Financial Crime Update

Clinton Esosa Osemwengie reviews recent financial law developments

AN APPRAISAL OF FINANCIAL PENALTIES UNDER DEFERRED PROSECUTION AGREEMENTS IN THE UK

Deferred Prosecution Agreements (DPA) are gradually becoming an established alternative that corporate offenders in the UK are turning to. The concept which encourages corporate offenders to self-report and pay the cost of the criminal acts allegedly committed, while affording them the opportunity to rectify their internal malfeasance have, since its introduction in 2014, recorded large scale financial penalties against corporate offenders. This Update argues that although the financial penalties agreed and arrived at by the courts appear to be effective, the computational methodology employed in arriving at the financial penalties gives room for inconsistency.

INTRODUCTION

Financial penalties are at the heart of the deferred prosecution framework. They play an important role in reflecting the severity of the offences allegedly committed by corporate offenders.

So far, only nine corporations have been subject to the DPA mechanism by the Serious Fraud Office (SFO) in resolving their alleged criminal conduct. This has brought to light some of the requirements that should be present in a DPA (financial penalty, compensation, disgorgement of profit, compliance measures, cooperation with relevant authorities, cost to the Prosecuting Authority among others). Of particular interest is the level of discounts applied by the courts.

In reviewing the financial penalties that have been handed down so far under DPAs agreed with the SFO, this Update examines the factors taken into account by the court to adjust the financial penalties and the circumstances when the court will apply discounts. Discounts are applied by the court to ensure that the penalties arrived at are fair, reasonable and proportionate to the offences allegedly committed on the one hand, while also ensuring that the penalty serves as a deterrence to prospective offenders on the other.

COMPUTATIONAL METHODOLOGY

The parameters to guide the court in the assessment of the financial penalties are wide. This is in order to ensure that the court achieves a penalty that is comparable to what would have been imposed if a conviction was to be entered following a guilty plea. In achieving that comparability benchmark, the cumulative provisions of para 5(3)(a) of Sch 17 of the 2013 Act; para 8.1 (iii), 8.3 and 8.4 of the DPA Code of Practice envisage that reference is made to the relevant Sentencing Council Guidelines. These guide the court in the computation and assessment of the financial penalties that will be imposed on the corporation.

In all the DPAs that have been conducted to date, the courts have made recourse to the Sentencing guidelines for Corporate Offenders: Fraud, Bribery and Money Laundering (Guidelines) in the assessment of the financial penalty. The starting point according to the Guidelines is to determine the severity of the offence. In computing this, the court considers the culpability of the corporate offender and the harm figure. Taking culpability, the guidelines group the multiplier effect based on the seriousness of the offence into high, medium and low culpability.

In using the appropriate culpability category, a starting point for the multiplier to the harm figure can be derived. That multiplier for the appropriate category range is then adjusted for aggravating and mitigating factors (by reference to a non- exhaustive list set out in the Guidelines). This allows for the assessment of a final multiplier. The Guidelines recognise that the culpability might be such that it is appropriate to move outside the category range altogether.

However, irrespective of the multiplier effect on the harm figure, the court takes into account the ability of the offender to pay. The DPA entered between the SFO and Guralp Systems Limited (*SFO v Guralp Systems Limited* (U20190840)), which was sanctioned by the court where no financial penalty was awarded, is a quintessential example of this.

A similar situation played out in *SFO v Sarclad Limited* (U20150856). Here the court in its assessment of the penalty, reduced the penalty it initially arrived at from £8.2m to £352,000.00 noting that *Sarclad Limited* would be unable to pay the sum arrived at because the sum would tip it into insolvency. Conversely a recent DPA entered between SFO and Arline Services Limited (*SFO v Arline Services Limited (ASL)* U20201913)) established that *ASL* had the capacity to pay for the financial penalty arrived at based on the backing of one of its largest shareholders.

The discretionary latitude enjoyed by the court in the measurement of financial penalties must be exercised in such a way that the penalty arrived at is comparable to what would have been imposed if there was a conviction. Flowing from this, another criterion the court has implicitly formulated in assessing the effectiveness of financial penalties is what can be described as the "extraterritorial test". This test

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is distilled from the court's analysis of the financial penalties imposed in *Standard Bank (ICBC) Plc*. The question that this test seeks to pose, where the wrongdoing took place outside the UK, is whether the penalty is comparable to that which would have been imposed if the matter were dealt with in another jurisdiction.

In *SFO v Standard Bank ICBC* (U201508254), Standard Bank Plc was alleged to have failed to prevent Stanbic Bank Tanzania Limited (its sister company) from committing bribery contrary to s 7 Bribery Act 2010. The circumstances of the case were such that there were possible violations of the US Foreign Corrupt Practices Act 15 USC. The court in imposing the financial penalty of US$16.8m asked itself whether the penalty was comparable to one that would have been imposed if the matter were handled in the US, using *R v Innospec Ltd* as a guide. The court resolved this in the affirmative and its decision was further confirmed by the US Department of Justice to be fair, reasonable and proportionate.

The assessment of the quantum of the penalty using the final multiplier, taking into account the corporate offender's capacity to pay, reflects the UK's commitment to the OECD Anti-Bribery Convention which seeks to punish bribery offences with effective, proportionate and dissuasive criminal penalties. Putting the financial penalty on an extra-territorial scale gives it an equivalence to what would be imposed in another jurisdiction. Furthermore, the approach disrupts practices engaged by corporations who are in the habit of "fishing" for jurisdictions to set up a presence where lighter penalties are imposed on corporate financial crimes. Corporates must now think twice before committing any wrongdoing in the UK, knowing that a comparative approach will be adopted to arrive at a penalty that reflects the severity of the offence beyond the UK jurisdiction.

The DPA mechanism in the UK has recorded some successes given the high financial penalties that have been imposed on companies so far. In *SFO v Tesco Stores Ltd*, the court approved a financial penalty of £128,992.50 on Tesco Plc for the overstatement of its financial position as a result of the alleged acts of false accounting, contrary to s 17 Theft Act 1968.

However, there is concern as to how the court arrived at the financial penalty using the Guidelines specifically for the offence of false accounting. Although the Guidelines specify that they are applicable to computing financial penalties for the offence of false accounting, they do not make provision for how the court will determine the harm figure, which is usually the starting point in computing a financial penalty. In *SFO v Tesco Stores Ltd* this lacuna created a difficulty and affected the approach taken by the court to arrive at a penalty sufficiently effective to reflect the severity of the alleged offence.

Where there was insufficient evidence of the amount by which the corporate benefitted from the false accounting, the court resorted to an approach under the Guidelines which provides that 10-20% of the relevant revenue may be an appropriate measure in determining the harm figure. With this formula the court arrived at a financial penalty of £128,992.50.

Interestingly, similar difficulties did not surface in a subsequent DPA between the SFO and Serco Geografix Limited *(SFO v Serco Geografix Limited* (U20190413)) which involved a combination of false accounting and fraud charges because the court could easily determine the harm figure based on the facts and circumstances of the case. However, the resurgence of similar circumstances as occurred in the *Tesco* case cannot be ruled out in subsequent DPAs, especially as false accounting appears to be a fairly standard offence.

These concerns align with submissions of the UK Law Society in its assessment of the Guidelines for the computation of financial penalties under the DPA scheme. It is recommended that in order to ensure consistency and certainty in the approach adopted by the court, there should be two types of guidelines – one overarching guideline which sets out the principles of a DPA, and more importantly, an offence-specific guideline which sets out the starting point or range for financial penalties and other conditions.

As noted earlier, the courts are careful to arrive at financial penalties that reflect the severity of the offence committed. This was clear in *SFO v Rolls-Royce Plc & Anor* (U20170036). Here, the amount of the financial penalty imposed was as a result of the gravity of the offence allegedly committed by the engineering magnate across multiple jurisdictions and the monies involved. The offences covered conspiracy to corrupt, failure to prevent bribery and false accounting. The court in computing the financial penalty after the application of discounts arrived at a sum of £239,082,645m.

However, given the hefty amounts of financial penalties imposed on companies so far, there is a growing argument that it would be better to go through the rigours of a criminal trial despite the interim reputational damage it could cause and allow the prosecution to establish the corporate's wrongdoing beyond reasonable doubt. This would give the company the chance of retaining the funds that would have been spent on the payment of DPA financial orders. This argument gained traction following Tesco's DPA where the three employees alleged to have been involved in fraud and false account reporting were all acquitted by the court for lack of evidence.

Similar issues also played out in the *Rolls Royce* case where despite the court's observation that the case to approve the DPA involved large scale bribery and corruption, one that even implicated top senior management, the SFO stated that there was either insufficient evidence of wrongdoing or that it was not in the interest of the taxpayer to prosecute the company.

The prosecuting agencies are required to pass an evidential test under the DPA Code of Practice (and a public interest test) that then gives the court the impetus to consider and approve the DPA financial orders agreed between the prosecuting agency and the corporation. In reliance on the Code of Practice the court assumes that the penalties are justifiable and anchored on admissible evidence. It is therefore essential that the prosecuting agencies under the DPA scheme acquire credible and admissible evidence, not just for the purpose of meeting the evidential test under the DPA but also in order to secure a conviction against those individuals

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involved in the alleged acts. This is crucial so that a company paying a DPA financial order is at least confident that the payments made are justifiable and are as a result of the offences allegedly committed, based on the evidence.

In addition, since the courts play a pivotal role under the DPA scheme, they should also ensure proper evaluation of the evidence produced by the prosecuting authorities before giving their approval.

ADJUSTING FINANCIAL PENALTIES AND THE CONCEPT OF DISCOUNTS ON FINANCIAL PENALTIES UNDER A DPA

The Guidelines give the court power to make further adjustments to the financial penalties.

They set out a number of factors that should be taken into account such as:

- where the company in question can show substantial financial hardship;
- whether the penalty impairs the ability of the company to make restitution to its victims;
- the impact of the penalty on employees of the company and its customers;
- whether the penalty affects the ability of the company to implement its compliance programme, amongst others.

Discounts

The Code of Practice also empowers the court to take into account discounts measured against what would be afforded if there was a guilty plea. The courts are guided by s 144 Criminal Justice Act and the Guidelines issued by the Council on Guilty pleas to ensure that the penalty arrived at by the prosecutors and the court is fair, reasonable and proportionate. The idea behind the concept of discounts under the DPA scheme is to incentivise openness, co-operation and voluntary disclosure of wrongdoing by the corporation.

It is important to state that the discounts applied should be equivalent to what would have been afforded if there was an "early guilty plea".

Records from concluded DPAs have shown that factors such as the extent of the corporation's admission, the level of assistance and co-operation offered to the prosecuting agencies and the extent of compliance are taken into account by the court.

Given the level of co-operation in DPAs concluded so far, it is worthy of note that all the companies that have embraced the DPA have had discounts applied to the financial penalty imposed on them.

CONCLUSION

This update has highlighted the level of discretion afforded to courts when setting financial penalties under DPA schemes. The argument remains that companies may be better off going through the rigours of a criminal trial to avoid paying out hefty financial penalties only for employees to be later acquitted. ■

Further Reading

- Cheung R, 2018, 'Deferred Prosecution Agreements: Cooperation and Confession', *Cambridge Law Journal* vol 77 (1), pp 12-15.
- OECD 2019, Implementing the OECD Anti-Bribery Convention, Phase 4 Two-Year Follow-Up Report: United Kingdom.
- The Law Society, 2012, 'Deferred Prosecution Agreements: Response to Ministry of Justice Consultation' at pp 5-6.