

Title: Criminal Corporate Liability IA No: LAWCOM0078 RPC Reference No: Lead department or agency: Law Commission Other departments or agencies: Ministry of Justice	Impact Assessment (IA)			
	Date: 10/06/2022			
	Stage: Development/Options			
	Source of intervention: Domestic			
	Type of measure: Primary legislation			
	Contact for enquiries: Robert.kaye@lawcommission.gov.uk			
Summary: Intervention and Options				RPC Opinion: RPC Opinion Status

Cost of Preferred (or more likely) Option (in 2019 prices)			
Total Net Present Social Value	Business Net Present Value	Net cost to business per year	Business Impact Target Status
-£43.09 m	£m	£m	Qualifying provision
What is the problem under consideration? Why is government action or intervention necessary? In 2020 there were more than 5,000 convictions of “non-natural persons” which includes companies, charities and local authorities. Such organisations committed criminal offences ranging from regulatory offences to offences such as manslaughter or fraud. The law relating to corporate criminal liability does not appropriately capture and punish criminal offences committed by corporations, and their directors or senior management. Government intervention is required to ensure organisations of all sizes can be held to account, but must also not be overburdened by processes they are expected to follow.			

What are the policy objectives of the action or intervention and the intended effects? The overall policy objective is that corporate criminal liability ensures fair and proportionate liability is placed on companies for wrongdoing, committed by senior management and other employees. <ul style="list-style-type: none"> To ensure fair treatment between organisations of different sizes and scales of operation. To maintain the reputation of England and Wales for high standards of propriety and respect for the rule of law.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base) Option 0: Do nothing – retain the current identification doctrine; do not introduce any new failure to prevent offences. Option 1: Undertake all recommendations – reform of the identification doctrine; introduce a failure to prevent fraud offence. Option 2: Reform the identification doctrine and do not introduce a failure to prevent fraud offence. Option 3: Introduce a failure to prevent offence and do not reform the identification doctrine. Option 1 is preferred because it achieves the policy objective of improving effectiveness of the law with proportionate change (i.e. the identification doctrine has a smaller change than other rejected options, and only one new failure to prevent offence is implemented).
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Will the policy be reviewed? It will/will not be reviewed. If applicable, set review date: Month/Year				
Does implementation go beyond minimum EU requirements?			Yes / No / N/A	
Is this measure likely to impact on international trade and investment?			Yes / No	
Are any of these organisations in scope?		Micro Yes/No	Small Yes/No	Medium Yes/No
What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent)		Traded:		Non-traded:

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible SELECT SIGNATORY: _____ Date: _____

Summary: Analysis & Evidence

Policy Option 1

Description: Do all recommendations – reform of the identification doctrine; introduce a failure to prevent fraud offence.

FULL ECONOMIC ASSESSMENT

Price Base Year 2019	PV Base Year 2020	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate: -£43.09
COSTS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)	
Low	Optional	1	Optional	Optional	
High	Optional		Optional	Optiona	
Best Estimate	43.09		N/A	43.09	
Description and scale of key monetised costs by ‘main affected groups’ Transitional cost: Familiarisation cost [to businesses] - £43.09 ¹ million one-off roll-out to existing staff. Ongoing costs: increased number of prosecutions under the identification doctrine as it applies equally to firms with 10+ employees.					
Other key non-monetised costs by ‘main affected groups’ Transitional costs: Training to reinforce familiarisation on new fraud guidance [business]; new systems and procedures; large firms with 10+ employees most impacted through change to identification doctrine and micro firms likely to be more impacted by fraud prevention requirements; updated guidance / forms: Government provided and also internal to businesses. Ongoing costs: Training – fraud prevention awareness is assumed to be part of CPD.					
BENEFITS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)	
Low	Optional		Optional	Optional	
High	Optional		Optional	Optional	
Best Estimate	N/A		N/A	N/A	
Description and scale of key monetised benefits by ‘main affected groups’ Transitional benefits: None identified. On-going benefits: Reduced incidence of fraud loss – by way of illustrative example estimated at 1 percent of total fraud loss of £190 billion = £1.9 billion annually.					
Other key non-monetised benefits by ‘main affected groups’ Ongoing benefits: Increased detection of fraudulent conduct particularly within firms with 10+ employees following the reform of the identification doctrine; improved international reputation as the UK’s corporate criminal liability standards aligns with similar jurisdictions; and fairer legal system that now applies equally to firms with 10+ employees as it does to micro firms.					
Key assumptions/sensitivities/risks				Discount rate (%)	3.5
Assumptions: Firms adopt a similar approach to training as seen in the roll-out of the Bribery Act requiring staff to engage in CPD. There is a distinction between firms which have less than 10 employees, and those which have more than 10 employees. The firms most likely to have been affected by the identification doctrine are those with 10 employees or less. Risks: We have under/over-estimated the numbers within each category.					

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs:	Benefits:	Net:	

¹ Central estimate

Summary: Analysis & Evidence

Policy Option 2

Description: Reform the identification doctrine and do not introduce a failure to prevent fraud offence.

FULL ECONOMIC ASSESSMENT

Price Base Year 2019	PV Base Year 2020	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate: -17.62
COSTS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)	
Low	Optional	1	Optional	Optional	
High	Optional		Optional	Optional	
Best Estimate	17.62		N/A	17.62	
Description and scale of key monetised costs by ‘main affected groups’ Transitional cost: Familiarisation cost [to businesses] - £17.62 million ² one-off roll out to existing staff. Ongoing costs: increased number of prosecutions under the identification doctrine as it applies to firms with 10+ employees.					
Other key non-monetised costs by ‘main affected groups’ Transitional costs: Training to reinforce familiarisation on new fraud guidance [business]; new systems and procedures: large firms with 10+ employees most impacted through change to identification doctrine; updated guidance / forms: internal to businesses. Ongoing costs: Training – assumed part of CPD.					
BENEFITS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)	
Low	Optional		Optional	Optional	
High	Optional		Optional	Optional	
Best Estimate	N/A		N/A	N/A	
Description and scale of key monetised benefits by ‘main affected groups’ Transitional benefits: None identified.					
Other key non-monetised benefits by ‘main affected groups’ On-going benefits: Reduced incidence of fraud loss; Increased detection of fraudulent conduct particularly within firms with 10+ employees following the reform of the identification doctrine; improved international reputation as the UK’s corporate criminal liability standards aligns with similar jurisdictions; fairer legal system that now applies equally to firms with 10+ employees as it does to micro firms.					
Key assumptions/sensitivities/risks				Discount rate (%)	3.5
Assumptions: Firms adopt a similar approach to training as seen in the roll-out of the Bribery Act requiring staff to engage in CPD; there is a distinction between firms which have less than 10 employees, and those which have more than 10 employees. The firms most likely to have been affected by the identification doctrine are those with 10 employees or less. Risks: We have under/over-estimated the numbers within each category.					

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs:	Benefits:	Net:	

² Central estimate

Summary: Analysis & Evidence

Policy Option 3

Description: Do not reform the identification doctrine and introduce a failure to prevent fraud offence.

FULL ECONOMIC ASSESSMENT

Price Base Year 2019	PV Base Year 2020	Time Period Years	Net Benefit (Present Value (PV)) (£m)		
			Low: Optional	High: Optional	Best Estimate: -25.82

COSTS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	Optional		Optional	Optional
High	Optional		Optional	Optional
Best Estimate	25.82		N/A	25.82

Description and scale of key monetised costs by 'main affected groups'
 Transitional cost: Familiarisation cost [to businesses] - £25.82³ million one-off roll-out to existing staff.

Other key non-monetised costs by 'main affected groups'
 Transitional costs: Training to reinforce familiarisation on new fraud guidance [business]; new systems and procedures: micro firms likely to be more impacted by fraud prevention requirements [than firms with 10+ employees]; updated guidance / forms: Government provided and also internal to businesses.
 Ongoing costs: Training – Fraud prevention awareness assumed part of CPD.

BENEFITS (£m)	Total Transition (Constant Price) Years		Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low	Optional		Optional	Optional
High	Optional		Optional	Optional
Best Estimate	None		N/A	N/A

Description and scale of key monetised benefits by 'main affected groups'
 Transitional benefits: None identified.

Other key non-monetised benefits by 'main affected groups'
 On-going benefits: Improved international reputation as the UK's corporate criminal liability standards better aligns with similar jurisdictions; reduced incidence of fraud loss.

Key assumptions/sensitivities/risks	Discount rate (%)	3.5
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Assumptions: Firms adopt a similar approach to training as seen in the roll-out of the Bribery Act requiring staff to engage in CPD; there is a distinction between firms which have less than 10 employees, and those which have more than 10 employees. The firms most likely to have been affected by the identification doctrine are those with 10 employees or less.
 Risks: We have under/over-estimated the numbers within each category.

BUSINESS ASSESSMENT (Option 3)

Direct impact on business (Equivalent Annual) £m:			Score for Business Impact Target (qualifying provisions only) £m:
Costs:	Benefits:	Net:	

³ Central estimate

Evidence Base

Introduction

Concerns have been raised over the effectiveness of current laws in criminalising corporate entities when they commit economic crime. Calls for reform have been revived following the mixed success of recent high-profile prosecutions. Without action to reform this area of law, there is a risk that the UK will fall behind international standards in the prosecution of economic crime.

In 2017 the Ministry of Justice published a Call for Evidence on Corporate Liability for Economic Crime. The evidence submitted to the Call for Evidence was considered inconclusive by Government. There was no clear consensus from respondents on what corporate liability offence should be created if the identification doctrine was replaced. Equally, some responses disclosed significant opposition to reform while others questioned whether there was a need for further criminal sanctions at all in the already heavily regulated financial services sector.

In November 2020 the Government asked the Law Commission to draft an Options Paper. The terms of reference were:

To review the law relating to the criminal liability of non-natural persons, including companies and limited liability partnerships.

In particular, we were asked to consider whether the identification doctrine is fit for purpose, particularly when applied to organisations of differing sizes and scales of operation. Among the other issues we were asked to consider was whether an alternative approach to corporate liability for crimes could be provided in legislation.

These were agreed with the Ministry of Justice, the Home Office, HM Treasury, the Department for Business, Energy and Industrial Strategy, and the Attorney General's Office.

Background

A corporation has “a distinct legal entity from its owners, officers or members – a separate legal person.” As such, corporations can be subject to criminal and civil liability. In the year to September 2020, with caution for inaccuracies in the data, there were over 5,000 convictions of non-natural persons, representing around 0.6% of all convictions. Many of these are for strict or absolute liability offences, such as breaches of environmental or trading regulations, which are often created with corporations in mind. But companies can commit offences with fault elements, which typically have been created with natural persons in mind.

The general rule of criminal liability applied to corporations is the “identification doctrine”¹. This provides that a company will generally only be liable for the conduct of a person who had the status and authority to constitute the company's “directing mind and will”. There are exceptions to the application of this doctrine – for instance, in the case of offences of strict liability, the courts are generally content to invoke vicarious liability and to hold companies liable for the conduct of their employees and agents. The identification doctrine may be displaced by express words in a statute or by necessary implication.

We published our discussion paper considering relevant law as it relates to corporate criminal liability, the identification doctrine and options for reform in June 2021.² We received 45 responses to the consultation. During the consultation period we had extensive stakeholder engagement.

¹ This is alternatively referred to as the “identification principle”. In the options paper, we use the term “identification doctrine” to refer to the current prevailing mode of attribution in the criminal law of England and Wales, and the term “identification principle” to refer more generally to a mode of attribution based on identifying or more natural persons with the requisite fault. However, we have also retained the term “identification principle” in direct quotations where it is used to refer to the identification doctrine.

² Law Commission, “Corporate Criminal Liability: A discussion paper”, 9 June 2021.

Problems under consideration

Unfair treatment due to firm size

At present, the identification doctrine operates such that the actions of individual members of the company will only bind the company if the individuals acted with the requisite status and authority to do so. This means they must have sufficient status to be the directing mind and will, and they must have been authorised to do the conduct in question. This has different effects on small and large companies. For small companies, it is likely that the directors have oversight and control over all operations, and are answerable to each other rather than a higher level, such as a board of directors. Such directors are likely to have the status and authority to act on behalf of the company. However, large companies with diffuse decision-making powers, and a board of directors with oversight, is unlikely to have given the requisite authority to individuals. This is the principal argument against the current identification doctrine.

Minimal incentive for senior leadership of large companies to monitor employees to reduce risk of fraudulent conduct

There is minimal incentive for companies to proactively reduce the risk of their employees and agents committing fraud for their benefit. This is because the identification doctrine, the principal mechanism by which criminal liability is attributed to companies, does not attribute the acts and mental states of every employee or agent to the company. In practice this means that anyone who is not the “directing mind and will” or most senior members of the company, cannot bind it, and therefore the company is not liable if they commit offences. A new offence of failure to prevent fraud would mean that companies are liable for fraud committed by any employee or agent. There is a defence available for companies which have reasonable procedures in place to prevent the offending. This incentivises proactive risk-reduction policies and measures.

Reputational risk on the international platform

The UK’s position as an international financial centre is at risk of being undermined by falling behind corporate criminal liability standards. The UK’s reputation is at risk if the identification doctrine is perceived to be, as some argue it currently is, incapable of holding large and small companies to account for crimes committed by senior members. It is also at risk if we are perceived to not be tackling fraud committed by employees or agents within companies, for the benefit of the company.

Overcriminalisation of directors and managers

There is a risk of overcriminalisation of directors and managers. Where a company is convicted of a criminal offence, there are often statutory provisions allowing for the directors or managers of that company to also be criminally liable if they took part in or contributed to the offending. In some cases, directors can be liable where they neglected to prevent an action which led to the offending. The problem occurs where, in some cases, directors and managers can be liable for their neglecting to prevent the offence, where the company itself can only be convicted where it has a mental state such as intention or dishonesty. This means directors are at risk of being fixed with liability without a principled or justified basis for doing so.

There is potential for all sectors to be affected by this, because the range of offences for which the identification doctrine can be used for companies is very wide, as are the consent, connivance and neglect provisions, and as are the risks of fraud. Because of the focus on fraud, there is the potential for the financial sector to be affected more significantly, but not exclusively. This means there may be an increased risk in the financial sector that directors and managers are unfairly criminalised.

Therefore, we establish in the options paper that as a point of principle, the basis for liability for directors should match that of the company, which means removing the “neglect” basis where it is not present in the company offence.³

³ This means the mental element required to convict the company is the same as the mental element required to convict the directors or managers of that company.

Policy Objectives

The intended outcome is - the reform of corporate criminal liability to ensure fair and proportionate liability is placed on companies for wrongdoing, committed by senior management and other employees.

- To ensure fair treatment between organisations of different sizes and scales of operation.
- To maintain the reputation of England and Wales for high standards of propriety and respect for the rule of law.

Rationale for intervention

The conventional economic approach to Government intervention in order to resolve a problem is based on efficiency or equity arguments. The Government may consider intervening if there are strong enough failures in the way markets operate or in existing interventions. In both cases the proposed intervention should avoid creating a further set of disproportionate costs and distortions. The Government may also intervene for reasons of equity.

The principal-agent problem arises due to asymmetric information and is evident at several levels: the principal [shareholders] are unable to observe and monitor the actions of agents [managers] responsible for daily business activities. Managers may make decisions or pursue fraudulent actions for their own self-interest. By extension senior leadership may line manage staff who may also not act in keeping with company policy or engage in otherwise fraudulent conduct.

The greater the risk of punishment along with the type of expected punishment, the greater the disincentive to pursue fraudulent conduct. Punishment includes all formal and informal sanctions as well as the costs arising from litigation. Initiatives that effectively increase the range of firms likely to be prosecuted are likely to also increase the risk of detection. Currently small firms are most vulnerable to prosecution but the introduction of a reformed identification doctrine provides for greater reach to incorporate large firms. Large firms potentially face a significantly increased clearing rate as they are now pulled into a new category.

The financial cost of fraud has been conservatively estimated at about £190 billion annually with the private sector experiencing the greatest loss of around £140 billion. The incidence of fraud is often under-reported by firms themselves because of the reputational damage caused by adverse publicity.

In-house training to build staff awareness of fraudulent conduct and its consequences helps promote an explicit anti-fraud culture and with it the rise in informal sanctions which extends to the social stigma from colleagues, family and friends should an individual be caught engaging in fraudulent conduct.

Scale and scope

The law reform focus is on corporate fraud. This is because fraud, as the primary example of an economic crime, is one of the most likely types of crime to be committed either by, or for the benefit of, corporations. This is distinguished from, for example, sexual offences, which are unlikely to be committed with intention to benefit the company or a client of the company.

As at the 1st January 2021 there were 5.6 million private sector businesses⁴ most of which will be small and medium sized businesses⁵. Rather than focus on the entire business population it is most helpful to

⁴ Business Statistics – Research Briefing, Georgina Hutton and Matthew Ward, House of Commons Library, 21 December 2021.

⁵ Small [to include micro business] and medium sized business defined as employing 0-9, 10-249 employees respectively.

focus on VAT registered companies⁶ as these will have a greater degree of permanence and basic systems/procedures in place as against non-VAT registered businesses. See table 1 below.

Table 1: Number/Turnover of VAT and PAYE Enterprises, 2021

	Count	Employment	Turnover (£000's)
0-9 Micro	1,824,140	4,066,276	797,944,226
10-49 Small	187,900	3,651,722	663,887,183
50-249 Medium	34,570	3,375,632	976,190,693
250+ Large	7,640	10,621,314	3,162,319,917
Total	2,054,250	21,714,944	5,600,342,019

Source: ONS request

In particular, proposed law reform will apply to those businesses that have employees. See table 2 below.

Table 2: VAT and PAYE enterprises with 1-9 employees, 2021

Count	1,812,925
Employment	4,062,346
Turnover	£782,230,321

Fraudulent activity

Fraud is often under-reported due to the reputational risk it carries for firms and individuals. An often-quoted figure makes reference to the 2017 Annual Fraud indicator that estimates fraud losses to the UK at around £190 billion. The private sector suffers disproportionately higher losses at about £140 billion.

Fraud is captured and reported by different reporting bodies. For example the National Fraud Intelligence Bureau [NFIB] records and collects fraud offences reported to the police from Action Fraud and two industry bodies, Cifas and UK Finance. The public-facing national fraud and cybercrime reporting centre, Action Fraud, reported a 15% rise in fraud offences compared to the previous year ending December 2020. Likewise there was a 29 percent and a 12 percent increase in financial investment fraud and advance fee payments respectively.

According to the telephone operated Crime Survey for England and Wales [TCSEW] recording victims' experience, there were 5.2 million fraud offences representing a 41% increase in fraud offences in the year ending 2021 relative to the previous two years.

Current legal Procedure

Investigating and prosecuting companies using the identification doctrine

The prosecuting authorities can investigate and prosecute corporations for offences using the identification doctrine. This is typically the Police, CPS and the SFO but this can also be done by agencies including HMRC, DWP, DHSC, and the NCA.

The identification doctrine applies to most criminal offences – including fraud, for example. The offences for which a company can be criminally liable can be categorised as follows – violent and sexual offences; environmental offences, trading standards and other strict liability offences; and economic offences, specifically fraud. Only the third category of offences will be affected by our option to reform the identification doctrine. This is because in reality, companies are not prosecuted for violent and sexual

⁶ Companies with an annual turnover in excess of £85,000 must register to pay VAT.

offences, and strict liability offences do not rely on the identification doctrine. Therefore, when considering the changes the option will affect to the current prosecutions of companies, only economic offences are relevant.

See below for the numbers of current cases which indicate how many companies are dealt with each year for offences of fraud and other relevant categories.

Investigating and prosecuting companies for existing failure to prevent offences

The offence of failure to prevent the facilitation of tax evasion is investigated by HMRC, and prosecuted by the CPS. The foreign tax offence will be investigated by the SFO or NCA and prosecutions will be brought by either the SFO or CPS.⁷ As of 27 May 2021, HMRC had 14 live investigations of corporations for the corporate criminal offences in the Criminal Finances Act 2017, and a further 14 live opportunities which were being reviewed.

The offence of failure to prevent bribery requires the personal consent of the DPP or the Director of the SFO.⁸ To date, there have been six deferred prosecution agreements entered into between the SFO and companies for the offence (sometimes in conjunction with other offences).⁹

Our option is to introduce another failure to prevent offence, relating to fraud. At present, companies can be convicted of fraud but only under the identification doctrine. This offence would constitute a widening of the liability basis for companies for fraud.

Number of Cases

We are considering cases against companies in the categories relevant to the changes affected by our options. As above, our options – reform of the identification doctrine and implementation of a failure to prevent fraud offence - will only affect offences broadly categorised as economic crimes, primarily fraud.

There are relatively few prosecutions of corporations, compared with prosecutions of individuals, for economic crimes. As such, we anticipate that these options will have a minimal impact on the number of corporate prosecutions. We do not anticipate the options will give rise to significant numbers of corporate prosecutions.

As an example of the current case rates against corporations, in 2020 8 corporations were found guilty of fraud offences and 7 were found guilty of forgery offences.¹⁰

Crown Court and Magistrates' Courts hearing time and costs

Both the Crown Court and Magistrates' Court have 5 hour long sitting days where the average cost of judicial and staff salaries is indicated in table 9 below.¹¹

Table 3: Crown Court and Magistrates' Court average staff and judicial cost per sitting day [5 hours]

	Crown Court	Magistrates' Court
Judicial	£981	£130
Non-judicial	£541	£981
Total	£1,522	£1,111
Upated 2020/2021 cost	£1794	£1309

⁷ HMRC, Tackling tax evasion: Government guidance for the corporate offence of failure to prevent the criminal facilitation of tax evasion, 2017.

⁸ Bribery Act 2010, section 10.

⁹ Deferred prosecutions agreements for the offence of failure to prevent bribery were agreed with Standard Bank Plc, Sarclad Ltd, Rolls-Royce Plc, Guralp Systems Ltd, Airbus, and Airline Services Ltd.

¹⁰ Ministry of Justice, Criminal Justice System Statistics publication: Outcomes by offence 2010-2020.

¹¹ Her Majesty's Courts and Tribunal Services Annual Report and Accounts 2013-14 (24 June 2014), page 7.

Hourly cost ¹²	£359	£262
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The average [median] hearing time for Crown Court cases with a guilty plea [70 percent of cases] was 1.2 hours¹³ and 7.2 hours for a not guilty plea. Data for the Magistrates' Court is not available in such granularity.¹⁴

We do not anticipate that the options will result in differences in hearing times for individuals and corporations. This is compounded by the fact that corporations do not qualify for legal aid.

Main stakeholders

- All enterprises with employees, in particular large firms which will be newly caught by an expanded identification doctrine.
- Senior managers and other staff of affected enterprises.
- Prosecution agencies, such as the CPS and the SFO.
- HM Courts and Tribunal Service.
- Lawyers and legal academics.

Option description

This impact assessment compares Option 1 against the do nothing [option 0]:

- Option 0 – Do nothing. Under this option the problems outlined above would persist;
- Option 1 – (preferred): Reform of the identification doctrine and introduce a new offence of failure to prevent fraud.
- Option 2 – Reform the identification doctrine and do not introduce a failure to prevent fraud offence.
- Option 3 – Introduce a failure to prevent fraud offence and do not reform the identification doctrine.

Option 0: Do Nothing

Current law	Problems caused
Identification doctrine	
The identification doctrine is the mechanism by which liability for criminal offences is attributed to companies. It applies a test, the “directing mind and will” test, which attributes the actions and mental states of those with the status and authority to act on behalf of the company, to the company such that the company can be said to	<ul style="list-style-type: none"> • It has been said that it is, in general terms, difficult to attribute liability to large companies with diffuse decision making structures. For example, in <i>Barclays</i>, the CEO acted on delegated authority in negotiations from the Board of Directors, so when committing an offence the CEO

¹² Rounded to nearest £10.

¹³ Ministry of Justice, Criminal court statistics quarterly, England and Wales, January to March 2020, page 9.

¹⁴ We rely on anecdotal evidence and an early activity-based exercise of the average length of a prosecution in Magistrates' court of about 20 minutes.

have committed that offence. This typically applies to offences which require a fault element (i.e. intention or dishonesty), rather than those of strict or absolute liability.	<p>did not have sufficient status and authority to be the directing mind and will, because that was reserved for the Board of Directors. It has been said that it is counterintuitive for the CEO to not be recognised as having authority to make decisions and take actions, and have a mental state, which binds the company.</p> <ul style="list-style-type: none"> • This is a particular problem in large companies – in micro companies, typically there will be directors with responsibility for and oversight of everything in the company, so they are more likely to have the requisite mental state for an offence to bind the company. • This means, in effect, that it is easier to convict large companies than micro companies, which is an unfairness in the operation of the doctrine.
Failure to prevent fraud	
At present, there are failure to prevent offences for bribery and the facilitation of tax evasion, but not for fraud. Fraud encapsulates a range of offences and can be committed in a variety of situations, meaning it can be committed within and with many companies. Liability of companies for fraud at present is fixed by the identification doctrine. There have been calls to introduce a failure to prevent fraud offence, which would effectively place a positive duty on companies to introduce procedures to prevent employees from committing fraud in certain circumstances (where the employees act with an intention to benefit the company).	<ul style="list-style-type: none"> • There are companies whose employees (other than those who are so senior they are the directing mind and will) commit fraud, with an intention to benefit the company, who are able to escape liability on the basis that the employees were not senior enough to satisfy the identification doctrine. This means companies can benefit from wrongdoing without liability. The individuals can be held liable of fraud offences, but the company which received a benefit will not.

Option 1 – Undertake all recommendations – reform of the identification doctrine; introduce a failure to prevent fraud offence.

This is not an exhaustive list of all our recommendations but covers those likely to be of particular public interest as well as those with significant costs and/or savings.

The options would be:

1. Reform of the identification doctrine, which is the primary way of attributing criminal liability to corporations. At present the doctrine is that the “directing mind and will” of the company can bind it with its mental state and actions, meaning the company can be said to have committed the offence committed by the person or people who constitute its directing mind and will. The two options to reform the identification doctrine are to expand it from this test to a “senior management” model, which means any senior managers can bind the company. The alternative second of these two options is to expand the doctrine to “senior management”, with the addition of the chief executive officer and the chief financial officer being named persons whose actions will bind the company.
2. Introducing a failure to prevent fraud offence. This would be committed where employees or agents (referred to as associated persons) of a company commit a fraud offence, with intention to benefit the company. There would be a defence of “reasonable procedures”, which means that if the company had procedures deemed reasonable, with reference to guidance, designed to prevent employees committing fraud, the company is not guilty of the failure to prevent offence.

Further options included in Option 1 which do not require an impact assessment:

3. Removing “neglect” from “consent, connivance or neglect” provisions where the base offence for the corporation has a mental element requirement, such as intention or dishonesty. This is an option recommended to provide a justified basis of liability for directors and managers. It is not thought at present that there would be a significant impact on costs or benefit.
4. Attributing negligence to a corporation for offences of negligence without an individual who is personally negligent. This is not thought to engage the need for an impact assessment.
5. In the alternative, the suite of civil measures are options – an administrative monetary penalty regime, new powers for civil actions in the High Court, and reporting obligations akin to the Modern Slavery Act 2015 or the Companies Act 2006. These are options which are presented as alternatives to the reform of the identification doctrine and the failure to prevent fraud offence. As such, more analysis is required before an impact assessment can be undertaken on these options.

Option 2 – Reform the identification doctrine [not introduce a failure to prevent offence].

1. Retaining the current identification doctrine. This will be retained as the directing mind and will test.
2. Introducing a failure to prevent fraud offence, as described in Option 1.

Option 3 – Introduce a failure to prevent fraud offence [not reform of the identification doctrine].

1. Reform of the identification doctrine, as described above in Option 1.
2. Not introducing a failure to prevent fraud offence.

Public Consultation Exercise

We held a series of consultation events over the three-month consultation period involving stakeholders from a wide range of sectors. We received 45 written responses. We received responses from a range of sectors – government departments with prosecutorial powers, representatives of businesses and financial institutions, lawyers, academics and anti-corruption organisations. There was a clear majority who opposed two of the options – attributing fault to corporations on the basis of their corporate culture, and on the basis of vicarious liability for the acts of their employees. On the remaining options there was a divide in responses. Typically, although not exclusively, the organisations and lawyers representing businesses and financial institutions tended to be more conservative in their approach to corporate criminal liability, and director liability, than the anti-corruption organisations, who tended to advocate for wider bases of liability and more significant reforms. There was no broad agreement on the suitability of the remaining options, which includes the identification doctrine remaining the same or being widened to senior managers, more failure to prevent offences, civil mechanisms, director liability and sentencing of corporations.

Monetised costs and benefits of each option

This Impact Assessment identifies monetised and non-monetised impacts on individuals, groups and businesses with the aim of understanding what the overall impact to society might be from implementing these options. The costs and benefits of the proposed scheme are compared to the “do nothing” option.

Impact Assessments place a strong emphasis on valuing the costs and benefits in monetary terms (including estimating the value of goods and services that are not traded). When calculating the net present social value¹⁵ [NPSV] we use a time frame of ten years, with the present being year 0. We assume the transitional costs and benefits occur in year 0, the current year, unless otherwise indicated. Ongoing costs and benefits accrue in years 1 to 10. We would normally apply a discount rate of 3.5%, in accordance with HM Treasury guidance.

For the purposes of this impact assessment, as we seek to assess the implications of the identification doctrine and the failure to prevent offences, we distinguish between micro firms (with up to 10 employees) and large firms (with more than 10 employees).¹⁶

Option 0: Do nothing [base case]

Because the “do nothing” option is compared against itself its costs and benefits are necessarily zero, as is its NPSV.

Option 1: Do all recommendations – reform of the identification doctrine; introduce a failure to prevent fraud offence

Costs

Transitional Costs

Familiarisation costs

Some familiarisation costs are likely as new guidance documents are produced detailing the roles and responsibilities across a range of users. Small firms have historically been disproportionately penalised by corporate liability because of clearer lines of responsibility/ownership compared to larger undertakings. Under the current review large firms are more likely to be impacted.

All staff will need to be familiar with the legislation but with differential degrees of in-depth awareness depending on job role. Table 4 below sets out additional reading times using readingsoft.com as a reference point. This provides an estimate of the time investment required to understand new requirements.

Table 4: Typical reading profile¹⁷

Screen	Paper	Comprehension	Reader profile
100 wpm	110 wpm	50%	Insufficient
200 wpm	240 wpm	60%	Average reader
300 wpm	400 wpm	80%	Good reader
700 wpm	1000 wpm	85%	Excellent reader

Source: readingsoft.com

Based on the above an estimate of additional familiarisation cost is indicated in table 5 below.

Table 5: Familiarisation costs of all England and Wales businesses¹⁸

¹⁵ Costs to society are given a negative value and benefits a positive value. After adjusting for inflation and discounting, costs and benefits can be added together to calculate the Net Present Social Value (NPSV) for each option. See HMT Green Book at https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/685903/The_Green_Book.pdf#page=1&zoom=auto,-47,842, p 21.

¹⁶ We received anecdotal evidence that typically, the smaller the firm, the more likely to be convicted under the identification doctrine.

¹⁷ A typical page will have 350 words including white space and sub-headings.

¹⁸ Based on labour costs of managers/proprietors plus an uplift of 18% for non-wage costs. See ONS ASHE

<https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/occupation4digitsoc2010ashtable14>.

	Low estimate	Central estimate	High estimate
Micro firm cost	£6.16 million	£8.54 million	£12.33 million
Firms with 10+ employees	£24.93 million	£34.55 million	£49.91 million
Total cost	£31.09 million	£43.09 million	£62.25 million

Assumptions:

- One-time costs impacting on all businesses.
- All staff are required to familiarise themselves with the guidance.
- Of the 40 – 60 additional pages of guidance most staff will read only ‘core’ guidance as follows:
 - Low scenario – 98% of staff read core material and 2% read all guidance.
 - Central scenario – 95% of staff read core material and 5% read all guidance.
 - High scenario – 90% of staff read core guidance and 10% read all guidance.
- Core guidance consists of 10% of all guidance.

Training

It is anticipated that all staff will require training in order to ensure awareness of legislative responsibilities. As is the case with similar legislation under the Bribery Act for example, such training is most likely to be online as part of the package of mandatory training all staff must undertake with regularity in order to maintain awareness. Such training is typically part of the time allocated to continuing personal development. It is not expected to be so onerous as to extract an additional cost.

New systems and procedures

The identification doctrine reform

It is anticipated that generally, large businesses will require more time and expense to implement new systems and procedures than micro businesses. This is because, typically, more large businesses would be caught by the reformed identification doctrine than were caught under the existing identification doctrine (one of the criticisms of which was that it failed to attribute criminal conduct to companies such that it was difficult to prosecute them). By contrast, small businesses are at present more likely to be convicted using the identification doctrine, and this is not expected to change. Therefore, for large businesses it is expected that they will require new systems to be developed for their senior management in particular.

The new failure to prevent fraud offence

It is anticipated that large and small businesses will require new procedures in line with the new failure to prevent fraud offence. In particular, they will in effect be required to implement reasonable procedures in line with any Government guidance so that if an employee or agent commits fraud, they can avail themselves of the defence. It is also anticipated that small, particularly micro, companies may be affected more than large companies. In some cases, large companies, or companies with more than ten employees, will already have procedures in place to counter bribery and, in some sectors, the facilitation of tax evasion. It may be more common that small companies not as exposed to these particular risks, will not have had procedures in place. However, what is considered reasonable is likely to be less onerous than what is considered reasonable for a large company.

Fraud, however, describes a category of offending which is more common, and which can be committed in a broader range of circumstances. Businesses which were not particularly exposed to bribery or facilitation of tax evasion risks, but which are exposed to fraud risks, may be small companies. Essentially, the fact that fraud can be committed in virtually any circumstance will mean that the majority of companies will need to devise and implement procedures to protect against the offence of failure to prevent fraud.

Updated guidance/forms

New offence of failure to prevent fraud

Introducing a failure to prevent fraud offence will require the Government to issue guidance to companies on the reasonable procedures defence. This can mirror the Government guidance on the failure to prevent bribery¹⁹ and the facilitation of tax evasion²⁰ offences.

By way of example, the guidance for the failure to prevent bribery offence is 45 pages and provides guidance in the form of six principles rooted in a risk-based approach. It includes, for example, guidance on the proportionality of procedures needed depending on the risk exposure of the business to bribery. The facilitation of tax evasion offence guidance is similar in length and bases the guidance around the same six principles – proportionality of procedures, top-level commitment, risk assessment, due diligence, communication and training, and monitoring and review.

Ongoing Costs

Increased number of prosecutions and appeals

The identification doctrine

Increased prosecutions and appeals are anticipated for the reform to the identification doctrine, as large firms now face the increased potential for prosecution. It is anticipated that some large firms would plead not guilty, and would appeal the decision if appropriate, because the term “senior management” has some flexibility and could be defined with reference to specific facts. It is not anticipated that trials and appeals would increase significantly in number, but any test cases may require significant time and money. The prosecutions of corporations for economic crimes currently are low, and as such we do not expect significant increases in prosecution numbers.

Failure to prevent fraud

It is not anticipated that there will be an increased number of prosecutions and appeals in relation to this new offence. With the help of Government guidance, in most cases it will be clear to companies whether or not the offence has been committed. It will likely be clear whether the fraud offence has been committed by the employee or agent. Importantly, it will be clear whether or not the company can use the reasonable procedures defence, because it can evaluate them against the Government guidance. Therefore, it is thought that a company will be able to decide at an early stage whether they have committed the offence or not, and, if so, will be able to plead guilty. The prosecutions of corporations for failure to prevent bribery and the facilitation of tax evasion are low, and as such we do not expect significant increases in prosecution numbers.

Benefits

Transitional benefits

¹⁹ Ministry of Justice, The Bribery Act 2010: Guidance, March 2011.

²⁰ Hm Revenue and Customs, Tackling tax evasion: Government guidance for the corporate offences of failure to prevent the criminal facilitation of tax evasion, September 2017.

None identified.

Ongoing benefits

Reduced incidence of fraud losses

The 2017 Annual Fraud Indicator estimated fraud losses to the UK at about £190 billion annually. Initiatives aimed at the prevention of fraud alongside reform of the identification doctrine have the potential to reduce the incidence of fraud through disincentives delivered through the increased likelihood of punishment. In particular the identification doctrine increases the likelihood of large firms being prosecuted with much bigger turnover values and potentially far more significant fraudulent activities.

By way of illustrative example, a 1 percent reduction in fraud losses is equivalent to some £1.9 billion. This is a conservative estimate if one considers the combined turnover of firms with 10+ employees accounts for about 86 percent [£4.8 billion] of total turnover value.

Increased detection of fraudulent conduct

Reform of the identification doctrine brings large organisations into the sphere of those corporations that can be successfully prosecuted. This enables the potential for increased compensation to be paid out to victims of fraud.

The preventative effect of the failure to prevent offence is such that the defence of reasonable procedures incentivises firms to put in place procedures to detect and prevent fraud taking place.

Deterrent effect

There is likely to be a deterrent effect from prosecutions brought using the reformed identification doctrine. The significance of the deterrent effect will be determined by the size of the company convicted; the bigger the company, and importantly the greater its turnover, the greater the deterrent is likely to be. This may be compounded by more coverage of the prosecution.

The deterrent effect of the failure to prevent fraud offence is likely to stem from prosecutions of companies which do not have reasonable procedures in place to prevent the offending. The significance of the deterrent effect may depend on the number of successful prosecutions.

Improved international reputation

The UK's corporate criminal liability standards maintains parity with similar jurisdictions' position as capable of holding large and small companies to account for crimes committed by senior members. The identification doctrine introduces a proportionate approach that applies to all firms and does not seek to over criminalise a group [micro firms] whilst others [large firms] might engage in similar actions but avoid the reach of the law. As small firms demonstrate an increasingly innovative capacity the UK has demonstrated its leadership abilities in keeping abreast of relevant law that supports firm growth and development.

Fairer legal system

Reform of the identification doctrine now makes it possible to attribute liability to large companies with diffuse decision-making structures. Senior management will be recognised as potentially having sufficient status and authority to make decisions and take actions, and have a mental state, which binds the company. Previously small and micro firms were at a disadvantage as they will have directors with responsibility for and oversight of everything in the company, so they are more likely to have the requisite acts and mental state for an offence to bind the company. On this basis it was easier to convict large companies than small companies, which is an unfairness in the operation of the doctrine.

Option 2: Reform the identification doctrine and not introduce a failure to prevent fraud offence.

Transitional costs

Business familiarisation

Table 6: Familiarisation costs of all England and Wales businesses²¹

	Low estimate	Central estimate	High estimate
Small firm cost	£0.18 million	£0.34 million	£0.62 million
Firms with 10+ employees	£12.47 million	£17.28 million	£24.96 million
Total cost	£12.65 million	£17.62 million	£25.57 million

Assumptions:

Primarily larger firms with 10+ employees are impacted. Firms with smaller staff numbers [micro] had previously been most vulnerable to prosecution and as a result are far more aware.

- 3-5 percent of micro firms Option 1 familiarisation costs, 4 percent for central estimate +/- 1 percent for low/high estimates
- 50 percent of firms with 10+ Option 1 employees familiarisation costs.

Training

All staff will require training in order to ensure awareness of legislative responsibilities. As is the case with similar legislation under the Bribery Act for example, such training is most likely to be online as part of the package of mandatory training all staff must undertake with regularity in order to maintain awareness. Such training is typically part of the time allocated to continuing personal development. It is not expected to be so onerous as to extract an additional cost.

New systems and procedures

It is anticipated that generally, large businesses will require more time and expense to implement new systems and procedures than small businesses. This is because, typically, more large businesses would be caught by the reformed identification doctrine than were caught under the existing identification doctrine (one of the criticisms of which was that it failed to attribute criminal conduct to companies such that it was difficult to prosecute them). By contrast, small businesses are at present more likely to be convicted using the identification doctrine, and this is not expected to change. Therefore, for large businesses it is expected that they will require new systems to be developed for their senior management in particular.

Ongoing costs

Increased number of prosecutions

More large businesses would be caught by the reformed identification doctrine than were caught under the existing identification doctrine (one of the criticisms of which was that it failed to attribute criminal

²¹ Based on labour costs of managers/proprietors plus an uplift of 18% for non-wage costs. See ONS ASHE <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/occupation4digitsoc2010ashtable14>.

conduct to companies such that it was difficult to prosecute them). By contrast, small businesses are at present more likely to be convicted using the identification doctrine, and this is not expected to change.

Benefits

Ongoing benefits

Reduced fraud losses

The potential for reduced fraud losses is likely to be less significant because the reform of the identification doctrine would not capture fraud by lower level employees.

All the following areas of benefit [and the accompanying narrative] listed under option 1 remain relevant here:

Increased detection of fraudulent conduct
Improved international reputation
Fairer legal system

Option 3: Do not reform the identification doctrine and introduce a failure to prevent fraud offence.

The costs and benefits identified under option 1 as it applies to the prevention of fraud are as follows:

Transitional costs

Business familiarisation

Table 7: Familiarisation costs of all England and Wales businesses²²

	Low estimate	Central estimate	High estimate
Micro firm cost	£6.16 million	£8.54 million	£12.33 million
Firms with 10+ employees	£12.47 million	£17.28 million	£24.96 million
Total cost	£18.63 million	£25.82 million	£37.29 million

Assumptions:

- Synergies created from implementing both offences are lost when offences are separated. Marginally higher costs expected.
- Micro firms experience all [100 percent] Option 1 familiarisation costs,.
- 50 percent of firms with 10+ Option 1 employees familiarisation costs.

Training

As outlined under option 1.

New systems and procedures

It is anticipated that all businesses will require new procedures in line with the new failure to prevent fraud offence. In particular, they will in effect be required to implement reasonable procedures in line with

²² Based on labour costs of managers/proprietors plus an uplift of 18% for non-wage costs. See ONS ASHE <https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/datasets/occupation4digitsoc2010ashtable14>

any Government guidance so that if an employee or agent commits fraud, they can avail themselves of the defence. It is also anticipated that micro companies may be affected more than companies with 10+ employees. In some cases, large companies will already have procedures in place to counter bribery and, in some sectors, the facilitation of tax evasion. It may be more common that micro companies not as exposed to these particular risks, will not have had procedures in place. However, what is considered reasonable is likely to be less onerous than what is considered reasonable for a large company.

Fraud, however, describes a category of offending which is more common and which can be committed in a broader range of circumstances. Businesses which were not particularly exposed to bribery or facilitation of tax evasion risks, but which are exposed to fraud risks, may be small companies. Essentially, the fact that fraud can be committed in virtually any circumstance will mean that the majority of companies will need to devise and implement procedures to protect against the offence of failure to prevent fraud.

Updated guidance/forms

Introducing a failure to prevent fraud offence will require the Government to issue guidance to companies on the reasonable procedures defence. This can mirror the Government guidance on the failure to prevent bribery²³ and the facilitation of tax evasion²⁴ offences.

By way of example, the guidance for the failure to prevent bribery offence is 45 pages and provides guidance in the form of six principles rooted in a risk-based approach. It includes, for example, guidance on the proportionality of procedures needed depending on the risk exposure of the business to bribery. The facilitation of tax evasion offence guidance is similar in length and bases the guidance around the same six principles – proportionality of procedures, top-level commitment, risk assessment, due diligence, communication and training, and monitoring and review.

Benefits

Ongoing benefits

Reduced fraud losses

The largest impact on fraud is likely to come from the failure to prevent fraud offence because, unlike the identification doctrine reform, this would also deter and capture fraud by lower level employees.

Increased detection of fraudulent conduct

There is some potential for increased detection of fraud as staff awareness increases.

Wider impacts

- Equality impact assessment

We believe the recommendations set out in Option 1 will have no adverse impact in terms of the protected characteristics. On this basis we are not required to complete a full equality impact assessment.

- Justice impact assessment.

²³ Ministry of Justice, The Bribery Act 2010: Guidance, March 2011.

²⁴ Hm Revenue and Customs, Tackling tax evasion: Government guidance for the corporate offences of failure to prevent the criminal facilitation of tax evasion, September 2017.

The impact on the justice system of our proposals is considered throughout this impact assessment. In summary, as we detail above, we expect there to be negligible additional costs through the increased number of prosecutions.

- International trade assessment

Our recommendations are expected to have a positive impact on international competitiveness.