5 SAH
FIVE ST ANDREW'S HILL
+44 (0) 207 332 5400

What happens when assets are tainted: financial remedies v confiscation proceedings revisited - Sarah Wood for FLJ

15 SEPTEMBER 2021

Sarah Wood

What happens when assets are tainted: financial remedies v confiscation proceedings revisited - Sarah Wood writes for Family Law Journal - [2021] FAM LAW 1064

In my 2019 article '***Financial Remedies v Confiscation Proceedings: What Takes Priority*** ?' (FLJ [2019] Vol 49 pages 941 to 945) I explored the question of whether confiscation proceedings in the Crown Court pursuant to the Proceeds of Crime Act 2002 ('POCA') ought to take priority over a spouse's claim for financial remedies in the Family Court and examined the case law that surrounds how this complex, and increasingly common question should be answered.

Main themes from the case law in the Family Law context

The one clear theme that emerges from the case law is clear, namely that neither claim should automatically be regarded as having a priority over the other. Upholding the decision of the judge at first instance, the Court of Appeal in *Re MCA; HM Customs and Excise Commissioners and Long v A and A; A v A (Long Intervening) ('Customs and Excise v A')* [2002] EWCA Civ 1309 held that there was nothing in the Drug Trafficking Act 1994 (one of the precursors to POCA), public policy or the authorities that demonstrated that the Court's jurisdiction to make a property transfer order from a defendant pursuant to MCA 1973 was suspended or ousted by the DTA. This was confirmed in *Crown Prosecution Service v Richards* [2006] EWCA Civ 849, [2006] 2 FLR 1220 and *Stodgell v Stodgell* [2009] EWCA Civ 243, [2009] 2 FLR 244.

The other clear theme that has emerged from the case law is that, whilst neither claim can automatically be viewed as taking priority, when the Family Court is being asked to exercise its section 25 discretion and distribute assets between the parties, if it is clear that the assets available for distribution are tainted and that the innocent party knew of the underlying criminality, then the Judge ought not to exercise his section 25 discretion in favour of the innocent spouse but, instead, ought to exclude those assets from the value of the marital pot that is to be distributed so that they may be 'ring-fenced' and treated as available assets of the Defendant within the confiscation proceedings.

A quick review of the relevant case-law underlines this theme. In *Customs and Excise v A,* a Receiver had been appointed under section 29(2) of the DTA 1994 in respect of the Defendant Husband's assets, save for the interest in the former matrimonial home that was jointly owned with his wife and the surrender value of two life insurance policies securing the mortgage on the property. Customs and Excise applied for the Receiver to be appointed over the entirety of the house and the Husband's interest in the policies and asked that the Receiver be empowered to take possession of and sell the house to realise the Husband's interest in it. As this was a claim brought under the previous legislation, a High Court Judge was able to hear both the application for the Receiver brought by Customs and Excise and the application for a MCA order. The Court rejected the application on behalf of Customs and Excise, having found that none of the equity in the property derived from the proceeds of drug trafficking and

that the Wife had no knowledge of the offending. The Court exercised its discretion within section 25 and ordered that the house and policies be transferred to the Wife.

A case at the other end of the spectrum is *Crown Prosecution Service v Richards*. In this case the parties owned four properties. With the exception of a 13.3% beneficial interest in one of the properties that had been gifted from the Wife's parents, the remainder derived from the proceeds of drug trafficking – with the Wife's knowledge. At first instance the High Court (this, again, being an application under the DTA) exercised its discretion within section 25 in favour of the Wife. That was then overturned on appeal, with Thorpe LJ observing at paragraph 26 that:

> *"where assets are tainted and subject to confiscation they should ordinarily, as a matter of justice and public policy, not be distributed".*

For an application of the same principles in relation to an application made under POCA, as opposed to the previous regimes, the case of *Webber v Webber* [2006] EWHC 2893 provides useful guidance. It also assists in emphasising the difference between the procedure under the previous confiscation legislation when a High Court Judge could hear both competing claims at the same time. In *Webber* the financial remedies proceedings were transferred to the High Court from Basingstoke Family Court. A consent order was agreed (without the knowledge of the CPS) that the matter should be dealt with by a Judge with experience of both sets of proceedings. That consent order was overturned by Sir Mark Potter, President of the Family Division at the time, on the basis that it was of no application to a POCA confiscation application as all aspects of those proceedings are dealt with by the Crown Court. It was conceded within those proceedings that the Wife's interest was not tainted and that she was entitled to 50% of the equity in the FMH, and so it was agreed between all parties that the Family Proceedings should take place first to enable the Crown Court subsequently to assess the Husband's available amount for the purposes of confiscation.

However, whilst the theme from these three leading authorities makes it plain that any Family Court considering exercising its section 25 discretion must have regard to the question of taint and knowledge, it is worth highlighting that the absence of those factors may not always be

sufficient – as the case of *Stodgell v Stodgell* [2009] EWCA 243 demonstrates. In this case the Husband was convicted of fraudulently evading income tax. A confiscation order was made in the sum of £900,453, comprising £531,000 in unpaid tax plus penalties of £368,000. It was agreed that the Wife had no knowledge of her Husband's criminality. The Wife had no proprietary interest in the properties and so sought an order in the Family Court based upon the discretion within MCA section 25. Notably the Wife also argued that the proceedings should be heard in advance of the Husband applying the assets to satisfy his confiscation order. The Family Court refused that application. The Wife unsuccessfully appealed that decision. In refusing leave to appeal the Court of Appeal found that the Wife's lack of knowledge was insufficient in the circumstances of this case. Nor was it critical that the properties had not been obtained from crime. Instead, the important factor was that the asset base available for distribution had only been accumulated due to the non-payment of tax and penalties, which could have been recovered by the Revenue in civil proceedings. Similarly, the Court of Appeal found that the Wife's concession that HMRC could have bankrupted the Husband was fatal to the claim. The case of *Stodgell* is, clearly, a fact-specific case and would not apply where, for example, the marital assets had been acquired through drug trafficking, but practitioners ought to be aware of it in case they are faced with a similar factual scenario.

Practical application of the legal principles

If there is a suggestion that the assets are tainted and/or the Wife knew of the criminality, then inevitably the CPS will apply to intervene in the Family Proceedings in order to protect the assets for confiscation in due course. Parties to the Family Proceedings ought to be made aware that if a POCA restraint order has been granted in the Crown Court to protect the assets for future confiscation (akin to a freezing order in the Family Courts) then sections 58(5) and (6) of POCA make it plain that any Court dealing with those same assets is obliged to hear from the CPS before either staying the proceedings or allowing them to continue. In those circumstances the CPS may therefore apply both to intervene in the Family Proceedings and that they be stayed until the conclusion of the confiscation proceedings. If the application for a stay is refused and the Family Court decides to embark upon a preliminary fact-finding enquiry to establish the extent of the tainted assets and the innocent spouse's knowledge, then the Court should be invited to set directions in line with those commended by Munby J in *W v H and HMRC* [2004] EWHC 526 (Fam/Admin). These directions allow for the provision of

the documents served in the Family Court to the CPS and for each party to serve narrative statements dealing with both their beneficial interest in any property and the scope of any financial remedy claim. In turn the statement from the CPS should set out whether the claims of each party are accepted, whether the assets are derived from criminal knowledge and the innocent party's knowledge of the criminality. If the CPS wish to utilise material served as part of the confiscation proceedings, then it will need to comply with the provisions of Criminal Procedure Rule 33.8 before doing so.

The relevance and importance of sections 58(5) and (6) of POCA ought not to be overlooked by parties who are contemplating agreeing a consent order in advance of any confiscation proceedings. As the Court of Appeal made plain within the postscript of *SFO v Lexi Holdings* [2008] EWCA 1443 at paragraphs 93 and 94, it is the obligation of all practitioners to be aware of these provisions:

> *"The other procedural matter which has caused us concern derives from s.58(5) and (6), the terms of which we have set out earlier at [14]. Those provisions require any court in which proceedings are pending in respect of any property, in respect of which a restraint order has been made or applied for, to give an opportunity to be heard to the applicant for the restraint order (i.e. the Crown in some manifestation) and to any receiver appointed under the 2002 Act, and to do so before it decides whether or not to stay the proceedings or to allow them to continue. Those provisions clearly applied to the proceedings brought by Lexi against M in the Chancery Division. We have been told that, although some of the judges dealing with those proceedings were made aware that a restraint order was in existence, their attention was never drawn to s.58 of the 2002 Act. It should have been. One consequence was that the SFO did not seek to intervene in the Chancery proceedings.*

> *We entirely accept that the reason why s.58 was not drawn to the attention of those judges was because counsel appearing then for Lexi was himself unaware of it. It was an innocent oversight. Nonetheless, steps do need to be taken to ensure that the terms of s.58 are observed. Some thought might usefully be given to the possibility of creating a register of restraint orders and applications for such orders, though that would not have cured the problem in the present case, since all involved were aware of the existence of the restraint order. The SFO and other prosecuting authorities could usefully publicise more widely the general tenor of s.58, to increase the awareness of it in the legal profession, and no doubt the relevant Bar Associations could also play a role. In addition, judges themselves should be alerted to its significance, perhaps through the training provided by the Judicial Studies Board. This is not just a matter for the criminal courts and criminal lawyers: the duty under s.58 applies to all courts in which proceedings about such property take place, and very often those will be the civil courts. We shall direct that a copy of this judgment, together with a note drawing attention to this postscript, be sent to the Chairman of the Judicial Studies Board and to the Family and Civil Procedure Rules Committees."*

It is not difficult to envisage circumstances in which the parties may seek to agree a consent order without notifying the CPS of their intentions and in circumstances in which the existence of the Restraint Order was not brought to the attention of the Court. Given that the CPS would, inevitably, be alerted to any attempt to implement the agreed order given the existence of the restraint order, any agreement reached in this way could prove to be a costly attempt to short-circuit matters and risks an application to set aside on the basis of material non-disclosure.

It is also not difficult to foresee that there will be cases in which the convicted party within the Family Proceedings may choose to deliberately not engage with those proceedings with a view to ensuring that the innocent wife receives the majority of the assets, as opposed to the state. As Wall LJ noted at paragraph 101 of *Customs and Excise v A*:

> *"There can be no question of the 1973 Act being used as a means to circumvent the provisions of the 1994 Act, and I am confident that the judges will be acutely alert to ensure that this is not the case".*

It follows that in cases where there is no suggestion of taint or knowledge, the CPS may still apply to intervene in the financial proceedings if they consider that there is the possibility of a sham divorce or a deliberate attempt to circumvent the confiscation regime. In those circumstances the CPS may simply seek to ensure that the Court exercises its section 25 discretion appropriately. The fact that any assets distributed to the convicted party may, ultimately, be confiscated is not a factor that weighs in favour of an increased award to the innocent party.

Section 10A determinations under POCA

As my previous article highlighted, Family practitioners should be aware that Section 10A of POCA allows for the Court to determine the Defendant's interest in an asset that a third party also has an interest in. This section was introduced by the Serious Crime Act 2015 and has been the subject of a series of important Court of Appeal decisions within the last twelve months. In straight-forward cases where a Husband and Wife are joint tenants of a property and are not contemplating divorce proceedings, Section 10A can be used to enable a Court to find that the Wife holds a 50% equitable interest in the property. Section 10A(3) makes it clear that any determination made pursuant to Section 10A is then binding for the purposes of any subsequent application for the appointment of an Enforcement Receiver in which the Court might have to determine the respective interests in a property.

The explanatory notes to the Serious Crime Act 2015 (and, in particular, note 21) made it clear that the Crown Court should only make a determination as to the extent of third-party interests in 'relatively straight-forward cases' and 'without too much difficulty'. It is this aspect that has been the subject of some of the more recent Court of Appeal cases on this section.

In the case of *R v Hilton* [2020] UKSC 29 the Supreme Court considered the equivalent provision in Northern Ireland, section 160A of POCA. In that case a confiscation order was made without the Judge seemingly being made aware of section 160A, or the interest of Ms

Hilton's partner in a property. In considering the scope of section 160A the Supreme Court observed that the Court of Appeal's ruling was premised on the basis that in every case where third-party interests arise, section 160A should be engaged. The Supreme Court disagreed with that observation, noting that:

> *"The enactment of the section was designed to streamline the system, not to complicate it. In my view, its purpose was to combine the confiscation and enforcement stages in simple cases where there could be no sensible debate about how the confiscation order should be enforced".*

In the subsequent case of *R v Forte* [2020] EWCA Crim 1455 the Court of Appeal didn't entirely agree with the ruling of the Supreme Court in *Hilton*. Instead, it stated that if the real issue in the confiscation proceedings is the third party's interest, then it may be convenient to deal with it at the confiscation stage even if it is a significant issue. In this case, the asset concerned was the matrimonial home. It was registered in the Wife's sole name and she asserted sole beneficial ownership of it. The Defendant and the Wife were divorced but, notably, there was no application or order for financial relief, it being the Prosecution's case that the divorce proceedings were a sham. The Court of Appeal upheld the Crown Court's decision and found that, given it was matrimonial property and the sham nature of the divorce, the Wife held the property on trust for the Defendant and that therefore he held a 50% interest in it that was available for confiscation.

In the case of *R v Bevan* [2021] 4 WLR 19 there was no dispute that the beneficial interest in the matrimonial home was held in equal shares. However, the mortgage had been partly redeemed (in the sum of £140,000) using the proceeds of the Defendant's criminality. The Crown Court determined that the Wife was only entitled to half of the equity, after the £140,000 had been deducted. The basis of that decision was that it was unfair and against public policy to permit the Wife to enjoy the fruits of her Husband's criminality, which is the theme that runs through the relevant case law when considering applications for financial remedies in these sorts of cases. However, the Court of Appeal rejected this approach and found that it was contrary to the decision in *RCPO v Gibson* [2009] 2 WLR 471. The Court observed that, absent any tainted gift provision, there was no statutory or other provision that

could alter the beneficial interest in a property. That, of course, is the distinction between decisions of a Crown Court made pursuant to Section 10A and MCA applications.

Tainted Gifts within POCA

Family practitioners will be at ease with the sort of proprietary and trust arguments that are often considered by Crown Court Judges as part of any Section 10A argument. What may be a little more alien are the determinations and arguments that are made in respect of the tainted gift provisions within POCA. A finding that property has been gifted to a third party as a tainted gift within confiscation proceedings means that the Court can include the value of that gift within a calculation of a Defendant's available amount that then forms the basis of a confiscation order. The statutory purpose is, perhaps, obvious. It is designed to ensure that Defendant's can't evade the confiscation regime by simply transferring their property to third parties.

Of note is the fact that the Prosecution may seek to utilise the tainted gift provisions in respect of the beneficial interest held by within the matrimonial home. Indeed, that would have been an option available to the Prosecution in the case of *Bevan* which the Court of Appeal observed within its judgment.

A Defendant makes a tainted gift to a third party if he transfers his legal and beneficial interest in an asset to a third party for no consideration. If the Crown Court has found that a Defendant has what is known as a criminal lifestyle then any gift is considered to be tainted if it was made by the Defendant at any time after a six-year period before the commencement of the proceedings – known as the relevant date. Alternatively, if the Defendant gifts property which is the proceeds of crime then that may amount to a tainted gift. If the Crown Court has determined that a Defendant does not have a criminal lifestyle then a gift is tainted at any time after the earliest date of the commission of the offence.

The case of *R v Hayes* [2018] 2 Cr App R (S) 27 is a notable case in considering the question of tainted gifts within a marital context. The family home in this case was purchased solely with the Defendant's funds (not all of which could be said to the proceeds of crime) and was purchased in the joint names of the Defendant and his wife. The Prosecution case was that

the Wife's half share in the property was a tainted gift. It was argued on behalf of the Wife that her providing a familial service of bringing up the child amounted to consideration for the purposes of section 78(1). In giving the judgment of the Court of Appeal, Davis LJ considered in detail cases of this type. He stated that consideration must have a value that is capable of being assessed in monetary terms, and that there must be a nexus between the consideration and the gift. He concluded that the familial service provided by the wife was incapable of monetary assessment and that, therefore, the gift was tainted. The case was followed in a subsequent Court of Appeal decision in *R v Cracknell* [2020] EWCA 132 where the Court was considering an application under section 22 of POCA to increase the available amount.

Conclusions

The conclusions of the Court of Appeal in these cases may seem unfathomable to Family practitioners who are used to the established principles that a contribution to a marriage can be made in both financial and non-financial terms, and that the Family Courts are well equipped to assess whether those different contributions are matched by either side. The approach of the Crown Courts is plainly at odds with the balancing exercise frequently undertaken by the Family Court.

The residual question that remains is what would happen in any subsequent financial remedies proceedings if the Crown Court had previously determined that the equity in the family home was held by the innocent party as a tainted gift? This is unlikely to be straight-forward but would, ultimately, depend upon whether the gift was tainted because it was made from the proceeds of crime or whether it was simply tainted by virtue of the fact that it was made within the relevant statutory time-period following the Court's assessment that a Defendant had a criminal lifestyle. If the latter, then the asset ought still to be available for distribution within the family proceedings; with the Defendant then being able to apply back to the Crown Court to reduce the available amount pursuant to POCA section 23. If the former, then any distribution is unlikely; particularly if the CPS (as interveners) are also able to establish that the innocent party knew of the criminality.

***Sarah Wood** is an experienced and highly accomplished practitioner who specialises in criminal and family matters involving high-value assets and complex financial arrangements. She is one of a handful of counsel at the Bar with experience of dealing with cases where there are contemporaneous proceedings in the criminal and family courts in relation to the same assets. She is ranked in The Legal 500 and Chambers & Partners for her POCA work and for her financial crime private prosecutions work.*