

Multi-Level Marketing Gets Multi-Level Attention

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Multi-level marketing has touched us all – whether it be purchasing beauty products, essential oils, or health supplements from a friend through social media, or receiving an invitation to join a team of seemingly successful people working their “side hustle.” But multi-level marketing is now getting some additional multi-level attention, both in the media and in the court room.

With interest in documentaries on the rise throughout the pandemic, Amazon recently delivered with its four-part docu-series “LuLaRich.” It follows the multi-level marketing company, LuLaRoe, which is known for its colorfully patterned clothing, messages of empowering women, and nearly \$2 billion in purported sales in a single year. But the docu-series also offers a glimpse at the dividing line between a multi-level marketing platform and a pyramid scheme, with the latter running afoul of the law.

Throughout its short existence, LuLaRoe has been no stranger to litigation. Several class actions have been filed against it, including one with allegations that LuLaRoe’s leggings ripped as easily as wet toilet paper. But most notable is a recent class action that was certified just last month by a Federal Court in Alaska. See, e.g., *Katie Van et al. v. LLR Inc. dba LuLaRoe et al.*, No. 3:18-cv-00197, in the United States District Court for the District of Alaska. The claims in *Van* allege that LuLaRoe charged sales tax on purchases to customers located in tax-free jurisdictions. This was, allegedly, the result of a customized point-of-sale system that did not allow sales tax to be assessed based on the location to where the “retailer” (sales person) shipped the merchandise. LuLaRoe addressed this by creating a “toggle switch” that allowed retailers to “turn off” the automatic tax charges and charge a different amount, including 0%. However, some retailers used the toggle switch to override the collection of sales taxes on taxable transactions while others did not use the toggle switch to override sales taxes on transactions that were not taxable. When LuLaRoe became aware of this, it allegedly disabled the toggle switch and asked retailers to leave the system’s sales tax box “checked,” while LuLaRoe developed a system that would compute and collect sales tax based on the address where the product was purchased and received. The outcome: consumers in jurisdictions without sales tax (or no sales tax on clothing) were improperly billed for sales tax on their purchases, based on the taxes imposed by the retailer’s location, rather than the consumer’s location. The certified class claim alleges LuLaRoe engaged in an unfair trade practice with the imposition of this non-existent sales tax. And, while attempts at similar class actions against LuLaRoe have been made in the past, this class, with more than 10,000 potential class members, has now been certified.

With so many sales happening through social media controlled by individual retailers, multi-level marketing entities must address unique challenges, including the calculation and imposition of sales tax, especially when customers are located in different states (or even different countries) than their sales person, as was the case in *Van*. Having the requisite resources – whether that be through staffing or usable technology and software – can be challenging when trying to keep up with the quick growth that often comes with multi-level marketing. Additionally, a multi-level marketing entity's approach to organizational structure, recruiting, compensation, and manufacturing warrants detailed attention and familiarity with state and federal law.

LuLaRoe's story, while colorful and seemingly worthy of a hit docu-series, highlights the need to carefully navigate legal issues when operating or becoming involved with a multi-level marketing entity. The potential for legal snags may be hidden in the seams. And it's never worth becoming too big for your (brightly patterned) britches when it comes to the law.

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