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**CONSUMER PROTECTION, THE GLOBAL
MARKET AND THE INTERNET**

LLM RESEARCH PAPER
LAW AND MARKETS (LAWS 536)

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VICTORIA UNIVERSITY OF WELLINGTON

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inadequate as goals. The third and ultimate objective is to determine whether or not the existing policy and goals require (and allow) the Government to regulate further to protect consumers now the Internet is being used as method of transaction.

To achieve these objectives the first part of this paper discusses the issue of consumer protection in New Zealand. In particular, its evolution culminating in the Consumer Guarantees Act 1993 and the Fair Trading Act 1986, the policy of consumer protection and the "regulatory tools" used to implement the Government's goals and policy to prevent (or correct) a market failure.

The Second part of the paper discusses what the Internet might mean for consumers transacting on line and in particular what new consumer issues it raises. I determine in this part of the paper that the Government's policy does not need to and has not changed because of the issues raised by the Internet. However given the likely importance of electronic commerce to the economy there is an additional goal to increase consumer confidence in the Internet. I then discuss the different tools, both existing and new, that could be used to increase consumer confidence in online purchases, including the possibility of regulating the architecture of the Internet.

The text of this paper (excluding contents page, footnotes and structures) comprised 13,000 words.

1. INTRODUCTION

ABSTRACT

The first objective of this paper is to address the question what the Government's economic policy and regulatory goals for consumer protection are. The second objective is to determine what tools are available to the Government to implement its goals. The third and ultimate objective is to determine whether or not the existing policy and goals require (and allow) the Government to regulate further, to protect consumers now the Internet is being used as method of transacting.

To achieve these objectives the first part of this paper discusses the issue of consumer protection in New Zealand. In particular; its evolution culminating in the Consumer Guarantees Act 1993 and the Fair Trading Act 1986, the policy of consumer protection and the regulatory tools used to implement the Government's goals and policy to prevent (or correct) a market failure.

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The text of this paper (excluding contents page, footnotes and annexures) comprises 17,902 words.

¹ The Ministry of Consumer Affairs, *The Economic Costs of the Ministry of Consumer Affairs*, (Wellington, August 1998), 1. (The Economic Costs of the Ministry of Consumer Affairs).

I. INTRODUCTION

In New Zealand the Government is focused on creating efficient markets because efficient markets increase social welfare. In efficient markets the consumer is sovereign. The consumer dictates what products and services are produced, at what price and to what level of quality. However this can only work in an efficient market. The Government considers this can be best achieved by leaving individuals to choose which transactions they want to enter into. When a market is efficient the following benefits will be obtained by society:

- (i) Prices in the economy will include, whenever possible the cost of all the resources involved in the transaction;
- (ii) Transactions will be left to private decisions with a minimum of constraints on participants; and
- (iii) Transaction costs are minimised.

The theory is that efficient markets will ensure that goods are produced with a minimum of waste and resources will be distributed efficiently ("production efficiency"). That is, consumers will be able to maximise their utility (or satisfaction) so that any reallocation of resources would make one party worse off ("allocatively efficient").

The Ministry of Consumer Affairs states that:¹

The economic theory that underpins this strategy holds that voluntary market transactions benefit the community as a whole, because each consumer gets a benefit from the product or service they purchase that is greater than the social cost of producing these products or services. That is, an economy based on voluntary transactions operates more efficiently than other models.

Sometimes however markets are not efficient, this could be for a variety of reasons, for example, the consumer may have insufficient information to fully assess the benefits and risks of a transaction. When this occurs and the consumer

¹ The Ministry of Consumer Affairs, *The Economic Context of the Ministry of Consumer Affairs*, (Wellington, August 1999),3, [The Economic Context of the Ministry of Consumer Affairs].

makes a decision which does not increase the consumers welfare (at least in the consumer's opinion) because the information they have been given is incorrect or incomplete, then the consumer will want to seek redress. If no redress is available or it is too expensive, the supplier's welfare will be increased at the expense of the consumer.

The risk that a consumer takes when entering transactions will vary according to the type of purchase the consumer is making. For complex items, that is, goods and services that are outside the range of experience of the consumer the risk to the consumer will be higher. Under these circumstances the consumer may take action to investigate the purchase further, for example, by collecting information about the supplier or the goods and services that they are contemplating purchasing.

In New Zealand the private sector provides services to reduce the transaction costs to the consumer. The Consumers' Institute is a privately funded advice provider which consumers can join for a fee. Other independent organisations have been established to test products and sell the results (for example, the Automobile Association). These service providers, where available, could be accessed by the consumer to reduce the risk of a contemplated transaction. More recently a host of consumer advice web sites have appeared some of which are interactive and give free consumer advice.

Traditionally however, market based solutions to problems however are often costly to the consumer and time consuming.

When voluntary markets fail to the detriment of the consumer, consumers will see this as unfair and interest groups may then decide to lobby Government to intervene. The extent to which the Government will take any action as a result of pressure groups will be constrained by its prevailing policy, goals and principles. The prevailing policy of creating efficient markets through voluntary transactions will mean that the Government should only intervene to the extent necessary to redress a market failure and create a fair market. Where it can the will try to address the issue through self regulation.

The concept of Fairness has been described as equity. That is equals should be treated equally and unequals should be treated unequally.² This description of fairness has its critics as it may be considered circular, after all what makes people equal or unequal? For a long time people were considered unequal on the basis of skin type, and in some countries people are considered unequal on the basis of religious beliefs. However, I suggest that what makes people equal may be transitive and alter as societies' change their normative values. In any case, fairness is a subjective concept and incorporates all of the inherent prejudices of the people attempting to define it (the prejudices will in most cases arise out of self interest).

Zajac explains that there are two pillars of human behaviour which dictate what "public interest" is or how the definition of what is fair is arrived at;

1. People tend to act in their own self interest; and
2. They tend to seek and benefit from gains through exchange.³

Because of this Zajac suggests that regulation should provide incentives to work towards the goal. (In this paper I will discuss some of the tools that the Government has made available to address some of these issues). In this regard the free market is the most incentive, compatible regulatory regime. This however will not suffice where there are market failures and where the free market is not meeting societal goals.

Historically markets were regulated by social norms. Social norms arise when people live in communities, they dictate how people will act in public and to a lesser extent in private. Social norms are a form of regulation that is enforced by the community. Over time however markets and the products got more complex grew as did rules and custom surrounding trade, these rules were enforced by the courts and slowly were incorporated into legislation.

² Edward E. Zajac, *Political Economy of Fairness*, paper back edition 1996 (MIT Press, Cambridge, Massachusetts), 105

³ Zajac, above n2, 158

The market place is now undergoing another critical change due to the advances of technology and, in particular, the Internet. The Internet provides consumers and firms with a new forum in which to share information, trade and engage in what is commonly called "electronic commerce". The trades may occur purely in cyberspace with no physical evidence of the trade occurring or they may be hybrid trades where some elements occur in the physical world (maybe registration or delivery) and others in cyber space. Therefore the Internet changes the way in which consumers interact with suppliers.

The Internet has features, which while not necessarily unique, provide enhanced benefits to consumers, however the same characteristics that create the benefits also magnify the potential risks to consumers. These characteristics are called 'architecture' in this paper. The architecture of the Internet has been described as including protocols, hardware, software and biometrics.⁴

In this paper I am going to discuss the issue of whether or not the Government should regulate to protect consumers that transact on line, and if it should, the form the regulation should take.

This paper is broadly divided into two parts; firstly I examine the issues of consumer protection, in general. I will not look at any particular industry or issue in depth, where they are referred to they will be used as an example only. Secondly I consider those issues in light of the evolution of the Internet as it is used to transact.

In the first part, consumer protection, I will look at the evolution of consumer protection. That will involve a general discussion of the historical development of commercial law and consumer protection. I will then take a close look at the Consumer Guarantees Act 1993 (CGA) and the Fair Trading Act 1986 (FTA).

goals of consumer protection can be applied to the Internet. To do this I look at whether the policy goals of the Government need to change because of the Internet. If so, what can be done to ascertain what it is that makes

⁴ Graham Greenleaf, "An Endnote on Regulating Cyberspace: Architecture Vs Law", (1998) 21 UNSW Law Journal, 12; www.law.unsw.edu.au/unswlj/e-commerce/index.html.

The CGA and the FTA are often considered the primary pieces of consumer protection law.⁵ However it should be kept in mind that the FTA and the CGA are not the only initiatives employed by the Government to protect the consumer. Other initiatives such as the Disputes Tribunal, which was established under the Disputes Tribunal Act 1988, ombudsmen and licensing service providers, are also examples of the methods the Government has developed to protect consumers in New Zealand.

Even though much of the law was already settled by the common law, it is argued that the summary legislation of the type of the CGA and the FTA is required to provide access to justice and to remove transaction costs. The Ministry of Consumer Affairs has identified the removal of transaction costs as its main method of increasing market efficiency.

After considering the CGA and FTA I will look at the general policy behind consumer protection legislation. I propose that there are two overarching considerations that take place when the Government considers legislating, market efficiency and fairness.

I will then consider the range of tools that the Government has available at its disposal to intervene in the market should it consider it necessary. I look not only at what is available at a domestic level but, because of the increasingly global market which consumers are able to transact in, I will also briefly consider what the Government could do (or participate in) at an international level.

In the first part of the paper I am not proposing to answer the question of whether or not we should have consumer protection legislation, I am proposing to assess why we have it and the extent to which it achieves the goals of the legislator.

In the second part of the paper I consider whether or not the existing policy and goals of consumer protection can be applied to the Internet. To do this I look at whether the policy goals of the Government need to change because of the Internet. However before I can do that I need to ascertain what it is that makes

⁵ *Laws of New Zealand* (Butterworths, Wellington), Common Law Collection, Consumer Protection. www.law.unsw.edu.au/unswlj/eCommerce/index.html.

the Internet different. I have identified that the architecture of the Internet is what makes it such an exciting new tool for trade, however it is the technical features which have potential to cause consumers problems and reduce the confidence the consumer has in the medium.

I will discuss what the Government can do to increase consumer confidence when transacting on line, some of the tools that are currently used may be helpful and to the extent they are not, consideration is given to new tools that may be developed. In this part of the paper I will consider articles written by Lawrence Lessig and Graham Greenleaf who suggest that if governments want to regulate at all, they should regulate the architecture of the Internet.

The paper focuses on consumer protection issues which may include investment. It does not include those issues which arise in furtherance of business pursuits.

II. DEFINITIONS

This part contains the definition of terms as they are used throughout the paper.

A Internet

The Internet refers to an informal, world-wide network of computers linking millions of users. The Internet provides users with various methods by which they can communicate with others including the World Wide Web (www), email, chat rooms and bulletin boards.⁶). Various industry bodies have been established to create the protocols by which the Internet operates, however there is no governing body that patrols the content all of the web sites and no one can be banned from using it.⁷ The Internet is an open platform that is self regulated.

The focus in this paper is on consumer protection regulation primarily Government regulation, which responds to a perceived market failure. I will also discuss consumer protection regulation which has arisen in response to perceived unfairness to the extent that the regulation is considered necessary to encourage

⁶ Bulletin boards are now becoming less prevalent due to the ease of using the World Wide Web.

⁷ The Government may be able to limit, through legislation, what content its citizens can look at, by legislating, for example censorship laws.

B The World Wide Web

The World Wide Web (www) is a huge network of web pages. Each web page is stored on a computer called a server. A person or a single entity normally controls the information on a web page. Simply posting information on the World Wide Web potentially makes it available worldwide unless the owner puts in place security policies to only allow pre approved visitors to the site. When a person visits a web site or enters into any activity on the Internet they are "on line".

C Consumer

Consumer means a natural person who purchases goods and services for personal consumption, which may include investment. It does not include those purchasing to resell or otherwise in furtherance of business pursuits.

D Consumer Protection

Consumer protection means the regulations and initiatives that exist to increase a consumer's sovereignty in the market or to redress a perceived unfairness.

In relation to consumers participating in market activities, consumer protection can manifest in regulations for two reasons:

- (i) To increase consumers' sovereignty in the market. This is normally done in response to market failure and is aimed at increasing market efficiency; and
- (ii) To redress "unfairness".

The focus in this paper is on consumer protection regulation, primarily Government regulation, which responds to a perceived market failure. I will also discuss consumer protection regulation which has arisen in response to perceived unfairness to the extent that the regulation is considered necessary to encourage consumers to participate in electronic commerce (in particular the Privacy Act 1993). In some cases the reasons for the regulation will overlap.

purpose. Various businesses will have different uses for the same goods.

III. CONSUMER PROTECTION

Commercial Law is the body of law that has evolved around the contract between the buyer and the seller at common law. However, consumer protection must go further than that as the contract is not the only concern of the parties nor is the contract only a concern for the parties to it. It is also necessary to protect the concerns of other parties, for example, it is necessary to look after the interests of the consuming public at large. Consumers need to know that certain products will not be injurious to health or life, that they are not paying monopoly prices and that they will not be deceived by false and misleading advertising. There is also the greater interest of the state, the national economy needs to be protected, the workforce needs to be productive, the economy needs to be able to attract investment and inflation needs to be controlled. Vendors will be concerned whether other vendors are engaging in unfair trade practices or monopolistic behaviour, the creditors of suppliers and consumers are interested in the terms and enforceability of contracts, and victims of theft and misappropriation will have an interest in whether their goods can later be resold. When the Government regulates all these interests need to be balanced. In this paper I focus principally on the relationship between the consumer and supplier, and the consumer's role in the market.

While in many respects the interests of consumers and businesses entering into transactions for the supply of goods and services converge, consumers are more vulnerable to market failures because a consumer is usually without the resources or expertise of a larger commercial enterprise.

A consumer will often not be an expert in the type of product that they are purchasing, this issue is becoming more prevalent with the advances in technology and the resulting complexity of goods. As a result consumers rely heavily on the information the supplier discloses about the goods and services they anticipate purchasing. A business on the other hand, will often purchase a number of the same type of goods in pursuance of its business activities, thereby developing an expertise in which goods are more suitable for the business's

purpose. Various businesses will have different uses for the same goods, whereas consumers will generally use goods for a very similar purpose.

A supplier will have more incentive to negotiate terms and conditions and to provide remedies for customers that represent a large revenue stream and an ongoing relationship. Businesses will generally have greater buying power, and buy a larger quantity of goods and services at one time giving them greater negotiating power.

However a consumer will have little power to dictate the terms of a transaction. Because of the comparatively low value of the transactions that consumers enter into it will be less economical to seek legal advice, negotiate a contract and seek remedies at law when entering into a transaction. Due to the comparative value of transactions businesses enter into it is more likely that it will be cost effective to seek legal advice prior to the transaction and to seek redress if the contract is not performed.

A Evolution of Consumer Protection

There have always been rules surrounding trade. At first the regulation of trade was by the community as people developed norms and trade practices to govern transactions. The original merchant law (*lex mercatoria*) developed international rules of trade that were enforced by "civilised states" and to that extent was international law. In 18th Century England the only commercial legal rules that existed were to protect the merchants. Trade was considered to be the lifeblood of the nation. The concerns and interests of other parties that may suffer some loss or hardship as a result of the transaction were simply not considered. Once the common law courts assumed jurisdiction over merchant law the rules were developed within each state, a development that continues today. I will discuss later in paper how this border centric view of the law creates difficulties in an economy moving towards globalisation.

The common law courts also developed the rule of "caveat emptor".⁸ This rule became the default proposition of common law. The doctrine of "caveat emptor" states that:⁹

In the absence of fraud, and provided the goods were open to inspection before being purchased, the buyer could not complain of defects in the article he bought. He or she should have used his or her own judgement ...for he or she could have exacted a warranty.

Over time commercial law has evolved from that position through market transactions where it was recognised that the seller had additional obligations to the obligation to supply. Those obligations were implied into contracts by the courts of England.¹⁰ New Zealand followed the United Kingdom and adopted the United Kingdom's common law rules for commercial transactions. These principles still apply to a large extent in New Zealand but additional rights and remedies have been given to consumers via legislation. The first such legislation enacted in New Zealand was the Sale of Goods Act 1908 which implied guarantees into contracts for the supply of goods. Today the principal pieces of consumer legislation in New Zealand are the Consumer Guarantees Act 1993 (CGA) and the Fair Trading Act 1986 (FTA).

1. Consumer Guarantees Act 1993

In March 1992 the Consumer Guarantees Bill (CGBill) was introduced. The CGBill was introduced by Hon. Katherine O'Regan (the then Minister of Consumer Affairs, on behalf of the Minister of Justice). The Minister, in her

⁸ *Pasely v Freeman* (1789) 3 Term. Rep. 51.

⁹ JF Burrows, J Finn and S Todd *Law of Contract*, (8th ed, Butterworths, Wellington, 1992),164, [*Law of Contract*].

¹⁰ for example; In a sale by sample it was an implied term that the bulk should correspond to the sample, and the buyer should be able to compare the bulk to the sample; In a sale by description the goods should not only meet the description but should also be of merchantable quality; If the buyer gave the seller an explanation of the purpose for which she wanted the goods and that she relied on the seller's expertise then the seller must either disclaim responsibility or be deemed to have accepted this additional responsibility; and the seller must be in a position to give good title.

introductory speech put forward the following reasons for the introduction of the CGBill:¹¹

- (i) to clarify the rights and obligations of manufacturers, traders, service providers, and consumers in a way that is appropriate taking into consideration the demands of the modern market place;
- (ii) promote fair and efficient market place practices;
- (iii) enhance the consumer's ability to participate effectively in the market;
- (iv) benefit fair and ethical suppliers by clarifying their obligations;
- (v) benefit the economy generally; and
- (vi) set out clear standards of quality, fitness, durability and safety to promote fair and effective competition in the market place.

The Hon. Katherine O'Regan then commented that the economic policies of the Government recognise that choice is the central element to consumer welfare and that consumer sovereignty in the market place is the central element of an efficient market.¹²

The Sale of Goods Act 1908 (the predecessor to the CGA) was criticised in her speech as being "archaic" and intended for transactions between merchants, and therefore, did not assist consumers in the modern market place. The CGA was seen as a way of ensuring that the current law was understood. The CGBill, the Minister said, was "about fairness".¹³

The essential principles of the CGA as introduced include:

- (i) Statutory Guarantees that apply to the supply of goods and services. The particular types of guarantee have been listed in Appendix A;

¹¹(17 March 1992), NZPD522, 6901, [NZPD, 522].

¹² NZPD, 522 above n 11, 6901.

¹³ NZPD, 522 above n 11, 6901.

- (ii) Consumers are given an equality of bargaining power with the providers of goods and services (the implied guarantees are mandatory);
- (iii) The obligations of manufacturers and suppliers are clearly stated; and
- (iv) The CGA implies mandatory terms into the contract between suppliers and consumers, there is no contracting out of the CGA (except where goods or services are acquired for business purposes).

The CGA is designed to regulate the behaviour of suppliers of specified goods and services to a consumer. A consumer under the CGA is a person who acquires goods or services of a kind ordinarily acquired for personal, domestic or household consumption and does not acquire them for a business purpose.¹⁴

It is important that consumers are protected because of the reasons discussed at the beginning of this part of the paper. In particular consumers are normally not as informed as a business and low value transactions mean the cost of negotiating a contract with all the guarantees of implied by the CGA may be greater than the value of the transaction in most instances.

By making the terms of the CGA mandatory the Government has increased consumer welfare by providing the consumer with some basic contractual terms and conditions for the purchase of goods and services. It reduces the transaction costs to consumers as they will no longer need to negotiate terms and conditions for the supply of goods and services. Consumers will still need to seek advice before entering into an agreement to purchase real estate. Real property is not a "good" under the CGA. It may be inferred from this that the Government is only interested in assisting consumers with purchase of lower value transactions. This would fit with the rationale that the benefit to consumers of enforcing their rights

¹⁴ It may also be inferred that consumers who can afford to purchase their own home can also afford to buy out their own insurance. This inference may also be supported by the Credit Control Act 1972 section 15 which defines "controlled credit operator" the definition being:

¹⁴ Section 2 defines service to include rights, benefits, privileges or facilities that are conferred by a supplier pursuant to a contract for or in relation to the performance of work (including work of a professional nature)

in lower value transactions is less than the cost of enforcement, and therefore consumers require protection.¹⁵

Part II of the CGA sets out a consumer's rights of redress against a supplier who fails to comply with the guarantees implied by the CGA, except for those guarantees relating to price and repairs. Depending on the nature and circumstances of the defect the consumer is able to have goods repaired, replaced or get a refund.

If a supplier of a service fails to comply with any of the guarantees listed above (other than the guarantee regarding price) the consumer may, depending on the nature of the failure, require:

- (a) the failure to be remedied,
- (b) the failure to be remedied and recover reasonable costs from the supplier,
- (c) cancellation of the contract, or
- (d) damages for any loss suffered.¹⁶

The consumer's redress for a higher price being charged than what is reasonable for the supply of goods or services is not to pay more than a reasonable amount for the goods and services.

By outlining rights of redress in the CGA, and particularly the inclusion of self help remedies, for example, requesting that the supplier fixes goods which can be repaired in a reasonable time frame, consumers are provided with inexpensive access to redress. Consumers do not require a lawyer to be involved while they

¹⁵ It may also be an indication that consumers that can afford to purchase their own home can also afford to look after their own interests. This inference may also be supported by the Credit Contract Act 1981, section 15 of the Act defines "controlled credit contracts", the definition excludes contracts where the debtor owes the same creditor \$250,000 or more.

¹⁶ Consumer Guarantees Act 1993, section 32, however, s35 provides that these rules will not apply if the performance of the service is merely incidental to the supply of goods and the consumer has or had the right to reject the goods.

have self help remedies available. This reduces transaction costs to consumers and can also increase allocative efficiency.

Part III of the CGA gives the consumer rights of redress against a manufacturer of non-compliant goods due to failure to comply with particular guarantees, including the guarantee of repair facilities.

This is a new statutory right. Without this right the consumer would not be able to seek redress from a manufacturer easily, and in any case not in contract. The consumer has now been given a statutory right to seek redress from a manufacturer which will be useful where the supplier has gone out of business or has not been able to provide a satisfactory remedy.

Therefore while Hon. Katherine O'Regan considered that the CGBill was to increase fairness, I consider the CGA has objectives other than increasing fairness, it also increases market efficiency by:

- (i) facilitating entry into trades. Consumers do not have to go to the expense of negotiating their own contracts for supply which they would often never do (except for maybe high value transactions) as the cost and time would outweigh the benefit; and
- (ii) giving consumers a low cost remedy if a vendor fails to meet any of the implied guarantees.

2. *Fair Trading Act 1986*

The courts of New Zealand have also followed the United Kingdom in developing common law rules around misrepresentations.

At common law a misstatement which:

- (i) is not simply an expression of opinion but made in such definite terms so as to lead the person to whom the statement was made to believe it to be true, and
- (ii) on reliance on its veracity, resulted in a contract between the parties, but

(iii) was not intended to be a term of the contract when the statement was made,

will give the buyer an opportunity to rescind the contract if the statement was a misrepresentation. However, it will not usually give the buyer an opportunity to obtain damages unless it was taken as term of the contract, or was made fraudulently.¹⁷

If the statement is not contractual in nature then the remedies at common law are more restricted. The recipient of the information may still be able to recover for loss resulting from a misrepresentation.¹⁸ Today in New Zealand the FTA and the Contractual Remedies Act 1979 both apply to misrepresentations. The FTA covers all representations and misleading conduct "in trade" and the Contractual Remedies Act 1979 deals with misrepresentations that induce the parties to enter into a contract.

The intention of the Contractual Remedies Act 1979 was to simplify the existing law by reducing the complex network of rules to a few simple principles.¹⁹ That Act takes away the distinction of whether a representation was a term of a contract or not. However, the Contractual Remedies Act 1979 still causes problems for consumers for example, they would have to show they entered into a contract on the basis of a misrepresentation.²⁰

¹⁷ *Heilbut, Symonds & Co. v Buckleton* [1913] AC 30.

¹⁸ If the representation was made recklessly there may be a remedy in tort if there is a special relationship between the parties, if the representation has been made fraudulently, the buyer would have a claim in tort for damages in deceit and set the contract aside, if the representation was innocent the buyer may be able to rescind the contract in equity however no damages would be available.

¹⁹ *Law of Contract*, above n 9, 293.

²⁰ Under the Contractual Remedies Act 1979 a consumer will need to show: the representation induced the contract (section 6), if the contract is required to have all its terms in writing an oral representation will not be enforceable, if the contract is for the sale of goods then it will still be important as to whether the misrepresentation is a term as that will impact on whether or not the contract can be cancelled. If the court considers it fair and reasonable it may still determine that a misrepresentation did not induce the contract if the contract excluded all pre contractual

Pre 1986 therefore the consumer would usually need to seek legal advice to identify their rights and seek compensation for any loss they suffered as a result of a misrepresentation. This would increase transaction costs to the consumer and often the expense of seeking legal assistance outweighs the value of the goods or services purchased. It would mean that suppliers that supplied goods and services to consumers would conduct their business largely unchecked because individual consumers would often not have the resources to identify and enforce their rights. The defects of the existing regulation were identified and have been addressed to some extent in the FTA.

In 1985 the Fair Trading Bill was introduced to Parliament by the Minister of Consumer Affairs, the Hon. Margaret Sheilds. In her introductory speech the Minister stated that the FTA was necessary for the following reasons:²¹

- (i) existing legislation was inadequate because it did not set clear standards for trade descriptions and trade conduct. No direct remedies were available;
- (ii) unfair trade practices such as pyramid selling and bait advertising, offering gifts and prizes without intending to supply them, referral selling, and demanding or accepting payment without ever intending to supply all needed to be prohibited;
- (iii) to prescribe product safety;
- (iv) to ban hazardous goods;
- (v) to give access to effective remedies;
- (vi) to consolidate the law;
- (vii) to align New Zealand law with Australia;
- (viii) to educate consumers on their rights and remedies; and

representations. It does not assist a consumer who suffered a loss but did not enter into a contract with the presenter.

²¹ (7 November 1985), NZPD, 467, 11985

- (ix) to benefit fair and ethical suppliers in relation to unfair competition that results from deceptive advertising and other conduct.

In her introductory speech for the FTA Margaret Shields stated:²²

The Bill is the corollary of the Commerce Bill ...That Bill promotes workable and effective competition in the markets in New Zealand. This Bill is designed to ensure that consumers, as participants in the market place participate in the benefits of competition by countering deceptive conduct and promoting informed choice in the key areas of price, quality and service, and ensuring that consumers have accurate comparative information on which to base their purchasing decisions.

The FTA came into effect on 1 March 1987. Its long title states the FTA is "...an Act to prohibit certain conduct and practices in trade to provide for the disclosure of consumer information and to promote safety."

Under the FTA the Commerce Commission is given the task of making information about the FTA available for persons in trade and for consumers. This is new obligation that did not exist prior to the FTA. The goal of this provision is to assist consumers to discover their rights without requiring the consumers to pay for legal advice. This obligation reduces transaction costs to the consumer by giving them information about their rights, who the consumer can complain to, and the type of remedies that may be available.

Part I of the FTA prohibits misleading and deceptive conduct, false representations and unfair market practices "in trade". Part I contains a general prohibition on engaging in misleading and deceptive conduct, or conduct that is likely to mislead or deceive.²³ There are other more specific prohibitions regarding misleading conduct in relation to goods, services and employment. Those more specific prohibitions also carry with them criminal liability.²⁴ Section 13 prohibits particular false statements about goods and services and section 14 prohibits specified false statements about land. The balance of Part I

²² NZPD 467, above n 22.

²³ Fair Trading Act 1986, Section 9

²⁴ Fair Trading Act 1986, Section 40

prohibits certain unfair practice (that is offering of prizes without the intention of providing them, bait advertising, pyramid selling, harassment and coercion and referral selling (offering a consumer some benefit in return for the consumer giving that person the names of prospective customers or otherwise assisting that person to supply goods and services to other consumers), if the benefit is contingent on an event occurring after that contract is made).

The FTA is different to the CGA in that it applies to all transactions, including land, entered into by both businesses and consumers. However, it is similar in an important way, a supplier cannot contract out of its obligations under the FTA. The FTA, like the CGA, implies mandatory terms into dealings between a consumer and a supplier. This is important for consumers because it redresses the imbalance of power between a large supplier and a consumer, as the consumer does not need to take any steps to affirm or retain their rights by seeking agreement of the supplier. Part one itself doesn't add much for the consumer as it is a restatement of the existing law, and doesn't do much to clarify the pre existing issues such whether silence constitutes a misrepresentation, (though the use of the phrase "misleading conduct" may make it more likely that a silence will be actionable).

Parts II and III of the FTA deal with information that must be disclosed about particular products and product safety standards (including the compulsory recall of products in certain circumstances) respectively. Section 33 makes it illegal to import goods that do not comply with the product safety provisions of the FTA.

Part IV deals with the safety of services. Services for the purposes of this part includes the performance of work by way of maintenance and repair, treatment or alteration of goods, transportation of goods, maintenance and the development of land and buildings.

Parts II, III and IV are a restatement of existing regulations and legislation that has been consolidated in the one Act by the FTA.

Part V specifies the remedies. The remedies are not as simple for consumers to enforce as under the CGA. Sections 40 to 43 set out the range of orders that can be made from criminal conviction for breaches of certain sections to injunctions,

fines, damages and other orders remedying damage caused by the breach. The Commerce Commission has the power to bring an action against parties in breach.

Part V of the FTA is helpful to consumers as it gives the courts a guide as to what remedies they can award a consumer. Further by giving the Commerce Commission the power to enforce the FTA action can be taken against suppliers that engage in unfair trade practices before consumers suffer any loss or where consumers have suffered loss but cannot afford to take an action, to prevent further customer's incurring loss.

The FTA was to achieve further objectives other than consumer protection, including aligning New Zealand's laws with those of Australia, consolidating New Zealand's law in the area, and set clear standards for trade conduct. The FTA goes somewhat towards setting clear standards for trade practices, by making the standards mandatory, however as mentioned above, it does not address the issue of silence. The FTA has also caused issues because a consumer would need to show the conduct was "in trade". I do not consider that the FTA has consolidated New Zealand's law as much as it could because the FTA adds to obligations of suppliers it does not replace them.

Both the CGA and the FTA provide a summary of consumers existing rights however they both add two important, additional features they cannot be contracted out of and they define the remedies that are available to the consumer. The FTA also allows the Commerce Commission to take an action against an errant supplier.

The comparatively low value of consumer transactions impacts on consumers in two ways; firstly the cost of enforcing their rights is often too high compared to the cost of the goods and services. Secondly a supplier will not have the same incentive to negotiate terms of a contract with a consumer which does not represent a high revenue stream. Therefore mandatory terms reduce the transaction costs to the consumer.

B Government Policy of Consumer Protection

The underlying theory of consumer protection regulation has been written about widely. Government policy driving consumer protection is recommended/developed by the Ministry of Consumer Affairs. The Ministry of Consumer Affairs was established in furtherance of the Labour Government's 1984 election policy of taking steps to improve consumer welfare.²⁵ The Ministry of Consumer Affairs is an operating branch of the Ministry of Economic Development. The relationship between the two Ministries is documented from time to time in a Relationship Letter, which is agreed by the head of each Ministry.²⁶ The services that the Ministry provides are:²⁷

- (i) Advising Government on regulation and self regulation of consumer markets,
- (ii) The provision of information, education and advice that helps consumers and businesses to understand and use consumer legislation,
- (iii) Advising on product safety issues; and
- (iv) The administration of trade measurement in New Zealand.

Within the Ministry, the Consumer Policy Advice Unit is responsible for policy advice on laws relating to consumer transactions, market place regulation and self-regulation.

The Ministry has published a number of policy papers. These state that its objectives are to remove the impediments to voluntary transactions and to minimise the cost of transactions between consumers and businesses. Keith Manch (General Manager, Ministry of Consumer Affairs) has written that the

²⁵ As advised by Pamela Rogers, Advisor, Ministry of Consumer Affairs (24 August 2000).

²⁶ The Ministry of Consumer Affairs, *Overview of the Ministry of Consumer affairs*, (Wellington, November 1999), Appendix A, [Overview of the Ministry of Consumer Affairs].

²⁷ *Overview of the Ministry of Consumer Affairs*, above n26.

desire to minimise the cost of transactions, in the broadest sense, fundamentally underpins the Ministry's work.²⁸

In October 1996, Keith Manch wrote; "The Ministry of Consumer Affairs exists to promote a fair and informed market place for consumers."²⁹

The Ministry of Consumer Affairs' key objectives are, in summary, to increase market efficiency and to increase fairness. The Ministry has concluded that; "The main driving force behind the process of making law or regulation in consumer markets is the creation and maintenance of efficient markets in which the legitimate rights of consumers are reflected."³⁰

These objectives are, the Ministry says, in pursuance of the political vision in New Zealand that is currently that voluntary transactions are preferable to transactions resulting from government directions.³¹

The Ministry's own view of its role has been reinforced by the view of commentators. Professor John Burrows³² reasons that due to the change in the nature of products which are now being offered, consumers are not able to use their own judgment to ascertain the quality or suitability of the goods or services that they are purchasing. As a result, consumers have formed interest groups (I suggest that these interest groups provide a common perspective on equality, that is, what criteria is used to discriminate between groups of people based on fairness arguments). Burrows continues and states that governments have formed organisations to care for the consumer such as the Ministry of Consumer Affairs. He also comments that in economic theory the consumer is the sovereign of the

²⁸ *The Economic Context of the Ministry of Consumer Affairs*, above n1, i,(Forward).

²⁹ Ministry of Consumer Affairs, *Assessing Costs and Benefits in Consumer Policy Development* (Wellington, October 1996),i, (Forward),[*Assessing Costs and Benefits in Consumer Policy*].

³⁰ Ministry of Consumer Affairs, *Market Self Regulation and Codes of Practice*, (Wellington, 1997), 2, [Market Self Regulation].

³¹ *The Economic Impact of the Ministry of Consumer Affairs*, above, n1, 1.

³² *Law of Contract*, above n9, 26.

market place (a view shared by the Ministry of Consumer Affairs³³), but concludes that this can only happen with Government intervention.

If the Government did not intervene in the market, the market can, where possible, respond to a market failure and unfairness. In this case the market might respond by:

- (i) consumers forgoing the transaction;
- (ii) a consumer could inspect the goods themselves, however this does increase transaction costs but could be expected in the purchase of a large asset (as assumed by the CGA by the exclusion of transactions for land);
- (iii) a consumer may ask friends (other consumers) what their experience of the product and vendor has been; ~~is may be allowed to perform poorly for~~
- (iv) Sellers and manufacturers could guarantee their products, however these may not meet the customer's expectations and there is no incentive on a seller to offer a guarantee unless the market is competitive;
- (v) Consumer may develop brand loyalty. The consumer can buy a brand that they have tried and liked before, and not take the risk of trying an unproven brand. (This, taken to the extreme, will raise the barriers to entry to new players in markets, as they will need to invest heavily in advertising and marketing to gain market share. This will have an anti competitive effect in long term and therefore reduce the consumer's choice).
- (vi) Independent organisations may test products or recommend sellers. However this does have free rider problems and there is an argument that all the information should be available in a perfectly competitive market in any case. The reality today is that there are so many goods and services available on the market today of varying technical detail that even if the information was available the consumer may not be able to

³³ *Market Self Regulation*, above n 30,4.

In the
different
understand or get hold of it. Consumer advice web sites are beginning to make significant inroads in addressing the information gap.

The Ministry of Consumer Affairs suggests that market based solutions have a number of drawbacks:³⁴

- (i) generally they are reactive,
- (ii) they lack compulsion
- (iii) not all traders are bound or elect to provide them
- (iv) no provision for redress when a trader will not accept being bound,
- (v) firms that fail through poor product or service quality generally take their customer's down with them. (firms may be allowed to perform poorly for a long time before market sanctions force the firm to go out of business, causing a reduction in social welfare).

Because of these drawbacks, the Ministry considers that there is a need to legislate to move our markets to an efficient state. The Ministry has identified the following five characteristics that it considers necessary for a perfectly competitive market:³⁵

- (i) free and equal access to markets,
- (ii) interchangeable commodities available from many sellers,
- (iii) buyers have perfect knowledge,
- (iv) no one party has sufficient power to unilaterally determine price, quality or performance ; and
- (v) all costs of providing the commodity are borne by the producer and all the benefits accrue to the consumer.

³⁴ *Market Self-Regulation*, above n 30, 4.

³⁵ *Market Self Regulation* , above n 30, 2.

In the same paper the Ministry cites four instances where a consumer may have difficulty exercising his sovereignty:

- (i) supplier is a monopoly
- (ii) externalities are not reflected in the market prices
- (iii) information asymmetries exist
- (iv) transaction costs are excessive

These are known in economic terms as "market failures". The list of difficulties is not exhaustive, however. It does not include non-rival or public goods. These are goods which are not unique (or non-excludable) and are not diminished by use. In these instances the consumer will not be offered the product in the market due to lack of demand, not because the consumer does not want or value the product but because once the product is produced the consumer can free ride (that is, get the benefit of the good without paying for it).

The Ministry of Consumer Affairs has concluded that to achieve an efficient market, its goal is to minimise the cost of transactions between consumers and business.³⁶

Transaction costs include three subcategories:³⁷

- (i) pre transaction costs, which include search and information costs (including the costs of labelling and advertising),
- (ii) contemporaneous transaction costs, which include the costs of agreeing the deal; and
- (iii) post transaction costs, which include the cost of enforcing contracted rights and seeking a remedy.

³⁶ *The Economic Context of the Ministry of Consumer Affairs*, above n1, i (Foreword), (Keith Manch).

³⁷ *The Economic Context of the Ministry of Consumer Affairs*, above n1, 17-18.

In some transactions where the consumer is in a strong position (for example, the purchase of groceries which the consumer has the opportunity to inspect), the transaction costs are non-existent or minimal. I suggest that, in this situation, the consumer will be more concerned with paying as little as possible and the seller will want to obtain as much as possible for the products sold, therefore there will be a strong case to leave regulation to the market.

The CGA and the FTA are evidence of where the Government has used regulatory tools to reduce transaction costs to the consumer, for example the mandatory terms of the FTA and the CGA reduce contemporaneous transactions costs and by stating the available remedies post transaction costs are reduced. Both Acts also can be used to reduce pre transaction costs by giving the consumer the right be able to rely on a recommendation or information given by the supplier about the goods or services they wish to purchase.

The Government divines the jurisdiction over which it has sovereignty from geographical boundaries. Therefore, while the Government can establish policy to guide regulation of consumer protection domestically, with the increasingly global nature of markets, the Government may also need to consider whether or not the objectives of the policy will be met through domestic regulation. If not then the Government will need to look at international initiatives and decide whether it wants to harmonise its consumer protection laws with that of other jurisdictions. This has policy implications of its own which are not the focus of this paper but will need to be considered in parallel with consumer protection policy and more importantly the tools chosen to implement it. Jurisdictional issues will be discussed in more detail later in this paper.

The type of regulation that the Government will consider implementing to achieve its policy and goals, will depend on a number factors which include the nature of the goods and services, the desirability of the transaction, the effect on other markets, and most importantly whether or not any proposed regulation will be effective. I will discuss the particular tools for regulation available to the Government below.

¹⁷⁷ Lawrence Lessig, "The Law of the Horse: What Cyberspace Might Teach", (1999) 61:301, *Harv J Rev*, 581, 582, 592.

C Tools for Regulation

Regulation is a way of changing people's behaviour. Lawrence Lessig identifies four modalities (ways of regulating to modify behaviour):³⁸

- (i) Law. This is the most obvious modality. It is directed by government and orders people to behave in a certain way or face the threat of punishment. The legislature enacts, the prosecutors threaten and the courts convict;
- (ii) Social norms. These are directed by the community we live in and dictate how we conduct ourselves in public and to a lesser extent in private. Social norms also regulate by threatening punishment, not though, through a centralised force but by the community. The community regulates, the community threatens and the community punishes. Social norms will effect what objects are traded and may reflect a prevailing definition of fairness.
- (iii) Markets. These regulate by price. In an efficient market the consumer will determine the price. Markets are only able to constrain in this way because of other constraints of law and social norms; property rights and contract law govern markets, and markets operate within the domain permitted by social norms. Markets will affect how easy or difficult it is to change architecture.
- (iv) Architecture/ Nature. Architecture is the physical world as we find it. If a river separates two cities there are limits on the way the citizens of those cities will interact. A high wall and barbed wire will prevent the people crossing over it. Architecture will affect the development of norms.

Lessig points out that these four modalities act together to regulate behaviour. It is the mix of these modalities that will determine the effectiveness of the regulation. Social norms, markets and architecture will all influence law. In this

³⁸ Lawrence Lessig, "The Law of the Horse: What Cyberlaw Might Teach", (1999) 113:501, Harv l Rev, 501, 522-533.

part I am going to focus on how law may effect markets, architecture and social norms. I consider separately the tools that are available for regulation domestically and internationally.

1. Tools for domestic regulation

I have already discussed the FTA and the CGA, two key pieces of legislation that underpin consumer protection in market transactions. These two pieces of legislation incorporate a number of tools listed below which are available to the Government to intervene in markets.

The Ministry of Consumer Affairs has identified a range of tools that may be used to achieve its objective of increasing market efficiency. The Ministry has also published guidelines, within which issues are defined, scoped and options considered and selected.³⁹

Government regulation can take many forms for example:

- (i) State ownership. The state will provide goods and services that are public goods such as defence and police. The state will often provide goods and services that are natural monopolies. In New Zealand the policy has been away from Government participation as a seller in a market.
- (ii) State allocation. The Government may allocate scarce resources to participants in the market based on a set of pre determined criteria. This may be done through the use of licenses and quotas (for example fishing quota).
- (iii) Limited property rights. The government may give a person the right to use property for a specified time or in a specified way. For example intellectual property rights are both regulate the rights of the creator and any other party. Licenses and permits may be used to give rights to people to use property for a particular purpose but not necessarily to

³⁹ *Assessing the Cost and Benefits in Consumer Policy*, above n 29.

dispose of it. Property rights are also limited by restricting the design and construction of the property, for example physical structures must comply with the Building Act and the Resource Management Act and cars must pass a Warrant of Fitness in accordance with the Land Transport Act.

- (iv) State approval of certain contracts. This can be used to prevent companies gaining undesirable market dominance.
- (v) Mandatory terms. The imposition of mandatory terms can be used to give certainty to consumers in low value transactions where the cost of negotiating terms would be higher than the value of the transaction and where there is an imbalance of power between the parties, for example refer to the CGA and FTA discussed above.
- (vi) Default remedies/ penalties. Default remedies in certain contracts give the consumer self help remedies which they do not require court sanction to enforce therefore reducing transaction costs, (for example see the CGA and the Companies Act 1992 (minority interests)). Default penalties have the same effect. For example, section 25 of the Credit Contracts Act 1981 provides that the penalty on the financier for not making proper disclosure will result in the debtor not being required to pay the specified amount.
- (vii) Restrict who may enter into a transaction. For example, a minor may not enter into a contract unless particular criteria are fulfilled (Minors Contracts Act 1969). Some classes of people are also prohibited from engaging as a seller in various markets (for example, the Credit Contracts Act 1981 prohibits certain classes of people from acting as financiers).
- (viii) Facilitating credible commitments. By providing a body of contract law parties can enter into agreements which enable one party to receive the benefit of the agreement later than the other. This reduces transaction costs as parties can often avoid going to court if the outcome is predictable, but also gives parties access to the courts (or other quasi judicial institutions) to enforce their rights.

- (ix) Providing default rules for common transactions. These are rules that may be contracted out of and are aimed at reducing transaction costs and can be found in the Sale of Goods Act 1908 and the Companies Act 1993. These are not found so much at the consumer end of the market. These are less likely to be found in consumer protection legislation today, but tend to be used to facilitate business transactions.
- (x) Prohibiting and imposing sanctions for various forms of deceptive or misleading conduct. This technique is used to increase allocative efficiency in markets and requires the sellers to tell the truth. This has been discussed earlier in terms of the Contractual Remedies Act 1979 and the FTA.
- (xi) Prohibiting activities that distort the operation of markets. Collusion, abuse of dominant market positions, onerous contracts and other unfair trade practices all go to distort price, quality and quantity of goods and services. For example the Commerce Act 1986 regulates these activities in New Zealand.
- (xii) Requiring disclosure in certain matters, in the context of certain transactions, to address information asymmetries. These are rules that require the seller to disclose information about the product, investment or themselves. This is a tool that may be used to increase allocative efficiency and to decrease transaction costs. In theory, the information will be readily accessible to the seller and therefore the search cost to the seller will be lower than they would be for the buyer.
- (xiii) Making provision for dispute resolution. Institutions have the important function of enforcing obligations that are imposed between the parties or by statute. In New Zealand the courts and the Disputes Tribunal provide dispute resolution forums. In addition to these bodies are self regulating bodies such as the New Zealand Law Society, which is a statutory body that hears complaints of consumers of legal services at the NZLS Disciplinary Tribunal.

- (xiv) Requiring market participants that wish to trade in particular goods and services to be authorised or licensed. This will enable transaction costs to be reduced by reducing search costs. This type of intervention requires a minimum level of competency and in many cases subjects the seller to industry regulation.
- (xv) Establishing institutions to monitor and regulate particular markets/ self regulation. This form of regulation delegates powers of regulation to industry and professional groups or to Government bodies. It should enable more effective and flexible regulation by empowering experts to identify the areas of risk and enforce an industry best practice and code of ethics thus increasing quality, for example, the Securities Commission.
- (xvi) Educating consumers. This has been delegated to various government bodies by statute and through policy. For example, the Commerce Commission has been delegated responsibility for educating the public about the FTA. The Ministry of Consumer Affairs provides a public information office and helpline which people can contact to obtain advice about market issues.
- (xvii) Exclusion from market transaction. In New Zealand there are very few examples of activities that are prohibited completely. It is suggested that those transactions that are prohibited tend to be so for the following reasons:
 1. prevent commodification (for example, the sale of babies or body parts)
 2. paternalism (for example minors cannot enter into in normal circumstances, some products or services may be seen to be "bad" and therefore prohibited)

The Government also has another tool, to do nothing, to leave it to the market and social norms to regulate behaviour. This will be effective if there is sufficient competition in the market or if there are enough, relatively low cost private organisations assisting the consumer.

2. Tools for International Harmonisation of Law

I will not consider the question of harmonisation of laws in depth, as it could be the subject of a paper in its own right. However it is necessary to discuss some of the issues briefly in this paper because new communication technologies make global transactions much more accessible to consumers. As a result domestic regulation alone may not be sufficient to protect consumers.

The issues for consumers transacting across jurisdictions arise from the uncertainty of the existing law. When a transaction takes place in more than one country or state, potentially the laws of all states could apply. This is called a conflict of laws. How the conflict will be resolved will be different in each state.

Broadly the issues that a court would need to decide on are:

- (a) Whether the court can exercise jurisdiction;
- (b) Whether the court will exercise jurisdiction; consumer's case.
- (c) Choice of law; and consumer's case to get any remedy they are awarded
- (d) Enforcement of foreign judgments.

At common law the New Zealand High Court will have basic jurisdiction over a person resident overseas and events occurring extraterritorially if the damage is sustained in New Zealand.⁴⁰ In other circumstances it will depend on whether or not the High Court will exercise its discretion to allow the defendant to be served. High Court Rules 219 and 220 outline in which circumstances the court may consider granting leave for service.⁴¹

⁴⁰ *Distillers Co (Biochemicals) Ltd v Thompson* [1971] AC 458, discussed by the New Zealand Law Commission in, *A Guide for the Legal and Business Community: R50*, (Wellington, 1998), 92- 97.

⁴¹ The District Court has jurisdiction through the District Courts Act 1947. The District Court has basic jurisdiction in civil matters up to a value of \$200,000. Up to that limit in civil matters the District court will therefore have the same jurisdiction of the High Court (District Court Rules 242- 243 mirror the High Court with respect to service).

Even if the court finds it has jurisdiction it may not exercise that jurisdiction if it is considered that it is forum non-conveniens. The approach of various states in addressing the issue of basic jurisdiction and exercise of jurisdiction differs and therefore a successful outcome for a consumer in one jurisdiction may not impact on the result in another jurisdiction.

Even after the consumer has managed to satisfy the court that it does have jurisdiction and that the court should exercise that jurisdiction the next step is to satisfy the court that the laws of New Zealand should apply. If the parties have selected New Zealand law in the contract then the courts will give effect to that unless there are overriding public policy reasons not to. If no system of law has been chosen then it will be determined on the application of New Zealand's choice of law rules. Whether or not New Zealand law will be applied is difficult to predict. If the court decides that the law of another jurisdiction will apply then the parties will need to produce evidence of that other state's law in the hearing. This will add further expense to the consumer's case.

The final hurdle for the consumer is to get any remedy they are awarded enforced in a foreign jurisdiction. This will mean a further application has to be made, this time to the court in the jurisdiction in which the consumer wants the order to be enforced.

The existing regulation will act to increase transaction costs to consumers because of the uncertainty they cause.

There are a range of ways New Zealand may harmonise its law with the laws of other states, for example:

- (i) by enacting domestic laws which are the same as the law of another state. An example of this that I have already discussed is the FTA,
- (ii) agree bilateral arrangements as occur between New Zealand and Australia pursuant to CER; and
- (iii) contributing to and be party to multilateral arrangements or treaties.

The principal sources of international law are treaties, international custom, judicial decisions, and academic writings.⁴² The Law Commission describes a treaty as:⁴³

A treaty is an international agreement between two or more states or other international persons, governed by international law. ('other international persons include bodies such as the United Nations, the World Bank, and the South Pacific Commission').

Treaties can be used to:

- (i) harmonise current consumer protection laws;
- (ii) establish new laws;
- (iii) unify choice of law rules; and
- (iv) unify rules of jurisdiction.

When a country signs a treaty it may require the signatory country to enact particular legislation domestically and may have an effect on the development of legislation in general.

The particular value of treaties is that they can be used to reduce transaction costs to consumers. Consumers will find it costly and time consuming to enforce their rights at law in New Zealand, against foreign suppliers. Treaties may eliminate issues over jurisdiction by either containing jurisdiction clauses or by conforming laws enough that jurisdiction will not have an effect on the outcome of a dispute.

Treaties have drawbacks however:

- (i) it takes a long time to create and ratify a treaty (Berne Convention was first adopted in 1886 and in 1919 (30 years later) only 15 of the 133 states which have ratified the treaty had joined.),

⁴² Article 38(1), Statute of the International Court of Justice.

⁴³ New Zealand Law Commission, *A New Zealand Guide to International Law and its Sources*: R34, (May 1996, Wellington), 6.

- (ii) difficult to create because it is difficult to reach consensus between national powers,
- (iii) they are costly; and
- (iv) they are inflexible.

Whether or not New Zealand should agree to align its laws with other nations depends on a number of factors including:⁴⁴

- (i) the extent that it is necessary to address a market failure,
- (ii) the extent to which diversity will promote competition,
- (iii) differences in commercial or regulatory environment (for example, if a country does not have the resources or skills to enforce a law harmonisation will be ineffective); and
- (iv) participation and accountability (the law making is removed further from those that must abide by it, this may reduce the quality and effectiveness of the law), costs of co-ordination.

However, despite these drawbacks, if an issue cannot be effectively regulated domestically then the Government may need to find a multilateral solution that will work.

3. Choice of Tools

The Government could use any one or a combination of the tools listed above to regulate for consumer protection. What is appropriate may vary depending on the product or service and the identified market failure. When considering the options the Ministry of Consumer Affairs has identified several factors that should be considered, including:⁴⁵

⁴⁴ David Goddard, "Making Business Law: the CER Dimension", (August 1999, Wellington).

⁴⁵ *Assessing the Cost and Benefits in Consumer Policy Development*, above n 29, 8

- (i) Constraints in the way of Government policy directives and resources. For example the current Government policy is towards voluntary transactions therefore state ownership is now a tool which is not used to the extent that it once was, if at all;
- (ii) Contribution to existing policy, for example, will the proposed use of the tool reduce transaction costs? Will it distort the market?
- (iii) Education may be the solution not further regulation or in addition to further regulation;
- (iv) Implementation and compliance. Are the resources required for enforcement realistic? How will compliance be enforced? (This is of particular concern when transactions in a particular market occur across national borders).
- (v) Avoid stifling innovation;
- (vi) What are the costs of the solution, when will they be incurred and who bears the cost?
- (vii) Who will get the benefit of the solution, will the benefits change over time?
- (viii) What is the effect on the ability of the consumer to participate in the market? and
- (ix) What incentives will be created?

The Ministry of Consumer Affairs has declared that self regulation has become the key initiative to ensure improved market practices driven largely because of the increasingly global economy.⁴⁶ The Ministry of Consumer Affairs has compiled a list of instances where, while Government regulation may provide

⁴⁶ *Market Self Regulation*, above n 30, I,(Foreword).

effective overarching controls on market behaviour, self-regulation may provide a more efficient outcome. These instances are:⁴⁷

- (i) Where only a segment of the market is affected and over arching Government legislation is unlikely to occur.
- (ii) Where the objective is to promote compliance with over arching Government regulation within a particular market sector, for example the Securities Commission has developed regulations to ensure that the Securities Act 1978 is complied with.
- (iii) Within a particular market sector there is widespread acknowledgement of the need for and commitment to, the development of controls to improve trading standards. For example trade associations such as builder's guilds.
- (iv) The objective is to provide customer focused benefits beyond the minimum standards provided by the law. For example a code of practice.

To begin to understand what the policy considerations might be with respect to protecting consumers trading on line. I will look at the features of the Internet and how the Internet is used today.

IV. THE ONLINE ENVIRONMENT

A The Architecture of the Internet

The Internet is an open platform, network of computers. It allows geographically diverse entities to communicate and transact almost instantaneously. The architecture of the Internet provides opportunity for great gains in efficiency in global markets but it also poses problems for consumers.

Communication over the Internet occurs by the message being broken up into packets and reassembled. Special Internet protocols are attached to each part of the message which tags where the message is to be sent and in what order it is to

⁴⁷ *Market Self Regulation*, above n 30.

be recompiled. The message then gets sent either over a network of wire or transmitted using wireless technology. The message can be sent through various parts of the network, through one of potentially millions of alternative routes that can carry a message anywhere in the world that is also connected to the Internet. There is no centralised system that the message has to go through, the Internet is decentralised.

No one person or country is responsible for maintaining and monitoring the whole of the Internet. Potentially anyone who has access to the relevant technology can use the Internet. Portals to the Internet are becoming more diverse and now the Internet can be accessed without the need for a person to own a computer. Mobile phones, cyber cafes and kiosks may also be used to access the Internet and the number of devices is increasing all the time.

Because of the architecture of the Internet there are many potential benefits to consumers and the economy, for example:

- Benefits of Internet*
- (i) The decentralised nature of the Internet gives consumers easy and cost-effective access to the global market. This gives consumers greater choice of products, price and quality, including greater customisation of products to suit the consumer's preferences;
 - (ii) Due to the speed of communication, companies can lower inventory levels, shorten supply times, simplify the order process, and shorten product cycles. The consumer will reap the benefits of these lower costs through lower prices;
 - (iii) Consumers will be able to access the suppliers directly without the need for intermediaries;
 - (iv) Lower transaction costs, greater access to information and potentially more competitors due to lower barriers to entry will move the market closer to perfect competition;
 - (v) The opportunities for customisation and the variety of products and services which may be offered at a lower cost may increase global productivity and economic growth;

- (vi) The Internet may enhance welfare because of easier access to information, greater convenience and greater specificity of products; and
- (vii) The decentralised nature of the Internet encourages innovation and maximises personal freedom.

The more people and businesses that use the Internet the more valuable the Internet will be to the other users. As a community of users develop that can share information and enter into transactions with each other, more opportunities are created to transact and share information. This results in an exponential growth in value that is called "the network effect". However more people using the Internet consequently increases the risks to those that use it. The architecture of the Internet that provides the benefits also provides opportunities for problems for consumers in particular. Because of the architecture of the Internet and the uncertainty how the existing law will apply to Internet transactions Consumers may find that they are exposed to new risks when they enter into transactions on line.

(a) The integrity of the network

There are at least two possible issues which consumers may face due to the Internet's diverse routing, lack of centralised control and the open platform. The first is that it gives hackers the opportunity to intercept information sent over the Internet. It has been reported that actual credit card fraud has increased since the increase in popularity of the Internet.⁴⁸ However the reason has not been breach of network security as credit card numbers are being obtained by traditional methods. It is the unauthorised use of credit card numbers over the Internet that is increasing fraud.

⁴⁸ Consumers should not be overly concerned with credit card fraud, currently at least. When an unauthorised transaction occurs the bank first tries to recover the money back from the merchant, if the merchant cannot repay the money the bank will take the loss.. The consumer can also ask for amounts to be charged back to their credit card where a merchant has failed to deliver goods which have been paid for in advance. (This approach is not consistent with that of eftpos transaction and PIN numbers).

The second issue is that because the network is so vast the quality of all the parts of the network, (for example, servers, telephone line infrastructure and switches) cannot be guaranteed. This may cause connection delays, failures or the opportunity for security of the communication to be breached. This may impact on the timing of receipt of critical information such as; information on investments, acceptance and withdrawal of acceptance of an offer.

✓ (b) Anonymity

This potentially has issues for consumers when contracting on line with vendors, currently consumers cannot easily confirm:

- (a) the existence of the party they are contracting with;
- (b) any relevant qualifications or licenses which may be necessary to engage in a particular transaction;
- (c) the nationality of the entity they are contracting with; or
- (d) whether the vendor has the capacity to contract.

In the physical world a consumer can apply their own personal criteria to assess whether the service provider is legitimate. Consumers may also be able to identify a person in the future to provide evidence of that person's identity should any action be brought against that person for fraud. There is more incentive on people to be honest in the physical world when they can be identified, even if it only through forensic evidence, that is, social norms may not be such a strong regulator in cyberspace.

In summary the issues are related to identity and jurisdiction. Consumers who cannot identify the party with whom they have contracted will not be able to enforce the contract. In some jurisdictions, New Zealand being one of them, there may be a prohibition on particular entities entering into certain transactions. For example, in New Zealand minors cannot enter into contracts and only certain licensed entities may sell particular goods or services.

(c) Flexibility

Flexibility may be an issue for consumers from an evidential perspective in so far as transacting on the Internet is concerned. A vendor is able to change the information on web pages as and when it pleases therefore a consumer will have to ensure they print a copy of the information they are relying on when entering into a transaction on line. Examples of the types of information that may be necessary to print are the terms and conditions of any contracts that the vendor will be bound by and any statements made regarding the quality of goods and services to be supplied.

(d) Hyperlinks

Hyperlinks are an example of a tool that vendors may use when constructing their web sites. Hyperlinks can be used within a document, web site or between web sites. They can be useful in that they provide rapid cross-referencing but they may potentially provide the consumer with problems. Improper use of hyperlinks may give the appearance of legitimacy to otherwise non-legitimate information. Put simply, the existence of a hyperlink may be construed to imply an endorsement by the owner of the site that the illegitimate site is hyperlinking.

(e) Interactivity

Interactive web sites that contain, for example, options to pay electronically or send an order to trade shares allow consumers to effect a transaction instantaneously. Such an environment, however, could increase the temptation for a consumer to react impulsively and make less reactive investment or purchasing decisions. It maybe that such actions could cause market over reactions or worse a market failure. In the physical world this may still be an issue but in cyberspace information can travel more widely and more quickly and therefore the effects of that information will be more widespread and occur more quickly.

(f) Privacy

The Internet makes it very easy to collect, store and manipulate information about consumers. While this may have some benefit to the consumer, the

technology is such that the consumer will often never know information is being cached. This subverts the consumer's ability to regulate the use of information about themselves.

(g) Control of the architecture

Lessig has identified that consumers (and the public in general), may encounter issues with the Internet, because they do not understand the impact of the Architecture on them. Code writers can manipulate consumers and digital environment.⁴⁹

The first is limited access to intellectual property. This problem is an example of how technology may be used to alter the range of products available to consumers. The idea is that if each of the rights attaching to a piece of intellectual property could be unbundled then each piece could be sold separately. For example if a book was sold it could be sold to read once only, it could be sold to read an unlimited number of times but so that it could not be lent to anyone else, or it could be sold with all rights attaching to it. This may of course have some advantages to consumers as they will only need to purchase (and pay for) the rights the consumer values. However Lessig is concerned that the benefit of all ideas will be protected beyond that which is allowed at law, therefore reducing the benefits to society.

The second issue is where the code writer assumes sovereignty. Lessig likens code constraints to contracts; "The code writer operates free of the implicit limitations of contract law, he or she can construct an alternative regime for enforcing voluntary constraints."⁵⁰

Lessig's point is that in real space the enforcement of a contract is determined either by agreement between the parties or by a court. In cyberspace the code writer can use code to enforce the terms of the contract whether or not they would be found to be enforceable at law. The consumer will have no opportunity

⁴⁹ Lawrence Lessig, above n38.

⁵⁰ Lawrence Lessig, above n 38, 529.

to question the enforcement. Public values will then not have an opportunity to enter the mix as they do when legislation is being passed or when an issue is considered by the courts.

B Internet Usage

Generally the Internet can be used to collect information, communicate with friends, colleagues and customers and to enter into transactions. The Ministry of Consumer Affairs completed a status report on electronic commerce and the New Zealand Consumer in March 2000.⁵¹ The Report shows that New Zealanders have spent NZ\$242 million on Internet shopping in the past year.⁵² It is predicted that by 2004 New Zealanders will spend US\$2.7 billion on business and personal transactions, with the Internet user population growing from 393,000 as at January 2000, to 1.9 million in 2004. Statistics published on 10 February 2000 by the International Data Corp (IDC) predicted that by the end of 2000 the number of users would be 1.14 million⁵³ (this figure has subsequently been revised down to under 1million).

The Australian Bureau of Statistics published a report in 1999 which reported that the majority of items purchased on line were books, magazines, computer software, music and tickets. The Australian Bureau of Statistics in 2000 has quoted that the number of business to consumer (B2C) transactions are purchases of less than \$300.00.⁵⁴ This may suggest that consumers do not yet trust the medium for high value transactions. I have found no further evidence however that this is because of the Internet specifically, it may be that mail order transactions and other forms of distance selling are also restricted to relatively

⁵¹ Ministry of Consumer Affairs, *Electronic Commerce and the New Zealand Consumer, A Status Report and a Proposed New Zealand Model Code for Consumer Protection in Electronic Commerce*, (Wellington, March 2000), [Electronic Commerce and the New Zealand Consumer].

⁵² Figures from IDC NZ as reported in the Dominion 11.01.00.

⁵³ http://cyberatlas.internet.com/big_picture/geographics/art.../0,1323,5911_302481,00.htm
26/06/2000.

⁵⁴ *Electronic Commerce and the New Zealand Consumer*, above n51, 2.

low value transactions. It may also be a function of human behaviour, consumers may like to experience expensive goods they wish to purchase by way of touch or inspection. The impact of social norms on consumer behaviour needs to be assessed before any definitive conclusions on this point can be drawn.

The OECD has also looked at Internet Usage (see Appendix B).⁵⁵ In summary, what the OECD has found is that there is rapid growth in the use of the Internet transactions, doubling the value of transactions every 12-18 months. Most of the activity is taking place between businesses (B2B) (approximately 70-85% of all business transacted is B2B according to OECD research). It is suggested in this paper that this is due to shift by companies to on line supply chain management with suppliers that they had an existing relationship with in the physical world.

The statistics contained in Table 2 in Appendix B, show that apart from the United States only 10% of Internet users make purchases over the Internet and these are typically small value transactions. In certain sectors the evidence shows that e-commerce sales have achieved significant penetration. The OECD quotes that one quarter of all share transactions in the United States occur on line. Appendix B, Table 3 shows the distribution of e-commerce penetration by product as recorded by the Boston Consulting Group.

This evidence indicates that the use of the Internet as a place to transact is growing at least in markets for intangible goods and low value items.

C The impact of the Internet

The OECD has considers the economic impact of the Internet is as follows:⁵⁶

1. On price

The Internet will widely improve efficiency due to reduced transaction and search costs, increased competition and more streamlined business approaches.

⁵⁵ Johnathan Coppel, *E-Commerce:Impacts and Policy Challenges* Economics Department: Working Papers NO. 252, (OECD, 2000).

⁵⁶ Johnathan Coppel, above n55, 5-10.

There is some empirical evidence that currently prices for books and CDs sold over the Internet is lower than the physical world.⁵⁷ The Internet reduces the cost of changing ticket prices (there are no physical materials required to change the price) as the Internet is a flexible medium. There are no 'shoe leather costs' to the consumer to collect information about other competing products and service on line. The retailers may also have a better understanding of their customers which means that direct marketing and mass customisation of products is possible which may lead to more differentiation and more narrowly defined markets.⁵⁸ It is suggested that if prices are based on an individual's own valuation of the product or service that there may be several prices for the same product or service. The greatest possibility for a change in a market is for those products and services that can be digitised as the production and delivery costs will be greatly minimised.

2. On competition and policy

The minimisation of reproduction costs may also be an argument for a reduction in competition in a market for goods and services that can be digitised. Firms operating in such a market will need to find a way of recovering their cost of producing the first item(s) produced. There may be issues for competition where Internet operators are large and create an established brand in the physical world. This may enable suppliers to under cut their competitors on the Internet to build market share and at the same time gain the trust of consumers. What may happen is that due to issues of 'trust management' which arise due to the

⁵⁷ Johnathan Coppel, above n55, 14. This is based on research by Brynjolfsson and Smith, 1999. It is suggested that this may be because on line traders are facing a competitive market (evidenced by the number of Internet start-ups trading at a loss). There is a race to grow market share and brand identification.

⁵⁸ Cookies for example gather information about the consumer's Internet habits without the consumer even knowing. A supplier can use that information to establish the interests and tastes of the consumer.

peculiarities of the Internet, consumers begin to trust a particular brand and will only purchase from established brands.

On the other side of the competition argument is that the Internet offers a low barrier to entry market place due to the open and interoperable standards of the Internet, and therefore it may be difficult for one player to dominate the market.

Technology may also advance so consumers, with the help of electronic agents that can navigate the Internet looking for particular triggers, for example a particular price, may reduce search costs to the consumer effectively shifting the power from the vendor to the consumer.

3. Economic performance and macroeconomic policy.

I will not go into this point in detail, as it does not directly impact on consumers entering into transactions but needs to be considered, as the decision to regulate will need to consider the wider macroeconomic effects. There may be an issue for New Zealand in attracting investment in local operations by our own citizens as New Zealanders may choose to invest in foreign companies due to the accessibility of the markets and of information about the markets. These factors will impact on the Government's decision on whether or not to harmonise laws with New Zealand's trade competitors.

V. GOALS FOR REGULATING ON LINE TRANSACTIONS

The Government has found it necessary to protect consumers from market failures in the physical world. The evidence shows that similar market failures could occur in cyber space. The increase in the popularity of the Internet and its use as a method of exchange, has prompted the Government to decide to regulate for transactions that occur on the Internet because the existing regulation may not be effective to protect consumers transacting on line.

I have identified above that there are simultaneous benefits and issues for consumers that use the Internet to purchase goods and services. The consumer is

at particular risk of falling victim to the peculiarities of the Internet for many of the same reasons they are exposed to risk in the physical world. Of particular concern currently, is that consumers transacting on line, may inadvertently transact in another jurisdiction where the laws of New Zealand do not apply and that consumers may transact with an entity whose identity they are not certain. These, and the other issues identified earlier in this paper are of concern to consumers in particular because consumers may not appreciate the risks involved due to lack of understanding of the technology, and lack of experience and understanding of the issues that the new environment raises. Further even if consumers are aware of the issues they may incur high transaction costs if they need to enforce and identify their rights in another jurisdiction or under another state's law. This will not fit with the Government's policy of reducing transaction costs to consumers.

These issues and more have come to the attention of the New Zealand Government. In October 1999 the Ministry of Consumer Affairs took part in an International Internet Sweep Day to assess how Internet shopping sites protect customers' interests.⁵⁹ Over 700 sites were visited. Of those 700 sites:

- (i) More than half failed to outline their payment security mechanisms;
- (ii) 62% provided no refund or exchange policies,
- (iii) 75% have no privacy policy;
- (iv) 78% failed to explain how to lodge a complaint;
- (v) 90% failed to advise customers what laws applied to their transactions; and
- (vi) 25% failed to show a physical address.

The Ministry of Consumer Affairs considers that something must be done to address these concerns and to protect consumers trading on line.⁶⁰ The

⁵⁹ *Electronic Commerce and The New Zealand Consumer*, above n51, 3.

⁶⁰ *Electronic Commerce and the New Zealand Consumer*, above n51, 3.

Government has decided that there is an issue of consumer protection that needs to be addressed with respect to Internet transactions. Before any tools for regulation can be considered, the policy and goals of the Government need to be identified.

The Internet does not change the policy goals of the Government. The policy is restated by, the then Ministry of Commerce in its publication, *The Freezer Ship of the 21st Century*.⁶¹ That is, the economic policy in New Zealand of minimal regulation on the basis that voluntary transaction increase market efficiency, which in turn maximises welfare of society, and will influence the choice of tools the Government chooses to regulate on line transactions.

Additionally there is no reason why the particular policy of the Ministry of Consumer Affairs needs to change because of the Internet. That is, consumers benefit from efficient markets, and markets can be made more efficient by lowering transaction costs. As discussed earlier the Internet might even be able to assist consumers by reducing transaction costs.

The prevailing economic policy is not the only factor influencing regulation, before any action can be taken it is necessary to ascertain whether or not there are real or simply perceived problems with the Internet as a method of communication for trade.⁶² I have discussed potential issues at a qualitative level above that arise due to the architecture of the Internet. I have also reproduced some empirical evidence which may assist in divining the real problems from the perceived problems, but it can only be taken as indicative because of the difficulty of measuring electronic commerce.⁶³

⁶¹ Ministry of Commerce, *The Freezer Ship of the 21st Century*, (Wellington, November 1998) [*Freezer Ship of the 21st Century*].

⁶² *Assessing the Costs and Benefits in Consumer policy Development*, above n28, 2.

⁶³ OECD, *Committee for Information, Computer and Communications Policy Measuring Electronic commerce*, (Paris, 1997), 5. In this report the OECD outlines the measurement hurdles which include defining electronic commerce, the speed of its growth and evolution, and the fact that often firms conduct both traditional and electronic commerce simultaneously.

Currently, low value transactions for digital products and services seem to be where consumers are comfortable transacting on the Internet, however electronic commerce is still embryonic, growth in electronic commerce transactions has been increasing by over 200% annually and technology is continually improving. It is difficult at this stage to ascertain why consumers are not using the Internet for more various transactions or for higher value transactions.

Despite the fact that it is difficult to measure and conclude that the reason that consumers are not entering into electronic transactions with the vigour that businesses are, it is safe to assume that the problems identified may cause a market failure and therefore, in terms of Government policy, it is justifiable to regulate.

The Government's regulatory objective is to encourage electronic commerce as evidenced by the following statements:

- (i) *The Korea – New Zealand Joint Statement on Electronic Commerce* states that; "this joint statement is intended to promote the development of electronic commerce in both countries..."
- (ii) "The global emergence of electronic commerce will have a major impact on the New Zealand economy. It is imperative that New Zealand meets the challenges and takes advantage of the opportunities presented by this new mode of business."⁶⁴

This goal is consistent with the goal of the OECD, United Nations and New Zealand's main trading partners, as is the particular goal relating to consumer protection, that is, to increase consumer confidence in electronic commerce.⁶⁵

⁶⁴ *The Freezer Ship of the 21st Century*, above n59, 8.

⁶⁵ *Electronic Commerce and the New Zealand Consumer*, 3-4, also noted in Ministry of Consumer Affairs, *Consumer Policy Overview and Current Issues*, (Wellington, November 1999), 2.

The Law Commission has suggested a set of principles that it considers are necessary to guide regulators when considering issues of electronic commerce.⁶⁶ Those principles are that any regulation should:

- (i) Allow people to choose the medium in which they wish to do business. (choice principle);
- (ii) Retain fundamental principles of contract and tort as far as possible. (adaptation principle);
- (iii) Be technologically neutral; to trade as 'trust management'.
- (iv) Ensure compatibility with our trading partners. (compatibility principle); and
- (v) Allow private sector leadership.⁶⁷

In submissions on the Report the Government and private sector have accepted the principles.⁶⁸

Having established that the Government's general policy of free market economics is unchanged by the Internet, and that the Government's objective is to increase consumer confidence in transacting on line in accordance with the principles suggested by the Law Commission. I consider below some of the tools the Government may use to regulate the problems of the Internet.

VI. TOOLS TO REGULATE THE ONLINE ENVIRONMENT

The Government will need to be cautious when regulating because the regulations will be ineffective if they cannot be enforced, and may reduce consumer confidence if the consumer is not aware that domestic law will not

⁶⁶ A *Guide for the Legal and Business Community*, above n40 ,13-18

⁶⁷ The fifth principal was added after submissions on the first report were made, New Zealand Law Commission, *A Basic Legal Framework*: R58, (Wellington, 1999) [A *Basic legal Framework*].

⁶⁸ *A Basic Legal Framework*, above n 67, Executive Summary.

always apply. A consumer will not be able to enforce any rights they are given at law if they cannot identify the party that has caused the loss or if the laws of New Zealand do not apply to the transaction. Problems of identity and geography are therefore currently the key and complex problems that need to be addressed by some form of regulation, whether or not it is within the control of the Government.

These problems arise due to the architecture of the Internet and are closely linked to consumer confidence. I am going to refer to the issue of managing consumer confidence in the Internet as a place to trade as 'trust management'.

The Architecture of the Internet is not the only barrier to trust management. In New Zealand and internationally existing laws have also been identified as reducing confidence in the Internet because of the uncertainty of how the existing law will apply to transactions concluded on line, if at all.

As the Government has decided to regulate to increase consumer confidence the Government needs to consider the tools it can use to achieve this, it may be that the existing tools are not enough to regulate the Internet, if they are not then thought will need to be given to alternatives.

A Are the existing tools sufficient?

1. Existing regulation incorporating existing tools

In New Zealand where consumers transact with other New Zealanders on web sites based in New Zealand any issues arising from the transaction will fall within the scope of any applicable consumer protection legislation already in place. Those laws are technologically neutral. However, New Zealand legislation may offer no assistance to the consumer who transacts with a foreign seller, nor will it assist a consumer if the consumer cannot identify the party with whom they are transacting.

2. *New regulation using existing tools*

(a) Harmonise domestic law

To address the potential increase in transaction costs to consumers which relate to the issues of multiple jurisdictions being involved in a transaction New Zealand may attempt to harmonise its own laws with that of other states. Enacting legislation that mirrors that of another state, in particular Australia, as our closest trading partner, may do this in part. This was done with the FTA and is being contemplated currently with respect to a proposed Electronic Transactions Bill.⁶⁹ However, the Internet is global and consumers are potentially able to transact with anyone in the world that uses the Internet, it would be very difficult to harmonise our law with that of every state in the world in this way.

New Zealand and Australia as members of The Ministerial Council of Consumer Affairs (MCCA)⁷⁰ have made a start towards harmonising jurisdictional dispute resolution issues as a result of electronic commerce. In August 1999 the MCCA adopted principles for dealing with cross-jurisdictional complaints involving electronic commerce between their jurisdictions. The Australian Competition and Consumer Commission is to determine the specific procedures for referral of complaints.⁷¹

(b) Prohibit access to foreign web sites

Another possible solution is for the Government to prevent consumers from entering into transactions that involve other jurisdictions by requiring that our international gateways are not made available to consumers. This suggestion would be unlikely to be accepted. It would have a negative impact on business to

⁶⁹ Ministry of Economic Development, *Electronic Transactions Bill, Discussion Paper*, (May 2000, Wellington). [Electronic Transactions Bill].

⁷⁰ The MCCA consists of the consumer affairs/ fair trading Ministers of the Commonwealth States and Territories in Australia and The New Zealand Minister of Consumer Affairs.

⁷¹ *Electronic Commerce and the New Zealand Consumer*, above n51, 9.

business transactions because there is currently no way an ISP would be able to identify whether traffic was legal or illegal. If the Government was serious about preventing global traffic they would need to ban consumer ISPs altogether and leave it to businesses that required an Internet connection, to purchase their own access to the international gateways for their own business purposes. I suggest that this would not be accepted by the New Zealand public, and would result in interest groups lobbying Government for change. Despite any other issues this solution may cause, it is not desirable because it is inconsistent with the Government's policy of increasing efficiency through voluntary markets. By restricting access to global markets one of the greatest benefits of the Internet to consumers would be lost.

(c) Multilateral Agreements

Of the existing tools the only response that will be effective is an international co-ordinated response. This response needs to utilise the principles established by the New Zealand Law Commission, in particular the response needs to be technologically neutral as technology moves fast and laws and international agreements in particular, move slowly. Technology specific regulation will also have the unwelcome effect of distorting innovation.⁷²

The Hague Conference has published a preliminary draft convention on jurisdiction and Foreign Judgments in Civil and Commercial Matters, adopted by the Special Commission on 30 October 1999. The draft convention is designed to include in its scope almost all civil and commercial matters.

Article 7 specifically provides for contracts concluded by consumers. A consumer is defined as a person who enters into a contract for purposes unrelated to their trade or profession. A consumer can bring an action in the country in which they live if the following conditions are met:

⁷² David Goddard, "Does the Internet Require New Norms?" International Law Forum, 2, 183-195 ["Does the Internet Require New Norms?"]

- (i) The conclusion of the contract relates to activities that the defendant (which will, for the purposes of this paper be a supplier) has engaged in the consumer's home state or which the supplier directs activities; and
- (ii) The consumer has taken necessary steps for the conclusion of the contract in their home state.

Similarly a claim can only be brought against a consumer in their home state.

A supplier cannot contract out of these rules, however they are only default rules because a consumer may request a clause in the contract, for the consumer's benefit only, for an alternative jurisdiction. The only other way an alternative state will have jurisdiction is if the parties agree it after the dispute has arisen.

This clause was drafted without taking into account issues of electronic commerce but it was discussed at the Hague Conference on Private International Law organised an expert meeting in Ottawa between 28 February 2000 and 1 March 2000.⁷³ At that meeting the draft convention as a whole was discussed in terms of electronic commerce. Issues with the current draft of the convention were identified at the meeting. The particular comments with respect to consumer protection are:

- (i) With respect to placing material on an Internet site the first condition will be met.
- (ii) The second condition is not a new issue as present day telecommunications allow a consumer to conclude a contract outside their habitual place of residence.
- (iii) The necessity of a business to bring an action against a consumer in the consumer's own jurisdiction may be onerous on the small Internet business (of which there will be many).

⁷³ Catherine Kessedjian, *Electronic Commerce and International Jurisdiction*, (Ottawa, 28 February to 1 March 2000).

- (iv) It has been suggested that a consumer who was fully informed of their rights could forgo the protection offered under clause 7 and opt instead for a choice of courts clause. The details of this were not recorded.

The Special Commission's debate made it clear that the trade off was between encouraging consumer confidence in the Internet and encouraging small enterprises to offer goods and services over the Internet.⁷⁴

Despite the issue of cross border transactions, the Government can still regulate for transactions that occur within New Zealand to increase efficiency where the existing law reduces confidence in electronic commerce. Existing tools can be used to do this also.

(d) Facilitating credible commitments

The Internet can decrease transaction costs to consumers who wish to purchase goods and services on line from domestic suppliers and because of this it is a valuable tool and should be encouraged. To this end the Government has produced a discussion paper which proposes a new Electronic Transactions Bill.⁷⁵ It is proposed the Bill would be based on the Australian Electronic Transactions Bill 1999, which is based on the UNCITRAL model law, and among other things would provide that agreements made electronically would not be unenforceable because they were agreed electronically. The Bill is based on the work of the Law Commission in its second report on Electronic Commerce.⁷⁶ It is considered imperative by the Law Commission that the legislation New Zealand enacts is aligned with Australia as our major trading partner.⁷⁷

⁷⁴ Electronic Commerce and International Jurisdiction, Ottawa, 28 February to 1 March 2000, summary of discussions, prepared by Catherine Kessedjian with the co-operation of the private international law team of the Ministry of Justice Canada.

⁷⁵ *Electronic Transactions Bill*, above n69.

⁷⁶ *Electronic Transactions Bill*, above n 69, 4.

⁷⁷ *A Basic Legal Framework*, above n 67, 10-14.

In the Law Commission's deliberations on the legal barriers to electronic commerce it concluded that the proposed Bill should apply equally to consumer transactions as it does to business transactions.⁷⁸ The Law Commission suggests that additional requirements may be necessary such as differentiating between provisions dealing with advertisements and those provisions that form part of the contract.

(e) Self regulation

Self regulation is currently the Government's preferred method of regulation. The Ministry of Consumer Affairs has drafted the New Zealand Model Code for Consumer Protection in Electronic Commerce since the Law Commission published its reports on electronic commerce. It fits with the 5th principle of regulation which was suggested by the Law Commission, that is that the private sector should lead the way in developing confidence in electronic commerce. It is based on the OECD's Guidelines for Consumer Protection in Electronic Commerce. The Code will be voluntary and is designed to underpin efforts by business to meet consumer's interests. The premise behind the guidelines is that:⁷⁹

Consumer laws, policies and practices limit fraudulent, misleading and unfair commercial conduct. Such protections are indispensable in building consumer confidence and establishing a more balanced relationship between businesses and consumers in commercial transactions.

The Code is a summary of the current legal obligations that business in New Zealand already has to comply with. However it goes further than that and provides a type of "best practice" of transacting on line, for example, clause 28 outlines the steps that a business should take to review a contract, accept or reject any errors and confirm or reject and offer.

⁷⁸ *A Basic Legal Framework*, above n 67, 50.

⁷⁹ *Electronic Commerce and the New Zealand Consumer*, above n51, 21.

Other suggestions for self regulation include seal of approval initiatives that are currently being considered by the International Marketing Standards authority.⁸⁰

(f) Education

Educating consumers on the risks of the Internet and what they can do to minimise the risks will be an important part of increasing consumer confidence. There are many steps that a consumer can take to protect themselves from some of the risks of trading on line, however before they can do anything they must be aware of the risks. Education can be used to address in part at least most of the issues that arise transacting on line.

(g) Market Regulation

Another option that the Government has is to do nothing and leave it for the consuming public to decide whether or not they will accept the risk of the transaction. Efficient markets can emerge without Government intervention where markets are competitive or it may happen with in combination with education and self regulation initiatives of the Government.

I suggest that market regulation combined with education could be used to address the issues that arise due to the control of the architecture of the Internet by code writers. Greenleaf points out that architecture can perish where market forces do not support it. In fact market forces may have much more force regulating cyberspace due to network effects. Greenleaf describes network effects as; "markets in which the value that consumers place on goods increases as others use the goods."⁸¹

Lessig is concerned that code may displace the values of public law. He uses the examples of Intellectual Property (which many commentators target as a

⁸⁰ *Electronic Commerce and the New Zealand Consumer*, above n51, 15.

⁸¹ Graham Greenleaf, above n 4, 10.

victim of Internet technology, not a benefactor) and contract which I have mentioned above.⁸²

Lessig makes the point that the law serves public values and thought should be given to a regime that tries to displace those values. The Government will need to consider whether or not it wants to regulate architecture, one of the new tools suggested below, to prevent this from occurring if market forces are not effective.

There is a real issue for consumers as self regulation by code writers is not transparent. The issue for consumers trading over the Internet is that they don't understand why they can only operate within a defined sphere. However if consumers do not like the restraints placed on them by one supplier they can "vote with their electrons" and shop elsewhere (assuming there are other satisfactory suppliers in the market).

It is also important to note that technology has a tendency to evolve to create technological solutions to issues to that technology raises. Competing technologies tend to cancel each other out over time.

B New Tools

The existing tools can be used to regulate domestically and internationally to some extent, however they are not the only possible ways to regulate. They do not address all of the issues, for example the existing tools will not be able to regulate to prove a person's identity. Below I discuss new tools and new ways of using existing tools that may be used to regulate business to consumer electronic commerce.

1. Law of Cyberspace

There has been much debate over how the issues raised by electronic commerce can best be resolved. Some commentators are of the view that a new law of the Internet could be developed that would be enforced within the new jurisdiction of

⁸² See part IV of this paper, The Online Environment.

cyberspace. Matthew Burnstein draws the analogy of the law merchant with the proposed new law cyberspace.⁸³ This would involve creating new norms, such as the law of Internet Torts. Other commentators, including the New Zealand Law Commission, consider that the existing laws are satisfactory and that there is no need for a Law Cyberspace.⁸⁴ To develop a Law Internet would be contrary to the suggested adaptation principle of the Law Commission.

2. ISP contracts

Another suggestion is that ISPs enter into agreements with each other and consumers will then be subject to the dispute resolution, jurisdiction and choice of law terms their chosen ISP has agreed with other ISPs.⁸⁵ Burnstein's argument is that as all users must go through an ISP to get on line, the contract between ISPs could act as the equivalent of treaties among nations, the ISP could be both the legislator and the enforcer.⁸⁶ I do not consider this to be a very efficient solution to the problem for the following reasons:

- (i) ISPs currently do not have to enter into agreements with each other, they do not need to due to the open platform of the Internet. This would be an additional cost that would be passed on to the consumer. If this logic was followed it may be more appropriate to put this obligation on the telecommunications network suppliers which already negotiate interconnect agreements with each other (however this would not avoid the other issues below).

⁸³ Matthew Burnstein, "The Internet and Territoriality" in K. Boele-Woelki and Kessedjian (eds), *Internet- Which Court Decides? Which Law Applies?, Quel tribunal decide? Quel droits s'applique?* (Kluwer Law International, The Hague, 1998), 23-34.

⁸⁴ "Does the Internet Require New Norms?" above n 72, and *A Basic Legal Framework*, above n 67, Executive Summary.

⁸⁵ Matthew Burnstein, above n 84.

⁸⁶ Matthew Burnstein, above n 84, 32.

- (ii) There are potentially many more ISPs than there are countries so the number of agreements that would need to be entered into would be large, and negotiations would be continuing as new ISPs are and will be being established somewhere in the world all the time. This would mean that the cost would be high and interim solutions would still need to be developed while the negotiations were taking place.
- (iii) Most ISPs, especially in New Zealand are small compared to those in other jurisdictions, New Zealand may end up a “cyber ghetto”, where New Zealand consumers would be subjected to foreign jurisdiction in most cross border trades, resulting in a low level of consumer confidence contrary to the aims of the Government;
- (iv) In the past businesses have not needed to use an ISP to access the Internet therefore there will be businesses that do not use an ISP. (Telecommunications companies sell businesses access to New Zealand’s international gateways directly, they still do but a business will still need an ISP to be allocated IP numbers); and most importantly
- (v) Consumers can use many different ISPs without even knowing it. A consumer may use a different ISP at work, at home, on their mobile phone or if they use a cyber café, kiosk or another person’s computer. A consumer will often not know which ISP they are using and will be even less likely to know what the terms of that ISP’s contract are with the ISP which they are accessing somewhere else in the world.

3. Regulate the Architecture

The issue of identity is more difficult to resolve by legislation because the ability to identify a party to a transaction is a problem that arises from the architecture of the Internet not the law. The problem has an impact on the law in that the consumer will not be able to enforce their rights against an unknown party. Lawrence Lessig suggests that by regulating architecture the Government may be able to solve this problem, resolve the issues around privacy, and of control of the code by code writers. Architecture in the physical world has not been able to

be regulated in the same way because not even the Government can regulate for nature as it is not plastic. No law can stop river running through a town or rain from falling. The architecture of the Internet however is different, it is created by people and therefore potentially able to be regulated.

While Lessig does not believe that any regulation of the Internet is necessary, he agrees that if a government regulates it should ensure the regulations are enforceable.⁸⁷ Lessig states that a government (in his case the United States of America) can "alter the regulability of the Internet."⁸⁸ The most effective way to do this is through regulating code.

Lessig suggests that architecture may be regulated by:⁸⁹

- (i) Making identity self authenticating by modifying the Internet's code so that when a person connects to a web site information gets sent to the site.
- (ii) Creating legal incentives for code writers to give effect to consumer's (and the public's) rights.

Lessig suggests that identity could be self authenticating by authenticating the browser or the IP address of the computer from which the consumer connects to the site. Both of these suggestions are flawed however as they assume that a computer's IP Address is static and that a browser is personal and "detachable". A browser is software which is loaded onto a particular computer. Therefore the suggested solution is unhelpful for those without their own computer, for people that share a computer and for people that travel and use computers at cyber cafes or elsewhere. It also requires that the developers of the web site programme their servers to react appropriately according to the information that the browser or address delivers to it. Without this architecture suggested by Lessig will not be helpful. Additionally, It does not address the issue raised by the Global nature of the Internet as no doubt havens will develop where organisations can locate their

⁸⁷ Lawrence Lessig, above n 38, 517.

⁸⁸ Lawrence Lessig, above n 38, 514.

⁸⁹ Lawrence Lessig, above n 38 514- 52.

servers so they do not have to comply with any particular regulation. This would be of more assistance to suppliers rather than consumers as consumers will be interacting with a web site which would not necessarily contain any feature which would allow the consumer to authenticate the supplier.

However I am not suggesting it is impossible to do, but maybe a better way is through digital certificates and PKI infrastructure. The electronic signature is one method of trust management. Electronic signatures are currently receiving a lot of attention from the legislative and advisory bodies around the globe. There are multiple types of electronic signatures but the type that most countries that are addressing this issue are either adopting or discussing is known as asymmetric key cryptography. Using this approach one key is used to create a document (private key) and another key, which is published or made available to particular parties, is made to verify the signature ("public key"). This form of electronic signature is defined in Singapore's Electronic Transactions Act 1999 as a Digital Signature. Each digital signature is unique to the document it is attached to and if the document is altered the digital signature is also altered.

For Digital Signatures to be effective with respect to "trust management" several steps need to be taken:

- (1) Private keys must be issued or designed
- (2) Each private key must be unique
- (3) The identity of the authorised user must be guaranteed.
- (4) Private Keys must not be able to be interfered with, they must have integrity
- (5) Any private keys that are compromised must be able to be revoked
- (6) Public keys must be made available
- (7) Public keys must not be able to compromise the integrity of a private key

The second initiative suggested by Lessig is to provide legal incentives to allow individuals to select preferences. This is a suggested as a way to increase

privacy on the Internet. Lessig identifies that the problem of the Internet is that the architecture is such that it interferes with regulation imposed by individuals (self regulation). Greenleaf explains that this is due to a combination of factors but particularly that the default regulation of the Internet architecture is on, that is computers are set to accept cookies, and in older computers at least, the software doesn't allow the user to turn this function off. Lessig, writing on the situation in the United States, suggests that the answer to this issue first requires the Government to establish some form of incentive for web site developers to request consent of consumers before they collect information from them. In New Zealand the Privacy Act 1993 already creates the incentive and we have not seen many web based suppliers offering consumers options for collection of personal information.

Technical solutions have been developed for example P3P. P3P allows individuals to select their preferences about the exchange of private information and then an electronic agent will negotiate the trade of such data when the individual connects to any given site. This technology is still available to consumers without the intervention of the Government and can be adopted by consumers so they can continue to self regulate for the dissemination of information about themselves.

I suggest that if the market demands tools such as P3P they will be invented and consumers will be able to choose whether or not they want to use them. There may however need to be a requirement that web site owners have to accept that they cannot circumvent the architecture.

Regulation of architecture might work to increase the ability of a government to regulate cyberspace within its borders to some extent. The mandatory use of PKI technology would potentially give the Government a lot of control over the Internet. It may even get to the stage that known fraudsters would be denied an electronic signature and therefore denied the opportunity from participating in Internet transactions (whether or not the public will accept this is another issue).

VII. CONCLUSION

The Government has identified that the Internet should be encouraged because of its potential to increase market efficiency. This is consistent with the Government's pre existing policy for regulation. However the Government has also identified the Internet creates problems for consumers which will need to be addressed if consumer confidence in the Internet is to increase. In particular the issues arising from anonymity are critical issues relating to the effectiveness of any regulatory efforts.

The Government's existing consumer protection tools and regulations will continue to be effective in so far as transactions are completed within New Zealand's jurisdictional borders. However to the extent they are not effective international initiatives will need to be invoked such the draft Hague Convention on Jurisdiction and foreign judgments in Civil and Commercial matters. Treaties are an appealing method of Internet governance. Nations are accustomed to negotiating treaties and may be prepared to consider them more readily than dramatic and confusing technological solutions. Treaties are also appealing because they may be brokered by international organisations.

Where the Government can regulate to increase efficiency domestically it can still do so, it will need to be careful however not to lull consumers into a false sense of security where those regulations will not be enforced outside New Zealand.

However government regulation causes its own difficulties, as it is relatively inflexible and slow to adapt to change (the new issues that have arisen, as a result of electronic commerce are evidence of that). Additional issues with government regulation include:

- (i) Government agencies may lack information themselves;
- (ii) the direct cost of developing and enforcing the regulations are high and borne by all taxpayers (even those that don't require protection due to their own personal attributes);
- (iii) the cost of complying and implementing regulation can be high;

- (iv) government regulation sets a minimum standard only;
- (v) government regulation is risks being indiscriminate;
- (vi) the cost of regulation should fall only on those markets which the regulation is targeted.

Therefore one option that a government has is to do nothing or, require that the industry regulates itself.

If the market can address the potential market failure or unfairness itself there will be good reason for the Government to leave resolution of the problem to market regulation. If not the Government may have to consider new tools for the regulation of electronic commerce, for example regulating the Architecture of the Internet.

It will be important for the growth of electronic commerce to achieve a resolution of the issues around conflict of laws, jurisdiction and identity. Without this transaction costs will be high and the benefits of electronic commerce to will not be fully harnessed by consumers. Any change to New Zealand's domestic law to facilitate electronic commerce will only go part of the way to increase consumer confidence. It will still not allow consumers to benefit from the global nature of the Internet, which is the Internet's primary benefit.

VIII. APPENDIX A

In relation to the supply of goods the CGA implies guarantees:

- (i) as to title,
- (ii) acceptable quality (whether or not goods are of acceptable quality is determined in accordance with section 7 as determined from the perspective of a reasonable consumer),
- (iii) as to fitness for particular purpose (unless it can be shown that the consumer does not rely on the suppliers' skill or judgement or it would be unreasonable for the consumer to do so.),
- (iv) that goods comply with description,
- (v) that goods will correspond with the sample and the customer will be given an opportunity to compare goods to with the sample,
- (vi) as to reasonable price (other than where the price is determined by contract),
- (vii) as to repairs and spare parts (where goods are first supplied to a consumer in New Zealand the manufacturer will take reasonable steps to ensure that facilities to repair the goods are available for a reasonable period after the supply).

The CGA also grants the following guarantees to the provision services:⁹⁰

- (i) As to use of reasonable skill and care,
- (ii) As to fitness for a particular purpose,
- (iii) As to completion within a reasonable time
- (iv) As to a reasonable price

⁹⁰Consumer Guarantees Act 1993, sections 28-31.

IX. APPENDIX B

A Table 1

Table 2. Consultant estimates of world-wide e-commerce

	1999 Billions \$	2003	Average annual growth
e-Marketer	98.4	1 244	89
IDC	111.4	1 317	85
ActivMedia	95	1 324	93
Forrester Low ^a	70	1 800	125
Forrester High ^a	170	3 200	108
Boston Consulting Group	1 000	4 600	46

a) includes Internet-based EDI.

Source: Cited in e-Marketer (2000) and Boston Consulting Group (1999b).

B Table 2

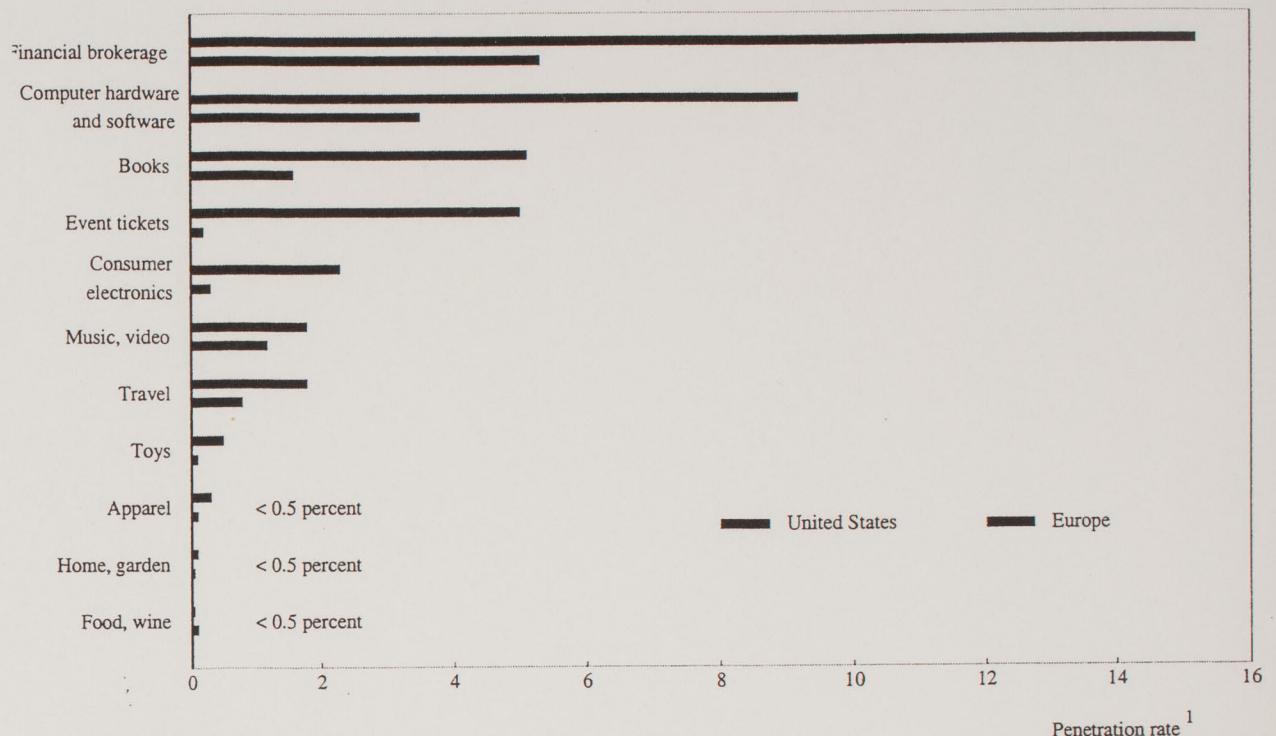
Table 3. B2C e-commerce in selected OECD countries

	Value of transactions - 1999, \$US million	Value of transactions - growth rate (1999/98)	Penetration rate, per cent of retail sales	Number of buyers, thousand, end 1998	Number of buyers, as a per cent of Internet users	Number of buyers, as a per cent of working age population
United States	24 170	195	0.48	19 666	39	11.1
Japan	1 648	334	0.06	..	..	..
Germany	1 199	200	0.30	1 370	13	2.4
France	345	215	0.14	310	8	0.8
Italy	194	145	0.09	360	12	0.9
United Kingdom	1 040	280	0.37	970	11	2.5
Canada	774	166	0.26	811	12	4.0
Australia	..	..	..	803	13	6.4
Austria	96	210	0.23	120	13	2.2
Belgium	82	420	0.16	90	11	1.3
Denmark	46	220	0.20	90	8	2.5
Finland	51	160	0.22	160	10	4.7
Greece	..	..	..	30	11	0.4
Ireland	..	..	..	40	13	1.6
Netherlands	182	210	0.34	320	13	3.0
Norway	61	200	0.26	100	10	3.5
Portugal	70	185	0.06	50	11	0.7
Spain	70	185	0.06	220	11	0.9
Sweden	232	170	0.68	260	10	4.6
Switzerland	127	110	0.29	130	12	2.7

Sources: OECD Secretariat; Boston Consulting Group; Warburg Dillon Read; Retail Council of Canada; MITI (Japan); and Australian Bureau of Statistics.

C Table 3

Figure 4. E-commerce penetration by product, 1999



1. As a percent of sales.
Source: Boston Consulting Group (1999a).

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