Client Alert | White Collar/Investigations

Follow the money - the Criminal Finances Bill

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The Criminal Finances Bill sets out measures to combat money laundering and tax evasion that will also affect corporate compliance requirements, particularly in the finance and professional services sectors.

The Criminal Finances Bill is intended to give effect to key elements of the government's April 2016 action plan on anti-money laundering and counter-terrorist finance. This alert summarises a number of key proposals from the Bill, which was published on 13 October 2016 and is due to be scrutinised in committee from 15 November 2016. The proposals include new corporate offences regarding tax evasion, changes to the current suspicious activity reports ("**SARs**") regime, and the introduction of unexplained wealth orders ("**UWOs**").[1]

These proposals reflect two major ongoing developments in UK criminal law following the Bribery Act 2010: namely, an increasing focus on foreign politically exposed persons ("**PEPs**"), and the expansion of corporate criminal liability through strict liability 'failure to prevent' offences.

New corporate offences regarding tax evasion

Further to a consultation that ended in July this year, the Bill introduces two new criminal offences for corporates and partnerships regarding tax evasion. These offences follow the strict liability 'failure to prevent' approach to corporate misconduct previously seen in section 7 of the Bribery Act.

An entity will commit an offence where it fails to prevent an associated person – someone acting for or on behalf of the entity – from criminally facilitating either: 1) a UK tax evasion offence; or 2) an equivalent offence under foreign law. Both new offences have extra-territorial effect, although the second offence (regarding foreign tax evasion) requires the entity or the facilitation to be linked to the UK.

For each offence, it will be a defence for the entity to show that it had reasonable procedures in place to prevent such facilitation, or that it was not reasonable to expect it to have such procedures.

In their current form, the offences may be difficult to actually prosecute. Each offence requires another two underlying criminal offences – regarding the tax evasion and the facilitation – to be proved (although not necessarily prosecuted). In addition, it is often difficult to distinguish between criminal tax evasion and aggressive (but legal) tax avoidance. There are potential workarounds for these issues, but the main impact of the new offences is likely to be compliance-related: as with the Bribery Act, businesses will need to ensure their procedures are sufficient to provide a defence.

Further analysis of these offences can be found in previous alerts: Just when you thought it was safe to go back in the water… and Criminal consequences of the use of leaked data by tax authorities.

[1] Other topics covered in the Bill, such as terrorist financing and seizure and forfeiture powers, are not addressed in this alert.

Enhancements to the SARs regime

A regulated entity making a SAR may request consent from the National Crime Agency ("**NCA**") to proceed with the reported activity. If the NCA grants consent, the entity has a statutory defence to the principal money laundering offences that it might otherwise commit by proceeding. If the NCA refuses consent, the entity loses the statutory defence (and so cannot proceed with the activity without risking an offence) for a 31-day 'moratorium period'. This is intended to allow investigators time to gather evidence and decide if further action (e.g. to freeze funds) is required.

In practice, 31 days is often insufficient for a proper investigation, and so the NCA often takes no further action. The Bill allows for extensions of the moratorium period (by application to the Crown Court) in 31-day increments, up to a total of 217 days, where more time is needed to finish an ongoing investigation.

To assist such investigations, the Bill enables the NCA to request further information from a person in the regulated sector after receiving a SAR[2] and, if it is not provided, to apply for an order compelling its provision. More broadly, the Bill extends the use of disclosure orders, allowing law enforcement agencies to compel the provision of information and documents in money laundering investigations.

The Bill also enables regulated entities to share information with each other regarding suspected money laundering, further to a notification to the NCA. This 'public / private partnership' approach, which has been piloted by the NCA and a number of banks in the Joint Money Laundering Intelligence Taskforce (JMLIT), is intended to allow multiple entities to compile detailed intelligence about suspected money laundering before providing this information to the NCA in a single joint disclosure report, or 'super SAR'.

In response to concerns expressed by regulated entities, the Bill also provides a clear legal basis for the sharing of confidential information regarding suspected money laundering. As with ordinary SARs, information shared with the NCA or with other regulated entities further to these provisions will not breach disclosure restrictions (e.g. regarding client confidentiality). Where the NCA requests or requires further information following a SAR, privileged information does not need to be provided.

These measures would undoubtedly help the NCA to investigate SARs regarding serious misconduct, although an extended moratorium period will pose a serious challenge to a company that has to place a transaction on hold for up to 7 months and avoid tipping off the subject of the SAR during that time.

However, the bigger difficulty with the current SAR regime is arguably the sheer volume of information: in 2014-15, more than 380,000 SARs were submitted to an aging IT system designed to cope with only 20,000 SARs. The information sharing provisions in the Bill may assist, if widely used, by allowing multiple SARs to be replaced with a single 'super SAR', but it is likely that the NCA will need more and better resources to take full advantage of improvements to the SAR regime.

Unexplained wealth orders, explained

UWOs are intended to allow law enforcement agencies to investigate and seize property from a person, without needing to prove serious criminality, where there are reasonable grounds to suspect that the person's known lawful income[3] would have been insufficient to obtain that property.

The Bill enables law enforcement agencies to apply to the High Court for a UWO (and, if required, an interim freezing order) regarding property thought to be held by:

- a PEP (i.e. a prominent foreign public official or their family member or close associate); or
- a person who there are reasonable grounds to suspect has been (or is connected with someone who has been) involved in serious crime[4].

For a PEP, there is no need to have reasonable grounds to suspect their involvement in serious crime.

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2 Or, in certain circumstances, where the NCA is assisting an investigation by foreign law enforcement agencies.

3 It is unclear whether this is intended to refer to income as distinct from capital, or to the person's total wealth (which seems to be a more sensible approach). This may be clarified in the final Bill.

4 This includes traditional organised crime offences such as drug trafficking and white collar offences such as money laundering, fraud, tax offences and bribery (per section 2 and Schedule 1 of the Serious Crime Act 2007).

UWOs will be available for general use by law enforcement, but it is likely that they will see particular use in support of SARs that identify valuable property held by such persons.

The UWO requires the respondent to explain the nature and extent of their interest in the specified property and how they obtained it. Non-compliance with a UWO (without reasonable excuse) will leave the respondent open to contempt of court proceedings and give rise to a presumption that the property is recoverable, making it easier for a law enforcement agency[5] to seize under the civil recovery regime. It will also be an offence to knowingly or recklessly make a materially false or misleading statement in response to a UWO.

The law enforcement agency may (and presumably would in most cases) apply for an interim freezing order at the same time as the UWO, in order to prevent dissipation of the property.

UWOs are a potentially powerful tool and will require careful handling, particularly as applied to PEPs. Besides the obvious political sensitivities and potential reputational damage (even if the UWO is not ultimately granted), the reversal of the normal burden of proof allows an application to be made on the basis of limited evidence and places significant pressure on the respondent.

One way to mitigate this, as raised in the recent Commons debate on the Bill, would be to have the initial application for a UWO be heard in private (as is done for restraint proceedings and at the initial stage for deferred prosecution agreements), with publication of the judgment and UWO taking place only if a UWO is granted. It remains to be seen whether this suggestion will be adopted in committee.

Conclusion

Further government action on money laundering, corruption and financial crime is expected. The recent Commons debate on the Bill saw a number of questions about the extension of the 'failure to prevent' approach to other economic crimes, and the government has indicated that a consultation on the topic is forthcoming. The Bill forms only one part of a wider package of measures. However, the measures it proposes will – if properly implemented and resourced – significantly enhance the UK's ability to combat money laundering and recover the proceeds of crime.

The finalised Bill is expected to become law next year, although no implementation date has yet been fixed. The effect of these measures on compliance requirements should be taken into account by those in the regulated sector and, in particular, companies in the financial and professional services sectors, ahead of the Bill coming into force.

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[5] Including HM Revenue & Customs and the Financial Conduct Authority, which under the Bill would have civil recovery powers for the first time.