



Law Society
of Scotland

Consultation Response

Corporate Liability for Economic Crime

24 March 2017



Introduction

The Law Society of Scotland is the professional body for over 11,000 Scottish solicitors. With our overarching objective of leading legal excellence, we strive to excel and to be a world-class professional body, understanding and serving the needs of our members and the public. We set and uphold standards to ensure the provision of excellent legal services and ensure the public can have confidence in Scotland's solicitor profession.

We have a statutory duty to work in the public interest, a duty which we are strongly committed to achieving through our work to promote a strong, varied and effective solicitor profession working in the interests of the public and protecting and promoting the rule of law. We seek to influence the creation of a fairer and more just society through our active engagement with the Scottish and United Kingdom Governments, Parliaments, wider stakeholders and our membership.

The Society's Criminal Law Committee welcomes the opportunity to consider and respond to the UK Governments consultation: Corporate Liability for Economic Crime. The Committee does not propose to answer every question posed but has the following comments to put forward for consideration.

The Background

Other than in the case of strict liability health and safety offences, prosecutions of companies in Scotland are very rare. In the case of financial crime, they are almost non-existent. Financial crime investigations tend to take a long time and require huge resource. If crime is detected, it is usually easier for the responsible individuals to be prosecuted. To indict a company, the Crown has to be able to show that the 'directing mind and will' of the organisation had the necessary mens rea, something which can be near impossible in large, complex corporate structures.

The Bribery Act 2010 codified the existing common law crime of bribery, and significantly extended its scope, allowing UK prosecutions for crimes committed abroad. Importantly, section 7 of the Act introduced the corporate offence of failing to prevent bribery: where an individual associated with a company engages in bribery for the company's benefit, the company is guilty unless it can show it had in place adequate procedures to prevent such conduct.

The 2010 Act brought with it systems designed to encourage self-reporting of criminality by companies: Deferred Prosecution Agreements [DPAs] in England & Wales, and Civil Settlements in Scotland. In both cases, the idea is that the company, upon discovering evidence of bribery, is incentivised to 'come clean' to the authorities; rather than facing prosecution, with the financial, procedural and reputational impacts, a settlement is negotiated with the authorities. DPAs follow a more formal process.

The legislation has led to only a handful of prosecutions. However, it has led to something of a cultural shift, with many companies investing much more in compliance than might otherwise have been the case. Some self-reports have been made to the authorities, with a few reported DPAs and civil settlements. It

might be argued that the legislation has achieved its aim – to change corporate culture. Investigations and prosecutions under the Act were always going to be difficult, particularly with the added element of non-UK conduct; much better to have companies coming to the authorities with the outcome of their own investigations, and an offer to make reparation.

The Bribery Act model was immediately seen as having potential for application in other areas. Following a consultation by HMRC, the Criminal Finances Bill (currently before the UK Parliament) proposes to introduce new section 7-style corporate offences of failing to prevent facilitation of tax evasion. It is likely that the new legislation, if enacted, will come with a similar encouragement to companies to self-report.

Underlying the present call for evidence is a proposal to take the Bribery Act model one stage further – to extend the concept of ‘failure to prevent’ corporate criminality to all forms of economic crime.

The Justification for Action

There is no doubt that corporate economic crime, where it occurs, ought to be addressed effectively. The call for evidence suggests that this may not be happening, and points the finger of blame at the ‘identification doctrine’, the principle by which the courts determine whether the company has the necessary mens rea to commit the crime in question. It claims that the doctrine ‘is regarded by prosecutors, practitioners and legal academics as not being fit for purpose when applied to large modern companies. The Government is concerned to explore fully whether the operation of the doctrine is hindering the effective administration of justice’.

In examining this issue more closely, the call for evidence refers almost exclusively to English law. There is no doubt, however, that the identification doctrine applies in Scotland; authority for that is found in the case of *Transco v. HMA* 2004 JC 29. The background to *Transco* was a gas explosion which destroyed a house, killing all four occupants. *Transco*, the gas supplier, was served with an indictment in which it was charged, in the first alternative, with culpable homicide, and in the second alternative, with a health and safety charge. *Transco* challenged the relevancy of the indictment. The plea was rejected at first instance, but on appeal the court agreed that the culpable homicide alternative was irrelevant.

What made *Transco* unusual is that it was a rare instance of a company being prosecuted in isolation; the Crown accepted that it did not have evidence to support a prosecution of any individual for culpable homicide. Its case against *Transco* depended upon the court accepting that mens rea could be ‘aggregated’: that the knowledge of various facts by different individuals at different times could be looked at cumulatively, and taken to meet the necessary threshold. On appeal, the court rejected this argument – there was no corporate mind or memory through which it could be held to retain knowledge or awareness.

Of course, had the Crown been able to point to a particular individual having the necessary mens rea for culpable homicide, that individual could have been prosecuted. Had that individual been someone ‘having and exercising the company’s directing mind’, whether as a director or delegate, a charge of culpable homicide could have been relevantly directed against the company. In any event, the second alternative

charge, under the Health & Safety at Work Act 1974, was unaffected by the relevancy plea.

Transco, accordingly, tells us nothing about the Government's apparent concern: that the identification doctrine acts as an impediment to corporate prosecutions. No actual examples are given. One might have thought that the prosecution authorities would be able to point to specific instances where legitimate prosecutions were frustrated by a difficulty in establishing where the directing mind of a company lay. Indeed, the call for evidence notes that work on examining the case for a new offence of corporate failure to prevent economic crime 'was stopped in the summer of 2015 because at that time the Bribery Act failure to prevent model had yet to be tested in an enforcement action and there was little evidence of corporate wrongdoing going unpunished'. The document goes on to refer to various developments under the Bribery Act, dealing with the first reason for cessation, but nothing more is said about the second; at no stage does the call for evidence provide any 'evidence of corporate wrongdoing going unpunished'. It is difficult to reconcile this with the premise at the heart of the consultation – that 'the Government is concerned to explore fully whether the operation of the [identification] doctrine is hindering the effective administration of justice'.

The call for evidence does go on to refer to the Libor-fixing investigation, suggesting that it supports the concern that an inability to hold companies to account has undermined public confidence in the UK's criminal justice system. It notes that UBS could not be prosecuted in the UK, but entered into a non-prosecution agreement with the US authorities, which resulted in it paying \$500m in fines. Others will be better placed to comment on whether the facts of the UBS case support the Government's conclusions, but it should be noted that a comparable fine (£160m) was imposed by UK regulators.

There is no doubt that corporate prosecutions are infrequent, particularly in Scotland. Whether that is because of difficulties around the identification doctrine is moot. Importantly, the call for evidence does not deal with the matter of resources. Economic crime is generally complex. Investigations are difficult and often lengthy. Although Police Scotland now has units dedicated to the investigation of financial crime, such cases rarely attract the level of resources provided to, for example, high profile murders. As a result, it can take years for prosecution reports to be submitted to the Crown and longer still before a decision is taken to commence criminal proceedings. Once a case has been made against an individual, there may be little relish to then pursue the company.

Resources may, of course, provide the most compelling argument for change. There is no slack in the public purse, and the criminal justice system continues to face considerable pressure. The call for evidence recognises that the Bribery Act has 'provided a significant incentive for companies to make proportionate bribery prevention part of corporate good governance...' In other words, the legislation has led to a focus on prevention and self-regulation, rather than prosecution. Such a shift reduces the pressure on those charged with the responsibility to investigate and prosecute economic crime.

Options for Reform; Specific Questions

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

We are not aware of any evidence to suggest that it does not. If there is insufficient deterrence, that is not necessarily a product of the substantive law, but may relate to other reasons for the lack of corporate prosecutions.

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

We are not aware of any clear evidence for this.

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

No. Others – particularly prosecution authorities – will be better placed to comment.

Question 4: Do you consider that any deficiencies in the identification doctrine can be remedied effectively by legislative or non-legislative means other than the creation of a new offence (Option 1)?

It is difficult to know what the identification doctrine might be replaced with. An aggregation model, such as contended for by the Crown in Transco, would require very careful thought. There may be convention rights implications.

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?

It is unclear that there are deficiencies in the identification doctrine. In the event that Government decides to legislate, then Options 3 or 4 would appear most appropriate.

Various issues would require to be addressed, however. What economic crime would be included (see response to question 11 below)? How would 'association' be defined? The Bribery Act regards an associated person as 'a person who performs services for or on behalf of' the company, whether as an employee, agent or contractor; would that be the model used here? Would it be necessary for the Crown to show that the underlying economic crime was designed to benefit the company? If so, how would 'benefit' be defined? If benefit were not a precondition, then companies could find themselves being prosecuted in almost limitless circumstances. Would there be a materiality test?

Any such reform must be accompanied by a sensible due diligence type defence. This would be a

necessary failsafe. Without such a defence, there would be a real risk of manifestly unjust prosecutions. It is not enough to rely on the good judgement of the prosecution authorities.

The terms of the due diligence defence must be clear. As the Bribery Act has led to few prosecutions, there has been no judicial scrutiny of the meaning of 'adequate procedures' to prevent bribery. The Criminal Finances Bill proposes a different wording for the due diligence defence: 'such prevention procedures as it was reasonable in all the circumstances to expect' the company to have in place. What is the difference between 'adequate' and 'reasonable'? What formulation will be chosen for the new economic crime offence? If the legislation is used as sparingly as the Bribery Act, how will companies know what they are required to do?

As the onus of proving criminality rests with the prosecutor, it should be for the Crown to prove that the appropriate action had not been undertaken by the company; on balance, therefore, Option 4 is preferable.

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

Much will depend upon the exact construction of the legislation, including the definitions of association, benefit and materiality, and the defence available. The territorial reach of the legislation will also be relevant. Companies, and in particular large organisations with business outwith the UK, will undoubtedly have to review their operations. Is it safe, for example, for companies to invest in parts of the world which have less robust traditions of compliance and good conduct? Are there greater risks in subcontracting as opposed to the use of employed staff?

The Bribery Act and the Criminal Finances Bill were each designed to attack a specific mischief. The call for evidence proposes a change that is much more far-reaching.

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

It is difficult to see how, unless a strict liability approach led to the authorities focusing their attention on companies rather than the individuals directly responsible.

If the point was reached where each instance of economic crime led to proceedings against both individual and company, one could envisage a situation where the company would seek to accept liability (which could only ever lead to a financial penalty) in return for the discontinuation of proceedings against the individual (who may face imprisonment). Such trade-offs, in different circumstances, are a common part of the criminal justice system; they often reflect the complexity of prosecutions and the limited nature of resources. It would be important to guard against any unintended diminution of individual accountability.

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?

Others may be better placed to comment on the options for regulatory reform.

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

It has long been recognised that companies, and indeed partnerships, can be held criminally responsible. Where there is clear evidence of corporate criminality, and subject to the usual public interest considerations, there is no reason why criminal proceedings should not be brought.

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?

Please refer to the answer to question 5 above.

The call for evidence observes that the section 7 model 'might enhance the effectiveness of DPAs as an alternative to criminal prosecution'. It should be noted that DPAs (deferred prosecution agreements) do not exist in Scotland. Instead, the Crown operates a self-reporting initiative which is designed to lead to civil settlements (that are then collected via the Civil Recovery Unit of Crown Office). The self-reporting initiative is not a permanent arrangement; rather, it is reviewed on a year-by-year basis.

Question 11: If your answer to question 10 is in the affirmative, would the list of offences listed above, 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?

The call for evidence says that 'the Government's starting position is that the offence should initially apply to a short list of the most common serious economic crime offences, which could be added to if necessary by secondary legislation'. The list that follows is written from an English law standpoint.

The Fraud Act 2006 and Theft Act 1968 do not apply to Scotland. In Scotland, fraud, theft and embezzlement are common law crimes. Such crimes can cover a multitude of circumstances, from the trivial to the gravely serious. If the Government's intention is to apply the proposed provision to a short list of the most serious crimes, how then are these to be defined? It cannot be enough to simply provide for theft or fraud, as that may mean there is a wider application in Scotland than in England & Wales. It may be that some threshold would be required.

For the avoidance of doubt, the money laundering offences at ss.327-33 of the Proceeds of Crime Act 2002 do apply in Scotland.

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?

Please refer to the answer to question 6 above.

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

One might expect that the greater risk of corporate prosecution would encourage companies to invest more in prevention and compliance, as appears to have been the case with the Bribery Act.

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?

Please refer to the answer to question 6 above. Matters become complicated when extra-territorial conduct is included. Different jurisdictions have different legal systems and often very different cultures. What is acceptable there may not be acceptable here, and vice versa. What would happen, for example, if a charity working in a country run by a regressive regime made an application for funding which did not disclose its involvement with a particular oppressed group? If that were categorised as fraud, could it lead to the charity being prosecuted in the UK? How would such situations be dealt with?

Another issue is the relationship between investigators and prosecutors within the UK. How would it be determined where a prosecution should take place? Would it follow the location of the company's registered office, or the place of significant connection to the crime, or the place where the matter first came to the authorities' attention? Given the different legal systems in Scotland and England, and the different approaches to self-reporting, it is essential that there is as much clarity as possible.

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?

There should be clarity and consistency. Companies should not face the prospect of having to choose between regulatory compliance and compliance with the criminal law.

The relationship between regulators and prosecutors should be clearly defined. As a matter of principle (specifically *ne bis in idem*), multiplicity of proceedings should be avoided.

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?

As mentioned above, the definition of adequate procedures in s.7 of the Bribery Act 2010 has not been judicially tested, largely because of the lack of prosecutions. It is important that companies know what is expected of them.

There should clearly be consistency between the expectations of regulators and those of prosecutors and the courts. It would be absurd for regulators to adjudge preventative measures to be adequate only for the courts to disagree.

For further information, please contact:

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