Dr Penny Dunbabin

Fraud Policy Unit

Economic Crime Directorate

Homeland Security Group

Home Office

2 Marsham Street

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13 February 2024

Dear Dr Dunbabin

RE: **DRAFT guidance for the new corporate criminal offence of failure to prevent fraud**

We would like to thank you for including us in the consultation exercise on the draft Guidance. While the draft represents a good starting point, on further analysis of the legislation and the Guidance we have identified a number of areas where we consider that it could be amended to more closely reflect the intention of the legislation and more usefully be of assistance to firms looking to rely on it, in practice.

Yours sincerely



Adrian Hood

Regulatory and Financial Crime Expert

# Response to consultation

## DRAFT guidance for the new corporate criminal offence of failure to prevent fraud

### About the Investment Association

### The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 250 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £8.8 trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. 48% of this is for overseas clients. The UK asset management industry is the largest in Europe and the second largest globally.

### Chapter 1

It should be clear throughout the Guidance that ‘the offence’ only applies to 'relevant bodies' as defined in section 199(13) of the Act. As such, where, as in the second paragraph of part 1.1, it refers to an organisation, this should be amended to ‘a relevant body’, where this would be appropriate.

### Chapter 2

2.1

This section should make clear that the two ways in which the new corporate criminal offence can be committed, under s199(1) and s199(2) apply to different firms in different circumstances:

* The first sub-section applies to large organisations (LOs) where an associated person commits a base offence, which benefits the relevant body or someone to whom the associated person provides services on behalf of the relevant body.
* The second sub-section applies to relevant bodies of **any size**, as long as its parent undertaking is a LO. The second way of committing the corporate offence only applies where an **employee** (rather than an **associated person**) commits the base offence, and makes **no reference to the offence benefiting a client** of the entity, only to it benefiting the entity.

The reference in s199(3) supports, by implication, the assumption that the second way of committing the corporate offence cannot be committed where an employee’s fraud benefits a client.

These two separate ways of committing the offence should be made clear in the Guidance, including: the lack of reference to clients benefiting from the base offence in the second way of committing the corporate offence; and the difference between associated persons and only employees committing the base fraud offence.

This differentiation should also be carried through to part 2.5, as some firms need to be concerned about all associated persons, and acts benefiting clients, while other firms need only be concerned about the acts of employees and their acts benefiting the firm itself.

When the Guidance refers to subsidiaries, some consideration should be given to situations where a parent undertaking has only partial ownership of a subsidiary. While it is clear how the rules should apply where a parent undertaking owns 100% of a subsidiary, it is less clear when they only own 50%, or even only 10%. The Guidance should explain how complex groups should apply the new offence, including a situation where a subsidiary has multiple parent undertakings, some of whom fall within the scope of the offence, and others do not.

With respect to the first paragraph at the top of the next page, it would be helpful if the Guidance could give some clarification about how it would be decided which relevant body would be prosecuted, and where more than one could be, in a given situation. As the paragraph notes, ‘the subsidiary of a large organisation, which is not itself a large organisation, can be prosecuted rather than the parent’: how would it be decided whether to prosecute the subsidiary or the parent?

2.2

The Guidance refers, repeatedly and we believe incorrectly, to the s199(1) offence applying to situations where the associated person commits a fraud which benefits the subsidiary of a client of the firm. (cf part 2.5 and Figure 3)

This is despite s199(1)(b) being clear that the offence relates to associated persons committing a fraud which benefits ‘any person [to whom, or] **to whose subsidiary undertaking**, the associate provides services on behalf of the relevant body’. This is clear that it is the parent undertaking of the client that benefits, rather than the subsidiary of the client.

There is also the point that the relevant body is guilty of the corporate offence where the base fraud committed by its associated person benefits a client (etc) to whom they provide services. This does not cover the situation where an associated person commits the base fraud offence which benefits another client of the firm, to whom they do not, personally, provide services.

2.4

Where the Guidance states that ‘Companies within an organisation’s supply chain are not associated persons unless they are providing services on behalf of the relevant body’ it would be welcomed if it could expand on this, possibly giving a few examples of where firms in a supply chain might be providing services to the relevant body.

2.5

This section should clarify that the organisation or parent undertaking is **not** guilty of the corporate offence where the associated person did not **intend** that the undertaking benefit from their fraud, but that it did so inadvertently or unintentionally. S199(1) is clear that there needs to be an element of intent for the corporate offence to apply.

There are situations where an organisation can be both the victim of a base fraud offence committed by an employee or associated person and, to some extent, a beneficiary of it. As s199(3) is clear that a ‘relevant body is **not guilty of an offence** …if the body itself was, or was intended to be, a victim of the fraud offence’, the Guidance should be clear that where this unusual situation applies, being a victim of the base fraud offence means that the organisation is not guilty of the corporate offence, despite them also being a beneficiary of the base offence.

Figure 3 – As noted above, this figure shows the s199(1) offence applying to situations where the associated person commits a fraud which benefits the subsidiary of a client of the firm. It should, in line with s199(1)(b) show that it is the parent undertaking of the client that benefits.

Figure 4 – According to s199(2) both the parent undertaking, and the subsidiary which employs the individual committing the base fraud offence are relevant bodies. It is the subsidiary which is guilty of the corporate offence, but this is not clear from the diagram. S199(2)(a) is not entirely clear on which ‘relevant body’ (the parent undertaking or the subsidiary, or possibly either) is intended to benefit, although it is implied that it is the subsidiary that is the employer of the fraudster. It would be helpful if the Guidance could clarify this point.

2.6

The Guidance is currently unclear as to whether it is the associated person or the organisation that is based overseas. Or it could be that either, or both, could be based overseas. This section should be made more clear on this point.

Also, in which unusual circumstances would a UK-based organisation be liable for their overseas employees or subsidiaries in relation to a base fraud offence that takes place abroad (with no UK nexus)?

2.7

It may be helpful for the Guidance to include a piece on when the relevant body should conduct reviews of the risk assessment, and whether this should be periodic or triggered by external events. This could include a list of potential trigger events that could prompt a refresh of the risk assessment, outside the regular review cycle chosen by an organisation.

Examples

It would be helpful if the Guidance could include examples which are less straightforward. For instance, overseas activities which do benefit a UK parent undertaking, or indirect benefits to the relevant undertaking.

### Chapter 3

3.2

The first paragraph should include ‘the risk of employees, agents and other associated persons committing fraud which benefits the organisation or clients, or their parent undertaking, of the organisation to whom they provide services.’

The part on ‘Means’ should also include reference to any FCA reviews, reports or enforcement actions from which firms can learn valuable lessons.

3.5

If the second paragraph of the part on Whistleblowing is to be retained, or moved to an annex, then it should be reviewed, as several words or phrases seem to be missing from it.

### Chapter 4

The heading section is incorrect. It seems to relate to part 3.3.

### Glossary

The definition of ‘Relevant body’ given in the glossary seems too narrow. According to s199(13) it is any ‘body corporate or a partnership (wherever incorporated or formed)’. According to s199(2) a relevant body which is not a large organisation can commit the corporate offence, as long as it has a parent undertaking which is a large organisation.