Corporate liability for money-laundering in supply chains

When you use your mobile phone or drive your electric car, or wear your jeans, put on your shirt or wash your hair, or use a host of other day-to-day products, you probably never stop to think where all the component parts or ingredients originated, or how the product has been manufactured. As consumers we principally care about price, product quality and functionality. We probably don't stop to consider whether the product or clothing we are using represents the proceeds of crime.

Dove J. was recently asked to consider this issue relating to garments made using cotton manufactured in the Xinjiang Uyghur Autonomous Region of China ("the Region"), in **R (World Uyghur Congress) v Home Secretary, HMRC and NCA [2023] EWHC 88**. There was expert opinion evidence, news articles and committee reports (but no direct factual witness evidence) before Dove J that China was committing large-scale human rights abuses in the Region including forced labour in the cotton industry. Evidence showed that 30% of the world's cotton originates from China, of which 85% of that originated from the Region. The Claimant argued: (i) Border Force, the NCA and HMRC had misdirected themselves or fettered their discretion regarding the prohibition on importation of the goods, contrary to s.1 of the *Foreign Prison-made Goods Act 1897,* s.1 of the *Modern Slavery Act 2015* and s.51 of the *International Criminal Court Act 2001* (crimes against humanity); and (ii) there was a separate duty to investigate offences regarding importations of these goods, pursuant to ss.327-329 of the *Proceeds of Crime Act 2002*.

The claim failed on all grounds for a number of fact-specific reasons:

- The threshold in s.1 of the 1897 Act was high: the Defendants had not misdirected themselves when requiring evidence linking a specific consignment of goods to manufacture in a facility that met the definition of "a foreign prison", although it was not necessary to identify which prison;
- Evidence that imported cotton goods *might* have been manufactured from forced labour or prison labour in the Region was insufficient to show that specific goods *had* been imported in breach of prohibition in the 1897 Act;

- Before the *Proceeds of Crime Act 2002* duties were engaged, there needed to be specific proof in relation to a particular consignment that an alleged offender knew or suspected that the goods were criminal property. There was no specific proof of the origins of any consignment in this case;
- The judgment of agencies such as the Defendants regarding their investigatory or enforcement powers would not be lightly disturbed. The Defendants took the view that evidence required for any prosecution was located in China and co-operation from the Chinese authorities was unlikely, so there was little merit in commencing an investigation that would inevitably go nowhere.

The judgment provides a useful analysis of issues relating to a growing Environmental, Social and Governance ("ESG") focus on supply chains, relevant to corporate compliance and white-collar crime lawyers.

Can retail goods or products ever be "the proceeds of crime"?

Yes. The Defendants conceded that offences contrary to s.1 of the *Modern Slavery Act 2015* and/or s.51 of the *International Criminal Court Act 2001* are capable of constituting "criminal conduct" for the purpose of s.340 of the 2002 Act. But Dove J. agreed with the Defendants that s.340 requires specific identification of the alleged criminal conduct and the resultant property, consistently with the Supreme Court's approach in **R v GH [2015] UKSC 24**. In particular, the *Proceeds of Crime Act 2002* does not apply where there is suspected offending to which it was not possible to attribute specific property.

Does "adequate consideration" provide a defence?

Yes, but the method of assessing the adequacy depends on the charge. Dove J confined his consideration of the legal principles to the "acquisition" offence under s.329(1)(a) POCA 2002 on the basis that the Claimant challenged the importation of the goods to the UK (rather than their subsequent use or possession by businesses in the UK), and the Defendants considered s.329(1)(a) to be the "*apposite offence in*

a supply chain case". The way arguments were developed meant that Dove J didn't fully consider the "use" offence under s.329(1)(b) or the "possession" offence in s.329(1)(c). In **R v Haque [2019] EWCA Crim 1028** Davis LJ considered that each of the offences under s.329(1)(a), (b) and (c) was a separate offence. All three of these offences require the prosecution to prove that adequate consideration was *not* paid, but the test for adequacy varies depending on whether the offence relates to "acquiring", "using" or "possessing" the criminal property.

For the "acquisition" offence considered by Dove J., the adequacy of the consideration is determined by reference to s.329(3)(a) POCA 2002: the value of the consideration must be "*significantly less than the value of the property*". There is no indication in the judgment how the Defendants assessed this issue, merely that it was an evidential hurdle the Defendants were entitled to take into consideration when deciding not to further investigate offences at that time. Following **Hogan v DPP [2007] 1 WLR 2944** (an "acquisition" case), the adequacy of consideration is an objective question of fact, separate from the defendant's state of mind, which should be determined by examining all the relevant circumstances. But neither Dove J. nor the Defendants grappled with how the "*market value*" of goods manufactured in a modern slavery case should be assessed for the purpose of s.329(3)(a). Should that be by reference to evidence from alternative suppliers from the same country of origin of their costs of manufacture without using forced labour? Or some other way?

For example, if a shirt costs £2 to manufacture legitimately in Thailand, but I instead pay £1 for the shirt to be manufactured in Thailand using slave labour, is the value of the shirt £1 that I actually paid for it (in which case I have paid adequate consideration), or £2 that I should have paid for it (in which case I haven't)? Presumably, paying a substantially reduced rate for goods manufactured using forced labour does not equate to the "*market rate*" or "*adequate consideration*", but what if the market rate for an entire jurisdiction is artificially low because modern slavery is endemic throughout that system? Perhaps expert evidence could be used to evaluate the market rate for goods had they been manufactured legitimately by reference to other countries of manufacture.

Further, because Dove J was only considering a claim concerning the importation of goods manufactured using forced labour, the Court neither fully considered the offences contrary to s.329(1)(b) or (c), nor the different approach to adequate consideration, only stating:

> "*It would not only be necessary to show that a consignment was criminal property, but also that, considering the question objectively, the consignment had been purchased for significantly less than its value or by some other measure for consideration which was not adequate*".

The gravamen of a business selling goods manufactured using forced labour is the "use" of cheaper garments to increase profit-margins for the business. The adequacy of consideration is then determined by s.329(3)(b): by reference to the value of the use or possession of the property to the purchaser. A jury might readily conclude that the value of the consideration paid for garments manufactured using slave labour was significantly less than the value of the use or possession of those garments to the business if there was a substantial disparity between the unit cost of manufacture and the profit from each unit sale.

By way of example, if I sell a shirt for £30 in the UK and it costs me £2 to manufacture cheaply but legitimately in Thailand and £1 to sell, the value of the "use" or "possession" of the shirt to my business is the potential gross profit, namely £27. Given the large disparity between the cost of manufacture and the gross profit derived from using the product in my business, a jury might consider £2 to be inadequate consideration applying the test in s.329(3)(b), particularly if workers at the factory were paid below a living wage, but no offence would be committed as the garment was not criminal property.

Assuming all other things are equal, if I instead pay £1 for the shirt to be manufactured in Thailand using slave labour and sell it for £30 in the UK, I have reduced my unit costs by £1 and thereby increased my gross profit by £1 per shirt. A jury might still consider that I had paid inadequate consideration, but this time an offence had been committed (subject to the requisite *mens rea*) because the garment was criminal property. This approach to the calculation of "value" to the business for the purpose of s.329(3)(b) of the *Proceeds of Crime Act 2002* levels the commercial playing-field

regarding the use of modern slavery in supply chains, and helps to eradicate modern slavery from supply chains by placing a proportionate compliance obligation on companies who seek to drive down their manufacturing costs.

Is suspicion / knowledge of criminal conduct still required?

Yes. Dove J emphasised that the prosecution had to prove the requisite *mens rea*. Currently for corporate liability, this would require proof that the directing will and mind at least suspected that the garments had been manufactured using slave labour. As stated in **Hogan**, the inadequacy of the consideration might be very relevant to proving the requisite suspicion, as might other red flags such as geo-political risks. The International Labour Report 2021 highlighted that the global manufacturing industry was particularly susceptible to the use of forced labour and the US Department of Labor has identified forced labour risks regarding garments produced in China, India, Malaysia, Thailand, Vietnam, North Korea, Nepal, Malaysia and Taiwan.

How difficult are these offences to prove?

On the evidence presented, Dove J agreed that the matter didn't come close to requiring the Defendants to commence an investigation. What was required was "*a concrete allegation of modern slavery*". But that is not to say that modern slavery in overseas supply chains is impossible to prove. Not only does the judgment refer to the NCA's International Liaison Office in Beijing, the Modern Slavery Tactical Advisors Team and the Modern Slavery Intelligence Development Team but s.81 of the *Health and Care Act 2021* legislates for the government's aim of eradicating the use of goods or services tainted by slavery and human trafficking from the NHS supply chain. The Explanatory Notes to that Act confirm this is particularly targeted at goods produced in the Region. The government clearly envisages being able to identify specific consignments of goods made using forced or slave labour, albeit the Defendants were entitled to rely on the inherent unlikelihood of China co-operating with requests for overseas assistance when declining to investigate further the allegations in this claim.

Dove J. concluded by referring to the fact that the Defendants continue to be "*troubled*" by the matters raised in this case, which are the subject of active policy work and

engagement. It was also emphasised that the claim failed because the "*legal tools alighted on by the Claimant*" had been properly understood by the Defendants, but that there may be "*other tools or measures available to the executive and law enforcement agencies which could provide an effective basis for tackling the issues raised*". In other words, this is an area of developing enforcement policy.

Is there a wider context?

S.1 of the 1897 Act should be contrasted with far more proactive legislation in the US, the *Uyghur Forced Labour Prevention Act 2021* (which bans imports from the Region except where the importer can rebut a presumption that all goods originating there are made with forced labour) and, separately, s.307 of the *US Tariff Act of 1930*, which provides a broader approach to that in the 1897 Act:

> "*All goods, wares, articles, and merchandise, mined, produced, or manufactured wholly or in part in any foreign country by convict labor or/and forced labor or/and indentured labor under penal sanctions shall not be entitled to entry at any of the ports of the United States, and the importation thereof is hereby prohibited...*"

Dove J referred to the high threshold in s.1 of the 1897 Act, which only applies to goods manufactured in foreign prisons and not to goods manufactured using forced or slave labour. Given the issue of modern slavery remains on the NCA's and HMRC's enforcement radar, Parliament should now consider introducing similar legislation to that implemented in the US.

More generally, the law relating to criminal conduct in overseas supply chains is becoming increasingly complex. From a compliance and white-collar crime perspective, many of the issues discussed in the judgment are relevant to other conduct in supply chains capable of amounting to money-laundering offences by companies and individuals in the UK. Although the discussion in this case focused on criminality contrary to s.1 of the *Modern Slavery Act 2015* and s.51 of the *International Criminal Court Act 2001,* the principles can be extrapolated to other crimes relevant to overseas supply chains, particularly environmental crimes such as illegal deforestation, illegal land grabs and illegal mineral mining, all of which would

potentially render resulting products used in the supply chain “criminal property”. Environmental crime is now big business; the Financial Action Task Force report in June 2021 highlighted that it generates between US$110 billion – US$281 billion globally per annum with most of these proceeds infiltrating international financial systems.

The government is already legislating to regulate supply chain misconduct. For example, Schedule 17 of the *Environment Act 2021* prohibits a regulated person from using forest risk commodities in their commercial activities – goods such as leather, beef, cocoa, palm oil or rubber produced as a result of illegal deforestation – and it remains to be seen whether the Secretary of State will yet use secondary legislation to criminalise such conduct by a regulated person. Placing illegally logged timber products on the market is already an offence, covered by *The Timber and Timber Products (Placing on the Market) Regulations 2013*. The EU is also ramping up legislation efforts in this area, including the *Sustainability and Due Diligence Directive* that requires human rights and environmental due diligence in supply chains under pain of penalty, and impacts on certain UK companies that do business within its trading bloc.

This claim considered by Dove J. reflects an attempt to compel action against companies and individuals involved in poor business practices, and represents a growing trend amongst NGO’s, investors and shareholders to litigate ESG issues in supply chains to plug gaps in perceived failings by regulators and enforcement authorities. The government has committed to relevant targets and dates for compliance with a range of objectives: s.1 of the *Climate Act 2008* requires achievement of “net zero” by 2050; the target date for achievement of the Sustainable Development Goals amongst the UN signatories is 2030 and Target 8.7 aims to eradicate modern slavery and child labour by that date; the 6th EU Anti-Money Laundering Directive now specifically includes “environmental crime” as a predicate criminal offence for money-laundering purposes (the UK has stated that it does not need to sign-up to the Directive as its laws are already broadly compliant). But without accountability these targets and objectives are unlikely to be achieved.

The issue of corporate liability for economic crime is high on the white-collar criminal lawyer's radar, given the recent indications that the government is considering the introduction of a "failure to prevent" offence relating to certain economic crimes including money-laundering, as well as reform of the identification doctrine in relation to these crimes. Should amendments to the *Economic Crime and Corporate Transparency Bill* be made, companies may well find themselves more readily liable for money-laundering offences relating to overseas conduct in their supply chains. This case marks an early warning bell.

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