

# Mission Impossible

## A Rebuttal to the Ongoing Attacks by Barry Minkow on Usana Life Sciences By Len Clements • MarketWave, Inc. © 2008

In February of 2007, ex-felon Barry Minkow<sup>1</sup>, under the auspices of his "Fraud Discovery Institute", published a scathing 86 page report on Usana Health Sciences.<sup>2</sup> He claimed, among others things, that Usana was an illegal pyramid scheme and its business model was untenable. At the time Minkow claimed that he had "uncovered", "investigated" and eventually "resolved" at least 13 previous cases of business fraud. In each case he would present his findings to various regulatory agencies, such as the SEC, FBI and IRS, who would then initiate their own investigation which ultimately resulted in the closure of the company – and various accolades and accommodations presented to Minkow which, understandably, he was fond of citing. It appears Minkow had, up until this time, a perfect 13-0 take down record.

Until Usana.

Although his shorting<sup>3</sup> of Usana's stock previous to publishing his report earned him over \$61,000<sup>4</sup>, and he was paid over \$200,000 by three different people to produce the anti-Usana report<sup>5</sup> – which appears to be a benefit not afforded him in his previous 13 victories – Minkow has not only utterly failed to bring down Usana, the subsequent and now concluded SEC investigation of them found no evidence of any wrong-doing of any kind. But then, Minkow may still declare this one for the victory column. He did, after all, bring down their stock price.

Minkow had likely become quite accustomed to writing up his findings, presenting them to his fed-friends, and sitting back with a box of popcorn to watch the implosion. I suspect, based on all that I have come to learn about Barry, it was probably a very infuriating ego buster to find Usana not only still standing after his first salvo, but actually *standing up* to him. How *dare* they! In Minkow's public response letter to Usana after he was sued, he stated:

"And by the way, do you really take the FBI and the SEC for fools? Do you know of the current criminal operations in which the Fraud Discovery Institute is currently involved? Or for that matter, how many cases unrelated to Usana we have helped uncover or are currently helping to uncover? The point is not to boast as much as it is to show that the Emperor has no clothes and the technique of diverting apparent law enforcement interest in Usana to me is inconsistent with our track record in pro active fraud uncovering with various government agencies."

"Inconsistent"? I bet it was. So, it appears Minkow had to, for the first time, call in counter strikes and reinforcements.

First, he hired (for a fee) über-anti-MLM zealot Robert FitzPatrick to produce additional attack reports on Usana. All of which Minkow was quick to also forward to the SEC, FBI and IRS, and with the assistance of a professional PR firm, the media was always made aware of them as well.

And Usana still stood.

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<sup>1</sup> Minkow was the founder of ZZZZ Best carpet cleaners. He and eleven others were indicted by a federal grand jury in 1988 on 54 counts of [racketeering](#), [securities fraud](#), [embezzlement](#), [mail fraud](#), [tax evasion](#) and [bank fraud](#), and eventually served over 7 years in prison.

<sup>2</sup> The rebuttal to this report can be found at <http://www.marketwaveinc.com/articles/FDI-Rebuttal-R1.pdf>

<sup>3</sup> Minkow purchased "Put Options" which generate profits as a company's stock price declines.

<sup>4</sup> <http://www.marketwaveinc.com/articles/WSJPrintEdition.pdf>

<sup>5</sup> Deposition of Barry Minkow.

He then followed up with a conga line of his own reports on "newly acquired" negative material on Usana, all of which was also forward to the SEC, FBI and IRS. These subsequent reports included such revelations as; A member of corporate and of their Scientific Advisory Board had both inadvertently omitted "(ret.)" after their respective CPA and M.D. designations, and; the large majority of commissions paid my Usana were only going to those who worked the hardest, for the longest period of time (what a bunch of fair, reasonable bastards!).

And Usana still stood.

Minkow produced several professional, high quality video segments attacking Usana, which he then published on YouTube.<sup>6</sup> He attacked their products, he attacked their ethics and honesty, and he attacked their business model (with a series of interviews with Usana "victims"). A press release accompanied each new video, which were viewed by thousands of people.

And Usana still stood.

He called in other heavyweights from within the anti-MLM division to produce supporting anti-Usana propaganda, and issued numerous press releases to the media every time a new report or video was published (which such publications as The Wall Street Journal and Forbes were more than willing to indulge). This included hit pieces from anti-MLM attorney Douglas Brooks and fellow anti-MLM zealot (and minor league "Forensic Accountant") Tracey Coenen. Soft punching but prolific anti-MLMer Jon Taylor offered up his own support of Minkow's allegations, although, to my knowledge, no one asked him to (and, unlike the others mentioned here, Minkow never even acknowledged any of his subsequent work). In his response to the Usana suit Minkow also stated:

**Expert opinions support our conclusions.**

What has been lost and unaddressed in this attack on me, is the many experts who are above reproach who, in their addendum materials, provide meticulous corroborating documentation and sound reason upon which they base their findings. Without their input, our original report would simply be the opinion of one person. With them, we have the opinions of several experts who support our findings and make a cumulative, persuasive case. For example, Doug Brooks, whose reputation is unimpeachable, made devastating arguments against the tenability of the Usana compensation plan and illustrated a convincing application of the Howey test.

In spite of Mr. Brooks "devastating argument" against Usana's pay plan and his "convincing" case that they were selling unregistered securities<sup>7</sup> illegally...

Usana still stood.

Whether at the behest of Minkow or not, various other online and print media have blindly parroted his assertions<sup>8</sup>, along with other Drudge-wanna-be bloggers and numerous conveniently anonymous message board bashers.

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<sup>6</sup> My Rebuttal Report on these videos and other attacks subsequent to Minkow's first report can be found at <http://www.marketwaveinc.com/articles/YouTubeResponse.pdf>

<sup>7</sup> Apparently Brooks' case was not convincing enough to the SEC, the very designer of the "Howey test". The SEC investigated Usana for ten months subsequent to receiving Minkow's report, which contained Brooks' arguments, and took no action of any kind.

<sup>8</sup> Including the Salt Lake City Tribune, which didn't even contact Usana for their side of the story before first reporting Minkow's initial findings. More recently they published an article by Paul Foy (Associated Press), an author of other negatively slanted articles about MLM companies, which was promptly removed in its entirety from their online edition due to inaccuracies subsequently pointed out by Usana.

And to this day, after more than a year of this constant bombardment, Usana not only still stands, but their foundation has nary more than a few micro-fractures. The IRS seems to have completely ignored Minkow's report, and the alleged FBI investigation<sup>9</sup> turned out to have never occurred (they "deferred to the SEC", according to The Wall Street Journal, with Minkow himself being their source). A derivative law suit<sup>10</sup> has already been dropped, and Minkow's action to have Usana's federal stock manipulation law suit against him dismissed was denied (their case is ongoing).<sup>11</sup> And again, the ten month long SEC investigation<sup>12</sup> found nothing – *nothing* – requiring any action on their, or Usana's part.

So, having thrown everything at Usana but – it was time for the proverbial kitchen sink. Which Barry Minkow christened...

## Cheating in China

Barry Minkow threw up a web site called CheatingInChina.com back in October, 2007<sup>13</sup> to exhibit his "findings" regarding an "undercover, two month long investigation" of Usana's marketing activities in Hong Kong and China. Included are the following allegations:

- 1) Neither Usana nor its distributors have legal approval to conduct business in or from China.
- 2) Usana has "30,000 active distributors in China".
- 3) Usana is "engaged in illegal business activities" in China and "conspiring to conceal them from U.S. and Chinese regulators and investors." Specifically, Usana reps are pursuing an underground movement to recruit Chinese Nationals as associates, and Usana field leaders and members of corporate are orchestrating this effort.
- 4) Minkow has "extensive evidence" of this "ongoing conspiracy".
- 5) Usana "appears to omit all material information in connection with its Hong Kong/China operations in SEC filings.

First, Usana indeed does not have legal approval to conduct business in China – because *no* MLM company has legal approval to do so in China. The Chinese government, due to an epidemic of outright pyramid schemes that had become rampant throughout the country in the 1990s, banned all forms of direct sales in 1998.<sup>14</sup> As one of the many banished babies covered in bath water, Usana is forbidden from conducting any form of direct sales or MLM business there.

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<sup>9</sup> Faithfully reported as already underway by both the National Business Review and Forbes.

<sup>10</sup> [http://en.wikipedia.org/wiki/Derivative\\_suit](http://en.wikipedia.org/wiki/Derivative_suit)

<sup>11</sup> Minkow did receive a favorable ruling on a subordinate state anti-SLAPP action related only to California, which Team Minkow members are hailing as a substantial, even definitive victory. Of course, Usana's federal level stock manipulation charge is the crux of their action against him, which still provides Usana the opportunity to show Minkow's allegations to be false.

<sup>12</sup> An "informal inquiry" actually, which is significantly different and less threatening than a "formal investigation". So the SEC not only found no merit to any of the allegations against Usana, they apparently didn't even see anything questionable enough to warrant escalating the "inquiry" into a full-on "investigation"!

<sup>13</sup> His press release hit on October 19<sup>th</sup>, and Usana's stock dropped another 2.5% that day.

<sup>14</sup> Due to heavy international pressure, and China's subsequent joining of the World Trade Organization, they have gradually softened this restriction. Today there are 13 international direct selling companies that have been awarded licenses to operate in China, on a single tiered commission basis, including Amway, Avon, Mary Kay and Nu Skin.

Throughout Minkow's verbose press releases and his various reports on the matter, he is fond of hedging his "extensive evidence" with terms such as "believes", "allegedly", "appears" and "apparent". This First Amendment friendly language *appears, I believe, to be there for a reason. I'm not saying anything I'm about to describe are facts, that I know are true. I just think I know why he's using them, based only on what it looks like to me. Get it?*

*I believe, based on how it appears, that Barry Minkow knew, or at least must have suspected, that his "extensive evidence" was flimsy at best, and outright bogus at worse, yet he published it anyway. You'll soon understand why.*

So how did Minkow's undercover investigation uncover this covert, "underground conspiracy" to set up Chinese Nationals with Usana distributorships, in spite of all their efforts to "conceal" them?

He asked.

I'm not kidding. He had an "operative" call Usana's customer service line, posing as a prospect, and asked. Another "operative" emailed a distributor under the same pretence, and asked. He sent "agents" to infiltrate Usana's Hong Kong office, met with their Distributor Services Director, and simply asked. But here is how Minkow describes his "investigation":

"To secure usable and legal evidence, the Fraud Discovery Institute brought in certain licensed investigators (more than one company) located in China and Hong Kong to secure in-person visits and taped phone calls within the limits of the governing countries laws."<sup>15</sup>

In fact, there is not a single piece of information presented by Minkow that you the reader could not have just as easily procured by simply calling, e-mailing or visiting a Usana representative and *asking* them! Of course, your *interpretation* of their responses, and how you might later present them, might be very different from Minkow's. You, I assume, don't have a perfect 13-0 company closure record to maintain, nor do you financially benefit by Usana's stock price going down, nor were you paid \$200,000 by those who do.

Minkow also employed the rarely known and ultra-sophisticated investigation technology called a "Google search" to "uncover" Usana associate web sites where such advocacy of this alleged activity was promoted. A total of *four* web sites were produced in Minkow's report. Out of thousands of associate web sites. Just in Asia.

Yes, *this* is how Minkow and his "licensed investigators" and "operatives" uncovered Usana's "illegal business activities" that they were "conspiring to conceal from U.S. and Chinese regulators and investors." But, apparently, they didn't bother even once to conceal any of this from several random strangers who simply called, or walked in off the street, and asked.

So were Minkow and his secret agents really encouraged to break the law and instructed on how to do so? Well, not exactly. As any Junior High School student should know, Hong Kong's government, political system and legal system operates independently from China's.<sup>16</sup> For example, Hong Kong is still a capitalist nation, where as China is socialist. Also, MLM is banned in China. It's legal in Hong Kong. It's also perfectly legal for a resident of China to officially establish a legal business entity in Hong Kong – even if that business happens to be an MLM distributorship. And, in fact, that's *exactly* what Barry's Angles were all told. Not

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<sup>15</sup> Footnote #1 of Minkow's initial report.

<sup>16</sup> [http://en.wikipedia.org/wiki/One\\_Country,\\_Two\\_Systems](http://en.wikipedia.org/wiki/One_Country,_Two_Systems)

once, anywhere, does Minkow present even a shred of evidence that anyone associated with Usana is actually trying to build downlines *within* the boundaries of Chinese territory. Minkow's supposedly mainland China based "prospects" were also told that, to enroll as associates in Hong Kong, they must provide their "Chinese ID or Chinese Passport". That's an odd requirement for such an "underground" operation trying to cover their tracks. Isn't it?

## Digging Yourself a Hole – All the Way to China

Are there really 30,000 residences of China who are doing this? Of course not. In fact, anyone familiar with MLM and this cross border pursuit of it would appreciate the challenges involved, and find the idea patently absurd. But then, the only ones that are *apparently* (that is a very comfortable word) guiding Barry are a small clutch of anti-MLM zealots<sup>17</sup> that have already demonstrated their acute ignorance of MLM reality. For example, when I was an active distributor I'd occasionally come across a Canadian prospect who still wanted to work with me even though we were not officially open in Canada. I can recall three or four occasions (over a 10 year period) where they either operated their distributorship via an American friend or relative's identity, or established a U.S. based business entity (usually an S-corp). The former scenario was always, without exception, a cumbersome mess that was quickly abandoned. Besides having to pay double shipping (to their friend, then to them), their friend's social security number had to be used. Thus commission checks not only had to be forwarded, but so would the Form 1099 the friend would have received in their name! In the latter scenario, more in line with what's going on in Hong Kong, even setting up a business entity still involves a costly double shipment of products, and just establishing an account with the "China Merchant Bank" (which is always the one recommended) usually takes "2-3 months".<sup>18</sup> I'm not familiar with the tax implications in Hong Kong, but certainly they exist. What's more, in both scenarios any cross-sponsoring or selling actually *within* the unopened country itself is virtually impossible (and *is* illegal). Indeed, no where does Minkow provide evidence of Chinese attempting to sponsor other Chinese this way (only those who have distributorships in legally established countries are the proposed sponsor).

But then, Minkow boasts an undercover video recording of Mr. Lesley Law, an "upper middle management executive", stating clearly and unequivocally that Usana does, in fact, have a "30,000 person underground sales force in China". That's Barry's paraphrasing of this executive's supposed revelation. To hear the actual comment, in its proper context, you must visit his CheatingInChina.com web site. Oh wait. No you can't. For some reason, the video of this "devastating admission" has been removed.<sup>19</sup> If you were to watch it you would see Usana's "Distributor Services Director" in Hong Kong<sup>20</sup> being asked numerous questions for almost 40 minutes related to how business is done in Hong Kong relevant to China, which he openly answers without reservation. Never once did he appear the least bit concerned about what he was describing, or who he might be describing it to. Almost as if... he had nothing to hide.

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<sup>17</sup> Start with Part 2 of: <http://www.marketwaveinc.com/articles/zealots01.asp>

<sup>18</sup> Transcript of phone conversation with a Usana Hong Kong support rep (page 16) where she confirms to Minkow's "operative" that it does take a "long time" to set up this account, and that there is no better or faster way of accomplishing this. Strange behavior for an illegal, underground operation that allegedly has no regard for rules or protocol.

<sup>19</sup> Although the panel where it is referenced, and where Minkow encourages the reader to "watch the entire video" curiously still remains.

<sup>20</sup> Which Usana defines as a low-middle management position, but which Minkow arbitrarily assigns a "high" middle management designation.

When Mr. Law was asked the question, "How many distributors roughly in China so far?", his response was to first pause, then say, "I think more than (pauses again, shrugs slightly), 30,000."

Let's start by admittedly picking some semantic nits. "Roughly"? "I think..."? A pause and a shrug before answering? Even if we were to assume, for only a moment, that everything Minkow is claiming is true, is this *rough guess* really a "devastating admission" of a "30,000 person underground sales force", or that Usana "really does have 30,000 undisclosed associates working illegally in and through China"? Again, if this activity was "concealed", "underground" and "undisclosed", why could two complete strangers easily walk into the Usana Hong Kong headquarters and simply *ask* to have it all explained to them in such detail? And how, after such a clear and lengthy description of it, could Minkow still interpret it as working "in and through China"? The whole process was about *not working in or through China!* It was about how to work in or through *Hong Kong!*

Or, maybe Mr. Law was citing the current associate count in Hong Kong and Taiwan, both of which are considered *part of China*, and would have had 27,000 active reps at the time, not counting about 1,000 Preferred Customers (those inconvenient folks who only purchase Usana products because they *want* them, which Team Minkow likes to pretend don't exist). Surely both Barry and his "operatives" knew that Usana was open in Hong Kong and Taiwan, and that they are both part of China. So to avoid any ambiguity, why didn't Barry simply instruct his "operatives" to specifically ask for the number of Chinese nationals operating distributorships outside of mainland China?

Or, was Mr. Law simply misunderstood? After hearing the number stated through his accent and the poor sound quality of the recording, I don't see how anyone can claim with 100% certainty that he didn't say 13,000. I've listened to his answer several times and, while it does sound a little more like 30 than 13, it's by no means conclusive. Especially when you consider the number of actual Usana associates in Hong Kong at the time was... *thirteen thousand!*

Or, perhaps Mr. Law was simply exaggerating, or just being overly optimistic in his rough estimate in order to impress two seemingly enthusiastic prospects who were claiming to have "many contacts" in mainland China (and ostensibly India as well)?

The point of all this isn't to speculate (nor is it necessary, as you'll soon see), but to show that even under the most worst case scenario, where Mr. Law meant exactly what Minkow obviously wants him so badly to mean, it certainly doesn't equate to "proof" that "confirms" anything. And it most certainly doesn't cause the claim "to be settled". Minkow has misplayed this "it's settled" card before. In his original report he claimed Usana says customers will "save 70%" on the price of their products due to the elimination of supply chain middle men. Several months *after* I challenged him to show even one shed of evidence of such a claim, he declared "once and for all" the "end of the 75% argument" when one of his spies (in this case the husband of the Fraud Discovery Institute's Media Liaison and Office Manager at Barry Minkow's church) claimed he heard a prominent distributor make this claim at a local meeting. This, *apparently*, is a sufficient level of evidence for Barry Minkow to warrant an end, once and for all, to all further investigation of the matter. It was settled.

But let's not assume anything. Why theorize as to what Mr. Law meant when we can use the same information extraction techniques that Minkow so often employs – we can simply *ask* him to clarify his answer (just as Minkow's "operatives", or heck, Minkow himself for that matter, could so easily have done), which is just what Usana did! In fact, they sent two high level corporate execs from the U.S. office to Hong Kong specifically to check out Minkow's allegations. When asked, Mr. Law stated he was referring to *all* Chinese distributors in *Hong*

*Kong*, which he assumed the "prospects" understood were all *part of China!*<sup>21</sup> Furthermore, he was guessing as to how many *total* associates had enrolled in Hong Kong, not just currently active ones (which means he was being extremely conservative!). In fact, during the attempt to entrap... I mean, interview Mr. Law, he never even remotely qualifies his estimate, yet Minkow later does it for him by claiming he said there were "currently" 30,000 "active" Chinese "nationals" (meaning residence of mainland China). These qualifiers are complete fabrications Minkow has pulled out of thin air.

Also, unlike Taiwan, those in Hong Kong are actually quite proud of the fact they are technically a part of China and routinely acknowledge this. In fact, at 11:45 into the video Mr. Law clearly refers to a "Chinese Hong Kong order" and the bank in Hong Kong he recommends they use is the "China Merchant Bank". In response to a direct question as to whether their enrollees could "recruit other people in China?", Law explained that "practically" it was possible (by setting up *legal* business entities in Hong Kong), "...but theoretically no. Actually, according to our policy, you cannot do any sponsoring activity in those areas where we haven't got any branches, like India or China. But as you know, China and Hong Kong is like one place." Why Minkow never quoted *that* statement, I completely understand.

Isn't it interesting that these "licensed investigators" would first load the question by preceding it with, "There must be quite a lot of distributors (in China)", and then ask for a "rough estimate" of such a damning number – which Minkow now exalts as the definitive smoking gun? And then, upon hearing Law's somewhat ambiguous guess, didn't bother to follow up with even *one* clarifying question? Wouldn't the obvious next step had been to confirm precisely what Mr. Law was referring to, so no one could come back with... well, *this!* But instead, the two "operatives" fain an impressed "Oooohhh, that's good." Then, apparently having procured the confession they were paid to acquire, they wrap up their lengthy interview five minutes later. As they prepare to leave, one "operative", who had earlier referred to her "friend in the United States", says to the other, "I think you should call... I think I will call your friend." Followed by a giddy chuckle. Mission *apparently* accomplished.

## Painful Sting

Another major part to Minkow's sting operation was a secretly recorded one hour phone conversation between what sounds like two English speaking American's posing as prospects, an Asian translator, and someone which Minkow identifies as Mr. Zhang Yi, the "Director of Sales for Usana Health Sciences (China)", and in the footnotes of his report describes his responsibilities as including "sales strategy and sales team development as well as client portfolio development." Minkow further claims that Yi was positioned as a medical doctor with over 20 years of experience.

The audio transcripts of this conversation are a prominent feature of Minkow's Cheating-In-China web site, and contains a few odd little curios. First, the sound quality is not just awful, but inexcusably so. It sounds as if at least one person on the line is calling from outdoors during either a period of sustained winds, or from a moving convertible with the top down (or perhaps Barry had just recently activated his ejector seat). Secondly, one of the Westerners on the call doesn't just have his voiced electronically altered to disguise it, but too obviously so. In fact, I was able to undisguise it with a simple speed and pitch adjustment (the voice was unfamiliar). Also, the disguised voice *wasn't* the one that clearly sounded like Barry Minkow! All of these subtle little James Bondish shenanigans *appear* to be nothing more than a gratuitous attempt to make the call sound more credible as part of a sophisticated "undercover" operation. Or, maybe there's more to it...

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<sup>21</sup> Although autonomous in most ways, Hong Kong is technically considered a "special administrative region" of China. See: [http://en.wikipedia.org/wiki/Special\\_administrative\\_region\\_%28People%27s\\_Republic\\_of\\_China%29](http://en.wikipedia.org/wiki/Special_administrative_region_%28People%27s_Republic_of_China%29)

To record a phone conversation without the consent of more than one participant you must initiate the call from a "one party consent state", which are most of them. Of the dozen which are not, California, where Barry resides, is one of them. So he needed to have someone conduct the call from one of the other 38 states. He chose someone in New York. What's interesting is that *this* person's voice is the one disguised, and Sam Antar<sup>22</sup> (who paid Minkow at least \$150,000 for the report on Usana, who's stock he also shorted)<sup>23</sup>, Whitney Tilson (hedge fund manager who paid \$40,000 for Minkow's report), Anthony Bruan (hedge fund manager who paid \$10,000), and Howard Sirota (attorney who represented Bruan, and Yahoo! message board Usana basher) all operate out of New York.

Mr. Yi's comments on this call are touted by Minkow as "absolute evidence" that Usana is operating "an underground pyramid" in mainland China. Although Yi does little more than describe the same strategies already covered, there's really no need to go into them in any detail.

Because, apparently, Mr. Zhang Yi *doesn't exist!*

Yes, in spite of all of the solid clues both Minkow and Usana have to work with, their "Director of Sales" for the last "two years", who's been a medical doctor for over 20 years, who's specific responsibilities within Usana Minkow so clearly defined – can't be found. In fact, Usana can't even locate his *position!* There is no "Director of Sales" anywhere in their corporate hierarchy. What's more, there is no, nor has there ever been, even a distributor by that name. One clue that Minkow might have been aware of Mr. Yi's tenuous veracity was the little excuse seed he planted as a footnote in his report. Here he hedges by disclosing "It is not known what (Yi's) Chinese name is or if he is referred to as 'Dr. Zhang' instead of 'Dr. Yi' or even 'Mr. Yi'." Another clue that *should* have tipped Minkow off was that, of all the numerous distributors and personnel interviewed, Yi is the only one to insist that his conversation be kept confidential. Why were so many others so freely and openly willing to provide essentially the same information to anyone, at any time, except for this *one* person?

What's worse is that, according to Usana, Minkow was informed that no such position exists within Usana, no such person ever worked for them, and despite their best efforts, no such person by that name (or any derivative of it) could be found. Minkow has since also been unable to locate "Mr. Yi". Strange then, isn't it, that over six months later these audio transcripts are *still* posted, unchanged, on Minkow's web site?

## More Hong Kong Capers

In his original "Cheating In China" report, Minkow also makes a big deal out of a grand total of *four* associate (not corporate) web sites that he found that appear to be promoting the establishment of Hong Kong distributorships to Chinese nationals, but in an overly aggressive and sometimes deceptive manner (i.e. making it sound simpler and easier than it really is).<sup>24</sup> He exploits one in particular as being particularly egregious and most indicative of "Usana's apathy towards these frequent and numerous abuses". The site in question belonged to Victor Yap, and his "efforts to recruit Chinese nationals" were "exposed" by Minkow using transcripts of an email dialogue between Yap and another of Minkow's "operatives", and Yap's own web

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<sup>22</sup> Antar was the co-founder and CFO of the "Crazy Eddies" electronics store chain, and was also convicted of racketeering and securities fraud in 1987.

<sup>23</sup> Previous to these payments Antar also sent Minkow \$100,000 allegedly for no other reason than to express his admiration and support. This "gift" was sent in mid-2006, right at the time that Minkow claims in his deposition he first considered a Usana investigation.

<sup>24</sup> A few other web sites were later added as additional "evidence" on the CheatingInChina.com web site.



site – which was pretty much already "exposed" to anyone on the internet (no secret password or hidden link was required). According to Minkow, when this definitive example was showcased in his report and press releases beginning October 19<sup>th</sup>, Usana's reaction was "initially not much at all."<sup>25</sup> His "evidence" of this was Yap's commission payments on October 12<sup>th</sup> of \$415.08 (although this one would have been *before* his report was first published), and another on November 2nd, 2007 of \$506.52 (never mind that these payments also provide additional evidence disproving Minkow's long standing claim that Usana distributors are "doomed to fail"). He then claims that "in fact, Mr. Yap was not even officially terminated until November 27<sup>th</sup>, 2007 – almost a month and a half after the evidence from the October report was first submitted."

So, Usana's reaction just after Minkow's first Oct. 19<sup>th</sup> report was "initially" not much. Yap wasn't "officially" terminated until November 27<sup>th</sup>. Minkow's wording here is curious for someone who normally chooses the most definitive, incriminating language. Why not just say Usana's reaction was to do *nothing*? Why say "officially" terminated when you can just say *terminated*? Oh, there's a reason.

Termination procedures against Victor Yap had *already* been initiated by Usana back in August, 2007! And *apparently* Barry knew it!

Of course Usana's "initial" reaction to his October 19<sup>th</sup> report was "not much". They had *already* taken action against Mr. Yap! Usana, like most MLM companies, has an appeals clause in their Policies & Procedures that allows a terminated associate to maintain their distributorship pending the outcome of such an appeal. Which, in the case of Mr. Yap, was exercised and which did indeed "officially" result in his final termination on November 27<sup>th</sup>. Furthermore, a web archive search shows that Yap's web site was revised to eliminate all references to Usana on August 19<sup>th</sup>, 2007<sup>26</sup> and what *was* there that supposedly so incriminated Usana was nothing more than this single paragraph:

"For INTERNATIONAL PARTICIPANTS such as HONG KONG, MALAYSIA, SINGAPORE, INDONESIA, INDIA, THAILAND, KOREA, JAPAN, BRAZIL, CANADA, USA, AUSTRALIA, NEW ZEALAND, CHINA, GERMANY, MIDDLE EAST, EUROPE, AFRICA, AND OTHERS..."

Yes, he included "China" in the list (the caps are original), but along with *nine other countries* that Usana has not opened. Which is probably why Minkow spends most of his attention on the subsequent email conversation that was initiated where Mr. Yap openly and enthusiastically offers his support to the fake prospect, even going so far as to ask him for his anniversary and birth date so he can send him a gift. Yap's contribution to these "frequent and numerous abuses" that Usana is "conspiring to conceal" was to recite, in detail and in writing, to a complete stranger, the steps to set up a legal Hong Kong distributorship. In fact, Mr. Yap appears to have been so confident that he had nothing to hide, he actually carried on this dialogue in October, while his termination was still under appeal!

In fact, Mr. Yap was warned, then eventually terminated, for two reasons: First, the above paragraph implied *anyone* from *any* country was eligible to join Usana, with no regard to the logistical challenges involved. Secondly, Yap published his own marketing web site without first having it reviewed and approved by Usana. Usana's own internal controls discovered these policy violations well before Barry Minkow did.

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<sup>25</sup> January 4<sup>th</sup> FDI press release.

<sup>26</sup> [http://web.archive.org/web/\\*/http://www.bayinspire.com](http://web.archive.org/web/*/http://www.bayinspire.com)

Minkow exhibits this same level of desperation to construct the illusion of evidence in his subsequent and similar attack on Herbalife. Here his showcase web site, presumably cherry picked as his very best example, is one where a self-proclaimed "International Herbalife distributor", Danny Castello, is seeking people with certain language skills, and merely includes "Chinese" on a list of eight languages. Mr. Castello goes on to claim his downline contains those who "live in the UK, Ireland, Italy, France, Spain, Mexico, Australia, China, Greece and South Africa." Note that "Hong Kong", where Herbalife is open and legally operating, is not included on this list, clearly suggesting Mr. Castello's understanding of geography is superior to Mr. Minkow's. That is, he understands that Hong Kong is *part of China*, and that the language spoken in Hong Kong is *Chinese!* Minkow semantically folds, spindles and mutilates these facts by asking: "How can Mr. Castello have distributors in China when the law prevents such a model? Moreover, why would this Herbalife distributor appear to be recruiting people who speak Chinese and live in China?" In a related footnote, Minkow quotes Castello as saying "We welcome all Chinese speaking customers and will assist with your Herbalife order as well as inquiries for our business opportunity here in the USA and in China", and then responds, "this statement... confirms the recruitment efforts of Chinese nationals in the U.S.". Since Herbalife *will not* ship orders into mainland China, Castello could *only* have been referring to orders into Hong Kong (or possibly Taiwan, also part of China). And again, Hong Kong *is* China, and *no where* does Castello even suggest he's looking for people who "live in" *mainland* China! Once again, this qualifier is a complete fabrication added by Minkow to force fit the facts into his allegation.

Getting back to Mr. Yapp, Minkow employs a "preemptive rebuttal", which is an effective debater's tactic where one predicts in advance his opposition's response and offers a counter-response to it unsolicited. The effectiveness of this ploy isn't so much in the counter-response as it is the reaction of the judging audience (in this case you, the reader) once his opponent does respond exactly as predicted. No matter how strong or obvious the response, it's power to influence is diminished simply by the fact he *told* you that's what they were going to say. This is one of Minkow's favorite tactics and he uses it often. In this case, he declares Usana's inevitable response to be that these are "rogue associates not within our control." Minkow continues, "Of course we are aware of the rogue associate defense and will address that later...". Other than to simply reiterate the same point once again in his conclusion, he doesn't.

While choosing his targets, Minkow has recently added not only Herbalife but also Prepaid Legal to his *short* list (pun most definitely intended). He accuses Herbalife as well of "regularly aiding and abetting the massive conspiracy to illegally recruit and pay commissions in China", based on the same openly and easily obtainable information, including a small selection of distributor web sites as discussed above. In his Herbalife attack report he states the following:

"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... 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 (related to their 'law of averages' defense)."

Here's what's funny about all of this. I mean, literally funny.

Barry Minkow has authored, co-authored, or had ghost-written but claimed he authored, five books.<sup>27</sup> All but one is essentially a telling, then repackaging, of Barry's story. There have also

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<sup>27</sup> "Making it in America" (self-published, © 1985); "Clean Sweep" (Nelson © 1995); "Buyer Beware" (Dove © 1997); "Cleaning Up" (Nelson © 2005), and; "Down But Not Out" (Nelson © 2006).

been two more objective and unfiltered tellings of the Minkow tale published by other authors.<sup>28</sup> Here's a passage from the chapter titled "Multilevel Marketing" in Minkow's book "Buyer Beware: A Home Encyclopedia":<sup>29</sup>

"Companies such as Amway, Avon, Excel, Mary Kay, Tupperware, and Herbalife are legitimate companies, but they do not have the time to investigate each and every distributor to make sure that he or she is representing the company correctly."

It's funny that Minkow not only once completely accepted this completely valid point, but here he was the *author* of it! But then, this was circa 1997 – before denouncing such explanations became profitable.

It's even funnier imagining the expression on Tracy Coenen's<sup>30</sup> face when Minkow proclaims Mary Kay Cosmetics a "legitimate company".

## Designing Facts

Within Minkow's Herbalife hit piece, which he code named "Doomed by Design", there are a number of other great examples of *designer facts* created entirely from the mind of Minkow.

At one point he quotes "one (stock) analyst" as claiming, "The prospect of China licenses for additional direct sellers beyond Avon is still the most significant catalyst we see for direct selling stocks." Here's how Minkow redesigns this comment: "Stock analysts have placed the very future of the success of the multilevel marketing industry on their ability to secure additional licensing and penetrate the market of China with its 1.2 billion people." Note how: 1) "one" analyst now becomes plural; 2) licensing in China no longer applies to just public or direct selling companies (many of which are not MLM), but now to *all* MLM companies, and; 3) licensing won't just be a catalyst to higher stock prices for the fewer than 1% of direct selling companies who are public, but now suddenly *must* happen to *save the entire network marketing industry!*

Another example is where he claims Herbalife's "ultimate goal" is to eventually get the rules changed in China to allow multilevel pay plans again, and that "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." First, I believe it is only fair that Minkow identify the psychic he hired to read the minds of Herbalife's management and investors. Secondly, the "forward-looking statement" he is referring to has nothing whatsoever to do with reopening MLM in China, and everything to do with Herbalife's *already* strong sales growth from their opening (per their license in China) of "47 stores and 37 service centers in 28 provinces throughout China."<sup>31</sup>

Immediately following the above manufactured fact, Minkow states that Herbalife, "by its own admission 'may' have Chinese nationals residing in China but signed up in other countries as Herbalife distributors...". He footnotes the source of this "admission" as page 32 of Herbalife's 2006 10-K, which we are apparently not suppose to go and actually verify. Because, if we do, we would find *no reference of any kind* to Herbalife being concerned about Chinese nationals being signing up in other countries (such as Hong Kong). Herbalife only acknowledges the

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<sup>28</sup> "Faking it in America" (Joe Domanick © 1989), and; "WonderBoy" (Daniel Akst © 1990).

<sup>29</sup> Page 158.

<sup>30</sup> Coenen was a contributor to Minkow's anti-Usana report and an ongoing Minkow propagandist, as well as a board member of the Pyramid Scheme Alert organization. She also operates an anti-Mary Kay web site.

<sup>31</sup> Third quarter 10-Q, 2007.

possibility that there may be those within or outside of China who may "violate our policies... or Chinese law." They make no mention of any specific ways this might be done, nor would they in the case of someone in China establishing a distributorship within Hong Kong, because it's *legal*! Minkow *completely made this part up!*

Like Usana, Minkow again turns to "government recognized expert on multilevel marketing, Robert FitzPatrick" to supply more ammunition. He claims FitzPatrick was "hired in 2005" by the Chinese government "to help them analyze whether or not China should allow multilevel marketing in that country." He then claims "In November of 2005, China passed a law prohibiting multilevel marketing in that country." No, they didn't. MLM was banned in China in 1998, and FitzPatrick had nothing to do with that decision. What's odd is that this can't be a simple misprint as Minkow states this ban as commencing in November of 2005 a total of *three times* in his report. Actually, September of 2005 was when China changed the law to allow some direct sellers, such as Avon, and eventually Herbalife, *back into* China! Doesn't he have some "experts" that can help him with this kind of stuff?

Here is an example that clearly demonstrates Minkow's disdain for the intelligence of his audience. He cites Herbalife's late filing of their third quarter form 10-Q in 2006 and claims "the reason for that late filing seems to have changed" between the Thursday and Monday that two versions of the company's explanation was published. Here he obviously implies that Herbalife has been disingenuous in at least one version of their explanation. You be the judge:

Version One: Despite diligent efforts, the Company was unable to file the Form 10-Q... primarily because the Company was unable to finalize review procedures with are necessary to complete the Company's financial reporting requirements..." (the underline is Minkow's).

Version Two: 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 request for extension on Form 12b-25 with the Securities and Exchange Commission (again the underline is Minkow's).

Basically, each version is saying *the exact same thing*, only with more detail in the second version. This is analogous to a motorist claiming he was late for a meeting because he had to pull over and check why a warning light was lit on his dashboard, then later explaining that he was late because a warning light went off on his dashboard which was due to engine overheating caused by a broken fan belt. In Barry Minkow's world the driver didn't voluntarily provide *more* information in his second explanation, he *withheld* information in his first one. Of course, that's only if the driver was the CEO of a public MLM company.

How does Barry Minkow still have *any* credibility left? Isn't anyone else in the government or media besides me seeing through all of this? Well, I mean, except for the SEC, which did investigate all of Minkow's accusations against Usana – and apparently saw through *all of it!*

## **Inventing Investigations**

When Minkow's Usana report, or more specifically The Wall Street Journal's reporting of it, first spurred an "informal inquiry" into Usana by the SEC, it was routinely referred to by ignorant (or dishonest) members of Team Minkow as an "SEC Investigation". The difference is more than semantic. A "formal investigation" is what an "informal inquiry" is promoted to if any evidence of wrong doing is discovered, or even suspected. The SEC closed their "inquiry"

into Usana after ten months with no action of any kind being taken – even after they "inquired" about Minkow's Cheating-In-China allegations!

Also in Minkow's first report he makes reference to an IRS "criminal" investigation of Dr. Wentz back in 2004-05. There was no such investigation.<sup>32</sup>

Forbes magazine and the New Zealand based National Business Review each cited an unnamed source confirming an FBI investigation of Usana in late 2007 (which neither publication apparently made any attempt to confirm). Minkow himself disclosed in a subsequent Wall Street Journal article that, in fact, the FBI had deferred any such investigation to the SEC. And we know how that ended.

And now, according to Minkow, the Chinese government has commenced an investigation into Usana corporate. First he claims the Nanning Business Administration Department has sent a "notice of interrogation" which "seeks to investigate the alleged multilevel marketing activities of Usana Health Sciences Inc. through an alleged associate(s) in that region". Then to remove any ambiguity as to whether this notice is really directed at Usana or just a single distributor, he adds the comment, "It would appear that the interrogation notice is interested in both the individual and the company as a whole. This is not an isolated look at one bad apple." Except, the notice *wasn't* directed at Usana, and *was* an isolated look at one apple (who may or may not have been "bad"). The reason Minkow must include this description of how the notice "appears" to him is because if it does involve only a single, isolated incidence it greatly diminishes its value as a stock devaluation device. At least, that's how it *appears* to me.

Here is the actual English translation of the section in question:

"Meng Yxxxx: In order to investigate and obtain information, you have been doing Usana product sales activity, which is suspected to be doing multilevel marketing activity."

Obviously the translation (the source of which Minkow does not disclose) is inaccurate. Surely the author did not intend to say that the recipient (who's last name was redacted) was doing this sales activity for the purpose of investigation and obtaining information. It is also obvious, even through the disjointed language, what the intended meaning of the Usana reference was. The writer was simply saying that the products Meng was allegedly selling were from a multilevel marketing company, thus fell within the restrictions on such selling activity. Furthermore, the "suspected" inappropriate activity was clearly defined as the selling of products, not recruiting into an MLM, and it was blatantly obvious who the notice was solely and specifically directed towards because it distinctly *identified* them – and it *wasn't* Usana!

And apparently it wasn't even a Usana *distributor*! No such associate by the name shown in the notice exists anywhere in Usana's distributor scrolls, past or present.<sup>33</sup>

Oh, and one more thing: This notice was issued on December 27<sup>th</sup>, 2007. As of this writing, more than six months later, and over nine months since Minkow first sent his "Cheating in China" report to legal authorities in China, Usana corporate has had no contact with any regulatory agency in China related to this issue. Neither their U.S. headquarters, nor their Hong Kong office. None.

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<sup>32</sup> Dr. Wentz did have his returns from two years in the mid-90s investigated by the IRS in the late 90s, but he was cleared and the investigation was dismissed without any finding of wrong doing.

<sup>33</sup> Such non-distributor sales activity is actually quite common. For example, based on research ironically performed by a Team Minkow member, as of July of 2007 eight of the top ten resellers of Usana products on eBay, totaling \$26,902 in sales to end user customers (which Minkow claims do not exist *at all*), are *not* distributors (the other two were also likely not distributors, but this cannot be confirmed).

## Stopping Traffic

Several times throughout his "Cheating in China" report Minkow paradoxically sites reasons why Usana should know better than to try to build downlines and sell product within mainland China. For example, he cites a three year old online article (translated from Chinese), that quotes from another article, describing how "overseas sales teams" from Usana were conducting "online trafficking" of Chinese nationals into their downlines. Since just "trafficking" sounds more sinister than the original "online trafficking" Minkow never once uses the qualifier in his own report (for that matter, the original symbols used in the article [偷渡] directly translate to "sneak crossing"). He goes on to comment, "the company was forced to address the problem", and, "Based on this past issue, Usana knew the laws of the Chinese government, had experienced an embarrassing incident as a result of apparently abusing those laws, and then just continued with increased zeal to expand their illegal Chinese operations all the while risking public scrutiny if caught."

Usana did "address the problem" back in '05 when a distributor group, known as "The Evergreen Team" attempted to recruit Chinese nationals online. Usana discovered their activity using their own internal controls and promptly shut them down. But then this group set up their own web site, making it appear to be the same corporate site, and continued to enroll people using fake applications. Their "downline" was entirely virtual, and no one was actually a Usana distributor (they never entered the Usana system). This, of course, made it difficult for Usana to take further action. How do you terminate a distributor that is not a distributor?

Usana was never challenged by any legal authority in China over this renegade web site, and they dealt with it back then as effectively as was possible. Minkow provides no evidence to support his claim that "the company was forced to address the problem" (emphasis mine). His claim that Usana was "embarrassed" by this incident is also wholly unsupported. Other than being mentioned as one example (among others) within a broader article about direct sales companies entering China (the article was not specifically about Usana), that appears to have only been published online, I have no idea why this would have "embarrassed" Usana, nor how Minkow could possibly have known how "Usana" felt about the incident. None-the-less, he continues to not only reference this single incident but later in his report he upgrades it to the plural "embarrassing experiences".

As one of his "Core Facts", Minkow states, "It is abundantly clear that Usana officials **know the laws of China and the restrictions associated with those laws, including the specific illegal 'structuring' of Chinese nationals into Hong Kong downlines**" (bold is original). A foot note within this statement references Usana's own 10-K where they acknowledge the restrictions on recruiting and selling in China, which states:

"China announced the adoption of new regulations governing direct selling. Single-level compensation models are permissible under these new regulations, but multi-level compensation models, as practiced by USANA and many other direct selling companies, are not."

It's unclear how Minkow believes his acknowledgement of this public disclosure supports his position. But what is most disconcerting about his bold exclamation is not only his specific reference to there being laws within China that specifically define the establishment of Hong Kong distributorships as illegal, but he even footnotes a link to the actual regulation that prohibits MLM on China's Ministry of Commerce web site.<sup>34</sup> The problem being, there is no such law forbidding this, nor do any of the regulations he links to even address this practice,

<sup>34</sup> <http://tinyurl.com/54mthr>

let alone specifically forbid it! As long as no sales or recruiting activity is being conducted physically within mainland China (i.e. you can't conduct a live meeting on mainland Chinese soil that instructs attendees on how to set up any kind of MLM distributorship), and all such activity is initiated and conducted outside of mainland China, there is no violation of any Chinese law. And Minkow provided absolutely *no* evidence to the contrary!

At one point Minkow devotes an entire page to how "Chinese law enforcement officials care about these abuses and zealously prosecute offender." He's right. According to the various articles he includes as addendums (besides the one discussed above, none even mention Usana), Chinese law enforcement has been "relentlessly dismantling multilevel marketing" operations. Their "harsh crack-down" on MLM activities within mainland China has involved "1,915 cases" and the arrest of "more than 16,700 people".<sup>35</sup> Yet, in spite of an alleged 30,000 such law breakers coming from Usana alone, not one word of concern from these same authorities has been directed towards Usana corporate. Strange, isn't it? Another article sites about ten months of statistics related to only the city of Nanning, where 84 people were arrested and "destroyed" 192 MLM groups – a "severe blow to enter Nanning City to carry out illegal (MLM) activities".<sup>36</sup> That would be the same city of Nanning which issued the "interrogation letter" to the mysteriously anonymous Usana product seller. Yet, no letters to Usana. Another inadvertent example submitted by Minkow of the immense dichotomy between China's exceptionally aggressive enforcement of their MLM restrictions and their utter disinterest in Usana is an article titled "Authorities Warn Over Pyramid Sales".<sup>37</sup> Within, Mr. Gao Feng, the Deputy Director of the Economic Crime Investigation Department of China's Ministry of Public Security, is quoted as saying his department had investigated 1,499 cases, detained an average of 32 suspects *per day*, and that China's SAIC<sup>38</sup> (comparable to our own FTC) had "dismantled 24,446 pyramid selling schemes"<sup>39</sup> in just the first ten months of 2006. He goes on to state that whenever any such activity "appears on our radar" his department "will waste no time in smashing it." Both Mr. Feng and a deputy chief from the SAIC are quoted as declaring their efforts to "ultimately eliminate the illegal marketing mode" a "success". "Following repeated crackdowns in recent years," Mr. Feng continues, "pyramid selling has been curbed in most parts of China." I guess Usana must have found one of those little parts where it hasn't to hide those 30,000 distributors.

At one point Minkow boldly (literally) summarizes this point by stating: "The Chinese government and Chinese law enforcement officials **care about these abuses and zealously prosecute offenders.**" Exactly! So why have they all, even with Barry metaphorically but firmly pressing his palms against the sides of their heads and forcing them to look towards all of his "extensive" and "absolute evidence", completely ignored it?! And get this: besides the Director of the SAIC, Minkow also addressed his Cheating in China report to Mr. Gao "waste no time in smashing it" Feng. Even *he* appears to have been unmoved to act on it!

Minkow continues firing his evidentiary buckshot with the subsequent comment: "For a public company to know this, have experienced this, and then risk the potential embarrassment that accompanies being caught breaking these laws again is simply reckless behavior." This comment immediately followed the one in bold above, therefore no other correlation can be made to the "have experienced this" segment other than to his previous reference to how

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<sup>35</sup> "Crackdown of Mainland Illegal Pyramid Schemes"; Sun News, 4/10/2007

<sup>36</sup> Guangxi News Network.

<sup>37</sup> China Daily, 11/23/2006.

<sup>38</sup> State Administration for Industry and Commerce.

<sup>39</sup> The article, which is poorly translated, appears to be primarily referring to blatant pyramid schemes. But based on the scope of China's ban on *anything* with a multilevel commission system, legitimate network marketing companies would be included in such enforcement activity.

Chinese official's "zealously prosecute offenders". But, again, no Chinese officials at any level of local, provincial or national government has *ever even communicated* with Usana corporate regarding any form of illegal recruiting or sales activity! The only event that Minkow could possibly be exploiting here to rationalize his claim of "experience" with Chinese authorities is the online news report from '05 that mentions the "Evergreen Team" rogue web site, which Usana "smashed" and "dismantled" on their own, without any regulatory encouragement!

In his effort to fabricate even more kitchen sink parts, he continues with: "To attempt to dismiss Usana's alleged current activities in China with an assertion that 'everybody is doing it' or 'the Chinese government knowingly allows such practices without enforcement,' flies in the face of the recent verifiable evidence" (emphasis mine<sup>40</sup>). Although placed in quotes, Minkow offers no guidance as to where or when anyone from Usana has ever employed such responses. Probably because no one, at least of any authority, ever has.

## Tall Tattle Tales

The object of Minkow's efforts here isn't just to get Usana in Dutch with China. Where he and other short sellers would really score is with Wall Street, and the SEC. He also tries to make a case to both that Usana's reported revenue figures were significantly inflated due to all these tens-of-thousands of illegally enrolled associates in China, that no one can actually find. If he were to successfully make this case the SEC inquiry would surely have been elevated to a full on investigation, Usana would likely have had to restate earnings for at least the last two years (excluding the ill-begotten gains from China), and most certainly their stock would nose dive – again. And anyone who had shorted it would be partying like it's 1999 and they were long on tech stocks.

There was no party.

Upon presenting his case Minkow stumbles at step one by cited Usana's reported 116% year over year associate growth in Hong Kong in their "most recent" 10-Q<sup>41</sup> filed with the SEC, which would have represented the second quarter of 2007. Not only does he direct by footnote to fourth quarter 2006 data (and to the wrong page number), but if you were to review the entire "most recent" 10-Q from which he is actually citing this data you would also find that this large *percentage* increase was due to only a net gain of 7,000 active distributors in Hong Kong (6,000 to 13,000). In fact, here is how Minkow presents all of his stats on this point:

- In 2006 net sales increased 31.4% over 2005; as compared to an increase of only 12.9% in 2005 over 2004.
- In 2006 active associates increased 125% over 2005; as compared to a decrease of 20% from January 1, 2005 to December 31, 2005.
- In 2006 total active customers increased 125% over 2005; as compared to a decrease of 33.3% from January 1, 2005 to December 31, 2005.
- 2nd Quarter 2006 compared to 2nd Quarter 2005:
  - o Sales: 81.1% increase.
  - o Active Associates: 116.7% increase.
  - o Total active customers: 133.3% increase.

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<sup>40</sup> Suddenly they are no longer "absolute" activities, but are demoted to merely "alleged" ones. But Minkow regains adjective balance in the following paragraph where he then refers to such activities as "disturbing."

<sup>41</sup> A 10-Q is a detailed quarterly disclosure of a companies financial condition. A 10-K, referred to elsewhere in this report, is an annual disclosure.



This is another cute little debater's trick Minkow often employs, and it *appears* he's doing it deliberately by such qualifying comments as "this is a substantial percentage increase...". I think there's a reason why he doesn't simply say "substantial increase", nor does he even once cite the *number* that represents this increase – because he knows there was no substantial increase in the actual rep count in Hong Kong. Consider this: If Usana were to open, let's say, Macau (another "special administrative region"<sup>42</sup> that, like Hong Kong, falls within China's "one country, two systems"<sup>43</sup> policy) and added 30,000 reps to their previous year's total of 5,000, that would be a 600% increase. But which number would a Usana antagonist use to support a claim of 30,000 illegal, underground reps in mainland China? Sure, he's probably use both, but certainly the *number* count would be showcased (but not here – why not?). If only 300 reps were added (let's say, 50 up to 350), you'd see "**600 PERCENT INCREASE!!!**" emblazoned across every page – and not a word about how many new reps were actually gained.

I appreciate that to some this may seem petty or insignificant, but an awareness of the manipulative psychology Minkow often uses, in this "Cheating" report more than ever, is what I'm trying to expose here more than simply the mathematics. Another great example is when, in an effort to show that very few were ordering Usana product because they genuinely wanted them, Minkow claimed in the press release for his original report that "only 14% of company revenues stem from retail sales." Of course, he was fully aware that this figure related to sales only by the company to those who signed up as "Preferred Customers" (not all sales of Usana products to non-distributors) and "only 14%" of this revenue came from 76,000 Preferred Customers! But which sounds more like a low amount: 14%, or 76,000? Yes, *percentages* are a math manipulators favorite tool.

Some of the manipulation employed here is more blatant. When reading the second and third bullet points above, and the bottom two under the fourth point, did you assume these were mutually exclusive classes of revenue sources? They are not. In fact, this is virtually the same group of people who's designations in Usana's 10-K Minkow exploits to pad his evidence list. "Active customers" is simply "active associates" plus "preferred customers", of which there were fewer than 500 in Hong Kong at the time.

Minkow also references the slower growth, or even declines in Hong Kong in the preceding year, which is accurate. In fact, here's some Hong Kong data since Usana's launch there in 2000:

	Active Associates	Percent Change	Sales (thousands)	Percent Change
2007	13,300	48%	24,400	52%
2006	9,000	125%	16,049	31%
2005	4,000	-20%	12,217	9%
2004	5,000	25%	11,117	26%
2003	4,000	0%	8,850	25%
2002	4,000	33%	7,098	36%
2001	3,000	-20%	5,208	-20%
2000	3,500	120%	6,471	120%
1999	1,500		2,941	

<sup>42</sup> [http://en.wikipedia.org/wiki/Special\\_administrative\\_region\\_%28People%27s\\_Republic\\_of\\_China%29](http://en.wikipedia.org/wiki/Special_administrative_region_%28People%27s_Republic_of_China%29)

<sup>43</sup> [http://en.wikipedia.org/wiki/One\\_country,\\_two\\_systems](http://en.wikipedia.org/wiki/One_country,_two_systems)

	Active Associates	Percent Asia/Pac	Asia/Pacific
Q1-08	12,100	17.5%	69,000
Q4-07	13,300	17.5%	76,000
Q3-07	13,000	17.3%	75,000
Q2-07	13,000	17.6%	74,000
Q1-07	9,000	14.3%	63,000
Q4-06	9,000	15.3%	59,000
Q3-06	8,000	14.5%	55,000
Q2-06	6,000	11.5%	52,000
Q1-06	5,000	10.0%	50,000

The numbers in red are estimates due to Usana's lumping of various markets into "regions" beginning with their 2007 10-K. However, based on what percentage Hong Kong was of the entire Asia/Pacific region the previous two quarters (17.6% and 17.3%) it is very reasonable to assume it was 17.5% in Q4-07 and Q1-08. The blue estimates are extrapolated from annual sales for those years. This is due to Usana's counting at year's end of all reps during 1999 and 2000, which was adjusted to the more accurate "active"<sup>44</sup> classification beginning in 2001.

So, this begs a question. Are we suppose to except Minkow's premise that these Honk Kong, nay *world wide*, Usana associates didn't figure out how to tap into this supposed underground mainland China gold mine for the first *seven years* after Usana launched Honk Kong (in 1999, the year after China banned all forms of direct sales), but then sometime during 2006 they all suddenly realized, "Hey, let's get them to create Honk Kong distributorships!?" And then, for some unknown reason, during the third quarter of 2007 – well *before* Minkow's Cheating-in-China material was published – they began to abandon this strategy that was supposedly causing all this massive growth? Certainly no rational person can attribute this to "saturation" of the Chinese market. Or, could Usana have simply followed the same general "foundation - momentum - stability" growth cycle that practically *every* enduring MLM company goes through! In deed, not only does Usana's growth pattern in Hong Kong track perfectly with many other companies who have entered foreign markets, but its even commensurate with their growth phases here in the United States (although somewhat more protracted). Based on industry wide historical precedent, there is absolutely *nothing* about Usana's associate growth in Hong Kong that is the least bit unusual. In fact, had Minkow and his minions not created such an acidic cyberspace environment for Usana associates the growth in Hong Kong the past couple of years would likely have been substantially greater!

There is more evidence against Minkow's case that, although circumstantial, would be compelling to anyone who actually understood the inner workings of this form of business (doesn't Team Minkow include several "multilevel marketing experts"?). In most MLM programs a new distributor's first order is typically their largest for no other reason than they simply want to experience and become familiar with a lot of the products, plus there are often initial "activation" quotas that encourage this, and more highly reward the establishment of initial inventory.<sup>45</sup> This is the case with Usana, therefore a disproportionate number of new enrollees during a given period should result in sales growth significantly *higher* than associate growth. However, Minkow's reporting of year-end 2006 data shows Usana gaining

<sup>44</sup> Those who have produced sales volume within the past three months.

<sup>45</sup> When too much product is purchased up front, or is purchased as merely a token act to meet personal or group volume quotas with no actual interest in the value of the product, this can be considered "front loading". This practice has been deemed illegal and is taboo in the vast majority of MLM companies. It also usually involves an initial order costing several thousand dollars. Usana's "activation" qualifications are, at most, only \$450 US, and is not required to be an associate.

116.7% more associates in Hong Kong, but only an 81.1% increase in sales. If a large proportion of this 116.7% gain were Chinese nationals activating new distributorships in Hong Kong these numbers should be the *opposite* of what they are!

Perhaps the most amusing and obvious display of Minkow's manipulation and gamesmanship is where he sites Herbalife's growth rates in Hong Kong and Taiwan during this same period. But here he has a major challenge to overcome. Because, you see, Herbalife *didn't* have the same kind of disproportionate growth in these regions like Usana did. In fact, Herbalife's sales *decreased* 29% during 2006 in Hong Kong, and were down 4% in Taiwan! So, how is Usana's exceptional *growth* in these regions "evidence" of Chinese nationals enrolling there en mass, but when exactly the opposite happens in Herbalife it's not evidence of the contrary? How does Minkow reconcile this blatant contradiction? He doesn't. Instead he tries to divert attention to Herbalife's explanation for this downtrend<sup>46</sup> and completely ignores the conceptual white elephant sitting between his two reports. What's most amazing is that he actually seems to expect *you*, the reviewer of his reports, to be *ignore*-ant of it as well!

## "Deviant Practices"

Cathy, an "operative" in yet another Minkow directed covert operation, was sent deeper undercover to gather intel by infiltrating Usana's prospect pool and eventually gaining the confidence of their customer support staff. This was accomplished by the investigator calling Usana Hong Kong's support line, and identifying themselves as a prospect. Then, once again, they applied the proven "illegal... black market... money laundering... fraud" busting tactic of *asking!* I just can't emphasize this point enough. *That's* how "concealed" and "underground" Usana's illicit "trafficking" operation was.

Two such calls were recorded and transcribed in Minkow's report (we are not told how many total calls were made). In each case the fake prospect was again informed that no products could be shipped into mainland China, nor could commission checks be paid to a resident there of. The distributorship must be operated from within Hong Kong, and then basic instructions were given on how to accomplish this.

And yes, in his zeal to conjure up within the reader the most visceral and negative impression of Usana possible, Minkow actually refers to this as one of Usana's "deviant practices."<sup>47</sup>

As I watched the video of Mr. Law, listened to the audio of Mr. Yi, read through the transcript of the email conversion with Mr. Yap, and now of these two calls, I've always been struck by the complete absence of any line of questioning that would clearly and definitively expose Usana's awareness of their guilt, and their efforts to conceal it. Why was no one *ever* asked point blank what the Chinese government thought of this practice, or what would happen if they found out that the distributorship in Hong Kong was owned and operated by a resident of mainland China? Why not ask for verification that this practice was not in violation of Chinese law? Why not ask for a specific explanation as to why this was not in violation? Why were *any* follow up questions that might have given the Usana rep an opportunity to legitimize or in any way support their suggestions completely avoided? Or, were these questions asked, and the responses now clutter Minkow's editing room floor?

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<sup>46</sup> That Hong Kong and Taiwanese reps are diverting their attention to mainland China, where Herbalife had just been granted a license to sell there on a direct sales basis.

<sup>47</sup> Minkow has previously referred to Usana during a televised interview (TheStreet.com) as "evil".

## Go Team Minkow!

At least Minkow has a profit motive beyond simply assuaging his own ego, which Barry himself describes as "avaricious". It seems the same cannot be said for Team Minkow's head cheerleader Tracy Coenen, who dutifully glorified Minkow's "Cheating in China" campaign in her blog. This assumes, of course, she is also not short Usana's stock. I sent a short, polite email asking her if she was short either Usana or Herbalife and in response she posted an 800+ word blog entry made up mostly of her gloating over how much I was apparently paying attention to her recently. For example, "In the last **eleven days**, Len Clements has made **92 visits** to my website" (apparently Tracy still doesn't understand the difference between "hits" and "visits", and the emphasis is original). She even listed all the sections of her site I had visited, and the exact search terms I used.<sup>48</sup> This isn't the first time she's done this kind of thing. Just a few days ago she railed over a company called LifeLock, then seemed almost giddy with pride in her follow up post describing how the company had actually *responded to her!* Considering the dearth of comments following each of her blog entries I suppose I can appreciate why she would get so excited over someone actually acknowledging her. I see people I've reported negatively on visiting my site all the time. I've kind of gotten used to it. Years ago, actually.

What's most telling is that no where in this long, acerbic response to my question as to whether or not Tracy was short Usana or Herbalife's stock does she include the word, "No".

Ms. Coenen is not just a card carrying board member of Robert FitzPatrick's Pyramid Scheme Alert organization, she is also a forensic accountant and fraud investigator her own self. Having those types of skills makes her full and unflinching support of everything Minkow says all the more – curious. For example, Peter, a reader of her blog that actually seems capable of thinking for himself, asked of her this question in early January, 2008:

"My understanding is that your organization has uncovered numerous instances of criminality by Usana by recruiting for and running MLM schemes in China. But what I can't understand is whether or not your efforts have led to the GOVT of China actually investigating Usana, and if your discoveries are accurate (30,000 MLM members in China), the Chinese authorities are/will be inclined to shut all of them down?"

Here is her response:

"China is investigating. Obviously it may take some time before action is taken."

We know now that not only was China *not* investigating, there was absolutely no evidence that they were at the time of her response (and if they were, it *doesn't* take them much time to take action). All she was relying on was what she heard from Barry Minkow. Which she accepted without question.

In early November, 2007, Coenen wrote this passage in her blog:

"About the only way Usana can get out of this one is to offer up a sacrificial lamb. Make Richardson the one who was responsible for it all. Get rid of him and vow to make things right in China. That's really their only chance for survival."

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<sup>48</sup> She also fabricated several outright false statements, such as the media and Usana have "totally ignored" my previous rebuttal reports (if she only knew how wrong that was!), and that she can somehow tell I've got a folder on my computer's desktop entitled "Coenen," in which I save copies of certain pages of her website (I don't).

Surely someone in her position, with her credentials, wouldn't cast in cyber-stone for all the world to see such a dire prediction that Usana's "only chance for survival" would be to make Brad Richardson, Usana's Executive VP of Asia Pacific, a scapegoat. Certainly Coenen *must* have had a substantial amount of evidence that: A) Usana is guilty of everything Minkow is claiming; B) An indictment of Usana on these issues would result in their ultimate demise, and; 3) That Mr. Richardson was indeed aware of, and to some degree responsible for, this potentially company destroying practice. Wouldn't she?

She continues:

"Fortunately (sic), the SEC is not that stupid. They (and we) know that Bradford Richardson was not solely responsible for the shenanigans in China. Dave Wentz is in on it. Myron Wentz is in on it. Gil Fuller is in on it. They are all actively involved in the China mess, and not only knew about it, but approved of it as well. Getting rid of Richardson will be a nice gesture, but it won't work."

*We know all this? Really? To the day of this writing, now seven months after Coenen made these remarks, she has yet to explain how everyone not only knows Usana was completely guilty of all this Cheating in China, but we all know precisely who within Usana was "in on it" and "approved of it". She hasn't offered one word to explain why everyone knows all of these things – except for those Chinese government regulators who would most care about knowing all of this!*

Oh, and one more thing. Mr. Richardson did recently resign (seven months after Coenen's comments), but did so completely voluntarily to pursue another opportunity, and with not a peep from anyone about anything related to China. Tracy Coenen could not have been more wrong, in more ways.

Before we leave the subject of Tracy Coenen, here's one more quote from a more recent post:

"I get nothing from warning consumers about these sketchy companies, other than the satisfaction that the information was made available for those who take the time to research."

*Take the time to research.* Perhaps Tracy Coenen, CPA, MBA, CFE, might want to try that the next time Barry Minkow throws up another propaganda web site. Heck, I was able to easily discover his entire Cheating in China attack was without merit in a matter of hours – and I don't have *any* letters after my name!

## **Conclusion**

I will conclude where Minkow does. In his "Cheating in China" conclusion he reminds us that "Chinese law enforcement officials... are aggressively investigating and pursuing violators." He's right. And I'll remind you, it's been over two years since, according to Barry, Usana has started to cheat in China, and nine months since he tried to throw them under the regulatory rickshaw – and not only have Chinese law enforcement officials not aggressively pursued Usana, they have not even contacted them (nor, to my knowledge, have they contacted Herbalife). Minkow goes on to reiterate how "...public company regulations in the United States do not take lightly a company's efforts to illegally increase sales... The cost of being a public company in the U.S. is being held accountable by the SEC and other regulators." Again, he is correct. However, the SEC inquiry into Usana that was initiated due to Minkow's original report<sup>49</sup> (indicating Minkow has, or at least had, some credibility with this agency), extended almost three months beyond Minkow's exposé of these "crimes" committed against Chinese

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<sup>49</sup> Published in March of 2007.

nationals by this "absolutely illegal multi-level marketing business model." The SEC apparently disagrees with Minkow as well. They closed their investigation without finding *anything* that warranted *any* type of enforcement action – including any related to sales in China.

Within his Herbalife conclusion he asks us "what are the odds" that he and his secret agents would find "the needle in a hay stack every time and every where we looked?" What are the odds, he goes on, that virtually every Herbalife employee and distributor they contacted would all say "the exact same thing" about how a Chinese national would establish a distributor business in Hong Kong if it were not a "common practice that occurs daily all over the world"? He suggests "a million to one". I think it's probably closer to 1:1, and here's why: Let's say you live in Nevada, but want to vote in the California primary. You ask 100 people at random *how* you would go about doing that. What are the odds that all 100 people would say, "Move to California!". Of course, setting up a primary residence in California, and establishing it long enough to have it qualify as such, would be time consuming and expensive. But, like Minkow's "operatives", you didn't ask for reasons *not* to do it, you simply asked "how". Although the difficulties with setting up an MLM distributorship in Hong Kong certainly aren't on the level of moving your residence to another state, it still poses challenges. Minkow at least allowed us a glimpse of some of them when it was revealed that products must be double shipped and it takes 2-3 months to establish the requisite bank account. But again, this does raise a very big question: Why not ask such questions as: Would you recommend I do this?; What are the problems I might have with this?; How many others are doing it this way?; or the overwhelmingly obvious, but *not once* asked question, What does the Chinese government think of this? If Minkow was really digging for the *truth*, and not just for the dirt itself, why *not* ask these more probing and definitive questions regardless of their potential to exonerate his subject?

For that matter, why has Barry Minkow *not once* even attempted to contact anyone in senior management from either Usana or Herbalife to *ask* them for an explanation to any of his concerns? Why does he only get the side of the story told to him by the alleged "victim", or "perpetrator", or anti-MLM "expert"? If his investigations are *really* about uncovering facts, and truths, and yes even mistakes or outright lies – but then *correcting them* – why has he *never* called anyone at Usana or Herbalife to get their side of the story? Why has he *never* contacted them first to inform them of his concern to see how they respond to it? Had he simply called Usana corporate and asked them about Victor Yapp he would have known that they had already taken action against him, and the status of that action. Had he called and asked he would have known that Zhang Yi was a fake, and that he was likely being set up. His Herbalife report is loaded with rhetorical questions and assumptions and subjective accusations. Why guess? Why wonder? Why not *just ask!*

Or, is this really not at all about righting wrongs anymore? Is Minkow really still trying to "get to the bottom" of the story – or is this now all about getting a company's stock price to the bottom?

Barry is fond of describing how the financial disclosures provided by public companies are what investors "relied upon" when making their investment decisions, thus the importance that this information be reliable. What makes Minkow's investigation and findings related to Usana so ironic and hypocritical is his apparent willingness to accept completely unreliable, or at least suspect, information about Usana if it in any way devalues the company. When information he has already presented is shown to be unreliable, or completely fictitious (such as the audio transcripts of Zhang Yi), why does Minkow continue to present it? Shouldn't the information provided by Barry Minkow and his "Fraud Discovery Institute" that we, and the federal agencies he provides it to, all "relied upon" be held to the same standard?

Minkow's perfect 13-0 take down record (at the time) is now ruined. Of all the agencies he has presented his findings to (SEC, FBI, IRS, and China's SAIC and ECID), only the SEC chose to investigate – and found *none* of his claims worth pursuing. This is what I was referring to earlier in this rebuttal report when I claimed that, even after all of these strafing and bombing runs my Team Minkow, Usana's "foundation has nary more than a few micro-fractures". That is, their foundation as a legal, viable business. But then, that certainly doesn't mean Minkow and his agents were not successful in damaging Usana's growth, at least in the U.S., and they certainly appear to have played a major (if not, in my opinion, *sole*) roll in successfully pulling Usana's share price from the high 50s to the low 20s. Which, ironically, *cost* those very investors Minkow claims he's trying to protect *multiple millions of dollars* – while he and his financial backers made substantial profits. So as far as making money from his Usana attacks – Mission Accomplished.

But getting the company shut down based on its illegality? That was Mission Impossible.

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Since 1989, Leonard Clements has concentrated his full-time efforts on researching and analyzing all aspects of Network Marketing. He is a professional speaker and trainer, and currently conducts "Inside Network Marketing" seminars throughout the world. Len is the author of the controversial book "Inside Network Marketing" and the best selling cassette tapes "Case Closed! The Whole Truth About Network Marketing" and "The Coming Network Marketing Boom." He is a court recognized expert in the field of network marketing.

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