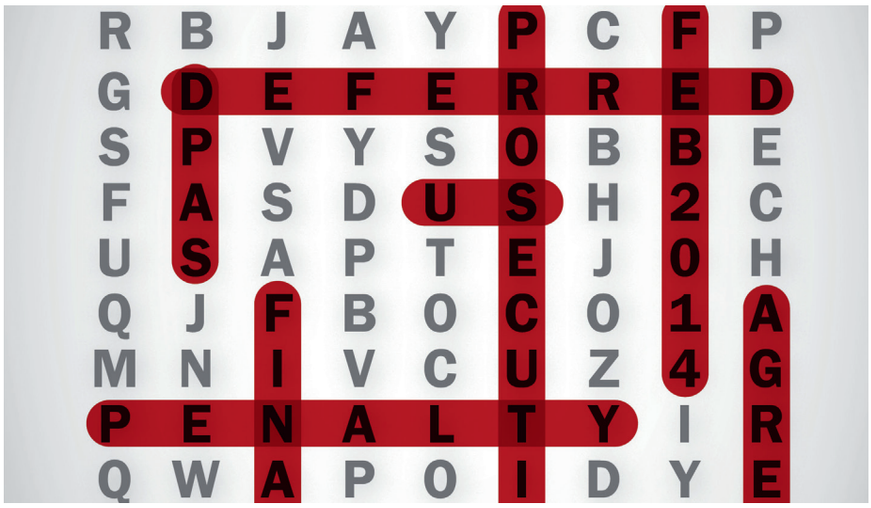
Time to agree terms?

Polly Dyer & HHJ Michael Hopmeier assess the role & impact of DPAs at home & abroad



IN BRIEF

- Section 45 of the Crime and Courts Act 2013 enacts Schedule 17, which provides for the introduction of Deferred Prosecution Agreements (DPAs), is expected to come into force in February 2014.
- DPAs will not be available for individuals, whether for individual crimes or for action untaken on behalf of an organisation.
- DPAs can be used in relation to conduct pre-dating the commencement of the legislation.
- Lessons learned from other jurisdictions.

The government's latest instrument in the fight against economic crime is the Deferred Prosecution Agreement (DPA). A DPA is a voluntary agreement between a prosecuting authority and a commercial organisation whereby, in return for complying with a range of stringent conditions including, eg the payment of a substantial financial penalty, requirements to make reparation to victims and participate in monitoring for a set period, the prosecutor will defer a criminal prosecution. If the required conditions are fulfilled, then the commercial organisation can reasonably expect that no prosecution will follow.

In the US, DPAs and Non-Prosecution Agreements have been in use for many years. According to an article from Norton Rose Fulbright, they have raised approximately £2.5bn a year in penalties. and are generally regarded as a beneficial enforcement mechanism, despite being dismised by detractors as offering an opportunity for corporations to avoid prosecution. With DPAs being introduced in to the UK next year the intention has been, as stated recently by Edward Garnier QC, the ex-Solicitor General, to take the idea from the US but "leave behind the worst bits".

Lessons from other jurisdictions

The case studies discussed below highlight the potential importance of co-operating outside the courtroom, both for the corporations concerned and for the prosecuting authorities.

HSBC

In December 2012, HSBC entered into a DPA with American prosecutors, which, according to media reports in *The Guardian* and BBC involved a record $1.9bn (£1.2bn) fine, to settle allegations it allowed terrorists and drug cartels to move money around the financial system after failing to implement anti-money laundering controls. The agreement included a five-year arrangement with the US Department of Justice under which the bank would install an independent monitor to assess reformed internal controls. It was also agreed that the bank's top executives would defer part of their bonuses for the the five-year period, while money issued in bonuses was reimbursed from a number of former and current executives.

While subject to stringent penalties and conditions, HSBC avoided criminal prosecution, a move that could have stopped the bank operating in the US. US authorities have defended their decision not to prosecute HSBC, highlighting the collateral consequences that could have resulted: had the US authorities decided to press criminal charges, according to *The Guardian*, HSBC would almost certainly have lost its banking licence in the US, putting thousands of jobs in jeopardy and the entire banking system could have been destabilised.

This case is one of the most recent in a succession in which a DPA has been utilised by USauthorities. In June 2012, the accounting firm BDO USA LLP agreed to a DPA: BDO admitted that it was part of a fraud that generated $6.5bn in phony tax losses but the agreement provided that if BDO continued to co-operate with a criminal investigation and met certain other conditions the tax fraud charge filed against the firm would be dismissed. As reported by *Forbes*, the firm agreed to pay $34.4m to the Internal Revenue Service as a civil penalty and forfeit $15.6m to the government. This settlement came nearly seven years after KPMG agreed to pay a $456m fine in a deferred prosecution agreement covering its role in tax shelter frauds and two years after Deutsche Bank agreed to pay $554m in a deferred prosecution deal.

Siemens

In 2008, US authorities fined the German engineering group Siemens $800m (c£523m) to settle a long-running bribery and corruption scandal. Siemens also agreed to pay a fine of €395m (c£354m) to settle a case in Munich, its home town, over the failure of its former board to fulfil its supervisory duties. As *The Guardian* reported, it was fined €201m in Germany in 2007 over alleged bribery by its former telecoms division. The US settlement, after a year of negotiations and plea bargaining, saw Siemens pay the US Department of Justice about $450m to settle charges of bribery and trying to falsify corporate books. The Securities and Exchange Commission, the market regulator, received another $350m on similar charges under the Foreign Corrupt Practices Act 1977.

When the problems first came to light, according to *The Guardian*, Siemens played down the affair as a matter of a few million euros. Within a month, this estimate had grown to €420m (c£350m). Key executives repeatedly denied awareness or involvement. This initial tack did little to protect, let alone enhance, stakeholders' impressions of its integrity and many viewed it as incompetent.

However, Siemens' full response has been widely praised by many independent anti-corruption and ethics experts, including the Organisation for Economic Co-operation and Development and US Federal

The DPA timeline

Following a consultation in 2012, the Ministry of Justice inserted a schedule 17 into the Crime and Courts Act 2013 (CCA 2013), which provides for the introduction of DPAs into UK law.

The Crime and Courts Act 2013 (CCA 2013) received Royal Assent on 25 April 2013. Section 45 enacts Schedule 17 to the Act. Schedule 17 is not yet in force but the date given in the Impact Assessment last July was early 2014. The Solicitor General, Oliver Heald, has confirmed in a speech to the C 5 7th Advanced Forum on Anti-Corruption in June that the government's aim is to implement DPAs in February 2014.

In June 2013, the Director of the Serious Fraud Office and the Director of Public Prosecutions published a draft Code of Practice explaining how they intend to use the new DPAs.

The consultation on this draft closes on Friday 20 September 2013 (www.sfo.gov.uk).

authorities. This involved appointing Michael Hershman, an anti-corruption expert and co-founder of Transparency International, to serve as its adviser. Siemens rolled out strict new rules and anti-corruption/compliance processes. It hired over 500 full-time compliance officers (up from just 86 in 2006), and a former Interpol official to head its new investigation unit. Siemens also announced it would avoid competing in certain known hotspots for corruption or unethical practice, such as Sudan. It also took the decision to voluntarily suspend its applications for funding from the World Bank for two years. Furthermore, the company agreed to a 15-year programme to pay $100m to non-profit organisations fighting corruption. Finally, the firm took over 900 internal disciplinary actions, including dismissals.

Overall, the scandal was said to have cost Siemens €2.5bn, including €2bn of fines. The firm was also barred from dealings with certain clients. The cost to employees of two years of shame under intense public scrutiny, especially in Germany, is difficult to calculate. However, the Siemens Group says its "extraordinary co-operation" in the US case meant that the US defence logistics agency, the leading body awarding federal contracts, has reaffirmed it as a "responsible" contractor and the settlement, after once fearing it would have to pay a penalty of up to $5bn, was seen as a personal coup for Peter Löscher, the Siemens Chief Executive. According to the late Joachim Vogel, in his lecture given to the European Criminal Law Association and Institute of Legal Studies on 26 June 2013, in November 2006, 23 prosecutors and 250 police officers were deployed to search the Siemens headquarters in Munich. Had the matter not been resolved, the cost of proceeding to trial would have been enormous.

The proposed UK model

In a UK DPA, under the Crime and Courts Act 2013 (CCA 2013), the agreement will be made between the Director of Public Prosecutions or the Director of the Serious Fraud Office (SFO) and a commercial organisation (companies, partnerships or unincorporated associations) in cases that can be classified as economic crime, in particular fraud, bribery and money laundering. In other jurisdictions such agreements cover all types of regulatory offences. The government had indicated in its May 2012 Consultation that it intended to review the list of qualifying offences and consider whether there is a case to broaden the range of economic crimes for which DPAs should be available, but this is not reflected in Part 2 of Schedule 17, where the offences to which DPAs are available are specified. Other financial or economic crimes may be added to the list by order of the Secretary of State. Primary legislation would be required to add any non-financial offences. The government's response to the consultation dated 23 October 2012 makes plain that it is keen to maintain flexibility but there are no current plans to extend DPAs to other types of crime.

> *"Respondents to the 2012 Consultation welcomed the proposals to create a new tool for prosecutors to tackle economic crime"*

Unlike in the US, DPAs will not be available for individuals, whether for individual crimes or for action untaken on behalf of an organisation. Given the current financial situation, it has been suggested, that it is not impossible to envisage DPAs eventually being extended to individuals as well. DPAs will be able to be used in relation to conduct pre-dating the commencement of the legislation (para 39, Sch 17, CCA 2013).

Under paragraph 5, schedule 17, CCA 2013, the terms and conditions of a DPA will be case specific. A DPA must contain a statement of facts and must specify an expiry date. A DPA may impose the following non-exhaustive conditions for a defendant to comply with:

a. to pay the prosecutor a financial penalty;
b. to compensate victims of the alleged offence;
c. to donate money to charity or other third party;
d. to disgorge any profits made from the offence;
e. to implement a compliance programme or make changes to an existing compliance programme;
f. to co-operate in any investigation;
g. to pay any reasonable costs to the prosecutor (any money received by the prosecutor in relation to a financial penalty or disgorgement of profits is to be paid into the Consolidated Fund).

DPAs will be shaped to each individual case and a DPA may impose a time limit within which compliance with the conditions must be fulfilled. It is to be noted in relation to (a) that on 27 June 2013 the Sentencing Council published draft sentencing guidelines for fraud, bribery and money laundering offences, including corporate penalties. The consultation in relation to these guidelines closes on 4 October 2013.

By virtue of paragraph 6(1) of Schedule 17, CCA 2013, the Director of Public Prosecutions and the Director of SFO published a draft DPA Code of Practice for Prosecutors (which is akin to the Code for Crown Prosecutors) on 27 June 2013. Under the Code, the starting point for determining whether a DPA will be appropriate in any given circumstance is to apply the following two stage test. Prosecutors must be satisfied either that:

a. the evidential stage of the Full Code Test in the Code for Crown Prosecutors is satisfied, ***or***, if this is not met,
b. there is at least a reasonable suspicion that the commercial organisation has committed the offence, and there are reasonable grounds for believing that a continued investigation would provide further evidence within a reasonable period of time, so that all the evidence together would be capable of establishing a realistic prospect of conviction in accordance with the Full Code Test,

and that the public interest would be properly served by the prosecutor not prosecuting but instead entering into a DPA (in accordance with certain criteria).

The aim of the introduction of DPAs

In 2012, the National Fraud Authority estimated that fraud committed by all types of offenders cost the UK £73bn per year. In the Impact Assessment published in July 2012, the government stated: "The present justice system in England and Wales is inadequate for dealing effectively with criminal enforcement against commercial organisations in the field of complex and serious economic crime. The system's deficiencies pose problems for prosecutors, defendants and judges and can have adverse impacts on victims, customers, suppliers and the wider economy. The increasing internationalisation of both the crime and the offending commercial organisations exacerbates the existing problems".

There is a general recognition that the options for dealing with offending by commercial organisations are limited and the number of successful prosecutions each year, through both criminal and civil proceedings, is too low. Policing of these offences is extremely difficult, relying heavily on self-reporting and whistle blowing (where there is usually limited incentive for an organisation to self- report offending) and as the complexity and size of commercial organisations grow, so too do the difficulties of investigating criminal activity and of bringing commercial organisations to justice. Further, criminal prosecutions of companies for fraud and kindred offences involve lengthy investigations and expensive trials.

From the prosecution perspective the best outcome in economic crime cases with a corporate defendant under the present system results in a conviction and fine against a corporate identity. However, companies that are convicted are likely to be stigmatised and locked out from bidding for governmental and local government work. The conviction and sentence can have an impact on share price, can lead the company to seek to avoid further liability by winding up and can have such an adverse effect on the company's viability that jobs are lost and shareholders, suppliers and customers are affected, none of which is in the public interest.

Respondents to the 2012 Consultation welcomed the proposals to create a new tool for prosecutors to tackle economic crime, with 86% of respondents agreeing that DPAs have the potential to improve the way in which corporate economic crime is dealt with and would enable prosecutors to bring more cases to justice. DPAs are viewed as attractive alternatives: investigators can avoid lengthy and expensive prosecutions, focusing their energies on a greater number of investigations and achieving higher levels of outcome combined with revenues from financial penalties imposed. Offending organisations, particularly those that self-report, can rectify their activities and move on without the very damaging effects of lengthy criminal prosecution and conviction.

The proposed procedure

Under the Code of Practice for Prosecutors, if the prosecutor decides to offer the company the opportunity to enter into DPA negotiations, it should do so by sending a formal letter of invitation. If the company agrees to engage in negotiations, the prosecutor will then send a letter setting out the way in which the discussions will be conducted (this includes making specified undertakings).

Unlike in the US, the UK government has insisted on Judicial oversight throughout each DPA. Under the current plan, as stated in the government response to the consultation dated 23 October 2012, "the judiciary will play a vital independent role in [the] process to ensure that DPAs are properly scrutinised, transparent and in the interests of justice".

Having made a decision in principle that a DPA is a suitable disposal and obtained initial agreement from the company under investigation, the prosecutor will commence proceedings in the Crown Court. Paragraph 32 of Schedule 17 inserts a new section (2)(ba) into the Administration of Justice (Miscellaneous Provisions) Act 1933 whereby an Indictment can be preferred in the Crown Court for the purposes of a DPA. The prosecutor prefers a bill of indictment which is then immediately suspended for the term of the DPA under paragraph 2, schedule 17, CCA 2013.

At a preliminary hearing in private a Crown Court Judge will be presented with an outline of agreed basic facts and alleged wrongdoing, a draft Indictment, the agreed or contemplated conditions to be attached to the agreement and an outline of any areas of dispute or on-going discussion. The Judge will then rule on whether it is "in the interests of justice" for a DPA to be entered into in that case. The Judge will also indicate whether the emerging terms are likely to be appropriate by determining if they are "fair, reasonable and proportionate" in the circumstances of the case (paragraph 7, Schedule 17, CCA 2013).

Although clearly indicative, a preliminary ruling that a DPA is appropriate will not be binding on the Judge until such time as the agreement is finalised. Once the parties have agreed the terms the case will be listed before the Judge in private for his final approval (paragraph 8, Schedule 17 CCA 2013). If accepted the Judge will then sit in open court. The terms of the DPA will be pronounced in public and subject to prejudicing any future litigation the prosecutor will be required to publish the final agreement (paragraph 12, Schedule 17 CCA 2013).

Under paragraph 9, Schedule 17 CCA 2013, the prosecutor can at any time during the period of the DPA apply to the Court where it believes there has been a breach of the agreement. The Court will then determine on the balance of probabilities whether there has been a breach and may then order the parties to agree proposals for remedying the breach or order the termination of the DPA. If the DPA is terminated criminal proceedings based on the suspended Indictment can be recommenced.

Paragraph 10, schedule 17 CCA 2013 sets out the procedure for the variation of the DPA. If during the period of the DPA it becomes apparent to the parties that the terms are unworkable and it is agreed they should be varied, the prosecutor must apply to the Crown Court for a declaration that the variation is in the interests of justice. There is no route by which the defendant can seek to vary the DPA without the agreement of the prosecutor until breach proceedings under paragraph 9.

After the expiry date of the DPA (the date on which the DPA ceases to have effect), the proceedings instituted are to be discontinued by the prosecutor. Fresh proceedings may, however, be instituted should it transpire that during the course of negotiations for the DPA, the defendant provided inaccurate, misleading or incomplete information to the prosecutor which he knew or ought to have known was so.

The commercial benefits of DPAs

The success of DPAs is likely to depend on how attractive they are seen to be by corporations. Self-reporting was introduced by the SFO in 2009 but under the proposed DPAs it becomes a central feature of the process.

Potentially problematically, there will inevitably be complications with admissibility of material obtained as part of

the DPA negotiations at any trial following the failure of negotiations or breach proceedings. Under paragraph 13, Schedule 17 CCA 2013, the statement of facts in any agreed DPA is to be treated as a section 10 Criminal Justice Act 1967 admission in any subsequent criminal proceedings. Where negotiations have taken place but have not resulted in an agreed DPA then draft material may be admissible in a prosecution for providing inaccurate or misleading information or if the defendant asserts in evidence something that the material demonstrates is inconsistent. Of course, any criminal court will retain the general power to exclude material on the basis of fairness under section 78 PACE 1984. However, corporations would still be bound by the statement of facts, which could expose them to follow-on claims.

Some have suggested that the government needs to do more to ensure DPAs give companies confidence that they will be immune from prosecution in other jurisdictions once they have entered into a DPA in the UK, especially as now more often than before economic crime crosses borders and, therefore, more than one country may have jurisdiction. A DPA will not be effective or attractive if a company fears it could still face prosecution overseas. However, DPAs are likely to create a more realistic prospect of reaching a global settlement in cross-border criminal investigations.

Furthermore, the decision whether to enter a DPA will remain complicated for companies, in particular where a company has received legal advice that a successful prosecution is unlikely. Currently, in the UK, unlike the US where the same doctrine does not apply, corporate criminal liability (even when applying the "reasonable suspicion" test) means that it is much harder to secure criminal convictions against corporations due to the need to find a "directing mind". It is to be noted that, as reported by *The Financial Times* on 2 September 2013, David Green, Director of the SFO, has suggested that the legal test used in section 7 of the Bribery Act 2010 of "failing to prevent" should be extended to other corporate offences. In these circumstances a company could be criminally liable for failing to prevent fraud by their employees. Shadow Attorney General Emily Thornberry has expressed her support of such a proposal.

Corporations wanting to take advantage of DPAs will have to, in effect, agree to be charged with criminal offences and it may be very difficult to justify that decision to shareholders. The process is also inherently uncertain because of the requirement for Judicial approval.

> *"There is a general recognition that the options for dealing with offending by commercial organisations are limited"*

However, DPAs are likely to be of particular interest to companies involved in public procurement where a conviction can result in mandatory and permanent debarment in certain jurisdictions from procurement processes (although it is appreciated those who enter DPAs may be ruled out on a discretionary basis).

It should also not be forgotten that if a corporation (aware of the criminal activity) allows, for example, corruption to go unpunished, then the profits of that crime may well form a separate offence under the UK's anti-money laundering legislation. If senior executives turn a blind eye to corruption, they themselves risk committing an offence under the Bribery Act 2010 (section 14) as well as committing personal money laundering offences, concealing criminal conduct and perverting the course of justice. In these circumstances, arguably an organisation may have no real choice about whether to self-report.

Public image will no doubt be a primary consideration for a corporation. The commercial desire to dispose of a problem as quickly as possible, and as cheaply as possible, where there would be less damage to a company's brand image and products than defending the case through a trial is likely to be a very significant driver in deciding whether to self-report. Coming clean about embarrassing issues does not come naturally to many corporations, but the threat of unlimited fines, combined with the possibility of public procurement debarment orders, the damage to reputation, and the likelihood of the withdrawal of business partners, are important factors to consider when weighing the alternatives to self-reporting.

Conclusions

On the 17 July 2013, the EU Commission adopted the proposal of a Council Regulation on the establishment of a European Public Prosecutor's Office (EPPO). It is understood that the EPPO will be likely to have the power to enter into a form of DPA. In Germany, proposals are being considered, subject to Constitutional issues, for formal DPA arrangements. It seems that in neither case will such arrangement be subject to Judicial control or supervision.

The restraints on public expenditure are likely to continue for some time. A recent article in the *Law Society Gazette* reports that there is concern, for example, that the SFO will struggle to enforce the Bribery Act under current budget restraints. According to its 2012–13 annual report, the SFO's total budget will be cut to £32.2m this year and to £30.8m in 2014. As recently as 2008–09, the SFO budget was more than £53m. Such realities cannot be ignored.

The introduction of DPAs will be challenging, but they present the opportunity for significant cost saving, both for corporations and prosecuting authorities alike, while providing for the imposition of robust sanctions and penalties on those corporations which depart from the expected standards. Further, they may well reduce the collateral damage which could have been suffered by innocent staff members and/or consumers of the defaulting corporation.

As we have seen from other cases in the US and Europe, DPAs have proved to be valuable in other jurisdictions and should prove to be an effective weapon in the government's armoury in the fight against economic crime.

While there is plainly concern that a DPA may be seen by some as a means for corporations to "buy their way out" of a prosecution, providing there is proper independent and effective judicial scrutiny, as required in the legislation (and deemed essential by the government, according to the speech given by the Solicitor General on 26 June 2013), it is suggested that the UK model is likely not only to provide a sensible and practical resolution in appropriate cases, but may in time be seen as a model which is respected and followed by other countries. Finally, we note that on 2 September 2013, in his keynote speech to the Cambridge Symposium, the Director of the SFO welcomed DPAs as a new prosecutorial tool. **NLJ**

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