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Regulator decision-making in the spot light following the Advalorem Judgment

Gibraltar's approach to regulatory control in the financial services sector has recently taken centre stage following the decision of the Supreme Court in Compson v Financial Services Commission and Weal v Financial Services Commission; Compson and Weal were connected to a fund named Advalorem Value Asset Fund Limited. The case involved an appeal against a decision of the Financial Services Commission. The Supreme Court upheld that decision whereby the Financial Services Commission decided that the appellants had failed to ensure that the Fund was being operated in a "manner that was not detrimental to the interests of its participants or potential participants and in compliance with its Private Placement Memorandum"[1].

Advalorem Value Asset Fund Limited was a collective investment scheme registered in Gibraltar as an Experienced Investor Fund. Its investment objective was to "achieve capital growth through direct and indirect investment in Distressed Assets". "Distressed Assets" defined in the private placement memorandum as "Property which is put up for sale at a value which in the opinion of the Investment Director is considered to be severely depressed." None of the appellants were the Investment Director although Mrs. Compson was a director of the Investment Director.

Following an investigation into the alleged inappropriate valuation of certain investments, the Financial Services Commission decided to take disciplinary action against Mrs. Compson (a director of Advalorem Value Asset Fund Limited's investment director) and Mr. Weal (a director of the Fund).

The Supreme Court, dismissing the appeal, found:

"The Financial Services Commission and its chief executive are likely to be better placed than the Court to determine what measures are necessary in order to protect the good reputation of Gibraltar, to protect consumers and to reduce crime, as well as the other regulatory objectives... The Court in my judgment should be reluctant to interfere with a sanction imposed by the chief executive, unless clearly wrong or if the chief executive has taken irrelevant considerations into account."[2]

And:

"The chief executive is better placed than I am to determine what sanctions are appropriate to further the regulatory objectives of the Financial Services Commission".[3]

The above evidently highlights unwillingness on the part of the Supreme Court to interfere with the decisions taken by the Financial Services Commission, which effectively undermines the effectiveness of any appeal against such a decision.

With an ever growing funds industry and financial services sector, the sanctions affirmed in these cases will be a cause for concern to the many individuals who offer their services as directors to regulated companies and funds. The decisions taken demonstrate the regulator's rigid interpretation of director's duties to act with due skill, care and diligence.[4] What is more concerning is that the entire process of review under the law as it currently stands offers little effective recourse to review decisions of the Financial Services Commission that have or may have serious repercussions on individuals, their businesses and earning capacity. This is a matter of serious concern.

The judge decided to follow a procedure by way of review as opposed to rehearing in the appeal proceedings; a review does not re-hear or re-test the evidence taken into account by the Financial Services Commission in a manner that it can be fully re-appraised and evaluated. The law should permit appeals from first instance decisions by the regulator to be by way of a re-hearing, where evidence can be heard, where the appellants can put their position across and where the regulator can actually be held accountable. In this context and without an amendment to the law that intersperses an appeal by way of rehearing to an independent tribunal the current system, has a public law deficit in that there is not a fair and just system of appeal.

That being so, fairness and justice, as recognised in public law, requires that the appeal to the Supreme Court should be by way of full rehearing with evidence and the ability to cross-examine and test witnesses. The stark contrast is the process of the review of enforcement decisions applied in the United Kingdom, which allows for appeals by way of rehearing to a tribunal. This comparison suggests that Gibraltar, despite its ever growing financial services industry, is still a step behind in terms of its governance and the application of the public law principle of fairness and justice.

[1] http://www.fsc.gi/enforcement/BrianWeal-DecisionNotice.pdf & http://www.fsc.gi/enforcement/MinetteCompson-DecisionNotice.pdf
[2] Paragraph 59 of the judgment
[3] Paragraph 109 of the judgment
[4] see Norman v Theodore Goddard [1991] BCLC 1028, Re Barings plc (No.5) [1999]1BCLC and 433Gregson v HTrustees ltd [2008] EWHC 1006 (Ch)

The procedure adopted in the United Kingdom in respect of the decisions of the Financial Conduct Authority can provide guidance on this point. The Financial Conduct Authority can have its decisions reviewed by the Upper Tribunal (Tax and Chancery Chamber), it does not, however, take the form of an appeal by way of review. This tribunal will consider the matter in question completely afresh before deliberating on what should have been the appropriate course of action that the Financial Conduct Authority should have taken. These reviews are conducted via oral hearings held in public and involve the examination of witnesses and the disclosure of information applying all judicial safeguards that persons have generally and as a matter of public law. The decisions of that Tribunal may subsequently be appealed to the Court of Appeal on a point of law, which at that stage is correctly by way of review; absent this procedure there is a public law failure in the appeal process as currently exists in Gibraltar, unless and if the judgment of the Supreme Court is appealed or changes in a subsequent case.

What is particularly worrying is the manner in which the need to decide how the 'appeal' should have ultimately been heard, whether by rehearing or review, was considered without much argument.[5] The issue whether the appeal should have been heard by way of re-hearing does not seem to have been argued or considered in any depth. This seems to have resulted in the focal point of the appeal ultimately hinging on the Financial Services Commission's power to make the decision in the first place without proper judicial oversight after consideration of all the evidence as tested by cross-examination. The Financial Services Commission was totally within its remit when carrying out the investigation and making their decision[6] but this does not mean that individuals, directors and the financial services sector generally should not be entitled to a fair, transparent and orderly review of the Financial Services Commission's decision-making process by the Supreme Court.

This judgment emphasises the urgent need to review the structure and governance of the regulator's decision making processes in order to arrive at a model with a holistic approach which delivers fairness and greater effectiveness, transparency and, above all, accountability of the Financial Services Commission as the regulator.

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[5] Paragraphs 49 and 55 of the judgment
[6] S.35 Financial Services (Investment and Fiduciary Services) Act 1989

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