CLIFFORD

CHANCE

CRIMINAL FINANCES ACT 2017: STARTING GUN FIRED FOR FINANCIAL CRIME CHANGES – NEW TAX OFFENCES ENTER INTO FORCE

On 30 September, new corporate offences in relation to failure to prevent the facilitation of tax evasion will enter into force. However, the Criminal Finances Act 2017, which introduces them, also contains a raft of other changes to UK financial crime frameworks. When these enter into force (expected to be later in 2017), they will have significant practical implications for financial crime compliance programmes. Their arrival coincides with a period of close scrutiny and strong enforcement activity by authorities worldwide.

This briefing examines the new corporate offences and the other imminent changes to financial crime frameworks. It also looks further ahead to measures which governments in the UK and further afield are considering introducing and summarises the approaches being taken by enforcement authorities in some key jurisdictions.

KEY MEASURES NOW IN FORCE

New offences of failure to prevent the facilitation of tax evasion

There are two new offences, namely failure to prevent facilitation of UK tax evasion offences (the UK offence) and failure to prevent facilitation of foreign tax evasion offences (the foreign offence).

Most businesses have been preparing for some time for these new offences, which are similar in many respects to the now relatively well tried and tested offence of failure to prevent bribery under section 7 of the Bribery Act 2010 (BA 2010).

The new offences are of broad application. A "relevant body", which can include advisers, will commit an offence if it fails to prevent the facilitation of tax evasion (whether in the UK or elsewhere) by an “associated person" (broadly employees and agents). Unlike the equivalent bribery offence, it is not necessary for the relevant body itself to have benefited from tax evasion. This, together with the fact that tax is a consideration in virtually every transaction,

has required businesses to look at a wider range of factual circumstances and staff/agents than they did when preparing for the implementation of BA 2010.

The territorial scope of the new offence is very wide. A relevant body may commit the UK offence regardless of where the facilitation occurs and regardless of where it is incorporated. A relevant body may commit the foreign offence if the facilitation occurs in the UK or if the body is incorporated in the UK or carrying on business in the UK. The foreign offence requires that the conduct concerned would amount to an offence in the jurisdiction concerned as well as in the UK. Prosecutions seem more likely for the UK offence but we expect the authorities will not hesitate to prosecute for the foreign offence if the entity concerned has a connection with the UK. We may also see political/media pressure for a prosecution where the foreign tax evasion is high profile, for example where it involves prominent individuals or companies.

The only defence is for the relevant body to show that it had in place reasonable prevention procedures or that it was not reasonable in all the circumstances for it to have such prevention procedures in place. The defence under BA 2010 is very slightly different (it requires a corporate to establish that it took "adequate procedures" to avoid the commission of a substantive bribery offence; not having procedures is not a BA 2010 defence).

The Serious Fraud Office (SFO) will have the power to investigate and prosecute these new offences in addition to HM Revenue & Customs (HMRC) and the Crown Prosecution Service (CPS).

HMRC has now finalised its guidance on the new offences. Points of interest include the recent clarification (added in response to the consultation process conducted earlier in 2017) that, as part of the reasonable prevention procedures, HMRC expects entities to draft and maintain a written statement setting out their "*position on involvement in the criminal facilitation of tax evasion, including the provision of services which pose a high risk of being misused to commit a tax evasion offence*".

What is necessary and appropriate will vary, but the key messages emerging from the guidance are that conducting a detailed risk assessment, demonstrating top level commitment (which may, for example, take the form of amendments to Codes of Conduct), implementing training and ongoing monitoring and review are important ingredients. The guidance makes clear that less is required of SMEs, but HMRC expects them to put some measures in place.

KEY MEASURES NOT YET IN FORCE

As noted above, the Criminal Finances Act provides for a number of changes to specific aspects of anti-money laundering (AML) and counter terrorism financing (CTF) frameworks and adds to them in some important respects. Current indications are that the provisions making these changes and additions will enter into force during Autumn 2017.

AML - Suspicious activity reporting: Extension of the moratorium period

The Government stopped short of complete overhaul of the suspicious activity reporting originally mooted in the action plan that foreshadowed the Criminal Finances Act. Instead, it has opted to retain the current model but to substantially increase the "moratorium period" (the time period within which those who have filed suspicious activity reports (SARs) and sought consent

from the National Crime Agency (NCA) are prevented from proceeding with transactions).

When the relevant provisions enter into force, it will be possible for the moratorium period to be extended by successive orders beyond the previous 31 day limit, up to a maximum of 217 days if enforcement authorities are able to persuade Crown Court judges that investigations relating to SARs are being conducted "*diligently and expeditiously*", further time is needed and "*it is reasonable in all the circumstances for the moratorium period to be extended*".

Cases in which such long extensions are sought and obtained are expected to be relatively rare. It is likely though that applications will be made by the NCA and other enforcement authorities, many of whose resources are under significant strain, to enable them to assemble evidence in support of applications for restraint orders and/or make mutual legal assistance requests to agencies in other countries (and the Government has encouraged them to do so).

Lengthy periods of hiatus are likely to create substantial practical problems for reporting institutions, particularly given the restrictions on disclosure of any details of SARs under tipping off provisions.

Resisting applications for extension of the moratorium period is likely to be difficult for "interested parties" (which is defined quite broadly as the person who submitted the SAR or "*any other person who appears to* [the enforcement authority applying for the extension of the moratorium period] *to have an interest in the relevant property*"). Enforcement authorities are likely to avail themselves of specific provisions enabling them to ask courts to withhold access to evidence upon which applications for extensions are based from interested parties.

In April 2017, in a case giving clues as to the approach likely to be taken by the court to suggestions by interested parties that the moratorium period should not be extended, the Court of Appeal overturned a previous decision providing declaratory relief to enable a payment services business to operate accounts frozen by a bank during the moratorium period. The Court did so notwithstanding claims that the freeze was having a "*disastrous*" effect. In doing so, the Court reiterated that "*the public interest in the prevention of money laundering as reflected in the statutory procedure has to be weighed in the balance and in most cases is likely to be decisive*".

The power to extend the moratorium period is at least partly directed towards encouraging those filing consent SARs to consider carefully whether it is in fact necessary to do so and at reducing levels of defensive reporting by some firms. The Government will be examining the effect of the changes on the numbers and quality of SARs submitted. Importantly, it has not removed the option of the complete removal of the consent regime from the table whilst it does so.

AML - New information sharing arrangements

The Act will put the Joint Money Laundering Intelligence Taskforce (JMLIT) on a permanent footing, a measure for which banks and law enforcement agencies had strongly advocated. It will enable information on suspicions of money laundering to be exchanged between private sector firms operating in the regulated sector (i.e. not only to/from the NCA) and provides a framework for joint SARs to be submitted to the NCA.

Unexplained wealth orders

The NCA, SFO, HMRC, Financial Conduct Authority (FCA) and CPS will have powers to apply to the High Court for unexplained wealth orders (UWOs) requiring individuals to explain the origins of assets that appear to be disproportionate to their known lawfully obtained income.

UWOs may be made against individuals who are "politically exposed persons" (PEPs) in countries other than EEA states (or their family members and known close associates) or where the relevant authority has reasonable grounds to suspect that the person concerned (or a person connected with him or her) has been "involved in serious crime". As was explained during the debates leading to the passage of the Act, this differential, and in particular the absence of any requirement for reasonable grounds to suspect non-EEA PEPs of having been involved in serious crime is aimed at targeting flows of funds to the UK from countries perceived as representing a higher risk in terms of corruption.

As with other parts of the Act, the scope of these new powers is broad. UWOs may apply to jointly held property and it does not matters for these purposes whether the property in question was obtained before or after the Act came into force or whether the "serious crime" is suspected to have occurred in the UK or elsewhere. Reflecting concerns raised during the passage of the Act about disparities in property prices across the UK, the threshold for the value of property in respect of which a UWO may be made came down from the originally mooted figure of £100,000 to £50,000.

During some of the debates leading to the passage of the Act, ministers insisted that the NCA and other agencies are adequately resourced to be able to use this new power wherever it is appropriate and useful. A document published by the Government to accompany the passage of the Act predicts that UWOs will not be used during the first year in which they are available, but that there will be approximately 20 applications per year in due course.

UWOs may be accompanied by interim freezing orders aimed at preserving property in respect of which authorities' suspicions prove to be well founded. Where such orders are made, enforcement authorities must make a determination about whether to pursue confiscation, civil recovery or other proceedings.

Institutions served with freezing orders in respect of their customers (or which learn that their customers have been served with UWOs) will have to consider whether the fact that authorities have pursued such orders engages other AML obligations. This may include considerations of whether it is appropriate to file SARs in some cases, but as a minimum is likely to involve assessments of whether, applying a risk based approach, levels of due diligence and monitoring applied to transactions and relationships with those customers are set at the correct level.

New civil recovery provisions

The Act amends the Proceeds of Crime Act 2002 (POCA) so that it now expressly provides that enforcement authorities may seek civil recovery orders in respect of property obtained from unlawful conduct which constitutes or is connected with the commission of gross human rights abuses or violations in the UK or abroad.

The amendment of the definition of "unlawful conduct" in Section 5 of POCA is targeted at recovering proceeds connected with the torture of any person who has sought to expose illegal activity of public officials or those acting in public capacities or who was seeking to defend human rights. Anyone profiting, assisting, directing or sponsoring, or acting as an agent in connection with activities relating to the commission of such abuses can be subject to such orders.

The so-called Magnitsky Amendment refers to the widely-reported fate of a Russian lawyer beaten to death in Moscow after uncovering the alleged theft of US$230 million from state funds by Russian tax officials.

Strengthened investigative powers

The Act includes various amendments to the powers of the NCA and various other agencies aimed at enabling them to respond more efficiently to SARs and to disrupt suspected money laundering through the forfeiture of monies and portable high value items used to store and move the proceeds of crime.

The process by which disclosure orders may be obtained has also been streamlined, meaning that it will no longer be necessary for investigating officers to obtain authorisation from prosecutors to obtain such orders. Rather, they will be able to do so on the authority of senior investigating officers. The scope of disclosure orders has also been widened to cover a wider range of money laundering and other offences.

The Act also extends certain investigative powers under POCA, including some search and seizure powers, to SFO officers and introduces new powers enabling bank accounts to be frozen or forfeited in some circumstances. The Government consulted on draft codes of practice relating to the exercise of these and other powers in July 2017, but the finalised versions of these codes have not yet been published.

OTHER UK PROPOSALS TO COMBAT FINANCIAL AND ECONOMIC CRIME

Many of the measures contained in the Criminal Finances Act arose in large part from a review of existing AML and CTF frameworks, and the Act progressed amid discussion about whether UK enforcement authorities have sufficient tools at their disposal to enable them to effectively investigate and prosecute financial and economic crime.

Offence of illicit enrichment

The UK Government, noting concerns about the reversal of the burden of proof, decided not to proceed with previously mooted proposals to introduce an offence of illicit enrichment. Commenting on its decision to do so when it introduced the Act in draft form, it also acknowledged the likely limited practical effect of any such offence, particularly against individuals not located in the UK.

Offence of failure to prevent economic crime

During the legislative process leading to the Act, an amendment was introduced seeking to enact a broad offence of failing to prevent economic crime by corporate entities. That amendment was ultimately withdrawn as it coincided with a call for evidence by the UK Government on which option(s) should be pursued to tackle corporate crime. The outcomes of that exercise

are awaited, although it is widely recognised that the appetite for large scale changes to fundamental tenets of the UK legal system (and the capacity of the Government to design them and Parliament to consider them in sufficient detail) has been substantially diminished by the decision in the intervening Brexit referendum.

For full details of the call for evidence, see our previous briefing.

Designation of entities as being of money laundering concern

The Government originally consulted on the introduction of a power to designate an entity of being of money laundering concern. Similar provisions appear in the US PATRIOT Act.

It decided not to even include any such proposals in draft legislation though, largely in response to indications from law enforcement agencies that there would be a need to disclose sources of intelligence and that there would probably be lengthy challenges to decisions to designate entities. It indicated at that stage that the question of whether or how to introduce the power was under review.

THE CHANGING UK AML REGIME

The new measures introduced by the Criminal Finances Act come at a time of considerable change to AML legislation in the UK. Businesses operating in the regulated sector have already had to adapt to the changes to customer due diligence and monitoring introduced under the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017, which implement the EU Fourth Money Laundering Directive in the UK.

These changes are occurring against a backdrop of sustained pressure from enforcement authorities. In particular, the FCA remains focused on taking strong action against firms and individuals alike wherever it considers that they have not done enough to prevent the financial system being used for the purposes of financial crime. It confirmed in its most recent annual anti-money laundering report that the number of AML related enforcement investigations pursued by it rose during 2016/17 (as did the number of AML related skilled person reports), and that there are a number of significant investigations underway and being contemplated.

THE GLOBAL AML ENFORCEMENT LANDSCAPE

It is not only in the UK where legislative changes are afoot and where enforcement authorities are under pressure to achieve conspicuous results. Following action taken against the same institution in 2012 in the UK for similar failings, the New York Department of Financial Services has recently underlined the importance it attaches to effective AML risk management and compliance processes, imposing a US$225 million fine on Habib Bank and its New York branch, which has also surrendered its licence to operate in New York. The action is the most recent example of the continued aggressive enforcement approach being adopted by US authorities.

The enforcement activities of the Australian authorities have also attracted substantial publicity in recent months, with the Australian AML regulator, AUSTRAC, commencing action against one bank in respect of alleged failings in its customer due diligence and reporting of suspicious activities associated with customers use of intelligent deposit machines. ASIC has since

announced an investigation into the bank and APRA has announced it will conduct an inquiry into the bank's governance, culture and accountability following the allegations raised by AUSTRAC. AUSTRAC can be expected to pursue large civil penalties in its action against the bank.

It is unlikely to be the last case of its type, as AML/CTF remains a hot topic in Australia and the Asia Pacific region. The Australian Parliament is currently considering a bill proposing a number of amendments to the Australian AML/CTF regime, including an increase in the powers available to AUSTRAC, to enforce compliance with the AML/CTF regime, in particular powers to issue infringement notices under a wider variety of civil penalty provisions, and to issue remediation notices. This legislation, which responds to concerns raised by the Financial Action Task Force, also contains proposals intended to facilitate sharing of certain information between reporting entities who are related bodies corporate reminiscent of those contained in the Act in the UK.

CONTACTS

Roger Best
Partner

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

David Harkness
Partner

T +44 20 7006 8949
E david.harkness@cliffordchance.com

Michael Lyons
Partner

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

Dan Neidle
Partner

T +44 20 7006 8811
E dan.neidle@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

This publication does not necessarily deal with every important topic or cover every aspect of the topics with which it deals. It is not designed to provide legal or other advice.

www.cliffordchance.com

Clifford Chance, 10 Upper Bank Street, London, E14 5JJ

© Clifford Chance 2017

Clifford Chance LLP is a limited liability partnership registered in England and Wales under number OC323571

Registered office: 10 Upper Bank Street, London, E14 5JJ

We use the word 'partner' to refer to a member of Clifford Chance LLP, or an employee or consultant with equivalent standing and qualifications

If you do not wish to receive further information from Clifford Chance about events or legal developments which we believe may be of interest to you, please either send an email to nomorecontact@cliffordchance.com or by post at Clifford Chance LLP, 10 Upper Bank Street, Canary Wharf, London E14 5JJ

Abu Dhabi • Amsterdam • Bangkok • Barcelona • Beijing • Brussels • Bucharest • Casablanca • Dubai • Düsseldorf • Frankfurt • Hong Kong • Istanbul • London • Luxembourg • Madrid • Milan • Moscow • Munich • New York • Paris • Perth • Prague • Rome • São Paulo • Seoul • Shanghai • Singapore • Sydney • Tokyo • Warsaw • Washington, D.C.

Clifford Chance has a co-operation agreement with Abuhimed Alsheikh Alhagbani Law Firm in Riyadh.

Clifford Chance has a best friends relationship with Redcliffe Partners in Ukraine.