



THE PROCEEDS OF CRIME ACT 2002 AND RESTRAINT OF ASSETS

A BRIEF GUIDE TO THIRD PARTY OWNERS OF ASSETS UNDER RESTRAINT

Henry Stevens, Guildhall Chambers

1. *The Proceeds Of Crime Act 2002* is the last in a scheme of statutory interventions¹ arising from political and social pressure, not merely to punish offenders but to physically remove the fruits of their criminality. The upshot of this doctrine is that third party victims of the criminal fraudster may often find their assets frozen under the prerogative of the Crown, whilst the criminal is investigated, and before a final confiscation order is made.
2. POCA and its predecessors are aimed at directly confronting crime through the use of confiscation - not as an adjunct, but as means in itself of defeating organised crime². The statute is draconian in application with little scope for judicial discretion in favour of the accused.
3. Under s.6 of the 2002 Act the Crown Court is under a duty to make a confiscation order upon conviction and upon request by the prosecutor, but that duty must also be read subject to s.6(6):

6) But the court must treat the duty in subsection (5) as a power if it believes that any victim of the conduct has at any time started or intends to start proceedings against the defendant in respect of loss, injury or damage sustained in connection with the conduct.

Restraint Orders

4. Many victims of criminal fraud are unaware of the investigation of the criminal (or for that matter the fraud) until after conviction or restraint of the fraudster's assets. Under Sections 40 to 47 of POCA 2002 applications can be made by the prosecuting authority for 'Restraint Orders' - *ex parte*, in writing, to a Crown Court Judge.
5. There are five conditions for the making of a Restraint Order, of which the most common are:
 - **s40(2)** – a criminal investigation has been started & there is reasonable cause to believe that the alleged offender has benefited ...
 - **s40(3)** – proceedings for an offence have been started but not concluded & there is reasonable cause to believe that the defendant has benefited ...

¹ The need for a law to divest criminals of the benefits of crime became evident after the 1979 drug trafficking case 'Operation Julie'. £750,000 worth of drug trafficking proceeds were traced and held following conviction (*R v Cuthbertson* [1981] AC 470) but in the House of Lords it was ruled that however unfortunate the fact, the assets had to be released to the accounts of convicts serving substantial sentences, because there was no statutory authority authorising further restraint of those assets. In that instance because the criminals had been convicted of inchoate offences and confiscation was sought under the substantive provisions of the *Misuse of Drugs Act 1971* there were no grounds under which to confiscate the assets. Thereafter the *Drug Trafficking Offences Act 1986* was enacted, followed by *The Drug Trafficking Act 1994* and subsequently:

- ❖ Criminal Justice Acts 1988 and 1993
- ❖ The Proceeds of Crime Act 1995
- ❖ The Proceeds of Crime Act 2002

² The greater part of the active confiscation regime now exists under the 2002 Act but there remain jurisdictional matters relating to the date of the commission of offence. For our purposes February 24th 2003 is the start date for most matters. Offences pre-dating that period are then referable to the 1994 Act or the 1988 CJA. There are still some commencement issues and the date of the offence rather than the date of detection will determine which regime is used.



6. Under s.41, if any condition under s.40 is satisfied then the Crown Court may make a restraint order applicable to all realisable property, whether transferred to D, or the recipient of a tainted gift, before or after the date of the order.
7. Once assets are under restraint they may not be used or dissipated without order of the court. Section 41(4), makes it clear that there is no provision under a Restraint Order to allow for legal fees for D's defence in the offence under investigation, or proceedings connected with it, and there is provision for public funding in such circumstances
8. A frequent problem arises where a Defendant subject to a restraint order owes a debt to a third party. Can the third party get hold of his property? There is scope for the varying of a restraint order, allowing the defrauded creditor to lay claim to some of the assets under restraint. However the victim needs first to show that s/he has an interest in the property.

The Legislative Steer

9. Under s.69(2) of the 2002 Act the Court must protect the **value** of assets for the purposes of confiscation, viz:

(2) The powers –

(a) must be exercised with a view to the value for the time being of realisable property being made available (by the property's realisation) for satisfying any confiscation order that has been or may be made against the defendant;

(b) must be exercised, in a case where a confiscation order has not been made, with a view to securing that there is no diminution in the value of realisable property;

(c) must be exercised without taking account of any obligation of the defendant or a recipient of a tainted gift if the obligation conflicts with the object of satisfying any confiscation order that has been or may be made against the defendant;

(d) may be exercised in respect of a debt owed by the Crown.

10. However the so-called 'legislative steer' towards the protection of all assets for confiscation is implemented subject to the rules in s.69 (3) -

(3) Subsection (2) has effect subject to the following rules –

*(a) the powers must be exercised with a view to allowing a person other than the defendant or a recipient of a tainted gift to retain or recover the **value** of any interest held by him;*

*(b) in the case of realisable property held by a recipient of a tainted gift, the powers must be exercised with a view to realising no more than the **value** for the time being of the gift;*

(c) in a case where a confiscation order has not been made against the defendant, property must not be sold if the court so orders under subsection (4).



11. Thus it is clear from s.69(3)(a) of the 2002 Act that a restraint order may be varied or discharged where a third party can demonstrate an interest in the property under restraint, and at the very least the value of such property must be preserved, as it should not form part of the available amount when the confiscation order is made.
12. For the purposes of both of the above sections it is helpful to examine what the nature of the property interest is under s.84 of the 2002 Act.

Property: general provisions

(1) Property is all property wherever situated and includes –

(a) money;

(b) all forms of real or personal property;

(c) things in action and other intangible or incorporeal property.

(2) The following rules apply in relation to property –

(a) property is held by a person if he holds an interest in it;

...

(f) references to an interest, in relation to land in England and Wales

or Northern Ireland, are to any legal estate or equitable interest or

power;

...

(h) references to an interest, in relation to property other than land, in -

clude references to a right (including a right to possession).

Unsecured vs Secured Creditors

13. It is easier to get a restraint order varied to permit the payment of a secured creditor as opposed to an unsecured creditor. In *X v Customs* [2004] EWHC 861 (Admin.) it was held that a third party creditor could be paid from restrained assets, despite the fact that there would be less available for the confiscation order, because he held a legitimate secured interest in the restrained assets. Similarly under the s.82(4) CJA 1988 (now s.69(3)(a) POCA), in the case of *Re K* [1990] 2 W.L.R. 1224 it was held by the High Court that a restraint order could not prevent a Bank from exercising its common law rights of combination and set off to reduce an account in credit and under restraint where another balance held by the defendant was in considerable arrears.
14. A 'secured' creditor (in the context of restraint orders) means a creditor who has an 'interest' in the restrained assets. 'Interest' is widely defined under the legislation and includes both legal and equitable interests. The following examples illustrate persons treated as 'secured' creditors.

14.1. A person who has an interest (legal or equitable) in property held by the defendant. An example would be the interest held by the spouse of the defendant in the marital home (At the restraint stage the Court will require some evidence that the assets of a thirds party fall to be restrained.).



14.2. A victim of the defendant's conduct who can show that he has an interest in the restrained assets. The simplest example is where a defendant steals property which is subsequently restrained. The victim plainly has an 'interest' in the stolen property. There may also be a possibility of tracing into restrained property.

Unsecured Creditors: Proceeds of Crime Act 2002

15. An unsecured creditor is any creditor who does not have an 'interest' in the restrained assets. This evidently includes legal as well as equitable interest.

16. The Crown Court is required to apply some thought to anticipating the nature of the confiscation order that will be made. Thus the Court needs to consider the likely nature of the confiscation before considering any application to release assets. If there are sufficient assets to satisfy an anticipated confiscation **and** the required variation then it may be made. Otherwise, the variation should not be made.

17. The Court of Appeal has held that restraint orders should not ordinarily be varied to permit payments to unsecured creditors. In *Director of the Serious Fraud Office v Lexi Holdings plc (in administration) and another* [2009] 2 WLR 905, it was stated that:

'unless there is no conflict with the object of satisfying any confiscation order that has been or may be made, a restraint order should not be varied so as to allow for the payment of a debt to an unsecured creditor'.

18. In *Lexi*, the criminal Defendant under restraint was a surveyor who had received substantial bribes from a corrupt director of Lexi Holdings plc. Those bribes were amongst assets restrained by the Crown Court.

18.1. Lexi Holdings, now in administration, had commenced proceedings in the Chancery Division against its former director for breach of fiduciary duty and orders were obtained against the surveyor as a knowing recipient of the funds and a constructive trustee. In due course default judgment was entered against the surveyor and an attempt was made to enforce judgment by seeking an interim charging order over a house and third party debt orders against the surveyor's bank accounts.

18.2. Lexi Holdings sought leave to vary the restraint orders in the Central Criminal Court in order to permit enforcement of the judgment against the Defendant. Judgment was awarded in its favour and was appealed by the Director of the SFO.

18.3. The Appellant objected to the variation of the restraint order on the basis that the form of order obtained against the surveyor had been in personam (although a proprietary remedy had originally been pleaded in the alternative), and therefore Lexi could not demonstrate the requisite proprietary interest in the money under s.69(3).

19. In *Lexi* the Court of Appeal was guided by the fact that unsecured debts owed by the defendant are ignored at the confiscation stage. As stated at paragraph 81:

We can see no reason why Parliament should have decided to allow unsecured creditors to reduce the assets during the restraint phase when such creditors could not reduce the assets at the confiscation stage. If that were the position, it would put a premium on well-advised creditors getting in quickly during the restraint phase before their opportunity is lost, and we do not accept that that situation is one which was ever intended.

20. It was the Court's view in *Lexi* that payments to unsecured third party creditors from assets under restraint would be inconsistent with the position at the confiscation order stage. Moreover, the potential 'harshness' to innocent third parties was 'to some extent softened' by two mitigating features of the legislation.



20.1. A restraint order is a temporary measure (paragraph 84).

20.2. Third party creditors who are also victims of the defendant's conduct are protected by the legislation in that they should ultimately recover the debt owed to them, either by way of a compensation order or, if they issue a civil claim against the defendant, via the mechanism of section 6(6) which permits the court to reduce the amount of the confiscation order in order to preserve sufficient assets to meet the civil claim.

21. Critically however, in *Lexi*, the Company maintained its right to variation of the restraining order because it could indicate a quasi-proprietary right arising from an equitable charge over goods held on constructive trust, The Court of Appeal agreed, stating at para 39:

As made clear by Lord Millett in Foskett v McKeown, an in personam claim against a defaulting trustee may be supplemented in addition by a claim to enforce an equitable charge or lien over the proceeds in which the misappropriated assets have been mixed. That is an available remedy to secure compliance by the trustee with his personal obligation to account.

22. Thus, where the victim can show that the property was obtained from him fraudulently, it will be held on trust, or if it has been applied to other property it will carry his interest as an equitable charge or lien, in which case it is capable of forming the basis for the variation of a restraint order. In those circumstances it may well be the case that the best course of action would be to commence civil proceedings, rather than wait for the conclusion of the criminal proceedings. On the basis that the final confiscation order will be made with reference to any civil judgment obtained by a victim there seems little logic in preventing a victim justified by order of a civil court from obtaining his money at the restraint stage.

23. A victim of fraud who is not able to trace his funds into a fund under restraint may still be entitled to compensation under s.130 of the *Powers of Criminal Courts Sentencing Act 2000* (cf s.6 POCA 2000), so long as sentencing has not yet occurred. It should be noted however that that remedy may well be limited to only those creditors who suffered losses because of the offence or offences for which the Defendant is convicted or because of other offences taken into consideration.

**Henry Stevens
Guildhall Chambers
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