



Model framework for guidelines on direct selling

Background

One of the biggest challenge for the Indian Direct Selling (DS) industry is a lack of express regulatory framework. As a result, often DS companies are compared to pyramid schemes under the Prize, Chits and Money Circulation Schemes (Banning) Act, 1978 (PCMCS). PCMCS, which was enacted much before the advent of a bona fide DS industry in India, is archaic and does not distinguish between rightful DS businesses from malicious DS schemes. States like Andhra Pradesh, Kerala, Sikkim, etc. and Union Territories like Chandigarh, on multiple occasions have taken misguided penal action against legitimate DS companies, and this has stunted the growth of the DS industry in India.

Apart from the ambiguity in PCMCS, there are many other regulatory issues including lack of definition of DS and separate regulatory provisions for the industry.

In the wake of the above challenges and pursuant to extensive interactions with the DS industry, recently, the Union Ministry of Consumer Affairs, Food and Public Distribution issued a Model Framework for Guidelines on DS¹ (Direct Selling Guidelines 2016 or Model Guidelines) for respective state government(s) [as retail trade is a state subject under the Constitution of India] to take necessary actions for implementation of the same.

The Direct Selling Guidelines 2016 (DSG) have been issued as guiding principles for state government(s) to consider regulating the businesses of DS and Multi-Level Marketing (MLM) and strengthen the existing regulatory mechanism on DS and MLM, for preventing fraud and protecting the legitimate rights and interest of consumers.

¹ Press release dated 12 September 2016-
<http://pib.nic.in/newsite/PrintRelease.aspx?relid=149728>

Key highlights of the DSG

Introduction of definitions

The DSG have defined certain key terms summarised as below:

- **Consumer:** shall have same meaning as defined under the Consumer Protection Act, 1986;
- **Direct selling:** means marketing, distribution, and sale of goods or providing of services as a part of network of direct selling other than under a pyramid scheme;
- **Direct seller:** means a person appointed or authorised, directly or indirectly, by a DS entity through a legally enforceable written contract to undertake DS business on a principal to principal basis;
- **Direct selling entity:** means an entity, not being engaged in a pyramid scheme, which sells or offers goods or services through a direct seller.
- **Network of direct selling:** means a network of direct sellers at different levels of distribution, who may recruit or introduce or sponsor further levels of direct sellers, who they then support. Network of direct sellers has been further defined to mean any system of distribution or marketing adopted by a DS entity to undertake DS business and shall include the MLM method of distribution.

- Cooling-off period: means the duration of time counted from the date when the direct seller and DS entity enter into an agreement as per these guidelines and ending with a date on which the contract is to be performed and within which the direct seller may repudiate the agreement without being subject to a penalty for breach of contract.

Distinct definition of pyramid scheme: Demarcated from money circulation schemes

The DSG has specifically defined the term pyramid schemes to create a distinction between the business of DS and a money circulation scheme.

In principle, a pyramid scheme has been defined to mean a multi-layered network of subscribers to a scheme formed by subscribers enrolling one or more subscribers in order to receive benefits, directly or indirectly, as a result of enrolment, action or performance of additional subscribers to the scheme.

Further, by way of a specific exclusion, it has been provided that the said definition of a pyramid scheme shall not apply to a multi layered network of subscribers to a scheme formed by DS entity, where the benefit is as a result of sale of goods/services by subscribers and such scheme/financial arrangement complies with all of the following conditions:

- a) No provision for payment of remuneration/ incentives for recruitment/enrolment of new participants;
- b) It does not require a participant to purchase goods/services (i) for an amount that exceeds an amount for which such goods/services can be expected to be sold/resold to consumers; (ii) for a quantity of goods/services that exceeds an amount that can be expected to be consumed by or sold/ resold to consumers;
- c) No entry/registration fee, cost of sales demonstration equipment/materials or other fee relating to participation;
- d) A written contract to describe the material terms (provisions relating to buy-back/ repurchase policy, cooling- off period, warranty and refund policy of participation);

- e) Provision for a reasonable cooling-off period and refund of any consideration given to participate in the scheme in case the participant cancels the participation in the scheme;
- f) Provision for buy-back/repurchase policy for 'currently marketable' goods/services sold at the request of the participant;
- g) Establishment of a grievance redressal mechanism for consumers.

Guidelines for setting up and conduct of DS business

- **Conditions for the setting up of DS business:** Every DS entity shall be required to submit an undertaking to the Department of Consumer Affairs within 90 days of publication of this Notification in the Gazette, stating that it is in compliance with the stipulations provided in the DSG and shall also provide details of its incorporation. The key conditions to be complied with are as under:
 1. DS entity to be registered as legal entity under the laws of India;
 2. Conduct a mandatory orientation session for all prospective direct sellers providing fair and accurate information on all aspects of DS operations viz. information about remuneration opportunity, related rights/obligations, etc.;
 3. Pay all dues and make withholdings from direct sellers in a commercially reasonable manner;
 4. Provisions for a full refund or buy-back guarantee to every direct seller on reasonable commercial terms within a 30 days window;
 5. Provision of a cooling-off period which entitles return of any goods/services purchased during the cooling off period;
 6. Promoter or key management personnel should not have been convicted of any criminal offence punishable with imprisonment in the last five years;

7. A dedicated office with an identified jurisdiction of its operations in the state to enable easy accessibility to the consumers and direct sellers.
- **Conditions for conducting DS business:** The following are certain key conditions which have to be adhered to by a DS entity in conduct of its DS activities:
 1. Be the owner, holder, licensee of a trademark, service mark, or any other identification mark which identifies the entity with the goods to be sold/supplied or services to be rendered;
 2. Issue proper identity document(s) to its direct sellers;
 3. Maintain proper records (either manual or electronic) of its complete business dealings and a 'register of direct sellers' with relevant details (PAN, proof of identity, proof of address, etc.) of each enrolled direct seller;
 4. Maintain a proper and updated website with all relevant details of the entity, contact information, its management, products, etc. and it should have dedicated space for registration of consumer complaints (to be addressed within 45 days of making such complaints);
 5. Monitor value of the purchases of all its direct sellers on a monthly basis to identify the purchase value meeting the VAT threshold, thereby, intimating the direct seller to pay VAT;
 6. Refrain from *inter-alia* using misleading, deceptive or unfair recruiting practices, including misrepresentation of actual or potential sales or earnings, in their interaction with prospective or existing direct sellers, etc.;
 7. The DS entity shall be responsible for compliance with these guidelines by any member of its network, whether appointed directly or indirectly by such DS entity.
 - **The mandatory legally enforceable contract between direct seller/distributor and DS entity:** Every DS entity would be required to execute a written contract agreement, whether directly or indirectly, with the direct sellers prior to the enrolment describing the material terms of participation. Such contract agreement would be governed by the provisions of the Indian Contract Act, 1982. The relationship between the DS entity and direct seller to be determined as per the express written agreement between the parties.
 - **Obligations of direct sellers:** Certain behavioural norms have also been enlisted in the DSG for direct sellers which, *inter alia*, include providing true and fair information about goods and/or services to a prospective consumer, not indulging in unfair trade practices, carrying identity card at time of sale, maintenance of proper books of accounts as required under applicable laws, etc.
 - **Conduct for the protection of consumer:** Direct sellers and DS entity shall be guided by the provisions of the Consumer Protection Act, 1986. All complaints shall have to be dealt with in a systematic manner for timely redressal. Every DS entity shall constitute a Grievance Redressal Committee in accordance with the DSG.
 - **Appointment of monitoring authority:** Department of Consumer Affairs at the Union Level and the respective state government(s) in the state(s) have been appointed as the nodal department to deal with issues on DS. The state government(s) have also been directed to set up a mechanism to monitor/supervise the activities of direct sellers, DS entity regarding compliance with the guidelines for DS business.

Our comments

The introduction of DSG is a welcome move especially in times when the industry is reeling under double jeopardy – an erosion of faith and an identity crisis.

The genesis of regulatory problems for the DS industry in India has itself arisen from consumer grievances and alleged fraudulent schemes which lure individuals to invest their hard-earned earnings into such schemes. Therefore, recognition of the Department of Consumer Affairs as the Nodal Ministry at the central level and substantive reference to the Consumer Protection Act, 1986 in the DSG (for redressal of consumer grievances) is a positive step for regaining consumer confidence.

Further, a separate but uniform policy framework for the DS business in every state could help clear the blurred lines between the bona fide industry players and fraudulent pyramid schemes resulting in the creation of a conducive environment for the industry to grow and achieve its projected potential of INR645 billion by 2025².

However, while the state(s) formulate their own guidelines basis DSG, it is also imperative to amend the PCMCS to succinctly outline the distinction between DS and fraudulent pyramid money circulation schemes and determine the exclusion of the DS industry from its scope.



² Source: KPMG and FICCI Report on Direct Selling – A Global Industry Empowering Millions in India 2014

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