Economic Crime and Corporate Transparency Act 2023 - amendment (Failure to Prevent Fraud offence)

Lead department	Home Office
Summary of proposal	The measure introduced a failure to prevent fraud (FTPF) offence covering large, incorporated bodies and partnerships.
Submission type	Impact assessment (IA) – 11 September 2024
Legislation type	Primary legislation
Implementation date	26 October 2023
Policy stage	Final
RPC reference	RPC-HO-5197(2)
Opinion type	Formal
Date of issue	1 October 2024

RPC opinion

Rating[1]	**RPC opinion**
Fit for purpose	On first submission the IA received an initial review notice (IRN). The revised IA has satisfactorily addressed issues around the assessment of direct impacts on business and the small and microbusiness assessment. The assessment of direct costs to business and wider cost benefit analysis would benefit from greater stakeholder evidence.

Business impact target assessment

	Department assessment	**RPC validated**
Classification	Qualifying regulatory provision (IN)	Qualifying regulatory provision (IN)
Equivalent annual net direct cost to business (EANDCB)	£76.4 million	£76.4 million (*2019 prices, 2020 present value*)
Business impact target (BIT) score	£382.2 million	£382.0 million
Business net present value	-£658.0 million	
Overall net present value	-£658.0 million	

[1] The RPC opinion rating is based only on the robustness of the EANDCB and quality of the SaMBA, as set out in the Better Regulation Framework. RPC ratings are fit for purpose or not fit for purpose.

RPC summary

Category	Quality[2]	RPC comments
EANDCB	**Green**	The department has monetised the key costs to business and correctly treated them as direct. The estimates have been tested against costs of comparable measures but would benefit from stakeholder input.
Small and micro business assessment (SaMBA)	**Green**	The measure is not expected to affect SMBs due to the business size thresholds being used. The IA has addressed why the measure applies only to large organisations. The IA would benefit from discussing the impacts on medium-sized businesses above the threshold, i.e. with between 250 and 499 employees.
Rationale and options	**Weak**	The rationale for intervention is supported by a Law Commission (LC) study but would benefit from having further information on the extent of existing corporate fraud, and how the measure can be expected to help reduce this. The LC study considered different options, however, the IA does not include non-regulatory (and non-legal) options, (e.g. incentives are employed to disincentivise fraud).
Cost-benefit analysis	**Weak**	The analysis would benefit from stakeholder input. To partly address the limited evidence, the IA provides a good sensitivity analysis and assessment of risk and uncertainty.
Wider impacts	**Satisfactory**	The IA has improved its assessment of public sector and competition impacts.
Monitoring and evaluation plan	**Good**	The IA appropriately outlines a ‘high evidence’ approach to post-implementation review. The plan has been strengthened by discussing data sources, research methods and the specific areas of the analysis that will be addressed by the PIR.

[2] The RPC quality ratings are used to indicate the quality and robustness of the evidence used to support different analytical areas. Please find the definitions of the RPC quality ratings here.

Background

The RPC issued an opinion in July 2022 on a final stage impact assessment (IA) covering the Home Office measures in the (then) Economic Crime and Corporate Transparency Bill.[3] Subsequent to this, the Bill was amended during its parliamentary passage to include a 'failure to prevent fraud' (FTPF) offence covering large organisations. Given that this measure was not included in the IA referred to above, the department has produced an additional IA covering its impacts and has submitted it for RPC scrutiny.

The RPC understands that there were no other amendments made to the Bill, relating either to the Home Office or other departments' measures, with a material impact on the estimated direct impact on business. An enactment stage IA has not been published for this Act.

Response to initial review

As originally submitted, the IA was not fit for purpose. The RPC was unable to validate the department's EANDCB figure for the reasons summarised below.

EANDCB

Evidence and data

The department needed to explain whether there is any supporting evidence from industry for the main estimates and assumptions used in the IA. Where such testing has not been undertaken, the department needed to provide further details of the testing against the costs of comparable measures. The IA needed to provide details of underlying evidence behind these estimates, such as the cost and duration of comparable training courses, and justify why these are a reasonable proxy for the cost of the FTPF measure.

Justification of training cost assumptions

The IA needed to demonstrate that the assumptions in the costing were appropriate, in particular whether all employees (in the 85 per cent of companies assumed to need to take action) would require the training. The IA also needs to explain its calculations and justify its assumptions for on-going costs.

SaMBA

The RPC asked the department to address the impact of exemption on achievement of the policy objectives to provide evidence to further support the exemption for SMBs.

[3] https://www.gov.uk/government/publications/economic-crime-and-corporate-transparency-bill-2022-home-office-measures-rpc-opinion-green-rated

The present IA has addressed these points satisfactorily, as described under 'EANDCB' and 'SaMBA' below.

There were also a number of other (non-red-rateable) areas for improvement suggested by the RPC. These, and the department's responses, are described in the opinion.

Summary of proposal

As noted above, the FTPF measure covers large organisations, where large is defined as meeting two or three of the following: more than 250 employees; more than £36 million turnover; more than £18 million on the balance sheet total. The offence will apply where the fraud is committed by an employee, or other associated person, with a view to benefiting the organisation or its clients. The offence is intended to mirror the existing failure to prevent offences in the Bribery Act 2010 and Criminal Finances Act 2017.

The department estimates an equivalent annual net direct cost to business (EANDCB) of £101.5 million (£76.4 million in 2019 prices, 2020 present value base year). This is calculated from a ten-year cost to business of £874 million in present value terms. This consists of £488 million set-up costs and £46 million costs in each subsequent year. These costs cover familiarisation, risk assessment, communication and training. Training accounts for the large majority of costs. The department is unable to monetise the benefits of the measure and, with no monetised indirect or non-business costs, the -£874 million (-£658 million in 2019 prices, 2020 present value base year) societal net present value figure consists solely of the ten-year cost to business referred to above.

EANDCB

See also comments under 'Cost Benefit Analysis' (in particular 'evidence and data').

Evidence and data

The revised IA more clearly explains the limitations in obtaining evidence, describing how it has not been possible to test estimates of impacts with stakeholders during or after the Bill passage (paragraphs 67-68, pages 13-14). The revised IA usefully sets out much more detail of its approach of using existing guidance for comparable regulations to estimate costs, in particular guidance related to the failure to prevent tax evasion and failure to prevent bribery offences. The IA seeks to further address the limited nature of the evidence by using sensitivity analysis (much expanded on re-submission – see 'risk and uncertainty') and making commitments in the post-implementation review (PIR) to test the validity of the assumptions following publication of the guidance.

There remains significant uncertainty over the impact of the measure on business and the RPC would normally expect a greater level of evidence for a measure of this expected scale of impact. Nevertheless, given that the measure was enacted in October 2023, and guidance has yet to be produced, the RPC accepts that it may not now be proportionate or productive to undertake significant stakeholder consultation. The department's approach appears to be proportionate in these specific circumstances.

The IA would benefit from discussing any PIR evidence relating to any similar measures, such as in relation to bribery or tax evasion, and addressing whether any similar measures have been introduced in other countries.

Justification of training (and other) cost assumptions

The revised IA sets out in much more detail the sources of the training cost assumptions and why this evidence is considered to be appropriate (in particular at paragraphs 87-88 but also throughout the IA). The IA also now commits, in the monitoring and evaluation section, to having specific evaluation questions regarding reviewing the assumptions. The revised IA addresses (mainly at paragraph 87) the specific concern with the assumption that all staff are required to undertake training. The IA tests the assumption in the sensitivity analysis. The approach is now justified and seems to be appropriate.

The IA now includes more explicit explanation and justification for assumptions regarding how on-going training and communication costs were calculated (paragraphs 91-103, in particular the discussion around staff turnover rates to estimate the number of new staff trained at paragraph 100). The approach is justifiable given employers must demonstrate that they have taken all reasonable steps to prevent fraud, and that they do not tolerate fraud. The IA notes that the approach is consistent with the failure to prevent tax evasion guidance published by HMRC. The IA would benefit from discussing how the training might fit in with induction or other training to minimise costs to employers.

More generally, the IA also now sets out its assumptions and the steps in the calculations in other areas much more clearly, for example in relation to familiarisation and risk assessments (pages 16-17).

Direct/indirect

The IA correctly treats all of the monetised costs to business as direct impacts. The IA refers (table 19, page 34) to the (non-monetised) benefits of the measure as being indirect. This appears to be appropriate, but the IA would benefit from discussing where these benefits fall and, where they accrue to businesses, why it considers them to be indirect.

Transparency of impact of the HO measures in the Bill

As noted above, the RPC previously opined on a final stage IA covering the Home Office measures in the Economic Crime and Corporate Transparency Bill. For transparency and completeness, we would normally expect the department to update this overarching IA to reflect the addition of the FTPF measure and its estimated impact.

Voluntary and Community Bodies (VCBs)

The IA usefully notes that impacts on charities and other VCBs within scope of the better regulation framework have been included. The assessment would benefit from including further details of the cost impact on VCBs, drawing upon the information provided in the annexes on the number of organisations affected.

Updating of estimates

The IA notes that guidance will be published on the procedures that organisations can put in place to prevent fraud but that this was not available when estimating the impacts in this IA. The IA would benefit from discussing who will be producing the guidance and whether the estimates will be revisited when the guidance is produced.

SaMBA

The measure is not expected to affect SMBs due to the business size thresholds being used. In this sense, SMBs are exempt. This is consistent with the better regulation framework's approach that exemption for SMBs is the default position. However, in the absence of a clear picture of the scale of corporate fraud and indication of how this is distributed across business size, the RPC asked the department to address the impact of exemption on achievement of the policy objectives to provide evidence to further support the exemption for SMBs. The department explains that it does not have the data for this, but the IA now sets out the reasoning for excluding SMBs in the rationale (paragraphs 42-45) and SaMBA sections (paragraphs 146-154). This reasoning is mainly around it being easier to identify and hold to account using existing offences perpetrators of fraud in SMBs. The IA also now has an explicit commitment in the M&E plan to review the impact that the exclusion of SMBs has on the policy's progress against its objectives (paragraph 182).

The IA could discuss the likelihood of businesses with fewer than 50 employees meeting the turnover and balance sheet thresholds. The IA usefully discusses possible consequential risks to SMBs, such as large organisations putting contractual clauses on small businesses that provide services for them. The IA would benefit from discussing the likelihood of this and whether there are any mitigations or protections for SMBs should these risks materialise.

Medium-sized business considerations

The IA usefully identifies the number of businesses with between 250 and 499 employees and argues against using 500 employees as a threshold, on the basis that this would very significantly reduce the number of companies in scope. The IA would benefit from explaining the benefit of including these larger, medium-sized businesses within the scope of the measure.

Rationale and options

The absence of data on the incidence of, and losses associated with, corporate fraud means that the evidence of existing harm is limited. However, the rationale for intervention is supported by an LC study that put forward similar proposals. The IA states that the measure closely mirrors these, but with powers usable over a wider set of cases. The IA would benefit from discussing the rationale for this extension of the LC's proposals. The IA usefully refers to market failure rationales for intervention, namely principal-agent and asymmetric information issues.

In response to the RPC's initial review, the revised IA now provides a much-expanded rationale for intervention section and addresses evidence that fraud committed by businesses is a problem in the UK more directly. The IA references the Crown Prosecution Service (CPS) and Serious Fraud Office (SFO) having identified numerous cases of fraud and false accounting where the current law has prevented them from prosecuting corporates when they appear to be the beneficiaries of fraud. The M&E plan now also explicitly covers that the policy will be reviewed on its progress against its objectives (paragraph 182).

The revised IA also now considers international evidence more clearly. Paragraph 20 notes that the Law Commission options paper on corporate liability considered equivalent systems in the US, Canada, Australia, the Netherlands and Italy. The IA would benefit from considering international evidence and precedence more directly. This would also be helpful in understanding the border issues between offences within multi-nationals.

The IA states that an objective is to help create an anti-fraud corporate culture and the document would benefit from discussing more specifically, in practical terms, how the measure might help foster this. More generally, the IA would benefit from evidence that the nature of the intervention (effectively requiring large organisations to undertake risk assessments, training etc) can reasonably be expected to achieve the policy objective.

On options, the IA now usefully includes more detail from the Law Commission's corporate liability options paper (paragraphs 19-24). This includes detailed consideration of civil options (rather than a criminal offence). However, the IA does not include non-regulatory (and non-legal) incentives to achieve the policy objective (e.g. through disincentivising behaviour within corporates that could lead to fraud being committed).

Cost-benefit analysis

Evidence and data

The IA uses the Economic Crime Survey to estimate the proportion of organisations that currently have anti-fraud policies in place. This appears to be a reasonable evidence base, combined with use of high and low scenarios. As noted above, the department explains why the evidence base is limited, but the RPC accepts that it may not now be proportionate to undertake significant stakeholder consultation, given that the measure has now been enacted.

The IA has usefully added a comparison of the average costs assumed in its cost modelling against the results of research on the costs incurred by organisations in complying with the failure to prevent bribery offence. Although this research relates to smaller organisations than those affected by the present measure, this addition to the IA provides a useful benchmark, based upon actual costs to business. The comparison suggests that cost estimates, at least for set-up, may be broadly in line with experience under the bribery offence.

Risk and uncertainty

As noted above, the IA provides a much-expanded sensitivity analysis (paragraphs 128 to 145). There is also a good and expanded discussion of analytical risk and uncertainty (pages 32-34).

Methodology

The department considered break-even analysis but concluded that it was not possible because a Home Office approved cost of fraud to businesses does not exist. Nonetheless, the revised IA discusses published estimates of the cost of fraud to individuals to give some scale context, concluding that this indicates that even small reductions in fraud would be needed to offset the costs of this policy. (paragraphs 120 to 124).

Wider impacts

Public sector impacts

The IA explains why it is not possible to monetise the costs to public sector bodies, such as NHS Trusts, schools and local authorities, due to there being no way to accurately estimate the number that would be in scope of the legislation. The revised IA now acknowledges that these impacts should, in principle, be captured in the NPSV figure and discusses the likely size of the impact (paragraph 108). There is also now a commitment to consider the impact on public sector bodies in the PIR (paragraph 180). The IA would benefit from providing a more developed assessment of the impacts of the measure on public sector organisations.

The IA now provides more discussion on expected number of prosecutions and how the measure might interact with Deferred Prosecution Agreements (paragraph 172) but would benefit more generally from discussing further, and potentially monetising, costs relating to enforcement and the wider criminal justice sector.

Competition impacts

The RPC's initial review noted that as the measure applies only to large organisations, the IA would benefit from consideration of potential competitions impacts between large and smaller businesses. The department has now added a discussion on this (paragraph 171).

Interaction between UK nations

Following RPC comments, the IA now clarifies the applicability of the measure and DPAs across the UK nations (paragraphs 8,9 and 15). The IA also notes consultation with devolved authorities and prosecution agencies (paragraph 18).

Monitoring and evaluation plan

The IA helpfully notes that the significant impact on business means that it will take a 'high evidence' approach to PIR. The IA sets out the principles it will follow and usefully notes data and research methods, including a survey of stakeholders. The plan has been strengthened to explain how the PIR will be informed by the evaluation approach for the Bribery Act 2010 and improved by indicating data sources and describing the assumptions and estimates that will be tested. The plan could be improved further by setting out the metrics to assess the cost effectiveness of the measure, in particular how an improvement in anti-fraud culture will be assessed. The IA could also consider whether some gathering of evidence from stakeholders now could be useful in setting a baseline for a PIR.

Regulatory Policy Committee

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