

Corporate
Criminal Offence:
Securing compliance
Minds made for empowering
financial services

February 2019

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Introduction

Securing long-term compliance with the requirements of the Criminal Finances Act 2017 means embedding the processes into business as usual.

30 September 2018 marked one year since the introduction of a new Corporate Criminal Offence (CCO) for any entity that fails to prevent the criminal facilitation of tax evasion.

With significant regulatory change and wider uncertainty in the market, some businesses have found carving out the necessary time and focus of delivering new compliance procedures a challenge. Many organizations in higher risk sectors, including financial services, have completed the risk assessment process and have begun implementing the required changes. For those who are yet to fully document their risk assessment, the immediate focus must be on completing that first step.

Once this has been completed, the key challenge is implementing change into business as usual and not just as one-off solutions or communications. One year on, businesses should assess whether they genuinely have reasonable prevention procedures in place to prevent the facilitation of tax evasion. They should also determine if these are sufficient to defend the business from inquiries from Her Majesty's Revenue and Customs (HMRC).

HMRC have already started to demonstrate initial signs of how they will assess compliance and have proposed inclusion of CCO compliance within the Business Risk Review process. Large businesses will be expected to evidence the steps they have taken to profile and manage their CCO risks. Those that are unable to do this will automatically be marked as high-risk with regards to tax governance.

This document gathers inputs from professionals across EY and considers the minimum standards along with evolving and best-in-class compliance activities for all organisations.



HMRC are developing new review methods to enforce CCO

- ▶ HMRC are currently piloting a new business risk review (BRR) process, which includes a specific requirement for large businesses to be able to evidence that they have taken steps to profile and manage their CCO risk.
- ▶ In practice, large businesses might need to ensure that they have documented their risk assessments, resultant action plans and their reasonable procedures more generally in order to be able to effectively demonstrate the approach that they have adopted to complying with the CCO legislation.
- ▶ Previously, businesses only ever needed to evidence their reasonable procedures if they faced the possibility of having to defend themselves against a prosecution.
- ▶ Under the proposed scoring mechanism, a business that is unable to evidence its approach to HMRC will automatically be marked as a high- risk business for tax governance. As such, businesses will struggle to secure a low risk rating with HMRC, increasing audit risk.
- ▶ Businesses which categorise themselves in industries which the CCO considers lower-risk, should document why they believe this to be the case. Failure to do so could impact their overall risk rating with HMRC, despite the lower risk rating.
- ▶ The BRR process is a periodic assessment by HMRC, performed every one to three years. With CCO featuring so prominently within the assessment criteria, it reinforces the need for businesses to regularly update their reasonable procedures, including their risk assessments, while continuing to demonstrate effective ongoing monitoring.

Next steps

HMRC's piloting of CCO in the new BRR process emphasizes that the standard of compliance is increasing. Minimum compliance may have been acceptable one year ago, however, HMRC now expects change to be embedded into business as usual and be sustainable.

Organizations that have not completed their risk assessments should do so as a matter of urgency.

Organizations that have completed their risk assessment but have not looked into any of HMRC's other guiding principles, should also consider this as a matter of urgency and swiftly implement any additional controls needed across their business and embed those controls into BAU in order to secure long-term compliance.

When planning and implementing prevention procedures that will stand up as reasonable

under legal scrutiny, it is vital for firms to consider:

- ▶ Each of HMRC's six principles in turn, and the related steps
- ▶ The existing controls they have in place to address these risks
- ▶ The need to enhance or improve these existing controls

Wherever possible, existing controls should be reused to address the risks raised by the new CCO. New controls should only be implemented when existing controls cannot be enhanced to address them.

The matrix on page 5 provides an overview of where different businesses are in their road to compliance.



Market observations

The matrix below looks at the minimum, evolving and best-in-class compliance activity EY has seen undertaken by medium inherent risk businesses, including those in the regulated sector.

Lower-risk businesses may not need to advance their control environment beyond the “evolving” stage, whilst higher risk businesses (or parts of the business) are likely to need additional controls to address specific risks identified as part of their risk assessment.

	Minimum	Evolving	Best in class
1. Risk assessment	Risk assessment complete for UK and affected non-UK business	Plan for future risk assessments in place, including 2018 updates if required.	Risk assessments integrated into ongoing framework.
2. Proportionality	Following the risk assessment businesses are expected to implement proportional enhancements across the other four guiding principles (below) and to controls to address residual risks identified.		
3. Top-level commitment	Communication of zero tolerance policy, combined with training	Accountable Executive appointed. Policies updated (inc. code of conduct, HR, contractors) and socialized	Accountable Executive has proportionate allocated resources to ensure ongoing compliance, clear scorecard and CCO role is aligned to their wider role
4. Due diligence	Communications with higher-risk Associated Persons	Adoption of due diligence standards for Associated Persons	Due diligence conducted on new third parties, controls executed for medium and high-risk third parties
5. Communication and training	Initial training pushed out to business. Code of conduct and culture changes made to business policies.	Materials available on intranet. Updates to whistleblowing and reporting processes.	Training implemented into yearly training requirements, targeted to risk, and included as mandatory training for new joiners.
6. Monitoring and control	Establishment of CCO as an ongoing program, with defined and measurable responsibilities across business and control functions.	Tax red flags list developed to help as a trigger point for escalation purposes. Management Information defined and regularly provided to Accountable Executive. Defined lines of defence model for CCO purposes.	CCO included within internal reviews for compliance and controls testing. Monitoring for evolving regulations and changes within the business that impact CCO.
For Regulated Businesses	Agreed roles and responsibilities between compliance (tax evasion) and CCO (facilitation).	Ad-hoc read across from KYC/AML to other tax risks, inc. CCO and tax reporting on a case by case basis (data pull)	Renewed focus on tax evasion as part of AML/KYC procedures, including client risk scoring, transaction monitoring, red flags and appropriate governance and escalation.

Recap of the main points of the legislation

Sections 45 and 46 of the 2017 Criminal Finances Act created a new corporate offense of failure to prevent the facilitation of tax evasion, which came into force on 30 September 2017. The new offense means a corporation can be held criminally liable if its employees, or anyone else providing services for it or on its behalf, assist a taxpayer in evading their tax liabilities. Penalties include unlimited fines.

1. The legislation includes a defense of having reasonable procedures in place to prevent the facilitation of tax evasion. This is similar to the “adequate procedures” defense in the Bribery Act.
2. The aim of the legislation is to create an environment that fosters corporate monitoring and self-reporting of criminal activity.
3. In most organizations, complying with the new legislation will require coordination between tax, financial crime, compliance and legal departments. It will also create new governance and control burdens.
4. Breaching the legislation is a criminal offense punishable by potentially unlimited fines. There is also likely to be significant reputational damage.

Extraterritorial scope expands the risks

In implementing their procedures, international groups with branches or representative offices in the UK should bear in mind the wide extraterritorial application of the offenses. Crucially, having a UK place of business means the entire company is in scope for offenses related to UK and non-UK taxes.

This extraterritorial scope brings significant risks that should be included in the risk assessment for the CCO. For example, if a customer walks into an office in France and convinces the person behind the counter to help them evade French taxes, the fact that the organization has a UK place of business means a prosecution could be brought in the UK.

Establishing reasonable prevention procedures

An organization could establish a defense against the CCO if it demonstrates that – at the time of the alleged offense – it had in place reasonable prevention procedures. This term refers to measures to prevent associated persons, such as employees and third parties providing services for or on behalf of the organization, from committing facilitation offenses.

A six-step process

Corporates looking to implement such measures should take six steps, as shown in the diagram below. These steps mirror the six principles set out in the HMRC guidance.

Step one: Risk assessment

The first step is a risk assessment that considers the inherent risks across the business, and the capacity of the existing control environment to mitigate those risks. This assessment will help to clarify the residual risks, and identify higher-risk areas where further prevention procedures are needed.

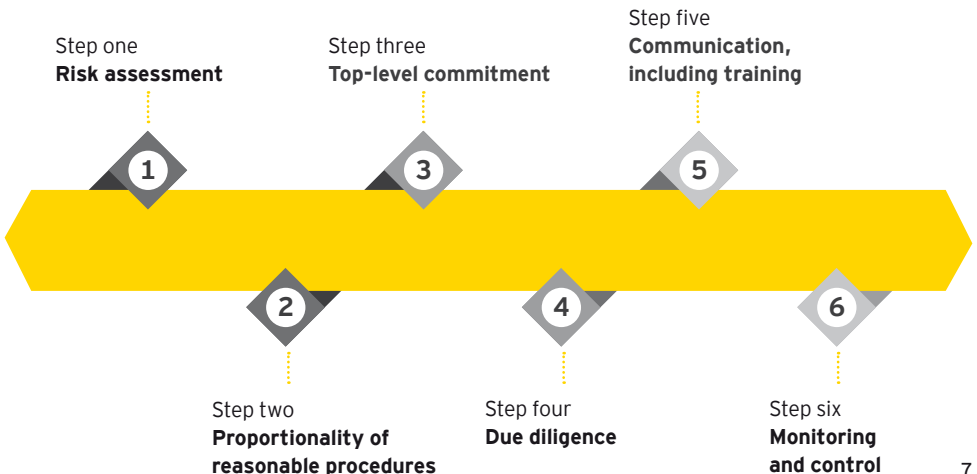
Steps two to six: Other reasonable procedures

Once the risk assessment has been completed, HMRC suggests organizations take five further steps to address residual risks:

- ▶ Proportionality of reasonable prevention procedures
- ▶ Top-level commitment
- ▶ Due diligence
- ▶ Communication, including training
- ▶ Monitoring and control

We will now take a closer look at the six steps below. Critically, all six must be embedded into business as usual (BAU) processes to maintain compliance. This is likely to require periodic reassessments of risk, either as stand-alone activity or as part of wider financial crime risk assessments. It is also likely to mean that procedures are put in place to monitor evolving industry practice, HMRC's expectations and the effectiveness of any reasonable procedures.

Figure 1: Six steps to establish reasonable prevention procedures



Risk assessment

Step one: Risk assessment

The initial risk assessment

As previously noted, the first step toward addressing the CCO is an assessment that looks at the inherent risks across the business. This helps identify any higher-risk areas requiring further prevention procedures, along with the existing control environment.

Assessments in subsequent years

Risk assessments are not a one-off exercise. Embedding the process into BAU will be essential for demonstrating reasonable procedures. Most organizations will already be undertaking financial crime, and anti-bribery and corruption risk assessments on either a continuous or periodic basis. Those reviews should be expanded to cover risks around facilitation of tax evasion.

In particular, organizations should ensure that:

- ▶ Risk assessments are reviewed periodically and updated in line with changing circumstances.
- ▶ There are procedures in place to identify emerging risks and feed these into the organization's risk assessment process.
- ▶ There is scope for risk assessments to be challenged internally.

Further investigations

While most organizations have probably completed their risk assessments for the CCO, they should carefully consider whether any further investigations may be needed. These usually come in two main types:

Deep-dive risk assessments



Particularly in cases where a lack of information or granularity has led to a conclusion that a business unit should be treated as a higher-risk one, a deep-dive assessment can enable better identification and quantification of the risk. Examples might include a global business unit with processes that vary in different locations.

Controls effectiveness testing



Many organizations have not conducted controls effectiveness testing specifically for the CCO, relying on their existing testing and management information. Instead, controls effectiveness should be approached as part of the longer-term implementation of CCO compliance, either comprising existing testing processes or on a stand-alone basis.

Proportionality

A CCO risk assessment checklist

Here are some key points to consider in evaluating CCO risk assessments and readiness checks

- Have you used a risk assessment process consistent with that set out in HMRC's guidance or documented why the approach taken is reasonable?
- Have you covered all the risks identified by HMRC in its guidance? If not, have you documented why the scope is reasonable?
- Have you documented how you have ensured that the risk assessment is complete and has addressed all areas of the business in scope for CCO risks?
- Have you addressed any extraterritorial effects of the rules, including the risk that other group companies or JVs might act as associated persons for a company that is in scope?
- Have you considered risks in the back office, including accounts payable, supplier and vendor management, HR, and group tax?

Step two: Proportionality of the risk-based prevention procedures

HMRC guidance says: "Reasonable procedures ... will be proportionate to the risk the relevant body faces of persons associated with it committing tax evasion facilitation offenses. This will depend on the nature, scale and complexity of the relevant body's activities."

This means any actions taken to address CCO risks should be appropriate in light of the nature, scale and complexity of the business, and the risk profile determined through the risk assessment. However, it is inevitable that many organizations will choose to be extra sure that they are

compliant by taking more prudent steps than those mandated by the risk assessment.

In deciding on the procedures to implement, organizations should take account of the fact that they already have a wide range of existing controls in place to manage risks across the business. Given this, they should take the time to identify and leverage existing controls and programs to address risks.

It is vital that the rationale for all decisions and steps taken to address the risks identified in the assessment are documented. This audit trail will be critical to its defense if the organization does find itself under investigation for alleged CCO breaches in the future.

Implementing the required changes

Step three: Top-level commitment

HMRC's guidance says: "The top-level management of a corporation is committed to preventing persons associated with the corporation from engaging in criminal facilitation of tax evasion. They foster a culture within the corporation in which activity to facilitate tax evasion is never acceptable."

To comply with this guidance, organizations will need to establish the right tone from the top, by ensuring that senior management sends a clear and consistent message to the whole business expressing that there is zero tolerance of the facilitation of tax evasion. They must also set the tone from the middle management by ensuring that on a day-to-day basis management is aware of, and follow the policies relating to the facilitation of tax evasion.

At the same time, a key aspect of establishing governance procedures is likely to be defining ownership and accountability within the senior management team. Unlike with financial crime, there is no specific requirement to make a specific individual within the organization accountable for risks around the facilitation of tax evasion. However, those that are at higher-risk are likely to appoint an individual with dedicated responsibility, to ensure on-going compliance.

As with other accountable persons, this individual will need to be supported with an appropriate level of resources to enable them to manage risks, policies and procedures, and to detect and address any risks embedded into business activities. The accountable person will probably be allocated responsibility for oversight of

CCO risks across the whole business, including support functions, management information, reporting mechanisms for suspicious activity, and regular reviews.

Step four: Due diligence

HMRC's guidance says: "The organization applies due diligence procedures, taking an appropriate and risk based approach, in respect of persons who perform or will perform services on behalf of the organization, in order to mitigate identified risks."

Organizations should be able to use their existing vendor management processes to comply with requirements relating to third parties. They can also make use of their existing infrastructure to establish a process for assessing the risks that third parties acting as associated persons could facilitate tax evasion, and for applying the necessary controls to all associated persons. These controls might include changes to contracts, restrictions on the types of activities that third parties can undertake and new approval processes.

For associated persons who present a relatively higher level of risk, appropriate controls could extend to a requirement for statements of compliance, together with additional checks and approvals, including a contractual right to review policies or audit procedures. In general, organizations should use their current risk management processes in this area as a starting point for determining what constitutes a reasonable approach for higher-risk relationships.

As the need for due diligence also applies to employees, organizations will already have many of the necessary controls in place. Appropriate checks may include background screening as well as contractual changes, including disciplinary procedures. Providing appropriate training – which we discuss further in step five below – will also be key. Annual statements of compliance may be appropriate for very high-risk groups. These are already used for other higher-risk relationships, so it may be possible to introduce them as a simple addition to existing procedures.

Step five: Communication, including training

HMRC's guidance says: "Internal communications should make clear the relevant body's zero tolerance policy for the facilitation of tax evasion by its representatives and the consequences for anyone found to be complicit in illegal activity" and "training should equip them (associated persons) to understand the scope of this offense and the associated risks, without needing to understand the underlying tax law."

All organizations are expected to provide their staff with communications and training on tax evasion facilitation risks. The training should be proportionate to the risks faced by individual employees, with more detailed training likely to be needed for higher-risk businesses, higher-risk staff, and targeted training for people in control functions who may need to review these procedures.

To support these communication and training interventions, an organization might provide its employees with details of the organization's approach to facilitation risk. This is in addition to implementing initiatives to reinforce the tone of zero-tolerance from the top and enable employees to understand and evaluate risks themselves. Further steps might include making updates to codes of conduct, employee handbooks, job descriptions and performance objectives.

As part of the training rollout, organizations will need to ensure that responsible senior management receives the level of training needed to oversee and manage risks effectively, and continue to communicate the right tone to employees and third parties. Organizations will also want to ensure there is appropriate communication with third parties – especially associated persons – about what the firm expects of them.



Developing training for staff

The purpose of training on tax evasion facilitation risks is not to make everyone in the organization an expert on tax or the Criminal Finances Act. Instead, training should be provided in clear and simple language and not overly focused on technical tax details. This will typically mean focusing on the dishonesty elements of the offenses.

The training should convey the key message that tax evasion and facilitation are broadly similar to fraud, and are characterized by dishonesty and concealment. At the same time, the focus on dishonesty needs to be carefully nuanced so it doesn't lead to "false positive" internal reporting because of a limited understanding of tax issues.

Other important elements may include interactive scenario-led training, providing staff with clear examples of what is and isn't evasion, and what they should do in different situations. Employees should also be given clear escalation routes as well as a final test to check their understanding and to help imprint the training in their memory.

Figure 2: A typical training program for employees presenting various levels of risk

Level	Training intervention	Potential audience	Description
0	Enhancements to existing training	At-risk staff in lower-risk areas	<ul style="list-style-type: none"> ▶ Enhance existing financial crime or AML training
1	CCO awareness e-briefing	Awareness raising for medium-risk staff	<ul style="list-style-type: none"> ▶ Provide a short e-briefing video that gives an overview of the key requirements relating to the CCO to address short-term concerns ▶ Visit bcove.me/jn5bov5y for a short demonstration video that was produced for a FATCA e-learning module
2	CCO operational and processes training	Higher-risk staff	<ul style="list-style-type: none"> ▶ Train staff on specific requirements covering operational, process and system needs ▶ Training being typically 20-30 minutes long, including an assessment to reinforce learning
3	Subject-matter expert training	Lines of defense and wider compliance teams	<ul style="list-style-type: none"> ▶ Designed to describe impacts per functional department ▶ Focusing on functional areas impacted by the new CCO, such as financial crime, or lines of business, such as wealth management
4	Senior management face-to-face briefings	Management and accountable executives	<ul style="list-style-type: none"> ▶ Brief senior management on an overview of the CCO, including its purpose and importance, and introduce key obligations and senior manager accountability

Step six: Monitoring and control


HMRC’s guidance says: “The organization will therefore need to change its procedures in response to the changes in the risk that it faces.”

Maintaining reasonable prevention procedures for the longer term will be a challenge for all organizations, and it is vital to recognize the risk that solid compliance on day one might gradually become inadequate over time. To minimize this risk, organizations should combine all the elements explained above with actions to embed compliance within BAU.

To lay the foundations, organizations should start by documenting the risks and related controls required across the business. It is likely that the

testing of controls will be covered by existing processes. However, the need to undertake ongoing monitoring of changes in the business, such as new client segments and jurisdictions or business areas will need to be adopted. This may trigger the need for a re-review of associated risk factors.

At the same time, organizations should establish monitoring and review processes for both facilitation risks and the effectiveness of the related controls, in order to check whether the controls are still proportionate to risks that have been identified or need to be enhanced. This should include monitoring for changes in market best practice as it evolves.



“Failure to prevent” offenses: the wider context

While the CCO defines a new offense of failing to prevent the facilitation of tax evasion, the UK Government’s approach in the legislation mirrors one that it adopted in the Bribery Act, setting a pattern for the future. Going forward, the CCO is also expected to share a number of characteristics and consequences of another new offense that may be introduced in 2018. This offense focuses on the failure to prevent economic crime.

The common features of both offenses are expected to include:

- ▶ Greater responsibility on businesses to prevent criminal activities undertaken on their behalf, including criminal liability if they fail to do so.
- ▶ A line of defense for businesses as to whether their preventative procedures are deemed sufficient in proportion to the risk.
- ▶ A global approach for many organizations as the legislation is international and wide-ranging.

As EY’s latest *UK Bribery Digest*¹ describes, the Bribery Act’s Section 7 corporate offense of “failure to prevent” is being cited in a growing number of cases. In some instances, this has resulted in the Serious Fraud Office handing down significant fines to offenders.

1. “UK Bribery Digest Edition 12”, March 2018, <https://www.ey.com/uk/en/services/assurance/fraud-investigation---dispute-services/ey-anti-bribery-and-corruption-uk-bribery-digest>

How EY can help

EY can help you achieve and maintain compliance with the legislation in four main ways:

1. Assess your current compliance model to prioritize compliance activities

EY can help you assess your existing CCO framework, identify gaps and help you embed a CCO compliance framework that can be used to evidence the organizations reasonable prevention procedures.

2. E-learning and e-assessment

EY teams can provide you with off-the-shelf and tailored e-learning and e-assessment modules that can be incorporated into your own training or provided as part of the EY tool.

3. Tax red flags library

EY can support in building a tailored tax red flags library for tax evasion and tax avoidance. Such a library will assist you and your associated persons identify tax evasion and tax avoidance.

4. Complete support from our multi-disciplinary teams

EY teams can provide end-to-end support for your compliance by leveraging tax, legal, financial crime, technology, training and implementation professionals. EY professionals support an independent view and through their extensive work will be able to benchmark you against your peers.

Why EY

If your organization faces the need to implement reasonable prevention procedures for the new CCO, there's good news: your existing controls already provide you with a solid foundation to build on. Reusing these lets you leverage prior investments and minimize costs and disruption, while managing your risks effectively and appropriately.

This is why EY teams look to utilize your existing control sets and only invest in new ones where completely necessary. Combined with the integrated multi-skilled EY teams, this approach has helped EY support risk assessments, implementation support and training for a large number of organizations, ranging from global banks private equity houses to football clubs, car manufacturers.

Contact us

The message is clear. The CCO is now a fact of life for your financial institution and completing your risk assessment under the new legislation is just the start. It's time to make the journey to embed compliance into BAU. EY can support you every step of the way.

For more information on how EY can help you tackle the challenges of the new CCO, please speak to a member of the EY CCO team or your usual EY contact.

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