



What is a Pyramid Scheme?

A pyramid scheme is a fraudulent system that participants attempt to make money solely by recruiting an ever-increasing number of "investors." The scheme is called a "pyramid" because at each level, the number of investors increase. The first people that started the scheme at the top require a large base of later investors to support the scheme by providing profits to the earlier investors.

The three most common factors that reflects a pyramid scheme is when:

- The promoter promises a high return in a short period of time
- No genuine product or service is actually sold
- The primary emphasis is on recruiting new participants

How does it work?

In a pyramid scheme, an organization forces individuals who wish to join to make a payment. In exchange, the organization promises its new members a share of the money taken from every additional member that they recruit. The directors of the organization (those at the top of the pyramid) also receive a share of these payments. For the directors, their only aim is for people to continue recruiting and get more money to the top of the pyramid.

For a pyramid scheme to make money for everyone who enrolls in it, it would have to expand indefinitely. This is not possible because not everyone will join the scheme and there is a limit to the number of people in a group or community. When the scheme inevitably runs out of new recruits, lacking other sources of revenue, it collapses. When this happens, everyone at the lower levels of the pyramid do not make any money; only the people at the top turn a profit.

In particular, when the scheme collapses, most members will be in the bottom layers and thus will not have any opportunity to profit from the scheme; still, they will have already paid to join. Therefore, a pyramid scheme will benefit the people on top and its members will lose money. For this reason, it is considered a scam.



Why do Pyramid Schemes always fail?

Pyramid schemes are doomed to fail because their success depends on the ability to recruit more and more investors. Since there are only a limited number of people in a given community, all pyramid schemes will ultimately collapse. The only people who make money are those few who are on the top of the pyramid

Why do people invest in Pyramid Schemes?

If all pyramid schemes fail, why would anyone invest in them?

There are three basic categories of people who invest in pyramid schemes:

Those who participate out of greed;

(The people who participate in pyramid schemes out of greed often know that they are illegal. They nevertheless participate, hoping that the scams will last long enough for them to make a profit).

Those who are misled into thinking that they are joining an "investment club" or a "gift program";

(Pyramid promoters often target closely knit groups such as religious or social organizations, sports teams, and college students to increase pressure to participate. They give some pyramid schemes attractive names such as "investment clubs" or "gift programs." These clubs or programs are usually presented to these investors with assurances that they are perfectly legal, approved by Government agencies)

Those who believe that the products or services are legitimate.

(Those investors who actually believe that the products or services which the promoters sold to them are legitimate, inevitably realize that they have been scammed. It is only when these products and services are unsaleable, and the promoters refuse to repurchase them, that they finally become aware that they have participated in an illegal pyramid scheme)

Spotting Pyramid Schemes

Almost everyone knows what a pyramid scheme is. People see them exposed on television and read about them constantly in newspapers and office websites. So, if everyone is so well informed about the pyramid, how does it survive?

The people promoting such schemes have several strong weapons at their disposal to convince recruiters:

- Cons say, "Get in now, or regret it forever". They don't have time – because of market demand or commitments elsewhere – for the person to check out the deal.
- Cons say, "They do pay off". Early players circulate the word and bring in new targets. Initial payoffs also keep early players coming back. Payoffs make the enterprise look legitimate and fuel the expansion process
- They target community groups, religious organisations, and social clubs. Pyramidisers know how to manipulate the trust of these groups
- "Everybody has friends and associates; you only have to sign up three or four people below you".
- The "opportunity" is usually pitched by someone familiar to the victim, or at least by someone with an affinity the victim trusts. Most important, the pyramid does return people's money, with the incredible profits attached as promised

Red Flags

People see them exposed on media and Facebook and other communication means;

- The promoters will charge high entry fees
- Complex trading strategies or business model is vague. Source of income is primarily based on recruiting new members
- Promise of low risks or high rewards
- High pressure sales tactics
- Pressure to re-invest
- Lack of transparency and access
- The "products" sold by the business is the biggest giveaways, usually overpriced and have no market value
- They promise you unusually high returns on your investments, the more you invest, the higher your returns it will be
- Not register agents
- Prior customer complaints regulatory problems
- Lack of background information with the business operation





Prevention

The following are some additional tips to help you steer clear of pyramid schemes:

- Gather all information regarding the company, its officers, and its products or services. Get written copies of the company's marketing plan, sales literature, contracts, etc
- Avoid promoters who fail to explain their plans clearly and details
- Find out if there is a demand for a product or services, if so how well does it sell?
- Beware if the start up cost is substantial. Some pyramid scheme pressure you to pay a large amount to become a "distributor" or "member"
- Resist the temptation to invest just because the people selling you the program are friends or are part of your religious or social organization. They may have been misled into believing that they could make large amounts of money in a short time
- Pyramid schemes aren't usually very sustainable. The setup eventually falls apart after:
 - The operator takes the remaining investment money and runs
 - New investors become harder to find, meaning the flow of cash dies out
 - Too many current investors begin to pull out and request the returns

What does the legislation say about Pyramid Schemes?

Competition and Consumer Act 2016

Pyramid scheme is prohibited under section 65 of the Competition and Consumer Act 2016 where it is an offence: For a person to promote and operate a scheme for the supply of Goods or services for reward if that scheme constitutes primarily an opportunity to buy or sell an investment opportunity as against an opportunity to buy or supply goods, and where that scheme is unfair to the participants because:

- i. The financial rewards are dependent on the recruitment of additional participants, and
- ii. Where the number of additional participants in the scheme must be recruited to produce financial rewards to participants is not attainable to other participants.

Crimes Act 2013

Person carries out such activities is charged with Section 172 of Crimes Act 2013 for obtaining by Deception or causing Loss by Deception of any property including money, and will face imprisonment not more than 7 years



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