A&L Goodbody

Submission to the Law Reform Commission on its Issues Paper on Regulatory Enforcement and Corporate Offences

Introduction

A&L Goodbody welcomes the opportunity to make a submission to the Law Reform Commission in response to its Issues Paper on Regulatory Enforcement and Corporate Offences. Where our comments apply to a number of issues we have dealt with those issues under one heading.

Please note that the views presented below are not intended to bind this Firm, its clients or other intermediaries and are supplied for the purposes of discussion and debate only.

ISSUE 4

Deferred Prosecution Agreements

Based on positive international experience, we recommend that deferred prosecution agreements ('DPAs') are introduced for the following reasons:

A. DPAs can allow for the imposition of a greater variety of sanctions by regulators. This flexibility facilitates the imposition of measures which more appropriately balance the interests of the public, the company, its shareholders, its employees, and any victims (ranging from fines to disgorgement of profits, compensation for victims, and implementation/monitoring of a compliance programme). It can be difficult for a judge to achieve this balance with the more limited sanctions typically available in legislation;

B. Such sanctions can provide a disincentive to breach the criminal law which is as, if not more, significant than that associated with a criminal conviction against a company. They can also provide for more effective remedial action.

C. DPAs can assist with the investigation and prosecution of offences committed by others by virtue of the company, as a condition of the DPA, providing the relevant authorities with significant additional information and other co-operation which those authorities may otherwise not obtain;

D. DPAs can result in very significant costs savings and resourcing efficiencies in the investigation and prosecution of corporate offences and in the incentivisation of corporate compliance.

We have considered the US and UK models for DPAs and consulted with lawyers who have advised on DPAs in both jurisdictions. We recommend that:

1. There should be oversight of DPAs, as in the UK. This is an important safeguard for ensuring that DPAs are used appropriately and serve the public interest. We believe that, while the particular Regulator might be responsible for negotiating the terms of a DPA, before any DPA could be effected it should receive the approval of the DPP. We believe that the DPP by virtue of her office, is best equipped to make an independent determination as to whether the DPA was in the public interest in the particular circumstances and that it would be unnecessary, burdensome and disproportionate to require a Court application in such circumstances.

2. Legal professional privilege should be protected in the negotiation of DPA. The applicant company for a DPA in the UK and US has to provide significant cooperation to the investigating authority in order to qualify for a DPA. This could include, for example, self-reporting, disclosing relevant documents, making witnesses available where possible, and implementing remediation measures. Legal professional privilege is a cornerstone of the Irish legal system, as

acknowledged by the Court of Appeal in *IBRC & Ors v Quinn & Ors* which stated that *"One of the great bulwarks of our legal system is the almost absolute right to claim legal privilege and to protect from disclosure documentation which currently falls into that category."* We believe it would be inappropriate and unlawful to impose a requirement (either expressly or impliedly) on a company that it must waive privilege to qualify for a DPA. Furthermore, it would potentially deter parties from entering into DPAs if communications or documents exchanged in that context were discoverable or admissible against them in litigation including litigation with other parties.

3. There should be a detailed Code of Conduct on the use of DPAs and detailed Sentencing Guidelines for relevant offences. For example, in the UK the Director of the Serious Fraud Office and the Director of Public Prosecutions have published a joint Code of Practice on their use of DPAs which supplements the Sentencing Council's Definitive Guidelines on fraud, bribery and money laundering for corporate offenders.

ISSUES 1, 5 AND 6

Background

This section of the submission addresses the following issues set out in the Issues Paper:

Issue 1: Standardising Regulatory Powers

Issue 5: Coordination of Regulators

Issue 6: Jurisdiction for Regulatory Appeals

The key question encompassed by these three issues is whether the supervisory and enforcement powers of the State's financial and economic regulators, and the level of co-ordination and co-operation between them, are sufficient or need to be supplemented. In the Issues Paper these issues are identified as being of relevance to the regulatory bodies listed below and for that reason the focus of this submission is on these specifically identified regulatory bodies:

- Central Bank of Ireland (CBI)
- Commission for Communications Regulation (ComReg)
- Commission for Energy Regulation (CER)
- Competition and Consumer Protection Commission (CCPC)
- Health Products Regulatory Authority (HPRA)
- Broadcasting Authority of Ireland (BCI)
- Office of the Director of Corporate Enforcement (ODCE)

Key Recommendations

In summary, we consider that the existing piecemeal legislative approach could usefully be supplemented by common powers (where appropriate) and greater coordination and cooperation between the regulators, whilst recognising the need for certain regulators to retain certain standalone regulatory powers relevant to their particular roles and responsibilities. Appropriate adjustment would provide for a more streamlined regulatory landscape in Ireland and, again where appropriate, a consistent approach to the exercise of statutory powers in similar circumstances.

However, while consistent language should be used where the regulatory objectives are identical, care should be taken before extending the powers of regulators which necessarily impact on the rights and freedoms of private citizens. In principle, regulators' powers should only go as far as required to achieve their regulatory objective and it is important that safeguards should be provided for to ensure regulators exercise such powers appropriately and proportionately, avoiding unnecessary impositions on private individuals and corporations.

Issue 1: Standardising Regulatory Powers

Under the current regulatory regime investigative and enforcement powers are conferred on the various regulatory bodies by a range of legislative instruments developed on a piecemeal basis. As a result the overlap between the responsibilities and powers of the regulators has not been addressed and this has given rise to inconsistencies.

While we are in favour of streamlining the regulatory regime where duplication of responsibility, or divergence in enforcement powers, has arisen purely from historical drafting inconsistencies, we do not advocate standardisation for its own sake. Given the wide ranging and disparate remits of the various Irish financial and economic regulators they may well need to retain different regulatory powers appropriate to their respective roles. The divergence in enforcement powers may well be appropriate, reflecting the specific functions or responsibilities of one or more of the regulators. Where there is a reason for a divergence in powers, the more draconian powers should not be extended to all regulators having responsibility for a particular provision.

As a general rule, we believe that the more draconian the regulatory power then the more judicious and discriminating the legislature must be as to who should use that power and in what circumstances.

Given the increasingly intrusive powers given to many regulators we believe it is important to have

guidelines in place to ensure that such powers are exercised fairly and in line with the Constitution.

We note that the Issues Paper refers to the possibility of introducing a standardised legislative framework similar to those adopted in Australia and the United Kingdom. While the Australian model in particular provides an attractive framework approach, we are concerned that adopting a standard approach could have unforeseen consequences in specific cases and should be considered very carefully.

An alternative would be to implement Codes of Practice or guidelines providing greater clarity and certainty to both regulators and regulated entities regarding the exercise of regulatory powers and the interplay between the powers of various regulators.

Issue 5: Coordination of Regulators

In line with our views on Issue 1 regarding the standardisation of regulatory powers we see merit in terms of efficiency and cost effectiveness in providing a strong framework for coordination and cooperation between regulators having overlapping remits. However, the issue of information sharing between regulators would need to be addressed appropriately to ensure the smooth operation of any such coordination and safeguards would be required to address concerns in respect of confidentiality, privacy, data protection, constitutional fairness and independence.

Sharing information

Before the legislature gives regulators the power to share information careful consideration should be given to the nature of the public entities involved and the entities regulated by them.

Each of the regulators covered by the Issues Paper are covered by statutory restrictions of the disclosure of information. We would be concerned to ensure that where information is shared between regulators, the purpose for which such information is deployed by the receiving regulator(s) would not be wider in scope than anticipated by the provider of the information.

It would be essential that when a party provides information to one regulator (in particular on a voluntary basis) that that party has certainty regarding the basis on which the information is provided and the consequences thereof.

Where information sharing between regulators is contemplated there needs to be transparency regarding the circumstances in which it can take place. In this regard, we would suggest that the delineation of such circumstances be publically available in the form of guidelines, a Memorandum of Understanding or, where appropriate, within a Co-operation Agreement.

Co-operation Agreements

Subject to our comments above regarding information sharing, we support the use of Co-Operation Agreements in appropriate circumstances. Some Cooperation Agreements are already in use in Ireland, including in the area of consumer and competition law enforcement.

For example, Section 19(1) of the Competition and Consumer Protection Act, 2014 enables the CCPC to enter into arrangements with prescribed sectoral regulators for the purpose of (1) facilitating cooperation between the CCPC and other bodies; (2) avoiding duplication of activities; (3) ensuring consistency; (4) enabling consultation and (5) conducting joint studies. The CCPC has already concluded a Co-Operation Agreement with ComReg pursuant to this provision.

Co-Operation Agreements provide a pragmatic framework that facilitates engagement between the parties on a case-by-case basis regarding the approach to be adopted including which party is best placed to lead a case.

We believe this legislation provides a strong model for coordination between the high market impact regulators covered by the Issues Paper. It may also be worth providing for multi-regulator Co-Operation Agreements.

Issue 6: Jurisdiction for Regulatory Appeals

Similar to the development of regulatory powers generally, regulatory appeals processes in Ireland have evolved separately resulting in divergence in the type of appeal permitted from decisions of regulators and the forum for such appeals.

In principle, we would support a streamlining of regulatory appeals processes to ensure they are as efficient and cost effective as possible. We consider this objective to be particularly important with regard to appeals from the high market impact regulators covered by the Issues Paper.

We note that at present there are a huge number of regulatory bodies in Ireland and a huge number of regulatory decisions are now delegated to those regulatory bodies. As result such decisions are less subject to political scrutiny than they were at a time when regulatory decisions were made at the Ministerial level. Given the effect regulatory decisions have on people's lives, it is necessary to ensure that private individuals and entities have some recourse in respect of regulatory decisions and that such recourse is sufficiently broad.

While Judicial Review is an important safeguard, of itself it will not always be a sufficient remedy because of its focus on process rather than the substance or merits of a decision. Therefore, in

view of the increasing significance of the powers delegated to regulatory bodies and order to ensure that an effective remedy is available to affected parties, we recommend that, where significant decision making powers have been delegated to regulatory authorities, and where there is no clear reason why a substantive review of those decisions would interfere with the overall purpose of a particular aspect of a regulatory framework (such as decisions made to deal with urgent criminal scenarios), there should be a right to appeal the substance of decisions emanating from such an authority as well as the process by which a decision was reached. We regard this as constitutionally important given the increase in the number and importance of the issues delegated to non-elected officials. Such powers should be subject to independent review in respect of the merits as well as in respect of procedures.

We note that the Issues Paper puts forward three different standardised approaches — (1) The High Court Commercial List, (2) UK Competition Appeal Tribunal (CAT) and (3) Australian Administrative Appeals Tribunal (AAT). In circumstances where speed of decision making is particularly important we believe there may well be merit in exploring further the CAT or AAT model. In addition to its efficiency, these models allow the development of specialist expertise and for the appointment of non-lawyers having relevant specialist skills thereby enhancing the effectiveness of the remedy, particularly in the context of substantive appeals.

ISSUE 11

Reckless Trading

Background

This section of the Submission addresses Issue 11 of the Issues Paper which raises a question as to whether there is a case for introducing an offence of reckless trading in this jurisdiction.

The background, as outlined by the Commission, is crucial to examining this question. The Commission traces this background to the 2008 banking crisis and reports which identified failings in regulatory supervision and enforcement in the years leading up to the collapse.

The Commission broadly describes any offence of reckless trading as seeking to criminalise corporate activity involving a reckless disregard within a corporate entity that its activities would cause a loss to another person. The offence would involve a significantly lower threshold than applies to existing offences, which require actual knowledge that the activity will cause loss and also an intention to defraud.

Similar Australian provisions do not appear to have been used by the authorities to tackle solely reckless behaviour and, as a result, are of limited instructive value. The UK provision criminalising reckless decisions causing the failure of a financial institution is of limited instructive value for reasons set out below.

Key Recommendations

1. There is no tangible evidence to suggest that the introduction of a criminal offence of reckless trading will protect society from what has been perceived as reckless decision-making during the financial crisis. Much of the evidence in the aftermath of the crisis indicates that key decision makers held a subjective belief – which was widespread among the banks and apparently shared by Government and by regulators - that they were acting in the best interests of their respective institutions. Accordingly, a criminal offence of reckless trading, had it existed at the time, would have been of limited applicability.
2. We submit that more effective regulatory supervision is a preferable alternative to the introduction of a vague and ill defined offence and more likely to prevent future problems arising (as opposed to a measure which would attempt to punish management after the event).
3. If any such offence is to be introduced, clarity on the elements of the offence will be required. The current language is excessively vague. Far greater precision would be needed if any such offence was to be created.
4. If any such offence is to be introduced, recklessness should be assessed on a subjective basis. Individuals acting honestly and in good faith should not be liable to criminal prosecution because, with hindsight, their course of action resulted in a loss to the company.
5. If any such offence is to be introduced, it should be limited in scope to corporate entities of systemic importance to the wider economy.

Should an Offence of Reckless Trading be introduced?

Part of the rationale for introducing the proposal is to protect society from the wider impact of reckless decision-making. It has been argued that the introduction of such an offence might focus the minds of directors, perhaps encouraging legal advice to be obtained prior to taking certain decisions to determine whether it could be characterised as reckless; in any case, it in supposed

that the introduction of such an offence is likely to slow down the taking of any potentially reckless decisions. However, there is no tangible evidence that this is in fact the case.

Even under the law as it stood at the time of the banking crisis, officers and decision-makers in financial institutions were already subject to onerous statutory, common law and fiduciary duties and could have rendered themselves personally liable to civil claims for breaching such duties. However, as the evidence from a number of institutions to the Oireachtas Bank Enquiry demonstrates, those then responsible for the affairs of the various banks generally did not consider that they or their institution were engaged in reckless conduct. Many institutions in Ireland (and in other jurisdictions) were following similar lending strategies and proved similarly vulnerable during the banking crisis. Most, if not all, of those involved apparently believed at the time that they were acting reasonably and appropriately in the best interests of their institutions. In those circumstances, it is difficult to see any basis for a prosecution under this provision even if it was on the statute books at the relevant time, regardless of whether an objective standard or a subjective standard of recklessness was employed.

In terms of securing individual accountability in a corporate context, existing statutory, regulatory and common law duties in conjunction with the existing sanctions provisions imposing civil liability and those relating to restriction and disqualification of directors, already provide a significant deterrent to reckless behaviour. In the wake of a corporate collapse, an assumption will arise that an individual should be held criminally accountable and that a custodial sentence should be handed down. However, this will (and should) only happen in the event that criminal activity has taken place. The paucity of disqualification and restriction orders imposed by the courts and the difficulties experienced by liquidators in meeting the standard of proof required in order to secure the imposition of such orders, provides good evidence that corporate collapse is rarely accompanied by improper conduct. Any criminal offence, even an offence based on recklessness, would have a necessarily higher standard of proof than that necessary to secure a restriction or disqualification order and, as such, is likely to be applicable in only the rarest of circumstances.

In the circumstances, it is doubtful whether, an offence of reckless trading would have been of much application in the context of the Irish banking crisis, even if it had been on the statute books at the time.

In fact, one of the seminal points that emerged from the Oireachtas Bank Enquiry and other enquiries into the causes of the banking crisis, was the need for more effective regulatory supervision of institutions of systemic financial importance. As a result, significant steps have been taken to reinforce the role of the Central Bank and the resources available to it. It is submitted that such regulatory supervision remains a more effective way of securing the objective presumably sought to be achieved by the introduction of criminal offence of reckless trading.

The elements of the offence: Recklessness

The ingredients of any such offence are likely to be numerous and complex and clarity on these elements will be paramount.

One of the key questions raised in the Issues Paper is the standard to be employed in assessing recklessness. While requiring greater culpability than mere negligence, recklessness (which can be broadly defined as the conscious running of an unjustifiable risk) already denotes a lesser state of blameworthiness than intent and criminalisation thereof should therefore be approached with caution.

Recklessness can be assessed either subjectively or objectively. The general rule in Ireland is that recklessness in the criminal context is assessed subjectively i.e. that the accused must actually be aware of the unjustifiable risk that they are taking; the test looks at the mind of the offender. This is in contrast with an objective assessment of recklessness whereby the actions of the accused can be deemed to be criminal where, even though actually unaware of the risk they were running, the accused reasonably ought to have been so aware. We agree with the Commission's observation that an objective recklessness definition is capable of leading to obvious unfairness as it is offensive to the principle of justice to convict someone on the strength of what someone else (the reasonable man) would have apprehended when the defendant had no such apprehension.

Furthermore, the reasonableness element which would necessarily be introduced into any gross negligence (or objective recklessness) standard is likely to pose a problem for juries. While it may be relatively easy for jurors to assess the reasonableness or otherwise of the behaviour of an allegedly dangerous driver in a manslaughter by gross negligence case, most potential jurors having been road users at some point, it may be more difficult for jurors to assess the reasonableness or otherwise of a company officer. Expert evidence will almost certainly be required given the highly specialised area with which the jury will be concerned.

Section 36 of the UK Financial Services (Banking Reform) Act 2013 (which enacted criminal offence of recklessness relating to a decision causing a financial institution to fail) adopts the subjective standard in assessing recklessness and it is submitted that this would also be the appropriate standard if such an offence was to be introduced in this jurisdiction.

For these reasons, where no good reason to depart from the well-established standard of subjective recklessness in criminal law exists, it is our view that no such departure is necessary in respect of any offence of reckless trading.

The scope of the offence

The Commission has also sought views on whether any such offence should be general or restricted to certain types of corporate activity. Any such offence should not be divorced from the background which precipitates its introduction. Some of the criticism levelled at Section 36 of the UK Financial Services (Banking Reform) Act 2013 has focussed upon the lack of safeguards against the offence being used to prosecute smaller operators as the term “financial institution” is not subject to a restrictive definition. Bearing in mind the rationale for the introduction of the offence, we are of the view that any such offence should be limited in its application to reckless trading in corporate entities of systemic importance to the wider economy.

Fully limiting the application of any offence of reckless trading to institutions of systemic importance would avoid criminalising directors of small and medium sized enterprises which are unlikely to have the resources of systemically important institutions allowing them to obtain legal advice on whether a decision (which ultimately transpired to have adverse consequences) could be characterised as reckless. Furthermore, the negative effects of reckless trading in a corporate entity other than one of systemic importance will not impact society in the ways which have prompted the Commission’s consideration of these issues and the introduction of this offence in the first place.

The UK Perspective: Section 36 of The UK Financial Service (Banking Reform) Act 2013

Section 36 of the UK Financial Services (Banking Reform) Act 2013 enacted a criminal offence of recklessness relating to a decision causing a financial institution to fail. The offence is committed where a senior manager agrees to (or fails to take steps to prevent) a decision being taken, aware of the risk that implementing that decision could cause the institution to fail, acting in a manner that falls far below what could reasonably be expected of a person in the accused’s position and the implementation of that decision causes the financial institution to fail. As outlined above, the mens rea requirement is subjective recklessness; the offence requires actual knowledge of the risk. It will not suffice to prove that the senior manager ought to have known of such a risk.

The background to the introduction of this offence is similar to the background to the Commission’s Issue Paper. Her Majesty’s Treasury (“HMT”), in considering the arguments for introducing sanctions for the directors of failed banks, accepted the important role that bank directors played in key decisions, decisions which were viewed as having far-reaching consequences, not just for the institution and its customers, but for the government, taxpayers and the wider economy. HMT took the view that this justified treating directors and senior management of banks differently from those in other types of companies. The introduction of criminal sanctions for serious misconduct in the management of a bank was portrayed as a way to shift the balance between risk and reward for bank directors.

Drafting an offence broad enough to provide a meaningful deterrent and satisfy public demand for accountability but avoiding substantial damage to the attractiveness of the financial services sector was an unenviable task. However, the UK enactment has provided us with an opportunity to critically assess its utility and its fitness for purpose and a number of important observations can be made. It is noteworthy that the Parliamentary Commission on Banking Standards (who recommended the enactment) admitted itself that it would not be easy to secure convictions for this offence.

In the first instance, defining recklessness or excessive risk-taking by bank management requires clear articulation of what constitutes normal or non-excessive risk-taking. Commercial decisions are, by their very nature, forward looking and imprecise. They involve a degree of judgment in relation to future developments that will always be less precise than, for example, the kinds of prediction possible in the natural sciences or engineering spheres. There will be an inherent difficulty in deciding whether an accused was aware of a risk but wrongly decided that the risk was insufficiently significant. The fact that these risks will invariably be judged years after they were run, in a different environment and with the benefit of hindsight will create significant challenges for a jury notwithstanding directions emanating from the judge. Causation is also likely to present huge practical difficulties.

The practicalities of conducting investigations should also be considered. Regulators are also likely to run into difficulties conducting investigations

which could potentially have an extremely wide breadth and are likely to significantly interfere with the daily functioning of the institution under investigation. The amount of data that could represent a reasonable line of enquiry requiring the prosecution to collect and review it in a case concerning the collapse of a large financial institution is likely to be significant and the task of analysing it to the required standard would be imposing. The time-consuming and expensive nature of such prosecutions are also factor for consideration particularly given the current lack of resources for prosecuting white collar crime in Ireland. Criminal trials in respect of alleged misconduct in financial institutions for Companies Acts offences during the banking crisis remain ongoing to date.

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