

FOR IMMEDIATE RELEASE

**PERSHING SQUARE RESPONDS TO RECENT RULING  
IN *FTC v. BURNLOUNGE, INC.***

NEW YORK, June 3, 2014//—Pershing Square Capital Management, L.P. (“Pershing Square”) today released the following statement in response to the recent ruling by the Ninth Circuit Court of Appeals concerning its decision in *FTC v. BurnLounge, Inc.*:

On June 2, 2014, the United States Court of Appeals for the Ninth Circuit unanimously affirmed the district court’s permanent injunction against continued operation of BurnLounge, Inc., an illegal pyramid scheme operating in violation of Section 5 of the FTC Act.

Herbalife Ltd. (NYSE: HLF) immediately spun this decision as ‘supportive’ of its business model – in the face of the Federal Trade Commission’s victory in shutting down a deceptive pyramid scheme, whose illegal elements closely parallel Herbalife’s own practices.

Investors are encouraged to read the appeals court’s ruling for themselves to see just how ‘supportive’ it is of Herbalife. <http://cdn.ca9.uscourts.gov/datastore/opinions/2014/06/02/12-55926.pdf>

In its decision, the Ninth Circuit reaffirmed the principles of its 1996 decision in *Webster v. Omnitrition International, Inc.*, which condemned as a pyramid scheme a company that was founded by a former Herbalife distributor and that mirrored Herbalife’s marketing plan almost exactly. The court instructed that “[t]o determine whether a MLM business is a pyramid, a court must look at how the MLM business operates in practice.”

BurnLounge’s so-called Mogul program (analogous to Herbalife’s Supervisor/Sales Leader program) was found to be illegal because “BurnLounge’s focus was recruitment” and because the bonuses that BurnLounge paid to its participants “were tied to recruitment rather than the sale of merchandise.”

Citing *Omnitrition*, the court wrote: “[t]he mere structure of the scheme suggests that Omnitrition’s focus was in promoting *the program* rather than selling *the products*.” In BurnLounge, “[s]elling packages [of products] was a way of recruiting new Moguls—in fact, it was the only form of recruitment—because purchasing a package was necessary to become a Mogul and earn cash rewards.”

In the same fashion, Herbalife’s distributors are pressured to reach Supervisor/Sales Leader quickly (at a cost of approximately \$3,000), qualifying them to receive royalties and other commissions, and then to pressure their own recruits to reach the Supervisor/Sales Leader level, too. As the Ninth Circuit observed, “in *Koscot*, participants joined the scheme by buying inventory, and participants earned rewards by recruiting others to join the scheme, i.e., by getting recruits to buy inventory.” In other words, a pyramid scheme cannot obscure its illegality by using a sale of inventory as cover for paying recruitment rewards.

The Ninth Circuit looked to the purchasing behavior of participants to determine that “Moguls were meant to be, and were, primarily motivated by the opportunity to earn cash rewards for recruitment.” As Pershing Square has shown repeatedly, including in its December 20, 2012 presentation, Herbalife distributors are also given strong incentives to focus their efforts on recruiting new distributors into the scheme rather than selling products to genuine retail customers outside the distribution network.

The Ninth Circuit rejected BurnLounge’s contention that the FTC was required to show that BurnLounge’s rewards were “completely unrelated to the sales of bona fide products,” holding instead that BurnLounge was a pyramid scheme because “the rewards BurnLounge paid were *primarily* for recruitment, not for the sale of products” (emphasis added). The Court explained that “BurnLounge participants joined the scheme by buying packages,” and “[p]articipants earned rewards by recruiting others to join the scheme, i.e., by recruiting new participants to buy packages.” Thus, “the participants sold something . . . , but the rewards the participants received in return were largely for recruitment, not for product sales.” Similarly, Herbalife distributors are strongly encouraged by senior distributors to (1) purchase large volumes of Herbalife products in order to qualify as a Supervisor, (2) recruit new distributors into the scheme, and (3) push those new distributors to do the same.

The Ninth Circuit also rejected BurnLounge’s argument that the company was not a pyramid scheme because participants, when they bought BurnLounge packages, were “ultimate users” of the products contained in those packages. The Court recognized that “some sales occurred” and noted the district court’s finding that the packages had “some value,” but the Court rejected any categorical rule that sales to participants constitute sales to ultimate users.

To the contrary, the Court held that BurnLounge was a pyramid scheme because the purchase of BurnLounge packages by participants did not reflect “consumer demand for the merchandise in the packages,” but, rather, “[t]he merchandise in the packages was simply incidental” to the purchase of the “right to participate in the money-making venture.” Similarly, as Pershing Square has shown repeatedly, there is little genuine retail demand for Herbalife products, and Herbalife distributors order those products for the primary purpose of qualifying for and maximizing the recruiting rewards they receive from Herbalife. In the Herbalife scheme, as in BurnLounge, the opportunity to earn recruiting rewards is “the major draw.”

The notion that the Ninth Circuit’s decision is a vindication of Herbalife is absurd. The case certainly does not support Herbalife’s position that sales of products to distributors who tried – but failed – to succeed in their pursuit of the Herbalife business should be regarded as true retail sales.

#### **About Pershing Square Capital Management, L.P.**

Pershing Square Capital Management, L.P., based in New York City, is a SEC-registered investment advisor to private investment funds. Pershing Square manages funds that are in the business of trading — buying and selling — securities and other financial instruments. Funds managed by Pershing Square have established short and other bearish economic positions against securities of Herbalife Ltd. Pershing Square may change its views about, or its investment positions in, Herbalife at any time, for any reason or no reason. Pershing Square may buy, sell,

cover or otherwise change the form or substance of its Herbalife investment. Pershing Square disclaims any obligation to notify the market of any such changes. Please see the full Disclaimer appearing on website [www.factsaboutheralife.com](http://www.factsaboutheralife.com).

**Contact:**

Carolyn Sargent  
(212) 843-8030  
[csargent@rubenstein.com](mailto:csargent@rubenstein.com)

Fran McGill  
(212) 843-9353  
[fmcgill@rubenstein.com](mailto:fmcgill@rubenstein.com)