

Consumer Affairs Victoria

Stopping Rogue Traders

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“ Preface ”

The experience of consumer agencies is that the great majority of businesses comply with the laws that protect consumers, or would do so if they were aware of their obligations. There is a small percentage of businesses, however, that deliberately breach the law.

These rogue traders intentionally engage in ongoing activities that exploit consumers, especially taking advantage of the vulnerable and disadvantaged. They can be difficult to detect and stop, often adopting schemes to hide their identity and location. They do not respond to the light-handed approaches used to encourage compliance among honest businesses, such as informing traders of their rights and responsibilities. Hence, consumer agencies need to target rogue traders specifically to detect and deter their activities, deter perpetrators, and to protect consumers and legitimate businesses.

This research paper is one in a series designed to stimulate debate on consumer policy issues. It is linked to the discussion in an earlier paper entitled *What do we Mean by 'Vulnerable' and 'Disadvantaged' Consumers?* as such consumers can be targets for rogues, and rogues can inflict severe hardship on those least able to protect their own interests.

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“ Stopping rogue traders ”

The motivation of traders that do not comply with consumer regulation ranges from those that are unaware of the law and inadvertently breach their obligations, through others that periodically behave inappropriately due to circumstances such as financial pressure, to those that deliberately engage in ongoing activities to exploit consumers. This latter group are known as ‘rogue traders’. In practice, it can be difficult to determine which traders fall into the category of ‘rogues’, because the seriousness of the activity that should give rise to such a classification is a matter of judgement.

Nonetheless, it is clear that the detriment caused by rogue traders is significant. While relatively small in number, they can:

- have large financial and emotional impacts on consumers
- disadvantage ethical competitors
- owe large amounts of money to suppliers and government agencies (which have little chance of recovering that money), and
- divert the resources of regulators to pursuing their detection and prosecution.

Given rogue traders’ tendency to target consumers when they are vulnerable, the damage they cause individuals is often severe. All consumer agencies are consequently concerned about rogue traders and many are implementing strategies to protect consumers. A Commonwealth, state and territory working group under the Ministerial Council on Consumer Affairs produced *The Little Black Book of Scams* to inform consumers about the tactics used by some rogue traders and how to avoid them (MCCA working group 2004). In the United Kingdom (UK) the 2005 strategy *A Fair Deal for All* foreshadowed new initiatives to improve the effectiveness of enforcement against rogue traders (DTI 2005, pp. 20–21) and the European Union is considering how to minimise the problems caused by rogue traders that operate across borders. (EU 2003)

The paper discusses the problem of rogue traders, why they are difficult to control, the role of general consumer regulation, licensing and consumer awareness in stopping rogues, and other policies that could target rogue traders. It identifies key issues for deciding how best to regulate rogues.

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“What are rogue traders?”

1

Generally, rogue traders seek to unfairly exploit consumers for their own benefit. Rogues knowingly and consistently breach the law, and usually have in place strategies to avoid being detected or prosecuted. They try to pass themselves off as legitimate traders and often prey on consumers when they are at their most vulnerable.

Rogue traders can be Australian- or overseas-based. Some of their activities involve scams¹ (Box 1).

Box 1: Scams

Investment and financial scams

Rogue traders promoting investment and financial scams claim to be financial advisers, stockbrokers or portfolio managers. They generally offer share, mortgage or real estate 'investments' and promise their victims high returns on their money. Such scammers may also encourage their victims to trade in foreign currency. Many of these scam promoters are based overseas.

In a typical real estate scam the promoter inflates the prices of investment properties to well above fair market rates and attempts to sell them, typically to buyers who do not live locally. When a victim later seeks to sell such a property, he or she discovers that enormous losses on the original purchase price will be suffered. Scam promoters bank on their victims not knowing the value of real estate in the area and often promote their offers as 'once-in-a-lifetime' opportunities and use high pressure tactics to secure sales.

Employment schemes: envelope stuffing

Advertisements for self-employment opportunities in local papers offer work stuffing envelopes. Consumers are required to pay some money up front for work that never eventuates. Once they have paid their money, consumers often discover that there are no envelopes to stuff. All they generally receive is instructions on how to lure others into the scheme.

One scheme asks consumers to send between \$32 and \$45 to cover a registration fee, postage and handling. Those who do, receive photocopied sheets advising how to place advertisements similar to the one to which they responded and 'How to start a mail order scheme from home stuffing envelopes'.

Medical, health and weight loss claims

Unsolicited mail order scams, spam and internet sites offer weight loss products and miracle cures for illnesses such as cancer and HIV/AIDS. Scam promoters might claim, for example, that a 'slimming capsule' will quickly and effortlessly reduce the recipients weight by a large amount and the scam correspondence will assert 'Lose 30 kilos in 30 days!', or 'Lose weight while you sleep!' Testimonials from people who purport to have used the product may claim they lost 40 kilograms in 40 days and were able to keep this weight off without exercising or altering their diets. Consumers who purchase such weight loss products find they have spent significant amounts of money on worthless products.

Source: CAV 2005a, *List of Scams*

¹ In some scams, such as advanced fee fraud (where promoters ask their victims to assist in transferring money out of another country) the perpetrators do not attempt to present themselves as legitimate businesses. These scams, while still a significant problem, are outside the scope of this paper. The perpetrators of other scams, however, like those described in Box 1, often fall within the definition of 'rogue trader'.

It is useful to distinguish rogue traders by their deliberate, ongoing intent to exploit consumers and avoid detection. Therefore, the key feature that distinguishes rogues from others that breach consumer regulation is their motivation, that is, conscious intentions to:

- deceive consumers or exploit their lack of knowledge or understanding to obtain payment for goods or services that consumers would not buy if they made informed objective decisions
- undertake this deception on an ongoing basis, and
- avoid detection and/or the consequences of getting caught.

As it is difficult to observe people's intentions or motivations, it is useful to look for behaviour that would indicate that someone is a rogue trader. Such indicators include:

- a history of breaching consumer regulation
- undertaking activities that individually or in combination cause considerable consumer detriment
- persistently failing to respond to concerns raised by customers
- failing or refusing to address issues raised by the regulator
- adopting business strategies to avoid detection or responsibility for illegal or unethical actions
- using strategies to conceal the identity of the person or people conducting the activities of the entity
- operating outside the ethical norms of the industry in which activities are being conducted, and
- using predatory behaviour to target vulnerable or disadvantaged consumers.

Meeting any one of the indicators listed above may not prove a trader is a rogue, nor is it necessary to meet all the indicators, but any operator that conducts its activities consistent with several of the listed indicators is likely to be a rogue trader.

Of most concern to Consumer Affairs Victoria are 'major rogues': those rogue traders that cause large amounts of damage; are highly predatory, dishonest or exploitative; have a history of rogue behaviour; and do not respond to light-handed approaches to resolving consumer issues. The discussion in this paper covers all rogue traders, not just major rogues.

“What are the effects of rogue traders?”

2

Rogue traders impose costs on consumers, the industries in which they operate, suppliers and taxpayers.

- Consumers lose money because of overcharging. They pay for goods or services that are not provided or are substandard, and/or to fix faulty goods or workmanship.
- Consumers and their families suffer distress and emotional pressure.
- Legitimate businesses are disadvantaged because rogue traders cause consumers to distrust their industries, which reduces demand and the opportunity for legitimate businesses to sell their services. Legitimate businesses also lose sales due to unfair competition from rogues.
- Rogue traders usually leave a trail of bad debts, imposing costs on other businesses and affecting suppliers and other traders (such as hotels and restaurants).
- They evade Commonwealth and state taxes, placing an additional burden on other taxpayers.
- Taxpayers must meet the cost of government pursuing and prosecuting rogue traders. As many rogue businesses have few assets, these costs are often not recouped, even if offenders are convicted.

It is virtually impossible to get an accurate statistical picture of the size of the rogue trader problem. It is difficult, without some investigation, to know whether a trader that has breached consumer regulation is a rogue. Consumers making complaints do not necessarily know they are dealing with rogues, so it is difficult to separate data relating to rogue traders from other complaints data held by Consumer Affairs Victoria. Many cases are also unreported. The report of the Victorian Drugs and Crime Prevention Committee recognised the problem of under-reporting.

Many people do not report fraud, as they feel it is somehow their own fault and they do not want others to see them as 'foolish'. (DCPC 2004, p. vi)

In a study of rogue itinerant traders, offering bogus property maintenance services door-to-door, the United Kingdom Office of Fair Trading suggested four main reasons for victims under-reporting:

- embarrassment
- fear induced by pressure from the offender not to report the incident, or concern (particularly among the elderly) that their family would conclude they cannot look after themselves
- victims being unaware they have been duped, and
- feeling that reporting is futile as nothing will happen. (OFT 2004a, p. 92)

While recognising data collection difficulties, the United Kingdom estimated the size of their rogue itinerant trader problem using police data from several regions. Their estimates were indicative only, but the data suggested that the United Kingdom had about 250 cases per million people each year. On average each case cost consumers around £2,500. (OFT 2004b, pp. 2-4)

The UK Office of Fair Trading estimates that consumers lose about £1 billion to scams each year (OECD 2005, p. 9). In the United States consumers reported to the Fair Trading Commission that they lost US\$545 million to fraud (OECD 2005, p. 17). Because of under-reporting, actual losses would be much higher.

Despite the lack of data on rogue traders in Victoria, there is considerable evidence that there is a significant problem.

- Consumer Affairs Victoria is currently investigating or taking proceedings in relation to investment and property based scams that together are estimated to have cost Victorians about \$9 million dollars.

- Australians have lost at least \$400 million in telephone investment fraud (ASIC 2005a). The Australian Securities and Investments Commission has on its database the names of about 200 overseas businesses that do not hold Australian financial services licences and have made unsolicited phone calls to Australians.
- New scams are emerging all the time, and scammers are constantly reinventing old scams. There is no evidence that this problem is decreasing and greater use of the internet provides a new mechanism that gives scammers widespread access to potential victims. (MCCA working group 2004, p. 5)
- Consumer Affairs Victoria identified concerns about:

The ease with which rogue traders can escape CAV action by utilising the bankruptcy laws and later re-establishing themselves in new phoenix organisations. A number of traders named for poor service in last year's annual report have taken this route this year, thus avoiding their obligations to compensate consumers for their poor trading. Amendment to the Commonwealth corporations law is necessary to deal with this problem. (CAV 2004a, p.7)
- A series of reports on phoenix companies have all concluded that, while difficult to measure, phoenix activity is a significant problem. These reports include the Victorian Law Reform Committee (Law Reform Committee 1994, pp. 9–10), the Cole Royal Commission (Cole 2003, pp. 127 and 161), and Rankin and Popkin (2004, p. 40).

Almost all regarded the problem [illicit phoenix company activity] as a serious one requiring the attention of the legislature and were supportive of strengthening measures against phoenix companies. For example, the Tax Office questioned whether the legislation governing voidable preferences, insolvent trading and fraud was sufficient to counter phoenix type activity. (Joint Committee 2004, p. 139)
- A confidential report on rogue itinerant traders in Australia estimated that traders engaged in fraud can make about \$10,000 a week. Itinerant traders are known to operate in Victoria.

Rogues often target vulnerable or disadvantaged consumers and the social and personal consequences of the losses caused by a rogue can be very high. The potential for rogue traders to harm consumers is illustrated in the examples in Box 2.

Box 2: The impact of rogue traders on consumers

Itinerant trader offering roof repairs

An elderly homeowner was approached by two men offering to repair tiles on the roof of her home. They had completed work on her neighbour's house so she assumed they were competent, but she later discovered their work was sub-standard and incomplete. Worse, being arthritic, she asked one of them to fill in the cheque for her when the work was completed. They altered the cheque, originally made out for \$100, to read '\$2,100'. The villains duped her of most of her savings. (Commonwealth of Australia 2005, p. 2)

'Interest-free' loan

Two hundred and twenty Queenslanders invested \$2.4 million in 'The Carsworthy Scheme'. People were told if they purchased a car through a car buyers' club, and borrowed a little more from their financier and invested it offshore, the high returns would repay their car loans. In fact, when the offshore investments failed to deliver promised returns, people were left to find their own repayments, often for very high loans that they would probably not have entered into otherwise.

Another case involved Wide-I Design Corporation (a company registered in Vanuatu), ETP Ventures Pty Ltd and Cyrus Strategies Pty Ltd. Car and home loans were offered on a similar basis to that outlined above. Investigations by the Australian Securities and Investment Commission found that, combined, these two schemes took at least \$4.6 million from around 400 investors. (ASIC 2005b, p. 1)

Skybiz

Skybiz purported to sell online tutorials on Web-based products. It was actually a massive illegal pyramid scheme, which was estimated to have conned consumers around the world out of approximately \$175 million (FTC 2001, p. 1). Around 156,000 Australians were affected. (ACCC 2005a, p. 1)

Central Casting, Global Capital Casting and MM Promotions

Kevin John Sims operated modelling and entertainment agencies. Sims advertised in the employment sections of newspapers throughout Victoria and promised work in modelling or the entertainment industry. He demanded up front fees and failed to honour promises and assurances given to prospective actors and models.

Consumer Affairs Victoria sought an injunction prohibiting Sims from engaging in misleading and deceptive conduct and running businesses as a modelling agent, casting agent or employment agent. In addition to the injunction to cease trading, the Court ordered Sims to refund a total of \$172,293 to 23 people (\$7,491 each) who had not received the services for which they had paid. (CAV 2004a, p. 68)

(continued)

Box 2: (continued)

Gino Memorials

Gino Carmignani, a stonemason, approached families at grave sites, offering to build lasting memorials for recently deceased family members. He offered discounts for cash and immediately requested deposits of thousands of dollars. He would later go to consumers' homes to request further payments.

He accepted over \$63,000 for memorials that were never built, taking \$17,000 in one case, and between \$2,500 and \$8,000 each from other victims. The Melbourne Magistrates' Court ordered him to repay the money. (Bachelor 2005)

The potential for rogue traders to affect legitimate businesses and undermine consumer confidence is well recognised. For example,

The Federation of Master Builders [in the United Kingdom] estimates that their members lose up to £1.5 billion to cowboy builders each year, a fair proportion of whom will be bogus doorstep traders. (OFT 2004a, p. 91)

To the extent that 'cowboys' are removed, the overall reputation of the industry is enhanced, i.e. regulation removes badly behaving firms from the industry that contaminate the reputation of all firms in the industry. (Llewellyn 1999, p. 45)

Effective control of this illegal activity is important for regulators and businesses alike ... It is important for businesses because illegal operators can undercut legitimate businesses, often by quite considerable sums. (Hampton 2005, p. 38)

The impact on government agencies is also significant. Rogues divert resources to detecting and pursuing a relatively small number of individuals. This potentially constrains regulators' other activities, such as informing and educating consumers or assisting ethical businesses to understand their obligations.

Consumer affairs agencies in Australia have recognised that good information is not available on the activities of rogue traders in Australia. A new Australasian Consumer Fraud Taskforce was established in March 2005. One of its roles is generating greater interest in research on consumer fraud and scams.

“ *Why are rogue traders difficult to stop?* ”

3

Rogue traders can be difficult to detect, identify and prosecute because they choose industries and adopt strategies that make detection more difficult or reduce regulators' ability to impose fines or recover losses if they are caught.

While rogues can emerge in any industry, some industries are more vulnerable to rogue activities. Rogue traders are most often found selling information technology services, home maintenance, motor vehicles, or wealth creation schemes, and often operate door-to-door. They frequently focus on industries or regions where there is a high proportion of vulnerable consumers, and are most common in industries where:

- it is possible to obtain large financial gains quickly
- consumers fail to protect themselves, because it is difficult to judge the quality of the product or service or they succumb to offers that are 'too good to be true', and
- authorities have difficulty catching and prosecuting rogues, because the industry lends itself to employing strategies to avoid detection.

Rogues may also be found in industries where the products or services being sold are linked to criminal activities, such as selling stolen goods through second hand goods stores or motorcar yards.

3.1 Ability to generate quick returns

Rogues usually seek to obtain large financial gains quickly. This allows them to maximise their takings and move on, reducing the risk of being caught. This could include targeting many people simultaneously for relatively small amounts of money or targeting small numbers of people for larger amounts.

Rogue traders often use the internet to access large numbers of people quickly. They request up front fees for registration or administration, postage and handling. Fees may be less than \$100; such scams rely on many people paying. The Rogue pockets the money and does not send the goods or services expected.

The home repairs, investment and real estate industries often involve large transactions, and are therefore industries in which rogues can extract thousands of dollars from victims and never deliver the products promised prior to sale (Box 3).

Box 3: Itinerant traders Itinerant trader offering roof repairs

Some itinerant traders are conmen who travel from town to town, touting for work. They come in from overseas each Spring and operate through to March, with scams that can involve asphaltting, fencing, painting, carpet cleaning and roofing. The quotes given can be exceptionally low and the work done, if any, is usually shoddy or incomplete. As soon as they are detected in one town they vanish, only to resurface with the same scam in another State. Their identification papers are often false.

Rogue itinerant traders obtain a quick return by requiring consumers to pay for the job up front in cash and can rush the consumer into a decision by telling them that the deal is a 'special offer' and is valid only for that day as another customer has cancelled. Rogue itinerant traders even drive their victims to the bank to obtain payment and then disappear, leaving an unfinished or sub-standard job. The rogue may ask their victims for money to purchase materials and then never return. (CAV 2005a)

Rogues may also target industries where they can gain financially by operating illegally. By avoiding the cost of purchasing a licence or meeting the regulated industry standards, for example, a rogue can obtain a financial advantage over its ethical competitors.

These financial incentives can be large in industries where regulation restricts the number of traders that can enter the industry or the level of output they can produce. In these industries new entrants purchase licences before they can start their businesses, or need to pay for a significant amount of good will. The cost of legitimately entering such industries, and the profit from operating unlicensed, encourages rogue traders to operate illegally. Similarly, if the cost of meeting industry standards is very high, there can be an incentive for rogues to not comply with the standards and subsequently undercut legitimate businesses.

3.2 Consumers may not protect themselves

Rogues rely on consumers failing to recognise that products or services they are being offered are not legitimate or not worth the asking price. To achieve this, rogue traders:

- offer goods for sale, unseen, through the internet or by telephone
- focus on goods and services of a nature that makes it difficult for consumers to judge their quality either prior to purchasing and using them (experience goods) or unless something goes wrong, requiring them to rely on the honesty of traders to ensure the products or services meet their expectations (credence goods), or
- use high pressure or other sales tactics to convince consumers to buy products or services, even though the benefits claimed are unrealistic.

A report in the United Kingdom on doorstep (door-to-door) selling noted that the problem of judging the quality of services was common in property maintenance because:

The consumer, especially if they are elderly, may have difficulty in checking the extent and quality of the work carried out. (OFT 2004a, p. 83)

Rogue traders often target industries where consumers have more difficulty protecting their own interests, as this increases rogues' chances of successfully deceiving consumers.

3.3 Strategies to avoid detection

Rogue traders also operate in industries where they can adopt business practices and strategies that conceal their rogue activity, making it harder to identify and catch perpetrators or, if perpetrators are caught, to recover the losses. They may use one or more strategies to avoid detection and prosecution, including mobility and anonymity, and avoiding compensating victims by exploiting loopholes and dispersing assets.

Mobility

A key strategy rogue traders use to avoid detection is mobility. The Office of Fair Trading described how itinerant traders in the United Kingdom take advantage of mobility:

The main problem faced by Trading Standards is the fact that the traders may be highly mobile, often travelling large distances for work and are therefore difficult to trace. When complaints are received trading standards departments can often do little because it is after the event. (OFT 2004a, p. 94)

The problems in Australia are similar. Rogues can be mobile internationally, among states and territories, and across regions. They may remain in the same industry or move industries. Mobility helps avoid detection by exploiting lags in regulators' ability to detect, identify and prosecute traders. By the time a regulator becomes aware of a problem the rogue will have moved on, and can no longer be found. Rogues can use mobility more readily in industries where it is possible to:

- avoid establishing a fixed business address or showroom
- stay in one location for only a short period and readily move across regions and among states and territories
- use sales techniques where the trader goes to the customer (door-to-door or via the telephone or the internet), rather than the customer approaching the trader
- operate as a small business, and
- easily enter and leave the industry, because of low overhead costs, for example, or few regulatory requirements before starting trading.

Anonymity

Combined with mobility, rogues use anonymity to avoid detection. If consumers do not know with whom they are dealing, it is more difficult for regulators to identify and catch offenders. In industries that accommodate anonymity, rogue traders can:

- hide their identities from customers and regulators by:
 - using prepaid mobile phones, so they cannot be tracked through telephone numbers
 - using false names
 - using post office boxes rather than street addresses, or
 - providing first names only to consumers and in advertisements

- use multiple business names, so it is difficult to track the links between the various business entities, and
- contact customers door-to-door, via the telephone or through the internet.

Exploiting loopholes

In addition to strategies to avoid detection, rogues use strategies to minimise the consequences of getting caught. They exploit a variety of loopholes such as:

- loopholes in legislation that make it difficult to prosecute rogue activity
- gaps in regulators' monitoring and enforcement
- gaps or inefficiencies in state and territory coordination
- lags in the time taken for different jurisdictions to respond to a problem – if a commodity is banned in one state because it is unsafe, for example, rogue traders may move to other states where they can continue to sell the dangerous product, and
- loopholes in international law that make it difficult for Australia to identify and prosecute rogues that target Australian consumers from overseas.

The ability to hold officers and employees accountable for their actions, separate from the company that engages them, is important to prevent rogues misusing the company structure to avoid accountability.

Without the power to hold individuals accountable, rogues could exploit consumers, disband the company responsible leaving no entity that could be pursued for compensation or redress, and avoid taking personal responsibility for their actions.

This is currently not the case. Two recent decisions of the Full Federal Court and one of the New South Wales Court of Appeal¹ accepted that directors, agents and employees of corporations are potentially liable for their actions if they engaged in behaviour that would breach the Fair Trading Act.

One of these cases, *Arms v Houghton* is on appeal to the High Court. The case was heard in October 2006 and Consumer Affairs Victoria intervened in the appeal as a friend of the court. Consumer Affairs Victoria highlighted the public interest in continuing to be able to pursue officers and employees of defunct or insolvent corporations who abuse the corporate form to shield themselves from personal liability for actions that breach the Fair Trading Act. A decision on the appeal is due in early 2007.

¹ *Arktos Pty Ltd v Idyllic Nominees Pty Ltd* [2004] FCAFC 119, *Arms v Houghton* [2006] FCAFC 46, and *Wong v Citibank Ltd* [2004] NSWCA 396.

The problems caused by inconsistency in regulation have also been recognised.

The European Union highlighted how rogues can exploit loopholes between countries:

The European Advertising Standards Alliance concluded in its 2002 annual report that 'cross-border complaints overwhelmingly concern the activities of 'rogue traders' and other fringe operators, who deliberately set out to exploit the loopholes between national regulatory systems'. (EU 2003, p. 2)

The current arrangements facilitated the life of rogue traders operating cross-border within the EU, weakening the credibility of the international market for consumers. The regulation on enforcement cooperation is therefore something of a landmark for consumer policy ... In addition, since rogue traders do not stop at the borders of the EU, cooperation with third countries will have to be stepped up. (Byrne 2004, pp. 4 and 6)

The risk of rogues operating internationally is rising as the internet allows them to operate more freely across national borders.

Using these technologies, fraud operators can strike quickly on a global scale, victimise thousands of consumers in a short time, and disappear nearly without a trace – along with their ill-gotten gains. (Majoras 2005, p. 2)

Box 4: Phoenix companies

A phoenix company is a previously bankrupt company that restarts under a new identity.

Phoenix company activity is not inherently unlawful. Business failure is not an offence. Nor is it an offence to fail on more than one occasion ... Nor [is] it unlawful for the company's officers to purchase the assets of the old company from the administrator for use in a subsequent business. (Joint Committee 2004, p. 131)

The Parliamentary Joint Committee noted, however, that some companies 'abuse the form and the privilege of limited liability' by establishing schemes that deliberately 'structure their operations in order to engage in phoenix activity, avoid detection and exploit loopholes in insolvency laws'. (Joint Committee 2004, pp. 131 and 132)

Company insolvency has the greatest impact on unsecured creditors. Companies may also fail owing large amounts in State and Commonwealth taxes. The impact on consumers varies. Consumers are most vulnerable when they have an ongoing relationship with the service provider, for example a need for specialist parts or maintenance, when they have unresolved problems with the product or service, or the regulator is attempting to obtain redress from the company for activities that previously caused consumer detriment. Insolvency and Trustee Service Australia observed that 'bad workmanship seems to often precede financial failure'. (IAIR 2004, p. 24)

Asset shedding

Another tactic rogue traders use to avoid compensating victims for their loss is to ensure there are no assets that can be called upon to fund compensation. A typical example is fraudulent phoenix companies. While not all phoenix companies are rogues (Box 4), this is a strategy that some rogues use to strip a company of its assets, send it into liquidation to avoid ongoing obligations to its creditors and customers, and then re-establish the same type of business or continue to trade through a related company.

3.4 Links to crime

While rogue traders are not necessarily involved in other criminal activities, it is possible that some criminals are also rogue traders. Many commentators accept that there is clear evidence of criminal organisations involved in legal activities. Criminals who are involved in rogue activities are likely to choose industries that exhibit the characteristics discussed above. Their choice of industry may be also influenced by links between the legal activity and their illegal activities. Fiorentini, for example, argued that organised crime operators could be attracted to operating legitimate businesses in areas that:

- provide sources of legitimate income to 'hide' true principal businesses
- provide places to trade – so that small shops, bars and restaurants are used to cover activities relating to certain crimes
- produce outputs that are also needed for operators' illegal activities (such as transportation, communications and warehousing) – taking advantage of the benefits of integrating legal and illegal activities;
- allow at least part of the profits of crime to be laundered in legitimate businesses – thus reducing the risk involved in money laundering, and/or
- provide opportunities to diversify portfolios with investments that have different mixes of risk and returns. (Fiorentini 2000, p. 448)

The involvement of criminals, and particularly organised crime, in rogue activity generates additional risks. These operators may include in their strategies to avoid detection and prosecution, attempts to intimidate and corrupt regulators. They may also intimidate, threaten or assault their victims to obtain payment or stop them from reporting rogue activities.

“Policies that deal with rogue traders”

4

Consumer regulation and other policy strategies protect consumers and assist in controlling the activities of rogue traders. But it is difficult to stop rogues. By their nature, rogues exploit loopholes in regulation and it is difficult to control traders' intent. It is necessary to:

- deter rogue traders from entering industries
- act quickly to identify and target rogues before they avoid detection
- stop offending behaviour so it does not cause further damage, and
- stop rogues from engaging in similar activities in the future.

As no single policy could achieve all these objectives a mix of strategies is necessary. As noted previously, the activities of rogue traders and the strategies they use to avoid detection also vary significantly, so a different mix of strategies may be needed to target each rogue.

Many policy tools are available. The following sections discuss the tools used most often against rogue traders. These tools usually attempt to discourage rogues by increasing the likelihood of being caught, making being caught costly, or increasing the cost or difficulty of continuing rogue activities.

“ The role of consumer policy tools ”

5

Consumer policy tools are the tools available to Consumer Affairs Victoria. They can be used to target rogue traders without cooperation from other agencies.

5.1 Enforcement under the Fair Trading Act

While the *Fair Trading Act 1999* (Vic) is not targeted solely at rogue traders its provisions can deal with rogue activity. The effectiveness of the Fair Trading Act in empowering Consumer Affairs Victoria to deal with rogues can be assessed against:

- the coverage of the Act – whether there are loopholes or gaps that limit Consumer Affairs Victoria pursuing some types of rogue activity
- the size and nature of the penalties and deterrents – whether these are an effective disincentives to engaging in rogue activity or incentives to ceasing such activity, and
- the powers to collect information and investigate complaints – whether these enable Consumer Affairs Victoria to build cases against rogue traders.

Many of the amendments to the Fair Trading Act in 2003 and 2004 enhanced the powers to detect and stop rogue traders. The 2004 amendments were directed specifically at influencing compliance.

Coverage of the Act

First, does Victorian legislation cover all types of rogue activity? The powers in Victoria's Fair Trading Act are relatively broad. Consistent with other Australian jurisdictions, Victoria's Act includes general provisions to prohibit unconscionable, misleading or deceptive conduct. An international comparison of consumer regulation, undertaken by the United Kingdom, identified that general provisions promote compliance and can address broad and changing consumer issues.

The UK does not have the equivalent of a general duty to trade fairly. This can act successfully as a backstop given the inflexibility of piecemeal legislation and ease of public comprehension of a simply worded basic right as in Australia and the US. (DTI 2003, p. 33)

Victoria has extended the coverage of its legislation to deal with emerging issues. Since the Fair Trading Act was passed in 1999 the regulation of consumer contracts and telephone marketing, for example, have been amended. Victoria's legislation is now as broad as, or broader than, other Australian Acts. The *Trade Practices Act 1974* (Cwth), for example, does not specifically regulate the fairness of consumer contracts.

Challenges can still emerge, however, as new industries like m-commerce develop:

There are also likely to be a number of limitations in current legislation to protect consumers using m-commerce. For example, current fair trading legislation in Victoria requires adequate disclosure about terms and conditions of purchase. How will these be transmitted via a mobile phone given the limitations of the screen? Another example is in the provision of financial services advice online. Prior to doing this, a firm must obtain a considerable amount of information about a prospective customer. It is not clear that these regulatory requirements can be met using a mobile phone as the small phone screens can show a maximum of 100 characters. It seems impractical and cumbersome to expect a customer to tap out the words on a mobile phone handset. (CAV 2002, pp. 16–17)

While new industries can present new challenges that may warrant future amendments to legislation, the Fair Trading Act appears to be broadly capable, subject to jurisdictional limitations, of covering the objectionable activities of most rogue traders.

Second, is Victorian legislation capable of capturing all activities that are linked to, or affect, Victoria? Could traders avoid Victorian laws by locating outside of Victoria, for example, or encouraging Victorian consumers to travel interstate or overseas?

Again, Victoria's Fair Trading Act has wide application. In 2003 section 6 was inserted into the Act.

6. Extra-territorial application of this Act

(1) *This Act applies within and outside Victoria.*

(2) *This Act applies outside Victoria to the full extent of the extra-territorial legislative power of the Parliament.*

This makes the Act applicable where: a trader is located or registered in Victoria; the goods or services are supplied in Victoria; or the trader makes claims about those goods or services in Victoria. While the scope of the legislation has not been legally tested, it is unlikely to cover loss or damage suffered by a Victorian if neither the transaction nor the trader is located in Victoria – such as where the product was not advertised in Victoria and was purchased interstate and brought back to Victoria.

When rogues operate across jurisdictions, there are benefits to consumer agencies coordinating their activities. Even where Victoria could legally take action, there may be advantages in another agency taking the lead in the investigation and prosecution. If a trader is located and active in another state or territory, for example, that jurisdiction may be in a better position to pursue the investigation successfully and it may have other laws, such as licensing requirements, that could be used to achieve redress for the activities of the rogue. Coordination is discussed in section 7 of the paper.

Size and nature of penalties and deterrents

The Fair Trading Act contains a range of penalties and deterrents, some of which were strengthened by the 2003 and 2004 amendments. Generally, the Act allows relevant bodies to:

- impose financial penalties on traders and/or require them to compensate consumers for the damage they caused, or rectify that damage
 - For example, many sections include penalties for breaching the Act and a variety of orders can be made against a person found to have contravened the Act (section 158). The Act allows the Director of Consumer Affairs Victoria to conduct proceedings against traders (section 142A), or conduct proceedings on behalf of consumers, when he/she considers there is a case that a trader has breached the Act and pursuing the proceedings is in the public interest (section 105).

- reduce the ongoing damage rogues cause by preventing them from continuing the objectionable activity or removing them from the industry
 - For example, the ability to obtain injunctions, including cease trading injunctions (section 151A), prevent a trader from transferring money or property (section 154), ban dangerous products (section 40), suspend the licence or registration of a trader (section 106D), and accept undertakings that put conditions on traders' future activities (section 146), and
- make consumers more aware of rogues so they can protect themselves
 - For example, the ability to require traders to publish information consistent with an adverse publicity order (section 153) and allow the Director of Consumer Affairs Victoria or the Minister to release public warning statements about rogue traders and their activities (section 162A).

Advertising the identity and activities of rogue traders is intended to:

1. make consumers aware of the rogues and their activities (this issue is discussed in section 5.3)
2. shame rogues into modifying their behaviour, and
3. make other businesses aware that the regulator is taking action against rogue traders, increasing the perception that rogues will get caught and deterring other businesses from engaging in similar practices.

In the case of rogue traders it is important not to overstate the effectiveness of the second objective. Most rogues do not rely on good will or their reputation to conduct their business. Actions that damage their reputation are, therefore, unlikely to be effective. Advertising would only damage a rogue if it successfully reduced the risk that consumers would fall for the rogue's tactics. The benefits of advertising the activities of rogues are, thus, greatest in making consumers aware of the rogues and increasing the perception that rogues will be caught, deterring others from engaging in rogue activity.

As a result of the amendments to the Fair Trading Act in 2003 and 2004 (Box 5), Consumer Affairs Victoria has greater flexibility in the deterrents it can use to stop rogue traders. Tools such as interim injunctions, 'show cause' notices and infringement notices allow it to respond more quickly to rogue activity. Final injunctions, which require traders to comply with directives such as ceasing trading, restraining from certain conduct or undertaking specified action, and greater powers to enforce undertakings, also increase Consumer Affairs Victoria's ability to stop rogue traders re-offending.

Box 5: Amendments to penalties and deterrents in the Fair Trading Act

In 2003 amendments to the penalties and deterrents in the Fair Trading Act approximately doubled applicable financial penalties and allowed for:

- issuing warnings and naming rogue traders to highlight their activities to the community
- suspending licences or registrations of rogue traders where urgent action is needed to protect consumers from substantial harm
- issuing 'show cause' notices to traders notifying them that Consumer Affairs Victoria believes they have breached the Act, requiring them to justify why they should be allowed to continue to carry on their businesses
- obtaining 'cease trading' injunctions against rogues
- providing for 'infringement notices' to be issued for appropriate offences, and
- expanding the Victorian Civil and Administrative Tribunal's powers to resolve fair trading disputes.

In 2004 there were further amendments to:

- strengthen the powers to enforce undertakings
- provide for interim injunctions or injunctions to require traders to undertake activities such as instituting staff training programs, refunding money to consumers, disclosing information or honouring promises, and
- allow for adverse publicity orders, which require traders to publish corrective advertisements or advertisements that acknowledge breaches of the law.

In 2004-05, as a result of a greater willingness to take action and the effectiveness of the new powers, Consumer Affairs Victoria:

- obtained 72 prosecutions, injunctions and disciplinary actions and 60 enforceable undertakings
- conducted 72 civil actions, and
- served 347 infringement notices.

Examples of enforcement activities undertaken in 2004-05 appear in Box 6.

Box 6: Examples of Consumer Affairs Victoria enforcement action

Diamond Security Doors and Screens

In March 2005 Consumer Affairs Victoria took enforcement action against Mr Michael Johnson, trading under the unregistered business name Diamond Security Doors & Screens. Mr Johnson advertised in newspapers, offering to supply and install security doors and screens on private homes. He called on customers by arrangement, gave quotes and accepted large deposits, and then failed to return to provide the goods. Customers then tried to contact Mr Johnson, without success.

Consumer Affairs Victoria obtained interim injunctions prohibiting the use of the unregistered business name and restricting Mr Johnson to operating on a cash on delivery basis. At the final hearing the injunctions were confirmed, permanently restraining Mr Johnson from accepting payment for the supply of goods or services until they had been provided. Mr Johnson was also ordered to provide full details of transactions he had entered into during a specified period and compensate 16 consumers for their losses sustained as a consequence of the breaches of the Act.

Livio Cellate, Astvilla Pty Ltd and Perna Pty Ltd

The Cellante group offered residential properties for sale in rural areas of Victoria, primarily to Melbourne-based consumers. Arrangements were made for potential customers to view these properties on Sundays, when local estate agents were closed. It was alleged that the Cellante group urged consumers to conclude sales on the spot, by making representations about the property markets concerned and the popularity of the relevant properties.

Purchasers alleged that they later discovered that the properties they had bought had been on the market for some time at prices much lower than those they had paid. It was further alleged that the Cellante group had represented themselves as sellers of the properties, but had in fact purchased the properties (at the much lower prices) after concluding sale agreements with purchasers.

(continued)

Box 6 (continued)

Consumer Affairs Victoria sought injunctions to restrain the Cellante group from employing these sales techniques and to compensate an affected consumer. In 2004-05 the Horsham Magistrate's Court found that the group had engaged in unconscionable conduct and misleading or deceptive conduct, granted injunctions restraining similar conduct, and awarded an affected consumer approximately \$30,000 in damages. The decision was upheld on appeal to the Supreme Court. The consumer was awarded over \$37,000 in damages, including interest.

Joseph Capri

Joseph Capri was prosecuted by Consumer Affairs Victoria in September 2004 and convicted of building offences giving rise to 30 charges, including trading as an unregistered builder, demanding excessive deposits and failing to deliver the services for which he had been paid, engaging in misleading conduct, and trading using a series of unregistered business names.

He was fined \$49,000 on conviction and ordered to pay \$15,535 in compensation to consumers and \$1,792 in legal costs to Consumer Affairs Victoria.

Still, there are two issues that warrant further consideration. First, Victoria's maximum penalties are considerably lower than Commonwealth penalties under the Trade Practices Act. Current maximum penalties in Victoria are usually around \$62,900 for an individual and \$125,800 for a company. Under the Trade Practices Act similar offences have a maximum penalty of \$220,000 for an individual and \$1.1 million for a company.

Victorian penalties are, however, higher than most other states'. In New South Wales, for example, the penalties are \$22,000 for an individual and \$110,000 for a company and in Queensland the maximum penalty for offences prosecuted in a summary way is \$22,250, and \$40,500 if the offence is prosecuted on indictment.

Actual penalties awarded in Victoria are consistently lower than the maximum allowed under the Act. During the period June 2003 to the end of 2005, most penalties imposed were less than \$10,000. Only three were more than \$50,000. Research conducted by Consumer Affairs Victoria indicates that, following the 2003 amendments to the Act increasing the value of maximum penalties that can be imposed, the value of individual penalties imposed did not increase. The total value of fines imposed on individual parties did increase, but this was due to Consumer Affairs Victoria changing its approach, charging parties with a number of offences simultaneously.

The penalties imposed under the Trade Practices Act appear to be substantially higher than those under the Fair Trading Act. It is difficult to substantiate, however, whether this difference is driven by differences in the circumstances of the cases or the approaches of the courts.

There is no clear justification for states imposing penalties lower than those provided for in the Commonwealth legislation. Increasing the penalties would send a clear message about the seriousness Parliament attaches to deliberate attempts to exploit consumers.

Second, in Victoria it is not possible to seek prison sentences under the Fair Trading Act, despite some of the offences involving fraud and theft, which do have imprisonment as a possible penalty. In contrast, section 6AA of the Trade Practices Act applies chapter 2 of the Criminal Code to offences under that Act, making imprisonment a competent sentence. In New South Wales the Fair Trading Act 1987 allows prison sentences of up to three years for second or subsequent convictions, as well as fines.

Victoria can seek prison sentences under some other consumer Acts. One of the penalties under the Consumer Credit (Victoria) Act 1995, for a person who offers financial broking services after being disqualified as a finance broker, or does not comply with conditions set by the Business Licensing Authority, is two years' imprisonment. The Estate Agents Act 1980 provides for a penalty of up to 10 years' imprisonment for an agent that fraudulently transfers or does not pay or appropriately account for money held in trust (section 91).

In addition, the Director of Consumer Affairs Victoria (or delegate) can commence criminal proceedings by filing a charge with the Registrar of the Magistrates Court of Victoria. Such charges could include summary or indictable offences² under the *Crimes Act 1958* (Vic), both of which can attract prison sentences.³

The Crimes Act includes provisions that make it an offence to dishonestly appropriate property belonging to another with the intention of permanently depriving them of that property (theft, section 74); obtain financial advantage by deception (section 82); engage in false accounting (section 83); falsify documents (section 83A); give or receive a false or misleading receipt (section 178); or fraudulently induce a person to invest money (section 191). All of these are activities in which rogue traders could be involved.

² In general, summary offences are heard by the Magistrates Court, indictable offences are more serious offences heard by a judge and jury.

³ The Director (or delegate) can file both summary and indictable charges but they can only conduct proceedings relating to offences heard summarily. Indictable offences must be referred to the Director of Public Prosecutions.

There are, however, limits on the ability of the Director (or delegate) to conduct summary proceedings. The Director of Public Prosecutions may take over and conduct any proceedings in respect of any summary and indictable offence (section 22 of the *Public Prosecution Act 1994* (Vic)). Where an accused person is charged with an indictable offence, capable of being heard summarily, he or she may decline to accept the summary jurisdiction, and the offence is then heard by a judge and jury. The Director (or delegate) would lose control of the proceedings, which must be referred to the Director of Public Prosecutions at this stage. This would be unusual, however: given the lower penalties usually attached to summary offences, an accused would not usually insist on a trial by judge and jury.

Finally, it is not clear how extensively provisions that allowed for prison sentences under the Fair Trading Act would be used in Victoria. The evidentiary requirements of a criminal case would often make it impractical and costly to seek redress for consumers and prevent ongoing damage by rogue traders through criminal prosecution, particularly given that the Director of Consumer Affairs Victoria already has a limited ability to prosecute consumer-related offences under the Crimes Act, where prison sentences are available.

Powers to collect information and investigate complaints

Finally, the Fair Trading Act's success in stopping rogue traders is affected by the regulator's powers to monitor compliance, detect the activities of rogues and collect evidence to prosecute them. These powers were also expanded in the recent Fair Trading Act amendments, giving Consumer Affairs Victoria added powers to use additional inspectors and require people to provide information and justify their actions.⁴

First, the Act provides for inspectors to investigate complaints and gives inspectors powers to collect evidence and question people (Part 10). The 2004 amendments to the Fair Trading Act expanded the categories of people that can be appointed as inspectors, including allowing Victoria to use inspectors appointed under fair trading legislation in other Australian states and territories. This increases Victoria's ability to cooperate on investigations with other jurisdictions.

Second, the Director can require people to provide information.

- Anyone can be required to provide information or documents to assist Consumer Affairs Victoria to monitor compliance, even if it would incriminate them (section 106HA).

- Anyone the Director believes can produce information on a suspected breach of the Act can be required to provide information, documents or evidence, even if it would incriminate them (section 106I). This allows the Director to conduct a hearing and require that evidence be provided under oath.
- On the Director's request, publishers and telephone marketers must produce the information they are required to retain under the Act (section 118).

The implications of providing such information and the extent to which it can be used in later legal proceedings vary depending on circumstances. Even when the information cannot be used in subsequent legal proceedings it helps target future investigations by informing the regulator about the scope of rogue activity. Consumer Affairs Victoria served 156 information notices in 2004-05.

Finally, the Director of Consumer Affairs Victoria can require people to justify their actions by substantiating their claims about a product or service (section 106A) or showing cause why they should be allowed to continue carrying on business (section 106B). Nine substantiation notices were served in 2004-05.

Overall, because it is general legislation, spanning all trade and commerce, the Fair Trading Act usually relies on standards (which specify the required behaviour), rather than rules (which define how behavioural requirements must be met). Standards are more appropriate in legislation with a broad application, as defining practical, effective rules would be impossible. They are also more flexible, ensuring that the law automatically covers new businesses or new forms of unfair trading. It can be more difficult, however, to collect evidence and demonstrate that a trader has breached a standard than to prove that a trader has not complied with a prescriptive rule.

While it is possible to debate the detail of some of the Fair Trading Act provisions relating to information collection and investigation, these powers are relatively wide. Key areas (such as the power to obtain information to monitor compliance) have been used to good effect and Consumer Affairs Victoria has been proactive in taking action and cooperating with other agencies, as in the case of Grove Conveyancing Services. Grove Conveyancing, a partnership providing conveyancing services in the Geelong area, collapsed after allegations of misappropriation of funds, affecting a large number of consumers. To secure evidence to protect consumer interests, Consumer Affairs Victoria seized 13,318 files from the offices of Grove Conveyancing Services under warrant. Victoria Police seized a further 168 files. Consumer Affairs Victoria catalogued the files, established an inquiry register, answered 396 enquiries, and returned 111 certificates

⁴ This is in addition to other sources of information, such as intelligence collected through consumer complaints and inquiries.

of title and other security documents found in the seized files to their lawful owners. Consumer Affairs Victoria identified specific transaction files to be forwarded to the Victorian Police for further action. Charges were issued against a proprietor of Grove Conveyancing in November 2005, and at date of publication were before the Geelong Magistrate's Court.

As these provisions are relatively new, it is too early to conclude whether further amendments are needed. There may, however, be scope for other amendments to improve the effectiveness of the Fair Trading Act. For example section 83 of the Trade Practices Act allows findings of fact in one case to be used as prima facie evidence in subsequent cases.

In a proceeding against a person under section 82 or in an application under subsection 87(1A) for an order against a person, a finding of any fact by a court made in proceedings under section 77, 80, 81, 86C or 86D, or for an offence against a provision of Part VC, in which that person has been found to have contravened, or to have been involved in a contravention of, a provision of Part IV, IVA, IVB, V or VC is prima facie evidence of that fact and the finding may be proved by production of a document under the seal of the court from which the finding appears. (Trade Practices Act section 83)

Section 83 reduces the cost of prosecuting subsequent cases and reduces the regulator's response time, as it does not need to wait until the cases for all claimants have been finalised before it takes action against a rogue trader. There is no equivalent provision in Victoria's Fair Trading Act.

5.2 Industry specific regulation including licensing

Often it is argued that industry specific regulation, such as licensing regimes, is needed to control rogue traders. Licensing, for example, can help stop rogues by controlling who can start a business, monitoring activity in the industry and removing traders that don't meet licensing conditions, from the industry. Many licensing schemes use a 'fit and proper person' test to prohibit people with histories of exploitative behaviour from obtaining licenses. In Victoria, approximately 40 Acts with licensing and registration provisions have a 'fit and proper person' test. About 20 Acts with licensing and registration provisions also have conditions on the characters of associates to the applicant.⁵

Licensing or registration schemes can also require ongoing reporting of the activities of the licensee and maintenance of certain types of records, or give the regulator the power to request the provision of information. Estate agents, introduction agents, travel agents, motor car traders, credit providers, second hand dealers and pawnbrokers, and prostitution service providers must supply annual statements when they renew their licences or registrations. They are also required to create and hold records on their activities. For example, motor car traders must record the details of the purchase and sale of each car in a dealings book (*Motor Car Traders Act 1986* (Vic) section 35). Some schemes include other strategies to reduce the damage that rogues cause consumers. For example, the Motor Car Traders Guarantee Fund may compensate consumers who have been victims of rogue motor car traders.

Licensing or registration can assist enforcement. The licence or registration of a trader can be revoked if it engages in rogue activities and the regulation may provide additional mechanisms to pursue unlicensed or unregistered rogues operating in the industry.

⁵ Derived from a search of the Victorian legislation database

The Business Licensing Authority can also impose conditions on licences to protect the public interest. Such conditions can limit the damage caused by traders that are suspected of being involved in rogue activities or reduce the ability of individuals who have histories of rogue activity being involved in licensed businesses. Conditions could include prohibiting a person from having any role in a business or being present on the business's premises, or requiring the licensee to provide additional information, undertake additional monitoring, set up a complaints handling process or provide additional financial guarantees to limit the risk of financial loss to consumers.

For those industries subject to licensing, such schemes can help deal with rogue activity. They can assist in identifying and excluding rogues with records of inappropriate behaviour before they enter licensed industries, and identifying and taking action against licensed or unlicensed rogues operating in the industry.

The next question often posed is whether new licensing schemes should be implemented to deal with rogue traders in other industries. Such suggestions should be treated with caution because licensing schemes can be costly for government, the regulated industries and consumers.

Licensing regulation requires government resources to develop, implement and enforce the regime.⁶ It also imposes costs on all businesses, including ethical businesses that are not the target of the regulation, but are still covered by its requirements. In some cases, it disproportionately disadvantages honest businesses that are fully compliant but are undercut by rogues that have lower costs because they avoid compliance. The extent of these costs will depend on the conditions in individual licensing schemes.

Consumers are affected when the costs of business compliance and cost recovery charges are passed on in higher prices. Consumers may be further disadvantaged because of difficulty government has setting conditions that exclude only rogue traders and do not also limit new services that could expand consumer choice.

In addition to these costs, licensing cannot eliminate rogue traders. While it significantly reduces the risk of rogues getting through the licensing screen, it is not possible to guarantee that no licensed operator engages in rogue activity or that unlicensed rogues do not enter the industry. Industry specific regulation simply provides additional tools to target rogues. The effectiveness of any individual scheme depends on the provisions in the regulation, the way it is administered and the resources and priority devoted to enforcement.

In industries where industry specific regulation already addresses other issues, it can help deal with rogue activity. Given there are relatively few rogue traders in most industries, however, the costs to legitimate businesses and consumers makes introducing industry specific regulation simply to target a rogue trader problem questionable – particularly given the scope and powers in the Fair Trading Act (discussed in section 5.1). To the extent that industry specific regulation allows for stronger powers (for example, the inspection powers in some licensing schemes) it may be possible to use the experience gained from this regulation to improve the effectiveness of the Fair Trading Act.

5.3 Creating informed and aware consumers

Sections 5.1 and 5.2 discussed policies that reduce the damage rogue traders cause. Other strategies empower consumers to look after their own interests, by educating and informing them about their general rights or about rogue traders.

The more aware the community is about consumer rights the more discerning consumers will be. They will be better at detecting rogue traders and responding quickly if they inadvertently engage businesses that are not delivering the goods or services they expected, reducing the damage rogues can cause. Informed consumers are more likely to lodge inquiries or complaints with consumer agencies, increasing agencies' ability to identify and target problems.

⁶ The cost met directly by government depends on the level of cost recovery from the regulated industry.

Consumer Affairs Victoria uses various strategies to highlight rogue businesses, scams or industries that are susceptible to rogue traders' activities. The Director of Consumer Affairs Victoria issues public warnings about unfair business practices and people who engage in such practices under section 162A of the Fair Trading Act⁷ and other Acts, such as the *Fundraising Appeals Act 1998*. At date of publication there were eleven traders named on the Consumer Affairs Victoria website:

- Ronald Heelan Fredericks (aka Bon Levi) and Little Joe Snacks
- Kevin John Sims (aka Simon Spain) and Central Casting, Global Capital Casting, MM Promotions and Little Stars Models
- Bevan Crowley, Ann Crowley, Hannah Crowley, Australasian Corporate Events (2004) Pty Ltd and Enews Publications Pty Ltd, and
- European Land Sales Partnership (aka European Land Sales Australia, ELS Australia and European Land Sales) and Stephen Cleeve.
- Gino Carmignani
- Australia Water Provisions
- Joseph Yelding (also known as Joe or Joey Yelding operating as Diamond Coat Roofing)
- Best Conferences Pty Ltd and Liam Crowley
- John Stewart, trading as Bitumen Driveways
- Christian Kalos (also known as Christopher Tsakalos)
- Victorian Emergency Relief Fund Inc. (CAV 2006, p. 1)

Adverse publicity orders (under section 153 of the Fair Trading Act) and other orders, including publicity orders under section 158, have been imposed. For example, Denise Keating was ordered to publish a statement recognising that she was operating as an estate agent without a licence and correcting misleading advertising. SJS Imports was convicted of supplying banned toys and cigarette lighters, which posed significant safety hazards. It was ordered to publish a public warning in the *Herald Sun* detailing the banned products it had sold and requesting consumers to return or destroy those products. Encore Systems, an internet trader, was ordered at an interim stage of proceedings against it to publish a notice on its website that informed visitors to the site that the company could not demand or accept payment for goods or services until these had been delivered to consumers.

⁷ If it is in the public interest, the Director may publish a public statement or issue a public warning providing information on: the goods or services that are unsatisfactory and the people supplying them; unfair business practices and the people engaged in them; and other matters that adversely affect consumers purchasing goods and services from suppliers.

⁸ This book was prepared by a Commonwealth, state and territory working group under the Ministerial Council on Consumer Affairs.

Other initiatives also inform consumers. For example:

- Consumer Affairs Victoria's Annual Report lists problem traders where it has received a significant number of complaints or identified persistent problems in relation to those traders
- Consumer Affairs Victoria's website contains a database that describes different scams and businesses that have engaged in such scams
- *The Little Black Book of Scams* describes various scams and how to avoid them⁸
- the Australasian Consumer Fraud Taskforce coordinates an annual consumer information campaign (involving private sector organisations) to coincide with Global Consumer Fraud Prevention Month, and
- the Australian Securities and Investments Commission website lists unlicensed overseas organisations that pose as brokers or investment houses and try to sell investments, financial advice or financial products by telephone.

If effective, information and education can benefit consumers by stopping damage before it occurs. Such strategies are particularly important when it is difficult or time consuming to identify and deal with the trader, for example, if the scam is instigated overseas using the telephone or the internet to target Australian consumers. While, in some cases, coordinated international action is taken, this is not always practicable or within Victoria's control. Arming Victorian consumers against scams is, therefore, often the only viable alternative. Education strategies can also target multiple rogue activities simultaneously, increasing the efficiency of the policy. There are, however, limitations to the effectiveness of consumer awareness campaigns:

- it is not possible to identify all rogue traders and scams
- it is difficult to inform all consumers who are likely to come into contact with a particular rogue trader or scam, and
- new traders and scams are always emerging, so continuous vigilance is necessary.

Therefore, while awareness raising is very important, it is only part of the solution. It is often a reactive strategy and the time lags mean that the most astute rogues may have disappeared before consumers are aware of their activities. It can be difficult to target those who are most at risk, and to ensure they listen, understand and take note of the messages and then retain and use that information when confronted by a rogue.

“ Other regulatory tools that target rogue traders ”

Rogue traders can be prosecuted under other legislation not administered by Consumer Affairs Victoria. Other Victorian legislation includes taxation legislation, and Commonwealth legislation includes companies regulation, tax Acts and the Trade Practices Act.

Many rogue traders breach Commonwealth and state taxation laws, but Consumer Affairs Victoria cannot, on its own, pursue rogues through that legislation. Commonwealth companies regulation and the Trade Practices Act can also be used to target the activity of rogue traders. There may be scope for considering amending these Acts to give state agencies more access to remedies under that legislation.

6.1 Companies regulation

Some rogue traders deliberately abuse the corporate form. They set up their affairs with the intention of avoiding paying their debts and escaping detection. Some structure their businesses around several entities, holding most of their debts in an arm that has few assets. When that arm fails, the organisation continues trading but creditors do not have recall on the assets held in the other entities. Another technique is to run down the assets of a business and accumulate debt, sending the business into receivership with the deliberate intention of recommencing activities through another business, which uses some or all of the previous business's assets and is controlled by parties related to the management or the directors of the previous entity. These may be called fraudulent phoenix companies.

As noted previously, phoenix companies are not illegal per se, but the actions of directors or other officers in the company do risk breaching the *Corporations Act 2001* (Cwth). If directors and other officers fail to meet their duties (such as the duty of good faith or the proper use of information or position), are involved in insolvent trading, or enter into agreements or transactions intended to reduce or prevent paying employee entitlements, they are in breach of corporations law. If the phoenix company is also involved in tax avoidance it potentially breaches the Commonwealth Criminal Code.

The Corporations Act provides for people to be disqualified from managing corporations:

- automatically if they are undischarged bankrupts, or convicted of certain offences that are serious breaches of the Act or involve prison terms (section 206B)
- by the court,⁹ if they have contravened civil penalty provisions in the Act (section 206C)
- by the court, for up to 20 years, if they were, during the previous seven years, an officer of two or more corporations at the time they failed and ‘the manner in which the corporation was managed was wholly or partly responsible for the corporation failing’ (section 206D)
- by the court, if they repeatedly contravene the Act (section 206E), and
- by the Australian Securities and Investment Commission (ASIC), for up to five years, if they have managed two or more corporations in the previous seven years at the time they failed and the liquidator has lodged reports under section 533 on the corporation's inability to pay unsecured creditors (section 206F).¹⁰

⁹ Includes the Federal Court, the Supreme Court of the state or territory, the Family Court or any other court appointed under proclamation.

¹⁰ Under section 533(1) a liquidator must lodge a report with ASIC if it appears that an officer has been guilty of an offence, a person involved in the company's management has been negligent or breached a duty to the company, or the company may be unable to pay its unsecured creditors more than 50 cents in the dollar. (Joint Committee 2004, p. 138)

Only ASIC can make an application under section 206. Many of the submissions to the Joint Committee that reviewed corporate insolvency laws were critical of the level of enforcement and the powers under the existing legislation (Joint Committee 2004, pp. 142–143, 145 and 148). The Committee made six recommendations to improve the effectiveness of action against people that deliberately abuse the corporate form (Box 7).

Box 7: Joint Committee recommendations

Recommendation 31

While recognising the need to foster risk-taking and entrepreneurship, the Joint Committee concluded that the legislative hurdles, under sections 206D and 206F, to taking action against reckless and dishonest directors were too high. Under section 206F, ASIC can only take action if the liquidator lodges a section 533 report. As a fraudulent phoenix company has few assets, creditors often choose to avoid the cost of appointing a liquidator. Therefore, regardless of the actions of the directors, the preconditions for section 206F would not be met.

The Committee recommends that ss 206D and 206F should not be subject to a requirement to have managed two or more failed corporations. They should permit a court, or ASIC in its discretion, to disqualify a person from being a director where essentially two conditions are met: the person is or has been a director of a company which has failed (as defined in s 206D(2)) and the person, as a director of the company (either taken alone or taken together with his/her conduct as a director of any other company) makes him or her unfit to be concerned in the management of a company.

Recommendation 32

To help identify companies engaged in phoenix activity the Committee considered ways to improve cross-checking of business names on State Business Names Registries with the ASCOT database of company names and ACNs.

The Committee recommends that the Government in association with the Council of Australian Governments review the adequacy of the arrangements for the checking of the business names of companies on State Business Names Registries against the ASCOT database of company names and ACNs.

Currently, information from the state business names register is automatically uploaded onto ASIC's database.

Recommendation 33

The Committee supported the earlier recommendation of the Victorian Law Reform Committee to 'enable the courts to freeze assets of a director or manager which are *prima facie* assets on which the corporation has a just claim' (Law Reform Committee 1994, p. xvii), to preserve those assets when there is a risk of fraudulent phoenix activity.

The Committee recommends that the Government consider the proposal to create a statutory process analogous to a Mareva injunction to enable the courts to freeze assets of a director or manager which are prima facie assets on which the corporation has a just claim.

Recommendation 34

The Committee argued that the procedures for establishing a company should be tightened.

The Committee recommends that the Government review the processes in place for registering a company with a view to improving the measures for determining the bona fides of those applying to register a company.

Recommendation 35

It concluded that ASIC could improve its processes for receiving intelligence on potential phoenix operators from groups like trade unions.

The Committee recommends that ASIC consider establishing a hot-line and guidelines for its operation in conjunction with strategically located employees for the purpose of facilitating possible early detection of, and intervention to prevent the implementation of, illicit phoenix activities.

Recommendation 36

A significant question is the extent to which members of a corporate group should be jointly liable for the debts of others in the group. The Committee concluded that the Government should consider this issue further.

The Committee recommends that the insolvency related implications and recommendations of the Companies and Securities Advisory Committee's Report on Corporate Groups should be examined by the Government and its response made available to the Committee as soon as possible.

Source: Joint Committee 2004, *Corporate Insolvency Laws: A stocktake*

6.2 Trade Practices Act

In response to this and other reports on corporate insolvency, the Australian Government released an exposure draft of the Corporations Amendment (Insolvency) Bill in November 2006 (the Treasury 2006, p. 1). Addressing the issues identified by the Joint Committee would strengthen ASIC's powers to act against fraudulent phoenix activity. These recommendations, however, still require ASIC to give priority to identifying and pursuing the directors of these companies.

The Joint Committee also recognised the need for co-operation between ASIC and state and territory governments, particularly agencies involved in revenue collection.

It is desirable for State and Commonwealth Government agencies who have responsibility for the collection of revenue or levies and ASIC to consult on their respective interests, concerns and responsibilities in responding to phoenix company activities and coordinate their efforts including exchanging information. (Joint Committee 2004, pp. 145–146)

ASIC has not actively pursued remedies under section 206. In 2004, members of the Fair Trading Officers Advisory Committee recommended to the Standing Committee of Consumer Affairs Officers that the Corporations Act be amended to enable the Directors of Consumer Affairs/Fair Trading to have standing to apply for the relief under section 206C in appropriate circumstances. Victoria continues to support these proposed amendments.

While the provisions in the Trade Practices Act are similar to the Victorian Fair Trading Act, the remedies under the Trade Practices Act have national (and extraterritorial) application, subject to constitutional limitations. There may be advantages, in some cases, in prosecuting rogues under the Trade Practices Act, rather than state legislation. It is easier to enforce a court order in another state, for example, if it was made under national legislation, than if it was made under Victorian legislation by a Victorian court (even with the extraterritorial application of the Fair Trading Act).

The Trade Practices Act enables the Commonwealth Minister for Consumer Affairs, the Australian Competition and Consumer Commission (ACCC) or any person to apply for injunctive relief (section 80). 'Any person' would include the Victorian Minister for Consumer Affairs or the Director of Consumer Affairs Victoria. Unlike the Commonwealth Minister or the ACCC, however, the Victorian Minister or the Director would have to give an undertaking as to damages if they made a section 80 application (section 80(6)). Such an undertaking is not required when the Director makes an application under Victorian legislation. Section 86C provides for additional remedies and only the Commonwealth Minister or the ACCC can make an application under section 86C.

As with the proposed amendments to the Corporations Act, Victoria supports the Fair Trading Officers Advisory Committee proposal to amend the Trade Practices Act to protect state and territory fair trading and consumer protection agencies against the requirement to give an undertaking as to damages when they seek to access relief under section 80 of the Act.

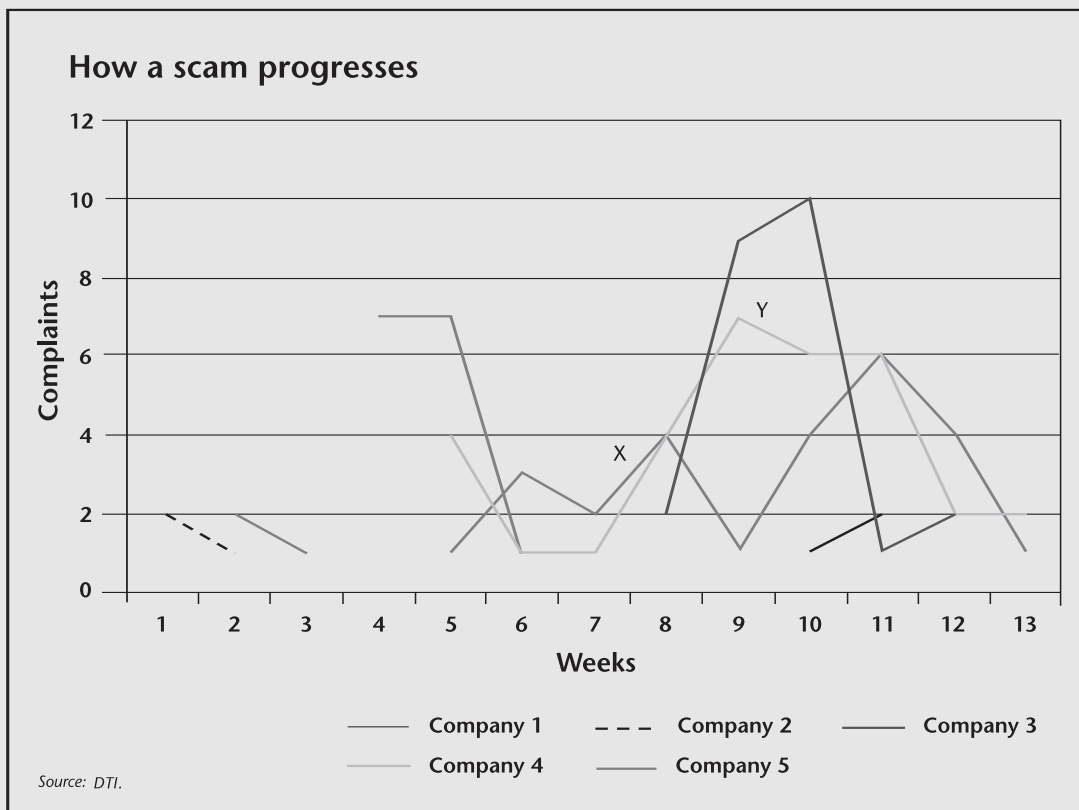
“ Coordinated action ”

7

Coordination prevents problems being experienced in several jurisdictions if traders move, and increases the range and effectiveness of enforcement tools. It helps to detect problems more quickly and solve them more effectively. Experience with a telephone scam in the United Kingdom (Box 8) illustrates the effects of lack of coordination.

Box 8: Detection of a UK telephone scam

Chart 4.1 shows the progress of complaints about a widespread scam uncovered by the UK Department of Trade and Industry. The telephone scam was instigated by a company trading under several names. Since the complaints were thinly spread across the country, individual authorities did not pick up on the problem and a simple analysis of the data at week seven (marked X) would have suggested the problem was decreasing. In fact, it was intensifying – diversifying into different company names. Only after nine weeks (marked Y) did a local authority realise that it was a national problem.



Source: Hampton, P 2005, *Reducing Administrative Burdens: Effective inspection and enforcement*, pp. 72–73

Similarly, in Australia in 1997 the Victorian Government regulated introduction agents because ‘a small but significant number of introduction agents have engaged in widespread and ongoing unfair conduct resulting in both economic loss and emotional disturbance for many, and in particular, vulnerable consumers in this state’(Wade 1997, p. 1631). The Act introduced licensing of introduction agents and placed requirements on their location, employees, behaviour, advertising and the collection and use of information. It also regulated agreements with clients and the information that must be provided to clients.

The legislation successfully removed rogue operators from the Victorian industry. Because of a lack of coordination action between jurisdictions, however, the traders, who were of most concern in Victoria, moved to Queensland. The Queensland Parliament recognised this when it introduced its own regulation for introduction agents in 2001.

After Victoria legislated to license introduction agents in 1997 many Victorian agencies moved to Queensland to avoid the Victorian regime. It is probable, then, that some of these same agencies will again relocate to a state in which they are unregulated. So I will be continuing to warn my interstate colleagues and commending this legislation to them. (Rose 2001, p. 2477)

Overall, the benefits of coordination between jurisdictions include:

- overcoming legal and logistical difficulties that one agency may encounter when attempting to prosecute a rogue that is operating across jurisdictions
- reducing duplication of activity between agencies, increasing their combined capacity to target rogues
- allowing agencies to call on the knowledge, intelligence and expertise of others, making enforcement more effective
- reducing the risk that rogues can avoid compliance by shifting their activities to another state or territory, and
- sending clear messages to traders that a national, consistent and effective approach to enforcement will be taken across the country.

These benefits were recognised in Australia when jurisdictions signed the 2004 Joint Consumer Protection Agreement and commenced developing protocols for national cooperation in the enforcement of consumer legislation. The agreement is ‘an important blueprint forward for national cooperation in enforcement and prosecution against traders who break the law’ (CAV 2004b, p. 1). States and territories have agreed to work together in areas like property investment advice, scam mail and product safety, and to take compliance action that benefits all Australian consumers, not just those in the jurisdiction leading the prosecution. The Auzshare system also facilitates information sharing among consumer agencies (Box 9).

Box 9: Auzshare

Auzshare is a new national fair trading notifications system. A database has been created to combat fraudulent practices against consumers by improving information sharing between participating agencies concerned with consumer protection in Australia. The database is available to all offices of fair trading across Australia as well as the ACCC. It allows these agencies to post alerts and complaints of a more serious nature in real time. These government agencies can use this information to investigate suspect companies and individuals, uncover new scams and spot trends in fraud.

This information will improve the use of resources, as agencies previously had to contact each other individually to obtain the required complaint information. It will also lead to more effective law enforcement by facilitating early warnings on emerging trends, quicker identification and allow for a coordinated response to unlawful activities by traders.

Source: ACCC 2005b, *Auzshare*, p. 1

In Victoria rogue traders not only concern consumer affairs agencies, but also other agencies with responsibilities in industries where rogues operate, those responsible for revenue collection (given rogues often avoid taxes and fees) and the police. Other agencies may also administer regulation that could be used to prosecute rogue traders. Consumer Affairs Victoria needs to cooperate with these agencies if their legislation is the best vehicle for targeting the rogue. Rogues also operate internationally and there is considerable uncertainty about international law enforcement.

Effective redress depends on both legal rights and mechanisms through which to obtain redress. To date, there is significant international uncertainty about which court has jurisdiction to hear a cross-border dispute and which country's law will govern the resolution of a dispute. (CAV 2004c, p. 25)

Even in the European Union, where inter-country relations are comparatively close, the ability of rogue traders to target regulatory gaps between countries is recognised. The European Commission is actively trying to address this problem.

The European Commission adopted today a proposal for a Directive on unfair business-to-consumer commercial practices ... which establishes a single, common, general prohibition of unfair commercial practices distorting consumers' economic behaviour. This single set of common rules will replace the existing multiple volumes of national rules and court rulings on commercial practices. This will give consumers the same protection against sharp business practices and rogue traders whether they buy from the shop around the corner or from a website in another Member State. (EU 2003, p. 1)

The OECD also recommended that:

Member countries should develop mechanisms for co-operation and information sharing between and among their own consumer protection enforcement agencies and their other law enforcement authorities, for the purpose of combating fraudulent and deceptive commercial practices.

Member countries should review their own domestic frameworks to identify obstacles to effective cross-border co-operation in the enforcement of laws designed to protect consumers against fraudulent and deceptive commercial practices, and should consider changing domestic frameworks, including, if appropriate, adopting or amending national legislation to overcome these barriers. (OECD 2003, p. 12)

Strategies that assist coordination and cooperation could include:

- Consistent approaches to regulation to minimise gaps and overlap – Australia's general consumer legislation is largely consistent, with a few key differences. Industry specific legislation is more diverse. Governments could assess the impact of these differences in priority areas and consider whether greater consistency is possible and desirable.

- Information sharing – Auzshare (box 9) and the new Australian Consumer Fraud Prevention Taskforce, for example. The taskforce comprises 18 government regulatory agencies and departments involved in protecting consumers against fraud and scams. These agencies work together to enhance enforcement, coordinate information campaigns, share information and generate greater interest in research on consumer fraud and scams.
- Regulators' forums – Regular meetings between regulators can encourage information exchange and identify joint priorities. The Ministerial Council on Consumer Affairs and the Standing Committee of Officials of Consumer Affairs are active at the national level. Victoria has a state regulators' forum that meets regularly to discuss priority state issues.
- Enforcement protocols – Jurisdictions have signed a Joint Consumer Protection Agreement and there are memoranda of understanding between some Victorian agencies. The Liquor Licensing Authority and Victorian Police have a memorandum of understanding to coordinate their roles in securing compliance with, and enforcing, liquor regulation.

Cooperative strategies are important internationally, interstate and intrastate. While there are initiatives at all these levels, effective cooperation is hard to achieve. It is hindered by the difficulties of maintaining open communication, reconciling priorities among agencies, identifying the key people across agencies and developing practical and effective processes and protocols. More work and ongoing monitoring is needed to improve the effectiveness of existing strategies and target areas where additional strategies are needed. In particular, Consumer Affairs Victoria could play a greater role in combating fraud by rogue traders if it had closer partnerships with local government and the Victorian Police.

While Victoria uses a range of mechanisms to deal with rogue traders, there are tools used overseas and in other policy contexts in Australia that could inform further development of Victoria’s strategies. Innovative approaches often involve improved intelligence to identify rogues and faster responses by the regulator. Some examples are discussed below.

8.1 Disruption techniques

Disruption techniques create barriers to contact between rogue traders and potential victims. For example, seizure and destruction of scam mail is used to intercept scams before they reach Australian consumers. In June 2005, 160,000 letters were seized and destroyed as part of a ‘coordinated national sweep by Australia Post, Consumer Affairs Victoria and other consumer agencies’. (CAV 2005b, p. 2) These were illegal ‘get rich quick’ chain letters that were part of a major pyramid selling scam.

The United Kingdom considered disruption techniques to combat rogue traders selling property repairs door-to-door, particularly in areas where many of the residents were older and vulnerable people. They looked at banning cold calling for property maintenance and repairs, but instead used community based information campaigns to discourage cold callers, including stickers that tell doorstep sellers they are unwelcome. This solution reflected the balance needed between combating rogues effectively and other objectives, such as maintaining strong competition and treating legitimate traders fairly.

A cold calling ban would have clear advantages for enforcement (eg in not requiring complex evidence of intent). But we recognise the difficulties and issues associated with legislating for a ban, including:

- *justifying a criminal offence that would catch activity that was not harmful along with the harmful*
- *how to avoid harm to legitimate business or potentially creating barriers to entry*
- *considering whether there was sufficient justification for making the offence arrestable, or for including prison among the available penalties: but if not, whether the ban would provide the improvement looked for in enforcement and deterrence*
- *how cold calling should be defined, and what would constitute prior arrangement*
- *what the scope of property maintenance/repair should be*
- *whether a ban might, at some point in the future, be in conflict with whatever emerges from negotiations on an Unfair Commercial Practices Directive.*

Some (though not all) of these difficulties might be addressed by alternatives that could be considered in a consultation exercise (eg coverage, exemptions etc.). It is at present unclear whether the balance of advantages and disadvantages argues for a ban on cold calling for property maintenance/repairs. (OFT 2004c, p. 5)

8.2 Rapid response strategies

A key problem in combating rogue traders is their speed and mobility, that is, their ability to cause damage and move on before the regulator can react. Trading Standards in the United Kingdom introduced the 'Doorstoppers' campaign to combat this problem. The campaign involves consumer information and education combined with rapid response teams. These teams are on standby to go to people's homes while workmen are still on site. The program is implemented on a regional basis. For example in West Yorkshire:

Trading Standards Service have introduced a number of measures to combat doorstep crime. One of the most effective has been the rapid response protocol. The aim is to despatch Trading Standards Officers to a consumer's home whilst the trader is still on site. The trader's work is examined and a fair price is negotiated. If the work is found to be fraudulent then the trader is informed that they will not receive payment. If the trader objects, they are advised how to pursue the matter through the small claims procedure – an option, they are unlikely to follow! At present officers have attended over 100 responses and been able to save vulnerable consumers approximately £35,000. (West Yorkshire Trading Standards Service 2003/04, p. 6)

If the trader has left but is due to return, officers can be available at the consumer's house at the time the trader is expected.

8.3 Raising awareness

Awareness campaigns usually focus on increasing consumers' knowledge of their rights and the identity and activities of rogue traders. This is not the only important issue. Government agencies' awareness of the problem of rogue activity and traders' awareness of enforcement action against rogues also need to be raised.

Consumer agencies can improve their effectiveness if other agencies know how rogue traders operate, how consumer issues relate to their interests and the role of consumer laws and consumer agencies. Such awareness improves intelligence gathering and interagency coordination.

In addition, rogues can be deterred by creating a business environment that discourages rogue behaviour. Such an environment depends on traders seeing rogue behaviour as unacceptable, discouraging traders (such as those in financial difficulty) from resorting to rogue tactics to solve their problems and encouraging honest traders to report rogues. One useful strategy is to raise the regulatory agency's profile and its successful enforcement activities. Activities might include:

- blitzes or high profile campaigns against problematic rogue activities
- publicising successful prosecutions (this can impact trader behaviour in similar industries as well)
- creating closer links with business organisations
- using industry organisations to advocate the benefits of ethical trading
- liaising with suppliers of material, such as paint and building products, which may supply industries where rogue traders are active
- creating closer local links with agencies such as local government and local police, and
- incorporating rogue trader issues into general communication with traders, such as seminars or conferences.

8.4 Intelligence gathering

A critical issue for any effective strategy against rogue traders is good intelligence. The difficulties in identifying rogue traders and collecting data on their activities is discussed in sections 2 and 3. Despite these difficulties the need to improve intelligence gathering is recognised worldwide and many innovative solutions are being considered.

- The Australian Communications and Media Authority is implementing a new spam reporting tool. SpamMatters is a plug-in to Microsoft Outlook and allows users to quickly and easily forward spam emails to the Authority.

Customers can use the software to forward spam they have received directly to the ACA's [now part of the Australian Communications and Media Authority] forensics database system for collection, research, analysis and action.

The system also automatically extracts relevant information from the spam that may help the ACA to track down spammers. This information can be used as evidence in court because the database also saves the spam message with the header and body intact.

The database system reduces the need for manual spam investigations and is able to process and analyse very large amounts of spam. (ACA 2005)

- The British Bankers' Association, the Building Societies Association and the Trading Standards Institute signed a protocol that gives bank and building society staff guidelines to follow if they spot an older or vulnerable person trying to withdraw unusually large sums of cash.
Counter staff are urged to be vigilant and step in to help people they suspect may be on the brink of falling victim to a doorstep con and contact Trading Standards or the police for back up if necessary. (BBA 2004, p. 1)
- Police in Lincolnshire in the United Kingdom are collecting information on bogus traders as part of a project collating and distributing data on distraction burglary. (OFT 2004a, p. 101)
- In 2003 the United States Federal Trade Commission conducted a national survey on identity theft. The survey allowed it to identify the nature and extent of the problem. (FTC 2003, p. 1)
- In 2004 the United States Federal Trade Commission considered but rejected, using financial rewards to encourage citizens to track, identify and report spammers. (FTC 2004, p. 1)

“Choosing policy approaches”

9

In choosing policy approaches to deal with rogue traders three key issues should be recognised:

1. rogues form a minority in nearly all industries; in some industries there may be only a few rogue traders
2. regulation targeting rogues could affect the behaviour of ethical businesses, and
3. there is no single strategy that can combat rogue traders, rather a combination of strategies is necessary.

9.1 Regulatory costs for consumers and ethical traders

It is well recognised that regulation is needed to combat the activities of rogue traders. Honesty is both expected by the community as a basic standard of behaviour and necessary to ensure that markets work effectively.

Competition may not always be enough to protect even the reasonably careful purchaser from dishonest or unduly careless sales practices ... we recognise a problem of 'market failure', such that the normal competitive processes need to be supplemented by legislative intervention to penalise the dishonest and unduly careless firm. (Victorian Consumer Affairs Council 1983, p. 49)

The regulation chosen is important, however. General consumer regulation usually specifies inappropriate behaviour, such as the use of unfair contract terms, false and misleading advertising or unconscionable conduct. Such provisions have few costs for ethical businesses. Other regulation is more prescriptive, it may require disclosing information, obtaining a licence, keeping records or obtaining certain qualifications. Such regulation can impose costs on all businesses, not just rogues. In some situations, ethical businesses may be at a greater disadvantage because they comply with the regulation and compete with rogues that avoid compliance. Debate about motor trader regulation in Victoria recognised these issues and the need to balance controlling rogue traders with the impact on small business (Lenders 2004, p. 1788).

The cost to business of complying with regulation is passed on to consumers. While consumers benefit from regulation that decreases the activities of rogue traders, they will be disadvantaged by regulation that raises the costs of the products or services they buy, or reduces their choice of products or services. Care is needed to ensure that the obvious costs to consumers caused by rogue traders are not removed only to be replaced by less obvious costs, the costs of regulation. Regulatory approaches that directly target the problematic behaviours of rogues, without affecting other traders, are most likely to reduce the rogue trader problem without generating unintended costs or impacts on consumers or businesses.

9.2 The effect of regulation on trader behaviour

The type of regulation chosen can discourage ethical traders from self regulating their behaviour. Braithwaite noted that some commentators argue that you should regulate for the worst case scenario because 'one case of knavery can have such disastrous consequences' (Braithwaite 1993, p. 84). He suggested, however, that regulators should:

take seriously the need to nurture business virtue ... without being so naïve as to believe that we will accomplish something by waving ethics texts in front of the glazed eyes of the most gruesome corporate criminals. (Braithwaite 1993, p. 84)

He argued that institutions that assume traders are not virtuous destroy virtue and encourage dishonest behaviour. He illustrated this using the example in Box 10.

Box 10: The effect of regulation on traders' incentives to behave ethically

The trouble with institutions which assume that people or firms or corporate subcultures will not be virtuous is that they destroy virtue. Some agencies that regulate business, particularly American agencies, tend to do just this. I have observed the tragic little drama of virtue being destroyed many times during my empirical research on business regulation. The government inspector marches into a workplace and starts making threats; citations are written; most critically, both the demeanour of the inspector and the policy that stands behind that demeanour communicate the expectation that the manager on the receiving end of the encounter is untrustworthy. The regulator communicates the assumption that it is only compulsion, or only the bottom line, that will move the manager to submit to the policy of the law. But this assumption is often wrong. The safety manager may deeply care about the safety of her workers, and she resents, bitterly resents, being treated as if she does not care. This resentment can destroy her good faith, her willingness to go an extra mile beyond what the inspector asks her to do. Common sense and a wealth of experimental psychological research instruct us that when human beings are compelled to do something their commitment to doing it erodes. More precisely, commitment erodes in comparison with a situation where they voluntarily choose to do that thing because they are persuaded that it is the right thing to do.

Source: Braithwaite 1993, 'Responsible Business Regulatory Institutions', in *Business Ethics and the Law* Coady, CAJ and Sampford, CJG (eds), p. 85

Therefore, regulation that is highly intrusive and prescriptive can reduce the incentives for business to act ethically. A more flexible regulatory environment backed by strong powers to deal with rogues may be more effective. Such an approach also frees government resources to deal with rogues as it reduces the need to regulate ethical businesses.

9.3 Combining regulatory strategies

By their nature, rogue traders target loopholes in regulation and enforcement activities to avoid detection and prosecution. A suite of strategies is needed to address the problem from several angles simultaneously. The challenge is to choose a package of strategies that is effective and has benefits that outweigh its costs. The policy tools discussed in sections 5 to 8 can target different aspects of the rogue trader problem. Because it is virtually impossible to get a comprehensive database on rogue traders a two-pronged approach is needed:

1. increasing the market's resilience against rogues, and
2. identifying rogues and targeting action against them.

Resilient markets reduce the incentives for rogues to set up and the amount of money they can extract. Policies that increase market resilience could include:

- building consumer confidence so consumers are more likely to stand up for their rights
- informing consumers about rogues and their activities so consumers can avoid rogue traders and more readily identify and avoid scams, and
- informing traders so that industry cultures are hostile to rogues and their activities, and businesses are more likely to inform consumer agencies about rogues and their activities.

As it is not possible to eliminate rogue traders other policies are also needed to identify rogues and act quickly. Quick identification minimises damage and reduces the rogue's ability to avoid prosecution. It often requires coordinating the activities of different agencies and levels of government.

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