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Aerospace & Defense Insights

The United Kingdom's fightback
against economic crime begins

Through Aerospace and Defense Insights, we share with you the top legal and political issues affecting the aerospace and defense (A&D) industry. Our A&D industry team monitors the latest developments to help our clients stay in front of issues before they become problems and seize opportunities in a timely manner.

Things are looking up for the SFO – and there is an enforcement focus on A&D

For some time, the Serious Fraud Office (SFO), the main UK government agency that investigates and prosecutes serious fraud, bribery, and corruption, has faced heavy criticism. But with a change of leadership and new legislation coming into force, things are looking up. The ECCTA received Royal Assent near the end of 2023 and this powerful legislation has given the SFO new tools to tackle economic crime. The new SFO Director Nick Ephgrave has been bold and ambitious in setting out his targets for the agency, and he has committed the SFO to a bolder, more pragmatic and more proactive approach under his leadership.

Notwithstanding the SFO's poor performance in recent years, the agency has found some success pursuing economic crime in the A&D Sector. Since deferred prosecution agreements ("DPAs") were introduced in the UK in 2014, the SFO has entered into DPAs with eleven companies in total, three of which are in the A&D sector. This is the most of any industry sector. And there is little sign of the SFO turning its focus away from this sector. In December 2023, the agency launched dawn raids at the aircraft parts supplier AOG Technic Ltd and has launched a criminal investigation into suspected fraud at the company.

ECCTA – a gamechanger in the fight against economic crime?

The ECCTA has the potential to change the SFO's fortunes.

This new legislation has expanded the SFO's powers, allowing the agency to compel people and companies to provide information at the pre-investigation stage.

The ECCTA also includes a new legal test for attributing criminal liability to companies. Previously, a prosecutor had to prove an offense was committed by the "directing mind and will" of a company. This narrow definition made it hard to hold companies to account. The new test applies to a wider group beyond board level. If a "senior manager" acting within their authority commits a relevant offense, say, fraud or bribery, the company is jointly liable. This lowers the bar significantly.

Finally, and most significantly for global businesses operating in the A&D sector, the ECCTA created a brand-new offense of 'failure to prevent fraud'. The ECCTA makes it an offense for a large company or partnership to fail to prevent fraud by a person associated with it. The only defense available will be that a company can show it had reasonable procedures in place to prevent fraud. The government will publish guidance about reasonable procedures before the offense comes into effect.

Corporate criminal liability attaches where the associated person (through their misconduct) intends to benefit, whether directly or indirectly (i) the company or (ii) any person to whom the associated person provides services on behalf of the company (i.e. clients and customers) unless the company itself was, or was intended to be, a victim of the fraud.

Significantly, unlike the UK's Bribery Act which came into force in 2011, any large company or partnership can be liable for the failure to prevent offense, wherever they are incorporated or formed. Where a relevant offense takes place entirely outside the United Kingdom, the company will only be guilty if it would be guilty in the jurisdiction the misconduct took place. Nonetheless, the extra-territorial scope of the offense is potentially very wide-ranging.

What does this mean for companies in the A&D sector?



Fraud takes many forms – from the shop floor to the C-suite

A PR blitz has accompanied the appointment of the new SFO Director, Nick Ephgrave. The new Director has vowed to move more quickly on investigations and senior officials at the agency are understood to believe that the new ‘failure to prevent fraud’ offense will lead to a big uptick in prosecutions. That’s because fraud is rife. It accounts for over 40% of all offenses in England and Wales. In contrast to bribery, which is relatively rare and often takes predictable forms (e.g. kickbacks, facilitation payments, gifts and hospitality), fraud is common and is committed by individuals at various levels of authority within an organization.

Yes, fraud can happen at the very top of a business, for example by senior officers manipulating accounting records or misrepresenting financial performance to investors, creditors or regulators. But decisions at lower levels of a company could have damaging ramifications too.

Take the middle manager based in Texas who is desperate to win a UK defense contract for their business. But when filling in the procurement documentation, they lie about the company’s credentials.

Consider the head of procurement in London who hasn’t been given enough money to acquire the parts needed to manufacture a product to the specifications agreed with their customer in the UAE. So they obtain cheaper counterfeit parts and sign off on documents confirming that the specifications have been met.

Or the technician on the shop floor in Manila who is struggling to meet their targets, and skips some safety checks, but claims to bosses in London that the checks have all been completed.

In all these scenarios, the company could be on the hook for failing to prevent fraud by the offending individual.

But that’s not all.

Think of the safety manager for a company in Senegal who knows that the most recent round of tests did not go well. But they need to get their equipment to the buyer in the United States by the deadline. They know the buyer is under pressure to get the equipment into

service as soon as possible. And so they certify that all is well.

In this scenario, both the Senegalese company and the United States buyer could be on the hook for failing to prevent the fraud by the safety manager, provided that the UK authorities are able to assert jurisdiction. They could do that if either company has a UK touchpoint, or if the fraud affects UK victims, for example if a safety issue arises which affects passengers on a flight to the UK.

The failure to prevent fraud offense is one of strict liability. A company found liable, if convicted, could face an unlimited fine.

What can I do?

The new Director of the SFO has committed the agency to a new campaign of prevention for corporates. In his first public speech in February 2024, Ephgrave spoke of the benefits of reaching out to CEOs, and encouraging good compliance programs. The Director indicated that he was prepared to be creative in partnering with big corporates, and mentioned the possibility of an SFO ‘kitemark’, as a seal of approval for companies who had been given a “*clean bill of health*” by the agency in terms of training and procedures in place to prevent fraud.

Accordingly, the first step for any business in the A&D sector is to refresh your financial crime risk assessments. Given the flurry of prosecution activity affecting companies in the A&D sector in recent years, this step should be an urgent priority for any business in this space. To demonstrate you have in place reasonable procedures you will need a fraud risk assessment to identify where risks exist, where and how representations by the business are made, and to work out what controls are in place. This will help with the design of procedures to stop people associated with your company from committing fraud.

If you would like to find out more about what this new offense could mean for your company, how best to approach your assessment of risk, or update your existing policies and procedures, please get in contact with our team today.



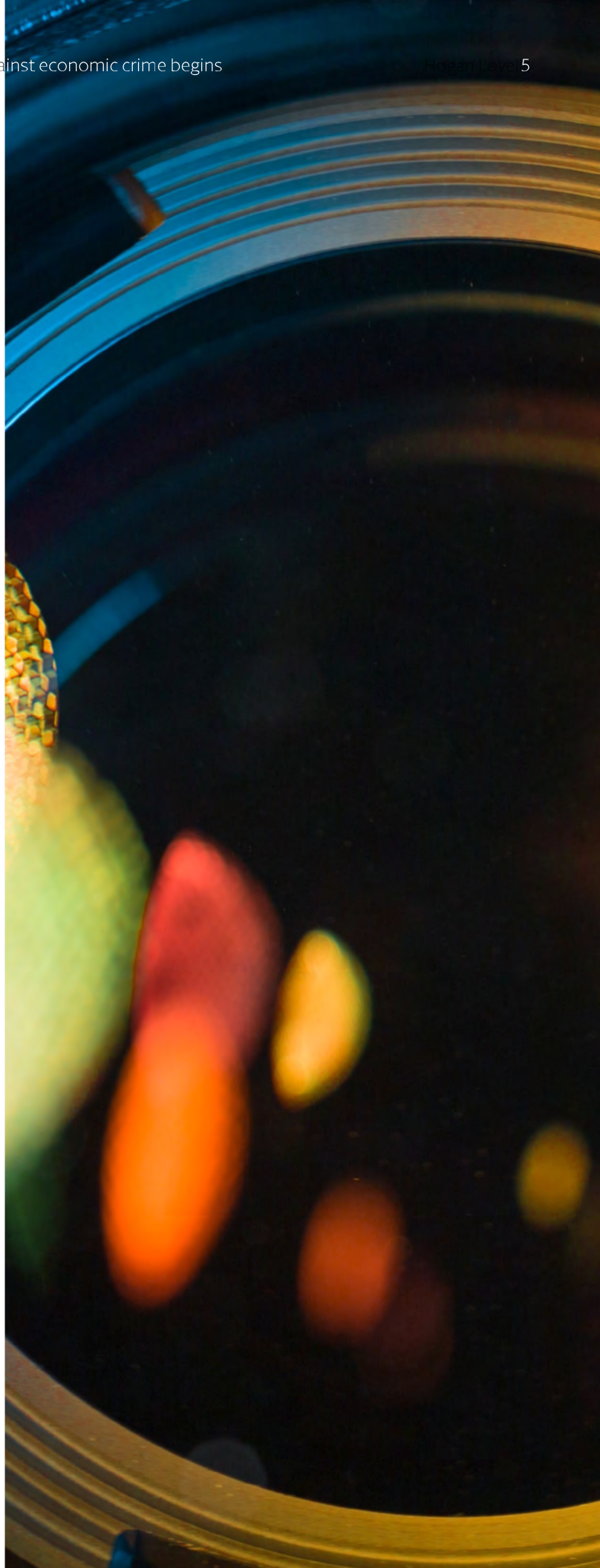
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