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United Kingdom: new powers for the UK white-collar fantastic four

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2014 was an active year for white-collar investigations and high-profile prosecutions – from the phone-hacking scandal to billion dollar fines against sanctions busters, multi-jurisdictional investigations into Libor and FX, huge money laundering and tax evasion actions, and the continued focus on corruption.

What does 2015 have in store? If the public statements by politicians, HMRC, the Serious Fraud Office (SFO) and the Financial Conduct Authority (FCA) are anything to go by, the answer is more prosecutions, bigger fines and longer prison sentences.

With almost all of the UK's key prosecution agencies getting new toys to play with in 2014, significant developments are anticipated. Below we highlight likely areas of focus over the coming months.

The SFO

The SFO faced some embarrassment in 2014 and 2015. It settled civil actions with the Tchenguiz brothers and Celtic Energy for over £10 million and a report from the Crown Prosecution Service (CPS) said that even though steps had been taken to address concerns raised in its 2012 report, much 'still needs to be done.'[1] The SFO has responded robustly, obtaining 'blockbuster' funding and taking on 80 active cases including Libor, FX and the Bank of England liquidity auctions. However, its public statements on privilege and the availability of DPAs are provoking debate.

Internal investigations

The SFO is seeking to challenge claims of legal professional privilege in the context of corporate investigations. It has publicly accused companies of 'hiding behind' privileged communications with their lawyers to 'obstruct' investigations.[2] These are strong words indeed. In the context of a production notice under section 2 of the Criminal Justice Act 1987, 'obstruction' is a criminal offence punishable by up to seven years' imprisonment.

When undertaking an internal investigation, a company will be mindful of legal professional privilege. The rules of the relevant jurisdiction where any challenge is likely should be followed. In the context of a UK investigation, whether litigation privilege is available to protect communications with third parties (such as accountants or witnesses) could have a dramatic impact on the disclosure of documents in subsequent SFO action.

English case law has called into question the availability of litigation privilege for documents created during a regulatory investigation. Further consideration was given in the case of *Rawlinson and Hunter Trustees SA v Akers*,[3] where the Court of Appeal upheld a High Court decision that:

> *the mere fact that a document is produced for the purpose of obtaining information or advice in connection with pending or contemplated litigation, or of conducting or aiding in the conduct of such litigation, is not sufficient to found a claim for litigation privilege. It is only if such purpose is one which can be properly characterised as the dominant purpose that such claim for litigation privilege can properly be sustained.*

A key consideration is therefore the reason for the creation of the document. The Court of Appeal confirmed that where documents are created for multiple purposes, those purposes will not necessarily be independent of each other. However, the burden is on the party claiming privilege to demonstrate that the purposes are related and that the dominant purpose was for use in the conduct of litigation. Even though this was not the context of the *Rawlinson and Hunter Trustees SA v Akers* case, it has been considered by UK white-collar crime experts as potential authority for the proposition that employee accounts provided during an internal investigation, with a view to making a self report to the SFO will not be privileged. Whether such a challenge to privilege in such employee accounts is successful will depend on the facts and circumstances of the case. What is certain is that any challenge will muddy the waters further, in what is already a complex area.

The SFO's approach

David Green, Director of the SFO, has stated that the agency will confront, and if necessary litigate, over what it sees as disingenuous claims of privilege.[4]

It is also clear that in the context of a self report in the UK, the SFO now expects that even where privilege attaches to a witness account it expects privilege to be waived.[5] Alun Milford, General Counsel of the SFO, summarised the SFO's stance on privilege in September 2014:

> *We will view as uncooperative, false or exaggerated claims of privilege, and we are prepared to litigate over them […]*
>
> *if a company's assertion of privilege is well-made out, then we will not hold that against the company […]*
>
> *if, notwithstanding the existence of a well-made out claim to privilege, a company gives up the witness accounts we seek, then we will view that as a significant mark of co-operation.*[6]

According to press reports, the SFO intends to come out fighting and will seek to challenge privilege in the context of internal investigations.[7] The results could have a dramatic impact on how cross-border corporate investigations concerning the UK authorities are undertaken in the future.

Deferred prosecution agreements

Related to this is the stance taken by the SFO in respect of the offering of deferred prosecution agreements (DPAs), which became available to the SFO from 24 February 2014.[8] Over one year on, no DPA has been agreed. Is this because the standard of 'cooperation' envisaged by the SFO to qualify for a DPA is simply unrealistically high?

The SFO has made it clear that its 'preferred option' will be to prosecute.[9] It has said that organisations will need to provide 'unequivocal cooperation.'[10] Ironically, this public stance of

'preferred' prosecution may assist companies in their claims of privilege – as litigation can be said to be contemplated up until the signing and approval of a DPA by the courts.

DPAs are voluntary agreements whereby prosecutors will not commence criminal proceedings against organisations pending successful compliance with a range of conditions, for example the payment of penalties, cooperating with investigators and implementing remediation and compliance measures. The DPA Code of Practice (the DPA Code)[11] issued by the SFO and the CPS on 14 February 2014 sets out factors in favour of a DPA that include:

- a genuinely proactive approach by management to deal with offending and a proactive corporate compliance programme;
- self reporting previously unknown offending;
- providing a report of any internal investigation, including witness accounts and source documents;
- making witnesses available for interview; and
- remedial actions such as completely changing the organisation's management and the compensation of victims.

Failures during the self-report will weigh against a DPA, including a failure to:

- make a timely report or properly engage with the prosecutor. Note that DPAs are not available to individuals so if companies have entered into a DPA, their employees can still be prosecuted. When an organisation self-reports wrongdoing, it must ensure that it does not withhold material that would jeopardise an effective investigation, and where appropriate, prosecution, of those individuals as otherwise this would be a strong factor in favour of prosecution;
- verify reported wrongdoing;
- make a full and frank report; and
- conduct the internal investigation within a reasonable period, leading to the destruction or fabrication of evidence.

The DPA Code states that there is no change to the law on legal professional privilege so an accused's right to refuse to disclose information subject to legal professional privilege will continue. However, the SFO has said that 'co-operation and the free supply of relevant information are key to the process of initiating negotiations with a view to entering a DPA'[12] and that while the SFO 'certainly wouldn't hold against a party any decision to properly claim privilege, what better way to demonstrate "co-operation" than by an open and frank view of privilege claims.'[13]

All bark and no bite? The SFO's use of the UK Bribery Act 2010

When the Bribery Act 2010 (the Bribery Act) came into force in July 2011, Kenneth Clarke proudly announced that 'Britain will play its full part in the international clampdown on corruption.'[14] However, four years on, there is little of substance to show. Five individuals have been convicted of committing offences under the Bribery Act, with sentences ranging from six years' imprisonment to two months' imprisonment (suspended for 12 months) and a two-month curfew.

Will 2015 see the first large corporate prosecution or conviction under the Bribery Act? As the Bribery Act does not apply to conduct that has taken place in whole or in part prior to 1 July 2011, this is unlikely. The length of time that it takes for corruption to come to light, to be investigated and prosecuted, means that a full trial through to conviction will not occur in 2015.

However, the SFO has confirmed that there are a number of ongoing investigations into 'top-end' bribery.[15] It is therefore only a matter of time before a large prosecution is undertaken against a corporate under section 7 of the Bribery Act. The limited defence available under section 7 will make such a prosecution extremely difficult to defend, and therefore a guilty plea or DPA is a far more likely outcome. The impact of the new sentencing guidelines will further show that the UK prosecutors and courts are a force to be reckoned with (see below).

US approach

It has become clear that there is a chasm opening up between the approach of the UK and US prosecuting authorities. At first glance, it does not appear that where the US goes, the UK will follow.

US companies were often finding themselves waiving legal privilege to demonstrate cooperation with an investigation during self-reports, so in 2006 the US Department of Justice (DoJ) issued guidance reminding prosecutors that they should seek waivers of privilege only in rare instances and only with approval from senior officials.[16] The DoJ strengthened this guidance in 2008[17] and the Securities and Exchange Commission followed suit in 2010.[18]

In 2014, an expansive view of privilege was taken in the case of *Re Kellogg Brown & Root, Inc.*[19] It was held that privilege applied to employee statements in the context of an internal investigation, even when made to non-lawyers, so long as 'one of the significant purposes' of the investigation was to obtain or provide legal advice.

HMRC

Tax avoidance and evasion is very much on the political and regulatory agenda. HMRC is targeting 1,165 prosecutions for 2014–2015. With an average of around 500 raids on premises per year since 2011, HMRC has demonstrated that it will aggressively pursue individuals and corporates. During this election year, the government[20] is parading its performance on punishing tax evasion and is quoting some staggering figures on its achievements since being in power:

- investing around £1 billion in HMRC's compliance activities;
- securing £100 billion of additional compliance revenues;
- securing £31 billion from large business compliance work;
- bringing in £2 billion of revenues from offshore tax evasion through international agreements and disclosure facilities;
- securing £852 million from the UK's 6,000 richest people;
- making 42 changes to tax laws;
- winning more than 80 per cent of cases in tax tribunals;
- increasing fivefold the number of criminal prosecutions for tax crimes;
- prosecuting more than 2,650 individuals for tax crimes; and
- securing 2,718 years of prison sentences.

The recent HSBC whistleblower case provides an interesting insight into the cross-party political will to pursue criminal sanctions for tax evasion. At the Treasury Committee meeting on 25 February 2015,[21] HMRC was pressed about why more individuals holding Swiss accounts at HSBC were not criminally prosecuted. Dismay was expressed at the fact that there had been only one successful UK prosecution for tax evasion from a list of more than 6,000. HMRC was criticised for not pursing criminal prosecutions involving wealthy individuals or Big Business with the same vigour as it pursues prosecutions against, for example, tax credit or benefit fraud. The implication is that the rich can buy justice while the poor go to prison.

George Osbourne's 2015 Budget shows that Big Business is now clearly within HMRC's sights.[22] HMRC is being equipped with a

greater armoury to pursue international tax evasion. From 2017, information on the accounts, interest and balances of UK tax residents' offshore accounts will automatically be shared with HMRC. In 2015, the existing disclosure facilities (used by HMRC to encourage voluntary disclosure of relevant information) will be closed and replaced with a new facility that will see tougher penalties and no guarantee that a criminal investigation will not be pursued. Those hoping for leniency should therefore act swiftly.

Further measures announced in this year's Budget include:

- a new strict liability criminal offence for offshore evasion;
- an offence for corporates of failing to prevent tax evasion or the facilitation of tax evasion on their watch;
- an increase in the financial penalties faced by evaders, including linking the penalty to the value of the asset kept in an offshore bank account;
- new civil penalties for those who enable evasion, meaning they will suffer the same penalty as the tax evader; and
- publicly naming tax evaders and those who enable evasion.

There is a loud and clear message that tax evasion by high net worth individuals and companies will continue to be scrutinised and HMRC has been given even greater powers to pursue evaders.

HM Treasury

Historically, UK authorities have been much less aggressive than their US counterparts in sanctions enforcement. For example, in contrast to fines imposed by the US in 2014 a company in the UK was fined over £1 million and its managing director imprisoned for over two years for exports to Iran in breach of sanctions.[23]

2015 is likely to see the continued and seemingly unfettered jurisdictional reach of US regulators to bring sanctions prosecutions against EU companies. During 2014, the New York Department of Financial Services imposed a ban on the clearing of US dollars by BNP Paribas and imposed a fine of US$8.79 billion.[24] In 2015, we have already seen a settlement of US$1.45 billion with Commerzbank.[25] It has since been widely reported that OFAC has reopened its investigation into Standard Chartered Bank, which was fined in 2012 for breaches of Iranian sanctions.

There are hints that the Treasury is enviously looking at the scale of fines imposed by OFAC. In the 2015 Budget, one of the Chancellor's lesser reported initiatives was that:

> *The Government will review the structures within HM Treasury for the implementation of financial sanctions and its work with the law enforcement community to ensure these sanctions are fully enforced, with significant penalties for those who circumvent them. This review will take into account lessons from structures in other countries, including the US Treasury Office of Foreign Assets Control.*[26]

The fact that three EU-based companies are among those mentioned in the most recent sanctions enforcement headlines for action taken by US regulators highlights the importance of having a multi-jurisdictional view of sanctions compliance, especially for any company with a global footprint.

FCA

Since its creation in 2013, the FCA has already made its mark as a force to be reckoned with. In early 2015, it announced plans to target financial crime, including failures in bribery and sanctions controls within regulated entities.[27] It has also made clear that it will hold senior individuals accountable for breaches of regulatory obligations. In January 2015, the FCA found that the former CEO and former compliance officer at Martin Brokers (UK) Limited had failed to take reasonable steps to prevent a culture developing that permitted Libor manipulation. They were fined and banned from performing significant influence functions at financial services firms. The FCA published a statement on its website stating 'this case [...] should serve as a warning to everyone that holds a significant influence function that if a firm's misconduct can be attributed to cultural failings, then we expect senior management to answer for this.'[28]

In its 2015/2016 business plan,[29] which was released on 24 March 2015, the FCA elevated financial crime to one of its seven key risk areas. Firms will be subject to particular scrutiny in the next 12 months and will need to have effective, proportionate and risk-based systems in place to ensure that their business cannot be used for financial crime. The FCA has indicated that:

- it will continue to focus its efforts on individual accountability in its enforcement work and will take action for misconduct and breach of rules;
- it will work closely with firms in its new role as regulator and supervisor of Libor to help them to identify potentially manipulative behaviour, managing conflicts of interest and implementing robust governance and oversight arrangements; and
- it intends to help firms foster a culture that gives their employees the confidence to speak out about wrongdoing, and will embed better arrangements and support for whistleblowers.

The new Senior Managers Regime, Certification Regime and Conduct Rules for FCA-regulated firms is also expected to be in force in the second half of 2015 and will result in increased accountability for individuals at all levels within regulated firms. Senior management and particularly those responsible for compliance oversight will be most affected. A key change will be the reversal of the burden of proof. Under the new regime, the senior manager responsible will be required to provide evidence that he or she personally took 'reasonable steps' to prevent and stop a regulatory breach. Senior managers will need to show that they have been proactive in ensuring that all staff are fully aware of what is and is not acceptable conduct, and also in monitoring conduct. If senior managers are found to be in breach of their obligations, the FCA will be able to impose an unlimited fine or to ban the individual from performing regulated functions.

New powers for all – the Serious Crime Act 2015

The Serious Crime Act 2015 (SCA) received royal assent on 3 March 2015. Its provisions will come into force on 3 May 2015 and on 1 June 2015.[30] The SCA makes a number of changes to the Proceeds of Crime Act 2002 (POCA) and provides for a new offence of assisting an organised crime group.

Restraint orders

Restraint orders are now available pre or post-charge where there are 'reasonable grounds to suspect' that an alleged offender has benefitted from his or her criminal conduct.[31] This is a lesser hurdle than the previous 'reasonable cause to believe' that the benefit has been so obtained. The new restraint powers will be available to the same range of authorities as permitted under POCA including, among others, the police, HMRC, the FCA, the SFO, the Home Office, the National Crime Agency and other 'accredited financial investigators.'[32]

Confiscation orders

It will be easier for the court to confiscate funds held in a bank or building society account following conviction, under a confiscation order.[33] The court is also able to make a ruling at the time of the confiscation order as to the interests of third parties (who can be ordered to make representations) in the defendant's property.[34] This should speed up the enforcement process. When the court makes a confiscation order, it can also order travel bans to prevent the dissipation of assets.[35] Prosecutors and authorities such as the CPS, the SFO and the FCA can make applications to the court for confiscation orders.

New offence

There is a new offence of participating in the activities of an organised crime group.[36] This is defined broadly and covers three or more people who act for the purposes carrying out criminal activities.[37]

The offence is designed to criminalise the activities of those who assist or help organised crime, for example by making payments or funds available. The mental threshold is whether the individual knew or 'reasonably suspected' that they were helping an organised crime group.[38] An individual does not need to know any members of the organised crime group in order to be guilty of an offence[39] and the gain or benefit does not need to be financial in nature.[40]

The offence has a wide geographical reach and extends to activities carried on outside England and Wales where the conduct would be an offence under the law of the relevant country, and would also be an offence in England and Wales.[41]

Authorities such as the CPS, the SFO and the FCA can prosecute those that commit this offence. It is a defence to prove that a person's participation was necessary to prevent or detect crime.[42] A person guilty of this offence can be imprisoned for up to five years.[43]

The old dog with new tricks: the courts' sentencing powers for corporate crime

The final development of 2014 under the spotlight is the Sentencing Council's Definitive Guidelines for Fraud, Bribery and Money Laundering Offences (the Guidelines).[44] The Guidelines apply to all organisations[45] sentenced on or after 1 October 2014, regardless of the date of the offence.[46]

The relevant offences are fraud, money laundering and bribery offences under the Bribery Act 2010. The Guidelines emulate the US 'multiplier' system. The court must first consider making a compensation order to the victim and the impact of confiscation. The multiplier is then calculated on the basis of 'level of culpability' and the 'harm' caused by the offence.

Culpability

The courts will assess the organisation's 'role' and 'motivation' in carrying out the offence. The non-exhaustive list of culpable characteristics, include:

- whether the corporate played a leading role in organised, planned unlawful activity;
- wilful obstruction (eg, destruction of evidence, misleading investigators, suborning employees);
- involving others through pressure or coercion (eg, employees or suppliers);
- the corruption of local or national government officials or ministers, including those performing a law enforcement role;
- offences committed over a sustained period of time; and
- culture of wilful disregard of commission of offences by employees or agents with no effort to put effective compliance systems in place.

Harm

Harm is calculated by reference to the gross amount the corporate obtained or intended to obtain from the crime; or the loss avoided or intended to be avoided from the offence. Harm is calculated as follows:

- fraud offences – the actual or intended gross gain to the offender;
- bribery act offences – the gross profit from the contract obtained, retained or advantage sought as a result of the bribery or the likely cost avoided by failing to put in place adequate procedures to prevent bribery; and
- money laundering offences – the amount laundered or the likely cost avoided by failing to put in place an effective anti-money laundering programme (whichever is higher).

The court will then take into account aggravating and mitigating factors to adjust sentences. Aggravating factors include evidence of calculated and endemic misconduct, attempts to conceal or hide evidence and the offence being committed across various jurisdictions. Mitigating factors include corporate cooperation, an early guilty plea and voluntarily reporting the offending behaviour.

The court must then look at the fine, compensation and confiscation in their entirety, and consider whether the fine calculated meets the objectives of 'punishment, deterrence and the removal of gain' in a fair manner. Any fine must be substantial enough to have a 'real economic impact so that both management and shareholders understand the need to operate within the law.' The Guidelines recognise that a fine may have the consequence of putting an offender out of business.

The UK has faced some criticism for its sentencing of corporate offenders when contrasted with the eye-watering penalties imposed by the US authorities and EU Competition Commission. The Guidelines go some way to addressing this criticism. Although it is early days and unlikely that the UK will emulate the multibillion-dollar penalties in the near future, the impact of the Guidelines will ensure a significant leap forward.

The Guidelines also reinforce the importance of self reporting and proactive compliance. In a time when the benefits of self reporting are at best uncertain, it is hoped that the courts will show clear and practical benefits to those entities that decide to take the time and expense to investigate and report of their own volition, rather than wait for the authorities to find out and then enter an early guilty plea.

The Dechert crystal ball – predictions for 2015 and 2016

Across the board, the UK's key prosecution agencies have been granted significant new powers to prosecute individuals and corporates for financial crime. During the last 12 months, there have been many aggressive public statements regarding enforcement. In these uncertain times, we predict that during 2015:

- the first significant corporate case will be brought under the Bribery Act;
- the UK's first ever DPA will be entered into;
- hard-fought litigation regarding the nature and extent of legal privilege in internal investigations will be undertaken;
- HMRC will be even more aggressive in its pursuit of individuals and corporates for tax evasion and new powers will be sought for a strict liability offence;
- there will be more activity in the prosecution of breaches of sanctions;

- the FCA will hold individuals to account for systems failures regarding financial crime within regulated firms;
- convicted defendants and third parties will have nowhere to hide from confiscation; and
- the English courts will begin handing down much larger corporate sentences.

Time will tell how many of our predictions come true over the next 12 months.

Notes

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