McDermott Will & Emery

Special Report

UK Criminal Finances Act 2017
Are You Compliant?

May 2018

McDermott Will & Emery

SPECIAL REPORT

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1. Introduction

This article provides important information regarding two new corporate criminal offences under the UK Criminal Finances Act 2017 (Act) that came into effect on 30 September 2017.

To comply with the Act and to protect your organisation from criminal liability under these new offences, you will need to implement policies and procedures aimed at preventing employees and other associated persons from deliberately and dishonestly helping others to evade UK or foreign taxes (*i.e.*, anti-tax evasion facilitation policies and procedures), even if the risk of your organisation being exposed to such illegal activity is low.

Heads of legal, risk and compliance and other key senior personnel should read this article, as they will be responsible for overseeing the implementation of anti-tax evasion facilitation policies and procedures for their employer organisation in accordance with the guidelines set out herein, to the extent they have not already done so.

2. What Are the Act's Implications for My Business or Organisation?

The Act created two new corporate criminal offences of failure to prevent facilitation of (1) UK tax evasion (UK CFA Offence) and (2) foreign tax evasion (Foreign CFA Offence) in much the same way as the UK Bribery Act 2010 created a corporate criminal offence of failure to prevent bribery. Like their UK Bribery Act equivalent, both the UK and Foreign CFA Offences have a wide reach outside the United Kingdom, meaning that businesses of all sizes and industry sectors must implement anti-tax evasion facilitation policies and procedures *now*, to the extent they have not already done so, in order to protect their organisation from criminal liability under the Act, regardless of whether they have operations in the United Kingdom. In practical terms, this means that all companies and partnerships are now required, amongst other things, to create and maintain anti-tax evasion facilitation policies and procedures alongside their existing anti-bribery and corruption policies. Further details on this point can be found under the section headed "*What Does My Business or Organisation Need to Do*?"

> "As a first step, your organisation should carry out a risk assessment of its business by evaluating the nature and extent of its exposure."

3. How Can a UK CFA Offence or a Foreign CFA Offence Be Committed?

Under the Act, a company or partnership (including an LLP) (a relevant entity) will automatically be guilty of an offence if, broadly, a person associated with the relevant entity deliberately and dishonestly helps others to evade UK or foreign tax. "Associated persons" for these purposes will typically be employees, but they can also include agents or other persons performing services for or on behalf of the relevant entity in their capacity as associated persons, such as contractors or sub-contractors, or even third parties providing services for one of the organisation's customers on a referral basis. The UK and Foreign CFA Offences do *not* apply to individuals, nor is there a requirement for a criminal intent (*mens rea*). (By contrast, UK tax evasion and helping others to evade UK tax, which are already separate criminal offences in their own right under UK law, *do* apply to individuals, and both offences require a criminal intent).

To be within the scope of a UK CFA Offence, a relevant entity need not have any UK operations, and any criminal conduct associated with tax evasion or tax evasion facilitation need not be committed in the United Kingdom. In this context, a relevant entity will automatically be guilty of a UK CFA Offence if 1) a taxpayer commits (for example) a UK common law offence of cheating the public revenue, or fraudulently evades VAT or income tax contrary to an applicable UK statute (tax evasion), and 2) an associated person of the relevant entity "facilitates" tax evasion by that taxpayer in any one of the following ways, while performing services for or on behalf of the relevant entity, whether as an employee, agent, contractor or in some other representative capacity (a facilitator):

- By deliberately and dishonestly facilitating the commission of revenue fraud by that taxpayer
- By becoming knowingly concerned in, or taking steps with a view to, that taxpayer fraudulently evading tax

- By aiding and abetting that taxpayer in committing a revenue fraud

The Foreign CFA Offence works in a similar way to the UK CFA Offence, except that the taxpayer and the facilitator would need to have committed offences under the local law of the relevant overseas jurisdiction equivalent to those of the UK law offences cited above, and the actions of both the taxpayer and the facilitator would need to have constituted a crime had they taken place in the United Kingdom, in order for a relevant entity to be automatically guilty of a Foreign CFA Offence. In addition, where a Foreign CFA Offence is concerned, a degree of UK nexus is required. This means that either the relevant entity would need to have UK operations, or any conduct constituting part of the associated foreign tax evasion facilitation offence would need to take place in the United Kingdom, in order for the relevant entity to be within the scope of the Foreign CFA Offence.

It will be a defence to both UK and Foreign CFA Offences for a relevant entity to have "reasonable prevention procedures" in place. (This is similar to the "adequate procedures" defence under the UK Bribery Act).

4. What Does My Business or Organisation Need to Do?

As a first step, your organisation should carry out a risk assessment of its business by evaluating the nature and extent of its exposure to the risk of its associated persons criminally facilitating tax evasion offences. The conclusions from the risk assessment and the fact patterns which give rise to the risks identified in the risk assessment will inform the content of the "reasonable prevention procedures" (which will include the anti-tax evasion facilitation policies and procedures referred to previously), as well as their level of "reasonableness". A regularly reviewed and updated risk assessment will be invaluable in demonstrating to HM Revenue & Customs (HMRC), the English courts and any applicable regulatory body that your organisation understands where and how the risks of tax evasion facilitation could arise within its business, and thus the reasons for its prevention procedures.

Existing Anti-Money Laundering (AML) and UK Bribery Act policies may be a useful starting point in creating a set of anti-tax evasion facilitation policies and procedures. One should not become overly reliant on existing AML and UK Bribery Act procedures, however, because the content of the anti-tax evasion facilitation policies and procedures will ultimately be driven by the risk assessment and its conclusions. Also, the fact patterns which give rise to tax evasion facilitation risks may not necessarily be the same as those which give rise to bribery or money laundering risks. For these reasons, implementing "reasonable prevention procedures" requires careful consideration and must not merely be an exercise in updating existing Anti-Bribery and Corruption Policies to reflect the requirements of the Act.

According to HMRC guidance, reasonable prevention procedures must be informed by the following six principles:

Risk Assessment

To conduct a risk assessment, you will need to carry out a 360-degree review of each business unit within your organisation by "sitting at the desk" of all business unit employees, agents and individuals who provide services for or on behalf of that business unit, and asking whether such persons have the motive, opportunity and means to criminally facilitate tax evasion offences, and if so, how those risks might be managed. The risk assessment must be documented and kept under review.

There is no set format for documenting a risk assessment, but it may, for example, include statements or descriptions of particular risks to which a business unit is exposed, with a category or rating (e.g., high, medium, low) allocated to each risk, plus an indication of the frequency of that risk's occurrence. You should also have regard to existing recommended risk-based approaches, such as the Financial Conduct Authority's guide for firms on preventing financial crime, the Law Society's Anti Money Laundering Guidance (particularly Chapter 2), the Joint Money Laundering Steering Group guidance and HMRC's guidance. If your organisation operates in a regulated sector, you should also consider any relevant guidance issued by the applicable regulatory body.

Proportionality of Risk-Based Prevention Procedures

The procedures must be proportionate to the frequency and degree of criminal tax evasion facilitation risk to which your organisation is exposed. For example, some organisations, such as those providing private wealth management services, may face significant risks that require more extensive prevention procedures than organisations facing limited risks. The level of protection required will depend on the nature, scale and complexity of your organisation's activities, but in general, small organisations are unlikely to need procedures as extensive as those of a large multinational organisation. HMRC recognises that the

reasonableness of any prevention procedures should take account of the level of control and supervision the organisation is able to exercise over a particular person acting on its behalf, and the proximity of that person to the organisation. Organisations need not undertake excessively burdensome procedures in order to eradicate all risk, but equally they should not merely pay lip service to preventing the criminal facilitation of tax evasion.

Top-Level Commitment

The top-level senior management within your organisation should be committed to preventing associated persons from engaging in criminal facilitation of tax evasion and should foster a "zero tolerance" approach to such activities. The nature and level of involvement of senior management will vary depending on the size and structure of the organisation, but any involvement on their part should include communication and endorsement of the organisation's stance on preventing the criminal facilitation of tax evasion, and oversight of the development and review of preventative procedures. With smaller entities, it may be proportionate for the most senior management to be personally involved in the design and implementation of preventative measures. In a large multinational organisation, it may make more practical sense for senior management to delegate the development and review of any preventative measures to a committee and to oversee the work of that committee, for example.

Due Diligence

Your organisation will need to apply appropriate and proportionate due diligence procedures in respect of persons who perform or will perform services on behalf of the organisation, using an appropriate risk-based approach, in order to mitigate any identified risks. For example, it may be that the risk identified in a given situation is so remote as to justify there being no procedures in place. Alternatively, an organisation may assess the risks as being substantial in relation to a particular associated person or service, and therefore may apply considerably greater scrutiny in relation to that person or service. Organisations may choose to conduct their due diligence internally or through consultants.

Communication (Including Training)

Internal communications should convey the organisation's zero-tolerance policy for criminal facilitation of tax evasion by its employees, agents and other representatives, and the consequences for anyone found to be complicit in such illegal activity. Training may be either bespoke or incorporated into existing AML or other financial crime prevention training. Where external communications are concerned, organisations may consider it proportionate and appropriate to convey these messages to partner organisations, particularly those to whom it is making a referral or from whom clients or customers are referred.

Monitoring and Review

An organisation will need to monitor and review its preventative procedures and make improvements where necessary, since the nature of the risks to which the organisation is exposed will change and evolve over time.

5. What Are Some Common High-Risk Scenarios?

Some common "red flag" business scenarios where an organisation may be at a high risk of its associated persons criminally facilitating tax evasion by another person, and thus at a high risk of committing a UK or Foreign CFA Offence, include the following:

- Receiving requests from a client, customer, counterparty or other third party to describe products or services, make payments, issue invoices or prepare financial records in an unusual way in order to accommodate the tax or financial planning purposes of that client, customer, counterparty or third party
- Rewarding executives for excessive risk taking (e.g., with bonuses or commission)
- Being asked to address invoices to a person who is not named in the relevant contract or terms and conditions of engagement as the recipient or customer of the goods or services being supplied, particularly where the effect of such a measure results in a more favourable VAT outcome for the person to whom the invoice is addressed or for the customer named on the contract
- Being asked to provide infrastructure—such as IT services, professional trustee services (including nominee services), virtual offices, legal services, banking services or escrow accounts services—to help a client or customer conceal income, profits or wealth from a tax authority, or referring that client or customer to a third party for the same purpose (this is why financial services firms, law firms and accounting firms are particularly at risk)
- Engaging in, or being asked to engage in, any complex or unusually large transactions which have no

apparent economic, commercial or lawful purpose

This list is by no means exhaustive, and each organisation may have its own specific high-risk scenarios depending on the nature of its activities.

6. What Are the Consequences or Sanctions for Non-Compliance?

If a relevant entity is found guilty of a UK or Foreign CFA Offence, possible sanctions include unlimited financial penalties, ancillary orders such as confiscation orders, and serious crime prevention orders. The mere fact of a criminal conviction under the Act could also have other adverse consequences for a relevant entity, such as reputational damage and loss of business. The entity may also be required to disclose any criminal conviction under the Act to regulatory bodies both in the United Kingdom and overseas.

HMRC will investigate potential UK CFA Offences, with prosecutions brought by the Crown Prosecution Service (CPS) for England and Wales, the Crown Office and Procurator Fiscal Service for Scotland, or the Public Prosecution Service for Northern Ireland.

The Serious Fraud Office (SFO) or National Crime Agency will investigate potential Foreign CFA Offences. Prosecutions for such offences will be brought by either the SFO or CPS, but only with the consent of the Director of Public Prosecutions or the Director of the SFO, which would only be given where a prosecution under this head was in the public interest.

7. The McDermott Difference

- We can advise more fully on how the Act potentially applies to the particular circumstances of your organisation, as well as the particular business scenarios or circumstances which are most likely to give rise to tax evasion facilitation risks, thus putting the organisation at risk of automatically committing a UK CFA Offence or Foreign CFA Offence.
- We can help you document your risk assessment. If appropriate, and as a preliminary step, we can also create a tailored and bespoke risk assessment questionnaire (RAQ) for you to complete in order to help you carry out your risk assessment. Unless you have already started the risk assessment process or do not feel that an RAQ is necessary, we recommend that you complete an RAQ as it can help sharpen your focus on the areas to be reviewed.
- Having documented your risk assessment, we can then draft “anti-tax evasion facilitation” policies and procedures from scratch to suit the needs of your organisation and the tax evasion facilitation risks it faces, together with any standard form documentation to help you manage tax evasion facilitation risks arising out of your business relationships (e.g., standard engagement letter clauses, standard compliance request letters, codes of conduct), in order to help you establish the required “reasonable prevention procedures” defence.
- We can also review any existing policies and procedures you have in place and make any suggestions or amendments where necessary so as to ensure that your policies and procedures comply with the Act.

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