



AN BILLE UM STUAIC-SCÉIMEANNA 2006 PYRAMID SCHEMES BILL 2006

EXPLANATORY MEMORANDUM

Purpose of Bill

In a scam that is from time to time resurrected, people pay to join what may be described as a “gifting club”, an “empowering network” or some other form of private club or network, with members eager to help new friends.

How does it work? There are various versions but the basic mechanism is as follows. Club promoters pitch the groups as win—win opportunities for participants to help each other achieve financial security or overcome money troubles. All you have to do is join the bottom tier of the club by paying or “gifting” an agreed amount of money to the network. Individuals on higher tiers collect some or all of the cash of the new participants and then they supposedly drop out once the “gifts” to them total a set amount.

This allows people in the tier below to move up. If you are a new member, you recruit your friends and relatives to join the club in a tier below you, and the process continues until you’re at the top tier and collect “gifts” amounting to a much greater sum than you paid to join the club. Your friends and neighbours will reap the same reward in turn. It sounds so easy.

In reality, the clubs are pyramid schemes. And the problem is that, like any pyramid scheme, gifting clubs must continually recruit ever-increasing numbers of members to survive. In order for members to make a return on their initial investment, an exponential rate of growth in the recruitment of new members is essential. It is a rate of growth very quickly proves to be unsustainable.

But won’t the pyramid succeed as long as new people keep joining? In reality, that’s just not possible. Take, for example, a pyramid where participants pay in €10,000 and withdraw when they’ve collected €80,000. They may be asked to introduce only two new members but, of course, for each member to withdraw with his or her €80,000, eight new members must join in the tiers below. For each of those eight members to move up to a point where they can withdraw, there must be eight more members, and so forth. The pyramid has to grow at a rate that would, from the initial recruitment of just eight members, very quickly exceed the adult population of Ireland.

$$\begin{aligned}
&1 \\
&1 \times 8 = 8 \\
&8 \times 8 = 64 \\
&64 \times 8 = 512 \\
&512 \times 8 = 4,096 \\
&4,096 \times 8 = 32,768 \\
&32,768 \times 8 = 262,144 \\
&262,144 \times 8 = 2,097,152
\end{aligned}$$

And, if you add just four more tiers, you will have exceeded the population of the entire world.

The fundamental issue, therefore, is that pyramid schemes are mathematically certain to fail. They require a constant supply of new participants to funnel money up through the pyramid. When there are no more willing recruits, the pyramid collapses. Most members who paid to join the clubs — the most recently recruited members who are still in the lower tiers — will never receive the financial return they expected and will lose everything they paid on joining.

To make matters worse, the pyramid's reliance on personal relationships to recruit new members means that, not only will participants lose their money, they will drag friends and relatives into the same mess.

Furthermore, no matter what the promotional literature may say, if you put money into such a scheme with the understanding that you will — or even that you may — get money back at a future date, it is not a gift or a charitable donation. It is an investment, regardless of your motives or what you plan to do with the money, and capital gains tax may be payable on any return.

The reality is that any deal that sounds too good to be true almost certainly is too good to be true. Like getting €80,000 back on a €10,000 investment, for little effort on your part, from an organisation that offers no actual product or service.

These schemes are not prohibited under the Pyramid Selling Act 1980, which confined itself to outlawing “trading schemes”, that is, schemes under which goods or services are supplied under transactions effected by the participants. The purpose of this Bill is to outlaw non-trading pyramid schemes.

Provisions of Bill

Section 1 sets out definitions of certain terms used in the Bill. In particular, a “scheme” is defined as meaning any scheme or arrangement (whether it is held out as conferring on participants a legally enforceable right or not but not being a scheme within the meaning of the Pyramid Selling Act 1980) for the organisation or bringing together of a group of persons under a plan or device involving the following elements:—

- there is provision for a payment being made by a new participant, to the promoter or to an existing participant, in respect of his or her admission to the scheme;
- there is provision for an increase in the number of participants through a chain process, whereby an existing participant invites two or more other persons to participate in the scheme;

- the prospect is held out that a participant, by securing the introduction and admission of additional participants, may receive payments (whether such payments are described as gifts or as a matter of legal entitlement) which exceed in aggregate the amount of the payment made by him or her in respect of admission to the scheme; and
- the terms of the scheme do not hold out any reasonable prospect of payments, goods, services or other benefit being made to participants, the amount of the aggregate value of which is or would be greater than or equal to the amount of the payments made by them on their admission to the scheme, other than the prospect of receiving payments in respect of the admission of new participants.

Section 2 provides for offences in relation to such schemes. *Subsection (1)* states that a promoter of, or a participant in, a scheme who, by holding out to any person the prospect of receiving payments in respect of the introduction of other persons as participants in the scheme, induces or attempts to induce him or her to become a participant or to make any payment, is guilty of an offence.

By *subsection (2)*, if any person who is a participant in a scheme, or has applied or been invited to become a participant in a scheme makes any payment to the promoter of, or a participant in, the scheme, having been induced to make that payment by reason that the prospect is held out to him or her of receiving payments in respect of the introduction of other persons who become participants in the scheme, the person to whom that payment is made is guilty of an offence.

Subsection (3) provides that, in determining, for the purposes of *subsection (1)* or *subsection (2)*, whether an inducement is made by holding out such a prospect as is therein mentioned, it is sufficient if such a prospect constitutes or would constitute a substantial part of the inducement.

By *subsection (4)*, where the person by whom an offence is committed under *subsection (1)* or *subsection (2)* is not the promoter or the sole promoter of the scheme in question, any other person who is the promoter or (as the case may be) one of the promoters of the scheme is also guilty of that offence.

Section 3 provides that an agreement for the making of a payment in respect of becoming a participant in a scheme is null and void and of no effect. A payment made under such an agreement may be recovered as a simple contract debt in any court of competent jurisdiction.

Section 4 provides for penalties in relation to offences under the Bill. On summary conviction, a person shall be liable to a fine not exceeding €3,000 or to imprisonment for a term not exceeding 12 months or both. On conviction on indictment, no limit is provided in respect of the fine that may be imposed; the maximum term of imprisonment is specified at 5 years.

Subsection (2) enables a court, on conviction, to order that the fine imposed be paid as compensation in respect of loss to any witness on behalf of the prosecution in the proceedings who suffered personal loss resulting, wholly or partly, from the offence.

Section 5 provides for liability on the part of directors and other officers of a corporate body where an offence is committed by that corporation.

Section 6 provides for the short title of the Bill.

Caitlín Uí Loinsigh
Aibreán, 2006