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Trade Practices Amendment Bill (No. 1) 2002

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I N F O R M A T I O N A N D R E S E A R C H S E R V I C E S

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Trade Practices Amendment Bill (No. 1) 2002

Susan Dudley
Law and Bills Digest Group
27 November 2002

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Trade Practices Amendment Bill (No. 1) 2002

Date Introduced: 26 September 2002

House: House of Representatives

Portfolio: Treasury

Commencement: Royal Assent

Purpose

The purpose of this Bill is to amend the *Trade Practices Act 1974* (TP Act) to include a plain English re-write of the pyramid selling provision in the Act, to clarify the operation of the defence provision in section 85 of the Act and to amend a minor drafting error.

Background

Pyramid selling

Chain letters, mailing lists, money making clubs and multilevel compensation plans for low-value publications are all examples of pyramid selling schemes. Pyramid selling schemes induce people to join and make payments (financial or non financial) to other scheme participants with the promise that they will receive payments when new participants are recruited into the scheme.

For some pyramid selling schemes the new participants may receive goods or services in exchange for their monetary contribution (or non financial payment).¹ Other schemes will simply involve the transfer of money between participants.² Either situation may be regarded as a pyramid selling scheme if a substantial part of the inducement into the scheme is the prospect of receiving payments or other benefits when new parties are recruited into the scheme.

Whilst the structure and nature of pyramid schemes varies, trade practices lawyer Russell Miller has noted that, in essence,

The pyramid nature of these schemes comes about because each person who introduces others receives a commission for each person introduced by those persons, as well as a commission for introducing those persons.³

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The ACCC has written that

The reality of pyramid selling is that it tends to heavily reward the very top of the pyramid at the expense of everyone else in the scheme. The great majority who join the scheme 'too late' are led to believe that they will also benefit financially.⁴

Sections 61 and 75AZO⁵ of the TP Act set out the legal position regarding pyramid selling schemes. The legislation does not actually prohibit the schemes, rather it is directed to conduct carried out by corporations in relation to these schemes. For example, under the relevant sections, a corporation is not permitted to promote a scheme that is identified as being a pyramid selling scheme.

Section 75AZO sets out the conduct in relation to pyramid selling schemes that is prohibited. A contravention of section 75AZO by a corporation is a criminal offence, punishable by a fine not exceeding \$1.1 million. Section 61 duplicates section 75AZO, however a contravention of section 61 of the TP Act has civil consequences. For example, where a person has suffered loss as a result of the operation of the scheme, they may claim damages (under section 82 of the TP Act) from the corporation involved with the scheme.

In 1997 the Federal Government released a report inquiring into the operation of Division 1 of Part V⁶ of the *Trade Practices Act 1974* and equivalent state and territory legislative provisions (including the provisions dealing with pyramid selling).⁷ Following from this inquiry the Ministerial Council on Consumer Affairs in October 1999 recommended that the pyramid selling provisions in the TP Act⁸ and equivalent legislation in the States and Territories be re-written.⁹ This re-write was considered necessary as the provisions were regarded as being difficult to understand, creating enforcement problems for regulators and compliance problems for scheme promoters.

This Bill contains a plain English re-write of the pyramid selling provision of the TP Act. The Bill is intended to clarify ambiguities that currently surround the interpretation of section 61. It is not designed to make substantial changes to the law relating to pyramid selling.

The Explanatory Memorandum contains a Readers Guide and Examples, which sets out examples of schemes that may and may not be regarded as pyramid selling schemes.

Section 15AB of the *Acts Interpretation Act 1901* sets out the circumstances in which extrinsic material may be used to assist in interpreting provisions of an Act. Section 15AB provides that extrinsic material may be relied upon;

- If the provision under consideration is clear on its face, to confirm the ordinary meaning¹⁰
- If the provision in question is ambiguous or obscure, to assist in the interpretation¹¹, or
- If the ordinary meaning given to the provision leads to a result that is manifestly absurd or unreasonable to assist in the interpretation.¹²

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Section 15AB contains a non exhaustive list of extrinsic material that may be used to aid in the interpretation of legislation. Included in this list is the Explanatory Memorandum relating to a Bill.

Therefore, if the circumstances in section 15AB of the *Acts Interpretation Act 1901* are satisfied, a court may refer to the Explanatory Memorandum to assist them in the interpretation of the provision.

Decision in *Gilmore v Poole-Blunden*

Section 85 of the TP Act sets out the defence provisions that may be invoked for breaches of the consumer protection Parts of the Act.¹³

Section 85 of the TP Act states, in part, the following;

- (1) Subject to subsection (2), in a prosecution for a contravention of a provision of Part VC, it is a defence if the defendant establishes....
 - (a) that the contravention in respect of which the proceeding was instituted was due to reasonable mistake,
 - (b) that the contravention in respect of which the proceeding was instituted was due to reasonable reliance on information supplied by another person.

Paragraph 85(1)(a) has been described as a mistake of fact defence. Mistake of fact has been described in the criminal law in the following way;

As a general rule an honest and reasonable belief in a state of facts which, if they existed, would make the defendant's act innocent, affords an excuse for doing what would otherwise be an offence.¹⁴

Under paragraph 85(1)(b) it is a defence if the relevant information was supplied and the defendant relied on that information. The operation of paragraph 85(1)(b) was recently considered in *Gilmore v Poole Blunden*¹⁵ (Poole Blunden). In Poole Blunden, the respondents promoted the "Concorde" and "Golden Galaxy" schemes. Prior to promoting the schemes, the respondents concluded that the schemes were both legal operations. The respondents came to this conclusion after carrying out their own research and reading a number of independent legal opinions which in essence stated that the schemes would not breach the relevant provisions of the Act, including the pyramid selling provisions.

The case went on appeal from the Magistrates Court to the Full Court of the South Australian Supreme Court. In considering the facts of the case the Court held that the scheme was a pyramid selling scheme within the provisions of the State's fair trading legislation. The Court went on to consider whether the respondents could rely on the equivalent of paragraph 85(1)(b) of the TP Act [paragraph 88(1)(b) *Fair Trading Act 1987* (SA)] to argue that the scheme operated because of reasonable reliance on information supplied by another person.

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The Court held that the legal opinions that were provided to the respondents amounted to “information supplied” for the purposes of the defence¹⁶ and that the contraventions were due to reliance on that information.¹⁷ Accordingly the Court held that the respondents had not breached the pyramid selling provisions of the Act.

The decision in *Poole Blunden* increases the scope of the defences under paragraph 85(1)(b) of the TP Act where there is an alleged breach of a provision within Part VC of the TP Act. It has been suggested that following this decision,

a defence to prosecution may now be available where the defendant can demonstrate that she/he relied upon legal advice provided by another person which is later shown to be incorrect.¹⁸

In response to this, the Standing Committee of Officials of Consumer Affairs met in December 1999 and agreed to a uniform amendment to the TP Act and state and territory fair trading laws to make it clear that the defence in paragraph 85(1)(b) (and state and territory equivalent legislation) be restricted to mistake of fact (not law).¹⁹

Main Provisions

Pyramid selling

Item 1 of the Bill repeals section 61 of the TP Act. **Item 2** of the Bill inserts the proposed new **Division 1AAA – Pyramid selling** into the TP Act, which contains a series of new provisions dealing with pyramid selling.

Clause 65AAA provides an overview of the new Division and states that the aim of the Division is to set out the meaning of pyramid selling and related concepts. **Clause 65AAB** contains relevant definitions for the operation of the new Division. Two noteworthy definitions include the definition of ‘participate’ and ‘payment’.

Clause 65AAC sets out the conduct relating to pyramid selling that is prohibited by the TP Act. The clause states that a corporation must not participate in a pyramid selling scheme. The proposed clause also states that the corporation must not induce or attempt to induce a person to participate in a pyramid selling scheme.

‘Participate’ in a pyramid selling scheme is defined in **clause 65AAB** to include a corporation that ‘establishes’ or ‘promotes’ the scheme or ‘takes part’ in the scheme.

Sub-clause 65AAD(1) defines a ‘pyramid selling scheme’. The definition focuses upon one key elements of the scheme, namely that new participants are entirely or substantially induced into making a payment to other participants in the scheme by the prospect of receiving payments when new participants join the scheme.

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'Payment' is defined in **clause 65AAB** to include the provision of financial and non-financial benefits. This makes it clear that payments can include monetary payments or some other form of benefit such as the receipt of goods.

Clause 65AAE sets out some matters that may be considered when determining whether the payment has been entirely or substantially induced by the prospect of an entitlement to payments when new participants join the scheme. For example the clause states that consideration may be given,

- to whether the payment bears a reasonable relationship to the value of the goods or services that are received in exchange for the payment [**proposed paragraph 65AAE(1)(a)**],
- to the emphasis that is placed on the supply of the goods and services versus the emphasis placed on entitlement to recruitment payments when the scheme is being promoted [**proposed paragraph 65AAE(1)(b)**].

Proposed clause 65AAD clarifies other aspects of the nature of a pyramid selling scheme. For example, sub-clauses (2) and (3) provide the following points of clarification;

- Either the promoter of the scheme or another scheme participant can advertise the inducement [**proposed paragraph 65AAD(2)(a)**]
- The recruitment payments may be made by either the promoter or another scheme participant [**proposed paragraph 65AAD(2)(b)**]
- The participant may be required to perform functions (in addition to making a payment) as part of the scheme [**proposed paragraph 65AAD(3)(b)**]
- Pyramid selling schemes can involve the sale of goods or services or simply involve the transfer of money [**proposed paragraph 65AAD(3)(e)**].

The offence provisions relating to the consumer protection parts of the TP Act are contained within Part VC of the Act. Currently section 75AZO makes it an offence to engage in pyramid selling. **Item 3** repeals and substitutes section 75AZO to make the wording of the provision consistent with the proposed new pyramid selling provisions in the Act.

The penalty for a contravention of the pyramid selling provisions continues to be 10,000 penalty units. It is interesting that the note currently contained in section 75AZO which states that section 4B(3) of the *Crimes Act 1914* does not apply has been removed from the re-drafted provision.²⁰ The conclusion to be drawn from this is that the drafter considers that the form in which the revised provision has been drafted makes it clear that the maximum penalty to be applied to a corporation in contravention of the provision is 10,000 penalty units rather than five times this amount, and hence displaces section 4B(3) of the *Crimes Act 1914*.

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For the abundance of caution however, it is arguable that a note stating that section 4B(3) of the *Crimes Act 1914* does not apply should be included in this provision. It would seem that the factors that encouraged the drafters to include the note in the current section 75AZO (and all other relevant consumer protection provisions in Part VC) are still present and therefore the note continues to be necessary to remove any ambiguities.

Item 4 makes it clear that the new pyramid selling provisions apply only to conduct engaged in after the commencement date

Amendments made in response to the decision in *Gilmore v Poole Blunden*

The Explanatory Memorandum to the Bill states that;

The amendment to section 85 of the TPA made by the Bill restructures the defences provided by the section to exclude information in the nature of legal opinions or advice on the legal consequences of conduct from the type of information to which the defence applies

The Bill in **item 5** proposes to implement this by repealing paragraphs 85(1)(a) and (b) and compressing the contents of the two paragraphs into a new **proposed paragraph 85(1)(a)**. **Proposed paragraph 85(1)(a)** states that it is a defence if the contravention was due to a mistake of fact including a mistake of fact caused by reasonable reliance on information supplied by another person. The effect of this amendment is therefore to remove the possibility of a mistake of law being relied upon under section 85 of the TP Act.

The amendment may not however achieve the objective as set out in the above extract from the Explanatory Memorandum. This is due to the fact that courts have held that in some circumstances reliance on legal advice constitutes a mistake of fact (rather than a mistake of law).

For example in *Palmer v Ostrowski*²¹, the appellant, a commercial fisherman, requested that the Office of Fisheries WA provide him with a copy of the current regulations for lobster fishing. The document that he was provided with was incomplete in that it omitted an amendment which closed an area for rock lobster fishing; this area was described in regulation 34 but Fisheries WA did not supply the appellant with this particular regulation. In this case the majority of the Western Australia Supreme Court held that the appellant was under a mistake of fact, the mistake of fact being that Fisheries WA had provided the appellant with a complete copy of all relevant material pertaining to where commercial operators could fish for lobster. In his minority judgement, Styetler J held that the mistake that the appellant made was a mistake of law, namely that he believed that it was lawful to fish for lobster in the place in which he was fishing when in fact it was unlawful.

Therefore, if the intent of the amendment is to make it clear that acting in accordance with legal opinions and advice is not a defence under section 85 of the TP Act (as opposed to a

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mistake of law not being a defence under that section), the legislation may need to be redrafted to explicitly address this matter.

Power to obtain information, documents and evidence

Section 155 of the TP Act confers wide powers on the Australian Competition and Consumer Commission (ACCC) to investigate possible breaches of the TP Act by requiring that information and documents be provided to the ACCC.

Failure to provide information and documents to the ACCC under section 155 has traditionally incurred a maximum fine of 20 penalty units or 12 months imprisonment. The *Treasury Legislation Amendment (Application of Criminal Code) Act (No. 2) 2001* inadvertently removed the 12 months imprisonment sanction for a contravention of the section. **Item 8** amends section 155 to re-insert this sanction.

Concluding Comments

This Bill contains a number of amendments to the TP Act to clarify the Act's operation in relation to pyramid selling and the use of the defence provision in section 85. It also rectifies a drafting error within the Act. It would appear from the Explanatory Memorandum accompanying the Bill that the Bill proposes to make it clear that acting in reliance on legal advice or opinion is not a defence under section 85 of the Act. Arguably, the Bill does not achieve this result and further consideration may need to be given to the effect of **item 5** of the Bill.

Endnotes

- 1 In *ACCC v Giraffe World Australia Pty Ltd* [1999] ATPR 41-718, Giraffe World sold a mattress (the Mat) that when connected to a source of electricity, emitted negative ions which would allegedly benefit the health of a person who slept on it. The mattress was sold for \$2,000. In association with the sale of the mattress, the buyer of the Mat was introduced to the Giraffe Club (membership fee \$300 and membership application fee \$50) and the Grow Rich System. A member of the Grow Rich System was entitled to be paid commission by Giraffe World for successfully introducing newcomers. It was possible to buy the Mat without joining the Giraffe Club however this was not emphasised and arguably never disclosed. The Federal Court held that this was a pyramid selling scheme in contravention of section 61 TPA.
- 2 In *ACCC v Golden Sphere International Inc* [1988] ATPR 41-638, Golden Sphere promoted a scheme whereby members of the public were required to pay \$150 to join the scheme. The 'target' was provided with a 'Certificate of Authenticity' which contained the names of seven people, numbered one to seven. The bank account details of the first named person in the list

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appeared opposite their name. The target paid \$50 to the person selling the scheme to them, \$50 to Golden Sphere and \$50 to the person named at the top of the 'Certificate of Authenticity'. Following these payments, Golden Sphere forwarded to the new member three numbered certificates and each certificate contained the target's name in the seventh position. The target's name would eventually progress to the top of the list as new people were recruited into the scheme. Golden Sphere represented to the target that he or she would eventually receive in excess of \$100,000 by participating in the scheme.

- 3 Russell Miller, *Miller's Annotated Trade Practices Act 1974*, Twenty third edition, Lawbook Company, 2002, p. 490.
- 4 Chris Field, 'Consumer Dealings', *Australian Business Law Review*, vol. 29, no. 4, Aug 2001, p. 348 referring to *Advertising and Selling*, Australian Competition and Consumer Commission, AGPS, Canberra, 1997.
- 5 The *Treasury Legislation Amendment (Application of Criminal Code) Act (No 1) 2001* (TLAA) amended the TP Act to make the consumer protection provisions in the TP Act, Criminal Code compliant. Prior to this amendment, both civil and criminal consequences flowed from a breach of the consumer protection provisions contained in Divisions 1 and 1A of the TP Act. In order to make these provisions Criminal Code compliant, yet maintain the civil regime, the TLAA created a new part, Part VC in the TP Act. Civil consequences continue to flow from a breach of Divisions 1 and 1A of the TP Act, however the criminal elements of the Division were transferred to Part VC. Part VC substantially reproduces Divisions 1 and 1A of Part V but contains the amendments necessary to ensure that the divisions are Criminal Code compliant. Section 75AZO is the criminal equivalent of section 61 of the TP Act.
- 6 Part V deals with Consumer Protection as does Part VC.
- 7 Audit of Consumer Protection Laws, Final Report Identifying Inconsistencies, Gaps and Overlaps in Consumer Protection Legislation, February 1997, http://www.consumersonline.gov.au/resources/audit_report1.asp.
- 8 Explanatory Memorandum, Trade Practices Amendment Bill (No 1) 2002, p. 1.
- 9 *Fair Trading Act 1999 (VIC)* section 22, *Fair Trading Act 1987 (SA)* section 70, *Fair Trading Act 1987 (NSW)* section 56, *Fair Trading Act 1922 (ACT)* section 27, *Fair Trading Act 1989 (QLD)* section 55D, *Fair Trading Act 1987 (WA)* section 24, *Fair Trading Act 1990 (TAS)* section 26B, *Consumer Affairs and Fair Trading Act (TAS)* section 56.
- 10 Section 15AB(1)(a).
- 11 Section 15AB(1)(b)(i).
- 12 Section 15AB(1)(b)(ii).
- 13 Parts V and VC.
- 14 Australian Trade Practices Reporter, CCH Australia Limited, p. 12,442.
- 15 [1999] SASC 186.
- 16 *ibid* p. 24.

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- 17 *ibid* p. 25.
- 18 Stewart Yeung, 'Defences under the Trade Practices Act – Gilmore v Poole-Blunden', *Australian and New Zealand Trade Practices Law Bulletin*, vol. 15, no. 3, 1999.
- 19 Explanatory Memorandum, Trade Practices Amendment Bill (No 1) 2002, p. 11.
- 20 Section 4B(3) *Crimes Act 1914* states that, where a body corporate is convicted of an offence against a law of the Commonwealth, the court may, if the contrary intention does not appear and the court thinks fit, impose a pecuniary penalty not exceeding an amount equal to 5 times the amount of the maximum pecuniary penalty that could be imposed by the court on a natural person convicted of the same offence. Therefore unless a contrary intention appears the maximum penalty that may be imposed on a corporation that breaches the provision is five times the amount expressed in that provision. The note currently contained in section 75AZO makes it clear that the maximum penalty that may be imposed on a corporation that contravenes that section is the amount expressed in that provision, ie 10,000 penalty units rather than five times that amount.
- 21 [2002] WASCA 3.

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