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24 March 2017

Dear Roderick

Corporate Liability for Economic Crime: Call for Evidence

Response of the Corporate Crime and Corruption Law Committee of the City of London Law Society (CLLS)

- The CLLS represents approximately 17,000 City lawyers through individual and corporate membership, including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multijurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

- This response has been prepared on behalf of the CLLS by its Corporate Crime and Corruption Law Committee, the members of whom are listed on the committee's website www.citysolicitors.org.uk. Please note that not all the opinions expressed in this response are necessarily the opinions of every member of the committee, or those of the firms in which they practice.

- We welcome the opportunity to provide submissions to the Ministry of Justice on this important topic.

Introduction and summary

1. The Committee welcomes the opportunity to contribute to the formulation of the Government's policy in the important area of corporate criminal liability. We have responded in detail to the questions posed in the Ministry of Justice's Call for Evidence on Corporate Liability for Economic Crime (the **Call for Evidence**) below and would be happy to discuss this further with the Ministry if that would be helpful.

2. In summary, the Committee is of the view that the evidential basis for a wide-ranging change to the identification doctrine in English law is lacking. The Committee has not

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seen evidence that large companies organise their affairs so as to obscure the involvement of their directing minds in criminality. The underlying policy question of whether the existing requirement to establish corporate mens rea through a directing mind should be replaced with negligence based or strict liability needs careful examination. Of the options for reform, requiring the prosecution to establish that the company failed to prevent economic crime is preferred. However, regulatory reform and effective individual accountability regimes are likely to be more effective in driving changes in corporate conduct. There is a real risk that creating corporate offences for compliance failings will burden business with a significant additional compliance cost. Further, the risk that the financial services sector will face regulatory and criminal sanctions needs to be managed. We would, however, support continued/increased funding for the relevant regulators and prosecutors to encourage adherence to the existing framework of regulatory provisions and criminal law.

3. If the Government nevertheless considers that the existing regulatory or criminal framework is inadequate in addressing corporate responsibility for combatting economic crime (as defined in the Call for Evidence), the Committee suggests that the Government closely consider empirical data as to where the risks of economic crime are likely to lie, what safeguards against those risks there are in the existing and potential future framework, and the costs of extending existing safeguards might

be, with a view to making any new regulatory or criminal provisions targeted, proportionate and risk-based. We note that the current framework includes:

3.1.1 the Money Laundering Regulations 2007 (which, among other matters, make it an offence for organisations within the regulated sector (as defined in the Money Laundering Regulations – this goes wider than financial services) not to have adequate policies and procedures to deal with money laundering risks;

3.1.2 the directors' disqualification regime;

3.1.3 the Financial Reporting Council, which recently called for regulatory powers over directors in respect of company accounts, as part of its review of the UK Corporate Governance Code;

3.1.4 civil recovery of assets;

3.1.5 civil claims for fraud and misrepresentation; and

3.1.6 the FCA Handbook, including the obligation on authorised firms to have adequate systems and controls to combat financial crime (SYSC 6.1), as well as the Senior Managers Regime (**SMR**) and Senior Insurance Managers Regime (**SIMR**).

4. In general, however, the Committee believes that any additional measures taken after such an assessment should be regulatory, rather than criminal, in nature. We support the recommendation of the Law Commission that:[1]

"*The criminal law should only be employed to deal with wrong-doers who deserve the stigma associated with criminal conviction because they have engaged in seriously reprehensible conduct. It should not be used as a primary means of promoting regulatory objectives.*"

The identification doctrine

5. By way of background to the Committee's response to the questions on the identification doctrine, the Committee notes that it is trite law that most criminal offences, including bribery, money laundering, fraud and false accounting, require both *mens rea* and *actus reus* to be proved. As noted in the Call for Evidence,[2] in a corporate context, while the *actus reus* may be committed by any of the company's employees or agents, the *mens rea* must be that of directing mind and will of the company, which will usually be (very) senior management.

6. It follows that, under the law as it stands, in cases where *mens rea* is an element of the offence, unless the requisite *mens rea* is found among the directing mind and will of the company, the company is not guilty of the criminal offence.

7. The Committee has some concern that some of the objections to the effect of the identification doctrine noted in the Call for Evidence do not give sufficient weight to that corollary. In particular, the Call for Evidence cites difficulties in prosecuting large multinational corporations because of complex management structures, the differences in effect between small and large companies and ensuring the effectiveness of Deferred Prosecution Agreements (**DPAs**) as arguments for changes to the identification doctrine.[3] However, if the company is not in fact guilty, prosecution difficulties, the differences in the impact on large and small companies and DPAs are irrelevant. These objections assume that the company <u>*should*</u> be criminally liable, even though, under the law as it stands, the company is not guilty of the criminal offence. They therefore merely beg the question as to whether the company – which, the Call for Evidence notes, is an entity distinct from its owners, officers and employees[4] - should be criminally liable for the acts of individuals acting as agents or service providers, even if those individuals are operating at some distance from, and without the knowledge of, the company's most senior management decision making organ, the board of directors.

8. This underlying policy question as to whether it is appropriate for the company to be criminally liable for the acts of others has been explored only partially in the Call for Evidence.[5] If the Government were to consider this further in its assessment of corporate criminal liability, the Committee believes that the following would need to be taken into account, among other matters:

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1 Proposal 1, paragraphs 1.28, 1.31 and 3.137, Consultation Paper No 195 "Criminal Liability in Regulatory Contexts" (2010).

2 Pages 12-13.

3 Pages 3, 13, 14.

4 Page 6.

5 The Committee notes the fuller exploration in Part 5 of the Law Commission's Consultation Paper No 195 "Criminal Liability in Regulatory Contexts" (2010).

8.1 the moral significance and weight of a criminal conviction (given that any other penalty for a company is likely to be financial, in the short (fines, confiscation) or long (debarment) term, whereas an individual may also be imprisoned);

8.2 the impact on shareholders, who have little control over a company except through voting for its memorandum and articles and for its directors, but would bear the brunt of any diminution in the assets of the company;

8.3 the emphasis placed in English criminal law on the requirement for *mens rea*;

8.4 the importance of the distinction between criminality and negligence, given that negligence has not, historically, been sufficient to found criminal liability in English law;

8.5 the distinction between a company and its employees and agents;

8.6 the difficulty for a company in controlling and/or supervising all aspects of the activities of its employees and agents, which increases as the size of the company increases;

8.7 the deterrence value of a conviction (ie in effect, the potential for improvement in corporate governance procedures);

8.8 the impact of a criminal conviction on the company's future operations in terms of business licences, regulatory approvals and potential involvement in public and other procurement bids;

8.9 the name of the criminal offence in terms of whether it indicates that the company has been guilty of dishonesty or negligence; and

8.10 international comparators (not only in the US).

9. We now turn to the specific questions raised in the Call for Evidence.

Question 1: Do you consider the existing criminal and regulatory framework in the UK provides sufficient deterrent to corporate misconduct?

10. Overall, the Committee considers that the existing criminal and regulatory framework in the UK does provide sufficient deterrent to misconduct by both individual employees/agents and by companies (on the basis of the identification doctrine).

11. Although the Call for Evidence refers only to the regulation of financial services, in particular by the Financial Conduct Authority, we note that all those in the regulated sector for the purposes of Regulation 3 of the Money Laundering Regulations 2007 are required to establish anti-money laundering procedures and are regulated by specified regulators. That is a much broader group than financial services alone. Some sectors are also regulated more broadly. For example, offences such as false accounting and fraud committed by those in the legal or accounting professions would attract regulatory sanction.

12. The Committee notes, however, that the framework's deterrence value is predicated on the frequency of enforcement. The Committee also considers that the strongest deterrent is provided by the prosecution of, or enforcement action against, senior

managers, rather than companies. This has been recognised by the introduction of the SMR and SIMR regimes which will be enforced by the Financial Conduct Authority.

13. The Committee would support continued/increased funding for the relevant regulators and prosecutors to encourage adherence to the existing framework.

Question 2: Do you consider the identification doctrine inhibits holding companies to account for economic crimes committed in their name or on their behalf?

14. The Committee notes that the nature of the identification doctrine is such that a company cannot be criminally liable for all economic crimes committed in the company's name or on its behalf. It will be liable for those crimes only where the directing mind and will of the company is involved in the wrongdoing. As noted above, the question of whether this is the proper policy position has not, in the Committee's view, been fully explored in the Call for Evidence.

15. Being convicted of a criminal offence, however, is not the only method of holding a company to account. Depending on the circumstances, even if it is not criminally liable, the company may be penalised for such conduct, whether by way of regulatory sanction, civil recovery of assets or civil claims (such as in follow-on damages claims for breaches of competition rules). It may also suffer serious reputational damage through adverse media reporting and/or Parliamentary scrutiny. The latter may be felt particularly by large listed companies, whose shares may suffer significant falls in value. The company may, therefore, be "held to account" by these means without itself committing a criminal offence.

Question 3: Can you provide evidence or examples of the identification doctrine preventing a corporate prosecution?

16. While the Committee is not able to give any specific examples, owing to obligations of confidentiality, its members have rarely, if ever, come across companies decentralising responsibilities to prevent the *company* being liable, as suggested in the Call for Evidence.[6] Businesspeople are not, in the Committee's experience, so focused on the identification doctrine as to run an entire business on the basis of avoiding a corporate conviction. (However, the Committee's experience is that in the United States where threshold for criminal liability of a corporation for crimes involving *mens rea* is lower, and prosecutors are more active, care is often taken to avoid recording legal advice on potential liability in writing.)

17. The Committee has come across cases where the evidence trail cannot be followed to a certain individual or more generally further up the management structure. If more senior wrongdoers were in fact involved, and evidence has been suppressed and/or not created, the Committee considers that steps of this kind would be more likely to be taken in order to avoid *personal* criminal liability on the part of the senior wrongdoers, rather than corporate criminal liability. (Equally, it may simply be that the demands on the management time of more senior wrongdoers were such that they deal with matters by less formal face-to-face meetings and calls.)

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6 Page 13.

18. In such cases, the identification doctrine may prevent a corporate prosecution: there would not be a realistic prospect of conviction on the evidence. However, that does not necessarily mean that a company should be prosecuted in such circumstances. It may simply be that the more senior wrongdoers were not involved and the company, under the identification doctrine, is innocent.

19. The Committee would ask the Government to consider carefully empirical data from organisations such as the SFO, CPS and the FCA as to investigations / prosecutions / conduct which they consider have prevented prosecuting companies for substantive offences where it is clear that companies were complicit in substantive offending rather than culturally failed to take steps adequately to prevent such offending. Further legislative reform would be necessary only if prosecutors were persistently thwarted by the issue. In the Committee's experience, instances of companies being complicit in the commission of substantive economic crime offences are few and far between and tend to occur in smaller companies where their purpose from the outset is fraudulent and where the identification principle (in a well-resourced investigation) does not provide a barrier to prosecution.

Question 4: Do you consider that any deficiencies in the identification doctrine can be remedied effectively by legislative or non-legislative means?

20. It is unclear to the Committee what deficiencies the Government is seeking to remedy.

21. If the Government considers that companies should be criminally liable for actions which have taken place without the knowledge or involvement of senior management as a general rule, the Committee believes that this could only be effected by legislative means.

22. If, however, the concern is directed at the steps companies are (or are not) taking to combat economic crime (as defined in the Call for Evidence), the Committee believes that any deficiencies should be remedied, in the first instance, by risk-based, targeted and proportionate regulation, for the reasons set out below.

Question 5: If you consider that the deficiencies in the identification doctrine dictate the creation of a new corporate liability offence which of options 2, 3, 4 or 5 do you believe provides the best solution?

Preferred option

23. For the reasons set out above, the Committee considers that further criminal or regulatory reform is unnecessary, as we fail to see an evidential basis for the notion that large corporates are involved in the economic crimes contemplated by the Call for Evidence for their own benefit.

24. Industry specific regulatory reform such as in financial services is the most proportionate response as a regulatory scheme would be specific to that industry, recognise the risks associated with it, provide for regulations that meet those specific risks, rather than a catch all type of offence as is contemplated by options 1, 2, and to a certain extent 3 and 4. It would also mean that in those industries/sectors where the risk is deemed low enough not to need regulating, companies would not have to engage in lengthy, cost- and resource-hungry adequate procedure exercises. In fact,

as should be the case, it would mean that a collaborative approach could be taken between the Government and industry regulators with the Government shouldering most of the time, cost and resource burden. This approach has proved effective in financial services and to a certain extent under the guidance of HSE in various industries.

25. However, if the Government were to introduce a new corporate liability offence, of the options put forward, the Committee would favour option 4. The Committee considers that, absent industry specific regulatory reform, option 4 would best deal with the mischief at which the Call for Evidence is aimed, i.e. to clean up corporate behaviour and to ensure companies take action to prevent economic crime and to criminalise companies who have a culture that allows economic crime to thrive. Both companies and prosecutors have some experience of that model already and to a certain extent understand it.

26. The Committee would prefer option 4 to option 3 because, unlike bribery and corruption or tax evasion which are specific offences which companies can deal with by focused and proportionate policies, the offences contemplated by the Call for Evidence, in particular fraud, are broader and encompass a myriad of different behaviours which would make it extremely difficult for companies to properly and proportionately identify both the risks of such offending and the policies and procedures which might prevent an offence occurring or avail them of a proper defence. We consider this might be an argument in favour of option 4 more than option 3 as that model places the burden on the Crown and recognises the nuances between bribery and corruption and wider economic crime. It would also recognise that a significant proportion of the companies that are likely to be at risk of economic crime being committed in their name are already subject to regulatory schemes which mitigate those risks significantly.

27. If further criminal offences are absolutely necessary Option 4 alongside retaining the current identification principle would allow the Crown the toolkit to still prosecute companies for the substantive offence in the right case (which they have been able to do by way of DPAs or prosecutions) where the evidence is there. There is a strong argument to suggest that the Government already has the tools to prosecute companies for economic crime but not the resources.

28. The Committee also considers it important that the name of the offence correctly reflects the *mens rea* and directing mind and will principles. For example, "breach of duty" or "failure to prevent" would be more accurate a description of the corporate failing than "fraud" or "money laundering".

Adequate procedures

29. If option 4 (or 3) is favoured, the Committee would urge the Ministry of Justice to produce detailed guidance not only on the scope and applicability of the substantive offence (akin to section 7 of the Bribery Act) but also on any procedures considered adequate to prevent commission of the offence or act as a defence. There may be economies of scale to achieve for companies in undertaking new economic crime "adequate procedures" work alongside ongoing bribery and corruption work, particularly with risk mapping, training and the like. However, unlike bribery, where widespread international comparison was available before the introduction of the Bribery Act, procedures to prevent money laundering, fraud and false accounting

would be entirely new internationally and domestically (outside the regulated sector under the Money Laundering Regulations 2007) and therefore unfamiliar to many businesses.

30. The Committee would, therefore, ask the Government to legislate only once it has a settled sense of the expectations as to adequate procedures in light of what it has learnt to date. A criticism of the guidance published in respect of the Bribery Act is that it did not go far enough to give comfort to companies as to what they were or were not doing would be deemed adequate. Companies have to a certain extent had to resort to professional advice either from lawyers or compliance consultants and many companies have had to take a piecemeal approach to policies and procedures and await jurisprudence on the issue, which has not been forthcoming in the four cases to date under Section 7 of the Bribery Act. This has resulted in significant cost, time and resources, often disproportionate to the actual risk and the expectations seen in the jurisprudence. We would urge the Government to use its experience of the Bribery Act and the SFO's and courts' approach to the inadequacy of procedures to inform any guidance published and to ensure a more detailed, robust and prescriptive approach to any such guidance.

Impact on senior management

31. We would, however, point out that further legislation to criminalise corporate behaviour is unlikely to satisfy the public desire to hold those at the top of such organisations to account. There has been criticism in the wake of significant misconduct within companies that results in the conviction of employees and/or regulatory fines for the company that those at the top escape criminal liability. The accountability of top level individuals, who were not themselves involved in the wrongdoing (or cannot be evidenced to have been involved) and are not personally culpable might better be achieved through regulatory schemes akin to the SMR and SIMR as seen in financial services or an extension to the directors' disqualification regime. The Committee also observes that the Financial Reporting Council has recently called for regulatory powers over directors in respect of company accounts, as part of its review of the UK Corporate Governance Code. This may be an alternative way of addressing accounting breaches which do not justify criminal culpability.

Question 6: Do you have any views on the costs or benefits of introducing any of the options, including possible impacts on competitiveness and growth?

Option 1 – Amendment to the Identification Doctrine

32. The Committee acknowledges that there can be some uncertainty as to the application of the identification doctrine.[7] There may be some benefit to bringing clarity as to the extent of the identification doctrine. Given the seriousness of the types of crime under consideration in the Call for Evidence, the Committee suggests that it should be limited to those who make decisions on behalf of the company at the highest level below the members' meetings.

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7 Explored in some detail in Part 5 of the Law Commission's Consultation Paper No 195 "Criminal Liability in Regulatory Contexts" (2010).

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33. On that basis, option 1 should involve the least cost of compliance because it would focus on the senior level decision makers. If, however, the identification doctrine were to be expanded to cover a significant number of more junior staff, that may have the effect not only of creating more governance bureaucracy to manage risks for those less senior individuals, but also of increasing the labour costs of a company. At present those at the top of companies are remunerated in a way so as to compensate them for the significant risks/responsibilities associated with acting on behalf of the company. Companies may face a situation whereby those employees further down the chain are reluctant (without significant remuneration) to take those jobs where their exposure to criticism/dismissal for acting on behalf of the company is increased by reason of changes to corporate criminal liability. This may have the effect of reducing the competitiveness of UK companies who have to absorb these fixed costs.

34. More importantly, however, the Committee would also point out that this option does not appear to address the perceived mischief which is bad corporate behaviours and cultures that encourage criminal activity on behalf of the company as it still derives the liability from individual behaviours not the corporate as a whole.

Option 2 – Strict (Vicarious) Liability

35. This option has the disadvantage of branding the company as fraudulent or dishonest when only a single errant officer is acting on behalf of the company in breach of express duties to the company. The demise of Arthur Andersen is an example of the potential damage that can be caused by a charge in which it is implicitly alleged that a company is fraudulent or dishonest when that alleged misconduct is confined to one branch of a large business organisation. The Committee would argue that the majority of economic crime committed in large companies is not wholesale and wide ranging and to stigmatise the company for the actions of an individual who is not part of senior management, as option 2 would do, is to go too far. If there is a failing at the corporate level, it is likely to be a question of a lack of sufficient systems and controls.

36. One of the examples cited in the Call for Evidence for the effectiveness of this option is its use and operation in the US. The Committee is concerned, however, that this neglects to recognise the relative lack of front-end regulation in the US, the historic and well established use of DPAs there, the fact that debarment following conviction need not be permanent, the significant discounts afforded which go well beyond that offered in the UK and the well-resourced investigative and prosecutorial bodies which result in relatively quick resolution by comparison with the UK.

37. The Committee considers that this option is likely to result in the most significant cost, time and resource burden on companies. It is not evident, either, given the US experience, that it would lead to a significant increase in corporate governance standards.

38. This option may also lead to satellite litigation, particularly in relation to companies that seek to rely on breach of contractual terms, to offer a defence to any criminal investigation pursuant to legislation which enacts vicarious liability. The option also puts larger companies at greater risk of conviction than small companies because they have a larger number of employees and other agents for whose acts the

company is liable. Further, the nature of convictions that companies face under this option put them at greater risk of being banned from procurement processes.

Option 3

39. Whilst the most clearly understood, given its use under the Bribery Act, the Committee is concerned that this option may lead to a lack of sufficient legal certainty for reasons set out above (difficulty with guidance, risk mapping etc). This is particularly so given the broad range of offences/conduct contemplated by the Call for Evidence. Unlike bribery and corruption which are relatively narrow concepts, the risks of which are fairly easily identifiable, offences such as fraud and conspiracy to defraud are extremely wide and can be committed in all manner of ways. There will be significant monetary, time and resource costs associated with companies, in particular, large multinational companies undertaking projects to identify where their economic crime risks lie both within sectors of the business but also in which jurisdiction.

40. In the short to medium term the significant costs that companies are likely to incur to assess risks and implement economic crime polices/processes (as has been the case with the Bribery Act) could adversely affect their competitiveness in trade deals, procurement exercises and in their ability to export, particularly at this sensitive time for UK trade amidst Brexit negotiations.

41. The Committee also notes that if money laundering is included in the economic crimes covered by an offence modelled under Options 3 or 4, there is likely to be a significant increase in defensive reporting to the National Crime Agency under the Proceeds of Crime Act 2002. Additional resources may be needed by the National Crime Agency to administer those additional reports.

Option 4

42. The observations made in respect of option 3 equally apply to option 4.

43. While the Committee would prefer option 4 to 3 for the reasons set out above, there is a concern that option 4 could lead to both lengthy investigations exploring all aspects of the company's systems and controls and extremely, long and document heavy trials and satellite litigation and put significant strain on the resources of the prosecution/investigation.

Option 5

44. One of the main concerns the Committee has over a general legislative reform to respond to the perceived risk that corporates are evading criminal liability due to the operation of the identification principle in conduct amounting to economic crime is the uncertainty that would flow from such a broad statutory offence and the uncertainty over what amounts to adequate procedures. In addition, criminal legislative reform would neglect to recognise that some sectors/industries pose a greater risk than others and as such should bear a greater burden than others.

45. One advantage of regulatory reform on a sector by sector basis is that any regulatory scheme would be designed to meet the specific needs of the sector and thus likely to be more effective in preventing economic crime but also it is likely to result in

companies engaging more meaningfully. It is likely to lead to savings as any policies and procedures can be more focused and narrower.

46. The Government may also consider that the regulators are best placed to supervise and enforce steps being taken within the sector/industry. Regulators are often funded by those they regulate (FCA for example) and are often well resourced and attract experts to work within their ranks. These circumstances may be better suited to changing the corporate behaviours that criminal legislative changes are designed to assist with by way of deterrent.

Question 7: Do you consider that the introduction of a new corporate offence could have an impact on individual accountability?

47. It would appear that there are two different issues at play in this question. One is the issue of individual accountability to the corporate and the other is (criminal) legal accountability of the individual.

48. In respect of (criminal) legal accountability, the Committee does not consider that the new proposals will hold those not already accountable, more accountable and they are unlikely to impose liability or individual accountability on senior decision makers that the public want to see prosecuted (although the DPA framework may result in companies cooperating with the authorities' investigations into individuals). If the evidence is there in relation to the consent and connivance of the board members and senior managers, then prosecutors have an adequate toolkit and could use that existing tool kit. We understand that there are currently over 400 statutes covering a range of economic and other activity that create offences that allow for individuals to be prosecuted because they have participated in the offending through consent, connivance or neglect. Many of the offences to which DPAs apply carry this form of liability.

49. To impose greater accountability on those individuals under the criminal law, the Government would have to further legislate to criminalise consent, connivance and neglect in relation to economic crime, where this does not already exist. However, the Committee does not believe that neglect forms an appropriate basis for the criminal liability of an individual (although it may form the basis for a regulatory sanction).

50. Any plans to broaden corporate criminal liability for economic crime may result in a corresponding increase in consent, connivance and neglect convictions of senior managers. This may have the unintended effect of reducing the willingness of people to serve in senior corporate positions.

51. In relation to individuals' accountability to the company, if companies were to become more easily prosecuted, this might result in greater internal monitoring and auditing the work of individuals to assist in establishing "adequate procedures". This would likely lead to greater accountability to the employer and may lead to employees who are discovered to engage in behaviours caught by the legislation being more readily dismissed. This might be by reason of companies deeming it a necessary step to mitigate losses, reputational damage, to reduce the risk of an investigation or once in an investigation to try and improve chances of diverting away from prosecution.

Question 8: Do you believe new regulatory approaches could offer an alternative approach, in particular can recent reforms in the financial sector provide lessons for regulation in other sectors?

52. The Committee considers that there is significant merit in the Government giving consideration to a regulatory approach to corporate responsibilities as most effectively seen in the financial services industry. One only has to look at the recent £163m fine imposed on Deutsche Bank by the FCA to recognise the potential such an alternative has. As noted above, the Committee would also point to the new SMR in the financial services industry as being a positive example of where individual accountability can be increased without creating new criminal offences.

53. The Committee's experience of advising companies and individuals in financial services, demonstrates to the Committee that there is greater accountability in the financial services than in other sectors and that this is contributing to promoting better cultures and corporate behaviours. Placing positive obligations on senior managers and also requiring them to be fit and proper, whilst placing a linked burden on the company to monitor and report on any such regime, places the company at the heart improving corporate behaviours. The Committee considers that to work there have to be positive reporting/notification requirements which ensure that both the company and the regulator are aware of what is going on and when steps are not being taken, such that intervention can occur. This type of regulatory approach also has the advantage of greater legal certainty for the company allowing them to assess and take the necessary steps in any given industry.

54. One significant benefit of an approach like the one adopted in financial services is the placing of the supervision and enforcement functions within the same organisation. This properly recognises that enforcement rarely acts as a sufficient deterrent to improve corporate behaviours but that when coupled with supervision functions, which help companies to comply with rules and helps them improve corporate behaviours, the combined system is a much more cost effective mechanism to mitigate bad corporate behaviour.

55. Such a regulatory approach has an added benefit of often being linked to a public redress scheme, which can mitigate the public anger directed at bad corporate behaviours.

56. However, the Committee does not consider that the approach in financial services can or should be adopted wholesale in other industries. The risk of economic crime (as defined in the Call for Evidence) is much higher in financial services than in many other sectors. Any extension of ideas from financial services to other areas should be risk-based and proportionate.

Question 9: Are there examples of corporate criminal conduct where a purely regulatory response would not be appropriate?

57. In responding to this question we have proceeded on the assumption that the question is/should be limited to economic crime as defined in the Call for Evidence, rather than matters such as health and safety.

58. The Committee does not consider the use of regulatory reform and criminal prosecution mutually exclusive as is seen in financial services where regulatory investigations are often followed by criminal investigations.

59. It could properly be argued that where "the controlling mind" test is met, a regulatory response may not be the appropriate response, although we consider that the instances of such conduct in a large organisation are few and far between. Similarly where the company is a sham/fraud from the outset and its only purpose was to facilitate economic crime, a regulatory approach may not be appropriate.

60. A further example might be where the economic crime results in a benefit to the company and an identifiable harm/detriment to public funds has resulted. For example, a fraud which results in the NHS contracting with a private entity paying more than they should. Under a regulatory approach, or at least the regulatory scheme currently in place, there is no provision for such companies to be barred automatically from public procurement exercises. That is currently reserved for companies that have been convicted of certain offences.

61. In the absence of empirical data or a solid evidential basis justifying the expense and time to legislate as per the Call for Evidence why not consider a Modern Slavery Act model? This model sets out substantive offences which subject to the identification principle being satisfied could mean that corporates are prosecuted. Modern Slavery poses a similar threat to economic stability, fairness and efficiencies. However, unlike the Bribery Act, the Government in 2015 favoured not the direct liability (subject to adequate procedures defence) but an industry-led, customer choice focused approach. One that sees a duty imposed on companies that meet certain criteria to publicly report on the steps they are taking to eradicate modern slavery. This provides a transparent way for the public (those who are often cited as the motivation for further corporate criminal liability) to understand steps being taken by companies and allows the public to make informed choices about the companies they deal with. The idea being that there will be a race to the top from within the industry. This system also recognises the resource and expense burden that faces companies in undertaking risk identification exercises, policy and procedure reviews and training and monitoring. The Government took a proportionate response and set de minimis criteria, which could be considered and applied to economic crime.

62. This model might allow the Government to use less onerous, less deterrent based legislation to see how industry itself deals with the problem and then analyse and monitor the results to determine at a later stage whether further legislation is necessary. It is also a model which gets to the heart of the stated reasoning for the Call for Evidence – a change to corporate cultures and behaviours.

Question 10: Should you consider reform of the law necessary, do you believe that there is a case for introducing a corporate failure to prevent economic crime offence based on the Section 7 of the Bribery Act model?

63. The offence created by Section 7 of the Bribery Act of failure of a commercial organisation to prevent bribery addresses a specific harm resulting from companies using intermediaries who pay bribes to win overseas business. The offence was introduced, in part, to meet criticism of the UK's compliance with its obligations under the OECD Convention on Combating Bribery of Foreign Officials in International Business Transactions (the **OECD Convention**) to establish liability of legal persons

for the bribery of foreign public officials. The OECD Convention was intended to tackle the specific difficulties of preventing overseas bribery of foreign public officials in jurisdictions where corrupt public officials enjoy impunity. The Section 7 offence was introduced at a time when international standards for corporate procedures to prevent bribery had been developed by the OECD and ICC and prosecutorial expectations of adequate procedures were evident through deferred prosecution agreements entered into by the US Department of Justice and that agency's guidance opinions as well as US sentencing guidelines. Further, the Bribery Act did not come into force until the Ministry of Justice had, as required by Section 9 of the Bribery Act, published its guidance about procedures which relevant commercial organisations can put in place to prevent persons associated with them from bribing.

64. The Committee does not consider that the Section 7 model fits all types of economic crime, for the reasons set out above. In particular:

64.1 By way of illustration, within business organisations, active bribery is mainly confined to sales and marketing and the types of conduct that may constitute acts of bribery are limited and generally recognisable. By contrast, fraud may take many different forms and within a commercial organisation it is likely that a much larger percentage of its employees could act fraudulently in the conduct of the organisation's business than the proportion that may engage in bribery.

64.2 Regulation 45 of the Money Laundering Regulations 2007 already provides for corporate criminality for specific compliance failings within organisations subject to the Regulations without requiring the prosecution to satisfy the directing mind and will test. The EU proposed Directive on Countering Money Laundering by Criminal Law also includes proposed provisions imposing criminal liability on legal persons based on a lack of supervision or control by individual persons having a leading position within a corporation.

65. The Committee consider that careful consideration should be given to the existing bases for imposing criminal liability on corporations for the various types of economic crime and whether the objectives of deterrence and sanction coupled with legal certainty are best achieved by the Section 7 model or the extension or amendment of existing specific legislation (e.g. the extension of the types of commercial organisation that fall within the scope of the Money Laundering Regulations 2007 or by the adoption of the corporate liability approach proposed by Article 7 of the proposed EU directive).

Question 11: If your answer to question 10 is in the affirmative, would the list of offences listed on page 22, coupled with a facility to add to the list by secondary legislation, be appropriate for an initial scope of the new offence? Are there any other offences that you think should be included within the scope of any new offence?

66. For the reasons explained above, the Committee does not consider the broad Section 7 Bribery Act model to be appropriate for each of the offences listed on page 22 of the Call for Evidence. Further, in relation to the proposal that there be a facility to add to the list of offences subject to the revised corporate criminal liability

framework by a secondary legislation, the Committee notes that this conflicts with the recommendations of the Law Commission:[8]

"*Criminal offences should be created and (other than in relation to minor details) amended only through primary legislation.*"

Question 12: Do you consider that the adoption of the failure to prevent model for economic crimes would require businesses to put in place additional measures to adjust for the existence of a new criminal offence?

67. The Committee consider that each of Options 2-4 would require businesses to put in place additional compliance measures to mitigate against the risk of employees or service providers engaging in criminal conduct in connection with the activities they undertake for the company's business. However, without legally binding guidance or the development of case law clarifying the requisite compliance standards to which companies will be held to account, there is a significant risk that the compliance burden will hinder the conduct of business.

68. To take the possible offence of failure to prevent money laundering as an example, this would require all businesses to consider whether they need to adopt procedures for customer due diligence, transaction monitoring and training equivalent of those adopted by the regulated sector. The risk of infringement of the Money Laundering Regulations has already resulted the exclusion of entire categories of customer as banks de-risk and a call by the Home Office for the reform of the existing law on the basis that the compliance response has been to adopt a tick box approach rather than compliance programs that focus on the customers and transactions that present the highest risk of infringing the law.

Question 13: Do you consider that the adoption of these measures would result in improved corporate conduct?

69. The Committee would expect that the adoption of these measures would result in some improvement in corporate conduct. However, this would bring with it the risk of a significant compliance burden, additional red-tape hindering the transacting of legitimate business and a degree of de-risking. Experience suggests that outside the limited areas of anti-trust and anti-corruption, the US model of corporate criminal liability has not resulted in standards of corporate conduct that are materially higher than those in the UK. The Committee's experience is that individual accountability for misconduct (through criminal law and regulatory sanction as well as the risk of civil liability through class actions) is likely to be more effective at improving standards of conduct in large commercial organisations than lowering the threshold for corporate convictions. The introduction of the SMR and SIMR in the financial services sector illustrates the effectiveness of increasing individual accountability on standards of corporate conduct.

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8 Proposal 8, paragraphs 1.48, 1.49, 3.144-158 and 8.8 of the Law Commission's Consultation Paper No 195 "Criminal Liability in Regulatory Contexts" (2010).

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Question 14: Do you consider that it would be appropriate for any new form of corporate liability to have extraterritorial reach? Do you have views on the practical implications of such an approach for businesses?

70. The extraterritorial reach of the Bribery Act reflects the OECD Convention approach of committing developed countries to criminalise overseas bribery of public officials in less developed countries because of their impunity in their home jurisdiction. The same rationale does not apply to other types of financial crime.

71. However, the existing money laundering offences under the Proceeds of Crime Act 2002 already have an extraterritorial element, as they require the reporting of money laundering outside the UK (save in some cases of low-level conduct that would not be an offence in the foreign country).

72. Considerable care would therefore be needed to ensure that any extraterritorial application takes into account (a) any differing burdens on UK and foreign controlled groups; (b) the risk of a multiplicity of investigations (for example a UK company operating in Switzerland which had engaged in money laundering would be exposed to both criminal investigation by the authorities there in respect of the Swiss corporate offence under Article 102 of the Swiss Penal Code and a criminal investigation in the UK. The company would face differing tests for corporate criminality in each jurisdiction as well as differing evidential burdens and potentially, multiple financial sanctions); and (c) the perceived interests of the UK in conducting investigations into conduct outside the UK.

Question 15: Is a new form of corporate liability justified alongside the financial services regulatory regime? If so, how could the risk of friction between the operation of the two regimes be mitigated?

73. Subjecting corporations operating in the financial services sector to parallel criminal and regulatory regimes is likely to give rise to significant issues. For example, will there be parallel investigations by the FCA and SFO, will regulatory sanctions prejudice criminal proceedings, is it appropriate to take regulatory action having regard to the scope of the criminal proceedings and how should financial penalties be calculated when there are regulatory and criminal outcomes? The risk of friction between the operation of the two regimes could be mitigated by providing that the FCA consider its criminal investigation and prosecution powers where misconduct occurs which may have criminal and regulatory consequences (rather than an FCA investigation into potential regulatory offences and an SFO investigation into potential criminal offences). The Committee considers that the potential friction between the operation of the two regimes should be mitigated by a requirement that companies do not face both a regulatory and criminal financial penalty for the same compliance failings connected with specific criminal conduct. Any Memoranda of Understanding entered into between prosecutors and regulators should also be public documents.

Question 16: What do you think is the correct relationship between existing compliance requirements in the financial services sector and the assessment of prevention procedures for the purposes of a defence to a criminal charge?

74. The Committee considers that where there are specific regulatory compliance requirements that have been met by a company, that company should not be at risk of criminal conviction for failure to prevent economic crime or, in the case of strict

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liability, deprived of an adequate procedures defence. It would be unfortunate if a judge, jury or prosecutor such as the SFO which claims to have no interest in being a regulator, were to set compliance standards that differed from detailed regulations published by experienced financial services supervisors after industry consultation. However, there must also be clear guidance from the government to those companies outside the financial sector as to whether the compliance requirements applicable to the financial sector are expected to be met by companies outside the financial services sector in order to avoid risk of criminal liability.

Yours sincerely

Eoin O'Shea
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