “that is just your opinion” rebuttal or the “even if you are right, China is a small percentage of our sales” rebuttal, we are providing

⁵¹ Although China appears to be the country of the aforementioned subsidiary, it does not necessarily mean that the investigation is directly related to Herbalife’s concealment of a multi-level marketing compensation plan in a country where such a plan is not allowed. In fact, a later filing indicated that this problem was resolved. For our purposes the issue is the two contradictory disclosures made within days of one another and that if they dealt with China they would be material based on evidence of undisclosed distributors provided in this report.

corroborative evidence. This evidence includes videotaped meetings in China, taped phone calls of employees both inside and outside of China, distributor that seek to recruit Chinese nationals, and other interview evidence. Together this evidence makes a cumulative case against Herbalife. If there is still doubt, please answer the following question. What are the odds?

What are the odds of multiple Herbalife employees from different countries and multiple Herbalife distributors from different countries and multiple Herbalife distributor websites from different countries all saying the exact same thing about an understood practice within the Company pertaining to how Chinese nationals are illegally recruited outside of China and how multi-level marketing, not direct selling, is the common practice within China? Did we just get lucky at finding the needle in the hay stack every time and every where we looked or did we find the evidence contained in this report because that is the common practice of how Herbalife normally and regularly does business? The odds are a million to one that we just happened to find fraud wherever we looked. The truth is we found fraud because it is the common practice that occurs daily all over the world.

The company may boast of sales exceeding \$3 billion, but our contention is that their sales are materially tainted by the illegal involvement of a pool of people who are banned from participating in multi-level marketing. This illegal involvement is necessary for a company whose doomed by design business model saturates markets and leaves them no other choice than the 1.1 billion "people" prize of China.

Respectfully Submitted,

Barry Minkow
Co-Founder
Fraud Discovery Institute
San Diego, California
www.frauddiscovery.net

Reviewed and Supervised by:

Juan Lopez
Licensed Private Investigator
CA PI License # 24817

cc: Mr. Peter Delgreco
Securities and Exchange Commission
5670 Wilshire Blvd 11th Floor
Los Angeles, California 90036-3648



info@frauddiscovery.net

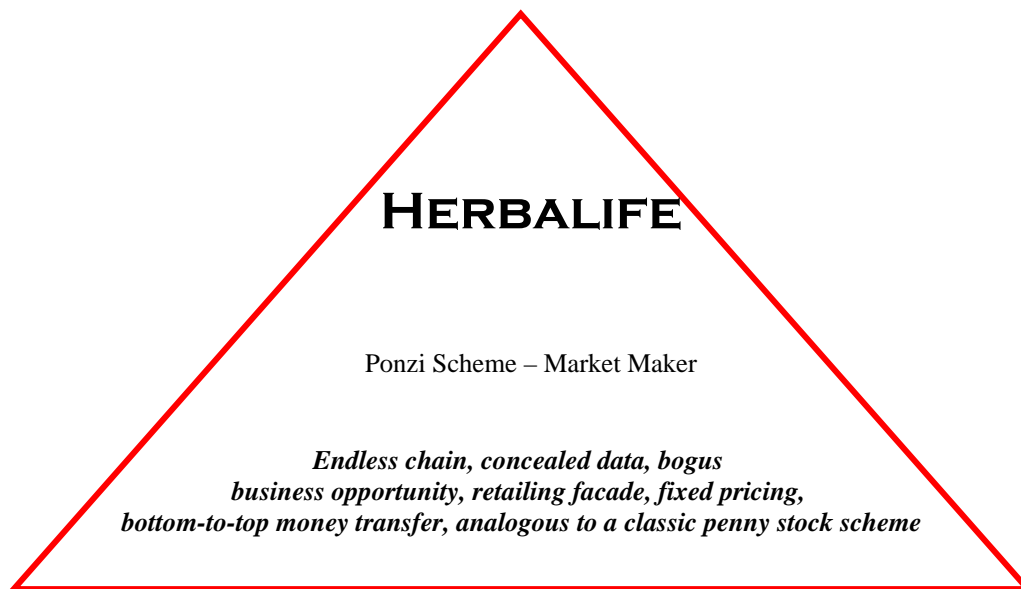
Phone & Fax:
1-888-300-8307

Special Agent Peter Norell
Federal Bureau of Investigations
901 West Civic Center Drive, Suite 300
Santa Ana, CA 92679

Special Agent Matt Galioto
Federal Bureau of Investigations
135 Pinelawn Road, Suite 350
South Melville, NY 11747

Addendums⁵²

Addendum One



by Robert L. FitzPatrick .
1800 Camden Rd. Ste. 107, #101
Charlotte, NC 28203
RFitzPatrick@PyramidSchemeAlert.org
<http://www.PyramidSchemeAlert.org>

⁵² Whenever seen, emphasis mine.

Date: September 28, 2007
To: Barry Minkow, Fraud Discovery Institute
From: Robert L. FitzPatrick
Re: Analysis of Herbalife Business Model and Business Practices

To prepare this analysis for Fraud Discovery Institute I studied the Herbalife 10K filings from 2004-2006 and the Herbalife website, including related links that are password protected and available only to qualified prospects. I reviewed various confidential letters that I have received over several years from consumers reporting their Herbalife experiences. I carefully read a current class action lawsuit brought by distributors (Minton vs. Herbalife and the Freedom Group). I reviewed various documents available on the Internet from other consumers, such as chat rooms and discussion threads. I conducted in-depth interviews with current- and ex-Herbalife distributors regarding the details of the marketing plan and their direct experience. As an overview, I characterize Herbalife as an international pyramid scheme that is duping millions of people into buying its products based on the deceptive lure of an endless chain reward system. Not only are huge numbers of individual consumers tricked out of thousands of dollars but many are cheated out of unrecoverable time and effort pursuing the untenable business proposition that has been disguised as a “home based business” or “direct selling.” The total number of people and the full amount of dollars that are lost due to Herbalife’s calculated program of deception are astonishing. They far exceed a million people each year and reach into 64 countries worldwide.

Plotted over a five-year period, the rate of all consumers that have participated and lost money exceeds 99%. Of those recruited each new year, their loss rates as a group approach the same figure. By Herbalife’s own data in the 2006 10K, over 80% of the entire sales channel is classified as failing to “re-qualify” or “turned over” each year, euphemisms for failed and quit. The average “incomes” of the others – when weighted by level on the sales chain – show that almost none earned enough to recover their investments in the “business opportunity.”

A tiny group of promoters in the top three ranks of the chain that carries out the deceptive recruitment system gains extravagantly from these large-scale consumer losses. This is accomplished through Herbalife’s complex pay plan. Commissions paid to the sales channel by Herbalife amount to 36% of Herbalife’s net revenue. Of all that money, 84% is transferred to less than one percent (.76) of the entire distribution channel, the group positioned each year at the top of the pyramid.

Herbalife’s business, therefore, and the value of its stock, rely entirely upon recruiting more than one million consumers who are doomed-by-design to financial loss. The business has no sustainable customer base or sales force. It essentially collapses each year but is sustained through its deceptive recruitment program that rebuilds its infrastructure and revenue base. The losses to consumers are inevitable, well designed and pre-determined, based on the multi-tiered structure of the plan, its practice of gaining a large front-end investment, its recruiting and purchase requirements on new recruits, and its top-loaded reward system.

While the “overrides” and “royalties” are concentrated into the hands of less than 1%, the other supposed income source for distributors – retail profit – is largely non-existent. Herbalife’s SEC filings and its promotional literature offer an elaborate pretense that nearly a billion dollars is “earned” by the 1.5 million person sales organization from retail sales. Abundant evidence shows that this sales activity does not and could not occur. While claiming to be a direct selling company, Herbalife maintains no records and carries out no system to monitor retail sales. Its pay plan is based entirely upon the purchases of the distributors, not their retail sales to end-users. The business model is based upon recruiting and expanding the sales channel, not carrying out retail selling. The investments of the distributors into a bogus “business opportunity” are falsely portrayed as Herbalife’s “sales.”

The lack of a retail sales base represents the most extensive area of deception. It also constitutes the clearest evidence that Herbalife is in violation of federal laws regarding the operation of a pyramid scheme. When the test used by the FTC regarding required levels of retail sales is applied, it shows that Herbalife’s distributors would have to retail 70% of all the inventory purchased from the company. The actual rate of retailing would not come close to this required level.

In my view, therefore, if Herbalife is investigated by the Federal Trade Commission or the SEC and criteria are applied that have been used in many previous prosecutions of similar multi-level marketing companies, Herbalife would be found in gross violation of the FTC Act, Section 5, covering “unfair and deceptive trade practices.”

The most fundamental fact that Herbalife conceals from shareholders and consumers – the fact that reveals the true nature of the business, rather than the false one of “direct selling – is that the company’s “revenue” consists of the *capital* lost by these home-based business investors. The company does not generate sales revenue as generally understood since fair value is not exchanged. The consumers invest in a grossly misrepresented business opportunity – which is Herbalife’s actual product, not weight loss pills – and Herbalife gains its money without delivering on its offer, claims or promises for an income opportunity. The failure rates are nearly total, making the term “opportunity” a sham.

Herbalife’s sales of “pills, potions and lotions”, the standard offering of many other multi-level marketing schemes, is only incidental to the sale of the false business opportunity. In this respect, Herbalife is closely analogous to a “pump and dump” scheme of penny stock promoters that solicits investments in an essentially worthless or virtually non-existent company whose stock, the promoters say, is poised to dramatically increase.

Year after year, Herbalife solicits consumers to invest in a non-existent or virtually worthless business – retail-based “direct selling” of Herbalife products. The value of the Herbalife distributorship, like the penny stock, is based upon drawing in new investors whose capital investments are transferred to the earlier ones. The pyramid recruiting is orchestrated by Herbalife’s “upline” like a “boiler room” phoning consumers about a “hot” new stock that is “going to be big.” The Herbalife Upline, like the Boiler Room, makes its money on the “spread” between the manipulated transactions of buying and selling at fixed prices.

The equity value of the Insiders of the stock scheme coincides with that of Herbalife's top shareholders and executives whose worth is actually a "bubble" produced each year by kiting up the number of "distributors" lured into making capital investments. By the end of the year, these investors are "dumped" and replaced.

The theft of consumer investments of money, time, talent and hope can have far reaching consequences for consumers – damaging relationships, family, careers and self-esteem. Herbalife's fraud upon the public is compounded by its association with groups of Herbalife promoters such as, My Success System, Newest Way to Wealth, On-Line Business Systems and The Freedom Group. Working collaboratively with the Herbalife Corporation these rapacious recruitment scams add to consumer losses by luring them into buying their marketing materials and incurring other costs with the false claim that they will help them gain success within the Herbalife business.⁵³

Herbalife's business deliberately inflicts large-scale consumer losses. It therefore requires an elaborate system of diversion, deception and disguise. Much of this trickery includes the manipulation or concealment of financial data and calculations regarding numbers of people involved and their incomes or losses. For this reason, this analysis required careful scrutiny of financial disclosures and other mathematical calculations. A reader seeking the truth behind the Herbalife disguise must, to some extent, be willing to examine the math and the data. Like a puzzle whose parts have been scrambled, Herbalife's true nature as a predatory pyramid scheme becomes apparent when the parts are properly organized. None of the math is advanced in complexity, but is a crucial component of the investigation. In the end, all pyramid schemes are math tricks.

SELLING THE "BUSINESS OPPORTUNITY" TO INDUCE PRODUCT PURCHASES

From even a cursory review of the Herbalife operation, the most striking characteristic is its great reliance on the enrollment of consumers into the "Supervisor" level of the distributor chain. In 2006, members of this group represented 27% of all distributors. The thrust of the entire recruitment program is to induce consumers to purchase enough inventory to gain this position on the sales chain.

Every consumer who becomes a Herbalife distributor participates in the Herbalife "business opportunity" by becoming authorized to sell the products and to recruit other distributors. All new investors in the business opportunity purchase "starter kits" and sign contracts as "contractors" of Herbalife. However, those that join at the Supervisor level make the largest, most overt and direct investment in pursuing Herbalife's advertised money-making opportunity.

⁵³ In a previously settled class action lawsuit brought by consumers against Herbalife and associated marketing companies, 2,700 former distributors filed claims with aggregate losses totaling approximately \$19 million. The suit charged Herbalife and the related recruitment groups with operating a pyramid scheme and using false and misleading claims about income to lure investors. (Nancy Jacobs, Individually on behalf of herself and all others similarly situated, and on behalf of the General Public, Plaintiff, vs. Herbalife International, Inc., Herbalife International of America, Inc., Dream Builders & Associates International, Inc., et. al., Class Action Complaint, Feb. 15, 2002 filed before the United States District Court for the Central District of California Los Angeles Division)

Consumers that are persuaded to sign up at this Supervisor level invest approximately \$3,000 (the figure can often be as high as \$3,500 or more) in a one or two month time frame. (This amount of actual investment translates to at least 4,000 “volume points” including shipping and taxes)

The initial high investment is very unusual in the multi-level marketing field, which often defines itself as a business that consumers can begin with a very small initial capital investment, often advertised as under \$100. Herbalife’s emphasis on an initial investment in the thousands of dollars, in combination with other factors such as recruiting new investors in order to rise in positions on multi-tiered chain is a classic hallmark of a pyramid scheme. This hallmark is further highlighted in Herbalife by the fact that the scheme awards the Supervisor status to anyone that makes a cash investment and is unrelated to retail sales.

Though the title of Supervisor clearly indicates a managerial role, no training at all or any experience is required. For each Supervisor the Herbalife sales channel has less than three non-supervisors that would need to be “supervised.” When the pay plan and other factors of the operation are understood, it becomes obvious that the Supervisor is nothing more than a key recruiter for the pyramid, and the initial investments of the Supervisors are the company’s largest single revenue source.

After reviewing the devastating financial returns of the vast majority of those who invest in the Herbalife “business opportunity” I conclude that Herbalife is engaging in extraordinary, systematic deception to induce these Supervisor investments and to enroll others who join at lower levels. In plain terms, Herbalife tricks consumers into buying positions on its endless chain. In exchange for a large cash payment, Herbalife offers what appears to be highly lucrative incentives to profit from soliciting others to invest.

Unknown to most participants, the pyramid design of the plan and the extreme requirement for ongoing investments result in only a small fraction, less than 1% of all distributors, ever being able to gain revenue even minimally. The prime incentive employed by Herbalife is the mirage of the “endless chain”. For those in the top three levels of the pyramid, Herbalife pays commissions based on investments from “infinite levels” of the (endless) chain. Herbalife’s distribution chain is potentially “endless” since each new recruit is authorized and rewarded to recruit others who can do the same *ad infinitum*. Millions of new people are thereby lured into the scheme by Herbalife and its promoters that are positioned in the top 1% of the chain. These promoters have advance knowledge that virtually all new recruits are doomed to losses and that nearly every new investor will quit the “opportunity” in less than a year after suffering losses.

RECRUITING SUPERVISORS TO RECRUIT SUPERVISORS TO RECRUIT SUPERVISORS

The consumers that make the large initial investments and purchase the Supervisor position account for the majority of Herbalife “sales.” Those lured into the business opportunity are then further lured to recruit others.

In 2006, Herbalife reported to the SEC that it had 408,000 Supervisors enrolled for the year. These Supervisors, therefore, account personally or for directly recruited downlines that provide between 65% to 80% of Herbalife’s net revenue of \$1.886 billion (408,000 multiplied by the

minimum investments required to become a Supervisor). Only Supervisors can earn royalty overrides, and only 3% of the Supervisors can earn Production Bonuses, the most lucrative part of the “business opportunity.”

Herbalife offers the Supervisor position immediately to those that make an investment of approximately \$3,000 or more in one month or a larger amount over two months. Herbalife does not disclose how many Supervisors gain the position with one-time personal investments. However, it disclosed in its 2006 10K report to the SEC that only 42% of its Supervisors remain in their positions for more than a year. Accounting for replacements of the dropouts and net growth, about 70% of all Supervisors each year must, therefore, be recruited that same year. The majority of Herbalife’s gross revenue each year is, therefore, directly tied to the annual recruitment of replacements and new enrollments of Supervisors.

Additionally, in its 2005 10K, Herbalife reports, “more than 90% of all non-Supervisor distributors quit within a year.”⁵⁴ This shows that the great majority achieves the Supervisor status immediately or within the first 12 months when they first enroll into the business, rather than beginning at a non-Supervisor level and working gradually. Herbalife literature refers to the outright purchase of inventory to gain the Supervisor positions as a way to “Jump Start your Business.”

The Supervisors are immediately entitled to a 5% “royalty” on purchases of their downlines up to three levels below. By definition, the incentive is to recruit other Supervisors who can profit from recruiting other Supervisors, etc.

Each level can be “infinitely” wide. They are also given the maximum margin when purchases are made by new recruits. Supervisors are entitled to a 50% margin while the Supervisors’ recruits purchase at a 25-35% margin. The difference in margin on each purchase made by newly recruited non-Supervisor is transferred to the recruiting Supervisor. The payment to the recruiting Supervisor is, *de facto*, a reward for recruiting a new investor into the “business opportunity”. Herbalife disguises the process as a “wholesale commission.”

The Herbalife pay plan – based upon rewards for recruiting – offers the appearance of a strong financial incentive to each new recruit to make a large up front investment in order to “jumpstart the business” and gain a Supervisor position on the endless chain. The extreme loss ratio of those at the lower levels to those at the top which is inherent in the closed recruitment system and the market limits on the number of possible new Supervisors are not disclosed in the Herbalife marketing literature or website.⁵⁵

⁵⁴ Herbalife 2005 10K: “For the latest twelve month re-qualification period ending January 2005, approximately 60 percent of our Supervisors did not re-qualify and more than 90% of our distributors that are not Supervisors turned over.”

⁵⁵ To get a sense of the mathematical trickery of this “royalty” incentive, in North America in 2006, Herbalife reported that it had 45,778 Supervisors. Supervisors are 27% of the total distribution channel. So there were about 125,000 non-Supervisor salespeople in North America. If just 10% of the Supervisors (4,578) would recruit three new Supervisors (Supervisors can receive royalties on three levels) and these three did the same and that group repeated the process (a downline of just 39 new people), there would be an immediate growth of approx. 180,000 (39 x 4,578) new Supervisors and a proportionate growth of about 650,000 non-supervisor sales, a 400% explosion in the Herbalife organization. If 10% of that newly recruited group would also build their 39-person downlines, Herbalife’s

The initial investment is only the first requirement to gain access to 5% “royalties” on a 3-level genealogy of new recruits. Each Supervisor must also maintain at least 2,500 volume points each month (including their own purchases) in order to collect.

The quickest and surest way to achieve the monthly group volume is to recruit more Supervisors whose large upfront investments exceed the monthly volume requirement. The right to receive the 5% royalty would be maintained and, more importantly, income could also be gained from the efforts of the new Supervisors as they seek to recruit their own chain.

The pay plan, therefore, not only offers an extreme enticement to make a large initial investment to gain the Supervisor position, but it also places a large requirement on the new Supervisor to rapidly recruit others in order to gain the full advantages that the position offers in “overrides.”

Other provisions of the reward system are similarly based upon recruitment but are relevant only to an extremely small group that is strategically positioned at the top of the Herbalife pyramid. These are incentives and rewards to accelerate the recruitment process. Once a Supervisor’s recruitment activity generates a group volume of 20,000 volume points the Supervisor gains the G.E.T. (Global Expansion Team) level and is eligible for the largest source of payments, Performance Bonuses.

Only those in the top three levels – having achieved at least the 20,000 Group Volume requirements – receive the Performance Bonuses, which range from 2-6%, increasing with volume growth. The Performance bonus is added to the Royalties on the volume of the first three levels, but the greatest advantage of these “bonuses” is that they are paid to “infinite” levels of the recruitment genealogy.

A MONEY TRANSFER FROM THE BOTTOM DIRECTLY TO THE TOP

In the classic pyramid structure, the vast majority of all the people – and the greatest percentage of total investments – are at the lowest levels (last ones in).⁵⁶ In 2006, the “bottom” of the Herbalife pyramid was massive:

North American force of “Supervisors” would approach one million and proportionately there would be 2.7 million more sales people many of whom are trying to reach the Supervisor level! Soon, every American would become a Herbalife “distributor.”

The hidden reality is that Herbalife is luring consumers into pursuing a recruiting scheme in which the market for investors is already saturated. It is mathematically impossible for any but a small few to successfully recruit enough new recruits to recoup their investments. Market saturation will doom nearly all new recruits to failure, but the *overall* market for their replacements remains for Herbalife to exploit, with necessary deception employed to accomplish the task.

⁵⁶ To understand this basic mathematical paradigm of all pyramid schemes, consider a simple structure of 1 person recruiting 5 others, with each new recruit doing the same and the structure extending just 3 levels from the top. $1 + 5 + 25 + 125 = 156$ in the pyramid. However, of the total, 125 are at the very bottom, which constitutes 80% of the total. No matter how much further the pyramid would extend in levels and how many new people it recruited, the bottom level would always constitute 80% of the total. Since the bottom level participants have no one below them, they can earn nothing. They are “doomed by design”, that is, 80% of all who ever participate are doomed from the start. In most pyramids disguised as “direct selling”, recruits must have more than one level below them before they

- Approximately one million non-Supervisors, i.e., 90% of all non-Supervisors that join during the year. These are the newest recruits with the least advantages for profit as defined by the business opportunity.
- Approximately 386,000 Supervisors, i.e., 94.5% of all Supervisors that earned on average no more than \$549 per year. Nearly one-quarter million Supervisors, or about 60% of all that were counted in 2006, were enrolled in that same year. These newest Supervisors along with those with minimal earnings are among the “last ones in.” At the Supervisor level, they have made the largest investments, but the vast majority earns nothing or next to nothing in “royalties” (5% of the volume points of new recruits.) and virtually none in this group is eligible for the most lucrative of all payments, the “performance bonuses.”

The Herbalife Performance Bonus can be as high as 6% (based on the “retail” value of the purchases, which is a 100% markup over the distributors’ actual dollar investment) and extends to “infinity” in depth of levels, thereby tapping into the huge base at the bottom, those entering each year. Those in the top three levels actually receive larger rates of commission, per sale, than those doing the recruiting, an extreme incentive to get into these top positions. The only way to get there is relentless recruiting.⁵⁷

The following charts reveal the extraordinary money transfer from the latest group of investors to the earlier ones. The data charts are only for those investing at the “Supervisor” level that requires an initial investment of between \$3,000 and \$4,000.

The calculations are based only on data provided by Herbalife on its website. The document is entitled “Statement of Average Gross Compensation of U.S. Supervisors in 2006.”⁵⁸

can recoup their own investments. In practice, therefore, the bottom two levels, at least, are doomed. In the above model, the bottom two levels will always constitute 96% of the total!

⁵⁷ According to Herbalife’s Statement of Average Gross Compensation of U.S. Supervisors in 2006, the distributors in these top three levels – that receive the “performance bonuses” – represent less than 3% of all those in leadership positions or less than one percent of the entire distributor chain.

⁵⁸ Without careful analysis, Herbalife’s “Statement of Average Gross Compensation”, is virtually useless to consumers considering an investment in the business opportunity and can be dangerously misleading. Among the confusing and misleading elements:

- It states that the average payment to “all leaders” in 2006 (“leaders” defined as Distributors that reach the rank of Supervisor and above, which it says are over 25% of all distributors) was \$2,200. However, that number multiplied by the number of Supervisors for 2006 reported in the 10K – 408,000 – is far higher than what the company paid out in total as Royalties and Overrides.
- The report also divides all leaders into Active and not-active. Yet, all of the Supervisors had invested thousands of dollars in a one or two month time frame. Those that failed to earn commissions are defined as not-active, as if they made no effort, after making this substantial investment.
- Further confusing to the readers, the report offers percentages of Supervisors at each level for the Actives” and for “All”, however both are under the subhead of “Active Leaders.” Offering percentage of the ‘actives” at each level shows a total group as “100%” in one column and the same group as 43.5% in the next column. Though the “actives” account for only 43.5% of all Supervisors, the report does not disclose that the other 56.5% received no commissions at all. The zero income for the majority of all Supervisors is excluded from the calculations of averages.

The charts present the data that Herbalife offers to consumers, followed by an analysis of that data using a sample of 1,000 Supervisors. When actual numbers in a sample, rather than just confusing percentages, are applied, the data reveal a pattern of massive financial loss and an extreme money transfer.

The pay plan is a complex set of rules, purchase requirements, and varying rates of payments. In the end, 36% of all the money that the distributors pay to Herbalife to buy and to maintain their “distributorships” is transferred from the last ones in to the earlier investors in the Herbalife “business opportunity.” More than half of all that money winds up in the hands of one-half of one percent of the total group of Supervisors. The Supervisors are the top 27% of the entire chain of 1.5 million investors.

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- The averages are mean averages, rather than weighted or median, which would offer a truer picture. For example, the report offers the mean average of the “Active” Supervisors as \$5,100. It does not note that the mean average of the 93% of this group – those at the bottom – was less than \$780 or only 15% of the number it offers as the “average.”
 - Finally, the report, in addition to misleadingly naming only those that made enough purchases to qualify for commission as “active”, totally omits the 1.1 million distributors that did not invest enough to reach the Supervisor level. These are excluded as if they are not part of the “channel” and not salespeople that represent Herbalife’s products. Yet, in the 10K report to shareholders, Herbalife states, “We sell our products in 63 countries through a network of over 1.5 million independent distributors.” To shareholders, Herbalife made no distinctions of how many are “active.”

HERBALIFE DATA:
“STATEMENT OF AVERAGE GROSS COMPENSATION OF
U.S. SUPERVISORS IN 2006”

Earning Level	% of Total Leaders	% of Active Leaders	Average Earnings (USD)
Presidents Team	0.1%	0.3%	\$ 611,094
Millionaire Team	0.4%	1.0%	\$ 111,444
GET	2.3%	5.3%	\$ 24,455
World Team	2.5%	5.8%	\$ 4,219
Supervisor	38.1%	87.5%	\$ 549
Total	43.5%	100.0%	\$ 5,192

Note that the data omits the zero income of all those defined as not “active” and does not calculate how much of the total payments go to each level.

USING HERBALIFE DATA

CALCULATIONS OF PAYMENTS TO ALL HERBALIFE
SUPERVISORS, ON A PER 1,000 MODEL

Earning Level	% of Total Leaders	Mean Average Earnings (USD) of Leaders	No. per 1,000 of All Leaders	Total Payout for Each Level per 1,000	% of Payout for Each Level per 1,000 Leaders
Presidents Team	0.1%	\$ 611,094	1	\$ 611,094	31.5%
Millionaire Team	0.4%	\$ 111,444	4	\$ 445,776	23.04%
GET	2.3%	\$ 24,455	23	\$ 562,465	29.08%
World Team	2.5%	\$ 4,219	25	\$ 105,475	5.45%
Supervisor	38.1%	\$ 549	381	\$ 209,169	10.8%
Supervisors no earnings	56.5%	–0–	565	–0–	N/A
Total	100%	\$1,934	1,000 rounded	\$1,933,979 Total Paid	100% rounded

When actual numbers are applied – a sample of 1,000, and all Supervisors are included – an enormous money transfer is revealed accompanied by financial losses suffered by the vast majority.

- For each 1,000 Herbalife Supervisors, 435 will earn some commission while 565 earn no commissions (did not purchase enough during the year – after making initial investments – to qualify for commissions).

- 0.5% (one-half of one percent) of the total group, that is 5 Supervisors at the top of the chain out of each 1,000, will get 55% of all Commissions paid out by Herbalife to the sample.
- The top 2.8% of the Supervisors (those eligible for the “Performance Bonus”) receive 84% of all Commissions paid out by Herbalife to the sample.
- The bottom 56.5% of the chain will get no commissions at all.
- The bottom 41% that does earn some commission receives an average payment of \$14.90 per week.
- Each Supervisor in the list has invested the same to join and to remain qualified. The difference in income is based not on the amount of investment or on “sales” but on position on the chain and recruiting activity.

Herbalife makes a distinction of the “active” Supervisors, those that generated 2,500 volume points after becoming Supervisors. Since *all* Supervisors invested more than \$3,000 and were entitled to the Royalty Overrides based on 3-levels of new recruits, it cannot be argued that *only* the “actives” were participating in order to earn income. However, as the chart below reveals, even if the calculations excluded those that Herbalife termed “not active”, the money transfer pattern remains extreme.

Using Herbalife Data

Calculations of Payments to “Active” Herbalife Supervisors, on a per 1,000 Model

Earning Level	% of Leaders	No. per 1,000 of Leaders	Average Earnings of Leaders	Total Payment to Each Level	%of Payment to Each Level
Presidents Team	0.3%	3	\$ 611,094	\$ 1,833,282	36.9%
Millionaire Team	1.0%	10	\$ 111,444	\$ 1,114,440	22.4%
GET	5.3%	53	\$ 24,455	\$ 1,296,115	26.1%
World Team	5.8%	58	\$ 4,219	\$ 244,702	4.9%
Supervisor	87.5%	875	\$ 549	\$ 480,375	9.7%
Total	100.0%	1,000 rounded	\$ 5,192 Actives	\$ 4,968,914 rounded	100%

From a Sample of 1,000 “Active” Supervisors in 2006:

- **Out of 1,000, just 3 would get 37% of all the money.**
- **13 of them at the top got about 60% of all the money**
- **The top 7% of the “Actives” got over 85% of all the money**
- **The mean average payments to the bottom 93% are less than \$15 a week.**

In summary, the revenue of the company depends almost totally upon the recruitment of Supervisors. This involves persuading consumers to invest more than \$3,000 initially. The program then powerfully induces them to recruit other Supervisors by requiring an ongoing monthly volume before they can gain the rewards. Finally, the reward system accelerates the recruitment process by top loading the pay plan with an enormous bonus available only to the top 1% (3% of the Supervisors). Recruiting is the only feasible way to reach these top positions

The pyramid pay formula, in conjunction with scheme's rules, results in the transfer of the great majority of all money to the very top of the pyramid, leaving virtually all others with financial losses.

THE HERBALIFE LURE: FALSE, MISLEADING REPRESENTATIONS, MISSING DATA

The first encounter a consumer will likely have with a presentation of the Herbalife "Business Opportunity is the company video at the "business opportunity" link at Herbalife's official website.

(http://www.herbalife.com/dsassign/business_opportunity_landing.jsp?_requestid=1931827)

The video begins with disparaging testimony on the frustrations and futility of traditional corporate, trade, and professional occupations. Long hours, little time for family, low pay and job insecurity are among the ills of the traditional workplace, the video dramatically explains. From these dreary reports and complaints, the music picks up in pace and the stories of satisfied and excited Herbalife distributors are offered as the solution to widespread economic pain. The reports and the theme of the presentation are not only on earning income but clearly on *very large incomes*.

"Big cars, big homes"

"It's all about making money."

The testimonials are supported with images of large homes, luxury cars and stylishly dressed people. Then the featured Herbalife participants share their actual incomes.

"\$1,500 - \$2,000 per month"

"\$300 a month, then \$800, then \$2,700 and I quit my job."

"First month - \$1,500"

"\$2,800 in the first month."

"\$16,000 in one month"

"\$10,000 in a month, then \$15,000, \$20,000, 30,000, \$40,000 in one month."

"\$25,000 in one month. I'm kind of excited!"

"First nine months that I got going, \$250,000"

The video asks the viewer if they want to change their financial future and reach their financial dreams.

It would be understandable that the viewer might believe that these claims are typical or generally achievable by large percentages of the Herbalife sales force. The only cautionary or qualifying information appears just before the video has begun, a silent script on screen for exactly 6 seconds. It reads in part: *"Examples are not necessarily typical or average. There is no guarantee. And some examples are those in the top 1% of all distributors."*

Even if a consumer had carefully read the disclaimer, it did not indicate that the examples were not representative, valid or applicable to the new recruit personally, but only that they are not "necessarily" typical (literally meaning that they could be) and that there was no "guarantee" of matching these reported incomes (seeming to indicate that it could be likely, just not "guaranteed – but who would expect a guarantee?").

Unless someone understood Herbalife's actual income data – for example, that there were 1.5 million people in the chain and that each year, perhaps as many as 99% of all who join during one year will quit within that same, and that each year 98.5% of all distributors earn less than \$10.50 a week on average, then the disclaimer note has little meaning. The advisory that “some” of the testimonials come from distributors in the top 1% would mean nothing unless one could understand what it would take and what the odds would be of getting into that tier. How well do the Supervisors actually do financially compared to that promotional video? According to Herbalife disclosure document 97% would not earn in commission on average even the amount needed to pay for qualifying inventory purchases. The odds of making a profit for those below the Supervisory level are so low they could not be meaningfully charted

CONFUSING THE SHAREHOLDERS

Since the Supervisors represent the vast majority of all company revenue, their financial condition, how they earn income, their rate of turnover and the precise number of them that are recruited – and need to be recruited each year for the company to sustain itself – would be crucial for an investor or analyst to know.

Yet, the Herbalife 10Ks offer confusing and contradictory data on these questions.

The 2005 10K reported, *“For the latest twelve month re-qualification period ending January 2005, approximately 60 percent of our Supervisors did not re-qualify and more than 90% of our distributors that are not Supervisors turned over.”*

This clearly states that between the end of 2004 and the beginning of 2005, 60% of the Supervisors were eliminated. Yet, the same report offers the following charts:

As of December 31,						
	2003	% Change	2004	% Change	2005	% Change
The Americas	110,165	4.4%	124,605	13.1%	160,878	29.1%
Europe	84,665	10.5	102,203	20.7	95,628	(6.4)
Asia/Pacific Rim	55,564	(14.7)	55,460	(0.2)	64,286	15.9
Japan	24,485	(23.3)	16,860	(31.1)	13,566	(19.5)
Worldwide	274,879	(1.5)%	299,128	8.8%	334,358	11.8%

Number of Supervisors by Geographic Region as of Requalification Period

As of February,			
	2003	2004*	2005
The Americas	67,921	75,359	87,925
Europe	51,290	70,239	65,104
Asia/Pacific Rim	35,637	31,790	38,524
Japan	18,287	13,946	9,547
Worldwide	173,135	191,334	201,100

While the 10K said that 60% of all Supervisors did not “re-qualify” each year, the chart offers different data. It shows that, for example, in Dec. 31, 2004 there were 299,128 Supervisors. Then at the end of February 2005, when Herbalife determined how many “re-qualify,” based on the required level of purchasing, there were 201,100. This would be only 33% loss rate. ($299,128 - 201,100 = 98,028$) and ($98,028 \div 299,128 = 33\%$)

If 60% failed to re-qualify, then the number of survivors would be 119,651. ($299,128 \times 40\%$). Where did the 81,449 others come from? (201,100 who were reported active in Feb. ‘05 minus the 119,651 that would have been active if just 40% survived.)

Herbalife’s data is particularly puzzling because it omits two months (January and February) in which the company recruited new people. But, if the missing two months of recruiting activity accounted for the discrepancy, it would mean Herbalife recruited 81,449 new Supervisors in just two months, or 40,725 a month. This would be an annualized recruitment of 488,700 ($40,725 \times 12$) and would be added to the 40% that stayed active (119,651). This should then be a total at the end of the year of 608,351 ($119,651 + 488,700$). In fact, Herbalife reported that just 334,358 were on the books at the end of 2005.

While the 2005 10K offers conflicting data, the key about “re-qualifying and “turning over”, euphemisms for failure and quitting, this data is missing entirely from the 2006 10K. The 2006 Herbalife 10K does not include the monthly data showing how many were accounted for at the end of each year for three years and how many were accounted for in February of those years when the lists were purged of those that did not re-qualify.

Further, in 2006, the reference in the 2005 10K that “more than 90% of our distributors that are not Supervisors turned over.” was not repeated. Investors reading the 2006 10K would not know that, combining the 90+% turnover of non-supervisors with a 60% failure rate among the Supervisors equates to an overall failure rate of more than 80%. They would therefore not know that just to maintain 2006’s level of distributors, Herbalife would have to recruit 1.2 million new distributors in 2007. (80% of its roster of 1.5 million distributors at the end of 2006.)

In summary, Herbalife presents a grossly misleading appeal to consumers to invest in its “business opportunity.” The misleading appeal includes the omission of key data, the presentation of absurdly irrelevant testimonials, and the confusion or distortion of historical data on loss rates, failure rates or market saturation.

The misrepresentation continues beyond consumers also to shareholders who are similarly presented a false picture of “direct selling”, and “financially rewarded” salespeople. Omitted are the facts that reveal a pyramid recruitment scheme that merely transfers investments from the newest recruits to a small group of recruiters positioned at the top of the chain, leaving virtually all with a financial loss and resulting in virtually all that join during the year quitting the scheme the same year and never buying the products ever again.

THE GREAT RETAILING CHARADE

Reading the Herbalife 10K submitted to the SEC and shareholders, one would conclude without doubt that Herbalife’s business model is a straightforward direct selling business that uses independent distributors to reach its customers. From the 2006 10K:

“The Company’s products are manufactured by third party providers and then sold to

independent distributors who sell Herbalife products to retail consumers or other distributors.”

“We believe that the direct-selling channel is ideally suited to marketing our products, because sales... are strengthened by ongoing personal contact between retail consumers and distributors.”

Indeed, the word “retail” shows up over 100 times in the Herbalife 2006 10K. Yet, it is also disclosed that Herbalife does not sell any products at all on a retail basis. It only sells to distributors. Any retail sales that would occur would be carried out by the distributors themselves. As to how much of their products the distributors resell to retail customers, Herbalife actually offers what seems to be a dollar amount of what the distributors would earn. It is called the “distributor allowance.” Along with the royalties and overrides, Herbalife claims in the 10K that the distributors rewards amount to 73% of the retail price, 50% gained from reselling to retail customers and 23% from Herbalife in the form of royalties, overrides and bonuses, based on “group volume.” These are payments made by Herbalife to the distributors. For the distributors who receive them – a small minority of the total – these payments are primarily based on the purchases of other distributors who are linked in the chain below them, i.e., “later ones in.” In 2006, Herbalife listed the amount that the distributors gained from retailing (the “allowance”) at more than \$1.4 billion (\$1,472,527,000), nearly \$1,000 for each distributor (based on 1.5 million distributors.) This figure is actually much larger than the company paid out in overrides, royalties and bonuses (approx. \$675 million).

In further support of this figure, which is supposedly gained by the distributors from retailing, Herbalife even lists \$3,100,205,000 as its “retail sales” revenue. This would be the amount of all its sales to the distributors marked up 100% and resold in the open market to the general public. This is a remarkable figure in that it indicates that 100% of all products were resold and they were sold at the manufacturer’s suggested price, without discounting or giving any away as samples.

In the history of direct selling, this would be considered a sales achievement of monumental proportions!

RETAIL REALITY

A conventional market and sales analysis, however, immediately and unquestionably reveals that Herbalife distributors do not – and could not possibly – retail a substantial amount of their inventory purchases.

1. The market for Herbalife’s weight loss and nutrition products is highly competitive and price-driven, while:

- The Herbalife brand name is not advertised and is unknown to most consumers.
- The similar products are abundantly and more conveniently available to consumers from multiple sources, including mail order and retail stores or even many other multi-level marketing companies.
- The company provides little or no marketing support in sales leads and in generating market awareness.

- Prices of some Herbalife products appear higher than competitive products available in stores.
- Many of the products are nutrition-based and potentially therapeutic, yet Herbalife salespeople are legally prohibited from making any therapeutic claims and the company has no formal training program in nutrition.
- More than 80% of Herbalife entire sales force quits the business within a year, not nearly enough time to build a retail customer base.

2. The unlimited recruiting policy of the company is totally contrary to sustaining retail selling.

- Profitable retailing requires some limitation on the number of retailers in any given area. Herbalife's policy of authorizing and incentivizing each distributor to recruit more distributors is contrary to a retail sales model. Each new recruit in an area dilutes the market potential of all existing ones. More new distributors that buy at wholesales levels not only dilute the market but force downward pressure on retail pricing. No sustainable retail-based sales organization could survive a company's policy of authorizing an unlimited number of new retailers in all market areas.

3. The entire reward system works against retailing.

- The vast majority of all Herbalife salespeople are allowed only 25% gross profit, a rate too small to cover the high costs of direct selling. The 25% is further eroded by the distributors having to pay shipping and taxes based on the suggested retail price.
- While the amount of inventory purchased by the non-Supervisor distributors is too small to provide a net profit, the distributors at the Supervisor level are prevented from significant retailing by *high* inventory purchase requirements. Recruiting other distributors becomes the only feasible way to recoup the investments and gain the overrides. They must find new distributors, and preferably more Supervisors to meet their high purchase requirements.
- The incentives to the Supervisors reward recruiting over retailing. These include incentives based on a three-level genealogy of other supervisors and a 25% "allowance" when they sign up new distributors at the starter level. Recruiting a new distributor, rather than a single retail sale to an end-user, provides a larger sale and offers the potential of ongoing recruiting.
- Overrides and Commissions are only paid on downline *purchases*, not retail sales. This basic fact is disguised by Herbalife's payment of overrides based on "volume points" that equate to retail prices. Though a retail price point is used for commission calculations and sales taxes, the actual commission is driven by a *wholesale* purchase, never a retail sale.
- Bonus payments are based on depth of the downline – the result of recruiting, not retailing – and increase in rate as volume grows. This overwhelmingly induces recruiting activity to maximize the formula.

- The net result of the pay formula sends the majority of all commission payments to the top levels. Recruiting is the only feasible strategy for reaching the top levels where the highly promoted “big incomes” are available.

4. Marketing and promotions of the company – contrary to some of the rhetorical references in SEC filings – overwhelmingly emphasize recruitment over retailing.

- Promotional presentations often used “exponential expansion” of downlines as the means to achieve high income (5 get 5 who each get 5 more, etc.) and the literature emphasizes the returns based on building a downline (achieved by recruiting).

5. Two more compelling factors from within the company itself reveal that the distributors themselves are the “customers” and the company has no true retail base.

- **The Distributors** anecdotally report that they do not retail, that the entire pay plan and business model make retailing unprofitable and that the company and its top promoters focus on recruiting, not retailing.
- **Herbalife** acknowledges in its 2006 10K that the vast majority of its distributors, those at the levels below the Supervisors, do not earn income from retailing.

Many of our non-supervisor distributors join Herbalife to obtain a 25% discount on our products and become a discount consumer or merely have a part-time income goal in mind. Consequently, non-supervisor earnings tend to be relatively low and are not tracked by the Company.

The “non-supervisors” constitute 73% of the sales force. Their prime financial incentive, though it is minimal, is to retail Herbalife products. They can sponsor other distributors, but they are not entitled to receive royalty overrides. This sector constitutes the bulk of the sales organization – the “feet on the street” – that is positioned to retail, yet Herbalife does not track their activity or earnings, which is to say, does not monitor their retail sales activity. Herbalife does not even assert that these people ever earn any net income, only that some have a “part-time income goal in mind.”

In its 2005 10K (not disclosed to shareholders in 2006), Herbalife also reported that 90% of these non-supervisors quit the company completely within one year. The extraordinarily high and quick turnover of the great majority of the sales force, coupled with their low purchase levels and Herbalife’s own disinterest in their sales activity, demonstrate that little or no retailing is occurring. The rest of the channel – the Supervisor level – is economically compelled by the Herbalife incentives and inventory requirements to recruit other distributors rather than retail. Yet, whatever retailing this group might actually do is similarly not tracked by Herbalife

It is inconceivable that a legitimate direct selling company – that is based on retailing – would not take measures to know about its end-user market and the retailing success of its sales channel. Herbalife’s behavior can only be accounted for by the glaring evidence that Herbalife is

not a direct selling business at all. Its real business is to market a “business opportunity.” As part of this opportunity, the investor must purchase inventory. The mission of the company is, therefore, to induce distributor investments in inventory.

What Herbalife reports to the SEC as “sales” are not sales at all. No legitimate direct selling company can report purchases made by the distribution channel as “sales” unless there is evidence that the channel can and will resell the goods to the end users. Herbalife only sells to the channel, which cannot profitably resell the goods. Market factors, the reward system, the purchase requirements and other costs and the unlimited expansion of the channel prevent any meaningful reselling.

Lacking a viable retailing opportunity, the distributors are compelled to pursue the other part of the “business opportunity” – seeking rewards from soliciting other investors into the business opportunity, that is, to promote the endless chain of distributor investment/purchases. This strategy, the only one available to the recruit, proves to be a futile and desperate measure, as 90-99% of all participants on the chain are doomed to be in the bottom positions where profit is not possible. Finding themselves trapped in this “failure” position, more than 90% of all who join each year will quit within the year. Herbalife and its top promoters then replace the “failures” by means of their highly developed and deceptive recruitment program.

Based on federal court rulings and precedents of prosecutions by the Federal Trade Commission, the non-retailing, recruitment-based business practices of Herbalife would be illegal.

APPLYING THE FTC TEST FOR LEGALITY:

70% RETAILING REQUIRED TO COVER HERBALIFE COST STRUCTURE AND RECRUITMENT REWARDS

The FTC has prosecuted about 20 multi-level marketing companies that were similar in model to Herbalife. In nearly all cases, the FTC determined that lack of retail revenue was the key indicator of the operation of a pyramid scheme disguised as “direct selling.”

One tool that the FTC used in making its evaluation is a retail business model “test” developed by FTC Senior Economist, Dr. Peter Vandernat, Ph.D. This tool does not determine legality, but it does determine how much retail revenue the multi-level marketing company must generate in order to be legal. When that figure is ascertained the FTC then can assess whether the company does, in fact, gain the necessary level of retail sales, or is primarily generating its revenue from endless chain recruiting, which is illegal under Section 5 of the FTC Act, covering “unfair and deceptive trade practices.”

The test has been applied by the FTC in declarations against multi-level marketing schemes such as Equinox International, Trek Alliance, and SkyBiz among others, which the FTC charged were pyramid schemes disguised as direct selling companies. The test was described and presented in a peer-reviewed article in a respected academic journal. This article was also

referenced in the FTC's Notice of Proposed Rule Making⁵⁹ to regulate business opportunity schemes, including multi-level marketing companies such as Herbalife.

To support the retail criteria for distinguishing pyramid schemes from legitimate direct selling companies, the FTC relied upon federal court rulings, such as Koscot, Omnitrition and Gold Unlimited, that have firmly established that a multi-level marketing company must source most of its commission payments along with other business costs from retail purchases, that is, from consumers *outside the chain*. If most of the money for costs and payments to recruits is coming from the recruits who are part of the chain, the scheme is an endless chain, which is an inherent fraud.

The test sets up a basic retail-based business model, using a base of \$1,000 of net sales of the company. The retail model affirms the basic reality that if a company is in the direct selling business, it must have customers. If it gains all or most of its revenues only and ultimately from its sales force without end-user customers, how would the sales force earn a profit?

If the sales force is treated as the customer base then how does the company induce them to become customers? If the company rewards all the salespeople for recruiting other salespeople, then the plan is utilizing an "unfair and deceptive trade practice", that is, to offer rewards based on an "endless chain."

The endless chain is "unfair and deceptive" because:

- It cannot deliver its promised rewards to any but a few, since only a few can be positioned at the top of the chain. Though the scheme, by design, must cause most to be in the bottom positions where no profit is possible, the scheme will claim that profit is available to all. This is deceptive and the harm caused is unfair.
- It is unsustainable since it is based on offering the same reward proposition to each group based on endless expansion of new recruits, which is impossible.
- It must lead to saturation while continuing to recruit new people and promising them the opportunity to recruit others, which is deceptive and causes financial losses to nearly all.

In short, an endless chain proposition used to induce product purchases is a classic fraud. Part of the disguise of endless chain scams is to present themselves as "sales companies" and imbed the money transfer in the product purchase price and in other related fees for the "business." In Herbalife's case, 36% of the base price paid by the distributors is transferred from purchaser/investor to the recruiters. The FTC, therefore, pursued questions aimed at uncovering such disguised pyramid schemes.

- Does the scheme have a true customer base in the open market?

⁵⁹ The Notice of Proposed Rule Making references the article by Peter J. Vandernat and William W. Keep, *Marketing Fraud: An Approach to Differentiating Multilevel Marketing from Pyramid Schemes*, 21 J. of Public Policy & Marketing (Spring 2002), at 139– 151. (Federal Register / Vol. 71, No. 70 / Wednesday, April 12, 2006 / Proposed Rules, 19060

- Or, does it “make its own market” by using the endless chain lure that promises profit from joining the chain and having the right to recruit others, with the participants having to purchase the products as part of the “opportunity”?

Legality, the FTC asserted, requires that the MLM pay for its basic business costs and at least 51% of its payments to the recruiters from retail revenue. Dr. Vandernat wrote,“(In legitimate MLMs)... “commissions,” or whatever the rewards paid to distributors may be called, are ultimately to be paid out of retail revenues... In pyramid analysis the core requirement for a legitimate business is that the rewards paid in connection with recruitment are to be tied to the sales of goods and services to the public (Koscot test).”

The test that the FTC’s Dr. Vandernat developed and which the FTC applied in numerous prosecutions is based on the logic that if less than 51% of the recruiters’ commissions come from retail revenue, but rather are sourced from the investments/purchases of the recruits, they are, *de facto*, payments for recruiting, the hallmark of the pyramid scheme. The 51% threshold is used in order to ensure that the rewards are “primarily” retail-based. This is the requirement established by federal court rulings. The FTC does not require that *all* rewards come from retail, just most of them. Consumption of some of the products by the distributors and product giveaways are accounted for.

When the test is applied to Herbalife it calculates that at least 70% of all purchases by the distributors would have to be sold to the public on a retail basis at full retail price (100% markup).

As has been shown, there is abundant evidence that Herbalife’s distributors do not retail any amount even approximating this rate. Herbalife itself, though it claims to be a “direct selling” business, has no mechanism or system for measuring levels of retail selling. It has no record of who or how many people ultimately purchase its products. It has no sustainable sales force to survey since, according to its 10K filings, more than 80% of all its salespeople fail and quit the business within a year.

THE FTC TEST APPLIED TO HERBALIFE, USING 2006 10K DATA:

70% of Herbalife Products Must Be Retailed to Actual Consumers for Herbalife Legality

FTC Retail Test: Basic Costs and 51% of Rewards to Recruiters Must Be Retail-based

- Projections are on a base of \$1,000 of distributor purchases
- Production costs were 20.2% of all purchases by distributors Upline
- Overhead costs were 30.4% of all purchases by distributors
- Payout was 35.8% of all purchases by distributors
- Distributor margin on retail sales was 50%
- FTC Test required 51% of commissions to be paid from retail revenue

Retail-base Cost Projections:

3 Production (from 2006 10K)	\$202
3 Overhead: (from 2006 10K)	\$304
3 FTC Test Figure of 51% of Royalties/Overrides	\$183 ¹
3 Retail Profit if 70% of Goods were Retailed to Public	<u>\$700</u> ²
Total Costs:	\$1,389

¹ 35.8% of net sales are paid out to the recruiters as "royalties and overrides."
 \$1,000 of sales x 35.8% x 51% = \$183

² At a 50% Gross Profit, \$1,000 of goods purchased by the distributors would be resold for \$2,000, yielding a \$1,000 Gross Profit. (\$1,000 x 70% = \$700)

Retail-base Revenue Projection:

Total Revenues from Retail Sales if 70% of all product purchased by the distributors were retailed to the public:

Total Revenue: \$1,400³

³ \$1,000 of distributor purchases retailed with a 50% gross profit would be sold for \$2,000 (70% of \$2,000 = **\$1,400**)

For Herbalife to be a legal sales company, not a pyramid recruitment scam, at least 70% of all Herbalife products would have to be retailled to consumers by Herbalife distributors

- The 70% figure is arrived at by testing other lesser amounts until a retail revenue level is reached that would cover all the basic business costs, including the retail profit margin for the matching amount of retail sales, and 51% of the royalties/overrides. When different retail levels are tested, the Projected Retail Profit amount changes on the left side and the projected total retail revenue changes correspondingly on the right side. All other variables on the left side would remain unchanged. They are derived from the 2006 10K are fixed amounts based on each \$1,000 of purchases by the distributors.

- For example if a 65% were tested, the retail profit figure under projected costs on the left side of the column would \$650 and the Total Costs would \$1,339. On the right side the projected revenue at a 65% retailing level would only be \$1,300 (\$2,000 of potential retail revenue x 65% = \$1,300) making it less than the costs and failing the test.

THE PENNY STOCK PONZI SCHEME ANALOGY

MAKING ITS OWN MARKET

At the price charged and sold to revolving group of untrained salespeople, is there really a market for Herbalife's virtually unknown brand of weight loss, food supplements and skin care products? Herbalife provides its distributors with no sales leads, no national advertising. It charges them heavily for marketing materials in addition to freight and taxes that it calculates on the suggested retail price which is 33-100% above the distributors' pricing, depending on their rank.⁶⁰

When all relevant marketing and sales factors are reviewed, it is obvious that the distributors do not – and cannot – resell Herbalife goods on a retail basis on the open market. There is no demand and the sales model does not support channel “pushing” based on the product itself. Herbalife does not have a system to measure or account for any retail sales and no company rewards are offered for retailing. Distributors anecdotally report that little or no retailing is occurring. Herbalife acknowledges that 73% of its sales force purchases Herbalife products only “to obtain a 25% discount on our products and become a discount consumer or merely have a part-time income goal in mind” and that any earnings, if they exist at all, “are not tracked by the Company.”

Though Herbalife suggests that some of these distributors purchase the products based on discount pricing, the sales were made to them only as part of their enrollment in a money-making plan. They did not buy the products straightforwardly but as part of their participation in the Herbalife “business opportunity.” Therefore, many in this group, were just seeking not products but had an “income goal in mind.”

Herbalife “sold” more than \$1.886 billion of goods to consumers in 2006. This was not done by distributors reselling the goods or due to any market demand for the goods. It was done in a classic Ponzi scheme manner by “making its own market.” Herbalife utilizes a version of the “pump and dump” system utilized by stock manipulators, often called “penny stock” promoters. In the penny stock model, a “boiler room” of stock promoters, representing a small group of Insider financial backers, sells a worthless stock at an arbitrary price to select consumers that are solicited usually by telephone. Each consumer is told that the stock is for a company, unknown to the consumers and the general public, that is poised for explosive growth and profitability. In a short time, after selling the initial offering of stock, the penny stockbrokers develop a later group of buyers, also through direct solicitation. They arbitrarily set the stock at a substantially higher

⁶⁰ According to the 2006 10K Herbalife collects more than \$100 million from its distributors for sales related company materials, approximately \$250 for each distributor at the Supervisor level.

price and convince the new group to buy the stock from the original group, giving them the very same story that the stock is destined to grow further. This process is repeated successively. On each transaction, the prices are fixed by the promoters. The stock that the penny stock promoters offer does not compete with other stocks in the open market and is not listed on any major exchange (equivalent to Herbalife's product not being available in stores.) Each buyer is led to believe they have "inside information" and are "at the right place at the right time." They are buying a "future."

In fact, the stock would never sell in the open market when true facts about the company were known. The market for this stock is closed and controlled by the promoters who take a large percentage of the "spread." The story about the company's expected growth is false.

Though the share price is manipulated up by the promoters, often doubling quickly, the total price paid for the shares by each successive new group of buyers is usually about the same. The promoters have in mind a total investment threshold that the solicited investors will pay. This allows the promoters to standardize the sales pitch and the price and to focus on a target market that fits this purchase price level.

In this example, \$2,500 is the price. This relatively low amount also protects the promoters when the stock price crashes and most investors – the last ones in – lose their money. Few will choose to legally pursue the promoters for fraud over a relatively low amount of losses when time and legal costs are factored. Most will often write off the loss as due to their own gullibility. Most will not even realize the stock was manipulated and will just assume they had bad timing or made a poor investment decision.

Therefore, with the price of the shares rising, but the average dollar price paid by each investor remaining about the same, the total number of new investors must grow successively. For example, the first group – usually uninformed and inexperienced investors that have been solicited by the stock promoters – pays \$2,500, and each share is valued at one penny (\$.01). Each investor receives 250,000 shares (250,000 shares x \$.01 per share is \$2,500). One hundred investors are found, raising \$250,000. The total number of shares sold is 25 million (250,000 shares x 100 new shareholders). This will be only 20% of the total issued. The Insiders will hold 80%, 100 million shares. That enormous block will have value and will grow in value only to the degree that the promoters can pump up the stock and find more investors.

All of the public shareholders that are solicited are told the stock will soon grow in price and they can sell at a good profit. They are asked to imagine what they might do "if the stock goes to a dollar – converting their \$2,500 investment to a quarter million dollars!"

The stock price is then doubled and a new group of investors is solicited to buy the originally issued shares now at two cents (\$.02). The first group nearly doubles their investment and most happily sell their shares. Members of the new group will also be sold \$2,500 blocks of shares each, since this is an amount most can afford and is the "block" that is promoted. For \$2,500 they will each receive only 125,000 shares, half of what the first group got for the same investment amount. To move the entire block of shares, the promoters, therefore, need to find nearly 200 new buyers, twice as many as they brought in earlier.

The process continues. The stock price is manipulated higher. More people must be found. Some will continue to ride the wave. They will take their gains and reinvest them in the stock again and perhaps add more capital, at higher share prices. But, even as the price per share rises dramatically, the total amount paid by each person in each new group will usually remain about the same as earlier groups. The total number of shares they receive will be reduced from earlier buyers who paid the same amount. For each group to unload its stock a much larger group of new buyers must be found.

Whatever the amount paid, the value is determined strictly by the ability of the promoters to find new buyers. The market is closed. Without the promoters' false story about the company's imminent growth, the stock is worthless. And even if the promoters can find new people, each successive level of buyers is paying more money for a stock that has virtually no intrinsic value. In number of investors, each new level will always account for the majority of all shareholders that have ever owned the stock. The bottom level will always be more than 50% of all that ever bought in.

HERBALIFE'S PUMP AND DUMP PONZI

In Herbalife, analogously, each new investor pays about \$3,000, the cost of becoming a Supervisor. The real value of this "distributorship" is based almost entirely upon new investors/Supervisors joining. They will all pay the same for the their Supervisor distributorships, level after level. If enough new investors are found, the original group can recoup its money. The value of the distributorship is based on "projected growth" of new investors. The story that the distributorship's value is based on the consumer demand for the Herbalife product, and that there is a viable opportunity to retail the product is as false as the penny stock promoters' story about their company's expected growth and profitability.

Like the penny stock victims, all successive levels of Herbalife investor/Supervisors are faced with a saturating market. The ability to find new investors declines as the base grows. So, though they paid the same as earlier investors, in fact, the "opportunity" shrinks. In Herbalife's case, the markets for new investors in most countries— in sufficient numbers for the latest ones to recoup their investments — were saturated many years ago. Distributors signing up now are doomed from the start.

The type of investors that are burned by the penny stock promoters closely resemble those that Herbalife targets, usually inexperienced and uninformed people regarding the stock market in the case of the penny stock or self-employment, direct selling or nutrition products in Herbalife's case. They are easily misled by the story of "changing your life" and "big incomes" from selling an unknown brand of vitamin pills, just as the penny stock victims swallowed the false story told by boiler room promoters about an unknown company that is going to grow explosively. And, in both cases, few will realize their plight even after they lose money. Most will never seek restitution or report the experience to authorities or even admit to friends they were duped. Most hide the losses in silence and shame.

The ability of the penny stock promoters to find new investors creates the illusion that the value of the stock is real. Earlier investors earn large returns. These "profits" are in fact capital gains that have been manipulated by transferring later investors' funds to earlier ones. The profit is

unrelated to the activity of the company whose stock is being promoted. Yet a mirage of a sustainable and viable enterprise is created.

Similarly, in Herbalife, the incomes paid to earlier investors appear to verify the story that the Herbalife “business” has value. The Herbalife video and the personal testimonials of the Upline about “big incomes” support the illusion. The evidence that retailing is not feasible is overlooked and only the potential of capital gains is now pursued. The penny stock investors also do not look closely at the story about the business activity and promised “growth” of the phantom company whose shares they now own. They are distracted by the rising stock price, and the promises of much greater growth. Few understand that the stock price increase has been manipulated by the promoters and is dependent entirely upon their solicitation of new investors.

COMPARING AND CONTRASTING THE CLASSIC PENNY STOCK SCHEME WITH HERBALIFE

1. The penny stock promoters “make the market” for their chosen stocks. The market is purely manipulated and is determined by their ability to find new investors. Share price is not determined by the actual business activity of the company whose stock they represent or any product it offers or service it may perform. The price of the share is not market-based and is not comparable to anything else on the market. It is arbitrarily fixed, non-competitive and the purchases are driven by a false story about growth and profit.

Likewise, the value of the Herbalife distributorship is unrelated to its alleged purpose and business model – selling weight loss products to distributors that resell them to end-users. The price paid by the investors, which includes the price set for the inventory, is also fixed and non-competitive. In fact, the retailing of Herbalife products does not occur on any measurable scale and virtually no Herbalife distributor earns any money from doing this. The only value that is developed and the only returns that are gained are derived from the recruiting of new investors. Purchases are also driven by a false story of profit and growth. Herbalife products, therefore, do not compete in the normal way with other weight loss products sold in the open market. The price is fixed and is inextricably bound up with income promises and claims. Sold in this way, consumers do no “price shop” because they are buying not just “pills, potions and lotions”, but an “extraordinary opportunity” that could “change their lives.”

2. The money transfer that occurs and is manipulated by the penny stock promoters is carried out under the guise of “selling securities.” No one actually pays the promoters or the Insiders directly. All the money is laundered as stock purchases and stock sales. The stock sales are said to be based on market demand. The boiler room and the price manipulation are invisible from the outside.

Likewise, the Herbalife money transfer is hidden behind inventory purchases that are required by the pay plan and related fees for Internet services, training, shipping, etc. These investments are disguised as “direct selling” and are claimed to be based on demand for the

products. The misleading income promises used to induce purchases and the associated reward system are invisible from the outside.

3. In both the penny stock and Herbalife the “last ones in” must ultimately lose. Those investors cannot ever recoup their money unless the schemes could expand forever, which cannot occur.
4. In both cases, the last ones in represent the majority of all that have ever been involved.
5. In both cases, the promoters – “boiler room” for the penny stock and Herbalife’s “upline” – gained their rewards from a money transfer based on capital investments. They both make money on the “spread.”
6. Neither the Penny Stock Boiler Room nor the Herbalife Upline delivers value because the stock and the distributorships respectively are inherently worthless.
7. The wealth of the Insiders in both schemes – the penny stock backers and the Herbalife Corporation – rests on the losses of the last ones in. There is no sustainable capital base. The value of the Insiders’ stakes in both cases depends entirely on the ability of the schemes to find new investors that will pay the fixed and manipulated prices for “shares” (stock in the case of the penny stock scheme, a distributorship that includes inventory in the Herbalife scheme). The Insiders’ wealth would evaporate immediately if new capital infusions were interrupted.
8. As the overall size of the penny stock scheme grows, the wealth of the Insiders grows correspondingly. The market capitalization of the penny stock scheme, for example, rose to \$5 million when the shares went to 4 cents (125 millions total shares issued) The initial 25 million shares was sold to the public for \$250,000 and was 20% of the total issued. When the stock reached four cents \$.04 the same number of share were worth \$1 million, making the Insiders value explode to \$4 million. To accomplish this, the number of public investors grew from 100 initially to 800 when the stock reached 4 cents in price. Each “level” of investor doubled in size over the previous one. Insiders gained all their wealth simply by sponsoring the “kiting” of worthless stock and being properly positioned as major equity holders.

Similarly, the Herbalife Corporation’s value and the wealth of its largest shareholders are based on the facilitation of the money transfer in the sales of the worthless distributorships. The number of distributorships grows dramatically as it moves from country to country.

The Herbalife Insiders’ wealth, like the penny stock backers’ is purely a “bubble” based on the purchases made by the last ones in. It would immediately collapse if a newer and larger group could not be found when that latest group and their distributorships are “dumped.”

9. The penny stock scheme eventually “dumps” the stock it has kited to take the final reward from the scam. Often the insiders’ stock is released to the closed market and the final group of buyers – representing the majority of all that have ever invested – is left with worthless shares. Some who rode the wave, and reinvested their money while adding new capital suffer larger losses. Many others at the end, having seen what appeared to be a verifiable record of

rising stock, purchase much larger blocks of shares. They suffer the worst at the hands of the penny stock promoters and their insider backers.

The penny stock scam appears to have ended but actually reconstitutes itself, sometimes under a different company name, and always with a new stock, another one promised to be “hot” and “going to be big.” The very same process is carried out with the new “product.” Often, many of the same investors that lost in the previous scheme, eager to recoup their losses and unaware of the scheme’s machinations, are enrolled once again.

Herbalife’s similarly, “dumps” its losers and their worthless distributorships. It carries this out without interruption or needing to rename itself (though some multi-level marketing companies do rename themselves, as in Amway’s new name, Quixtar, which was adopted when the Amway name had been widely sullied.

Herbalife’s “last ones in” lose *each year*. After the scheme has reached saturation points in most of its market regions – which occurred in most countries years ago – it continues to bring in more investors who face losses *immediately*. More than 90% of each new investing group discovers that it cannot pursue the publicized business of retailing and few can find enough new investors for them to recoup their own investments. They and their distributorships are “dumped”, and then replaced by a new group that will be similarly dumped within the next year. Effectively, Herbalife “collapses” each year and, like the penny stock scheme, resurrects with a new set of victims, some of whom are carried over from the previous period, still hopeful and unaware of the nature of the plan.

10. The viability of both the penny stock enterprise and of Herbalife depend on three key factors:
 - 1) The ability to continuously gain new investors, since the company has no sustainable business and offers no value in exchange for investments.
 - 2) The ability to maintain a disguise over the worthlessness of its alleged businesses – a “growth company” for the penny stock, and a retail-based “direct selling” distributorship for Herbalife. In both cases, news media investigations can be devastating and can trigger total collapse.
 - 3) The lack of any government regulator bodies – SEC, FTC state Attorneys General or regulators in other countries – investigating the business models, sales practices, and financial consequences of the operations for consumers or enforcing anti-pyramid scheme and consumer or securities fraud laws.

Addendum Two

Summary of Video Taped China Meeting

Part 1:

This video records the conversation among three gentlemen. One is a business representative, who introduces his business products, operation, and structure to the other two gentlemen. He tells them the company was started in 1980. The company's stock was offered on New York Stock Exchange in December 2004 with its current value at \$46 per share. The company has over 90 stores in China and two stores in every province. The company has two stores in Guangzhou, two stores in Wuhan, one store in Chengdu.

The company sells health-related products and has its own factory. The investor of one of the products is David Haibo (translated phonetically), who won Nobel Prize in 1998. The company sells products that can prevent heart problems, hypertension, diabetes, cancer, hypotension, anemia and also products used for weight loss, weight gain, and facial care. The products are safe and made from plants. The products are certified by the Ministry of Commerce of China. Everyone can use their products, including the elderly, children, and pregnant women.

A person who wants to join the company is required to have an ID, full-time working card from his/her factory, personal account, and 100 yuan to buy the company information material. After the person fills the application, the company issues a certificate to the applicant, who then becomes the company's business representative. The company is structured on a multilevel basis. The entry level is a business representative, followed by business director, senior director, manager, senior manager, and executive. There are 8 executives, 40 senior managers, over 100 managers in China. A senior director is required to have 10,000 points. A manager is required to have a total sale of 200,000 yuan for three consecutive months. A senior manager is required to have a total sale of 800,000 yuan for three consecutive months. An executive is required to have a total sale of 2 million yuan.

(Source certified Mandarin Translator summary. Full, certified transcript provided to law enforcement).

Addendum Three

Phone Taped calls from Employees and Distributors

Subject: HERBALIFE HONG KONG CANTONESE CONVERSATION PART 1

Please find transcript below of most relevant parts of the 40 minute call with Herbalife Hong Kong this morning:

Herbalife Conversation-----Quote to Herbalife_17Oct_HKdistributor_1

(In Cantonese)

C: Cathy (Investigator)M: Herbalife distributor ~ Maggie

October 17, 2007 (9:45am)

09:45~09:52

M: I feel so surprised. Why you want to be our distributor suddenly?

C: Actually the main point is I have a lot of relatives & friends in China. They are very interested in Herbalife. They want to be the first one to join.

M: Well, I just back from China. Honestly, it quite disorder in China. You know, because lot of things is out of control in China

C: Yes, I know it.

M: Even we have a office in China, we are a big company, but some distributors still doing bad thing.

C: I see. May be it quite hard to control.

M: Yes, we have lot of rules but they still to become absolutely lawless. So you are in Hong Kong, the simple & direct way is? you know, the plan is different between China & HK. HK have an international rule, but China have they own rule. **For example, we are the supervisor, we have 50% benefit, but in China they only have max 35%. They should purchase products with original price, but we have discount. But actually, we will rebate to them**

later. Because they are not allow to do this, they have the rules, they need to do this to avoid the Law.

C: Yes, my friends in China tell me that they have a lot of rule.

M: You can register in HK, and then give them your ID #. They can purchase product in China. And it's good for you, coz you can get the rebate from them. We have different level, like Kendo, he is the normal one member? He can get only 25%. Upper one is distributor, can get 42%. For supervisor, they can get 50% discount. For long term, it better to be a supervisor if you want to get all benefit from Herbalife. For example, if your China friends purchase products under your ID, you also can get the rebate from them.

C: you mean?

M: They don't have benefit in China. They have to give out around \$50,000 to be a supervisor, but of coz they will get 15% rebate of \$50,000 back within one month. Also, they cannot sell the Hong Kong Herbalife product in China

(Conversation is not relevant from 09:53-09:59)

10:00~10:01

C: Can my friend sign up in HK?

M: They are not allowed to do this. Let me double check for you.

(Conversation is not relevant from 10:02-10:03)

10:04 ~ 10:06

C: How can I get the commission?

M: Cheque or autopay. If you get the commission from your China friends, then you will get US dollar. Otherwise, is HK dollar.

C: How about my friend in China?

M: They must to open an account in ICBC, the only bank that we accept.

(Conversation is not relevant from 10:07-10:13)

10:14~ 10:15

M: You know, the highest commission you can get from Herbalife is around 73%.

C: My friend in China?

M: Only in Hong Kong.

(Conversation is not relevant from 10:16-10:22)

10:23 ~ 10:24

C: Okay, let do review to make sure that I am not getting the wrong message from you. First, I have to sign up in Hong Kong and my friends from China? They cannot sign up in Hong Kong?

M: Yes.

C: Cost around \$35,000 to be a supervisor in Hong Kong & around \$50,000 for my friends in China?

M: Yes.

C: Commission?

M: They can only get around 15-25% commission. **For the membership (supervisor), they have to give out \$50,000 first, but they will get the rebate after 1 month, there are around \$15,000. So they are only have to pay around \$35,000 in total.**

(Conversation is not relevant from 10:25-10:27)

10:28 ~ 10:28

M: Because they are not allowed to buy in discount price, it will become (Trans. MLM). Which is not allow in China. **So they have to pay original price first, then rebate to them later.**

(Conversation is not relevant from 10:29-10:29)

10:30 ~ 10:31

M: **Also don't mention the policy of HK Herbalife in China. Coz it's not allowed.**

C: Can my China friends get more commission?

M: 35% is max. I will double check for you.

(Conversation is not relevant from 10:31-10:32)

10:32 ~ 12:32

C: One more thing, they have to sign up in China?

M: Yes. I will double check.

C: Is it possible to do it on internet?

M: No.

(Conversation end)

Subject: 9/10 HERBALIFE SINGAPORE ENGLISH & CANTONESE CONVERSATION (8 OCT 2007)

Herbalife Singapore Conversation

(in English & Cantonese, 8 Oct 2007) -----quote to C003 Herbalife Singapore 8 Oct 2007

C: Cathy (Investigator) Z: Herbalife ~ Zen

C: I want to join Herbalife. What is the procedure?

Z: How do you know about Herbalife?

C: My friend told me.

Z: Your friend is our distributor?

C: Actually no. But she is using Herbalife products.

Z: The customer?

C: Yes

Z: Are you currently stay in Singapore?

C: Yes.

Z: What you can do is drop by our office.

C: You will introduce a sponsor to me?

Z: Yes, a lot of distributor around at the office, you can talk to anyone. When you are feel comfortable, you can sign up.

C: I also want to ask, some of my friends who is living in China. They can be my down line after I join?

Z: For China, they can only do the business in China, join in China. Cannot make purchasing in other countries.

C: **So they can be my down line?**

Z: **They can still be your down line**

C: **How to get my commission? I need a bank account in Singapore?**

Z: **Correct.**

C: **How about my friend in China? How to get the commission?**

Z: **They will get the check from China office.**

Subject: 8/10 HERBALIFE GUANGZHOU CANTONESE CONVERSATION (5 OCT 2007)

Herbalife Guangzhou Conversation

(in Cantonese, 5 Oct 2007) -----quote to A006 Herbalife Guangzhou 5 Oct 2007

C: Cathy (Investigator)?? M: Herbalife ~ Ms. Man

C: What is the procedure if I want to join Herbalife?

M: You have to provide your identity card & bank account. Also prepare \$100 for company brochure & sign up form.

C: I have lot of my friends are very interested in Herbalife business. So they will become my down line?

M: Yes, they can.

C: Is it a lot of people doing Herbalife business in Guangzhou?

M: Yes, a lot.

C: Well, I want to get more information about Herbalife

M: How about you come to our office for detail?

C: Ya. And I want to know how can we get the commission?

M: It depend on how many products you bought and which level you are.

C: So do you mean that you want to have a meeting with me for the further information?

M: Yes.

C: Um So you will pay me by cheque or bank in to my account for the commission?

M: Every 20th, we will bank in all commission to your account.

C: How about my down line from HK, Taiwan?

M: If they want to get the updated and right information, I suggest they register in their country. Just write down you are the referrer is fine.

C: Taiwan?

M: Taiwanese can only register in Taiwan. I am not sure is Taiwanese can refer by China peoples.

Subject: 7/10 HERBALIFE TAIWAN MANDARIN CONVERSATION (5 OCT 2007)

Herbalife Taiwan Conversation

in Mandarin, 5 Oct 2007) -----quote to A007 Herbalife Taiwan 5 Oct 2007

Cathy (Investigator) H: Herbalife ~ Ms. Hon

C: What is the procedure if I want to join Herbalife?

H: You have to refer by distributor.

C: But I don't have any distribution refer me. What can I do?

H: So do you know any distributor in Taiwan?

C: No.

H: In this case, we can introduce our senior distributor to you.

C: I see.

H: But we do not accept any people who are hold the China passport.

C: I understand

C: Ok, if I join Herbalife in Taiwan, but my down line is from HK & China, is it ok?

H: Yes.

C: How can I get the commission?

H: If you are taking HK ID, then our office in HK will transfer money to your bank account directly.

In Taiwan area, we all pay in US dollar.

C: um

H: If you earn money out of Hong Kong area, then you will get US.

C: They will bank in to my Hong Kong bank account?

H: Yes.

C: Is it possible to bank in to Taiwan bank account?

H: **First, you have to provide Taiwan address and you have to pay tax if bank into your Taiwan bank account.**

C: **I see. How about my friends in China?**

H: **Our China office will send them money. Not from Taiwan.**

Meanwhile, please find transcript below of most relevant parts of the 20 minute call with Herbalife Hong Kong this morning:

Herbalife Conversation-----Quote to Herbalife_17Oct_HKdistributor_2

(In Cantonese)

C: Cathy (Investigator) M: Herbalife distributor ~ Maggie

October 17, 2007 (11:55am)

11:55

M: I check for you, China people only can sign up in China.

(Conversation is not relevant from 11:55-02:56)

11:56

M: Actually, only \$100 your China friend can be Herbalife member, but only buy & sell product, cannot get commission from their down line, they will not have down line.

(Conversation is not relevant) from 11:57-11:57

11:57 ~ 11:58

M: **Once again, remember don't tell anybody about your HK Herbalife plans or rules, otherwise somebody will accuse you.**

C: But why?

M: Accuse you are talking about ?? (Trans.?MLM)

C: But I am only talk about this, not to do.

M: **No, you can't mention this.**

C: So it's legal to do in HK?

M: **Yes, of coz. Just don't mention in China, may be someone will misunderstanding you are working on?**

(Conversation is not relevant from 11:58-12:00)

12:00 ~ 12:01

C: **Besides commission, do we have any other bonus?**

M: **Yes, if you can archive the sales. You will have bonus and level up too.**

C: **Same in China?**

M: **Yes.**

(Conversation is not relevant from 12:01-12:08)

12:09 ~ 12:10

M: Tell you, you can be a distributor first, pay \$10,000 to be a distributor, no need to pay \$35,000 to be a supervisor. Once you sign up, you can ask your friend sign up to be a supervisor with \$50,000, then both of you two are supervisor too.

(Conversation end).

**Addendum Four
Herbalife
“China key growth market”**

Herbalife Sponsor London Triathlon

Is Herbalife the "Best Business Opportunity in the World" ?

Highlights:

- Obesity and Diabetes Epidemic Worldwide
- Products proven over 25 years, with million plus testimonials on file
- Wellness market expected to increase 5 times in the 8 years
- Herbalife sales increased 21% in the last quarter. Quite remarkable growth for a company that has been around since 1980
- Malaysia and China are key growth markets for the company. Help us develop the Chinese market from Malaysia?
- Massive Herbalife awareness campaign via Sponsorships
- Support provided by BIG Marketing, with permanent staff in KL.

Addendum Five

HERBALIFE RECEIVES ADDITIONAL ACCESS IN CHINA

**HERBALIFE.**

Herbalife Ltd., a global nutrition direct-selling company, announced today that it has received a direct-selling license from China's Ministry of Commerce to conduct business throughout the entire Jiangsu province. In March 2007, the company received permission to conduct business in just two cities, Suzhou and Nanjing.

Located on China's east coast, the Jiangsu province, consisting of 13 cities with 61 counties, has a permanent and transient population of approximately 85 to 90 million people. Cities approved are Nanjing, Suzhou, Xuzhou, Lianyungang, Suqian, Huan'an, Yancheng, Yangzhou, Taizhou, Nantong, Zhenjiang, Changzhou, and Wuxi.

Herbalife currently operates 47 stores and 37 service centers in 28 provinces in China. The company operates a unique direct-selling model in China in accordance with local regulations, where our supervisor-level distributors are employed by, and conduct their business, in retail locations owned by Herbalife China. Consumers and other distributors come into the store to buy product and learn more about the business opportunity. In areas where the company is licensed, distributors will be allowed to conduct business outside of the store.

Headquartered in Shanghai, Herbalife sells more than 35 products in China. The company operates its own manufacturing facility in Suzhou, China, that produces products for local use and export.

Herbalife is affiliated with, and plays an active role in a large number of industry trade organizations, including The World Federation of Direct Selling Associations, the Federation of European Direct Selling Associations and 40 individual Direct Selling Associations globally.

Addendum Six

In-Person meeting in China Herbalife Office

Introduction to the roles

A : Xiao Tang's boyfriend

M : Mandy(female) is the wife of Peter.

B : Peter (male)

C : Xiao Tang (female)

Z : Sister Jane (female)

A: This is the way of making money!

A: Hello!

B: Hello!

A: How do you do ?

B : How do you do ? How do you do ?

M : How do you do ? This is my husband Peter. I am Mandy.

A : You are Mandy, aren't you?

M : Yes. Have a seat, please! Have a seat, please!

A : This is my girlfriend. You may call her Xiao Tang.

M : Xiao Tang, how do you do? Have a look at the photos of our activities.

A : How many days of the activities did you perform?

M : Three days.

A : Three days, right?

B : It should be two days. Have a look at the photos of the activities we performed in Qingdao.

M : This is our partner, Sister Jane.

Z : Yes! Yes!

M : This is the result that she reduced weight by 14 kilograms.

A : Oh. She decided to do this business after reducing weight, didn't she?

B : She was a manager of Perfect in the past.

Z : Yes.....

M : This was the status 7 years ago.

Z : This product was used while I was breast-feeding the baby.

B : This is my mother. This is me.

M : This is me while I was 22 years old.

B : This is the photo taken 12 years ago.

M : This is the time when we were in love.

A : Ha, ha.....

B : This is the biggest in China, and in Taiwan.

M : The biggest in all the Southeast Asia.

A : Oh.

M : It was in Taiwan. All redundant weight was reduced. Excellent.

B : In addition, this is a world record.

M : The man who was taken picture of with him was our president.

B : This man.

M : This man.

A : Oh.

M : This is our president. Our president had reduced weight by 20 kilograms. Now looks pretty young.

A : Oh.

M : I thought he was just over 30.

B : He was over 30. Somehow he made his skin looked like this.

A : How long did it take for him to reduce weight?

B : Three months.

A : Three months?

B : Yes, three months. Approximately. It is mainly due to the effectiveness of this product. General products will not be so effective as it is. Then, for breakfast and supper each day, balanced nutrition is very important. Redundant fat within the body is burned. It is impossible if you understand this principle, isn't it?

A : In fact, I come here because I have already checked the primary first phase information of these products. I searched some information about the products online.

B : Yes. Yes.

A : I used to sell other brands of direct marketing, too. In these years I also sell many brands of direct marketing. I have been primarily involved in the sales of almost all brands appearing on the market. I understand these systems. I come here because I only want to know what the systems are about. The remuneration system is comparatively advanced within the industry. So, I want to know this segment. I want to go to the company today to look for Zhou Fang,, my former colleague because Zhou Fang was my managing officer when I worked in Avon. I also operated an Avon franchised store by myself. Later, I was also engaged in the sales of Amway brands. I was engaged in the sales of every brand. I sold Amway brands. I also sold Perfect brands and every brand.

M : I also sell Perfect brands.

A : But as far as Perfect is concerned, my mode of sales is unlike yours. My mode of sales is unlike that of Perfect and Amway. I replenish the stock of goods in bulk and sold them in a traditional way. The discount obtained by us for the sales of Amway products was very, very low, too. However, the sales volume of goods was roughly the same as that of diamonds. That is to say that I directly replenish the stock of goods, sold the goods and deliver the goods. Up till now, no direct marketing method has attracted me and made me make efforts to perform it, no matter what kind of method it is. I have many primary sales outlets and terminals below. In regard to these personnel and their sales volume, that is to say, the customers around them have already got accustomed to buying these stuffs. So, we count it according to discounts. Then we give them higher discounts. That's it and the sales volume is large. So, I understand every aspect of the system. But I have no time to do this business. So, if it is possible to sell the brands of Herbalife, I want you to join me to sell the products leveraging large volume.

B : For this, I feel to some extent that we can only succeed by luck. This is unlike the ways of other companies. But some health products sell well and some don't. If you take them home and eat them, some will neither become fat, nor thin and nor die.

A : Will Herbalife cause death?

B : Why do we select Herbalife? Why not come to our place here to sell it? It has market potential absolutely. With the support of advertisement, the products will be sold out right away.

A : En.

B : Because this mainstream product of his has the functions of increasing and decreasing weight as well as health care. The effects vary depending on the method of eating it. For example, I sell it in a supermarket. Consumers make a mistake by eating the product of increasing weight as the product of reducing weight or vice versa. This is the different effect. How can I say.....If you really want to sell Herbalife, you must be in good faith. Let me say something about my background.

A : Which one?

B : I was born in China and my monthly income amounted to RMB100,000.

A : Oh. I see.

B : What happened to me later? For family reason, I left China. I lived in Hong Kong then. Later I was promoted to a position of working in China. I saw the prospect of development in China. Do you know this system?

A : Yes, I do. This system is approximately like this.

B : You see. Think of it.

A : This system, that is to say, varies substantially in kinds, including all kinds like those of other brands.

B : Telling the truth. The scheme I consider is conservative. My purpose of doing business is not to simply operate a store and to make a certain amount of money. I have no time to consider this. I am 46 now and unable to bear running out of money at 70.

A : Yes, it is.

B : Each president earns such income in the amount of RMB300,000 to RMB400,000, or at least RMB200,000. Think of it. In Guanxi, my current monthly income amounts to RMB20,000-50,000. I actually closed down my garment store only three months ago.

M : It was closed down last month.

B : It was operated for a whole period of half a year. This brand should be at least operated by the most excellent people. This time it depends on your method of operation. If you adopt a traditional method, you are doomed to failure.

A : En.

B : Because it was made in the same one method across the world in a span of 26 years. It requires a group of huge markets at the beginning of the business. Let's look at the existing weight loss companies. Which one has succeeded in business so as to rank among the top five? No one does. Why? Because the products are not good enough.

A : En.

B : For example, when the products of Sibutramine were sold, the sellers said bye-bye and went away. Why has this product been used across the world for 26 years? Because it is armed with very excellent after-sales service. This is the nutriment well supplied and consumed. I can warrant that after eating this product, you will feel and see the effect. It is possible after 5 years, 10 years or 20 years, too. You may see the quality of the products of Herbalife. Is its external shape attractive?

A : No.

B : BMW and Benz are excellent products absolutely not because they have a beautiful external shape but because they are manufactured with top technologies. Could you ask the personnel within the company why Benz sells best? When you have made lots of money, you are surely to choose Benz instead of BMW. It is the same in the domain of health products. As you know, the production and sales of counterfeit goods are rampant in China.

A : I would like to have further knowledge of its system.

B : Okay.

M : Some people came to visit us, wanting us to supply some cheap products. It didn't matter that I supplied the cheapest products in terms of my capacity. But I am worried about the reputation after the

sales of products. This is one simpler version of ours. In terms of levels, the lowest is business representative, then it is director. This means a period of within one month. Appraisal is performed on monthly basis. The management ability of the level of manager or above is appraised for a period of three months. As far as business representatives are concerned, their personal volume (PV) are reduced to zero each monthly and the commissions are awarded in proportion to the amount of monthly sales. The amounts of sales are divided into the levels of 1,200 to 6,000, 6,000 to 12,000, 12,000 to 30,000, 30,000 to 48,000 and above 48,000. You may find a partner to cooperate with you so as to reach this level by completing the sales amounting to 30,000 each.

A : Do you mean to count the total PV of two persons?

M : If the PV of one person is counted, it is 48000.

A : It comes out to be double 30000PV if the total PV of two persons is counted, doesn't it?

M : Right. The amount of PV. The PV is 2500 points. Then assume that one person has 4000 points, there is one quota for 4000 points. If there are 5000 points, two quotas are available. If it is evenly divided, there is 30,000.

B : Then 27% is obtained for the first time. When you are promoted to the position of director, you obtain 30%. Like this.

A : That is to say, all PV is reduced to zero before being promoted to the position of director?

B : Right. That's it. The lowest level is the business representative.

A : Unless you are promoted to the position of business director.

M : Generally speaking, the director is also eligible to obtain 5% management bonus of three generations apart from 30% profits. That does not mean that you are to be awarded bonus for doing nothing. According to the stipulations, when you gain 500 points, you are awarded 1% of the three generations; if you completes the sales of 12000 and gain 1,000 points, you are awarded 2%; if you gain 1,500 points, you are awarded 3%; if 2,000 points, 4%; if 2500 points, you are awarded all bonus.

A : That is to say that even you have been promoted to the position of director, you are still required to gain 2500 points of PV, the primary requirement for the business representative, right?

M : Right. It is approximately RMB30,000. This point is not the point done by you alone, rather it is done by you and the business representatives below you.

A : It is the business achievement to be made by a team.

M : Yes. That is to say that the director is excluded because once he is promoted to the position of director, he cuts himself off from you. You are the division and the achievement is the achievement of the division.

B : It is your division.

M : Belongs to your division and your division is at the level of a team.

A : That is to say that after I become a director, the persons recruited by me.

B : The persons recruited by you?

A : Yes. The person recruited by me. That is to say that I recruited three of you. If the points gained by three of you total 2500 points, full points have been gained. Then I do not need to contribute any points.

M : Yes.

B : Yes, provided that three of us are all business representatives.

M : Yes. You do not need to gain even one point. You are eligible to obtain all bonus.

A : En.

M : The director of this level receives the business bonus of limitless generations. I feel that 5% bonus is received.

A : The three generations mean that I recruit you, you recruit her and you recruit her again. Each means 5%, doesn't it?

M : Yes. If the points do not exceed the quota, you are not the first generation. For example, I am the first generation and I have gained only 300 points instead of 500 points. Then I am regarded as your first generation and he is your first generation.

A : You will not be regarded as one generation unless you gain 500 points.

M : Yes.

A : What happens if the points he gains fall below 500 in the second month? That is to say that he fails to gain 500 points in the second month.

M : He should not be one generation.

A : He shouldn't be one generation, should he?

M : Assume that each of previous three generations gains 300 points and the fourth generation gains 2000 points, and the fifth generation gains 2500 points. You may receive 5% from the previous three generations, but they are not one generation. Only the fourth one is your first generation. He gives all points to you. So, it is very fair as the points are compressed. One generation can provide 10,000 points. That is to say that when you recruit four directors in one month after you are promoted to the position of director, you become a senior director. Or if in the four consecutive months 4500 points are gained each month, you become a senior director. So, 2500 points are very important. All bonus below may be available. If one is promoted to the level of senior director or above the level of director, the income of over three generations are available. At the level of business manager, at most one month of examination on the business manager is performed. That is the business achievement of your team. That means those people who cut themselves off from you and become directors. If their business achievement is of within three generations, and they gain 20,000 points, you may receive 5% in addition to the points of three generations. After the examination covering three months and from the fourth month onwards, you are officially promoted to the level of manager. By the fourth month, you are eligible to receive 1.5% in addition to the business income.

A : That is to say that after I become a business manager, apart from receiving all 5% of A, B, C, I am eligible

M : To receive another 1.5. You may also receive 1.5.

A : That is to say that A, B, C receive 6.5. D and recruits after D all receive 1.5.

M : Yes.

B : Your income is RMB60,000 as I just said.

M : Yes. If after the examination on the total amount your business achievement of no more than three generations reaches 80,000 PV, then your administration bonus is 8 , 5+3. The income of that level amounts approximately to between RMB60,000 and RMB150,000.

A : The administration bonus of business manager is 5+1.5+3 if the business achievement is that of previous three generations.

M : No. 5+3.

A : Is he ineligible to have 1.5?

B : No.

M : Yes. 5+3.

A : 5% for the previous generations is assured, isn't it?

M : Yes.

A : That is to say that the following generations are ineligible to have it.

B : You add your own functions.

A、 B : Ha.....

M : Anyway when you become a business president and the business achievement of the first three generations reaches RMB200,000, you will be able to receive the administration bonus of 5+4.5. Your income is approximately over RMB150,000.

A : En.

M、 A : The case of the highest income is in the Northeast China where one recruit receives approximately RMB500,000.

M : After one month, one star president will appear. If you are a star level president, you may receive this amount of income. If I train you to be a star level president, I will be a one-star president. If I train another recruit to be the president on the second line, I will be a two-star president.

A : You mean that so long as a recruit is trained by me, no matter which generation he belongs to, he can become a president.

B : Business president.

A : So long as he becomes a business president, I will be a one-star president. If there are two, I will be a two-star president until.....

M : It is not like this. There is only one star on the same one line.

A : Oh. The same one line.....

M : Assume that you are my first generation. From you onwards there are five stars below, then I am only a one-star president. But you can surpass us, Assume that there are three presidents below you, then you are a three-star president.

A : Yes.

M : Then I am only one one-star president because I have only one line of president of yours. It is pretty fair.

A : This is that one has surpassed another.

M : You have surpassed me. No problem. In Hong Kong, there is one one-star president below whom there is one three-star president. There is also a special scheme of bonus distribution for China region in China. The persons at the levels of chief officer and president all are eligible to obtain 1% bonus distributed for China region. As the sales in China amounted to RMB300,000,000 last year, RMB3,000,000 was allocated to chief officers and presidents. And there were 19 chief officers and 2 presidents last year. Over RMB300,000 was allocated to each president and at least over RMB100,000 was allocated to each chief officer. The charm of Herbalife is here. It is a listed company and its bonus may not be withheld as deposit. All the bonus must be distributed out. Yes. A five-star president may become a member of the board of directors and is eligible to enjoy the yearly vacation of the company for free.

B : Do you know that we went to attend a meeting this time? We saw that Herbalife had created so many things in our China. We saw Herbalife was able to create so many things in China. Herbalife provided a wide range of over 60 kinds of products across the world.

M : This was the party of manager level we went to attend in Qingdao. Speeches were made in a span of several evenings. We were granted the award as the top five in the sales of individuals in the three regions of the Mainland China, Hong Kong and Taiwan. It is the culture of Herbalife that if you have obtained this award, the company will give you a significant treatment.

A : I see.

B : Do you understand? To be invited by the people of Hong Kong, the supreme leaders of the company, to attend a feast is an honor.

A : I understand this.

M : The number one among the Chinese across the world.

B : After graduation from the university, he began to work. He used to work as a reporter after graduation. He had no knowledge of Herbalife at the beginning. Later, he succeeded in this business until becoming number one among the Chinese.

M : He is a seven-star president.

B : There are over 20 altogether. He prepares to become.....

M : One of the founders.

B : When chatting with him, I was the fifth generation below him. As we are on this position, our brilliance was self-evident. He was really an old shareholder. If you happen to meet him on the street, you

will never say he is very capable. But the system is of the first class. So long as you perform business this way, you will surely succeed.

A : When I search this information online, I actually asked him why he did not operate a store. He replied that he found no proper location. How would it be rated in China now if he did?

B : Very good! Our team was rated the third of the Store in the Air in three consecutive months.

A : I have no Store in the Air. Isn't his store an office?

B、M : Yes!

A : Then isn't your store an official store of Herbalife?

B、M : We are one service outlet of it.

B : We maintain a very good relationship with the central office. I don't know other places. In the past several months, namely, July and August, we maintained very good relationship with the Office of External Affairs. We have an office of external affairs which is responsible for keeping good relations with the government.

M : Have you met Chen Xi today? He works in the Office of External Affairs.

A : The Office of External Affairs is very normal. Each direct marketing brand has a place for external business.

M : The Office of External Affairs means that for example, no meeting is to be held in July and August. What business is cancelled will be notified. At each meeting, we will scrap some products.

B : Zhou Fang has been the managing officer of this company. We are much comfortable doing business. But our Herbalife

A : But I feel that quite a few things went wrong just after Zhen Au obtained the license. That is because we are now the dealer of Avon, which is engaged in direct marketing, too. It is just like what you said that we attended many meetings. Over four years have passed. At that time I also went to attend the meetings, such as to go to Hong Kong and Singapore to attend the meetings. I used to do business in these fields. I believe that each direct marketing company will give awards to each staff member and encourage him to make efforts. And what I am concerned about is that the company's policy in China changes too quickly. As Avon is a docile company, it is the first to obtain the license among a group of companies chosen for pilot operation. I am very confident on Avon. In fact, I feel that among the big five direct marketing companies of the United States such as Amway, Herbalife, Mary Kay, Nu Skin and Avon, in terms of their operation in China, the company which enjoys the highest reputation and has been operating the business for the longest time is Amway. In terms of the size of the network of outlets, Avon is number one. Herbalife is a late comer. What I am concerned most is the relations with China. I have been concerned about it all the time.

B : Herbalife has already made investment amounting to over RMB840,000,000 in China. Which company dare invest so much money in China? But could you think of the stores licensed by Herbalife and look at the importance attached by it? You should think of it from another angle. You see why Amway keeps on operating direct marketing? Amway has never stopped its direct marketing, never.

A : Did Herbalife operate this in this period of time, too?

B : If it begins this business now, it will lag behind substantially. Herbalife is very docile, too.

M : It does it temporarily, too. But why does it always perform business in direct marketing cities? The actual reason is that it encounters problems in service. This product requires the person-to-person service. It officially launched its operation and started to do this business after making sure that it would obtain the license. Otherwise, think of it that it built its factories in 1999 but only officially brought the direct marketing mode into China in 2005.

A : But did Herbalife do business based on the system such as this before 2005?

M : No.

A : Since 2005, the company has given tacit approval to this model anyway.

M : No. It officially entered China in the form of direct marketing model in September 2005.

A : It entered China in the form of direct marketing model because at that time the state had not approved it yet. The Direct Marketing Law was made in February 2005.

M : It obtained the license in March 2006.

A : It obtained the license after Avon. Avon obtained the license in February. What I am always concerned about is that it doesn't matter for Avon as it performs one-level while others such as Amway or Herbalife have to re-return 50% or even higher rather than 30% as they perform multi-level.

M : No. Actually our current public opinions don't vary. We now perform the business in the form of business done by staff members.

A : Does it actually belong to a kind of multi-level?

M : We now perform the business in the form of business done by staff members.

A : To do it in another method in which business is done in the names of staff members.

B、M : Yes. Yes.

B : Oh. You are Chinese and you have to comply with China's policy.

A : You are also Chinese, aren't you? Ha.....

B : I was born in China and I should also understand Chinese. Such as the hotels in China, the business cards of all Chinese hotels have English translation because if the Chinese law wants this sector to die, it will immediately.....

A : That is what I am concerned about.

B : What will die is the entire sector.

A : If we are going to die, we all die, right?

B : You understand me and I am conservative. I am also concerned about this. However, the large wheel keeps on rotating and can not be stopped. It keeps on developing its business in view of the entire sector. I know the system you are talking about. The problem is how to do it. I feel that it is related and designated. Only over 20 are involved in direct marketing. If it treats foreign patients in a foreign country,

you and I are treated in the same way no matter where you and I are. All have to do business in good faith. So it is impossible for an American company to say that I only do business with a Chinese company. If you say that it wants to do business with Herbalife, it is possible because Herbalife has plants and Amway doesn't. We and the staff members working in the plants total 10,000. Could you undertake the pressure from this public opinion? Do you understand? That is which is more important to some extent and which is more high-handed. If you owe me money, it is impossible for you to kick me away. I only analyze these points.

A : It's impossible.

B : You should look at risks and you should have a unique point of view. To view it from a different angle. No company will make money if they perform business in accordance with the Chinese laws.

A : Actually I feel that after each company obtains good stuffs, obtains good products, it sells them through recruits. In a nutshell, all companies sell products through recruits.

B : Yes.

A : It is except that the management of their company do not want to say it out. So, I now want to know something about the system administration of their company. I am going to contact somebody working in the company instead of a dealer. So I want to visit an old friend. He has traveled on official business. That one working in the office of external affairs as said by you frequently uses official jargon. He said that we were working for the boss. Ha.....He said that in terms of the system, you could go to contact dealers. If I asked him, he would say 30%. As he refrained from continuing talking, he told me to contact dealers.

B : Yes. He won't tell you the truth. But you know that Herbalife has 73% across the world because the founder of Herbalife has relations with China. All the agreements were made by him one by one with the Chinese counterparts from a lower level to a higher level. So the corporate system aims at servicing dealers. Think of it that no company does the business this way.

A : That is to say that after he obtains this product, he raised the price by several times and by four times. Three fourth is set aside for the distribution for the direct marketing model level by level. It is done this way.

M : In fact the products of all direct marketing model themselves only take account of 50%.

A : I know this. In fact as I think of so many contacts I have Herbalife is just like this. It depends on how many recruits you have on down line.

B : Wrong, Wrong, Wrong. I feel that Herbalife is special in one aspect. Each one wants to sell goods and he should know how to sell goods. It is crucial. Even if you have been promoted to the position of president, you have to have the record of retail in order to obtain bonus each month.

A : Actually if he is promoted to the position of president and the business achievement is supported by the team, he does not need performing retail.

B : Yes. Yes.

A : In fact in theory retail is required, but in reality if he is promoted to that level, he does not need performing retail.

B : But the junior manager of ours is required to make this business achievement each month. Each month. You are required to make the business achievement of RMB30,000 absolutely.

A : If you fail to sell out goods in this process.....

B : But I really have customers. If you don't have a large number of customers, you won't be able to keep this business. How can the person above talk about high income? Do you understand?

A : I do.

B : So, I feel that Herbalife has been so healthy in the last over 20 years because each one it required to work effectively. It's impossible for me to be a president for doing nothing here. He is finally responsible for quality control. Think of it that you sell products alone each month. Why does Amway fail to make good business achievement? Because you don't have the business of retail. It's impossible to do this by paying money out of one's own pocket. That's why each of us should perform retail. When you have a group of friends as customers, the business will be very stable because each staff of Herbalife starts his business from the bottom. Why do 7 million people in Hong Kong select Herbalife in the 28 years of its operation? This is the choice selected by each.

M : Because it is very easy for Herbalife to retain customers. Because you really see the change of your skin color by eating it.

B : After you eat Herbalife, you will gradually feel the effect.

Z : Let me have a try by eating it.

M : Not to mention eating it for a year. After you eat it for a month, there will be a change in your waist. Sister Jane has eaten it for four years.

Z : Teaten 20,000 Herbalife.

M : She suffered all kinds of illnesses. She was unable to run. It was really moving. You see there are many moving stories about Herbalife. During the chat in my own QQ, for example, he said in the past that I was also a manager of Perfect. Why did I switch job to work for Herbalife? I said that you did not need to do it I said that you did not need to do it. It was enough for you to use the products by yourself. After he used it, she became thin. She was over 40. She said yeah! Then I asked you if you had ever said yeah like this when you worked for Perfect. Then she said that she would come to work for Herbalife. And it is very easy for Herbalife to attract those like us who are moved by the products rather than eyeing direct marketing at the beginning but later come in to do business. And they also insist on doing this business. Even if you are a client referred to by another client, it will be difficult for her to switch the job to do other ordinary business. Like Sister Jane, it's even impossible to dissuade her from stopping eating it. She will eat Herbalife all her life because by so doing she will be young and beautiful.

B : I have a team at the bottom working in the rural credit unions in Yunnan. Her income amounts to RMB2000 to RMB3000 each month. She said that I had the income of so much money. She has such high income though she works part time for Herbalife. Her total income should amount to RMB5,000 to RMB6,000. The manager of her rural credit union is even unable to match her.

A : Earn only RMB2,000 to RMB3,000. She should only be a business representative.

M : That is 30% of all business transaction she makes. If she makes business transaction in the amount of RMB10,000, she is able to earn RMB3,000.

B : They all have their own divisions. Each division at the bottom has RMB2,000 to RMB3,000. So can't you say it isn't easy for survive?

M : And she won't leave at all, and she keeps on performing retail.

B : She won't leave in her entire life and she will work for this company all her life.

M : And she will do more and more wonderful job until it is useless to talk about the idea if there is no money to support you.

Z : Right. Where are You walking slowly while being hungry?

B : But, you should be very far-sighted and keep on doing this for ever. It is no problem to obtain RMB35,000,000 in over ten years.

M : If you keep on working for Herbalife in good faith for 3 years, you may be promoted to the position of president. If it is slower, it will take 5 years. If it takes you 5 years to be promoted to the position of president and to receive RMB150,000 per month, are you willing to do this job? Herbalife is one of the simplest companies. When you use the product, you should act as a spokeswoman of the product. I assume that it takes 5 years for you to become president. Are you willing to spend this time? Assume that Herbalife has only three kinds of products. You go to attend Herbalife's meeting. All successes will teach you. No things are special. Herbalife only requires you to use products in good faith. Even you attend a summit meeting, nothing is special. The same thing is talked about. Take how to do the business of retail for example, I have many ways to do this. Take me for example, I like to perform interviews in the city on weekends very much. I carry question sheets and ask questions whenever I meet a person. I feel at the bottom of my heart that I am saving you and I don't feel disgraced. If you did not meet me in your life, you would be always such fat and wouldn't be beautiful. In this case you will be in trouble. Another example is that today when I was on board of the airplane that gentleman in the air especially came to me and called me back saying that could you come over as one girl wanted to loss weight? Actually it was that gentleman who wanted to loss weight. He was shy a little bit and it was not that girl who wanted to loss weight at all. I mean that Herbalife is very attractive. Though we are receiving therapy due to illness or cardiovascular disease, weight reduction is always our focus. If you are fat, others will see it. If others suffer from some illness like heat disease, others will not see it. If you directly ask others if they suffer from illness, others will feel that you are in mental disorder. So there is a good opportunity for Herbalife to start talking. After you start talking on the topic, you can gradually chat with her about how to become young and beautiful. Take me for example, I also tried to loss weight first. After eating it, I found that I became more energetic and my skin color improved. Then I was unwilling to stop eating it and gradually I would like to become your long-term client. One of her clients worked in Nanning. After talking with her, she came to meet me. After contacting me, she made her son eat it first. She bought a vehicle at the price of over RMB400,000. She herself was reluctant to eat it and made her son eat it first. She was reluctant to allow her son to go to the school because others would call her son fat boy when meeting him. Her son reduced weight by 15 kilograms in two months. Her son was fat and inactive. After he lost weight, he was very active in class. He felt that his product was simply wonderful! It can even change her son's living habit. He has become very active. Then she starts eating it herself. Later, she introduced this product to the children of her two relatives.

B : One is 9, the youngest client of ours. Then his parents were moved due to his successful reduction of weight. And later they wanted the father to increase weight.

A : Is it possible to increase weight?

B : The method of increasing weight is to increase diet. The same kind of products requires different methods of eating it.

M : So you see that it is easy to make clients order Herbalife again. So I asked her if you can become a director? Your son has already eaten over 5,000. Her son called me from Qingdao, saying that he would set up a weight controlling club in Guangxi.

A : Is it difficult to sell the products to students?

M : You know one of my clients saved all his expenses of traveling to the university in order to buy Herbalife each year when he studied in the university.

B : You should know that it does not mean that after this product of Herbalife is sold, the products will be different from the products of Amway three months later. He said that I exchanged a can of nutriment for a big bag of cleaning stuffs of Amway. Think of it. One of my clients left me. He didn't come back to me until three months later. I almost distribute goods every day.

M : I bought a package of skin care products and used them for three months. But isn't it difficult for you to make me buy them once for all? Suppose that I buy a package of nutriment to reduce weight. If I am over-weighted by 30 kilograms, I will have to eat it for at least 6 months plus another 6 months. How many months will it take me to reduce weight and for how many months should I eat them? That is to say that I have to buy your products in all 12 months. Think of how much the volume is. And I don't expect any one in entire Guangxi or actually in our team will die after joining our team. I want to train everybody to perform retail because you can't succeed unless you work this way. If you do not practice, you will not know how to practice this business. I did it every time and they will surely learn it.

B : I am in your taxi for a ride and you give me an invoice. I give money to a person who provides service to me. Will you swear at me because I give you money? So this can be done gradually. Any way is okay. Our Herbalife has many methods.

M : Now they are already recruiting personnel. They will be trained ten by ten. Herbalife has just launched its business in Guangxi. It will not operate stores until November. He will provide many corporate resources to us. For example, we are going to perform market promotion by holding a badminton game. We do this at our expenses. We do not need to do this at our expenses. The company will make payment. So all the facilities in the hall of the game will be provided by the company. We have received from the company a projector amounting to RMB over 10,000 this year. This projector was lent to us by the company.

B : The more active you are, the more likely she will help us. Primarily, it is Zhou Fang who will help us.

A : Because Zhou Fang directly trained me in the past and I was a dealer and a managing officer below her. So at that time she helped me open Salon and formulate many forms for recruitment.

M : She really contributed a lot. Really gave us substantial support and gave us many resources. We sought stability in the course of fast growth.

B : Our value is also on the steady increase. We have sold the products targeted for this year in over 20 days.

M : My director here assigns work to them and the products in the amount of RMB25,000 must be sold out this month.

A : You can make your line in turn. I mean will your team's business cover every corner of the country after you are promoted to the upper level?

B : It depends on how you want to develop your business, of course. You may absolutely do this. But my personal view is that will you travel throughout the country? My business in Hainai is comparatively stable now.

M : Now I receive phone calls from across the country such as from Hunan and Zhejiang. I will not develop my business there, but I will keep in touch with them.

A : Does the sales region approved by him cover whole China?

B : No. At the moment it excludes Guangzhou. Why should we now set up outlets online? It is only because there are too many sub-regions.

M : It is about RMB256 a month. A package amounts to approximately RMB895. It may take 3 or 4 months to eat them.

B : Now when we bill the products, one bill at least amounts to over RMB5,000.

A : It's time to go. I want to go home. I leave now. Could you research the system first?

B : I don't want to give you a white and black material.

A : Then send it to my e-mail box.

M : Do you have any business card? Could you give me one business card?

A : I don't have it on me. I forgot to bring it with me.

M : Then please write it for me.

A : Internal system. Because I have already established a network, I told them that I want to digest it first. I mean that I want to work until I am promoted to the position of director first. So long as I have one below me and he makes RMB200,000 a month, I will receive a fixed amount of RMB10,000 and I even won't need to sell the goods.

B : No. You have to gain 2,500 points.

A : Yes because he gains those points for me.

M : Right. The triangle of your business representative gains those points for you.

A : Business representative? Assume that I am director, I have recruited a business representative and below him there is another business representative.

B : So long as they are not an independent division, you are not required to do this. But I hope that all the goods delivered by us will not be sold to him for him to eat them in an unexpected way.

M : We have many retail experiences and we all want to tell the friends whom we want to make that if you are worried that you are unable to sell the goods amounting to only over RMB20,000, you will only have to do it according to our method. If you are unable to sell the goods in 6 months, I will buy in the goods because we don't mean that after you join us we will not take care of you in future. We are really intending to train everybody and let him know how to follow in clients and to communicate with them. When you do it this way and you get a client, you will have two and three clients. When we fulfilled our target in the shortest time, the goods amounting to over RMB20,000 were sold out in only over ten days.

A : tomyzhao0912@162.com

M : Is your name Tommy? You may call me Mandy.

A : En. Mandy, Peter. We have to go. It is time to go.

B : Okay. Take care. Let's cooperate when an opportunity arises.

Addendum Seven

Articles Proving China enforcement of MLM fraud in China and Hong Kong

Massive Recruitment during Golden Week Holiday

Hong Kong becoming the Headquarter of China's Multi-Level Marketing Activities

04/10/2007

According to a special report by The Sun News, there has been an increase in multi-level marketing ('MLM') activities in Hong Kong. As MLM is illegal in mainland China, many companies are shifting activities such as the recruitment of members to Hong Kong. Companies are riding on the one week public holiday, i.e. Golden Week in China and wantonly recruiting people to Hong Kong to join in their MLM scheme. After the newly recruited members returned to China, they will in turn persuade their friends and relatives to come to Hong Kong to join in the scheme. Indirectly, Hong Kong is fast coming the headquarter of China's pyramid scheme. Some scholars have expressed concern that if left unchecked and unmonitored, such activities may jeopardize the good reputation of Hong Kong.

Lured to pay \$5000 to join scheme

During the Golden Week period, about 90% of the attendees in a MLM workshop conducted by one company located on the Hong Kong Island were visitors from the mainland China. More than 20 participants sat in to listen to the speaker, 'Sister Lan' allegedly from the Fujian province, who promotes the so-called 'money-making scheme'. One of the participants is Mr. Wong, a businessman from Shenzhen who has come to Hong Kong and are attending the workshop together with several friends under the recommendation of his relative.

Sister Lan described this business as one that generates handsome profit involving little / minimal capital. All it takes is \$5000 to join the scheme and one will then be granted the distribution right and provided with products sample. Once became a distributor, this member can then introduce a minimum of 5 friends &/or relatives to be his / her lower-tier members. When these lower-tier members recruit other members, the higher-tier member who is their initial recruiter, will be eligible for a cut of the commission. Hence, with more lower-tier members being recruited, the higher-tier members can receive a larger amount of commission.

In the midst of the workshop, Sister Lan flashes a bank saving passbook proclaiming that she was only involved in this business for one year but has already earned more than \$500,000. She said that even for this month where her earning is lesser than usual, there is at least \$20,000 to \$30,000. She also assured the participants not to worry, claiming that as long as these activities

are being carried out in Hong Kong and they continue to bring their friends to Hong Kong for membership registration, they will not run into any problem.

A workshop earns \$120, 000

Whenever Sister Lan finds out that someone is interested in the scheme, she will persuade them to participate in the 'Money-Making' workshop and each participant will be charged a fee of \$200. Apparently, the number of participants can be as high as 600 in a single workshop which mean the company will receive about \$120, 000 from one workshop.

Mr. Wong You-Jin, Chinese Legal System researcher from the Asia-Pacific research institute of the Chinese University of Hong Kong, said that recruitment of multi-level marketing members in China constitutes an infringement of the legislation and this also extends to Hong Kong citizens who carry out any recruitment activities in China. He commented that should any incident happen during the aggressive recruitment drive that is taking place during the Golden Week, it will adversely affect the reputation of Hong Kong.

Crackdown of Mainland Illegal Pyramid Scheme

04/10/2007

The Sun News reported that the central government viewed multi-level marketing to be extremely detrimental to the economy. Hence as early as 1998, all forms of multi-level marketing activities were banned in China. On 1st November 2005, the mainland authority enacted legislations to prohibit and illegalized all forms of multi-level marketing activities.

To combat multi-level marketing activities, mainland's Public Security authority has been relentlessly dismantling multi-level marketing syndicates. In last year alone, the Public Security Bureau has cracked 1,915 cases that are related to the pyramid marketing scheme; arrested more than 16,700 people involved in multi-level marketing activities and froze a total asset of RMB 660 million. Close to 300,000 subjects were victims of these scams.

Despite the relentless and harsh crack-down by the authority, multi-level marketing activities could not be entirely eradicated. In recent times, multi-level marketing in China has evolved to better evade Police's action. In addition to utilizing the internet to promote the activities, the organizations adopt the guerrilla warfare tactic; dispersing their units in different locations to make it harder for the Police to wipe out an entire organization. According to estimates from the mainland authorities, multi-level marketing activities in mainland China have 'absorbed' about RMB 4 to 50 billion.

28 veterans class pyramid scheme chieftain dinner when he was arrested (AP)

Guangxi News Network - Contemporary Hayat reporter Kaye camp Correspondent PAN Yan-ming

"Stop all, seated inspection." The evening of October 3 7 am, Nanning Municipal Public Security Bureau of Economic Investigation Detachment more than 40 plain clothes officers, quietly surrounded the West Nanning Lang a luxury restaurant "presidential box." 1 million yuan in the seafood at one stroke had captured "last supper" of the 28 "CEOs - class" pyramid scheme chieftain.

This is the police in combating Nanning "of the family's" illegal nature of the case, such as pyramid schemes, by careful planning, the city once again strike out with a successful banned the amounts of money involved over 20 million yuan to-, headed by the Fujian Fengsuqiong illegal pyramid scheme membership organization staff a marvelous scene.

Police stormed "presidential box"

The evening of October 3, a group of suits young men, also wearing fashionable beautiful woman, driving different types of cars, Lang went to the Nanning City West a high-grade restaurants, entered the restaurant "presidential box," under the 10000-odd points delicacies prepare for the big festival. However, serving soon, dozens of plainclothes policemen suddenly ran into the box, showed documents, ordered all those who attended the banquet were not allowed to tamper with.

The public security bureau of Nanning City, the Honorable Deputy Economic Investigation detachment commander told reporters, after lasted nearly three months with assurance investigation, the police had to grasp, headed by the Fujian people Fengsuqiong illegal pyramid scheme organizations.

August 3, Economic Investigation Detachment of the crimes alleged illegal file for investigation of illegal pyramid scheme organizations. After dispatched a group of long-term, hard evidence, access to the pyramid marketing organizations "manager level" leader in October will host a dinner meeting on the 3rd of intelligence, Economic Investigation main police detachment deployed in the banquet will be on-one stroke, Fengsuqiong Fujian headed by 28 senior officers who arrested suspected pyramid schemes. The same day, police also arrested eight suspected pyramid schemes Fujian, the Fujian license plates were seized

[Vehicle](#) five, and seized 21 million, involved.

Why is it necessary to arrest people on the banquet? Cheung Kam said, mainly in the banquet on pyramid schemes uncovered evidence of the most vulnerable, because these high-level pyramid scheme leaders gathering for dinner, the main purpose is the exchange of pyramid scheme "achievements" and, therefore, they will bring many documents, to show off their own skills.

At this point arrests, the best timing. At that time, there are many MLM leaders to rush for the document to throw underneath the table, but all seized by the police. 36 suspects were detained on criminal charges.

Currently, the case is still further review.

The "three noes pyramid scheme" can not escape the Kensaku Hogen

According to the Ministry of Public Security, the Regional Public Security Department on July pyramid schemes as a nationwide centralized and unified action against the plan of the work, Nanning police from July to begin by Economic Investigation Detachment mainly coordination with other police has launched a number of large-scale pyramid schemes against the centralized and unified action to take against successively Associating the Xinjiang "of the family's" illegal pyramid scheme organizations. However, MLM organization's illegal activities, often in Nanning City has also occurred.

In July this year, Economic Investigation Detachment received reports from the masses: some senior Hotels Nanning City hotel foreigners in illegal pyramid scheme activities. This article has aroused Nanning City of

information at all levels of leadership attached great importance to the public security bureau of Nanning City Economic Investigation Detachment immediate investigation.

As the development of the MLM organizations in the absorption of members, launched the so-called "three noes principle," that is: any ID card holders Guangxi local development officers not to join;

[The civil service](#), military service, not to develop accession; Students do not develop. MLM organizations in the development of downline members, the eyes of "observation" in the aged 30 to 45 years old, and in the community have a certain economic base, especially in the business on staff.

These two means, the main aim is to cover the activities of pyramid schemes, pyramid marketing activities for more economic benefits. But the police is also very important access to a number of valuable intelligence information, and promptly broke out of the illegal nature of the pyramid schemes.

MLM organizations implementation of "three-tier system"

At the trial the people involved with the confession, since last year, to-, headed by the Fujian Fengsuqiong staff MLM organizations on the Nanning City some hotels, guesthouses organizations in MLM activities. The external direct sales organization called "new-hsin Fuzhou

[The real estate](#) company ", and" Xin Fuzhou new real estate company "in the name of the city and some hotels, guesthouses concession agreement signed between business, the long-term rental of hotel, a hotel room, officers involved in pyramid schemes or intends to provide the new members joining the scheme place of residence and as a " one on one " brainwashing place.

The multilevel marketing organizations to "pull poll" approach seek illegal interests. MLM different from the past and attract participants yes, this three-tier pyramid marketing organizations to take out off the assembly line system (that is, when participants in the development of three generations of my offline, and when it became all three generations of veterans downline levels, I must be "out of the game" and will no longer receive their downline purchase of the allowances). All join the MLM organizations must have membership on the lines of the seminar, the time limit per person direct delivery of cash 69800 yuan (that is, each person could only purchase 21 share, with the exception of No. 1 for 3800 yuan, after 20 each for 3,300 yuan Total 69800 yuan), and each participant can be made up Show off the assembly line three.

The pyramid scheme organizations implementation of "three-tier system" that is, officers, managers, CEOs. All participants may purchase 21 to become director level; When the participants and their development off the assembly line in the total purchase of 65 participants at the level I can be a manager; When the players off the assembly line with their development of 600 cumulative purchase, and the development of three generations of my offline when all the managerial level, participants can be promoted to manager level . Organizations participating in the pyramid scheme of the most direct benefits, that is, from its development can pay off the assembly line in the purchase of access to allowances, allowances amount in accordance with its own development off the assembly line at the level in which to be determined. This lure has a lot of businessmen and speculation boss participate in the organization, the amount of funds involved over 20 million yuan.

Breaking the 13 illegal

According to incomplete statistics, since January this year, police in Nanning City reunification special action against pyramid schemes, pyramid schemes nature of the legislation with the 20 illegal operation, detection 13, involving more than 12 billion yuan. Officers arrested 84 people in connection with the case, which were punished, detained 84 people and arrested 32 people, destroyed 192 MLM dens. Severance of the pyramid schemes from across the country to reach more than 3,000, a severe blow to enter Nanning City to carry out illegal activities of the arrogance of the MLM organizations.

Addendum Eight
Business Card translated to English of Mendy Xi translated
(In person meeting in China—original card, last addendum)

Herbalife
Number One Brand Name in Weight Control in the World

Mendy Xi
Business Manager
License Number: 24112151

Telephone: 13878706898 (for the whole country)
13377218868 (for Liuzhou only)
(852) 81011961
QQ: 2820012021
E-Mail: mendyxi@hotmail.com
Company website: www.herbalife.cn

Retail store in Nanning: No. 6, Building 11, Jinwan Huacheng, No. 19, Baisha Dadao, Nanning
(right side of the main door)
Liuzhou Branch: Suite 1307, Huaqi Building 1, Jinyuxiangkou, Jiefangnan, Liuzhou (upstairs of
Sanming Communications)
Other Branches:Guangzhou, Shenzhen, Xi'an, Haikou, Sanya, Guiping, Guangxi etc.

Increase weight or lose weight, come to ask me for the way!

Facts say more than anything else!

[Picture on the left: February 10, 2000. 68 kg before weight loss.]

[Picture in the middle: May 25, 2000. 54 kg after weight loss.]

[Picture on the right: October 18, 2006. No change after 7 years.]

- The only way to control product that even a pregnant woman can take.
- With 27 years' experiences of healthy weight loss, nutrition, and cellular rejuvenation
- Products sold in 68 countries all over the world with more than 50 million loyal consumers
- Global nutrition authority; number 21 on the global Fortune 500 companies
- Publicly traded company on the New York Stock Exchange (HLF)

Speaker: International Sports Star Beckham

Follow up by a special agent. Lifetime tutoring. Never change back!

Addendum Nine

News Release Herbalife containing China size and scope

News Release

[View printer-friendly version](#)

[Back](#)

Herbalife Receives Additional Access in China

LOS ANGELES--(BUSINESS WIRE)--July 9, 2007--Herbalife Ltd. (NYSE:HLF), a global nutrition direct-selling company, announced today that it has received a direct-selling license from China's Ministry of Commerce to conduct business throughout the entire Jiangsu province. In March 2007, the company received permission to conduct business in just two cities, Suzhou and Nanjing.

Located on China's east coast, the Jiangsu province, consisting of 13 cities with 61 counties, has a permanent and transient population of approximately 85 to 90 million people. Cities approved are Nanjing, Suzhou, Xuzhou, Lianyungang, Suqian, Huan'an, Yancheng, Yangzhou, Taizhou, Nantong, Zhenjiang, Changzhou, and Wuxi.

Herbalife currently operates 47 stores and 37 service centers in 28 provinces in China. The company operates a unique direct-selling model in China in accordance with local regulations, where our supervisor-level distributors are employed by, and conduct their business, in retail locations owned by Herbalife China. Consumers and other distributors come into the store to buy product and learn more about the business opportunity. In areas where the company is licensed, distributors will be allowed to conduct business outside of the store.

Headquartered in Shanghai, Herbalife sells more than 35 products in China. The company operates its own manufacturing facility in Suzhou, China, that produces products for local use and export.

Herbalife is affiliated with, and plays an active role in a large number of industry trade organizations, including The World Federation of Direct Selling Associations, the Federation of European Direct Selling Associations and 40 individual Direct Selling Associations globally.

[About Herbalife](#)

Mendy Xi Business Card



HERBALIFE® 康宝莱
全球体重控制第一品牌

奚敏
Mendy Xi
业务经理

电话: 13878706898 (全国)
13377218868 (柳州)
(852) 81011961 (香港)
Q Q: 280012021
E-mail: mendyxi@hotmail.com
公司网址: www.herbalife.cn

资格证号: 24112151

南宁专卖店: 南宁市白沙大道19号金湾花城11栋6号铺面 (正门右侧)
柳州分公司: 柳州解放南金鱼巷口路花旗一号楼1307室 (三明通讯楼上)
其他分公司: 广州、深圳、西安、海口、三亚、广西桂平等

增重减肥, 办法问我!

Card Front



事实胜于雄辩!

2000.2.10 减肥前 68公斤
2000.5.25 减肥后 54公斤
2006.10.18 七年不反弹

- 全球唯一孕妇也能食用的体重控制产品
- 拥有 27 年健康减肥、营养及细胞更新经验
- 畅销全球 68 个国家及 5000 多万忠实消费者
- 世界营养权威, 全球 500 强企业排名 21 位
- 美国纽约证券所上市公司 (代码HLF)

代言人: 国际球星 贝克汉姆

专人跟进, 终身辅导, 永不反弹!

Card Back