

UPDATE

Successful court challenge to GFSC decision

Update prepared by Robert Shepherd (Senior Partner, Guernsey) and Sally French (Senior Associate, Guernsey)

Guernsey benefits from strong regulation, but the expectations on the regulator are high. A recently released judgement found in favour of the Appellant in an appeal against the level of sanctions imposed upon him by the Guernsey Financial Services Commission (GFSC) in its capacity as the Bailiwick's financial services regulator. The Royal Court's judgment was upheld when challenged by the GFSC on appeal.

As a result, the GFSC will need to make a fresh decision on the appropriate level of fine.

This case demonstrates that the GFSC must act within the powers accorded to it and that the Royal Court will be robust in policing the use of those powers. Change is on the horizon, however, as Guernsey has recently approved the drafting of new legislation to increase the maximum level of fine for licensees, former licensees and relevant officers.

David John Merrien v Cees Schrauwens (Chairman of the Guernsey Financial Services Commission) (2016) (Unreported, Royal Court, (250915) 9 June) (Guernsey Judgment No 23/2016);

Cees Schrauwens (Chairman of the Guernsey Financial Services Commission) v David John Merrien (2016) (Unreported, Court of Appeal, 17 March) (Guernsey Judgment No 24/2016).

The Royal Court, by a recently released judgment, has found in favour of the Appellant in an appeal against sanctions imposed upon him by the Guernsey Financial Services Commission (GFSC) in its capacity as the Bailiwick's financial services regulator. The Royal Court's judgment was upheld when challenged by the GFSC on appeal.

Royal Court

By a judgment published on 9 June 2016, the Royal Court of Guernsey issued its findings in respect of an appeal against a decision of GFSC (the **Appeal**).

The Court was sitting in its capacity as the appellate body in respect of decisions of the GFSC. The Appeal concerned, amongst other issues, appeal against a financial penalty of £200,000, currently the statutory maximum financial penalty which the GFSC has the power to impose.

The decision to overturn the financial penalty

The Court found that as a whole the GFSC's process for decision making was fair and not subject to a material error. But it nevertheless overturned the GFSC's decision in respect of the financial penalty imposed for the following reasons:

Wednesbury unreasonableness

Deputy Bailiff Richard McMahon found that in imposing the maximum financial penalty the GFSC's Senior Decision Maker had mis-directed himself and reached a decision that no reasonable decision maker could have made.

The Court found that:

- the matters which the Senior Decision Maker must take into account are exhaustively set in section 11D(2) of the Financial Services Commission (Bailiwick of Guernsey) Law, 1987 (**FSC Law**). Those categories did not include any sort of catch-all;
- the Senior Decision Maker had wrongly not confined himself to the section 11D(2) considerations and approached the imposition of the financial penalty on the basis of the penalty which he would have imposed but for the statutory cap;
- the FSC Law should ensure that a consistent approach to financial penalties is developed and that this approach must recognise the statutory cap. However, it was not open to the GFSC to conduct itself as though the cap were not there;
- the Senior Decision Maker wrongly had regard to the level of penalties imposed in the UK, where no statutory cap applies. Whilst the GFSC may, in building its own framework, look to other jurisdictions when dealing with matters novel to its own experience, for example, assistance regarding the banding/grading of the conduct – it is not entitled to look for guidance on the like-for-like penalty sum to impose.

Proportionality

In addition to being unreasonable, the penalty imposed was found to be disproportionate. In reaching this conclusion the Court noted two factors:

1. Disparity between the parties sanctioned

The Appellant's two co-accused were each subject to financial penalties of £10,000 (reduced to £8,000 for early settlement). The Deputy Bailiff questioned whether right-thinking members of the public might consider the disparity between these figures and the £200,000 penalty imposed on the Appellant to be fair and proportionate. There needed to be an accompanying explanation which was clear and compelling to explain the disparity. The Deputy Bailiff was not persuaded that the Statement of Reasons met that requirement. Though satisfied that the Senior Decision Maker could legitimately put the Appellant's case in a different band from his co-accused, the disparity of approach was so great that it brought into question whether the financial penalty imposed on the Appellant was disproportionate.

2. Ability to Pay

The Court was not satisfied that the GFSC's approach taken to section 11D(2) (e) of the FSC Law was the correct one. Section 11D(2)(e) requires the GFSC to take account of the potential financial consequences to the person concerned. It was clear to the GFSC that the Appellant had no prospect of paying the penalty imposed. The Court observed:

'It looks as though a decision had been taken to impose the statutory maximum to make an example of the Appellant whatever his financial circumstances and ability to pay.'

The Court considered that the Senior Decision Maker had adopted the approach of looking at seriousness to a greater degree than anything else, thereby paying little or no regard to a person's ability to pay. This mindset appeared to have established itself at the GFSC because the statutory cap was regarded as unduly inhibiting. In this way the GFSC was not complying with the statutory regime as it was affording section 11D(2)(b) significantly more weight than sub-paragraph (e), where the legislature has simply provided that all these matters must be taken into consideration. The Deputy Bailiff found that the Senior Decision Maker had failed to address his mind properly to section 11D(2)(e) because he had not indicated that he satisfied himself that the Appellant was in a position to pay the penalty imposed. It was incumbent on the Senior Decision Maker to spell out that the financial penalty being imposed was capable of being satisfied. If it was not, then the level of penalty is wrong in principle. The Senior Decision Maker had not satisfied this requirement, with the consequence that the Court could not be satisfied that the financial penalty imposed was proportionate.

Guidance on the imposition of financial penalties

The case provides useful clarification regarding how the GFSC is to exercise its powers in imposing financial penalties in future. The following points were made:

- In deciding whether or not to impose a financial penalty the GFSC should confine itself to the considerations in section 11D(2) of the FSC Law and nothing further.
- Though not going so far as to say that the section 11D(2) factors are to be given equal weight, they are all to be considered and the GFSC should not afford sub-paragraph (b) significantly more weight than paragraph (e).
- It is for the GFSC to set its own scale of culpable conduct for Guernsey and it must do so with regard to the statutory cap and the legislative framework in which it operates.
- The GFSC may look to other jurisdictions for guidance as to where a particular matter may be placed on the scale of culpable conduct. It may not however look at the fine imposed by a jurisdiction where the level of sanctions is uncapped and find that an equivalent fine is applicable here.
- To comply with section 11D(2)(f) of the FSC Law the GFSC must adopt an approach that is objectively consistent. Anyone considering the level of penalties imposed across the board should be able to understand, from a full appreciation of the relevant facts and circumstances in each case, why the financial penalty has been fixed at the level it has.
- Even in a case where the GFSC finds itself considering the imposition of the maximum penalty, it is still required to take into consideration all the matters specified in section 11D(2) of the FSC Law. Those include having regard to what may be viewed as significant mitigation, which should be reflected in the penalty imposed. It would be an exceptional case where the statutory maximum penalty would be imposed if there was substantial mitigation.
- The GFSC must have regard to a person's ability to pay the level of financial penalty to be imposed.
- Any financial penalty to be imposed must be fair and proportionate.
- When dealing with a case with multiple parties to be sanctioned, if the treatment of the parties is to be markedly different, any explanation given for the comparative disparity must be clear and compelling.
- Cases must be dealt with in a manner that does not create any disparity between the penalties being imposed both with regard to previous decisions of the GFSC and also in respect of the other persons being dealt with in the present case.

Court of appeal

The GFSC appealed the Royal Court judgment challenging the following two findings, that:

- section 11D(2) of the FSC Law exhaustively lists the factors which the GFSC may take into account; and
- section 11D(2)(e) of the FSC Law required the GFSC to be satisfied that the person sanctioned is in a position to pay, or will be within a reasonable time.

Extent of section 11D(2)

The Court of Appeal upheld, but finessed, the Royal Court judgment in this respect.

The Court of Appeal affirmed that the section 11D(2) requirements are exhaustive. However, they include, at section 11D(2)(b), a consideration of the seriousness of an infraction. What informs the consideration of seriousness is open ended. Accordingly, if the GFSC considers that it needs to take into account a factor not listed in section 11D(2), it may have regard to that factor if and to the extent that such a factor is material to the seriousness of the conduct or infraction.

Ability to pay

The Court of Appeal pulled back a little on this point, holding that imposing a fine which could not be paid was not automatically wrong in principle. In exceptional cases, on the clearest of reasoning, the GFSC may impose a sanction of such a level as to make insolvency an inevitability.

Conclusions

Both judgments are clear that the GFSC must act within the powers accorded to it. It is understandable that the GFSC may view the statutory cap to its powers of financial sanction as unduly constraining. This point has been made by the IMF and MONEYVAL, in otherwise predominantly complimentary reports. It is also a point of pending legislative reform. Following the States' Resolution of January 2016, Guernsey has approved the drafting of legislation to:

- increase the maximum level of fine for licensees and former licensees (other than personal fiduciary licensees) from £200,000 to £4,000,000, with any fine over £300,000 being limited to a maximum of 10 per cent of the turnover of the licensee/former licensee in question; and
- increase the maximum level of fine available for relevant officers (that is, directors and other officers of licensees and former licensees) and personal fiduciary licensees from £200,000 to £400,000 together with the inclusion of an additional criterion for the GFSC to consider emoluments arising in respect of the relevant officer's or personal fiduciary licensee's position.

However, until such legislation is in force the GFSC needs to work with the statutory cap of £200,000.

The judgments also serve as a reminder of the high standards to which the GFSC will be held and of the important role played by the Court in Guernsey's regulatory regime. This has been further emphasised by the recent decision in *Bordeaux Services (Guernsey) Limited & Ors v The Guernsey Financial Services Commission*.¹ In that instance the Royal Court stated that the GFSC's Decision was to be subject to a higher level of intensity when reviewed by the Royal Court, particularly because the availability of discretionary penalties meant that the process was quasi criminal. The Bordeaux judgment further held that the GFSC's reasoned sanctions decisions should 'bear the hallmarks of fairly closely reasoned decisions at, or approaching, the style of decision that would be expected from a judicial tribunal.'

Guernsey benefits from strong regulation, but the expectations on the regulator are high. The GFSC is required to comply with the legislative brakes on its powers. The cases referred to above demonstrate that the Court will be robust in policing the GFSC's use of its powers.

The Appellant was represented by Advocate Robert Shepherd, Senior Partner, and Sally French, Senior Associate, both of Mourant Ozannes.

UPDATE: On 30 August 2016 the GFSC confirmed that, having reconsidered the question of the financial penalty, in the particular circumstances it was not appropriate to impose any financial penalty.

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¹ (Unreported, Royal Court, 11th May) (Guernsey Judgment No 18/2016).
See also: May 2016 update: '[Courts will apply greater scrutiny to regulatory penalties](#)'

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