

Truth-In-Advertising Law: New Zealand's Experience

Grant Hannis

New Zealand's Fair Trading Act is the country's truth-in-advertising law. It is an important piece of legislation, forming an integral part of the government's pro-competitive economic policy. The Act is pervasive, applying not only to transactions between consumers and businesses but also to business-to-business dealing. The penalties for breaching the Act can be severe. Large fines and compensation orders have been imposed, and a firm that breaches the Act can expect to see its transgressions publicised in the media, damaging a reputation that the firm may have taken many years and considerable expense to establish.

Given the importance of the Act in New Zealand's economic landscape, it is worthwhile investigating the economic impact of the law. The Act was passed in 1986, and since then a considerable body of case law has developed. This article considers that case law in light of the economic theoretical debate over truth-in-advertising legislation. The first section summarises the Act. The following section considers the statute's objectives and the economic theoretical debate. Case law under the Act for the ten years ending May 2000 is then reviewed. Lastly, the general conclusions are presented.

Summary of the Act

Under Section 9 of the Fair Trading Act, no person in trade can engage in 'conduct that is misleading or deceptive or is likely to mislead or deceive.' In addition to this general prohibition, certain false or misleading representations are specifically banned. For instance, Sections 10, 11 and 13 prohibit false representations about the attributes of products. For example, traders cannot give false representations about the quality, origin, or price of products. Similarly, Section 14 prohibits specific false representations regarding the sale, or grant, of an interest in land. These provisions have the effect of requiring truth-in-advertising. They also ban any other form of misrepresentation traders may make to consumers (for instance, a misrepresentation made by a salesperson during a conversation with an individual consumer). Although often thought of solely as a consumer protection law, the Act also prevents traders from making misrepresentations to other traders.

Other sections in Part I of the Act prohibit certain unfair business practices. For example, Section 24 prohibits pyramid selling, which is where a network of

Grant Hannis is an Economist at the Consumers' Institute of New Zealand.

people sells products for reward, with the primary method of making money being the recruitment of others to the network. Pyramid selling has little chance of financial success — the market for new recruits is soon saturated, so most people who join pyramid selling schemes lose money.

The Act contains several other provisions, including the requirement for three consumer information standards and five product safety standards. As we are primarily interested in the Act insofar as it promotes truth-in-advertising, these other provisions are not germane to our discussion and are not considered further.

The Fair Trading Act is enforced by the Commerce Commission, a government agency. As well as prosecuting, the Commission can enter into agreements and settlements with traders it believes are engaging in practices that breach the Act. Typically, under these agreements an offending trader must cease the practice, undertake remedial action (such as placing advertising to correct misleading impressions) and introduce a compliance programme to avoid breaching the Act in future. On average, in the five years ending 2000, for every Commission court case completed, the Commission issued nine warnings and entered into two settlements with traders (Commerce Commission, 1996-2000).

The Commission is also required to ensure traders are aware of their obligations under the Act. For example, the Commission produces guidelines for traders and publicises its prosecutions, warnings and settlements (Commerce Commission publications may be accessed at www.comcom.govt.nz/publications).

Consumers and traders can take their own prosecutions under the Act. A member of the Commerce Commission (Harrison, 1997:61) has observed that allowing such private action reduces the cost of enforcing the Act:

The Commerce Commission has the job of policing the Fair Trading Act, but its resources are limited. Accordingly, it cannot hope to prosecute more than a fraction of alleged infringements. By empowering private individuals or corporations to take enforcement action, the Act vastly extends its 'reach'.

Consumerists also support this aspect of the law. David Russell, Chief Executive of Consumers' Institute a New Zealand consumerist organisation which publishes *Consumer* magazine (the Australian equivalents are the Australian Consumers' Association and *Choice* magazine), sees trader-to-trader cases under the Act as having an important benefit for consumers (Russell, 1997:80):

If one trader believes that another is behaving in a misleading or deceptive way and successfully pursues a case through the courts, then consumers are protected by the stopping of the complained-about practice.

Civil and criminal penalties can be imposed for contraventions of the Act. Only civil penalties apply if a trader breaches the general prohibition against misleading or deceptive conduct. The court can, for example, grant an injunction

to stop the practice, order the placement of corrective advertising and order compensation to be paid.

If a person contravenes other provisions of the Act, criminal penalties can also apply. The courts can impose fines of up to \$100,000 per offence for companies and \$30,000 per offence for individuals, plus costs (all dollar amounts in this article are New Zealand dollars). Under Section 39, disputes tribunals (New Zealand's small claims courts) can hear all cases under the Act other than those under Section 9. But unlike the courts, the disputes tribunals cannot impose fines. They can merely direct an offender to refund money or return property to the person who has suffered a loss.

Generally, the Act applies even when there was no intention to breach the Act, but there are some exceptions. Most notably, if the breach was due to a reasonable mistake, or was due to reasons outside the person's control and the person had diligently taken reasonable precautions to avoid breaching the Act, a trader would not face criminal liability, but would continue to face civil liability.

Economic Theory of the Act

In the years immediately following the election of the Labour Government in 1984, many of the regulations that had long controlled the New Zealand economy were removed in an effort to make the economy more competitive (Silverstone, Bollard and Lattimore, 1996). The Fair Trading Act, passed in 1986, was part of that pro-competitive reform process. As the Minister of Consumer Affairs noted at the time, the Act 'complements other aspects of the Government's economic policies that promote effective competition in markets within New Zealand' (Shields, 1986).

The Fair Trading Act encourages the competitive process by promoting fairness in economic transactions, and by reducing consumers' search costs.

Promoting fairness

The Fair Trading Act is acutely concerned with issues of fairness. One need look no further than the Act's name to see proof of that.

The notion of fairness is deeply ingrained in society. Most parents teach their children about the importance of fair play, and in Australia and New Zealand the belief that everyone deserves a 'fair go' is regarded as a trait of the national character. In consumer markets, among other things, fairness can be taken to mean the information traders provide consumers must be truthful. That is, it is wrong to lie. It also means that outright fraudulent activity that preys on more vulnerable consumers should be banned. For instance, pyramid-selling schemes are banned because the schemes exploit less mathematically aware consumers, who do not realise that such schemes have no chance of success. A Commerce Commission representative has observed that, with pyramid-selling schemes, 'Only a small number of people at the top can ever make money, and that is by ripping-off the people below them' (Commerce Commission, 1999a).

Although some may think notions of fairness exist outside the sphere of pure economics, some economists have acknowledged the importance of fairness in economic policymaking. Governments cannot be blind to concerns over the fairness of economic transactions, it is held, as to do so could imperil a pro-competitive economic policy. As Viner (1960:68) observes:

No people will have a zeal for the free market unless it operates in a setting of distributive justice with which they are tolerably content.

Indeed, the historical context of the Fair Trading Act makes it clear that the Act seeks to legitimise market processes by ensuring markets behave fairly. The government believed the Act would provide ‘a fair deal for consumers’ and would be ‘a significant step on the way towards recognising that consumers often bear the brunt of any ill effects arising from traders’ efforts to pursue profit’ (Shields, 1985 and 1986). As well as protecting consumers, the government anticipated that the Act would ‘enhance the position of ethical traders in relation to the unfair competition that results from deceptive advertising and other conduct’ (Shields, 1985).

Reducing search costs

As well as promoting fairness, the Act seeks to reduce consumers’ search costs. Traders supply much of the information provided in the marketplace, and although advertising can offer consumers useful information about goods and services, there is always the suspicion the information is tainted. After all, advertising is typically designed to portray the trader in the best possible light. For instance, a well-regarded brand name on a product provides consumers with useful information on the likely performance of the product. A firm’s good reputation imparts similar benefits. But against this, consumers are often unable to check many of the claims made by traders. Few consumers will have the time to check a trader’s claim that their prices are ‘the best in town’. Moreover, consumers often do not understand the technical nature of many goods and services, and therefore may not be in a position to judge whether a traders’ claims about its products are accurate. For example, few consumers would be able to judge the veracity of the technical specifications a retailer gives about the computers they have for sale. Yet, if consumers are poorly informed, the market will not perform efficiently — producers will be able to exploit false product differentiation or sell goods at inflated prices (Martin and Smith, 1968; Ramsay, 1989).

The Fair Trading Act reduces the cost consumers incur checking the accuracy of the information provided by traders. That is, traders that disseminate misinformation risk prosecution, so traders have an incentive to provide only truthful information. Consumers do not have to check every claim made by traders, they can simply make a reasonable assumption that the claims are truthful. Even if a certain claim does turn out to be false, the consumer can seek redress

under the Act. By improving the level of information in the market, the Fair Trading Act promotes efficient market outcomes.

The government made it clear at the time the Act was passed that the objective of reducing consumers' search costs was as important as the fairness objective. The Minister of Consumer Affairs noted that the Act 'is designed to ensure that competition centres on the key areas of price, quality, and service, and that product comparisons are not distorted by misleading, deceptive, or unfair practices' (Shields, 1986).

Not all economists are convinced about the need for truth-in-advertising law to reduce consumers' search costs. Jordan and Rubin (1979) argue that few firms have an incentive to mislead. They claim there are only three essential types of goods (taken here to include services) — search, experience and credence goods. Search goods are those for which consumers can obtain sufficient information to make an informed buying decision prior to purchase (a pair of shoes for instance), an experience good is one that must be consumed to be evaluated (such as the taste of a chocolate bar), a credence good is one whose qualities cannot be measured by the consumer even after consumption (such as information in an encyclopaedia, which the consumer assumes is correct). Jordan and Rubin hold that suppliers of search goods have little incentive to use misleading advertising, as consumers will verify the quality of the goods before purchase. Suppliers of low-priced experience goods will have little incentive to mislead, as they will lose repeat custom. Suppliers of expensive experience goods have little incentive to mislead as they may face lawsuits that are expensive to defend and damaging to the traders' reputations. Suppliers of credence goods who have invested in a reputation stand to lose those reputations if they mislead, so they do not mislead.

The only suppliers likely to mislead, according to Jordan and Rubin, are suppliers who do not care about their reputations and brands, and sell either mid-priced experience goods or credence goods. In the former case, consumers are unlikely to sue if misled because the price of the good does not warrant the cost of litigation. In the latter case, traders are in the best position to mislead as consumers cannot verify the quality of the products.

Another criticism of truth-in-advertising law is that it is not necessary for all markets, as it is unnecessary for every consumer to be well informed for the market to operate competitively. If firms cannot differentiate consumers that search out information and those that don't, and there are a reasonable number of search consumers in the market, firms will have to charge a competitive price, which benefits all consumers (Schwartz and Wilde, 1979).

Finally, Friedman and Friedman (1980:267) suggest truth-in-advertising will simply be enforced by competition, without the need for laws and government enforcement agencies:

If business advertising is misleading, is no advertising, or government control of advertising, preferable? At least with private business there is competition. One advertiser can dispute another.

Although we shall subject all three of these arguments to an empirical test, the Friedmans' contention is not convincing on purely theoretical grounds. In part, this is because they overlook a free-rider problem. If a market has only two firms, A and B, and A engages in misleading advertising to increase its market share, B could issue corrective advertising or sue A in order to halt the promulgation of A's misinformation. Consumers would then be fully informed and the market shares between A and B would return to their original state. Here, B reaps all the benefit of its policing of A's advertising. However, if more firms are in the market, say four, A, B, C, and D, and A engages in misleading advertising, B's advertising explaining this deception may switch consumer purchases not only to B, but also to C and D, who free ride on B's policing work. As B does not capture all the benefits of revealing A's deception, it may decide that engaging in further police work is not economic. A is then free to engage in misleading advertising. The existence of this free-rider problem suggests there is a good case for a government agency, such as the Commerce Commission to prosecute A, for the benefit of B, C, and D.

The Friedmans' thesis also overlooks the case where all firms benefit from spreading misinformation. That is, if A, B, C, and D all benefit from A's misinformation, none has an incentive to issue corrective advertising or to sue A. This is the case, for instance, with the tobacco industry, where none of the firms involved have an incentive to inform consumers about the dangers of smoking (Hadfield, Howse and Trebilcock, 1998).

These theoretical arguments are now considered in light of the judicial experience of the Fair Trading Act. As there is no detailed information on Fair Trading Act cases heard in the disputes tribunals, this paper confines itself to court cases and Commerce Commission warnings and settlements.

Analysis of Case Law

There is no exhaustive catalogue of cases heard in New Zealand courts. Briefcase and Linx legal databases (the best available) summarise many, but not all, cases. These databases provide a good indication of the nature and composition of cases, but understate the actual number of cases heard. From these databases, the author obtained summaries of cases over the past 10 years where the Fair Trading Act was the primary relevant statute (see table). The 'success rate' of various types of cases was also calculated, which is the number of cases where the complainant's case was either wholly or largely successful, expressed as a percentage of all cases where the summaries indicate the court handed down a decision.

The author also reviewed cases summarised in *Fair's Fair*, the Commerce Commission's regular newsletter, for the same time period. This was done to pick up Commerce Commission cases not found in the databases, as well as Commission warnings and settlements. This information is not included in the table, but is considered in the text below.

Fair Trading Act Case Law: Cases in Ten Years Ending May 2000

Nature of Case	Number	Sub-Total	Proportion of Total ^a	Proportion of Sub-Total ^a
Trader-to-trader cases:	483		75%	
* Misrepresentation in dealing		265		55%
* Passing off ^b		115		24%
* Other misleading conduct ^c		31		6%
* Other		<u>72</u>		<u>15%</u>
		<u>483</u>		<u>100%</u>
Cases involving consumers ^d :	80		12%	
* Property		27		34%
* Insurance		10		13%
* Cars		8		10%
* Major loans		7		9%
* Professional services		7		9%
* Other		<u>21</u>		<u>26%</u>
		<u>80</u>		<u>100%</u>
Commerce Commission cases ^e :	66		10%	
* Consumer misrepresentation		47		71%
* Trader misrepresentation		7		11%
* Other (product safety, etc.)		<u>12</u>		<u>18%</u>
		<u>66</u>		<u>100%</u>
Other:	18		3%	
Total:	647		100%	

Notes:

^a Percentages may not sum due to rounding.

^b Decision made in 111 cases; claim successful in 61 (55 per cent success rate).

^c Decision made in 28 cases; claim successful in 23 (82 per cent success rate).

^d Decision made in 71 cases; consumer successful in 35 cases (49 per cent success rate).

^e Decision made in 63 cases; Commission successful in 50 cases (79 per cent success rate).

Source: Derived from Briefcase and Linx databases.

The database search produced 647 Fair Trading Act court cases. Trader-to-trader cases (cases where one trader is suing another, with neither consumers nor the Commerce Commission involved) accounted for the lion's share of court action under the Act (75 per cent). There were two major areas for trader-to-trader litigation. The first was claims of misrepresentations in dealing, that is, in negotiations and agreements (for instance, representations about the value of franchises and disputes over the details of business contracts). These represented 55 per cent of all trader-to-trader cases. In these cases, the Act was invoked merely to strengthen one party's claim that information given by the other party was misleading. These cases do not involve issues of truth-in-advertising and are not considered further.

Of more interest are the 30 per cent of cases involving claims of passing off or other claims of misleading conduct. A passing-off action is where one firm

claims that a competing firm is offering a product that is similar to one supplied by the complainant, in an effort to exploit consumer awareness of the complainant's brand. In 55 per cent of passing-off cases, the claim was successful. For example, Wellington Combined Taxis successfully obtained an interim injunction stopping a rival taxi firm using similar signage and logos (*Wellington Combined Taxis v. Wellington Ace Taxis*, Wellington High Court, 11 October 1996).

Looking at the other claims of misleading conduct in trader-to-trader cases, the claims have been successful in around 80 per cent of all actions. For example, car manufacturer BMW successfully sued retailer Pepi Holdings for knowingly selling imported second-hand BMWs with odometers that had been wound back. BMW sued because of the effect Pepi's actions would have on BMW's reputation. This result was upheld by the Court of Appeal (*Pepi Holdings v. BMW New Zealand*, Court of Appeal, 25 August 1997). Similarly, National Insurance, which offered a customer assistance service, successfully obtained an interim injunction stopping Allied Mutual Insurance advertising that Allied Mutual Insurance was the only insurer offering such a service (*National Insurance v. Allied Mutual Insurance*, Auckland High Court, 16 December 1992).

As will be recalled, Fair Trading Act advocates support the use of the Act by traders, arguing that this extends the reach of the Act. The case law suggests that this enthusiasm is warranted. The success of passing-off cases and other misleading conduct cases reduces the likelihood that firms will attempt to mislead consumers by engaging in such behaviour. This reduces consumers' search costs.

It is significant that in all the cases of passing-off and other claims of misleading conduct (successful or not), the complainant was seeking to reap private benefits from the action that it alone would enjoy. With passing-off cases, the other trader is allegedly seeking to pass its products off as being those of the complainant. With the other claims, the other trader is allegedly engaging in conduct that undermines the value of the complainant's brand. The author could find no instances where trader-to-trader cases involved the complainant seeking public benefits. That is, the complainant was pursuing an action that, if successful, would benefit all the firms in the market. Those actions were confined to the prosecutions undertaken by the Commerce Commission (as discussed below). These empirical results confirm the argument used above to refute the criticism of Friedman and Friedman. That is, firms will only enforce truth-in-advertising in cases where they reap all the benefits of such enforcement action.

Another 12 per cent of cases involved an individual consumer seeking redress. Given the cost of seeking redress through the courts, it is not surprising that the goods and services involved in consumer cases were typically relatively expensive. Only in cases involving such items as property, insurance, cars, major loans and professional services would the loss to the consumer merit the cost of litigation. Jordan and Rubin (1979) claim that sellers of expensive experience goods do not have an incentive to mislead as they risk facing costly court action. But many consumer cases centre on just such consumer products, for instance cars and professional services. This indicates that not all traders comply with Jordan

and Rubin's theory. This may be because some traders erroneously anticipate that the cost of litigation will dissuade consumers from taking judicial action.

Consumers were not guaranteed success in their cases, only managing to succeed in around half their cases. They were successful only in cases where they had been genuinely misled and deserved the judgement to go in their favour. For instance, in one case a consumer purchased an unregistered car at auction. A notice on the vehicle said that the consumer would have to pay \$619 to fit seatbelts in the back seats in order to bring the vehicle up to registration standard. But after paying the money and taking delivery of the vehicle, the consumer discovered the seatbelts had not been fitted. The court cancelled the sale, a decision upheld on appeal (*Hammer Auctions v. Williams*, Auckland High Court, 10 April 1997). In another case, the consumer was misled by a real estate agent as to the boundaries of a property. The consumer was awarded the difference between the lesser actual value of the property and the price paid, plus damages and costs (*Baker v. Harvey Corporation*, Henderson District Court, 21 July 1995).

The primary reason why consumers failed in the unsuccessful cases they took was that the claimed misrepresentation had simply not taken place. For example, in several cases the court found that the consumer was demanding that their insurance company honour a claim to which the consumer was clearly not entitled (see, for instance, *Pooley v. State Insurance*, Greymouth High Court 20 August 1990). In another case, a consumer claimed they had been misled, despite the fact the court found the contract to be clearly unambiguous (*Garrett v. Max Pennington Motors*, New Plymouth District Court, 7 February 1996). It is disturbing that consumers take such a high proportion of cases apparently doomed to fail, thereby imposing a needless cost on traders. This may indicate that consumers need to be better educated about their rights and to form more realistic expectations regarding the likely success of any case they may be contemplating.

On a more positive note, as with trader-to-trader cases, the successful consumer cases indicate how giving private individuals the right to sue extends the reach of the Act. Rather than complaining to the Commerce Commission, consumers sought redress themselves. But, once again in common with trader-to-trader cases, this activity only occurred where consumers were seeking private benefits that they alone would reap. That is, they were seeking compensation for private losses they had incurred. This implies it would be wrong to rely on traders and consumers to enforce those aspects of truth-in-advertising law that relate to public benefits. For this, we need the Commerce Commission.

Ten per cent of cases were Commerce Commission actions, most of which centred on misrepresentations. Seventy-one per cent of cases involved accusations of misrepresentation in consumer transactions and 11 per cent involved accusations of misrepresentation in business transactions. In fact, it was a business misrepresentation that attracted the highest total fine yet under the Act. Ashley Guy Rhodes and his four companies were fined a total of \$130,000 for demanding payment for advertisements run in Rhodes' magazines that businesses had not ordered, a decision upheld by the High Court (*Zennith [sic] Publishing v. Commerce Commission*, Auckland High Court, 20 November 1998). The

remaining 18 per cent of Commission cases involved breaches of the product safety and consumer information standards and pyramid selling. The Commerce Commission succeeded in around 80 per cent of the cases it took.

The Commerce Commission cases strike further blows against Jordan and Rubin (1979), who claimed that those selling search goods will not mislead, as consumers can obtain sufficient information prior to purchase. In many Commerce Commission cases, the trader attempted to mislead consumers even though consumers would have become aware of the deception prior to purchase. For instance, when ANZ Bank ran newspaper advertisements for mortgages stating that it had halved its standard fee to no more than \$500, the small print of the advertisement said that the maximum fee could be as high as \$1000 if the consumer did not take their other banking business to the ANZ. The Commission successfully prosecuted the bank for this and other misleading promotions. The court found that the bank's advertising campaign had generated more than \$1 billion in home lending business, and that consumers might have been enticed to apply for finance from the bank even after being told the real situation (*Commerce Commission v. ANZ Banking Group*, Wellington District Court, 23 February 1996). Likewise, in 1996, Ford advertised the price of a car, but only mentioned additional costs in the advertisement's small print. Ford entered into an agreement with the Commission to refund these additional costs to all those who had bought the advertised cars (Commerce Commission, 1997a). In 1999, Telecom entered into a settlement with the Commission acknowledging that some of its cellphone advertisements breached the Act. The advertisements contained small print that qualified the cellphone offers by adding extra fees and conditions (Commerce Commission, 1999b).

In all these cases, consumers would have become aware of the deceptions prior to purchase, despite the fact Jordan and Rubin's (1979) theory is that deceptions involving information that can be verified by search would simply not occur. It would appear the traders' strategy was to entice consumers towards a purchase using a misrepresentation, and then to correct that misrepresentation immediately prior to purchase in the hope consumers would still go through with the transaction. The momentum towards purchase may be such that consumers still proceed, despite learning before committing themselves that the offer is not as good as they had been initially led to believe. In such cases, consumers who later think better of the purchase would be unlikely to sue. This is for two reasons. First, the consumers have not suffered a direct loss and therefore could not sue for compensation. True, they have still been misled, so could prosecute in order to see the trader fined. But any fine imposed would pass to the government, rather than the consumer. Second, only courts can impose fines, so the consumer would have to incur the expense of bringing a court trial.

Many reputable companies appear on the list of Commerce Commission prosecutions and settlements, names like ANZ Bank, Ford and Telecom. Unlike private court action, Commerce Commission actions typically receive wide media coverage. The cases are publicised on the Commission's website, in *Fair's Fair*, the daily newspapers, *Consumer* magazine and on the radio and television news.

It is probably fair to say that, given its newsworthiness, the more well-known and highly-regarded a company is, the more likely its prosecution under the Fair Trading Act will be widely publicised. This runs counter to the predictions of Jordan and Rubin. It suggests that companies with a reputation to protect may still breach the Act. Perhaps firms do not value their reputations as highly as economic theorists might suppose, or do value their reputations but suffer occasional lapses of judgement when devising marketing campaigns. Whatever the reason, it is clear that reputations and branding, although very desirable market signalling devices, are not necessarily alternatives to truth-in-advertising law.

As will be recalled, Schwartz and Wilde (1979) argue that truth-in-advertising law may be unnecessary as not all consumers need to be well informed for a market to operate competitively — if firms cannot differentiate between those consumers that search out information and those that don't, as long as there are a reasonable number of searchers in the market, firms will have to charge a competitive price, which benefits all consumers. This may be so, but not all markets exhibit these characteristics. There have been many instances in the Commerce Commission case law where firms have been prosecuted for misrepresentations where it is unlikely that a sufficient number of consumers would have had the knowledge and resources to see these misrepresentations for what they were and shopped elsewhere. For instance, in some cases, firms have been prosecuted for misrepresentations that only technically knowledgeable consumers would have identified as such. Consider Edge Computer, which was fined \$50,000 for selling computers which did not contain the memory the firm claimed was in them (*Commerce Commission v. Edge Computer*, Wellington District Court, 20 February 1997). The effect of the deception was widespread — any New Zealand-assembled 486 computer could have Edge Computer components inside it. If a computer contained Edge Computer components, it would work slower than it should and some programmes may not have run at all. It was only the suspicions of some technically aware consumers, realising that their computers were not running as fast as they should, that led to the deception being uncovered. In the absence of Commerce Commission action, it is unlikely that such a relatively small group of consumers would have acted as a competitive discipline on the traders involved. That is, this small group of consumers may have complained and obtained a refund, but most consumers would not have realised that the reason their computers were running slow was because the computers did not contain the claimed memory. Indeed, most consumers did not realise anything was amiss.

The same point is highlighted by the 1997 prosecution of appliance retailer Bond and Bond. It was prosecuted by the Commerce Commission for, among other things, promoting price savings on Bond and Bond's usual prices when the retailer had not normally charged those usual prices. For this and other breaches of the Act, Bond and Bond was fined \$63,000 (*Commerce Commission v. Bond and Bond*, Christchurch District Court, 7 May 1997). As most consumers do not habitually record the prices charged by retailers, they are unlikely to know that the claimed previous prices had in fact not normally been charged. Traders could

make such false price comparisons with relative impunity were it not for the Commerce Commission.

The evidence therefore suggests that in these cases at least, there are insufficient searchers in the market to remove the need for truth-in-advertising law. Yes, truth-in-advertising law may only be necessary for those markets, but it seems ridiculous to suggest the government should carefully assess each market to see whether truth-in-advertising law should be applicable to that market. The cost and time involved would be prohibitive. It is far simpler to have a truth-in-advertising law that applies to all markets. To be fair to Schwartz and Wilde (1979), though, their insights can be helpful in judging whether, in addition to being subject to general truth-in-advertising law, certain markets should require the disclosure of specific information. An example is the disclosure of the finance rate (also known as the annual percentage rate) in consumer finance markets. Such disclosure, required under so-called truth-in-lending laws, can assist consumers in identifying which of a host of competing finance deals charges the lowest price.

The various Commerce Commission cases again highlight the limitations of Friedman and Friedman (1980). That is, the Commission prosecuted firms that engaged in misrepresentations in instances where other firms were unlikely to take action because of the free-rider problem. For instance, although another bank could have issued corrective advertising in response to the ANZ Bank's advertisements, no bank had the incentive to do this as all banks not charging the additional fees would have benefited. Likewise, another computer retailer could have revealed Edge Computer's deception, but the benefits of this would have been shared by all other computer retailers.

The analysis so far has concentrated on the search-cost argument in favour of truth-in-advertising law. But in promoting truthfulness in economic transactions, the Fair Trading Act also attempts to ensure markets behave fairly. If it is accepted that the government has a role to play in ensuring markets are fair, this is another reason for the Commerce Commission, a government agency, to enforce the law and publicise its activities.

Society's dim view on unfair business practices is highlighted by the pyramid-selling cases heard under the Act. These have attracted the most severe penalty meted out under the law. In September 2000 (that is, outside the time coverage of this paper's consideration of the case law), the Commerce Commission successfully prosecuted the Maximus pyramid-selling scheme. Maximus was ordered to pay over \$3.1 million in compensation to those who had invested in the scheme. Maximus's bank accounts were frozen, its assets seized and liquidators appointed (Commerce Commission, 2000). Other large compensation orders and fines have been awarded in pyramid-selling cases (Commerce Commission, 1997b and 1999a).

Similarly, the Rhodes prosecution mentioned above attracted a large fine because Rhodes and his companies were seen as exploiting hard-working businesses that did not have time to check all their invoices. Rhodes was seen as an unethical businessperson, fully deserving a large fine. Peter Allport, then-

Commerce Commission chairperson, noted 'Advertisers pay out hard-earned money for what is no more than a scam.' Among his tactics, Rhodes used debt collectors in an effort to obtain money from an old peoples' home and took small businesses to the disputes tribunal. Rhodes' employees swore at, threatened and personally abused people to obtain payment for advertising, none of which had been ordered (Commerce Commission, 1998).

Conclusions

The Fair Trading Act bans misleading representations and certain unfair business practices. It promotes competition in markets by ensuring markets behave fairly and by reducing consumers' search costs.

Not all economists are convinced there is a need for such law. The first criticism is that only some categories of traders have an incentive to mislead. However, New Zealand case law does not support this. For instance, although those that sell search goods will supposedly not mislead, the Commerce Commission has successfully prosecuted traders that misled consumers and then corrected the misrepresentation before the purchase took place. Apparently, the hope was that the consumer had built up an inexorable momentum towards purchase. Were it not for a government agency enforcing truth-in-advertising law, it is likely such action would go unpunished.

The second criticism is that truth-in-advertising law is unnecessary in markets where traders cannot differentiate search consumers from non-search consumers. Maybe so, but not all markets reflect those characteristics. The case law revealed instances where few consumers would have known they had been misled. Rather than laboriously assessing the characteristics of every market, it seems expeditious to impose an economy-wide truth-in-advertising law.

The third criticism is that competing firms can be relied on to police truth-in-advertising, without the need for government regulation. However, this overlooks the free-rider problem. That is, it would only hold in cases where competitors would reap all the benefits of enforcement action. The Commerce Commission has prosecuted in cases where the free-rider problem exists.

The Fair Trading Act is a relatively unobtrusive form of market intervention. Traders can make whatever representations they like about their products, so long as the representations are not misleading. This allows firms to use reputations and branding, important market signals as to the quality of goods and services, but constrains traders who attempt to distort market processes.

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