

立法會
Legislative Council

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Bills Committee on Pyramid Schemes Prohibition Bill
Background Brief

Purpose

This paper sets out the background of the Pyramid Schemes Prohibition Bill and the views expressed by Members on the Bill and related issues.

Background

Pyramid schemes

2. According to the Administration, during the period from 2007 to November 2009, the Police received complaint cases relating to suspected pyramid schemes, and arrested 21 persons in respect of four cases involving 157 affected persons and \$8.78 million. Pyramid schemes are different from ordinary business model in that profits under the former are mainly derived from recruiting participants who pay to join the schemes. Pyramid schemes serve no economic purpose and are unsustainable as they rely solely on the recruitment of new members.¹ Participants may suffer from financial loss when such recruitment runs out².

3. At present, pyramid selling is prohibited under the Pyramid Selling Prohibition Ordinance (Cap. 355) (the Ordinance). One of the defining characteristics of pyramid selling schemes is that the reward a participant may receive through the introduction of another participant to join the scheme is not based on the fair market value of goods or services that are actually sold. Under the Ordinance, any person who knowingly promotes a pyramid selling

¹ Even if the sale of goods or services is involved, such selling and buying are only used as a smoke-screen.

² Under a scheme design where participant may introduce five new participants, there could be 2 441 406 participants if the scheme expands to ten full tiers.

scheme commits an offence and is liable on conviction upon indictment to a fine of \$100,000 and to imprisonment for three years. It is also a criminal offence to conspire to defraud others to join pyramid schemes.

4. In 2003 and 2004, when ruling on two cases involving alleged pyramid selling schemes³ (CACC 96 of 2003 and CACC 55 of 2004), the Court of Appeal acquitted the defendants in both cases of charges of breaches of the Ordinance. The Court held that the Ordinance implied that the operation of a pyramid selling scheme must involve the selling of goods or services by or through participants. In other words, schemes not involving the sale of goods and/or services, and schemes under which goods and/or services are sold in other ways (for example, sold by the company directly to new participants) would fall outside the scope of the Ordinance.

Legislation on pyramid selling in other jurisdictions⁴

5. In the European Union (EU), the practice of pyramid schemes is on the blacklist of practices banned EU-wide under the Unfair Commercial Practices Directive (Directive)⁵. Ireland, in particular, has enacted the Consumer Protection Act in 2007 to formally establish the National Consumer Agency as a statutory agency to defend consumer interests in Ireland. The Act transposes into Irish law the provisions of the Directive and introduces new provisions in relation to pyramid schemes, making it an offence to establish, operate, promote or participate in a pyramid promotional scheme.

6. In Australia, the government has recently revamped its consumer protection legislation and the Australian Consumer Law (ACL) was enacted in 2010 as a result.⁶ ACL is a single, national law concerning consumer protection and fair trading administered by the Australian Competition and Consumer Commission and each State and Territory's consumer law agency. The new law re-enacts, with improvements, the then existing legislative provisions against pyramid schemes and provides that participation in such schemes is a criminal offence under ACL.

7. In the Mainland and Singapore, a total ban on marketing schemes adopting a multi-level structure is imposed. Only schemes meeting specified

³ The sole purpose of the schemes in question was to make money from the recruitment of other participants with no element of trading in goods at all.

⁴ Source: Public consultation paper on proposed legislative amendments to eradicate pyramid schemes.

⁵ Directive No. 2005/29/EC of the European Parliament and of the Council of 11 May 2005.

⁶ The Australian Consumer Law was introduced by two Acts, namely the *Trade Practices Amendment (Australian Consumer Law) Act (No.1) 2010* and the *Trade Practices Amendment (Australian Consumer Law) Act (No.2) 2010*.

requirements and registered with competent authorities are allowed.⁷

8. The regulatory regime in Taiwan prohibits "distorted multi-level selling activities" (meaning arrangements where participants receive economic benefits mainly from introducing others to participate, rather than from the marketing or sale of goods or services or from work rendered at reasonable market prices). At the same time, a series of record-filing requirements concerning the operations of multi-level marketing schemes are laid down.⁸

9. In Macao, the government amended the Proibição da venda «em pirâmide» (《禁止層壓式傳銷》法例) in 2008 to eliminate fraudulent pyramid selling activities. Under the new Ordinance, pyramid selling refers to activities of sale of goods or services organized in the form of chains or similar forms, and participants of such schemes receive rewards which depend mainly on the recruitment of new participants. The Ordinance also prohibits anyone initiates, organizes or solicits others to join pyramid selling scheme.

Previous discussions by the Legislative Council

Council question and motion

10. Hon WONG Kwok-hing raised an oral question on pyramid selling activities at the Council meeting on 18 November 2009. He noted that the Macao government adopted a tougher stance than Hong Kong in curbing fraudulent cases related to pyramid activities and enquired about the timetable for amending the Ordinance.

11. Hon Starry LEE moved a motion at the Council meeting on 6 January 2010 on "Establishing a comprehensive consumer protection regime", urging the Government to, among others, expeditiously amend the Ordinance with a view to combating and eliminating all types of fraudulent multi-level marketing practices. The motion was passed as amended by Hon WONG Kwok-hing and Hon Fred LI.

Panel on Economic Development

12. When the Administration briefed the Panel on Economic Development (EDEV Panel) on 24 May 2010 about the policy directions to strengthen

⁷ Mainland: Regulations on Prohibition of Multi-level Marketing Activities and Regulations on Administration of Direct Selling Activities; Singapore: Multi-level Marketing and Pyramid Selling (Prohibition) Act and Multi-Level Marketing and Pyramid Selling (Excluded Schemes and Arrangements) Order 2000.

⁸ Article 23 of the Fair Trade Act and the Supervisory Regulations Governing Multi-Level Marketing Activities.

consumer protection legislation, Panel members expressed dissatisfaction about the prevalence of pyramid schemes in Hong Kong which had been rooted in Hong Kong for many years. In particular, secondary school leavers were vulnerable to such malpractices that might cost them and their families indebted to huge amounts of loans.

13. The Administration conducted a review of the current regulatory approach, and briefed the EDEV Panel on the review outcome at the meeting on 25 October 2010. Members in general welcomed the Administration's proposed amendments to the Ordinance since more and more youngsters and housewives fell prey to pyramid schemes. Some members urged the Administration to differentiate clearly pyramid schemes from other concession schemes under which existing scheme members could enjoy a discount by introducing new members. They were keen to ensure that normal business practices would not be affected.

14. On 7 December 2010, the Government issued a public consultation paper on a package of proposed legislative amendments aimed at eradicating pyramid schemes. The consultation period ended on 31 January 2011.

The Bill

15. The Pyramid Schemes Prohibition Bill was gazetted on 20 May 2011 and introduced into the Legislative Council on 1 June 2011. The Bill seeks to repeal the Ordinance and introduce a new regime for the prohibition of all pyramid schemes irrespective whether they involve the sale of goods and/or services. The Bill contains 9 clauses and the major provisions are –

- (a) clause 1 sets out the short title and provides for commencement;
- (b) clause 3 defines the meaning of "pyramid scheme", with clause 4 setting out the matters which the court must consider when determining if a scheme involving the sale of goods and services (or both) is a pyramid scheme;
- (c) clause 5 provides for the offence of knowingly promoting a pyramid scheme and the offence of participating in and inducing others to join a pyramid scheme with the knowledge that the benefit receivable is entirely or substantially derived from the introduction of new participants into the scheme. Either offence attracts a maximum penalty of a fine of \$1,000,000 and imprisonment for seven years upon conviction on indictment;
- (d) clause 6 provides that if a body corporate or a member of an unincorporated body commits an offence under the Bill, a relevant

person of the body is also liable for the offence if it is proved that the offence was committed with the consent or connivance or is attributable to the neglect of that person;

- (e) clause 7 empowers the court to order a person who is convicted of an offence under the Bill to pay compensation to any person who has suffered financial loss arising from the offence; and
- (f) clause 9 repeals the Ordinance.

Views on the Bill

16. At the meeting of the EDEV Panel on 28 March 2011, the Administration briefed members on the outcome of the public consultation on the key elements of the Bill. Panel members were generally in support of the legislative proposals. Some members urged the Administration to step up publicity and public education to help the public to differentiate legitimate marketing schemes from illicit pyramid schemes and unfair trade practices. The Administration advised that it would include in the legislation factors to be considered by the courts in ascertaining the nature of schemes involving the marketing of goods and/or services (see clause 4 of the Bill). Other members enquired whether the Administration would consider adding a provision in the Bill stipulating disgorgement of improperly gained money as part of the penalties, and whether existing legislation was insufficient to deal with deception cases.

Latest development

17. At the House Committee meeting on 3 June 2011, a Bills Committee was formed to scrutinize the Bill.

Relevant papers

18. The relevant papers are available at the following links:-

The High Court of the Hong Kong Special Administrative Region Court of Appeal Criminal Appeal No. 96 of 2003 (On Appeal from DCCC No. 898 of 2001)

http://legalref.judiciary.gov.hk/lrs/common/search/search_result_detail_frame.jsp?DIS=7593&QS=%2B&TP=JU

The High Court of the Hong Kong Special Administrative Region Court of Appeal Criminal Appeal No. 55 of 2004 (On Appeal from DCCC no. 757 of 2002)

http://legalref.judiciary.gov.hk/lrs/common/search/search_result_detail_frame.jsp?DIS=39018&QS=%2B&TP=JU

LegCo question on "Pyramid selling activities" raised by Hon WONG Kwok-hing on 18 November 2009

<http://www.info.gov.hk/gia/general/200911/18/P200911180130.htm>

LegCo motion on "Establishing a comprehensive consumer protection regime" moved by Hon Starry LEE at Council meeting on 6 January 2010 and Progress Report

http://www.legco.gov.hk/yr09-10/english/legco_rpt/legco_motion01071-e.pdf

<http://www.legco.gov.hk/yr09-10/english/counmtg/motion/cm0106-m2-prpt-e.pdf>

Minutes of the Panel meeting on 24 May 2010

<http://www.legco.gov.hk/yr09-10/english/panels/edev/minutes/edev20100524.pdf>

Administration's paper on review of Pyramid Selling Prohibition Ordinance (Cap. 355) for the Panel meeting on 25 October 2010

<http://www.legco.gov.hk/yr10-11/english/panels/edev/papers/edev1025cb1-95-3-e.pdf>

Minutes of the Panel meeting on 25 October 2010

<http://www.legco.gov.hk/yr10-11/english/panels/edev/minutes/edev20101025.pdf>

Administration's public consultation paper on proposed legislative amendments to eradicate pyramid schemes

<http://www.legco.gov.hk/yr10-11/english/panels/edev/papers/edev1025cb1-707-1-e.pdf>

Minutes of the Panel meeting on 28 March 2011

<http://www.legco.gov.hk/yr10-11/english/panels/edev/minutes/edev20110328.pdf>

LegCo Brief on Pyramid Schemes Prohibition Bill

http://www.legco.gov.hk/yr10-11/english/bills/brief/b32_brf.pdf

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