Financial Services

Market abuse – will the FSA impose penalties as an alternative or in addition to, criminal prosecutions?

by Peter Richards-Carpenter

Peter Richards-Carpenter

On 17 June 1999, the final version of the Financial Services and Markets Bill was published and the Bill is expected to become law around the summer of 2000. Apart from the assumption by the Financial Services Authority (FSA) of the authorisation and regulation of all financial services activity, the measure that has attracted most attention has been that relating to penalties for market abuse.

The term 'market abuse' seems quite wide, but its definition for the purpose of the Bill is really quite narrow: the conditions laid down in clause 95(2) are such that it really covers only insider dealing, market manipulation and misleading investors. Other forms of behaviour, for example fraud or money laundering, although they may involve financial markets and be considered abusive, do not come within the Bill's definition.

At present market abuse is dealt with in two ways. Insider dealing and misleading statements and practices are criminal offences and may be prosecuted accordingly by the Crown Prosecution Service or, where the misleading statement or practice constitutes serious fraud, by the Serious Fraud Office (SFO). In addition, they are all prohibited under the rules of the various SROs (self-regulatory bodies) and RPBs (recognised professional bodies), which will continue to carry out their present functions until the Bill becomes law. Nevertheless, the rules on this vary from one body to another: the Law Society Rules, for example, do not prohibit insider dealing in terms.

Under the new regime the above criminal and regulatory routes will both still apply. Those forms of market abuse that are criminal offences will continue to be such; the offence of making misleading statements under s. 47 of the *Financial Services Act* 1986 is re-created in clause 341 of the Bill while Part V of the *Criminal Justice Act* 1993, which covers insider dealing, will remain in force. Similarly, although the FSA, which will take over the functions of the current SROs and (in so far as they apply to financial services) RPBs, has yet to publish its rules, it is certain that those activities which are currently prohibited and subject to disciplinary sanctions under the rules of the SROs will be dealt with in a similar manner by the FSA.

In addition, however, the FSA will have the power to impose financial 'penalties' for market abuse. The earlier draft of the Bill, published as part of the Consultation Paper, referred to 'civil fines' and it would seem clear that that is what they are. They may be compared to the fines which, for example, the French Commission des Opérations de Bourse (COB) or the US Securities and Exchange Commission (SEC) may impose. Although they are arguably administrative in nature, in so far as the FSA will have the power to impose them directly rather than bringing an action before the courts, they have two important characteristics that mark them out as civil. First, they may be enforced as a judgment debt. Secondly, and more fundamentally, they apply to everyone and not simply authorised persons. Paragraph 168 of the Guidance Notes to the Bill states:

'This clause [ie. clause 98] *allows the Authority to impose a monetary penalty on any person, whether an authorised person or not, who has engaged in market abuse or induced another to engage in market abuse.'*

The power is thus very different in nature from the existing power of an SRO or RPB to fine its members for regulatory breaches, including those amounting to market abuse.

All of this is now well-known and has been widely discussed. There has been rather less discussion however on the potential overlap between this new civil (or quasi-civil) jurisdiction and the criminal law. Since the forms of market abuse as defined in the Bill are criminal offences, a person could commit an act that on the face of it renders him liable to both criminal prosecution and a penalty from the FSA.

on the Internet

http://www.parliament.the-stationery-office.co.uk/pa.cm199899/cmbills/121/1999121.htm

Copies of the Financial Services and Markets Bill are available from the Stationery Office, price £13.40, or can be directly accessed on the internet at this website.

It has been suggested in some quarters that, in practice, one or other enforcement route will be taken, but not both. Clause 105 states that the Treasury may issue written guidance to assist the relevant authorities to determine what action to take in cases of overlap, ie. where an act appears to be punishable with a penalty under clause 98 but also constitutes the criminal offence of insider dealing under Part V of the *Criminal Justice Act* 1993 or making a misleading statement under clause 341 of the Bill. Paragraph 174 of the Explanatory Notes, commenting on clause 105, seems to imply that a person would not be subject to both forms of enforcement, stating:

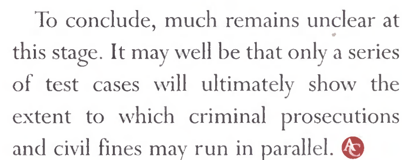
'The purpose of this guidance would be to help those authorities in deciding whether a

case should be subject to criminal prosecution, or the imposition of penalties under the market abuse provisions.'

No guidance from the Treasury has, however, as yet been published, although this may simply be due to the fact that the new regime will not come into force until next year. In any case, the question arises as to what extent this guidance will be legally binding: if it is mere guidance, the FSA (who will have the power to bring prosecutions for insider dealing) or the Crown Prosecution Service may be free to disregard it. The general assumption that no one could ever both be prosecuted and suffer the imposition of civil fines is a dangerous one. In France, for example, insider dealing is, as in the UK, prohibited under both the criminal law (Article 10-1 of Ordinance 67-833 of 28 September 1967 (as amended)) and an administrative regulation (COB Regulation 90-08). It is rare for a given case to be dealt with and punished under both provisions, but it has been known, notably in the case of *Delalande/Synthélabo*, in which a director through insider dealing made a profit estimated at FF69.5m (approx. £7m). Following proceedings under the COB regulation, in which he was fined the maximum penalty of FF10m (approx. £1m), the director was then also prosecuted under the Ordinance. Although, in the event, the court imposed no further penalty other than to order that he pay the costs of the hearing, the principle had clearly been established that regulatory proceedings of this type do not automatically rule out a criminal prosecution. Since the FSA is arguably a unitary authority modelled on those of other jurisdictions, such as the COB, it may well be that in time such principles are adopted in the UK as well.

Clause 99 of the Bill requires the FSA to publish a statement of its policy in relation to the imposition of penalties for market abuse. Sub-clause (2) makes clear, however, that the FSA is empowered to alter or replace that policy should it see fit, although if it does so it must publish the replacement or alterations. It is not clear, however, what redress a person fined by the FSA other than under the published policy would have. There would arguably be grounds for judicial review on the basis that, whether or not it was actually illegal, it might be unreasonable for the FSA, having published a policy in accordance with its legal obligations, then to depart from it. Nevertheless the possibility cannot be ruled out that the Divisional Court might be less than sympathetic to a person who had recently been convicted of insider dealing or misleading investors.

To conclude, much remains unclear at this stage. It may well be that only a series of test cases will ultimately show the extent to which criminal prosecutions and civil fines may run in parallel.


Peter Richards-Carpenter
Head of Financial Services, Rowe & Maw

European Law

Medicinal products and essential similarity: the preliminary ruling in R v Medicines Control Agency ex parte Generics

by Frank Wooldridge

Frank Wooldridge

The Community legislation concerning the authorisation of medicinal products is of considerable complexity. However, the European Court of Justice (ECJ) has recently elucidated the controversial meaning of the concept of 'essential similarity' in its recent decision in *R v Medicines Control Agency ex parte Generics* (Case C-368/96, not yet reported). It will be impossible to understand this ruling without some elementary understanding of the relevant provisions of the applicable Community legislation.

According to Council Regulation 2309/93 (OJ 1993 L214/1), authorisations of certain medicinal products must take place at Community level. Other such products require authorisation by the competent authority of the relevant member state (in this case the Licensing Authority established by the *Medicines Act* 1968, acting by means of the Medicines Control Agency) before they can be marketed, in accordance with the provisions of Council Directive 65/65 (OJ 1965–1966, Eng. Spec. Ed., p. 20), subsequently amended by Council Directive 75/318 (OJ 1975 L147/1), Council Directive 87/21 (OJ 1987 115/36), Council Directive 93/39 (OJ 1993 L214/22) and Commission Regulation 541/95 (OJ 1995 L55/7).

An application for authorisation is required by art. 4(2).8 of Council Directive 65/65/ (as amended) to be accompanied by the results of certain tests and clinical trials (which generally involve the use of humans or animals). However, the applicant is not required to provide the results of pharmacological and toxicological tests or the results of clinical trials under three circumstances. Thus, art. 4(2).8(a)(iii) provides that such results are not required if the applicant can demonstrate that the product is essentially similar to one which has already been authorised within the Community for six or ten years and