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Bell Gully submission to Law Commission – Issues Paper on Civil Pecuniary Penalties

1. Bell Gully is a leading New Zealand law firm, advising major New Zealand and overseas clients on all aspects of commercial law (including securities, competition and regulatory law). We frequently advise both corporate and individual clients in relation to pecuniary penalties.

2. We are grateful for this opportunity to submit on the Law Commission's first principles review of the law relating to pecuniary penalties. In this submission, we comment briefly on the following matters:

   (a) the nature of pecuniary penalties;

   (b) proper protections;

   (c) the relationship between criminal, quasi-criminal and civil proceedings;

   (d) penalty-setting; and

   (e) settlement.

3. We would be happy to discuss our views further with the Law Commission. Please contact:

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The nature of pecuniary penalties

4. In our view, the key to understanding pecuniary penalties is to begin by identifying the purposes which they serve.

5. Pecuniary penalties are not designed to compensate the victims of wrong-doing (like an award of damages). Nor are they are designed to compel a wrong-doer to disgorge ill-gotten gains (like a restitutionary remedy). They are designed to protect the public as a whole, by deterring citizens from breaching the law and punishing those who do. In other words, their functions closely match those of truly criminal sanctions.

6. Given that their principal purposes are deterrence and punishment, it is a misnomer to refer to such measures as "civil pecuniary penalties". The use of the first epithet might lead future policy-makers to assume that the more accommodating rules of the civil law must apply, when in truth those rules only apply as a matter of policy choice. In this submission, we adopt the terminology presently used in regulatory legislation and refer throughout to "pecuniary penalties".

7. We do not suggest that pecuniary penalties are truly criminal in nature. They do not attract the same stigma as a criminal conviction, or carry with them the risk of imprisonment. Nevertheless, they involve the imposition by the State on private citizens of financial and reputational costs which can be – and frequently are – very substantial. For instance, the Biosecurity Act 1993, Commerce Act 1986, Dairy Industry Restructuring Act 2001 and Hazardous Substances and New Organisms Act 1996 all contemplate the imposition of

pecuniary penalties of up to "10 per cent of turnover": in *Commerce Commission v Telecom*,[1] Rodney Hansen J noted that under section 80(2B)(b)(ii)(B) of the Commerce Act, that „10 per cent of turnover" rule meant that the maximum penalty the court could impose on Telecom was $279.2 million (it ultimately settled on a penalty of $12 million). In our view, Fisher J was quite right to describe these sanctions as "quasi-criminal".[2]

8. We hold some concerns about the proliferation of pecuniary penalties in regulatory statutes which has occurred in recent years. However, we recognise that pecuniary penalties can be an important addition to a regulator's enforcement toolkit (along with prosecution, management bans, licence revocations, cease and desist notice, leniency policies, warning letters, and educational initiatives). In some cases, they offer an appropriate, efficient and effective alternative to the pursuit of more serious criminal sanctions.

9. However, in our view quasi-criminal measures must be subject to quasi-criminal procedures and protections. If civil rules are unthinkingly applied, policy-makers and regulators may begin to perceive pecuniary penalties as an easy way to achieve the objectives of punishment and deterrence whilst neatly sidestepping the strict rules and protections of the criminal law. Those rules and protections have developed over centuries to prevent the State from abusing its power over private citizens. In twenty-first century New Zealand, their importance can hardly be questioned (especially as regulation and the investigatory powers of regulators have increased). Their abrogation in relation to pecuniary penalties would lead to substantive unfairness, regulatory over-enforcement (and hence a chilling effect on legitimate business), and a loss of confidence in government administration.

10. For those reasons, we consider that there are dangers in adopting the definition of a "civil pecuniary penalty" put forward by the Law Commission.[3] We suggest instead that any order that may be made by a court:

    (a) on the application of a regulator or enforcement agency;

    (b) in respect of a breach of legislation by a private party;

    (c) requiring that party to pay a substantial financial amount to the Crown;

    (d) without entering any criminal conviction against that party,

    should be referred to as a "pecuniary penalty".

Proper protections

11. As noted above, we consider that quasi-criminal measures must be subject to quasi-criminal procedures and protections. A potential defendant to damaging, costly pecuniary penalty proceedings is entitled to expect greater safeguards than those offered to civil litigants. We comment here on some of those safeguards.

Privilege

12. The privilege against self-incrimination (**PASI**) is one of the key safeguards upon which the integrity of the criminal law depends. It recognises the importance of individual autonomy, of constraining State power, and the seriousness of criminal conviction and severity of criminal punishments. In our view, if a party may in the future face criminal proceedings brought

1 (2011) 13 TCLR 270 at [47]. This judgment dealt with penalty issues in connection with the data tails litigation.

2 *Commerce Commission v Roche Products (New Zealand) Ltd* [2003] 2 NZLR 519 at [57].

3 Issues Paper at [7.1].

under a regulatory statute then he should be entitled to invoke the PASI and maintain his silence.

13. Equally, we consider that if a party may at some point in the future face quasi-criminal proceedings under a regulatory statute then he should be entitled to invoke the privilege against self-exposure to penalty (**PASEP**). The omission of the PASEP from the Evidence Act 2006 was perhaps not fully thought through and should be revisited. As noted above, the main purposes of pecuniary penalties are punishment and deterrence – the same aims which motivate criminal sanctions. Reinstating the PASEP in the Evidence Act would recognise the rights and dignity of private parties, support our system of accusatorial justice, preserve a fair balance between State and individual, and accord with section 25(d) of the New Zealand Bill of Rights Act 1990. There is no risk that the revitalisation of the PASEP would compromise the administration of civil remedies, as it would only be available in respect of proceedings which could result in the imposition of a penalty (and, indeed, could be limited to cases involving pecuniary penalties).

14. If Parliament were concerned that the operation of the PASEP would neuter the effectiveness of a particular pecuniary penalty regime, then it could give consideration to disapplying the PASEP whilst simultaneously declaring that answers given by a potential defendant could not be used in proceedings against him (similar to the approach taken in sections 27 and 28 of the Serious Fraud Office Act 1990). The point here is that Parliament should have that debate in connection with each regulatory regime, rather than simply assume that the PASEP can never apply.

Standard of proof

15. We recognise that the effectiveness of pecuniary penalties as a regulatory tool would be diminished were the courts to demand proof beyond reasonable doubt in all cases. Nevertheless, we have emphasised that pecuniary penalties are a grave sanction, serving the same ends as criminal sentences. It follows that the courts should not impose pecuniary penalties without a high degree of confidence that the defendant has indeed committed the conduct of which he has been accused.

16. Weighing these factors, we consider that it may be worth exploring in a policy-making context the possibility raised by the Law Commission that the regulator should be asked to prove the necessary elements to an intermediate standard of proof (falling between the civil „balance of probabilities" and the criminal „beyond reasonable doubt"). The precise definition of the standard would merit further consideration, but we see some attraction in the „clear and convincing evidence" standard applied in the US.[4] Such a standard may more properly reflect the function and severity of pecuniary penalties without making it unduly difficult for the regulator to obtain an order in appropriate cases.

Fault

17. The fact that many pecuniary penalty provisions do not presently require the prosecutor to prove fault may lead to a misconception that it is appropriate for policy-makers to impose strict or absolute liability. In our view, the significance and severity of pecuniary penalties demonstrates that serious consideration should always be given to requiring some degree of intention or knowledge as a pre-requisite to liability. It is not sufficient that fault be taken into account only at the penalty-setting stage.

18. Equally, we consider that some degree of fault should be required before the courts can impose accessorial liability or attribute the conduct of an individual to a corporate (or vice versa). We cannot see any basis for deeming a party to be automatically liable for the conduct of another party in a quasi-criminal context. That places too great a compliance burden on both individuals and organisations.

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[4] Issues Paper at [6.27].

Defences

19. Although we do not see any great benefit in exhaustively setting out defences in legislation, limitation is one form of defence which should perhaps be set out in the particular regulatory statute. Relying on the general rules of the Limitation Act 2010 risks confusion. In particular, where the statute provides for both civil and quasi-criminal liability in respect of the same conduct, the limitation period should be the same in each case (for instance, pecuniary penalty proceedings under section 80 and actions for damages under section 82 of the Commerce Act are subject to similar three year / ten year limitation periods). The same should be true where the statute provides for both quasi-criminal and criminal liability. The contravening conduct in each case is the same.

The relationship between criminal, quasi-criminal and civil proceedings

20. A particular set of issues is presented by the overlay of criminal, quasi-criminal and civil liability in the context of regulatory legislation. Careful thought needs to be given to the interaction of such heads of liability to avoid unfairness to potential defendants.

Double jeopardy

21. Enforcement proceedings of any nature are incredibly taxing for citizens, and often follow lengthy and similarly taxing regulatory investigations. They are subjected to substantial expense, reputational harm, distraction and anxiety (even before the court makes its decision). Equally, the possibility of bringing multiple proceedings against a defendant offers the prosecutor or regulator two bites at the cherry and hence the ability to wear down a defendant and exhaust his resources, pressuring him into settlement.

22. The rule against double jeopardy is designed to prevent such unfairness. For that reason, we consider that it protects against the bringing of multiple proceedings just as much as it protects against the imposition of multiple penalties. In other words, the rule should apply even before the first proceedings have been withdrawn or concluded. In our view, in this context the rule against double jeopardy should be stated in these terms:[5]

    (a) once criminal proceedings have been commenced, no pecuniary penalty proceedings may be commenced; and

    (b) once pecuniary penalty proceedings have been commenced, no criminal proceedings may be commenced.

23. Unless the defendant itself consents, we cannot see any reason why a regulator should be able to commence criminal proceedings against a defendant and then „downgrade" to pecuniary penalty proceedings if its case turns out to be weaker than expected; similarly, it should not be able to 'upgrade' its case by commencing criminal proceedings once it has had the benefit of watching its pecuniary penalty proceedings unfold. There is no hardship in this – it simply represents a fair, principled and consistent restraint on the exercise of State power against the individual.

24. The interface with exemplary damages should be treated in a similar way. As exemplary damages serve a punitive function, they have more in common with pecuniary penalties and criminal sanctions than they do with compensatory damages. For reasons that are not perfectly clear, some regulatory statutes allow the court to impose both pecuniary penalties

[5] Some statutes provide for different regulators to take enforcement action in respect of the same conduct ie there is overlapping jurisdiction. To state the obvious, the rule should apply no matter which regulator takes the initial action.

and exemplary damages in private proceedings in respect of the same conduct (eg see section 82A of the Commerce Act). In our view, that also violates the rule against double jeopardy as both mechanisms are intended to punish rather than compensate.

Use of evidence

25. If the regulator is not to be put to an election of the type described above, clear rules must be put in place in relation to the use of evidence acquired by the regulator. Otherwise, there is an obvious risk that the regulator will be able to take advantage in criminal proceedings of information acquired in pecuniary penalty proceedings. That risk would be even more pronounced if the relevant pecuniary penalty proceedings are subject to usual civil procedural rules (such as discovery, or interrogatories). Any conviction obtained in the criminal proceedings would be tainted by unfairness.

26. In our view, if a regulator is to be free to commence both criminal or pecuniary penalty proceedings at any time then:

    (a) the regulator should not be permitted to use in criminal proceedings evidence it acquired by reason only of having previously commenced pecuniary penalty proceedings;

    (b) the regulator should not be permitted to use in criminal proceedings evidence which another regulator acquired by reason of having previously commenced pecuniary penalty proceedings (ie where there is overlapping jurisdiction).

Privilege

27. The unfairness associated with the kind of 'cross-pollination' just described may extend beyond evidence. For instance, the defendant to a pecuniary penalty proceeding may be required to make its defence plain in pleadings or evidence – that could be of great advantage to the regulator in subsequent criminal proceedings, and would be a signficant erosion of the right to silence in criminal matters.

28. As noted above, we consider that the PASI should be available in connection with all criminal proceedings and the PASEP in connection with all quasi-criminal proceedings. The possibility that a regulator pursuing a pecuniary penalty may later seek a criminal conviction weighs in favour of the scope of the PASEP matching that of the PASI. Otherwise, a defendant could be compelled to provide information to a regulator in connection with pecuniary penalty proceedings only to find that information being used against it in connection with criminal proceedings.

Penalty-setting

29. The process by which the court determines the applicable pecuniary penalty is often over-looked in favour of questions of liability. However, the level at which the relevant penalty is set is obviously capable of making a very great difference to the defendant.

Maximum penalties

30. Statutory maximum penalties have considerable symbolic value, guiding courts as to the sanctions that should be imposed in the very worst cases. As we have already noted, some maximum pecuniary penalties are presently capable of being inordinately large: regulatory statutes provide that a court may impose a pecuniary penalty of $10 million (or more). There is a danger that the perception that 'corporates can afford large penalties' will lead to policy-makers introducing higher and higher maximum penalties, and so to courts feeling compelled

to impose higher and higher penalties. In our view, in a small economy like New Zealand a sense of perspective must be preserved.

31. We consider also that careful thought should be given to the place of pecuniary penalties in an enforcement toolkit. We have emphasised that pecuniary penalties should be seen as more serious than ordinary civil remedies, but less serious than truly criminal sanctions. For that reason, we consider that it would be very rarely appropriate for a maximum pecuniary penalty to be set at or above the maximum (criminal) fine that could be imposed for that conduct. To do so would give regulators a perverse incentive to take pecuniary penalty proceedings rather than pursue more demanding criminal proceedings. The proper approach must surely be to set maximum pecuniary penalties at a level materially lower than the maximum fine for criminal conduct of that nature.

Relevant factors for court in setting penalty

32. As the Law Commission has pointed out, there are a number of factors which can be relevant to the court's determination as to an appropriate penalty.[6] Not all of those factors apply with equal strength in all regulatory regimes. Indeed, not all of those factors apply with equal strength even in cases brought under a particular regulatory regime. Some will be entirely irrelevant in some cases. In our view, careful consideration should be given to whether it is necessary for each regulatory statute to set out an exhaustive list of relevant factors (or even a core list of relevant factors). The better approach may be to allow the parties and the courts to identify the factors relevant in a particular case.

33. It goes without saying that we see no basis for legislation to direct a court that it *must* impose a pecuniary penalty (as in section 80(2) of the Commerce Act, which states that the court must impose a penalty on an individual in certain circumstances). Such rules could just lead to a court imposing a nominal penalty, or being compelled to impose an arbitrary statutory minimum. In our view, the court should consider the same range of factors in determining whether to impose a penalty at all as in determining what magnitude of penalty to impose.

Pecuniary penalties and compensation

34. We have emphasised in this submission that pecuniary penalties are punitive and deterrent rather than compensatory. Indeed, the imposition of pecuniary penalties may be quite contrary to the interests of other affected parties (especially if the defendant nears insolvency). In our view, it may be worth considering further whether a pecuniary penalty should be imposed if to do so would unfairly disadvantage the victims of wrong-doing.

35. Pecuniary penalties in the securities law context provide a useful illustration. An order requiring a director to pay a penalty to the Crown will deplete and may even exhaust the pool of resources available to compensate parties who have suffered actual loss (such as the company, its shareholders and security-holders). In that situation, a pecuniary penalty may only end up „punishing" creditors.

Settlement

36. It is both common and appropriate for pecuniary penalty proceedings to be settled by agreement between the regulator and the defendant. Such settlements allow the parties to avoid unnecessary expense and litigation risk.

37. In our view, there may be limited benefit in requiring the court to further scrutinise penalties agreed between regulators and defendants. In nearly all cases, the regulator is an experienced and well-resourced public body charged with acting in the public interest – it is

[6] Issues Paper at [7.51], [7.56] and [7.58].

unlikely that such a body would agree to accept payment by the defendant of a particular sum without good reason. We consider that further thought should be given to providing a statutory basis for regulators to agree penalties with defendants, and enforce compliance as required.

Concluding comments

38. We are conscious that pecuniary penalty provisions have been developed by a range of policy-makers within Government over a lengthy period. We consider that a single flexible expression of principles should now be developed to guide policy-makers in the future, so as to ensure consistency and coherency across regulatory regimes. As the Law Commission has suggested, the best approach may be to insert a chapter in the LAC Guidelines to deal with the use of pecuniary penalties.

39. We wish to express our appreciation for the Law Commission"s carefully researched and presented Issues Paper. We look forward to considering its recommendations.

Bell Gully
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