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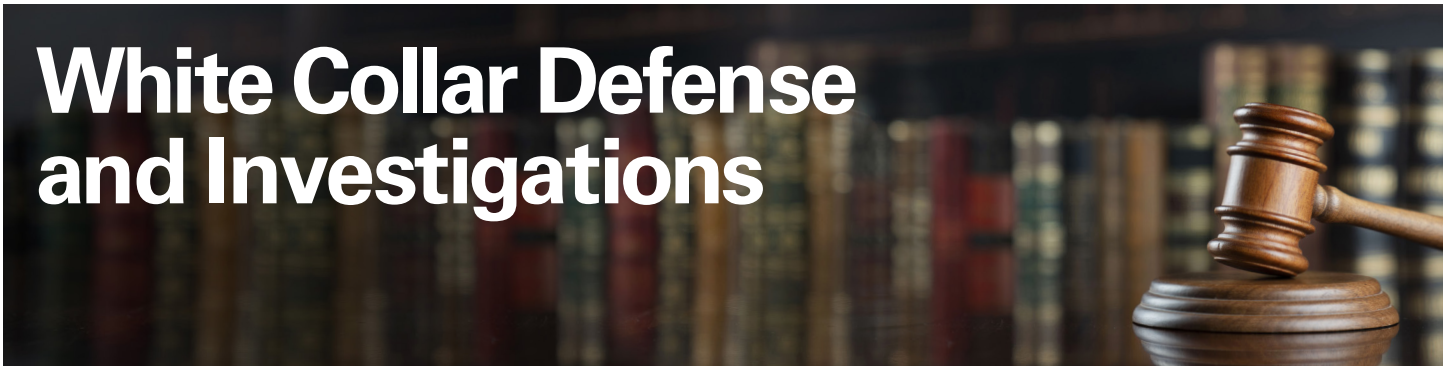

Elizabeth Robertson
Partner / London
44.20.7519.7115
elizabeth.robertson@skadden.com

Jason Williamson
Associate / London
44.20.7519.7093
jason.williamson@skadden.com

Jack Zaher
Associate / London
44.20.7519.7237
jack.zaher@skadden.com

One Manhattan West
New York, NY 10001
212.735.3000

40 Bank St., Canary Wharf
London, E14 5DS, UK
44.20.7519.7000

UK High Court Judgment Spotlights Importance of Managing Supply Chain Risks

On 20 January 2023, the UK High Court of Justice (the High Court) delivered its judgment in *R. (on the application of World Uyghur Congress) v Secretary of State for the Home Department*. The case concerned a judicial review application brought by the World Uyghur Congress (WUC), a nongovernmental organisation which promotes the interests of exiled Uyghur groups, relating to the decision of certain UK enforcement agencies not to investigate alleged criminal wrongdoing.

While the court ultimately decided against WUC in the judicial review, concluding that UK enforcement agencies had not erred in law in deciding not to use their investigatory powers, the judgment is a helpful reminder that money laundering liability could attach to an organisation where there is evidence of human rights violations in its supply chain.

Background

The WUC brought a judicial review claim against the Home Office, HM Revenue & Customs (HMRC) and the National Crime Agency (the NCA) (together, the defendants) in relation to their decision not to investigate exports to the UK of cotton products manufactured in the Xinjiang Uyghur Autonomous Region (XUAR) in China.

- In April 2020, the WUC sought to encourage enforcement agencies in the UK to investigate the supply of cotton to certain UK entities from XUAR.
- The WUC said it provided the enforcement agencies with "a large amount of evidence concerning the issues of forced labour and human rights abuses in the XUAR."
- As part of its judicial review claim, the WUC asserted that the defendants ought to have investigated whether the cotton imports manufactured in XUAR constituted breaches of the Proceeds of Crime Act 2002 (POCA) and certain other provisions in the Foreign Prison-Made Goods Act 1897.

Legal Arguments

The basis for the WUC's judicial review application was that UK enforcement agencies had "misdirected themselves in their approach to the exercise of their powers," including under POCA.

In particular, the WUC argued that the agencies ought to have exercised both their criminal investigatory powers related to the substantive criminal offences in Part 7 of POCA and their civil recovery powers under Part 5.

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Part 7 contains the primary money laundering offences. It provides that it is an offence for a person to:

- Conceal, disguise, convert or transfer criminal property (Section 327).
- Enter into an arrangement which facilitates the acquisition, retention, use or control of criminal property (Section 328).
- Acquire, use or possess criminal property (Section 329).

Part 5 contains civil recovery powers which allow UK enforcement agencies to seize assets suspected to be the proceeds of crime.

These powers serve as an alternative to criminal proceedings and allow for enforcement agencies to recover property that has been obtained through "**unlawful conduct**," which is defined in POCA as that which constitutes an offence in any part of the UK or would constitute an offence in the UK if it had occurred within the jurisdiction.

Enforcement agencies are required to prove that property has been obtained through unlawful conduct and can therefore be recovered, to the civil standard of proof (*i.e.*, the balance of probabilities).

The WUC argued that HMRC and the NCA in particular had failed to use their criminal investigatory powers under Part 7, on the basis that cotton goods originating from XUAR could be criminal property and trading in them could therefore amount to criminal conduct.

As with the definition of "unlawful conduct" in relation to the civil recovery powers, POCA defines "**criminal conduct**" as that which constitutes an offence in any part of the UK or would constitute an offence in the UK if it had occurred within the jurisdiction.

"**Criminal property**" is defined as property which constitutes a person's benefit from criminal conduct (or represents such a benefit), and which the alleged offender knows or suspects that it constitutes or represents such a benefit.

Both HMRC and the NCA accepted that offences under the Modern Slavery Act 2015 and other human rights violations could constitute criminal conduct within the meaning outlined in POCA. However, the key issue in the case related to the application of the definition of criminal property.

The enforcement agencies argued that, for the substantive money laundering offences under Part 7 to be triggered, "any criminal conduct [must be] clearly and specifically identified," and the resultant criminal property must be "specifically identified."

Key Findings in Relation to POCA

Identifying criminal property. The WUC had contended that the presumption that cotton originating from XUAR was, by its very nature, criminal property because of well-documented human rights violations. The High Court determined that in the absence of a specific consignment of goods identified as the product of criminality, the requirements of POCA were not met and no substantive money laundering offence had been triggered.

Ultimately, the High Court considered that the agencies' approach was not a misdirection of law. In particular, the judgment agreed with the view that the starting point for considering whether the criminal offences under POCA had been triggered was the identification of criminal property, applying the definition set out in Section 340.

The High Court noted that the requirements under Section 340 were precise; in order to prove that a consignment of goods was criminal property, it had to be shown that it constituted an alleged offender's benefit from criminal conduct, and that the alleged offender knew or suspected that it constituted such a benefit.

Using the adequate consideration defence. The enforcement agencies also argued that exceptions to certain substantive money laundering offences were also relevant. With respect to the offence of acquiring, using or possessing criminal property under Section 329 POCA, the agencies pointed to Section 329(c), which provides that it is a defence for a person to acquire or have possession of criminal property for "adequate consideration."

The agencies submitted that, even if it were possible to identify a specific product as criminal property, an offence would not have been committed by a UK entity if the product had been the subject of a transaction for adequate consideration. The relevant criminal property would be the proceeds of that transaction in the hands of the criminal seller, not the product in the hands of the purchaser, the agencies argued.

The High Court agreed with this contention and noted that the adequate consideration defence raised challenges as to the practicality of prosecuting an offence under Section 329. In particular, the High Court noted that it would be necessary to show that a consignment of goods was both criminal property and that it had been purchased for significantly less than its value, which presented considerable difficulties in the context of the international trading of goods.

However, this defence is only applicable to the offence under Section 329. The High Court noted that other criminal offences

under POCA — in particular, the other primary money laundering offences under Sections 327 and 328 — could also be relevant in this context.

Using civil recovery powers. The WUC's application regarding the defendants' alleged failure to use their civil recovery powers under Part 5 also failed. The High Court noted that, although the standard of proof in relation to these powers was civil rather than criminal, evidence of a specific consignment of goods would similarly be required in order to demonstrate that the goods were the product of unlawful conduct and therefore able to be recovered.

Liability Under POCA

Although the High Court limited its decision to the very specific facts of the case and, in particular, the legality of the defendants' decision not to engage their investigatory powers, it did make clear that money laundering liability under POCA could attach to a company where there are alleged human rights abuses or criminal wrongdoing in its supply chain.

The High Court acknowledged that there "may be other tools or measures available to the executive and law enforcement agencies" to tackle the types of concerns the WUC raised, which appeared to leave the door open to the potential use of POCA-type powers in this context.

The judgment also hinted that the NCA in particular would look to increase its appetite towards enforcement in this area, noting that, although the WUC had been unable to identify a specific consignment of goods to be investigated, the NCA "remain[ed] open to the possibility that the intelligence picture may change at any time."

In addition, in a statement provided to *Global Investigations Review* following the publication of the judgment, the NCA reiterated that it would "assess any new information received and … review accordingly."

Nevertheless, as highlighted above, the judgment outlines two key obstacles which may hinder significant enforcement activity in this area.

First, it is clear that specific proof of criminality in relation to a specific consignment of goods will be required, and this cannot necessarily be inferred from the nature of the available evidence. This appears to establish a particularly high evidential threshold, especially in light of the "extensive volume of material" the WUC submitted as to the significant concerns in relation to the use of prison and forced labour in the production of cotton in the XUAR. Indeed, the High Court noted that there was "undisputed evidence of the widespread use of forced labour in the XUAR to produce cotton products," but that POCA required specific proof, rather than suspicion or inference from such evidence, in order to establish liability for a criminal offence.

Second, and provided that specific proof of criminality in relation to a specific consignment of goods has been established, a claim will also need to show that such goods were purchased for inadequate consideration. As the High Court pointed out, this requirement poses significant complexities for prosecuting authorities in the context of international trade.

There is limited guidance from the courts as to what may amount to adequate consideration, other than confirmation that it is a question of fact in each case and, in deciding it, the court is obliged to look at all the relevant circumstances.[1]

The courts have also confirmed that the burden of proving that consideration was inadequate is on the prosecution. Therefore, it remains to be seen how the courts would assess whether adequate consideration had been paid where, for example, a company sources goods which have been manufactured by forced labour.

Modern Slavery Concerns and ESG

Notwithstanding the hurdles to establishing liability, concern about the modern slavery risks in global supply chains is expected to be a growing area of focus. This is particularly true given the increased emphasis businesses, investors and the public have placed on environmental, social and governance (ESG) matters — a trend which is only likely to continue in the near future.

For example, on 26 January 2023, the Competition and Markets Authority announced its intention to focus on alleged "greenwashing" in relation to consumer goods. We expect to see increased pressure levied against companies from investors and the general public in relation to these concerns, which may in turn drive enforcement or further legislation on this issue.

As outlined in our September 2022 article "Avoiding Potential Pitfalls When Developing Alternative Supply Chains," the Uyghur Forced Labor Prevention Act came into effect in the US in June 2022 and created a presumption that goods produced in the XUAR are manufactured using forced labour and thus prohibited from entry into the US.

[1] *Hogan v Director of Public Prosecutions* [2007] EWHC 978 (Admin), para. 17. See also, *R. v Kausar (Rahila)* [2009] EWCA Crim 2242, at paras. 8 and 9, which confirmed that the term "consideration" is to be given the meaning which it usually has in contract law.

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This legislation, which stands in stark contrast to the High Court's decision in *R. (on the application of World Uyghur Congress) v Secretary of State for the Home Department*, has forced US companies to evaluate their supply chains.

With the spotlight on this issue in the UK becoming more profound, the pressure on the government to introduce similar legislation may grow, particularly from concerned parties such as the WUC.

Reputational risks exist for organisations that fail to maintain adequate ESG standards, particularly in relation to forced labour but also by being associated with suppliers linked to environmental misconduct, workplace cultural issues or with ties to authoritarian regimes.

Takeaways

The High Court's judgment makes clear that liability could attach to organisations with alleged human rights abuses or criminal wrongdoing in their supply chains. Beyond legal consequences, the reputational consequences for organisations caught up in human rights abuses and modern slavery scandals can be severe.

This should encourage organisations to evaluate their supply chain and manage the associated risks, including with thorough due diligence and a compliance programme which commits suppliers to high standards. As part of an effective compliance programme, organisations should ensure that risk assessments properly account for not only potential bribery and corruption risks but also for ESG and modern slavery concerns.