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October 10, 2014

Dear Keshav,

**Subject: Regulatory Authority for direct selling.**

Common Cause has been exercised over the unchecked fraudulent operations of the so-called direct selling and network/multi-level marketing companies, which entrap millions of unwary members of the public by holding out prospects of quick enrichment. Once enrolled as distributors/business associates, they are incentivized to prey on unsuspecting relatives and social acquaintances to extend the ‘downline’, which sustains the cash flow to the top of the pyramid.

Evidently, the underlying objective of the Prize Chits and Money Circulation Schemes (Banning) Act, 1978, which was enacted to curb such exploitation, has not been achieved. This failure is largely the result of the indifference or incapacity of the agencies charged with the responsibility of implementing the Act and overseeing its enforcement.

It would be pertinent to refer here to the verdict in writ petition *Geminitech Marketing Private Ltd, Amway India Enterprises &Others Vs State of A.P. and Others* in the Andhra Pradesh High Court, wherein the petitioners had sought a declaration that the provisions of the Prize Chits and Money Circulation Schemes (Banning) Act, 1978 had no application to the business carried on by the petitioners and their distributors. They sought a consequential direction to the respondents not to apply or enforce the provisions of the Act in relation to the petitioners’ businesses. The High Court comprehensively dismissed the writ petition vide its order dated 30.7.2010, holding that the schemes run by the petitioners squarely attracted the definition of “money circulation scheme.”

Excerpts from the judgment are reproduced below for ready reference:

*“What is within the mischief of the Act is not “any scheme, by whatever name called, for the making of quick or easy money” simpliciter, but a scheme for the making of quick or easy money, “on any event or contingency relative or applicable to the enrolment of members into the scheme”, (whether or not such money or thing is derived from the entrance money of the members of such scheme or their periodical subscriptions). Two conditions must be satisfied before a person can be held guilty of an offence under Section 4 read with Sections 3 and 2(c) of the Act. In the first place, it must be proved that he is promoting or conducting a scheme for the making of quick or easy money and secondly, the chance or opportunity of making quick or easy money must be shown to depend upon an event or contingency relative or applicable to the enrolment of members into that scheme. It is necessary that the activity, charged as falling within the mischief of the Act, must be shown to be a part of a scheme for making quick or easy money, dependent upon the happening or non-happening of any event or contingency relative or applicable to the enrolment of members into that scheme. The systematic programme of action has to be a consensual arrangement between two or more persons under which the subscriber agrees to advance or lend money on the promise of being paid more money on the happening of any event or contingency relative or applicable to the enrolment of members into the programme. Reciprocally, the person who promotes or conducts the programme promises, on receipt of an advance or loan, to pay more money on the happening of such event or contingency. (State of W.B. v. Swapan Kumar Guha).*

*The event or contingency on the happening of which the amount would become payable must be relative or applicable to the enrolment of members into the Scheme. It is immaterial by whom such members are enrolled. It may be by members, by promoters or their agents or by gullible sections of the society suo motu (by themselves). The sole consideration is that payment of money must be dependent on an event or contingency relative or applicable to the enrolment of more persons into the Scheme, nothing more, though nothing less. (Kuriachan Chacko1).”*

The practice of camouflaging money circulation schemes as direct-selling/mullti level marketing schemes for distribution of goods and services is now firmly entrenched. The promoters of such schemes generally take shelter behind a specious distinction with pyramid-structure schemes and try to secure declarations from government authorities as well as the courts that the penal provisions of the said Act do not apply to them.

There have been persistent demands from the industry circles to get this distinction recognized statutorily and these demands have become more vociferous and strident following the arrest in May 2014 of Bill Pinckney, CEO & MD of Amway India, by the Telengana police for violations of the Banning Act. In our view, it will be disastrous to accord legitimacy to operations having the characteristics of money circulation schemes on account of the different appellations used by them and grant them immunity from the provisions of the Banning Act.

Common Cause had written to the Prime Minister in July 2012, underlining the danger inherent in giving credence to labels such as multi-level/network marketing company and assuming that all so-called direct-selling companies or companies dealing with the distribution of goods are exempt from the penal provisions of the law against money circulation schemes (Annexure 1).

The matter was also taken up with the Ministry of Consumer Affairs at the level of the Minister and followed up with two of your predecessors (Annexure 2). Letters were addressed to the authorities in the Ministries of Finance, Company Affairs and the Reserve Bank of India as well (Annexure 3). It goes without saying that there was no response from any quarter.

Nothing is known of the outcome of the deliberations of the working groups appointed by the Ministry of Consumer Affairs and the Department of Financial Services, to consider the issues of bridging the regulatory gap and protection of the gullible public. We have been informed that there was an initiative on the part of the Ministry of Company Affairs, to draft Model Rules to be adopted by the state governments to streamline the implementation of the Banning Act and ensure a certain measure of uniformity. It is not known whether the draft rules (Annexure IV) found favour with any of the state governments, but they do provide a set of legally sound and practical criteria for uncovering the true nature of any operation that styles itself as a muti-level/direct selling company.

Against the backdrop of the Saradha and similar chit fund scams, the Finance Minister in his Budget speech referred to the need to bridge the regulatory gap under the Banning Act of 1978 and bring about effective regulation of companies and entities which have duped a large number of poor and vulnerable people. It was indicted that stronger regulatory authorities would be put in place for early detection and deterrence of Ponzi schemes. While this is a laudable objective, it needs to be ensured by the Ministry of Consumer Affairs that we do not end up diluting the rigour of the Banning Act in the name of regulation and protection of legitimate direct selling activity. The Indian Direct Selling Association is an extremely influential and resourceful interest group with an impressive array of legal luminaries on its pay roll.

I have thought it fit to inflict this long letter on you in order that we may have a more pointed discussion when we meet this Wednesday.

With warm regards,

 Yours sincerely,

Kamal Kant Jaswal

Director

Shri Keshav Desiraju,

Secretary,

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