

Joint Committee

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ANNEX D: Advice by Lord Lester of Herne Hill QC and Monica Carss-Frisk

We are asked to advise on two issues:

(a) Whether the institution of disciplinary proceedings by the Financial Services Authority ("FSA") purely on the basis of a breach of one of its proposed statements of principle could potentially infringe Article 7 of the European Convention on Human Rights ("ECHR");

(b) Whether, in the light of the policy statements in Chapter 5 of the FSA's Consultation Paper 17, the nature of the disciplinary proceedings which the FSA will be empowered to bring under the Financial Services and Markets Bill ("the Bill") is criminal or civil.

2. For the reasons given below, we consider that (1) the conviction of a firm of a disciplinary offence purely on the basis of a breach of one of the statements of principle, where the conduct in question does not fall within any detailed rule, evidential provision, code or guidance, would be contrary to Article 7 of the ECHR; and (2) disciplinary proceedings under the Bill would be treated as criminal in substance for the purposes of attracting the procedural safeguards guaranteed by Article 6 of the ECHR.

Article 7 of the ECHR

3. As the earlier joint Opinion advised, Article 7 of the ECHR, which prohibits the retrospective imposition of criminal offences and penalties, includes a requirement in accordance with the principle of legal certainty that an offence must be clearly defined in law, so that an individual may reasonably foresee the consequences of his actions. See *Kokkinakis v Greece* (1993) 17 EHRR 397: an offence is sufficiently clearly defined to satisfy Article 7 where any individual can to a reasonable degree foresee from the wording of the relevant provision and, if need be, with the assistance of the courts' interpretation of it and with the benefit of legal advice, what acts and omissions will make him liable. Respect for the principle of legal certainty requires the act which entails the individual's criminal liability to be clearly set out in the law. The requirement is satisfied where it is possible to determine from the relevant statutory provision what act or omission entails criminal liability. The principle of legal certainty is a general principle of European Community and Convention law, and is part of the constitutional and legal systems of many common law and civil law countries. We would expect German firms, for example, who have automatic authorisation, to be astonished by the lack of adherence to the principle of legal certainty enshrined in their constitutional and legal system.

4. Insofar as disciplinary offences under the Bill are to be regarded as criminal for the purposes of the ECHR (as to which see below), the definition of those offences must comply with the principle of legal certainty guaranteed by Article 7 of the ECHR. We are asked to advise in relation to the institution by the FSA of disciplinary proceedings for a breach of a statement of principle issued by the FSA. We will assume for these purposes that the disciplinary offences provided for

in Parts V and XII of the Bill are criminal, rather than civil, with the result that the requirement of certainty in Article 7 of the ECHR applies.

5. Consultation Paper 13, published in September 1998, sets out the FSA's proposed Principles for Business ("the Principles"). (We are instructed that the consultation paper on principles for approved persons has not yet been published.) The Principles are extremely widely and vaguely drawn. For example, Principle 1 provides that "A firm must conduct its business with integrity", and Principle 5 states that "A firm must observe proper standards of market conduct". They are "high-level precepts" and binding "obligations" (paragraph 1 of Consultation Paper 13).

6. It is intended by the FSA that the implications of the Principles will be elaborated in binding rules, evidential provisions and guidance (see paragraph 9 of Consultation Paper 13). However, it is important to note that the FSA has indicated that there may

be instances when disciplinary action will be taken in respect of conduct which is not identified in any such rule, evidential provision or guidance. We have in mind, in particular, the following statements by the FSA:

(a) "...the Principles may be relevant in situations for which no rule or guidance yet exists. In such situations firms and supervisors alike need to be prepared to make judgments based on the values embodied in the Principles." (Consultation Paper 13, paragraph 10);

(b) "...since the Principles as a general statement of regulatory requirements are designed to be applicable in new or unforeseen situations, and in situations in which there is no need for guidance, the FSA's evidential provisions and guidance should not be viewed as exhausting the implications of the Principles themselves." (Consultation Paper 13, Annex A, paragraph 6);

(c) "...disciplinary action for breach of a Principle may often be appropriate where there has been a breach of related detailed Rules, evidential provisions/Codes of Conduct and/or guidance. However, there may also be circumstances in which it will be legitimate for the FSA to take disciplinary action based exclusively on a breach of one or more of the Principles." (Consultation Paper 17, paragraph 94).

7. In our view, the Principles are so widely and vaguely drafted, that the conviction of a person of a disciplinary offence on the basis of an alleged breach of a Principle, where the conduct in question does not fall within a rule, evidential provision or guidance, would amount to a breach of the requirement of legal certainty in Article 7 of the ECHR. We do not consider that the Principles alone will enable the members of a firm to foresee to a reasonable degree what acts and omissions will make it liable (see Kokkinakis (above)). We find further support for our view in the recent judgment of Brooke LJ in *Westminster City Council v Blenheim Leisure Limited & Ors* (judgment of the Divisional Court of 12 February 1999; unreported; New Law Online Case 499020801). Brooke LJ observed, in relation to the possibility of conviction of a criminal offence on the basis of a breach of a Rule operated by Westminster Council that "The Licensee shall maintain good order in the premises" that:

"The Council would do well, in my judgment, to tighten up the language of Rule 9 if it wishes to be able to use it to prohibit activities like these on licensed

premises after the Human Rights Act 1998 comes into force. The extension of the very vague concept of the maintenance of good order to the control of the activities of prostitutes may have passed muster in the days when English common law offences did not receive critical scrutiny from national judicial guardians of a rights-based jurisprudence, but those days will soon be over. English judges will then be applying a Human Rights Convention, which has the effect of prescribing that a criminal offence must be clearly defined in law. I do not accept Mr Carter-Manning's submission that it is impossible to define the kind of conduct his clients desire to prohibit with greater precision, or that it is satisfactory to leave it to individual magistrates to decide, assisted only by some fairly arcane case-law, whether or not activities of the type of which the Council complains in this case amount to a breach of good order so as to render the licensees liable to criminal penalties."

8. The FSA has stated that it will not invoke the Principles as a basis for disciplinary action in an arbitrary and unpredictable fashion, but that it should be able to take enforcement action where "it is clear that the conduct in question violates the Principles, regardless of whether any detailed Rule, Code or evidential provision has strictly been breached; or the behaviour in question is closely analogous to behaviour which would constitute a breach of a detailed Rule, Code or evidential provision..." (paragraph 95 of Consultation Paper 17).

9. These statements by the FSA do not, in our opinion, meet the concern as to legal uncertainty to which we have referred. We consider that it should be possible for the FSA to prescribe with a reasonable degree of certainty the conduct which will amount to a breach of a Principle in the detailed rules, evidential provisions, codes of conduct and guidance that are to be published in relation to the Principles, and that it would not be reasonable to expect a firm to foresee that acts and omissions falling outside such detailed rules, evidential provisions, etc, might render it liable to disciplinary action for breach of a Principle.

Article 6 of the ECHR

10. We are also asked to consider the nature of disciplinary offences under the Bill, in the light of Chapter 5 of Consultation Paper 17. Chapter 5 deals with disciplinary offences other than market abuse (which is dealt with in Chapter 6), and we assume, therefore, that Instructing Solicitors are mainly concerned with these offences. We will, however, also briefly revisit the offence of market abuse.

11. So far as concerns the disciplinary offences provided for in Parts V and XII of the Bill (i.e. offences other than market abuse), we have found nothing in Chapter 5 of Consultation Paper 17 (or indeed in the speech by Mr Howard Davies of 3 March 1999) to cause us to differ from the view expressed in the joint Opinion of 27 October 1998, that such offences are likely to be treated as criminal in substance for the purposes of attracting the procedural safeguards of Article 6.

12. It is well-established in the jurisprudence of the European Court of Human Rights that even where the offence is classified as being civil in nature as a matter of domestic law, it may be criminal for the purposes of Article 6 of the ECHR where the nature of the offence (including the purpose of any sanction) or the nature and degree of severity of any penalty so indicates (see eg. *Lauko v Slovakia*; judgment of the European Court of Human Rights of 2 September 1998, as yet unreported).

13. Chapter 5 of Consultation Paper 17 makes it very clear that it is a major purpose of the exercise of the FSA's powers to impose a financial penalty and/or to make a public statement to deter Authorised Firms or Approved Persons from future breaches and to deter others from misconduct (see paragraph 82, as well as paragraphs 104 and 107). Where a penalty has a deterrent and punitive purpose, this is sufficient to show that the offence is criminal in terms of Article 6 (see Lauko, above). The statements as to the purposes of disciplinary action contained in Chapter 5 of Consultation Paper 17 lend support, therefore, to the conclusion that disciplinary offences under the Bill are criminal.

14. Mr Howard Davies, in his recent Chancery Bar Association and Combar Spring Lecture (delivered on 3 March 1999) stated that good arguments could be made to the effect that the proposed civil fines regime for market abuse is civil in nature (see page 11 of the written lecture). He referred to the facts that there was no penalty of imprisonment, that the purpose of the fining power was primarily to protect and compensate organised investment markets, that the market abuse regime (although it would apply beyond the authorised community) would be linked in its scope to those persons who chose to take advantage of the facilities of organised investment markets, and that the criminal courts would not be involved. Mr Davies fairly accepted that the issue is "by no means clear cut" (page 11).

15. The arguments deployed by Mr Davies are not, in our view, persuasive in relation the offence of market abuse:

(a) The fact that an offence is not punishable by imprisonment and does not give rise to a criminal record is not decisive of the classification of the offence for the purposes of Article 6 (see Lauko, above, and *Ozturk v Germany* (1984) 6 EHRR, ECtHR);

(b) As for the purpose of the market abuse regime, Mr Davies has stated that the purpose is primarily one of protection and compensation, but it is clear from Consultation Paper 17 that this involves deterrence as an important objective (see eg. paragraphs 138 and 144). In paragraph 144 of the Paper, it is provided that any civil fine for market abuse will reflect two main considerations, the first of which is stated to be "the need to provide an adequate disincentive to future abuse...". The fact that deterrence is a major purpose of the market abuse regime provides strong support for the argument that this offence is criminal for the purposes of the ECHR. It may be as a matter of domestic law that an allegation of market abuse is different from an allegation that the criminal law has been breached (paragraph 126 of Consultation Paper 17) but that is not in any way determinative of the position under Convention law;

(c) As for the argument that the market abuse regime is linked to those persons who take advantage of the facilities of organised investment markets, we do not think that this provides any indication that the offence is civil rather than criminal. Even if (which is not accepted) the market abuse regime were linked to those persons who take advantage of the facilities of organised investment markets, the offence is still of general application, just as a road traffic offence is of general application, albeit that it will in practice only apply to those who chose to drive a car. In any event, as was pointed out in the Joint Opinion of 27 October 1998, whether or not an offence is of general application is not a conclusive factor (see eg. *Campbell and Fell v UK* (1985) 7 EHRR 647, where prison discipline offences were held to be criminal for the purposes of Article 6). The decisive test is what is at stake for the individual or firm, the gravity of the offence, and the severity of the potential sanction.

16. We consider, therefore, that the offence of market abuse is likely to be characterised as criminal in relation to the ECHR. We also consider that it is strongly arguable that the other disciplinary offences established by the Bill are to be regarded as criminal, for these main reasons: (1) whilst these offences apply only to authorised or approved persons, they are created by statute and are, unlike the disciplinary rules of the old SROs, not dependent on any contractual relationship; (2) deterrence is a major purpose of disciplinary action, and (3) the fines and penalties that may be levied may be very substantial (being on the face of the Bill unlimited).

17. We should add, that the argument that disciplinary proceedings are of a criminal nature is particularly compelling in the light of the fact that the disciplinary proceedings operate separately from the powers relating to fitness and propriety, under which authorisation or approval can be withdrawn or not granted.

18. The decisions of the French courts in the Oury case, to which Instructing Solicitors have drawn attention, provide further powerful support for our view that where heavy financial sanctions are imposed by a disciplinary tribunal as a punishment, the offence is properly to be regarded as criminal for the purposes of Article 6, so as to give rise to the full protection of the procedural safeguards in Article 6.

19. The Court of Appeal's judgment in Dame Shirley Porter's pending appeal may cast further light on the approach of English courts to this important matter.

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