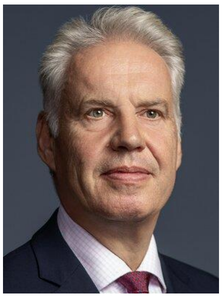
Taking Stock Of Changes UK Economic Crime Act Will Bring

By **Alistair Graham, Chris Roberts and Nazia Sohail** (May 30, 2024)



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With more than six months since the Economic Crime and Corporate Transparency Act 2023 receiving royal assent and becoming law on Oct. 26, 2023, it is time to take stock of some of the changes that the act will introduce in the near future and the steps corporate leaders can take.

The act introduced a number of changes, some of which came into effect immediately in October and others that are still due to be implemented.

Why Did These Reforms Come About?

Fraud is the most common offense in the U.K. As the government's 2023 Fraud Strategy notes, "Fraud now accounts for over 40% of crime but receives less than 1% of police resource."[1]

The act seeks to help combat this by, for example:

- Holding organizations to account if they profit from fraud committed by their employees;
- Improving fraud prevention;
- Protecting victims;
- Strengthening existing powers to fine and prosecute organizations and their employees for fraud by closing loopholes that have allowed organizations to avoid prosecution in the past; and
- Driving a major shift in corporate culture to help reduce fraud.[2]

This article will cover changes that are yet to come into effect, namely:

- The new failure to prevent fraud offense;
- The second set of expanded powers for Companies House; and
- Changes to help combat crypto-related criminal activity.

Changes Yet to Come Into Effect

New Failure to Prevent Fraud Offence

A new strict liability corporate offense of failure to prevent fraud builds on the existing strict liability corporate offenses of failure to prevent bribery under the Bribery Act 2010. It also extends the failure to prevent the facilitation of tax evasion under the Criminal Finances Act 2017.

The new offense only applies to "large organizations," i.e., those that meet at least two of the following criteria in the financial year preceding the year of the fraud offense, with:

- More than 250 employees;
- More than £36 million ($46 million) turnover; or
- More than £18 million in aggregate assets on its balance sheet.

A corporation is also a large organization where it is a parent undertaking of a group that meets at least two of the following criteria in the financial year preceding the year of the fraud offense, with:

- An aggregate turnover of over £36 million net — or £43.2 million gross;
- An aggregate balance sheet total of over £18 million net — or £21.6 million gross; or
- More than 250 aggregate employees.[3]

A large organization is liable under the new offense if it fails to prevent one of the fraud offenses specified in Schedule 13 of the act where:

- An associate of the organization commits the fraud; and

- The fraud is intended to benefit the organization or a person to whom services are provided on behalf of the organization.

The term "associate" is defined as an employee, agent, subsidiary or employee of a subsidiary of the organization, as well as any others who perform services for or on behalf of the organization.[4]

The offenses listed in Schedule 13 of the act include false accounting, fraud by false representation, fraud by abuse of position, and fraud by failing to disclose information.[5]

The secretary of state is empowered to pass secondary legislation to add or remove offenses from this schedule. Aiding, abetting, counseling or procuring the commission of one of the listed offenses also amounts to an offense.

The failure to prevent fraud offense has potentially wide extraterritorial effect. Unlike the offense of failure to prevent bribery, there is no requirement for a company to be incorporated in, or carrying on a business or part of a business in, the U.K. for the failure to prevent fraud offense to bite.

The territorial effect of the failure to prevent fraud offense therefore flows from the territorial effect of the relevant underlying fraud offense in Schedule 13 of the act.

If an associate commits fraud under U.K. law, or targeting U.K. victims, the organization could potentially be liable to be prosecuted, even if the organization — or the associate — are based overseas.

The organization will only have a defense if it can show it either had so-called reasonable procedures in place to prevent fraud, or that it was not reasonable for the organization to have such procedures in place.[6]

We await the government's guidance on the reasonable procedures defense to the new failure to prevent fraud offense, which will assist organizations when designing and implementing those procedures.

The failure to prevent fraud offense will only come into force some time — currently six months — after the guidance is published. It is currently anticipated that the guidance will be published later this year.

Companies House: Second Set of Expanded Powers

Further changes to Companies House authority will come into effect later this year, including the introduction of compulsory identity verification for all directors and people with significant control of U.K. corporate entities.

Identity verification requirements will apply to all new and existing registered company directors, people with significant control and anyone else filing documents with the registrar.

For new directors, identity verification will need to take place before the company is formed, while people with significant control will be required to be verified within a short time after incorporation.[7]

More detail on the process is awaited, but we know that there will be two types of identity verification: Direct verification via Companies House or verification through a so-called authorized corporate service provider, i.e., a person subject to the U.K.'s money laundering regulations and who has registered at Companies House.

There will be a transition period for existing companies to comply with the requirements, but after that, anyone who was required to verify their identity but failed to do so could be subject to criminal or civil proceedings. A new company's incorporation could also be rejected, and directors could be barred from their positions.

Crypto-Related Criminal Activity

The act expands the powers available to law enforcement in respect of crypto-related criminal activity. This includes extending the confiscation and civil recovery regime under the Proceeds of Crime Act 2002 to crypto-assets, granting law enforcement agencies significant authority to seize, store and potentially sell or destroy crypto-assets as part of investigations.[8]

Given that these expanded powers required amendments to the Proceeds of Crime Act 2002, secondary legislation has been enacted to that effect.

The Proceeds of Crime Act 2002 (Search, Recovery of Cryptoassets and Investigations: Codes of Practice) Regulations 2024 were published on Jan. 23 and came into force on April 26.

Action Steps

In light of the changes already introduced by the act and those still pending, we recommend that organizations do the following.

- Review and reinforce their:
    - Policies, procedures and controls to mitigate identified fraud risk;
    - Financial management systems, such as for managing expenses and payments to suppliers;
    - Whistleblowing program;
    - Training;
    - Third-party contractual documentation;
    - Third-party (including subsidiary) oversight;
    - Use of data analytics;
    - Monitoring of fraud risk on an ongoing basis; and
    - Internal audit program.
- Identify those captured by the new definition of "Senior Manager," whose acts may lead to the organization's liability for the specified economic crimes.
- Ensure that these Senior Managers are aware of identified risks and applicable policies and procedures.
- Seek to create an organizational culture and governance structure to address economic crime risk.

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[1] Fraud Strategy: stopping scams and protecting the public, updated 1 June 2023 (https://www.gov.uk/government/publications/fraud-strategy/fraud-strategy-stopping-scams-and-protecting-the-public).

[2] Factsheet: failure to prevent fraud offense, updated 26 October 2023 (https://www.gov.uk/government/publications/economic-crime-and-corporate-transparency-bill-2022-factsheets/factsheet-failure-to-prevent-fraud-offence).

[3] Sections 201-202 of the act.

[4] Section 199(7) of the act.

[5] Section 199(6)(b) of the act.

[6] Section 204 of the act.

[7] Sections 64-69 of the act.

[8] Sections 179-181 of the act.