Briefing note

January 2017

UK government explores reform of corporate criminal liability

The UK government has issued a call for evidence examining whether or not the law on corporate criminal liability needs reform. Although it sets out potential options rather than concrete proposals at this stage (including one option of regulatory reform on a sector by sector basis, as an alternative to extending the criminal law), it is nonetheless an important acknowledgment of sustained political pressure as well as pressure from prosecuting authorities. It may lay the foundations for important changes to the way in which investigations and prosecutions concerning corporate wrongdoing may be conducted. The paper invites responses by 24 March 2017.

What are the problems with the current law?

The UK government is acutely aware of the difficulties inherent in prosecuting corporate entities under the law as it currently stands. Its paper cites a number of high profile instances where the "identification doctrine", the tenet of English law that requires prosecutors seeking to pursue a corporate entity to show that the individual(s) involved in particular misconduct represent the "directing mind and will" of that entity, has presented an insurmountable obstacle to prosecution.

The identification doctrine has been heavily criticised in the UK and abroad, including by the OECD, as an impediment to meaningful action against offending corporate entities. The UK government is conscious in particular of unfavourable comparisons with other jurisdictions, particularly the US, where prosecuting authorities are much better able to prosecute corporate entities (and indeed have done so on multiple occasions where their UK counterparts have not been able to do so). Such criticism led to the introduction of the offence of failure to prevent bribery under section 7 of the Bribery Act 2010 ("the section 7 offence") and, more recently, the inclusion of the analogous offence of failure to prevent the facilitation of tax evasion in the Criminal Finances Bill, which is currently progressing through Parliament.

The paper acknowledges arguments long advanced by senior representatives of the Serious Fraud Office ("SFO") that the continued existence of and requirement to use the identification doctrine in respect of cases not concerning bribery (and, soon, also tax evasion) may encourage undesirable corporate cultures and practices and result in unprincipled and uneven enforcement outcomes. It suggests that there is a perverse incentive for corporate entities to compose deliberately bland meeting minutes and/or to construct "contrived corporate structures" to avoid attributing responsibility to those senior in the organisation. Notably though, it offers no examples of such practices being employed as the result of the identification doctrine and does not indicate either how widespread it considers them to be.

What could happen?

This is not the first time that changes to the law of corporate criminal liability have been suggested, but it is the most detailed discussion to date of the shape such changes could take. Indications that the law could be changed to make corporate entities criminally liable for a wider range of wrongdoing by individuals within them were placed on hold in 2014, but were reinvigorated by an announcement by the then Prime Minister David Cameron at the Anti-Corruption

Summit held in May 2016 that the government would consult on the extension of the section 7 offence to other economic crime.

The government has outlined five potential options:

1. Amendment of the identification doctrine (for example, by broadening the scope of those regarded as a directing mind of a corporate entity) - it has indicated that it does not regard this as an attractive option as it would encourage companies to adopt undesirable corporate practices and cultures to continue;
2. A "strict (vicarious) liability offence" – a new statutory form of vicarious liability enabling corporate entities to be guilty of substantive offences through the actions of employees, representatives or agents without the need to prove any fault element;
3. A "strict (direct) liability offence" – a new wide ranging offence akin to breach of statutory duty aimed (effectively a widening of the current section 7 offence) at encouraging corporate entities to take responsibility for avoiding the commission of offences in their name or on their behalf and to exercise appropriate supervision;
4. Incorporation of "failure to prevent" wording into particular substantive offences – akin to option 3 above but the burden is on the prosecution to establish that the corporate has not taken adequate steps to prevent the unlawful conduct occurring, rather than it being for the corporate to establish that it did take such steps.
5. Possible sector by sector regulatory reform – implementation in other sectors of similar arrangements to new individual accountability regimes introduced in the financial services sector.

In terms of underlying offences, the government has suggested that the common law offence of conspiracy to defraud, statutory fraud offences (under section 1 of the Fraud Act 2006), false accounting (under section 17 of the Theft Act 1968) and money laundering offences (under sections 327 to 333 of the Proceeds of Crime Act 2002) could be covered. It has not at this stage suggested that criminal market abuse offences should be within scope.

The government has been careful to make clear that it has not decided which option(s), if any, to pursue, stating that at this stage it is simply "concerned to establish the extent to which the identification doctrine may be hindering effective criminal enforcement" and that it is keen to better understand perceptions of the impact of adding any new corporate offences to existing regulatory arrangements. It has said, "In assessing the suitability of any reform proposals, should the case for change be made out, the Government will need to consider any additional costs against the anticipated benefits of more efficient application of the criminal law and improved corporate good governance."

It seems likely to favour the third option above. This species of "control liability", strongly advocated by the Director of the SFO, is closest to the existing section 7 offence, which the government credits with having "provided a significant incentive for companies to make proportionate bribery prevention part of corporate good governance and encouraged the private sector to play its part in the fight against corruption".

The call for evidence acknowledges that the second, third and fourth options, if pursued, would need to incorporate a due diligence defence such as that provided by the section 7 offence, namely the "adequate procedures" defence, aimed at preventing bribery. Appropriately detailed guidance describing the standards expected of corporate entities would also be required. Such guidance would need to cater for a significantly wider range of offences and potential factual scenarios than are provided for in either the guidance relating to the section 7 offence or the offence of failure to prevent the facilitation of tax evasion contained in the Criminal Finances Bill. The process of drafting it would be likely to be much more complex and would require input from a wide range of corporate entities and their representatives.

Financial services firms in particular are likely to point to existing onerous regulatory requirements and to the potential for disproportionately damaging consequences to result from the criminalisation of conduct already caught by these regimes. For example, convictions typically carry serious negative consequences under public procurement legislation in many jurisdictions.

Would changes mean more deferred prosecution agreements?

The paper was released shortly before the third deferred prosecution agreement ("DPA") to be concluded in the UK (between the SFO and Rolls-Royce) received judicial approval (full details of which are set out in a separate **Clifford Chance briefing**). It refers though to the two previous DPAs as examples of the "utility" of section 7, which it describes as having provided "a powerful incentive for the inclusion of bribery prevention procedures as a component of corporate good governance". The same messages have since been reiterated in the proceedings leading to the approval of the most recent DPA.

Contrasting the often tortuous path of using the identification doctrine and prosecuting the section 7 offence, the paper suggests that "clarity on corporate liability [provided by the section 7 offence in cases to date has] facilitated early and decisive conclusions". It suggests that the extension of the failure to prevent model would mean that the likelihood that cases involving alleged wrongdoing by corporate entities could realistically be prosecuted and that convictions could follow would be much higher. It predicts that this would reinforce the use of DPAs in appropriate cases and lead to increased numbers of negotiated outcomes as corporate entities would be incentivised to cooperate in order to avoid the negative consequences associated with prosecution and possible conviction.

What would be the impact on individuals?

The government sets out its clear view that "crimes are committed by individuals, who should be held to account in law for their actions" and that "corporate liability is not an alternative to individual accountability but an addition". This may have important implications for individuals alleged to have been involved in wrongdoing, as corporate entities may find it more difficult to resist suggestions from prosecutors that providing active assistance in connection with investigations and/or proceedings pursued in respect of those individuals is an essential ingredient of cooperation justifying a DPA.

Remaining questions

The paper is designed as a catalyst to discussion rather than as an indication of whether or which changes will follow. Some significant questions remain. For example, although it acknowledges the extraterritorial reach of the Bribery Act 2010, it does not indicate whether it would be proposed that any extended failure to prevent offence would similarly apply across borders. Other questions left to be decided include whether, for example, individuals attempting or conspiring with others to commit any of the underlying offences or assisting, encouraging, aiding or abetting the commission of those offences would engage any new failure to prevent offence.

The government has recognised that, particularly for corporate entities in the financial services sector, the same conduct by individuals within them may potentially be covered by any new widened criminal regime and existing regulatory provisions, particularly the newly implemented Senior Managers and Certification Regimes. It acknowledges the need to ensure that any changes to the criminal law reinforce rather than undermine these provisions. It asks whether a new form of corporate liability is justified alongside the financial services regulatory regime and if so, how the "risk of friction between the operation of the two regimes" could be mitigated?

The list of questions posed suggests that, despite a sense of inevitability that the law of corporate criminal liability will be extended, the government is keeping an open mind as to which option, if any option, or which combination of options, it may choose. Among the questions it poses is what the costs or benefits of introducing any of the options, including possible impacts on competitiveness and growth, might be. In a post-Brexit era, this question may feature more prominently than it otherwise might.

Contacts

Roger Best
Partner

T: +44 20 7006 1640
E: roger.best
@cliffordchance.com

Michael Lyons
Partner

T: +44 20 7006 4317
E: michael.lyons
@cliffordchance.com

Judith Seddon
Partner

T: +44 20 7006 4820
E: judith.seddon
@cliffordchance.com

Luke Tolaini
Partner

T: +44 20 7006 4666
E: luke.tolaini
@cliffordchance.com

Zoe Osborne
Director - Investigations

T: +44 20 7006 8293
E: zoe.osborne
@cliffordchance.com

Chris Stott
Senior Associate PSL

T: +44 20 7006 4231
E: chris.stott
@cliffordchance.com