RECOGNISING THE MORAL CULPABILITY OF CORPORATE STRUCTURES

INTRODUCTION

The identification principle, articulated by the House of Lords in the seminal case of *Tesco Supermarkets v Nattrass*, requires that where proof of *mens rea* is necessary to show corporate criminal liability, such intent must normally be attributed to the company by reference to the ‘directing mind’.¹ This has been defined as the acts of ‘the board of directors, the managing director and perhaps other superior officers of a company who carry out functions of management and speak and act as the company.’² The rationale underpinning this is that ‘a corporation must act through living persons… acting as the company.’ The ‘directing mind’ becomes an ‘embodiment of the company’, and if he has a ‘guilty mind then that guilt is the guilt of the company.’³ This principle is at present the only route to liability for all major economic criminal offences, such as fraud, false accounting, and money laundering, with the recent exceptions of bribery and facilitating tax evasion.⁴

This essay has two parts. The first part will argue that the ‘identification principle’ indeed undermines the effective enforcement of economic crimes to a significant extent. The second part of this essay argues for the introduction of a ‘failing to prevent’ model of corporate criminal liability, because of its preventative impact, consistency, and national as well as cross-jurisdictional effectiveness. This model would be based on Section 7 of the Bribery Act 2010.

The main issue confronted by such a change is the displacement of our traditional understanding of criminal liability. The identification principle is underpinned by the notion that corporate bodies are unable to think, and act, as personalities in themselves, and that it is the human mind(s) within them whom pull the levers. Hence, identifying the ‘directing mind’ allows blame to be assigned, and justifies the imposition of a criminal sanction in line with an ordinary understanding of *mens rea*. Moving towards an organisational model of imposing criminal liability must therefore be accompanied by a change in this understanding of corporate criminality. In other words, there must be a shift towards recognising corporate bodies as moral agents, with the ability – through their structures, culture, policies, brand, and actions – to be separately and distinctly culpable for wrongdoing.

² *Tesco Supermarkets v Nattrass* [1972] AC 153 per Lord Reid, paras. 170-171  
³ *ibid*  
⁴ David Green QC (Director of the Serious Fraud Office), Cambridge Symposium on Economic Crime (2016) <https://www.sfo.gov.uk/2016/09/05/cambridge-symposium-2016/>
THE LIMITS OF THE IDENTIFICATION PRINCIPLE

This part argues that the identification principle undermines the effective criminal law enforcement of economic crime in three key ways. First, by ignoring the reality of modern-day corporate structures. Secondly, by perpetuating an unequal application of the law. And thirdly, by favouring a demonstrably weaker enforcement regime than, for example, the United States.

I. Ignoring the Reality of Corporate Structures

In practice, modern-day companies, particularly larger or multinational corporations, often have complex, decentralised, and devolved policy or strategic decision-making processes. This means that significant matters can be – and often are – determined at a local or regional level, and in any case, at a level lower than that imagined in *Tesco Supermarkets v Nattrass*.

This conflicts with the identification principle, which focusses on attributing acts and states of mind of a limited range of senior people to the corporation. Consider, for example those classed as ‘the directing mind’ creating or rewarding a culture of disregard for the law in pursuit of profits for the company, or a failure to implement adequate training or oversight mechanisms for compliance. In these cases, such senior managers, and the corporation by implication, would be protected from liability for any resulting criminality due to the difficulty in proving their *mens rea* for any relevant offence.

The identification principle therefore ‘requires an evidence trail that is likely to dry up long before getting near to the Board’. In turn, this allows corporations to escape liability despite blameworthiness. In this regard, Cavanagh notes that when the identification principle is applied to large companies, it becomes *impossible to establish the facts relevant to satisfy the requisite elements of the offence*. Due to the range of stakeholders involved, from day-to-day supervisors, to middle-level managers, blame cannot be neatly tied to one individual. The identification principle thus becomes ‘an unsatisfactorily narrow scope for criminal liability’.

II. Unequal Application of the Law

The identification principle further hampers effective criminal law enforcement of economic crimes through its unequal application to small and medium-size enterprises (‘SMEs’). In SMEs, especially in owner-managed companies, ‘the identification doctrine works well.’ It is easier to identify the ‘directing mind’, and then to determine whether he or she has the requisite degree of culpability. Moreover, due to the size of such corporations, those identified as the ‘directing mind’ are more likely to have direct knowledge and input in the day-to-day running of their company.

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5 See n. 1, para. 5.85
6 *ibid*
8 *ibid*, p. 3
9 Smith & Hogan, *Criminal Law* (2008), p 249
10 See n. 7, p. 3
11 e.g. *R v OLL Ltd and Kite* [1996] 2 Cr App R 295, involving a small business, where in his ruling the trial judge Ognall J stated: ‘Mr Kite and the company, OLL Ltd, of which he is a managing director, stand or fall together. One for all and all for one’.
This provides an incentive for prosecutors to prioritise such ‘low-hanging fruit’, and results in the targeting of only a small sample of offending.\textsuperscript{12} As Gobert points out, the identification principle seems to work \textit{worst} in cases where it is needed most.\textsuperscript{13} Moreover, it is a basic principle of the rule of law that the law should be applied equally to all. Equal and consistent enforcement increases the deterrence effect of the criminal law and instills it with a sense of fairness crucial to encouraging compliance.

Related to this, the Law Commission has indicated that the identification principle ‘gives a perverse incentive for companies to operate with devolved structures that insulate directors (or equivalent persons) to a certain extent from knowledge of what their managers or employees are doing, when that knowledge might involve awareness of offences being committed for the benefit of the company.’\textsuperscript{14} A model of liability which encourages bad governance further undermines the effective criminal law enforcement of economic crime.

\section*{III. Relative Ineffectiveness}

The United States imposes a wider model of attributing liability to corporations for federal economic crimes. This is in essence a form of vicarious liability following the US Supreme Court decision in \textit{New York Central & Hudson River Railroad Company v US}, which allows a corporation to be held liable for the conduct of even ‘low-level employees’.\textsuperscript{15} The case of Tom Hayes after the LIBOR Scandal is illustrative of the relative ineffectiveness of the United Kingdom’s corporate liability regime in comparison to the US.\textsuperscript{16}

Tom Hayes was a trader for UBS and Citigroup who was arrested, tried, and sentenced to fourteen years in prison for his role in the LIBOR Scandal.\textsuperscript{17} During his trial, Hayes claimed that managers at these banks condoned his actions. In 2016, the Serious Fraud Office explicitly noted the identification principle meant they ‘could not touch the bank for which [Tom Hayes] worked whilst manipulating LIBOR.’ In contrast, ‘That bank was held to account… in a New York courtroom, where vicarious liability made the prosecution a much simpler matter.’\textsuperscript{18}

\textbf{THE ‘FAILURE TO PREVENT’ APPROACH}

As demonstrated above, the identification principle is unsatisfactory in holding corporations to account for economic crimes. This part argues that the time has come for a ‘failure to prevent’ approach to such corporate criminal liability.

This is largely argued on the basis of the successes arising from the Bribery Act 2010, and the need for cross-border cooperation. The final section of this part suggests that the most appropriate ‘failure to prevent’ model would take the same form as that in Section 7 of the Bribery Act.

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\textsuperscript{12} See n. 1, para. 1.66
\textsuperscript{13} i.e. big business. See J Gobert, Rethinking Corporate Crime (2003), p. 63
\textsuperscript{14} See n. 1, para. 1.65
\textsuperscript{15} Nicholas Ryder, ‘Too scared to prosecute and too scared to jail?’ A critical and comparative analysis of enforcement of financial crime legislation against corporations in the USA and the UK (2018) Journal of Criminal Law, p. 3
\textsuperscript{17} \textit{ibid}
\textsuperscript{18} \textit{ibid}
\end{flushright}
IV. The Successes of the Bribery Act 2010

(i) Effectiveness

The Bribery Act created a new offence – better-termed a method of attributing liability – where if a person associated with Company A commits an offence of bribery, Company A is guilty of the offence. The ‘failure to prevent’ aspect of this is the defence embodied in Section 7(2), which provides that it is a defence for the corporation to prove, when charged, that it had in place ‘adequate procedures designed to prevent persons associated with [the corporation] from undertaking such conduct.’

The result of this is an automatic overcoming of the unrealistic evidential burden which the identification principle suffered from, and a method of attributing liability that better reflects the reality of modern corporate decision-making, ‘which is often the product of corporate policies and procedures rather than individual decisions.’ This is particularly well-accomplished by the ‘failure to prevent’ model due to its focus on whether a corporation has such ‘adequate procedures’ in place as the gravamen of the offence, rather than the attribution of human intention.

The increase in effective enforcement has been notable. Ryder points out that the Serious Fraud Office (‘SFO’) has already secured several Deferred Prosecution Agreements (‘DPAs’) against corporations after this change. For example, the SFO quickly obtained DPAs for breaches of the failing to prevent bribery offence against Standard Bank PLC. This was followed by DPAs against XYX Ltd, and most notably, in 2017, with Rolls-Royce.

(ii) Preventative effect

In addition to allowing the SFO to take substantive action against corporations, the Bribery Act has also promoted good governance. Wells notes that by placing the responsibility on the commercial organisation to develop adequate compliance procedures under threat of direct liability, there has since been a major commitment to ethical corporate culture. Indeed, the Ministry of Justice itself recently acknowledged that the Bribery Act has provided significant incentives to companies to make bribery prevention part of good governance. In the same way, expanding the failure to prevent model will have a similar preventative impact in relation to other economic crimes.

(iii) Consistency

A further reason to expand the failure to prevent model to other economic crimes is for the purpose of consistency. The introduction in 2013 of DPAs applied to bribery and a range of

19 Bribery Act 2010, Section 7(1)
20 See n. 7
21 See n 15, p. 10
22 ibid, p. 8
23 Serious Fraud Office, Rolls-Royce PLC <https://www.sfo.gov.uk/cases/rolls-royce-plc/>
24 Wells, Corporate failure to prevent economic crime - a proposal Crim. L.R. (2017) 6, 426, p. 2
25 ibid, p. 8
26 See n. 16, where Transparency International notes that ‘With the Bribery Act we have seen industry standards will develop, the sharing of best practice, and ultimately collective action, whereby companies work together to minimise their exposure to bribery.’

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economic crimes, including fraud, tax evasion, and money laundering. The Sentencing Council also published definitive guidelines for this same ‘family’ of offences in 2014. Additional consistency in the applicable mode of liability for economic offences would create more certainty in this area of criminal law, the importance of which cannot be overstated.

V. Increasing Cross-Border Cooperation

Another benefit to implementing the ‘failure to prevent’ model is its impact on cross-border cooperation. Corporations increasingly operate across borders, and fighting economic crime therefore requires transnational efforts. The world’s biggest multinational corporations are disproportionately located in the United States and Europe. Investigation and prosecution in these areas also requires cooperation with a number of international bodies and organisations.

Amongst the largest financial markets, the United Kingdom has the narrowest corporate criminal liability regime for most economic crime. This certainly impedes effective enforcement, as seen in the LIBOR Scandal. By comparison, South Africa has a similar liability model to the US. Switzerland, another example, employs a ‘failure to prevent’ model by imposing corporate liability ‘if the corporation can be said to have not taken all reasonable and necessary organisational measures to prevent such a breach.’

As a result, the move towards a wider corporate liability regime would allow the UK to more effectively participate in cross-border enforcement action with key partners, and likewise uphold its reputation amongst its allies. In particular, this would align the UK’s enforcement powers with those in the US and Germany, with whom the SFO often cooperates. Another aspect of this is that the UK must not fall behind – financial and economic crimes are often international in scope and harmonisation via the OECD, UN and the EU is already under way.

VI. What Would Need to Be Proved, and to What Standard?

The form suggested for any new model of corporate criminal liability would reflect that in Section 7 of the Bribery Act 2010. A company would be guilty of the economic offence if an agent of the company commits the offence, with the intention of benefitting the corporation. The intention to benefit the corporation element is important, as without it, an unfairness would be created where even where the corporation itself is, for example, defrauded by an employee, it could be held liable. The Criminal Finances Act 2017 failure to facilitate tax evasion offence does not have such a provision.

A defence would then be open to the corporation with a reverse burden of proving that it ‘had in place adequate procedures designed to prevent’ the offence being committed. Due to the corporation’s particular knowledge of its own procedures and internal monitoring structures, a

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27 Crime and Courts Act 2013, Schedule 17
28 ibid, p. 1
29 ibid, p. 5
31 See n. 24, p. 5
32 Swiss Penal Code, Article 102 (2)
33 See n. 24, p. 6
34 ibid, p. 8
reverse burden of proof in this sense would be justified under Article 6 of the European Convention on Human Rights.\textsuperscript{36} Guidance would be provided by the relevant authorities for each type of offence on what constitutes ‘adequate measures’, as is done by the Chancellor of the Exchequer for the facilitation of tax evasion offence.\textsuperscript{37} Such measures as are ‘adequate’ would only consist of those proportionate to the risk faced by the company, in any case, in order to address costs concerns for SMEs.

**CONCLUSION**

This essay has demonstrated that the effective criminal law enforcement of economic crimes is severely undermined by the identification principle, which perpetuates an artificial understanding of how modern-day corporations are structured, encourages bad governance, and results in an unequal application of the law. The ‘failure to prevent’ model of corporate liability is far more effective, and should be implemented in order to build on the successes of the Bribery Act, and allow the UK to take its proper place in a globalising world where corporations increasingly operate across borders, with immense influence, and with much needed oversight.

The ‘failure to prevent’ model introduces an organisational method of imposing liability on corporations, and this new approach requires a commensurate recognition of the capacity for corporations to operate with autonomy and attract moral culpability. The House of Lords decision in *Tesco* was based on a traditional understanding of criminal liability and entrenched the identification principle in order to sustain an ordinary notion of *mens rea* as a reflection of *personal* or human fault.\textsuperscript{38} Conversely, organisational models of fault hold corporations directly culpable for their own acts and omissions. This raises a pivotal issue, as culpability can only be imposed on moral agents.\textsuperscript{39}

It has been suggested that corporations are ‘fictitious legally created persons incapable of culpability.’\textsuperscript{40} Wolf aptly encapsulates this notion, by stating that ‘evil lurks in the hearts of men and women, or it lurks nowhere at all.’\textsuperscript{41} It is submitted our understanding of corporations must take a step forward. As French points out, the primary condition of moral agency is the notion of intentionality. If a body can have intentions, aims, and patterns of behaviour, then for practical and legal purposes, it must also have agency as a being.\textsuperscript{42}

Corporations have a system of decision-making structures, from their articles of incorporation, to policies, ethos, and objectives, which in terms of longevity far outlive any particular appointment of Boards of Directors or employees. These amount to intentionality.\textsuperscript{43} As a result,

\textsuperscript{36} *R v Lambert* [2001] UKHL 37
\textsuperscript{37} Criminal Finances Act, Section 47
\textsuperscript{38} See n. 2, Lord Morris at [170]
\textsuperscript{39} See n. 7, p. 10 – Cavanagh also suggests that organisational models cannot be justified unless this issue is overcome; C. M. V. Clarkson, *Kicking Corporate Bodies and Damning their Souls* (1996) 59 MLR 557 at 566
\textsuperscript{40} G. Sullivan, *Expressing Corporate Guilt* (1995) 15 OJLS 283
\textsuperscript{43} *ibid*
a company may have an ‘intention’ which no individual associated with the organisation shares.\textsuperscript{44}

Moreover, an examination of the role corporations have in modern society reveals their capacity to be culpability-bearing agents.\textsuperscript{45} Indeed, the notion that corporations are free-standing moral agents is no longer exceptional in academic literature.\textsuperscript{46} Even intuitively it is difficult to overlook that our organisations, companies, and groups often have what can be termed as a unique ‘culture’.\textsuperscript{47}

Therefore, an organisational model of fault, which attributes liability directly to the corporation by focussing on what structures the company has in place to prevent offending is a more realistic reflection of how corporations exist, operate, and even commit offences. The ‘failure to prevent’ model is not only a more effectively enforceable model of liability, it is also a correct recognition of the individual culpability of modern-day corporations as autonomous structures. It is a recognition which is long overdue.

\textsuperscript{44} See n. 7, p. 10
\textsuperscript{45} ibid
\textsuperscript{47} See n. 1, para. C.28; Clough, \textit{Bridging the Theoretical Gap: The Search for a Realist Model of Corporate Criminal Liability} (2007) 18 Criminal Law Forum 267, p. 271

Clough summarises this position aptly, noting that the personality or culture of a corporation is unique, and arises from a number of identifiable characteristics which include the corporation’s structure, goals, training provisions, compliance systems, reactions to past violations, incentives and remedial steps.