ICC FraudNet
Global Annual Report 2023

FRAUD AND ASSET RECOVERY IN AN UNSTABLE WORLD

EDITED BY
DR DOMINIC THOMAS-JAMES

ICC FraudNet

ICC FraudNet Global Annual Report 2023
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The ICC FraudNet Global Annual Report 2023 is made up of individually-authored articles. The views expressed in these articles do not represent the views of ICC FraudNet, ICC Commercial Crime Services, the International Chamber of Commerce, or the Editor, and are the individual author's own views.

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ICC FraudNet

ABOUT ICC FRAUDNET

ICC FraudNet is an international network of independent lawyers who are the leading civil asset recovery specialists in each country. Using sophisticated investigation and forensic tools and cutting-edge civil procedures, FraudNet members have recovered billions of dollars for victims of some of the world's largest and most sophisticated global frauds involving insurance, commodities, banking, grand corruption and bankruptcy/insolvency. FraudNet was founded in 2004 and operates under the auspices of the Commercial Crime Services of the International Chambers of Commerce (ICC) – a Paris-based world business organization with offices in 90 countries.

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Acknowledgments

The Editor wishes to acknowledge the following people who have been of instrumental assistance and valued support in the publication of the third ICC FraudNet Global Annual Report. Peter Lowe, Executive Secretary of ICC FraudNet, has provided, as usual, steadfast support and ongoing enthusiasm for this initiative. His guidance has been most valued throughout this publication. ICC FraudNet's Co-Executive Directors, Kate McMahon and Rodrigo Callejas, have given considerable support during the preparation of this report. The authors of the 2023 are owed significant thanks, for it is their thought leadership and expertise which shines through the papers contained in this compendium and makes this publication the true research and practical resource that it is. Indeed, many FraudNet members have worked with co-authors in the writing of their papers, which has contributed greatly to the quality of the insights provided. FraudNet's Members and Strategic Partners have contributed en masse, and the turnout of such relevant and topical papers in this publication is nothing short of impressive. As a practitioner and academic, working closely with such a group of practitioners in the compilation of this publication has been a privilege. The Editor also wishes to acknowledge the assistance received by Members' and Strategic Partners' colleagues and staff. Their support of the authors during the editorial process has been of great assistance to the editorial team. Thanks also to Priya Jethwa, FraudNet's Director of Marketing and Communications, for her promotional efforts – ensuring that this Report has meaningful global reach within and beyond ICC FraudNet's network. Gratitude also goes to all ICC Commercial Crime Services and FraudNet staff for their ongoing support in making this publication possible.

Executive Directors' Foreword

Kate McMahon &
Rodrigo Callejas

June 2023

Kate McMahon

Rodrigo Callejas

Greetings readers,
It gives us great pleasure to present the ICC FraudNet Third Global Annual Report. This report serves as a reminder that fraud and commercial crime continues to be a significant and growing threat in today's business landscape. It also highlights the invaluable work that ICC FraudNet is doing around the world to combat this issue.

ICC FraudNet is a global network of lawyers and strategic partners, based across 75 jurisdictions, who all specialise in fraud and asset recovery. Our members are experts in identifying and resolving complex fraud cases that span borders and jurisdictions. The network is a key player in the fight against fraud and has made great strides in recovering stolen assets and holding fraudsters accountable.

This year's report provides a comprehensive overview of the activities and achievements of ICC FraudNet during the past year. It showcases the network's accomplishments in key areas such as education, prevention, and recovery. It also highlights some of the challenges faced by the network in its efforts to combat fraud, including the rise of new and emerging technologies that have given fraudsters new avenues to carry out their crimes.

As the Co-Executive Directors of ICC FraudNet, we are proud of what our network has accomplished in the past year. Our network has worked hard to educate businesses and individuals about the risks of fraud and empower them to protect themselves. We have also successfully recovered millions of dollars in lost assets for victims of fraud around the world. Further, as the demand for specialised practitioners continues to grow globally, we have incorporated future generations of specialist lawyers into our network, through the ICC FraudNet Future initiative, which looks to continue developing our network that next year will celebrate its 20th anniversary!

We would like to thank all of our members for their dedication and hard work this past year. We would also like to express our gratitude to our strategic partners and supporters for their continued support of our mission.

We invite you to read this year's report and learn more about ICC FraudNet's efforts to combat fraud and protect businesses and individuals around the world. Together, we can make a difference in the fight against fraud.

Sincerely,
Kate McMahon and Rodrigo Callejas
Co-Executive Directors, ICC FraudNet

Editor's Summary

Dr Dominic Thomas-James

June 2023

Dr Dominic Thomas-James

The third edition of the ICC FraudNet Global Annual Report takes as its theme "Fraud and Asset Recovery in an Unstable World". The first and second Global Annual Reports (2021, 2022) were published during unprecedented times – both at the relative outset, and height, of the global Covid-19 health pandemic which has now, at the point of publication, been downgraded as such by the WHO. Yet, the global backdrop to the third annual Report is still beset by conflict, political instability and sustained economic uncertainty around the world. Underpinning this landscape is the sinister reality that fraud and associated acquisitive misconducts continue to thrive. The UK government, as an example, published in May 2023 its "Fraud Strategy" taking aim at reducing fraud by 10% on 2019 levels, by 2025. Indeed, at the time of writing legislation is currently making its way through the UK Parliament to create a corporate failure to prevent fraud offence. While fraud appears to be, if at least ostensibly, at the forefront of government agendas – the fact remains that fraud is complex, multifaceted, and even nebulous. With sustained uncertainty, one thing is certain: fraud continues to be the crime we are most likely to fall victim to, thereby making the 2023 ICC FraudNet Global Annual Report of timely importance.

The 2023 Report comprises original articles by FraudNet's unparalleled global network of leading fraud and asset recovery lawyers, strategic partners, and associated collaborators from the investigative, consulting, advisory and academic worlds. The papers herein represent a unique contribution of knowledge to increasingly pertinent issues that continue to be at the forefront of international agendas. Displaying the network's leading practices in the areas of fraud, asset recovery, insolvency, and investigations – the contributions exhibit expert insight from the authors' respective jurisdictions and practices.

The 2023 Report, building on the success of the first two editions, comprises 28 original articles authored by 52 contributors, from some 20 jurisdictions. Many of the network have been involved in some of the most high-profile and complex asset recovery cases, and their experience makes for highly interesting and instructive reading. Papers share experiences from all corners of the world, including the following jurisdictions: UK, USA, Ireland, Guernsey, Malta, Hungary, Spain, Poland, Guatemala, Panama, Argentina, the Cayman Islands, the British Virgin Islands, Ghana, South Africa, Singapore, Malaysia, India, Luxembourg, and Japan.

Against the aforesaid backdrop, the Report addresses a wide range of important and timely topics in the fraud and asset recovery space. For example, in the Members Insight section, the Report includes analysis on issues including new legislative developments in fraud and asset recovery cases in the US; proceeds of crime laws in Ghana; cyber-crime case reviews from Argentina; freezing orders in South Africa; fraud litigation in Malaysia; asset recovery in Panama; virtual-asset regulation in Poland; and crypto-related enforcement and awards in Spain.

Elsewhere in the Report, we see discussions and insights from FraudNet's Strategic Partners, as well as insights from academics and associated collaborators. Such discussions include the difference between evidence and intelligence in investigations; asset recovery tools in Ireland; civil recovery mechanisms such as Unexplained Wealth Orders in the UK; an analysis of the proposed corporate failure to prevent fraud offence; and developments in the psychology of fraud.

With a work of this kind, it is not possible to capture commentary on every possible issue of pertinence within our field; but rather the discussions in the papers reflect a wide range of interest areas, respective practices and perspectives of the distinguished authors. In deference to their various professional and academic disciplines, as well as differences in citation methods between jurisdictions, the editorial team has not attempted to impose a single style or form of citation.

These articles aim to provide informative, practically-relevant and instructive insights and therefore be of use to the wider FraudNet and International Chamber of Commerce network, Strategic Partners, professional collaborators and colleagues, existing and future clients, and those with a practical, policy or academic interest in these issues. At a time of increased global uncertainty, in order to advance integrity in our societies and systems, and to disrupt fraud and financial crime and repatriate ill-gotten gains, it has never been more important for practitioners and experts at the coalface to contribute their expertise, knowledge and thoughts to the debate. It is only with greater understanding of best practices and individual experiences, that solutions can be shaped, and responses be developed. In this sense, ICC FraudNet's unparalleled international reach exhibits the utility of meaningful cooperation and collaboration. When fraud is increasingly transnational in nature, this is not only valuable, but essential.

Dr Dominic Thomas-James
Editor
ICC FraudNet Global Annual Report 2023

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STRATEGIC PARTNER INSIGHTS

ACADEMIC AND RESEARCH INSIGHT

AUTHORS

SEAN ANDERSON | Mintz Group

Sean Anderson is a director at the Mintz Group, heads the Mexico City office and works closely with the Mintz Group's Washington D.C. office. He works in our Latin American practice and has experience conducting complex litigation, integrity due diligence and asset tracing investigations. Sean has conducted numerous investigations throughout Latin America, with a particular emphasis on the infrastructure, energy and financial services sectors. Recently, he undertook comprehensive pre-deal investigations into companies in Honduras, Guatemala and Mexico, which uncovered ties to organized crime, large-scale tax fraud and money-laundering. Sean has also led internal investigations into contract fraud and bribery at a large mining company and undisclosed conflicts of interest leading to multimillion-dollar distressed loans at a multinational financial institution. He also manages cryptocurrency-related investigations on behalf of clients involved in multimillion-dollar lawsuits. Sean is fluent in English, Spanish and proficient in French.

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Réka Bali is an attorney-at-law at Forgó, Damjanovic and Partners Law Firm. She is specialised in litigation and commercial law. She works on several complex litigation cases which require comprehensive approach and deep understanding both of law and practice in the area of commercial relations. She has extensive experience in fake president fraud cases.

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Bobby Banson is the Founding Partner of Robert Smith Law Group, which is a boutique law firm located in Central Business District of Accra, Ghana. He heads the firm's practice areas focusing on Alternative Dispute Resolution, Investment Advice and Corporate Governance. He has acted as Counsel in both Domestic and International Arbitration matters. He has provided legal services to several multinational Companies doing business across the West African sub region; particularly in the area of due diligence of prospective investment opportunities. He has gained experience in wide areas of legal practice including Corporate, Investment, Real Estate and Dispute Resolution. He was educated at Adisadel

College, the Kwame Nkrumah University of Science and Technology (KNUST), Kumasi-Ghana for his Degree in Law (LLB) before proceeding to the Ghana School of Law in Accra-Ghana for his Professional Qualification in Law (BL) where he graduated as the best student in Law of Taxation. He has an LLM in International Business Law from the University of Brussels and a Certificate in Oil & Gas Contracting as well as a Certificate in Advanced Studies in Arbitration. He also has a Diploma in Financial Management. He has attended courses at the Harvard University, as well as the Africa International Legal Awareness (AILA) Conferences. As a Fellow of the Chartered Institute of Arbitrators (FCIARB), Mr. Banson has spoken at various conferences organized by CIArb. across the globe and AILA and participated extensively in SOAS conferences on Arbitration in Africa. He teaches Civil Procedure at the Ghana School of Law and has several legal articles published in his name. He is the author of the book "Civil Litigation in the High Court of Ghana".

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JOANNA BOGDAŃSKA | KW Kruk and Partners

Joanna Bogdańska is an Attorney at law, and Partner at KW Kruk and Partners Law Firm, Poland. Joanna provides comprehensive legal advice and represents clients in the field of broadly understood economic crime, corruption and fraud leading to exposing business entities to losses. Joanna participates in conducting audits, including due diligence of business partners, individual transactions and adopted procedures and solutions in terms of compliance thereof with the law. Additionally, Joanna specializes in transaction advisory, with particular focus on mergers and acquisitions. Advises in complex restructuring projects of companies, including mergers, transformations and divisions.

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DIANE BUGEJA | Camilleri Preziosi Advocates

Diane Bugeja practices primarily in financial services law, financial regulation and anti-money laundering regulation, providing advice to local and overseas clients on the impact of the current and forthcoming regulatory regime on their business models. Diane also advises clients on the regulatory aspects of a wide range of transactions, including licensing-related matters, capital markets initiatives and on-going liaison with regulatory authorities more broadly. Diane joined the firm as an Associate in 2016 and was promoted to Senior Associate in January 2017. She was previously a risk and regulatory consultant at a Big Four audit firm, working in Malta and in London, and subsequently joined the enforcement departments of the UK and Maltese financial services regulators. Diane successfully completed her

PhD in Law in 2017 at King's College London. She is a visiting lecturer at the University of Malta and is regularly invited to speak at conferences and deliver seminars on various aspects of financial services law and financial crime.

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CHRISTOPHER N. CAMPONOVO | Drumcliffe Partners

Christopher N. Camponovo is Managing Director at Drumcliffe Partners. Chris has over 20 years of experience working in government and the private sector. He has held senior positions at the White House and U.S. State Department. Chris has spoken, written and published articles on a diverse range of topics, including U.S. foreign investment treaties, international human rights, and corporate ethics. He holds a JD from the University of California Los Angeles Law School, and a BA from UC San Diego.

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CALVIN CHRUSTIE | CRT Critical Risk Team

Calvin Chrustie is a senior partner and critical risk consultant, with a background in resolving critical risk for governments, corporations, families, and individuals. He has managed crises, security operations and complex investigations in Europe, the Middle East, Africa, the Americas, and Asia over the last three decades. Calvin is a former Royal Canadian Mounted Police senior operations officer and United Nations veteran. As a former Senior Ops Officer for Transnational Organized Crime within the RCMP, Calvin led complex international investigations and intelligence operations throughout the world. Calvin was Team Leader of Canada's 'International Negotiators Team', which specialized in negotiating with terrorist and transnational organized crime networks relative to kidnaps and extortions. He has led complex negotiations, representing C-suites, corporations, governments, and NGOs, navigating armed conflict, community conflicts, terrorists, cyber and hostage situations. He is a graduate of the FBI's and Scotland Yard's Hostage Negotiation Program. His experience includes working with Indigenous groups and other community groups. Calvin holds a BA in Justice and Law Enforcement, a second BA (Honors) in Law, an LLM in Dispute Resolution and Negotiations, and recently completed Harvard University's Executive Program for Cyber Security. Calvin was seconded to the Federal Government for several years to assist in managing numerous volatile disputes across Canada. This included being requested to advise and consult on other international intractable conflicts. After 33 years of exemplary service, he received the 2016 'International Police Award' from the Canadian Association of Police Chiefs for his work in transnational crime and crisis responses involving terrorist kidnaps. As a founder of the Critical Risk Team, he has been working with clients and enhancing their awareness of the

world's most acute and contemporary threat actors and activities. This includes building solutions and resilience through integrating expertise, technology, and global networks to support clients' needs. This includes focusing on threats and the changing threat activities clients face currently and in the coming years. He also possesses a significant international network of associates in the security and intelligence profession that are often part of the solutions CRT offers clients. He is currently a Director of the Steering Committee for *Project Seshat*, an NGO-based entity focused on building leadership capacity to meet the challenges of global conflict and its security issues facing Western democracies.

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TYLA LEE COERTZEN | Primerio

Tyla has assisted the Primerio team in various matters and has experience in matters relating to commercial and competition law, litigation, white-collar crime and regulatory work. Tyla completed her studies at the University of Pretoria and the University of the Witwatersrand. In addition to her practice areas, Tyla is a contributor to *Africanantitrust* and *Africanantifraud* and regularly assists the Primerio team with various advocacy initiatives.

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LUCÍA FILIPELLI COLLETTO | Durrieu Abogados

Lucía Filipelli Colletto graduated as a Lawyer with orientation in Criminal Law and Criminal Procedure Law in the University of Buenos Aires, and she obtained a Specialized Program in Criminal Law in the Universidad Torcuato Di Tella, Argentina. She was assigned as chair assistant of Professional Internship in Criminal Law class in the UBA. Currently, she is chair assistant in Criminal Law General Principles subject in the Universidad Nacional de Avellaneda (UNDAV – Argentina). Moreover, she is member of the Permanent Renewal of Criminal Doctrine Seminary in the University of Salvador, and member of the Research Project in Legal Sciences "Omisión impropia y trasgresión de normas (subyaentes al tipo penal) en la República Argentina." (USAL-CONICET – Argentina). She performs as editorial assistant in the Newspaper of Criminal Sciences from USAL. Besides, she published several articles about Criminal Law and Criminal Procedure Law and presented herself in different seminaries and academic conferences. She is part of the Estudio Durrieu team since May, 2022. Previouosly, she performed herself in Estudios Gottheil & Suriz and Privanza, and in the corporate field as an in-house Lawyer. Currently, she is member of the Colegio Público de Abogados de la Capital Federal and of the Colegio Público de Abogados de Avellaneda-Lanús.

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Michael-James Currie is Director of Primerio. Michael's expertise includes complex commercial litigation (including cross border) and dispute resolution before the superior courts including arbitration. Michael is an active member of the ICC's Fraudnet, the world's leading asset recovery group, Michael-James is well versed with the anti-corruption laws in Southern Africa as well as the UK Bribery Act and the Foreign Corrupt Practices Act. Michael-James' practice in this area includes conducting internal investigations, compliance, litigation and asset recovery. Mike currently serves as the International Bar Association Anti-Corruption Committee's regional representative for Africa.

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Gábor Damjanovic is co-managing partner of Forgó Damjanovic & Partners Law Firm. He heads the Dispute Resolution Practice Group and handles complex, high-value commercial court cases and arbitrations, as well as fraud cases; almost always with a cross-border element. Gábor is frequently nominated as an arbitrator, both as wing and chair and has represented clients/acted as arbitrator under a number of different institutional rules, as well as under the UNCITRAL rules. According to Legal 500: "Gábor Damjanovic stands out for his 'impressive practical knowledge in court cases and arbitration'". Gábor is also listed on the Arbitration Powerlist 2021 CEE published by the Legal 500.

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Edward H. Davis, Jr., a founding shareholder of Sequor Law, focuses his practice on the representation of individual, corporate and institutional victims of fraud throughout the world. Ed conducts financial fraud investigations, prosecutes civil claims for fraud and pursues misappropriated assets, having tracked such funds in jurisdictions across the globe, including Japan, the Bahamas, Latin America, Switzerland and Liechtenstein, among others. A highly recognized and sought-after leader in his field, Ed is a Certified Fraud Examiner, Inaugural Chair of the Asset Recovery Sub-Committee of the International Bar Association's Anti-Corruption Committee, and member of other distinguished boards and committees. Under his direction, Sequor Law has established itself as a leading member of the ICC Commercial Crimes Services FraudNet Network. Ed frequently lectures on financial fraud and corruption to groups ranging from one of the world's most prominent banks, to associations of certified public accountants and

investigative agencies. He also counsels clients in fraud response crises based on his experience handling high-profile cases, including the second-largest Ponzi scheme in world history. Ed also is noted for filing the first Chapter 15 bankruptcy petition in the state of Florida. Admitted to practice in Florida and before the United States District Courts for the Southern and Middle Districts of Florida and the 11th Circuit Court of Appeals, Ed is a Past Chair of the International Law Section for which he has served as the Chair, Chair-Elect, Secretary and Treasurer as well as on the Executive Council. He is the Founding Chair of its International Litigation and Arbitration Committee; a member of the Bankruptcy Bar of the Southern District of Florida, and a member of the American Bankruptcy Institute and the Florida International Bankers Association.

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Nick Dunne joined Walkers' Cayman Islands office in 2008 and is a Partner in the firm's top-tier Insolvency & Dispute Resolution Group. His practice focuses on major and complex international and cross-border commercial disputes and arbitrations with a particular interest in fraud and asset recovery. Nick frequently appears before the Grand Court and the Cayman Islands Court of Appeal, and also has experience of appeals to the Judicial Committee of the Privy Council. Nick has also been listed as a recommended lawyer in the leading independent legal directories, including Chambers Global, Legal 500 and Who's Who Legal.

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Kirt W. Gallatin is a Director at Drumcliffe Partners. His professional background focuses government, elections, and law. Prior to joining Drumcliffe, he serving as the Director of Policy for the U.S. Department of Commerce’s International Trade Administration. He has advised several Heads of State on pre- and post-election strategy, and practiced law, specializing in civil litigation. He holds a JD from Northwestern University Pritzker School of Law, and a BS from Florida Gulf Coast University.

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Robin Gist, Senior Associate, is an advocate in the dispute resolution and litigation group. He brings a unique mix of significant experience of both the private and public law spheres, including in regulatory and data protection matters. Robin works with both international and local clients on a broad breadth of contentious issues, regulatory matters and general advisory work, including private client and property matters. Robin is a director of the Institute of Law, Guernsey, a member of the Guernsey Bar Council and sits on the Tax Tribunal. Robin is Deputy Bâtonnier of the Guernsey Bar Council, and he also sits on the Tax on Real Property Tribunal. He has extensive experience of appearing in all the Bailiwick of Guernsey's courts, including the Court of Appeal.

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Carlos Santaló Goris is a lecturer at the European Institute of Public Administration (EIPA) in Luxembourg, with a specialisation in European Union (EU) law. During the course of his Ph.D. research at the University of Luxembourg, he also served as a research fellow at the Max Planck Institute in Luxembourg. At this institute, Carlos was involved in two EU-funded research projects focusing on the field of EU civil procedural law. Additionally, he holds a registration as a lawyer with the A Coruña Bar Association in Spain.

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John Greenfield is a Consultant in the dispute resolution and litigation group in Guernsey where he was previously senior partner. John undertakes the complete range of major litigation and advocacy work including asset tracing, multijurisdictional disputes and commercial and trust litigation. John has been counsel in many major litigation cases before the Royal Court of Guernsey and the Guernsey Court of Appeal and is one of the few Guernsey advocates to have appeared as counsel in the Privy Council. John was a member of the Committee that completely overhauled Guernsey's civil procedure in 2008 and is now part of the new review Committee in 2021. He has been the Guernsey member of the UK Fraud Advisory Panel since 2001.

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Craig Heschuk is Executive Vice President at Greylist Trace. Craig is a legal and management professional with 30 years' experience in commercial project development. He was admitted to the Canadian Bar Association in 1990. His career spans dozens of countries starting in the early 1990's when he was advising a major Canadian energy company on international projects. His subsequent experience includes 17 years living abroad with his family in Abu Dhabi, Singapore, Doha and Quito. His career has centered on corporate/commercial work, mainly in the development of major infrastructure projects in the energy, real estate and manufacturing sectors. Most notably he has acted as General Counsel to companies involved in upstream oil & gas development in South East Asia and utility-scale solar and wind power projects in Europe and elsewhere.

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Shreyas Jayasimha read law at the National Law School of India University and was a Chevening Scholar at the University of Warwick. He is the founding partner of Aarna Law LLP. He is currently serving as co-counsel for a state party in two significant investment treaty arbitrations. Shreyas advises clients including banks, financial institutions, non-banking financial companies and insolvency professionals on various issues, including assisting banks and asset recovery companies in India to recover wrongfully retained assets presently concealed abroad, or 'round tripped' back to India; issues in relation to cross-border insolvency, among other matters. Shreyas is the only India-based representative of ICC FraudNet, which formed the Asset Recovery Group India (ARGI) to pursue substantial-value cross-border asset recovery claims for Indian banks, asset reconstruction companies and other creditors. ARGI comprises specialist fraud and asset recovery lawyers from various jurisdictions who provide superior legal representation to financial institutions, corporations and individuals in asset tracing and recovery, securities litigation and arbitration.

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David Jones is a Partner and head of the restructuring and insolvency team in Guernsey. He advises on complex restructurings and formal insolvencies in contentious, non-contentious and multijurisdictional matters. David has been involved in many of the largest insolvencies involving Guernsey entities, ranging from investment funds to global retailers. He is able to assist lenders in respect of

the taking and enforcement of all forms of security. He regularly advises the boards of distressed entities and has extensive experience acting for office holders on all aspects of their appointments including the tracing and recovery of assets. David is a member of the Insolvency Lawyers Association and R3 and sits on the young members Committee of INSOL International. David lectures on INSOL's Foundation Certificate in International Insolvency and is part of the working group tasked with updating and revising Guernsey's insolvency laws. He has also been appointed as a member of Guernsey's first ever Insolvency Rules Committee (IRC).

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Hiroyuki Kanae focuses on corporate law, including mergers and acquisitions (domestic and international), corporate reorganizations, joint ventures, labor and employment law (including dispute settlements), corporate governance, IP license agreements, and real estate transactions. He also advises on commercial litigation matters, including domestic and cross-border litigations involving major Japanese and foreign companies. He represents major Japanese manufacturing companies, foreign financial institutions and high tech companies, as well as private equity funds. He has been advising on the global development projects mainly for the major Japanese companies investing in North America, Europe and Asia pacific regions and has more than 30 year experiences in the cross-border M&A. In recent years, he has completed M&As and joint ventures not only in Europe and the North America but also in Asian and pacific rim developing countries by collaborating with rich overseas networks in the areas of semi-conductor, high tech, nano-tech, aviation and space, pharmaceutical, medical equipment and software industries. Through experience of a member of the audit and supervisory board of a major logistic company that has been seeking the global strategy, he advises on the real need of management strategy foreseeing the post-merger integration.

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MARTIN KENNEY | Martin Kenney & Co (MKS)

Martin Kenney is one of the world's leading asset recovery lawyers, specialising in multi-jurisdictional economic crime and international serious fraud. He has acted for international banks, insurance companies, individual investors, and other private and governmental institutions. Based in the British Virgin Islands (BVI), Martin is founder and Head of Firm at Martin Kenney & Co (MKS). The firm's work lies at the intersection of cross-border insolvency, creditors 'rights and complex commercial litigation – *WIRED* has styled MKS as among "the world's sharpest fraudbusters". Leading a team of lawyers, investigators and forensic accountants,

Martin is widely regarded as a ground-breaker in the use of pre-emptive remedies, multi-disciplinary teams and professional litigation funding in response to global economic crime, uprooting bank secrets and freezing hidden assets in multiple jurisdictions. He is a practising solicitor advocate of the senior courts of England & Wales and the Eastern Caribbean at the BVI and at St Vincent & the Grenadines, and a licensed foreign legal consultant in the state of New York. He is also a Visiting Professor at the University of Central Lancashire School of Justice, and ranked among the world's leading asset recovery lawyers by Chambers and Partners, plus is a Who's Who Legal "global elite" Thought Leader.

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NATHALIE KER | Lim Chee Wee Partnership

Nathalie Ker is a partner in Lim Chee Wee Partnership. Her fraud and asset recovery practice includes high profile and complex fraud matters involving cross-border elements. She is well-versed in obtaining and executing search orders and freezing orders to secure evidence and assets, discovery orders against banks and other third parties, and other interim orders in aid of effective litigation. Nathalie is a founding committee member of the Thought Leaders 4 NextGen FIRE (Fraud, Insolvency, Recovery, Enforcement) Community.

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Matthias Kleinsasser, Of Counsel, is a member of Winstead's Business Litigation, White-Collar Defense, and Business Restructuring/Bankruptcy practice groups. He regularly represents officers, directors, and other clients involved in private securities litigation, as well as in investigations brought by regulatory agencies such as the Securities and Exchange Commission and the FDIC. Matthias diligently represents clients in almost any kind of contested matter, be it a state court receivership, class action, AAA arbitration, inverse condemnation suite, or other dispute. He also frequently advises firm transactional clients with respect to contract negotiations and business disputes, particularly in the technology and healthcare fields. Matthias has significant fraudulent transfer litigation experience. He has advised foreign clients on asset recovery procedures under US law, as well as represented debtors, creditors, and trustees in virtually all aspects of business bankruptcy proceedings, including contested asset sales and debtor-in-possession financing.

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The Price of Ice – Cross Undertakings In Damages In Mareva Injunctions

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The Price of Ice – Cross Undertakings In Damages In Mareva Injunctions


COLETTE WILKINS KC AND NICK DUNNE

Abstract

The Mareva injunction is a central feature of common law legal systems when dealing with asset recovery, but is not without risk for parties seeking relief. The potential exposure to damages in the event that an injunction is found to have been unjustified is an important tactical consideration, and this article summarises the key principles which courts will bear in mind in this regard.

Introduction

The "nuclear weapon" of the Mareva injunction is well known to asset recovery lawyers across the common law world and beyond. The ability to freeze both tangible and intangible assets worldwide is perhaps the single most useful tool available to ensure that judgments against wrongdoers translate into actual recoveries.

It can however sometimes be forgotten that a price is typically exacted for the grant of a Mareva injunction in the form of the cross-undertaking in damages, a promise to pay for any losses sustained by a respondent to the order if the injunction is later discharged. Potential exposures can be very large, particularly in the context of long-running litigation where commercial assets are frozen for a significant period of time.

As such, whilst plaintiffs are naturally apt to focus upon the potential fruits of success, the consequences of failure are ignored at their peril.

Damages

Whilst the undertaking is often referred to as the "price" of an injunction, and although almost every plaintiff will be required to give an undertaking[1], not every unsuccessful plaintiff will be liable to pay under it. Because the undertaking is given to the court as opposed to the counterparty, leave must be obtained for that undertaking to be enforced, which will not be granted unless the court considers that the injunction was wrongly granted, and a *prima facie* loss can be established.

That loss must also be a consequence of the injunction, as opposed to the mere existence of the litigation, or a particular ruling. Where such losses can be shown, the jurisdiction is compensatory, not punitive: its function is to make good losses as opposed to sanctioning the unsuccessful party for having obtained an injunction in the first place.

The correct approach to the award of damages was recently considered by the Privy Council in *Ennismore Fund Management Ltd v Fenris Consulting,*[2] on appeal from the Cayman Islands Court of Appeal. It was made clear that assertions from injuncted parties as to their losses will not be taken at face value – the ordinary principles of causation apply – and it is for the party claiming under the undertaking to prove its losses on balance of probabilities. On the facts of that case, an initial award of well over GBP £5 million based upon a claim that the injuncted funds would otherwise have been invested in a highly profitable way was ultimately revised downwards to a figure of slightly over GBP £500,000.

The calculation of damages can be an uncertain science, particularly where the damage arises from an inability to deploy funds, as it is not straightforward to answer the hypothetical question of what a party would have done with them had they been available. What is clear, however, from *Ennismore* is that claims under the undertaking do not amount to "open season" on an unsuccessful plaintiff: they must always be proved in a properly forensic and defensible way.

Mitigation

The fact that losses must be properly proved should not however distract from the fact that a party obtaining an injunction also accepts responsibility for its consequences, which may be very significant.

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[1] Undertakings are invariably required, even where there is no foreseeable prospect of loss at the time that the injunction is granted.
[2] [2022] UKPC 27

This is well illustrated by the English decision of *SCF Tankers v Privalov*[3], in which an argument that an injuncted party could and should have mitigated its loss by seeking variations of the injunction in order to allow it to conduct business and thus avoid its losses was roundly rejected by the Court of Appeal. In ordering a payment of over USD $70 million under an undertaking, it was held that regard should be had to the practical reality both of how difficult it might be to secure a substantial variation of an order whilst litigation was ongoing, and the commercial unlikelihood of a counterparty wishing to engage in transactions for which court approval was required.

A further example of that approach to mitigation of loss can also be seen the Cayman Islands case of *Sagicor General Insurance v Hurlstone*[4], where a party had taken legal advice as to the possibility of seeking to discharge an injunction, but having been advised that it would be a long and costly process, declined to do so. Although the Court considered the advice to be unduly pessimistic, there was no failure to mitigate losses: it was not unreasonable for a party to refrain from potentially expensive litigation on legal advice.

The practicality that underpins the grant of freezing injunctions is reflected by the courts' approach to the consequences of failure. The Mareva jurisdiction is firmly grounded in the real world, and just as it is accepted that fraudsters are liable to dissipate funds, so it is accepted that depriving a party of access to funds or property is likely to result in unavoidable losses. Technical arguments to the contrary may struggle to find favour, and plaintiffs can be exposed to very substantial liabilities.

Fortification

The utility of an undertaking in damages is entirely contingent upon the ability of the party providing it to pay in the event that it is called upon: a promise which cannot be kept amounts to no promise at all. As such, in some cases the undertaking alone will not suffice, and the court will require security for that undertaking in the form of a payment into court, known as "fortification".

A request for fortification is a potentially powerful weapon in the hands of a Defendant, as in the event that it is ordered and the Plaintiff cannot, or will not, pay, the likely consequence is that the injunction will fall away, which may be sufficient to defeat the claim altogether.

[3] [2017] EWCA Civ 1877
[4] [2011] 1 CILR 130

There is no right to fortification, it being a matter within the discretion of the Court. It has been reiterated recently[5] that the discretion will not be exercised unless a Defendant is able to provide credible evidence amounting to a good arguable case as to (i) risk of loss, (ii) that the loss in question would be caused by the injunction, and (iii) that the size of the loss can be intelligently estimated. In common with claims under the undertaking, it is not sufficient for a Defendant to speculate as to possible losses, or pluck numbers from the air, Courts are alive to the fact that fortification places a burden on a Plaintiff andfortification is likely to be ordered only where losses are both likely and identifiable, and where the party obtaining the injunction lacks assets within the jurisdiction to make good on any liability.

Although there is a challenging evidential threshold, the potential for fortification is an important consideration for any foreign Plaintiff seeking Mareva relief. This is particularly so where resources are limitedand a significant part of any war chest is required to be held as security for an undertaking rather than deployed in order to progress the litigation. That difficulty can be mitigated now that some litigation funders are willing to offer insurance as collateral for the purposes of fortification. However, parties minded to seek injunctions should be aware from the outset that a mere promise to pay may not be enough: they may also be required to put their money where their mouth is.

Conclusion

In the initial excitement of seeking Mareva relief, it can be easy to overlook the undertaking in damages and ignore its potential consequences, both in the event that the claim is unsuccessful or at an earlier stage through requests for fortification. As such, consideration of the undertaking should form a key part of any asset recovery strategy so as to avoid unpleasant surprises after an injunction is obtained. Prospective plaintiffs would be well advised to hope for the best, but plan for the worst.

[5] *Claimants listed in Schedule 1 v Spence and ors* [2022] EWCA Civ 500

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Dealing with the Proceeds of Crime in Ghana

Finding the Balance Between Unjust Enrichment and the Enforcement of Illegal Contracts

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Dealing With Proceeds of Crime In Ghana: Finding The Balance Between Unjust Enrichment And The Enforcement of Illegal Contracts

BOBBY BANSON[1]

ABSTRACT

This paper seeks to analyse the legal regime in Ghana relating to proceeds of crimes committed outside and which proceeds are brought into, received in or invested in Ghana. Sometimes, Parties to these illegal acts, may enter into contracts and arrangements for the distribution of the proceeds from their unlawful activities in another Country where the crime was not committed. Where there is a breach of such contracts, how would the court ensure that justice is achieved for all parties involved? We will discuss the position of the law in Ghana on such matter in the context of finding the balance between unjust enrichment and enforcement of contracts deemed to be illegal either in the country of execution or where the proceeds are brought into or both.

[1] The Author would like to thank and acknowledge the efforts of Vanessa S. Zormelo, Joseph Bondzie Afrifa, Antoinette Kyeremanteng, Afua A. Danquah, Kwame Appiah Oduro, Theophilus Boateng Osei and Isaac Adjei – all Law Students of the Ghana School of Law who spent their summer internship assisting with research for this article.

INTRODUCTION

With the advent of technology and digitisation, it has become ever easier to transfer money across countries. Unfortunately, the proceeds of crimes are often sent to countries other than where the crimes were committed by electronic and other means. There are also instances where the proceeds of an act considered as legal in the country of commission are sent to and/or invested in a country where said act is contrary to its legislation and public policy; or vice versa. Crimes of corruption or dishonesty may arise from private contractual arrangements between parties. Individuals involved in any such private arrangements found to be illegal are sometimes caught in the dilemma of recovering whatever consideration they may have given pursuant to such illegal contracts.

Recently, the Supreme Court of Ghana held that a woman was entitled to her share of the proceeds from prostitution which she undertook in Italy with the assistance of a man, and which proceeds had been invested in Ghana.[2] This article was inspired by the facts and ratio in that case.

In the proceeding parts of this article, the Author will discuss the existing legal regimes in Ghana on dealing with proceeds of crimes committed outside Ghana when the funds are brought into Ghana, and how persons may recover property or funds paid in consideration of contracts which are found to be crimes and illegal. In addition, the Author will discuss the provisions of the Criminal and Other Offences (Procedure) Act, 1960, the Economic and Organised Crime Act, 2010, the Office of Special Prosecutor Act, 2017 and case law, as well as the applicable Common Law provisions which are deemed to be part of the laws of Ghana by virtue of the provisions of the 1992 Constitution. This discussion will be situated in the context of finding the balance between unjust enrichment of a party to such illegal acts and the duty of the Courts in punishing illegal actions.

1. JURISDICTION OF GHANAIAN COURTS IN DEALING WITH CROSS BORDER ILLEGAL CONTRACTS

In this article, cross border illegal contracts refer to contracts:

i. Executed by Parties outside Ghana but to be performed in Ghana and which contract is found to be illegal for being in breach of statutes in Ghana.
ii. Executed by Parties outside Ghana and to be performed outside Ghana but which proceeds are brought into, received in, or invested in Ghana.

[2] See www.dennislawnews.com new item titled "Breach of Promise to marry: Supreme Court grants woman properties of her toil" published on 18th July 2022 at accessed on 13th October 2022.

Broadly, the jurisdiction of the Ghanaian Courts can be invoked in both criminal and civil actions.
For Civil actions, the 1992 Constitution provides the High Court of Ghana with original jurisdiction in all matters. For a foreigner to be able to institute a civil action in Ghana in respect of a contract which is found to be unlawful, the Defendant must be resident in Ghana, or the purported contract ought to have been executed in Ghana.

For criminal actions, Section 56 of the Courts Act, 1993 confers jurisdiction on the Ghanaian Courts in criminal matters where the offence is committed by a Citizen of Ghana or by a person who is resident in Ghana if the offence is wholly or partly committed in Ghana.

Hence, where persons execute a contract outside Ghana, which ought to be performed in Ghana, or the Defendant/Accused person is resident in Ghana, the jurisdiction of the Ghanaian Court may be invoked. This can be either by criminal proceedings instituted on behalf of the victim by the Office of the Attorney-General, or by civil proceedings commenced by the victim himself. Where the proceeds of the illegal contract are brought into or received in Ghana, the Ghanaian court will have jurisdiction to make a determination on the same.

2. ILLEGALITY OF CONTRACTS

A contract is an agreement between two or more parties creating obligations that are enforceable or otherwise recognizable at law.[3] The elements of a valid contract are namely: offer and acceptance, capacity to enter into the contract, consideration, and intention to create legal relations.

A contract may be treated as illegal for various reasons. It may be considered so because it contains an illegal promise and/or object. A contract may also be deemed illegal if a promise contained therein has been, or will be, performed illegally, though lawful.[4] The legality or otherwise of a contract is often determined by statute, public policy and/or morals.

Though the Courts do not ordinarily enforce illegal contracts, in the absence of a dominating public interest to invalidate an illegal contract, such a contract could be enforced if: (a) the party seeking the enforcement is less guilty than the other party; (b) the law was violated without any severe moral turpitude; (c) the other party would benefit unfairly from the contract voidance, and (d) the penalty would

[3] Black's Law Dictionary, 11th Edition
[4] George A. Strong, "The Enforceability of Illegal Contracts" (1961), 12 Hastings L.J. 347

be disproportionally harsh compared to the degree of illegality.[5] In such situations, the party seeking enforcement will likely obtain certain reliefs based on a quantum meruit basis and recover the justified value of the services or goods provided.[6]

2.1 Can Illegal Contracts executed or performed outside Ghana be Enforced in Ghana?

Every contractual agreement assumes that the parties will uphold their respective ends of the bargain and achieve the intended purpose of the agreement. However, there are instances where a valid contract would be rendered void or unenforceable by certain vitiating factors.

At common law, where a contract is illegal, property transferred or money paid under the contract is not recoverable, mainly when the Plaintiff's claim relies on the said illegality. This principle is captured in the Latin phrase, *"ex dolo malo non oritur actio",* stated by Lord Mansfield in *Holman v Johnson* [1775][7] and loosely translated as: "no court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act."

There are four known exceptions to the rule that money paid, or properties transferred, under an illegal contract are irrecoverable.[8] First, where the Plaintiff's claim is not founded on the illegal act. Thus, in *Schandorf v Zeini* [1976][9], the Court held as follows:

> *"For if the plaintiff can present his case for relief without necessarily disclosing or relying on the illegality, the cases show that the courts will not decline to assist him on the ground of his wrongdoing."*[10]

Second, where one party to an executory contract repents before performance. The said party, in this instance, is allowed a *locus poenitentiae.* That is, an opportunity to repent or change his mind.
Third, where the Plaintiff is not *in pari delicto* (equally guilty) with the Defendant. Finally, where the contract is prohibited by a class protecting statute, that is, where the party who is a member of the protected class is not regarded as *in pari delicto* with the other party.

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[5] UpCounsel, "An Illegal Contract: Everything you need to know", available at https://www.upcounsel.com/illegal-contract#is-the-contract-void-or-unenforceable-because-it-is-illegal accessed on September 6, 2022
[6] Ibid
[7] (1775) 1 Cowp 341
[8] Christine Dowuona-Hammond, "The Law of Contract in Ghana" (2011), Frontiers Printing & Publishing, Accra, Ghana
[9] [1976] 2 GLR 418
[10] Ibid, paragraph 37 at 435

In the case of *Agbeko v Standard Electric Company* [1978][11], it was held that:

> *"The position at common law was that, considerations of illegality and public policy apart, where money was paid by the Plaintiff to the Defendant in pursuance of a transaction thought to be a valid contract but which in form was devoid of effect in law, such money was recoverable in quasi-contract as money received by the Defendant to the use of the Plaintiff."*[12]

Further, the Supreme Court of Ghana, in the case of *City & Country Waste v Accra Metropolitan Assembly* [2007-2008][13], on enforcing illegal contracts, noted that a modern discretionary approach was necessary to ensure that justice would be rightly served. In that case, the Court held that since the Plaintiff was not aware of the illegality, the purpose of the rule rendering the contract illegal would not be defeated if the Plaintiff was awarded "*some compensation at a rate below the contract rate for the services rendered to the Defendant*."[14]

It is important to note that the Court held, in addition to the above, that the Plaintiff's claim for restitution was distinct from the illegal contract.

Notably, the Supreme Court's decision in the *City & Country Waste*[15] case has, to a large extent, made some advancement in finding a balance between unjust enrichment of parties and enforcement of illegal contracts in Ghana.

Hence, it is submitted that under the current legal regime in Ghana, where Parties execute a contract outside Ghana for the discharge of obligations in Ghana, the contract may be rendered a nullity if the same is found to be at variance with public policy and/or statute in Ghana. However, if a Party has received money in consideration of discharging an obligation under the said illegal contract, the other party may recover the money paid if that other party is able to prove that he was not aware of the illegality of the transaction.

2.2 Proceeds of Crime and the Concept of Equitable Tracing

[11] [1978] GLR 432
[12] Ibid, holding 1 at 432; paragraph 20 at 438
[13] [2007-2008] SGCLR 409
[14] Ibid, paragraph 33 at 424
[15] Ibid

'Proceeds of Crime' or 'proceeds' refers to any property or economic advantage derived from or obtained directly or indirectly through unlawful activity, and includes economic gains from the property and property converted or transformed, in full or in part, into other property.[16] Proceeds from crime may arise from private contracts (e.g. for corrupt actions) or from dishonest receipt of funds. It is accepted and practised in many legal jurisdictions that a criminal (or dishonest person) should not be allowed to benefit from his criminal or dishonest activity. However, it is not always easy to identify whether or not said material gain was acquired through crime. Proceeds of crime are easily determined when they are directly obtained from crime. For example, in countries where prostitution is a criminal offence, monies paid to a prostitute for her services are direct proceeds of crime.

On the other hand, proceeds of crime are not easily ascertainable when they are indirectly obtained from crime. For example, properties bought with money obtained from crime can be proved to be proceeds of crime only if it can be shown that the money acquired from the criminal activity is what was used to acquire the property. It also becomes difficult to ascertain proceeds of crime when they become mixed with other properties owned by the individual.

How, then, can a proceed of crime be established? There should be a causal link between the criminal activity and the economic advantage or asset to show that the economic advantage or asset was acquired through crime. In the case of *NDPP v Salie and Another* [2014][17], the High Court of South Africa had to decide whether or not the property in question was qualified to be proceeds of crime. In this case, the National Director of Public Prosecutions had made an application against the Respondents for the forfeiture of property allegedly obtained by keeping a brothel and living off its earnings, contrary to the Sexual Offences Act 23 of 1957 of South Africa. The Respondents first admitted that it was known that the massage parlours were being used for sexual services, but later denied this. The Court therein held that there was no evidence that either of the Respondents had any income from legitimate sources and the money used to repay their debts was sourced from the three brothel businesses they ran. Therefore, the properties in question were proceeds of crime and would be forfeited.

Although the properties were not directly obtained from the commission of the offences, the Court was able to identify a close connection between the property and the commission of the offences.

[16] Anti-Money Laundering Act, 2020 (Act 1044), s 63
[17] [2014] 2 All SA 688 (WCC)

Due to the difficulty in tracing mixed funds, the principle of equitable tracing was created to ensure that individuals do not forfeit their lawful assets. Per Lord Millett in *Foskett v McKeown* [2000][18]:

> *"Tracing is neither a claim nor a remedy. It is merely a process by which a claimant demonstrates what has happened to his property, identifies its proceeds and the persons who have handled or received them, and justifies his claim that the proceeds can properly be regarded as representing his property."*[19]

In the words of Lord Ellenborough, CJ, in *Taylor v Plumer* [1815][20]:

> *"… the product of or substitute for the original thing still follows the nature of the thing itself, as long as it can be ascertained to be such, and the right only ceases when the means of ascertainment fail, which is the case when the subject is turned into money, and mixed and confounded in a general mass of the same description."*[21]

The equitable principle of tracing of proceeds of illegal contract has received judicial pronouncement in Ghana. In the case of *Owusu and Others v Agyei and Others* [1980][22], it was held that:

> *"Furthermore, through the equitable principle of the constructive trust and the mechanism of tracing, a man could be forced to disgorge property in his possession which belonged to another person."*[23]

3.3 Dealing with Proceeds of Crime in Ghana

In Ghana, every person has the right to own property either alone or in association with others.[24] Does this right permit an individual to enjoy property acquired from the proceeds of a crime? For the purposes of this discussion, the most applicable crimes will be a crime involving dishonesty which may arise in contractual dealings between private persons and/or the crime of a private person corrupting a

[18] [2000] 3 All ER 97 at 120
[19] Ibid, paragraph 6
[20] (1815) [K.B.] All ER 167 *(Reprint: 1814-1823)*
[21] Ibid, paragraph 9 at 171
[22] [1980] GLR 1
[23] Ibid, holding 1 at 3; paragraph 86 at 37
[24] 1992 Constitution of Ghana, Article 18(1)

government official. These crimes may arise from contracts executed between the parties involved.

There are laws which have been enacted to recover money or properties acquired by an individual from crime. These laws create institutions which are empowered to confiscate such assets for the State. There are other statutory provisions which require that the proceeds from the crime may be returned to the victim of the crime. In this part of the article, we will discuss some of these statutory provisions:

- The **Economic and Organised Crime Office Act, 2010 (Act 804)** establishes the Economic and Organised Crime Office (EOCO) and has as one of its functions, the recovery of crime proceeds.[25] The office also has the power to seize any property upon the reasonable suspicion that the property was acquired from the proceeds of a crime.[26]

- The **Office of the Special Prosecutor Act, 2017 (Act 959)**, the purpose of which is to recover and manage proceeds of corruption and corruption related activities.[27] This law establishes the Office of Special Prosecutor which has the power to seize any property upon suspicion that the property was acquired from the proceeds of corruption or corruption related offences.[28]

- The provisions of the **Criminal and Other Offences (Procedure) Act, 1960 (Act 30)** are more instructive. For the purpose of emphasis, the relevant provisions will be reproduced verbatim:

  Section 146—Restitution of Property Stolen, Etc.
  "Where any person is convicted of having stolen or having obtained any property fraudulently or by false pretences, the Court convicting him may order that the property or a part thereof be restored to the person who appears to it to be entitled thereto."

  Section 147—Restriction Disposal of Property of Accused Person.
  "Where any money or other property in respect of which any person has been charged before a court with an offence involving dishonesty is in the custody or possession of a person other than the accused, the trial court of its motion or on the application of the prosecutor or the alleged victim of the offence or any other court on the application of the prosecutor or the alleged victim of the offence may

[25] Economic and Organised Crime Act, 2010 (Act 804), s 3(b)
[26] Ibid, s 24 (1)
[27] Office of Special Prosecutor Act, 2017 (Act 959), s 2(b) and 3(d)
[28] Ibid, s 32

order that the person in whose custody or possession the money or property is shall not part with or dispose of the money or property until otherwise directed by the Court."

Section 147A.—Payments of Money made by Accused Persons.
"(1) Where a person convicted of an offence involving dishonesty has, since the commission of the offence, made payments of money or transferred any property to any person, such payments or transfers shall be deemed to have been made out of the proceeds of the offence, and accordingly any court may, on the application of the prosecutor or the victim of the offence, order the person to whom the payments or transfers have been made to return the money or property to such person as may be specified by the court unless it is shown to the satisfaction of the court by the person in respect of whom the order has been made—

(a) that he gave valuable consideration commensurate to the payments, of money or transfers of property made to him, or;
(b) that he is a dependant of the person convicted and that the payments of money were his reasonable living expenses made to him as such dependant."

On reading these statutory provisions as a whole, one can safely conclude that where a crime arises from civil/contractual arrangements outside Ghana which are found to be illegal, institutions created with the obligation to investigate and prosecute these crimes may trace and seize these properties. In addition, a Court of competent jurisdiction may order that victims of such illegal acts are to be restituted with these properties.

From the foregoing, a person who acquires properties illegally will have his/her constitutional right to own the property curtailed.

3. THE "CURIOUS" CASE OF AMA SERWAA V. GARIBA HASHIMU[29]

In this 2021 decision, the Plaintiff alleged that the Defendant acquired the properties in Ghana, albeit in his name, with her earnings from prostitution in Italy, an undertaking she was engaged in with the assistance of the Defendant. The Plaintiff, thus proceeded to issue a writ of summons in Ghana to claim *inter alia* the following reliefs:

(1) General damages against the Defendant for breach of promise to marry.

[29] Civil Appeal No. J4/31/2020 with judgment dated 14th April, 2021

(2) Refund of loans to the tune of €20,000 from the Defendant with interest thereon from 2003 to date of payment.
(3) Half of the property located in two neighbourhoods, Madina and Adjirigano
(4) Half of the seven (7) machines brought in with the Plaintiff's money which have been in the custody of the Defendant as well as an account of proceeds from same to date.
(5) An order for her to be given her share of the proceeds from their criminal conduct.

The trial Court found the Defendant liable and entered judgment in favour of the Plaintiff. In delivering its judgment, the trial Court accepted the evidence of the Plaintiff that she acquired most of the properties they possessed from the act of prostitution. The trial Court took judicial notice of the fact that the act of prostitution is lucrative in Italy and the fact that the Plaintiff obtained a lot of resources while in such business is not exaggerated. The profession of the Defendant, on the other hand, was considered by the trial judge as not lucrative to purchase all the properties acquired within that space of time.

In addition, the trial Court stated that the Plaintiff having contributed to the properties should have a share of same. This was to prevent the Defendant from having the enjoyment of the properties to the exclusion of the Plaintiff. There were supportable documents evidencing that the properties in issue were acquired during the subsistence of the relationship between the parties although these relevant documents covering the properties were in the name of the Defendant.

The Defendant, dissatisfied with the judgment by the Trial Judge, filed an appeal at the Court of Appeal. The learned justices of the Court of Appeal in overturning the judgment of the trial Court, covered a number of reasons. For the purpose of this article, we will focus on the issue of the proceeds from the crime of prostitution and how same was dealt with by the Court of Appeal.

The Court of Appeal accepted the submission made by the Defendant that prostitution is a criminal offence in Ghana and for the trial Court to admit facts and evidence on proceeds of prostitution as the foundation of the Plaintiff's claim was erroneous in law. Relying on Section 40 of the Evidence Act, 1975 (NRCD 323) which provides that: *"The law of a foreign country is presumed to be the same as the law of Ghana",* the Court of Appeal concluded that the Plaintiff failed to prove that prostitution was a lawful business in Italy and that she was duly certified as a prostitute. Failing to do so, the presumption that the law of Italy on prostitution is the same as that of Ghana was inaccurate and the Plaintiff could not find an action based on illegality and adduce evidence to support same. The issue of the illegality of prostitution in Italy was a matter that went to the very jurisdiction of the trial Court and to the Court of Appeal, it was duty-bound to consider such a

fundamental issue. The appellate court also emphasized that by its judicial oath, it must uphold the Constitution and the laws of Ghana and not gloss over clear violations of the statute. Based on this reasoning, the Court of Appeal set aside the judgment of the High Court and concluded that the Plaintiff cannot be allowed to enjoy in Ghana, the fruits of illegal conduct in Italy.

The Plaintiff, piqued by the decision of the Court of Appeal, appealed to the Supreme Court. The Supreme Court set aside the judgment of the Court of Appeal and restored the judgment by the High Court Judge. The Supreme Court found that the Plaintiff sufficiently proved her claim for a half share of properties acquired in the name of Defendant during the period of their relationship. By means of evidence led at the trial Court, the Plaintiff contributed substantially to the acquisition of the property through her source of income made as a commercial sex worker in Italy. The Plaintiff therefore was deemed to have beneficial interest in the property though held in the name of the Defendant. The Defendant held the property merely as a trustee, that is constructive trustee, and the properties were intended for the benefit of both parties. There was sufficient understanding between the parties to demonstrate that they were preparing for a life together back home in Ghana, and thus the beneficial interest in the property should cover both parties. It was therefore reasonable for the Supreme Court to prevent the unjust enrichment of the Defendant through the sole retention of the properties. The Defendant being a constructive trustee of the properties was bound to allow the Plaintiff benefit from the proceeds of prostitution which took place in Italy. However, the fact that the prostitution was committed in Italy, did not deny the Court in Ghana jurisdiction to order the Plaintiff to receive her portion of the proceeds of the crime as long as the proceeds were invested in, or brought into, Ghana.

The Supreme Court thus concluded that the Defendant cannot be unjustly enriched or benefit from his wrong to the disadvantage of the Plaintiff. In addition, the Supreme Court set aside the conclusion reached by the Court of Appeal that the trial Court judge had the obligation to dismiss the entire claim on grounds of illegality and public policy. In its explanation, the Supreme Court stated that that the result of upholding the decision by the Court of Appeal will mean a person who acquires property by means of sexual immorality should not be allowed to keep it, but that one who was complicit in that immoral lifestyle was so morally superior that he had a better right to keep the “unclean property”.

4. CONCLUSION

The position of the law is clear that illegal contracts are generally unenforceable. However, where a case falls under any of the exceptions mentioned above, the Courts, judging from the Supreme Court's disposition in the *Ama Serwaa* case, may allow a party to recover such sums especially where this would prevent unjust enrichment of the other party.

From the foregoing discussions, it is the opinion of the author that the legal regime in Ghana ensures that persons who are parties to contracts found to be illegal are not unjustly enriched or allowed to benefit from their wrongs at the expense of the other Party. Either by means of criminal or civil conduct, the Courts in Ghana have demonstrated that unless otherwise dictated by law, they will enforce the terms of a contract, albeit illegal or unlawful, if the interest of justice in a given case dictates. The position of the Ghanaian Court should be a disincentive to persons who might be thinking of avoiding contractual obligations on the basis that the contract is illegal in Ghana; for to allow the enjoyment of proceeds from crime to the detriment of the other party involved in same, would offend public policy in Ghana.

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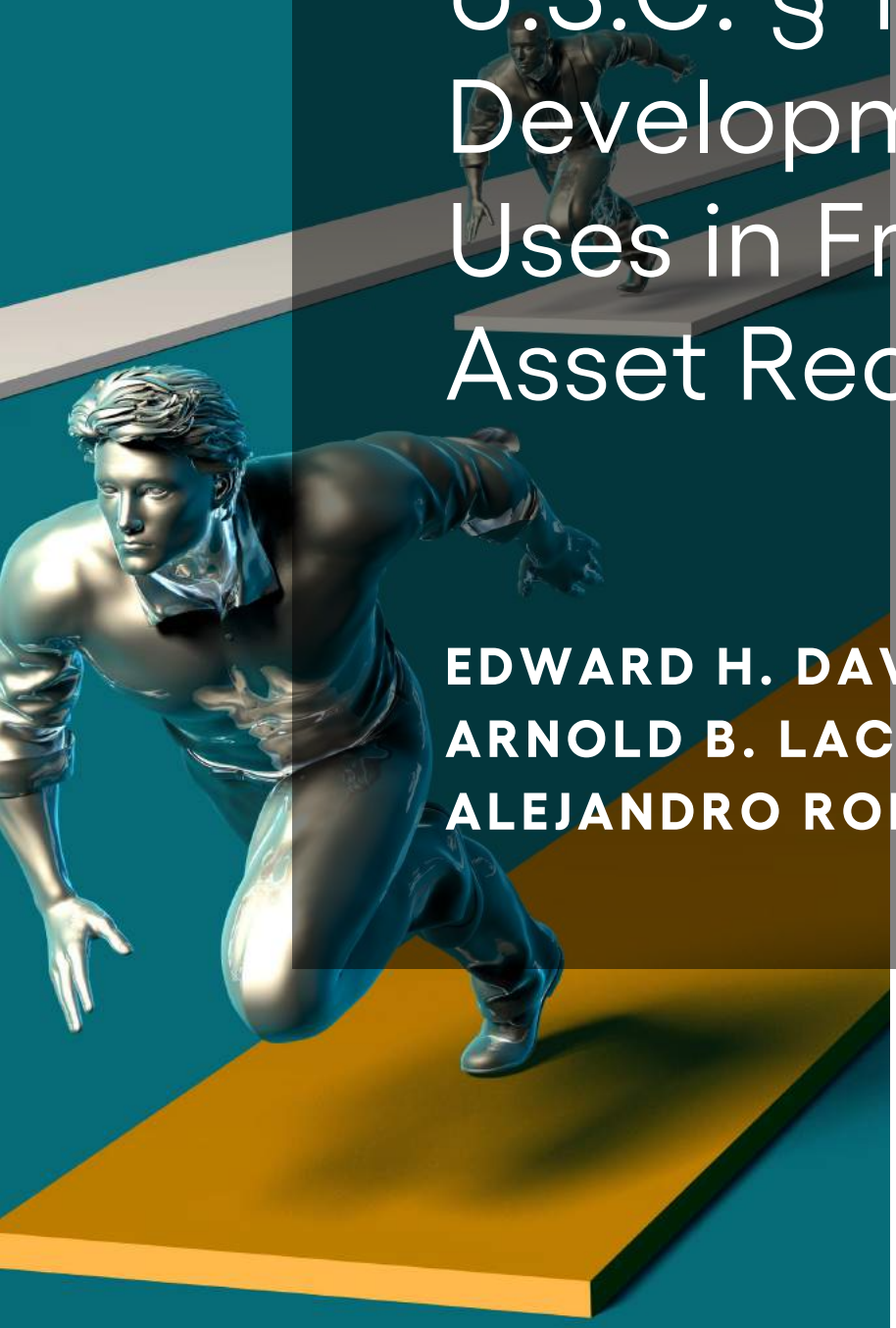
Chapter 15 and 28 U.S.C. § 1782: New Developments and Uses in Fraud and Asset Recovery cases



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Chapter 15 And 28 U.S.C. § 1782: New Developments and Uses in Fraud and Asset Recovery Cases

EDWARD H. DAVIS JR., ARNOLDO B. LACAYO, ALEJANDRO VANZETTI

Abstract

Cross-border litigation is ever evolving, particularly as to the use of insolvency and U.S.-style discovery as tools in fraud and asset recovery matters. The U.S. Supreme Court and circuit courts continue to weigh in on critical issues, such as the definition of a "debtor" in a Chapter 15 proceeding or the breadth of a "foreign or international proceeding" in a § 1782 Application. In this article, examine these and other recent developments, with the goal of educating litigators and encouraging the use of creative solutions and tools to facilitate the recovery of assets in cross-border proceedings.

CHAPTER 15

Overview

One of the goals of Chapter 15 proceedings is to foster uniformity in cross-border cases.[1] Foreign clients may wish to initiate a Chapter 15 proceeding to protect

[1] *Chapter 15 – Bankruptcy Basics: Ancillary and Other Cross-Border Cases*, U.S. COURTS (accessed on Feb. 15, 2022), https://www.uscourts.gov/services-forms/bankruptcy/bankruptcy-basics/chapter-15-bankruptcy-basics.

assets in the U.S. or to provide an avenue for an orderly repayment of creditors.[2] Regardless of the motivation, recognition of a foreign insolvency proceeding in the U.S. comes with several benefits: the debtor, through the Foreign Representative, may seek an automatic stay on execution of debtor's assets[3] as well as the examination of witnesses and taking of evidence under the broad latitude afforded in U.S. bankruptcy proceedings.[4] Above all, it allows a specialized bankruptcy court—including experienced judges—to oversee complex, cross-border insolvency proceedings.

A Chapter 15 petition requires identifying whether the debtor's foreign proceeding is considered a *foreign main proceeding* or a *foreign non-main proceeding*. A foreign main proceeding is one that is "pending in the country where the debtor has the center of its main interest."[5] Although a debtor's registered office is presumed to be the center of main interest, this is a rebuttable presumption,[6] and U.S. courts have considered a number of factors in making this determination, including: the location of the debtor's headquarters, the location of those who manage the debtor, and the location of the majority of the debtor's creditors, among others.[7] If the court recognizes the foreign proceeding as a foreign main proceeding, automatic relief is triggered, which includes a stay and enjoining actions against the debtor.[8] On the other hand, a foreign non-main proceeding is a foreign proceeding pending in a country where the debtor has an "establishment,"[9] which is "any place of operations where the debtor carries out a non-transitory economic activity."[10] If the court recognizes the foreign proceeding as a foreign non-main proceeding, it may (but is not required to) grant certain relief, including relief automatically available to a foreign main proceeding and discovery.[11]

Requirements for recognition as either a foreign main proceeding or foreign non-main proceeding are twofold. Procedurally, a petition for recognition of the foreign proceeding must be filed by the *foreign representative*: the foreign proceeding's representative appointed to administer the reorganization of the debtor's assets.[12] This includes providing the order commencing the foreign proceeding and appointing the foreign representative.[13] Substantively, the foreign proceeding

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[2] Leyza F. Blanco, *Inside the Minds: Challenging Aspects and Issues of Cross-Border Chapter 15 Filings*, ASPATORE BOOKS (2012).
[3] 11 U.S.C. §1519(a)(1).
[4] 11 U.S.C. §1521(a)(4).
[5] 11 U.S.C. § 1517(b)(1).
[6] 11 U.S.C. § 1516(c).
[7] *In re SPhinX, Ltd.*, 351 B.R. 103, 117 (Bankr. S.D.N.Y. 2006), *aff'd,* 371 B.R. 10 (S.D.N.Y. 2007).
[8] 11 U.S.C. §1519 (a)(1).
[9] 11 U.S.C. § 1517(b)(2).
[10] 11 U.S.C. § 1502(2).
[11] 11 U.S.C. § 1521.
[12] *See* 11 U.S.C. § 101(24).
[13] 11 U.S.C. § 1515(b)(1).

must be (1) a proceeding that is (2) judicial or administrative; (3) collective in nature; that is (4) pending in a foreign country and (5) related to insolvency or adjustment of debts; with (6) foreign court supervision; and in (7) liquidation or reorganization.[14]

Since its enactment in 2005, Chapter 15 of the U.S. Bankruptcy Code, based on the UNCITRAL Model Law on Cross-Border Insolvency, has proven to be an indispensable fraud-fighting and asset recovery tool. The contours of Chapter 15's reach continue to be defined in cases from around the world. The below touches on a selection of new developments that every cross-border insolvency practitioner should be aware of.

New Developments

In re Al Zawawi

Sequor Law represents the foreign representatives in a Chapter 15 proceeding currently before the Eleventh Circuit Court of Appeals.[15] The court will decide an issue of first impression in the circuit: whether "debtor," as defined under § 109(a) of the bankruptcy code, imposes a threshold requirement for Chapter 15 cases requiring that the foreign proceeding involve a "debtor" that fits the U.S. statutory definition. In *In re Al Zawawi*, 637 B.R. 663 (M.D. Fla. 2022), the debtor refused to pay his former wife £24 million following a divorce, so he was adjudged bankrupt under English law. The foreign representative sought discovery in the Middle District of Florida and filed a Chapter 15 petition, which was subsequently granted. On appeal, the debtor did not dispute that the foreign representative satisfied the requirements of § 1517; instead, he argued that the requirements of § 109(a)—that debtor reside or have a domicile, place of business, or property in the United States—was not satisfied. The connection between § 109(a) and Chapter 15 lies in § 103(a) of the U.S. Bankruptcy Code, which establishes that various chapters of the U.S. Bankruptcy Code are applicable to Chapter 15 cases.

The district court disagreed with debtor's argument and agreed with the bankruptcy court's assessment, basing its decision on the legislative history, Eleventh Circuit Court precedent, and comity: "[F]or a foreign representative, recognition serves as the door to much of our nation's judicial system. Limiting recognition to proceedings involving foreign debtors that qualify as "debtors"

[14] 11 U.S.C. § 101(23); *See also In re Global Cord Blood Corp.*, 2022 WL 17478530, *7 (Bankr. S.D.N.Y. Dec. 5, 2022).

[15] Sequor Law's cross-border insolvency practice has ample experience in filing and prosecuting Chapter 15 proceedings. The firm has filed over 70 petitions across several U.S. federal courts in aid of insolvency proceedings stemming from North and South America, the Caribbean, Europe, and Asia.

under the Bankruptcy Code is simply inconsistent with the express language and fundamental purpose of Chapter 15."[16]

The Eleventh Circuit's forthcoming decision on the issue may have significant implications in the field of cross-border insolvency. The decision may limit the relief available under Chapter 15 by incorporating § 109(a)'s definition of "debtor" to foreign debtors as a threshold requirement, or, may expand that relief by differentiating between a Chapter 15 "debtor" and "debtors" under Chapters 7 and 11.

In re Three Arrows Capital

Service of court documents abroad—necessary to initiate a lawsuit or to obtain discovery—is closely intertwined to Chapter 15 proceedings which are cross-border in scope by their very nature. Generally, in the U.S. federal courts, service of process abroad is governed by FRCP 4(f), while service of a subpoena abroad is governed by FRCP 45(b)(3). FRCP 4(f) has been recognized for its flexibility, such as providing a path to serve process via e-mail and social media.[17] However, service of a subpoena has generally been executed via more traditional means, such as hard copy delivery of the documents. But a recent Southern District of New York Bankruptcy Court decision discussed how FRCP 4 governing service of process may be "persuasive, if not controlling" to serving a subpoena abroad.[18] In *In re Three Arrows Cap., Ltd.*, 647 B.R. 440 (Bankr. S.D.N.Y. 2022), the debtor's cryptocurrency trading business collapsed, leading to the commencement of liquidation proceedings in the British Virgin Islands ("BVI"). The foreign representatives then filed a Chapter 15 petition, and the U.S. bankruptcy court entered an order granting recognition of the BVI bankruptcy as the foreign main proceeding. The foreign representatives subsequently issued eighteen subpoenas to banks and cryptocurrency exchanges, but the issue before the court was the service of subpoenas upon the debtor's two founders and investment managers. With no knowledge of the founders' whereabouts, the foreign representatives sought to serve them via alternative means: social media and e-mail. While one founder and the investment managers did not meet the territorial requirement of FRCP 45(b)(3),[19] the court did allow service of a subpoena on the other founder, a U.S. national residing in a foreign country, via the proposed alternative means. In granting the foreign representatives' request, the court agreed that FRCP 4's

[16] *In re Al Zawawi*, 637 B.R. 663, 670 (M.D. Fla. 2022).
[17] *See, e.g.*, *WhosHere, Inc. v. Orun*, No. 1:13-cv-00526-AJT-TRJ, 2014 WL 670817 (E.D. Va. Feb. 20, 2014) (authorizing service on an individual in Turkey by email and through Facebook and LinkedIn); *FTC v. PCCare247 Inc.*, No. 12 Civ. 7189(PAE), 2013 WL 841037 (S.D.N.Y. Mar. 7, 2013) (authorizing service on individuals in India by email and through Facebook).
[18] *In re Three Arrows Cap., Ltd.*, 647 B.R. 440, 456 (Bankr. S.D.N.Y. 2022).
[19] The requirement is that the targets be U.S. nationals or residents in a foreign country.

requirement that service be "reasonably calculated" to provide notice is instructive in the context of FRCP 45, as this standard "derives from the underlying due process requirement applicable under both rules."[20]

28 U.S.C. SECTION 1782

Overview

28 U.S.C. § 1782 ("§ 1782 Application") allows an interested party to seek U.S.-style discovery for use in proceeding before foreign or international tribunal. The seminal case *Intel Corp. v. Advanced Micro Devices, Inc.*, 542 U.S. 241 (2004) established the mandatory requirements that a § 1782 Application must meet: (1) the request must be made by a foreign or international tribunal, or by any interested person; (2) the request must seek evidence, whether it be the testimony or statement of a person or the production of a document or other thing; (3) the evidence must be for use in a proceeding in a foreign or international tribunal; and (4) the person from whom discovery is sought must reside or be found in the district of the district court ruling on the application for assistance. The case defined an "interested person" broadly to include litigants before the foreign or international tribunal as well as foreign and international officials and any person who has a reasonable interest in obtaining judicial assistance.

The court in *Intel Corp.* also analyzed certain discretionary factors that courts may consider in granting or denying judicial assistance under the statute: Whether "the person from whom discovery is sought is a participant in the foreign proceedings"; "[t]he nature of the foreign tribunal, the character of the proceedings underway abroad, and the receptivity of the foreign government or the court or agency abroad to U.S. federal-court judicial assistance"; "whether the § 1782(a) request conceals an attempt to circumvent foreign proof-gathering restrictions or other policies of a foreign country or the United States"; and whether the request is otherwise "unduly intrusive or burdensome."

While both the mandatory and discretionary factors have been heavily litigated since the *Intel Corp.* decision, the issue of whether the proceeding abroad constitutes a "foreign or international proceeding" was recently analyzed by the U.S. Supreme Court in a case that resolved a split among the U.S. Circuits Courts of Appeal.

New Developments

ZF Auto and its Nominal Progeny

[20] *In re Three Arrows Cap., Ltd.*, 647 B.R. 440, 456 (Bankr. S.D.N.Y. 2022).

In *ZF Auto. US, Inc. v. Luxshare, Ltd.*, 213 L. Ed. 2d 163, 142 S. Ct. 2078 (2022), the U.S. Supreme Court addressed the issue of whether an arbitration proceeding abroad constitutes a "foreign or international proceeding" under § 1782. Before *ZF Auto*, circuit courts disagreed on this issue with respect to private arbitral tribunals. The U.S. Supreme Court thus consolidated two cases—one involving a private arbitration and one involving an investor-state arbitration—to decide the issue.

In excluding the private and investor-state arbitration proceedings before it from the scope of "foreign or international proceedings" under § 1782, the court held that a "foreign tribunal" exercises governmental authority conferred by one nation, while an "international tribunal" exercises the same control conferred by two or more nations. However, the court accepted that the issue of investor-state arbitration is a closer question, stating that "sovereigns might imbue an ad hoc arbitration panel with official authority."[21]

Even though the *ZF Auto* decision is recent, district courts have already weighed in on the issue of whether an investor-state arbitration proceeding constitutes a "foreign or international proceeding." In *In re Alpene, Ltd.*, No. 21MC2547MKBRML, 2022 WL 15497008 (E.D.N.Y. Oct. 27, 2022), a magistrate judge in the District Court for the Eastern District of New York stayed a § 1782 Application filed by a Hong Kong corporation and claimant in an investor-state arbitration against the Republic of Malta. This particular arbitration took place before the World Bank's International Centre for the Settlement of Investment Disputes ("ICSID"). The court's inquiry centered on whether Malta and China (the treaty parties) intended to "imbue the body in question with governmental authority," as outlined in *ZF Auto*.[22] The court analyzed certain parallels between the arbitration proceeding initiated by the Hong Kong corporation and the investor-state arbitration in *ZF Auto*, noting that "the inclusion of domestic courts as one option [in the treaty] undercut the contention that the arbitration panel had governmental authority."[23] Recognizing that the purpose of § 1782 is to promote comity, the court stated that ICSID tribunals are unable to provide reciprocal discovery assistance for U.S. cases. Even though the decision is a major shift towards non-recognition of investor-state arbitration in the context of § 1782 Applications, the court acknowledged that *In re Alpene* is the first case to analyze the issue in the context of ICSID post-*ZF Auto*. The applicant has filed an objection to the magistrate judge's ruling. The district judge's decision to either adopt or reject the magistrate's ruling is likely forthcoming and may shed further light on the issue.

[21] *ZF Auto. US, Inc. v. Luxshare, Ltd.*, 213 L. Ed. 2d 163, 142 S. Ct. 2078, 2091 (2022).
[22] *Id.*
[23] *In re Alpene, Ltd.*, No. 21MC2547MKBRML, 2022 WL 15497008, at *2 (E.D.N.Y. Oct. 27, 2022).

Soon thereafter, another New York federal court came to the same conclusion as *In re Alpene*. In *In re Webuild S.P.A.*, No. 22-MC-140 (LAK), 2022 WL 17807321 (S.D.N.Y. Dec. 19, 2022), the court held that an ICSID proceeding stemming from a treaty between Panama and Italy is not a "foreign or international tribunal." Even considering these recent district court decisions, it is premature to rule out the use of § 1782 Applications in investor-state arbitrations. Given the U.S. Supreme Court's ambiguity in *ZF Auto*, a circuit split may yet again result.

While the door may have seemingly closed to the use of § 1782 in the context of some arbitral disputes, § 1782 remains as vital as ever to fraud and asset recovery practitioners. The recent decisions have left undisturbed the ability to file § 1782 Applications on an *ex parte* basis, both before (in reasonably contemplation of) a foreign proceeding, as well as during the pendency of an already-filed proceeding. As well, § 1782 judicial assistance remains available to gather evidence for use in a wide array of cases including civil, criminal, administrative, probate, marital and post-judgment cases. In the arbitral setting itself, § 1782 may remain relevant in the context of cases where arbitration, corruption, and post-arbitral award enforcement intersect.[24]

[24] Sequor Law has been and continues to be at the forefront of these and other developments in the realm of § 1782, representing diverse interested parties seeking various forms of evidence in U.S. courts.

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Sony Insurance $150m Fraud Case

Successful International Cooperation to Seize Embezzled Funds Converted to Bitcoin

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Sony Insurance USD 150M Fraud Case: Successful International Cooperation to Seize Embezzled Funds Converted to Bitcoin

HIROYUKI KANAE & HIDETAKA MIYAKE

Abstract

In this article, Hiroyuki Kanae, and Hidetaka Miyake, Partners at Anderson Mori & Tomotsune discuss a recent significant fraud case in Japan. There were many noteworthy points in this case, such as the fraudulent transfer of a huge amount of illegal money by an employee who was working remotely, the conversion of the stolen funds into cryptocurrency, and the prompt recovery of all assets through international cooperation between the Japan and U.S. authorities.

1. Introduction

Sony Life Insurance Co., Ltd. ('Sony Life') publicly released on August 4, 2021 that its overseas consolidated subsidiary, SA Reinsurance Ltd. ('SAR'), learned that approximately JPY 17 billion (approximately USD $155 million) had been transferred from its bank account without approval. On December 1, 2021, Sony Life stated that its employee ('Mr I') was arrested by the Tokyo Metropolitan Police Department on November 29, 2021 on suspicion of fraud. Furthermore, on December 21, 2021, Sony Life revealed that another case concerning Mr I had been sent to the prosecutor's office on suspicion that he had violated the Act

Concerning Punishment of Organized Crimes, Control of Crime Proceeds and Other Matters.

In the meantime, the U.S. Department of Justice ('U.S. DOJ') announced on December 20, 2021 (local time) that it had filed a civil forfeiture complaint to protect and return to Sony Life more than USD $154 million seized by the FBI on December 1, 2021. The U.S. DOJ's public announcement revealed that Mr I had carried out the fraud in May 2021, and that the stolen funds had been converted into approximately 3,879 bitcoins worth more than US $180 million at the time of the public announcement.

There were many noteworthy points in this case, such as the fraudulent transfer of a huge amount of illegal money by an employee who was working remotely, the conversion of the stolen funds into cryptocurrency, and the prompt recovery of all assets through international cooperation between the Japan and U.S. authorities.

In this article, we review this case based on publically available information and discuss the lessons that can be learned from it.

2. Massive illegal money transfers carried out during remote work

SAR was engaged in the reinsurance business in Bermuda and was in liquidation with a view to being dissolved at the end of September 2021. Mr I was seconded to SAR from Sony Life and was in charge of the liquidation procedures such as converting SAR's financial assets into cash and returning them to Sony Life. Three persons including Mr I were seconded from Sony Life to SAR, and Mr I had only one supervisor.

SAR held funds in multiple accounts, and Sony Life transferred those funds to banks in Japan through a pattern of transactions. Specifically, Sony Life transferred Japanese yen to its Citibank account in Bermuda and converted it into U.S. dollars. Mr I was in charge of these currency exchange and fund transfer transactions. Sony Life handled the international remittance process securely through Citibank's Secure Financial Transfer Portal/Protocol ('SFTP'). The money transfer process by SFTP required double authentication through the email accounts of Mr I and his supervisor.

From December 2020 to February 2021, Mr I changed the email account of his supervisor in the SFTP authentication process from the official email account of Sony Life to another email address controlled by Mr I without permission. In March 2021, Mr I opened an account without permission in the name of SAR

with a crypto asset company, Coinbase, by using false information that gave the impression that his supervisor was the individual associated with the Coinbase account, and in April of the same year, he set up a cold wallet and established a rule that would cause all funds deposited into the Coinbase account to be transferred into the cold wallet.

Following these preparatory actions, from May 18 to 20, 2021, Mr I fabricated his supervisor's approval in the SFTP authentication procedure and transferred JPY 16,962,800,068 to the Citibank account in Bermuda, and converted the amount from Japanese yen to USD 154,932,103.17. In addition, Mr I instructed Citibank to remit the converted US dollars in full to a Silvergate Bank account in California which he managed. The account was a Coinbase credit account, and the entire dollar amount was converted into approximately 3,879 bitcoins and transferred to Mr I's cold wallet as configured under the abovementioned rule. It appears that Mr I thought that if the stolen money was converted to cryptocurrency, it would not be frozen even after the discovery of the crime, so he exchanged it for Bitcoin.

3. Prompt asset recovery via international cooperation

On May 20, 2021, Sony Life confirmed the illegal fund transfer and reported the incident to the Financial Services Agency and the Tokyo Metropolitan Police Department. Furthermore, Sony Life filed a criminal complaint with the Tokyo Metropolitan Police Department after it found in its investigation into the incident that no unauthorized access or system malfunction had occurred.

On May 25, 2021, 5 days after the illegal money transfer was executed, Mr I sent an anonymous email in both Japanese and English to his supervisor’s official email address with the message, "If you accept the settlement, we will return the funds back." Over the next two days, May 26 and 27, Mr I sent anonymous e-mails to his supervisor and certain executives of Sony Life threatening them not to report the incident to the police.

In the meantime, the Tokyo Metropolitan Police Department asked the FBI to cooperate in the investigation and identified the final recipient of the money from Mr I's Bitcoin address. The U.S. DOJ announced that it had seized all of the approximately 3,879 bitcoins and that it had filed a civil forfeiture complaint with a local US court to protect and refund the funds to Sony Life. The bitcoins were kept in Mr I's cold wallet, but the Tokyo Metropolitan Police Department conducted a search of his house and other places and obtained evidence leading to the discovery of the private key to the wallet, and conducted an analysis in cooperation with the FBI. The U.S. DOJ stressed that the stolen funds were

successfully seized in full because Sony Life and Citibank had immediately contacted and cooperated with the authorities after discovering the fraudulent money transfers and because of the FBI's international cooperation with foreign authorities.

4. Criminal charges and preventive measures

After conducting the necessary investigations, the Tokyo District Public Prosecutors Office indicted Mr I on fraud and other charges. On June 7, 2022, the first public hearing was held at the Tokyo District Court where Mr I admitted to the criminal charges. On November 18, 2022, the Tokyo District Court imposed a jail term of 9 years on Mr I.

On July 20, 2022, Sony Life announced measures to prevent a recurrence of this incident. In particular, Sony Life announced that it will strengthen its management of employee information, based on its analysis that one of the causes of this incident was that copies of the ID documents related to the persons who were authorized to authenticate transactions through SFTP were stored in a location that Mr I could access and use illegally, and that appropriate measures such as setting a password to restrict access were not taken.

Sony Life also emphasized that SAR did not conduct its own ID management through online banking since it ceased its reinsurance operations in April 2021, and that SAR did not conduct daily checks of its bank account balances since April 2021, when daily fund transfers ceased to occur. In addition to thorough checking of bank account balances on a daily basis, Sony Life also decided to conduct regular checks of ID registrations by overseas subsidiaries, and to have the results verified by the overseas subsidiaries management division and headquarters management division of Sony Life.

Sony Life also announced on July 20, 2022 that, following judicial proceedings in the United States, the bitcoins were converted to US dollars for the purpose of protecting assets, and on July 12 of the same year, a court ruled that approximately USD 161 million would be returned to SAR. It was suspected that Sony Life recovered approximately JPY 22 billion, which is JPY 5 billion more than Mr I fraudulently transferred, due to the weaker Japanese yen.

5. Lessons learned from this case

While remote working practices create environments that facilitate employee access to company materials and information to improve operational efficiency, it is also important to note that this increases the risk of fraud.

This case has a significant precedential value in the sense that funds converted into cryptocurrency were successfully recovered. This means that the conversion of stolen funds into cryptocurrency does not allow a perpetrator to escape the authorities' pursuit. However, considering the fact that the rapid response of companies and international cooperation among authorities contributed significantly to the early recovery of assets in this case, companies need to bear in mind the importance of responding quickly at the initial phase of an incident.

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Argentine Leading Cases in Cyber Crime:

First conviction for computer fraud in Ciudad Autónoma de Buenos Aires

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Argentina: Leading Case in Cyber Crime: First conviction for computer fraud in Ciudad Autónoma de Buenos Aires

JUSTO LO PRETE & LUCÍA FILIPELLI COLLETTO

Abstract

In this article, Justo Lo Prete and Lucía Filipelli Colletto discuss convictions for cyber crime; and computer manipulation techniques accessed by the defendants to use the money from the virtual wallets of mobile devices that were reported stolen, lost or misplaced, in the context of Argentina.

Introduction

On July 20, 2022, the first conviction[1] for computer fraud took place in the jurisdiction of Ciudad Autónoma de Buenos Aires. Judgment was reached by the judicial approvement of an in-court settlement entered into between the accused and the Specialized Prosecutor's Division for Cybercrimes and Misdemeanors, with the consent of the private prosecutor.

[1] Preliminary Criminal Investigation (*IPP*) Number 26836/2022-0, Legal Id. Code (*CUIJ*): IPP J-01-00026836-0/2022-0, Case No. 1983681/2022, of the Criminal, Misdemeanor and Petty Offenses Court No. 8 of Ciudad Autónoma de Buenos Aires, in charge of Judge Natalia Marcela Molina.

The investigation began on March 16 2022. Several evidentiary measures were ordered, including a search warrant carried out on July 11, when the accused parties were arrested and property that could be related to the act was seized. Among said property was the cell phone of the —currently convicted— accused party, which was accessed by means of their biometric data, pursuant to a granted access request.

The conviction was based on the complexity of the acts, the involvement of multiple parties, the legal interest affected, which was determined to cause multiple offenses, and the violation of the victims' right to privacy.

In addition, investigative tasks were ordered to determine the ownership of the seized assets for their restitution.

a. The facts

It was proven that by means of computer manipulation techniques that the accused accessed the virtual wallets of more than one hundred users through their logged-in sessions in the cellular devices that were reported stolen, lost or misplaced.

After entering, they sent money, requested account funds, made payments and applied for credits. In order to make use of those funds, the money was sent to bank accounts owned by the convicted party. The latter kept part of these funds and transferred the rest to third parties.

b. About the access to the cell phone through biometric data

In the search warrant, the cell phone of the now convicted party was seized, and then the Prosecutor's Office requested this party to show their face, iris or fingerprint to effectively unlock the device in order to preserve the information contained in it related to the investigation, in case third parties could remotely access the stored data. The Prosecutor’s Office also emphasized that the measure was necessary due to the technology of the equipment, since there was no tool that would allow the unlocking of the relevant smartphone.

They understood that the privilege against self-incrimination was not violated, since this measure did not imply obtaining confessions or statements in a coercive manner. Furthermore, they warned that expert evidence on the accused was not prohibited, such as: line-up identifications, compulsory blood extractions, urine analysis, fingerprinting and alcohol breathalyzer tests.

Finally, the Prosecutor's Office understood that the limited content of the information to be sought implied a minimal intrusion in the intimate sphere of the accused.
In order to grant the measure, the Judge concluded that, given the type of crime, the need to unlock the cellphone was relevant and evident. Nevertheless, it should be carried out with absolute respect to the privacy of the accused party.

The Judge also took into account the international context including the Budapest Convention, the proportionality of the measure, the principle of freedom of proof and the non-existence of absolute rights. In this sense, the Judge understood that the requested access to the equipment was legal because it protects the rights of society, who becomes a potential victim, thus contributing to social peace. In this regard, the Judge added that the measure was proportional in view of the rights of the victims, and also made reference to previous judgments issued by the National Supreme Court of Justice, which ruled on the coordination of private and public interests and individual rights with those of society.

Finally, the Judge understood that the privilege against self-incrimination was not affected, referring to case law and the need to avoid anachronism, in relation to technological advances in the interests of society in the pursuit of crimes. In addition, the Judge held the accused was bound by a duty of tolerance in accordance with the requested measure, since said party was a passive holder of the property and the request did not imply degrading, humiliating, ill-treatment, cruel or unnecessary practices, nor practices harmful to health.

c. <u>On the conviction and its grounds</u>

The accused was sentenced to two years and nine months in prison for being considered a direct participant of the offense, pursuant to article 173(16) of the Argentine Criminal Code (hereinafter "CC"). Furthermore, the accused was sentenced to abide by certain rules of conduct for three years according to article 23 of the CC, and all the seized assets were confiscated.

In the Conclusions of Law of the sentence, the Judge provides an analysis of the criminal offense of Article 173(16) of the CC as a special type of fraud, where it is required that:

"*...changes in ownership (are) carried out without the owner's knowledge, who suffers the manipulation of his or her data or system without the person being aware,*

and does not apply to cases in which information science is one of the means with which the scheme or deception was forged."[2]

In this sense, the judge ruled that:

"*...the protected legal interest appears as multiple or subject to diverse offenses, since it should not be forgotten that in this case not only the property of each of the victims — who are all individuals— was affected, but there was also an alteration of the normal development of the information system that nowadays automates the distribution of money and organizes the economy of a system, since new technologies also undoubtedly contribute to the economic development of a society*."[3]

On the other hand, it was noted that the fraud entailed a complex criminal structure, with the participation of different perpetrators, at different times and making use of technology, often state-of-the-art, for the consummation of the act.

The Judge uses the terms "*informatic mule*" or "*cybermules*" to explain the direct participation of the convicted party, given that the party enabled the subtraction and disposal of the funds using a number of accounts where the funds were received, and where these funds were subject to broad powers of disposal.

Prior to the intervention of the accused, other parties were also involved, like those stealing the cell phone or carrying out phishing actions; those manipulating the information (unlocking the devices, collecting the data, sending the funds); and the party in question who received the money and later partially forwarded it to higher links in the criminal chain. Although these actions may be carried out by the same person, cybercrimes already committed show the involvement of different actors mainly in an attempt to avoid receiving any punishment under this scheme. In spite of this division of roles and duties, all of them were considered to act maliciously and as direct participants for the consummation of the crime.

In addition, the judgment states that the victims were deprived of their funds through an intrusion into their privacy, noting that the judgment did not judge the way in which the cell phones were obtained, but rather the crime of disposal of assets perpetrated with them. Specifically, it states:

[2] "*Casos especiales de defraudación"* [Special cases of fraud] by Pedro Rodriguez at https://www.pensamientopenal.com.ar/cpcomentado/37768-art-173-casos-especiales-defraudacion, p. 31.
[3] Idem citation 1.

"*...the victims' assets were misappropriated through an invasion of their privacy, since they directly accessed their accounts, their cell phones and attempted against the reliability of the information system or directly attacked the information security.*"[4]

This impact is reinforced when analyzing the type of acts carried out, since the judgment states:

"*Regarding the invasion to the privacy revealed with this criminal actions, it was necessary to overcome the scope of reserve in the device established through the information security system, such as, for instance, to enter the passwords to access the bank accounts. To make it clear, something that has a password, or whose access is not 'open to the public' is undoubtedly within a sphere of private life that each individual wishes to keep safe, to avoid possible intrusions or undesirable dangers; similar to what happens when the door of a house is closed.*"[5]

Finally, the confiscation of the seized assets was determined — aimed at them being returned to their owners – as "*...a measure that will certainly provide a remedy for society and possible victims, since it will undoubtedly be a fundamental element to bring peace to society.*"[6]

Conclusion

The conviction in this matter demonstrates the rapid and effective work carried out in this case. It further shows a proportionate and reasonable intervention of the different authorities in relation to the rights at stake. Measures were taken to preserve the rights of the convicted party, while the rights of the victims and of society as a whole were protected as parties indirectly affected by the actions that had been carried out.

[4] Idem citation 1.
[5] Idem citation 1.
[6] Idem citation 1.

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Friend or Foe – The Regulator as an Ally?

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Friend or Foe – the Regulator as an Ally?

JOHN GREENFIELD, DAVID JONES & ROBIN GIST

Abstract

In this article, John Greenfield, David Jones and Robin Gist of Carey Olsen examine tools available to the Guernsey regulator which, if deployed correctly, can provide powerful assistance in investigating wrongdoing in regulated business and in effecting recoveries or investors.

Introduction

So – you have just received instructions from investors (or on their behalf by liquidators) to recover their investments which appear to have disappeared down the black hole of a Ponzi scheme. The Regulator in the jurisdiction responsible for supervising the people or entities involved in the scheme will be on your side – right? Well, maybe or maybe not. Those Regulators may have other influences on them, e.g. political, financial (resources), reputational which may make it feel like the first priority is not always recovery for investors.

We have seen all of these – often combined in one case. A few years ago, one such Ponzi scheme resulted in liquidators being appointed over the Fund in question by the BVI Court, such appointment being recognised by the Royal Court in Guernsey as substantial proceeds were resting in a Guernsey bank account. The liquidator sought orders from the Guernsey Court to enable them to take charge

of these proceeds and be in a position to distribute to all the victims.

At the last minute, the US Securities and Exchanges Committee ('SEC') sought to intervene and be joined as a party in the Guernsey proceedings on the basis that there were some US resident investors among the victims. Apart from anything else, this would certainly have led to increased costs in professional fees and a consequential reduction in the ultimate funds available for the victims. On this occasion, the Guernsey Court stood firm on the basis that the victims did not need another "cheer leader" in the proceedings.

Some legal principles

It is inescapable that one consequence of the international sanctions imposed as a result of Russia's invasion of Ukraine has been a heightening of the regulatory risks - and scrutiny of them - for offshore businesses and regulators alike.

The *Russia (Sanctions) (EU Exit) Regulations 2019* (the 'UK Regulations') are given the direct effect of law in Guernsey. Upon the designation by the UK of a person or entity, that person or entity becomes a designated person pursuant to Guernsey law as well.

Failure to comply with any obligations under the UK Regulations, as implemented by the *Sanctions (Implementation of UK Regimes) (Bailiwick of Guernsey) (Brexit) Regulations, 2020* (the '2020 Regulations'), or under the *Sanctions (Bailiwick of Guernsey) Law, 2018* (the 'Sanctions Law') is a criminal offence under the Sanctions Law punishable with imprisonment and/or a fine.

When a person becomes designated pursuant to the power in regulation 5, they become subject to an asset freeze as set out in regulations 11 to 15. Broadly, these provisions amount to a complete asset freeze.

Some companies registered in Guernsey continue to be adversely affected by sanctions, and careful thought is proving necessary when dealing with any entity or person with a Russian nexus – whether designated or not. Banks, in particular, appear to have modified their risk appetite such that certain Guernsey entities find themselves without banking services – even though they are not dealing with any person that is the subject of sanctions.

In some cases, companies have become so crippled by the consequences that the Regulator has had to step in.

The Guernsey Financial Services Commission (the 'GFSC') might expect to receive

criticism from an article such as this for getting in the way of debt recovery and fraud investigation processes. However, this is not our experience. There are occasions where the GFSC may be there to lend a hand. Guernsey regulated entities are always required to approach their dealings with the GFSC with openness and transparency, and the need for this has never been more apparent than in the current circumstances. This requirement for openness and transparency has, on occasion, provided justification for the GFSC taking matters into its own hands and putting companies in to administration management.

The *Financial Services Business (Enforcement Powers) (Bailiwick of Guernsey) Law, 2020*, as amended (the 'Enforcement Powers Law'), provides the power for the GFSC to make an application for an administration management order (an 'AMO') under section 81(1)(b) where it is of the opinion that it is necessary or desirable that an order should be made in relation to an administered person for the purpose of the protection of the public or the reputation of the Bailiwick as a finance centre. An administered person is, effectively, a regulated or registered entity.

Recent use of the AMO in respect of Russian Sanctions

The procedure was utilised in April 2022, when the GFSC was granted an AMO in relation to VTBC Asset Management International Limited ('VTBC'), a company licensed under the *Protection of Investors (Bailiwick of Guernsey) Law, 2020* (the 'PoI Law').

VTBC is a Guernsey subsidiary of VTB Capital plc, one of three strategic business arms of the VTB Group. VTB was made the subject of asset freeze sanctions on 24 February 2022 due to its ownership and/or association with the Russian government. The imposition of sanctions led, inexorably, to significant trading difficulties.

In a publication on the GFSC's website, it stated that it felt that it was necessary to bring VTBC into administration in order to protect the interests of investors, and on a larger scale, the Bailiwick of Guernsey as a financial centre, given the ongoing impact of sanctions arising as a result of the Russo-Ukrainian war. Administration managers were subsequently appointed conditional on the issue of a licence by the Committee for Policy & Resources under regulation 64 of the UK Regulations (which allows for the issuing of licences for actions that would otherwise be prohibited).

Carey Olsen later assisted the GFSC in an application for an AMO over ITI Trade

Limited ('ITI'), a prime brokerage business with significant dealings with Russian entities, individuals and securities also licensed under the PoI Law. The appointment of Joint Administration Managers was granted effective immediately, the Regulator again maintaining that this was imperative to protect the Bailiwick's reputation and to protect investors.

Why are AMOs of interest in the asset recovery context?

While the examples of the use of AMOs above were, without doubt, driven by the impact of the sanctions regime, they have demonstrated the utility of the AMO process in assisting in recovering assets for defrauded investors in a wider fraud context.

The GFSC is the only entity that can apply for an AMO. In addition to utilising an AMO where there is a risk to the reputation of the Bailiwick of Guernsey as a financial centre, the GFSC may apply for an AMO where there has been, will, or is likely to be an act or omission, that has caused or is likely to cause undue risk to customers or potential customers. If it considers that the making of an AMO would protect existing or potential customers (section 80(1)(a) of the Enforcement Powers Law), the GFSC can make application to the Court. Consequently, the two available limbs can be applied in a broad context including to protect victims of a potential fraud.

An AMO directs that, during the period for which the order is in force, the business, property, and affairs of the administered person will be managed by the administration manger(s) appointed by the Royal Court.

The GFSC itself may also be appointed as administration manager (section 81(3)). In practice, however, it appears that the general rule of thumb will be that an experienced insolvency practitioner or professional will be appointed.

The application for, and subsequent grant of, an AMO creates a moratorium on other action against the company. While insolvency proceedings may continue during the period between the application for an AMO and the making of an order (s.83(2) of the Enforcement Powers Law), once an AMO is in force, no insolvency proceedings may be commenced against the company (s.84(1)), and from application onwards it cannot be voluntarily dissolved (s.83(1)(a)/s.84(2)(a)) and no proceedings may be commenced against it save with leave of the administration manager (once in place) or the Royal Court (s.83(1)(b)/s.84(2)(b)).

In addition, the administration manager has significant powers. By s.86(7) of the

Enforcement Powers Law the administration manager has power -

- to remove any holder of a supervised role; and
- to call any meeting of members, creditors, customers, partners, limited partners or general partners of the administered person.
- By s.100 the administration manager has the power, among other things -
- to employ and dismiss servants;
- to take possession of, collect and get in the business, property and affairs of the administered person;
- to sell or otherwise dispose of the business, property and affairs of the administered person;
- to appoint an Advocate or other professionally qualified person to assist in the performance of his or her functions;
- to bring or defend any action or other legal proceedings in the name and on behalf of the administered person; and
- to appoint any agent to do any business which he or she is unable to do or which can more conveniently be done by an agent.

The GFSC's powers do not end upon the appointment of an administration manager. It retains the power to apply for an injunction where it is concerned either that an administered person has or may perform any act or make any omission that is likely to cause undue risk to customers, the public or the reputation of the Bailiwick as a finance centre – or where there is a reasonable likelihood of the same (s.99(1) of the Enforcement Powers Law).

The result is a powerful weapon for asset recovery and enforcement which is, in many ways, even more powerful than a traditional insolvency appointment. While the ability to apply for an AMO does not, itself, sit in the hands of the ordinary creditor or concerned investor, it would appear to be open to such persons to approach the GFSC to seek to persuade it that applying for an AMO is the only appropriate course of action.

Conclusion

An AMO may, in the right circumstances, provide a powerful tool in the asset recovery toolkit by placing a company into the hands of an experienced professional with power to take control of assets and with significant investigative powers. Those powers are bolstered by the support of the regulator which, itself, may have broader powers available to it to secure further information.

To summarise, it can be very helpful for the victim to be able to piggyback on the

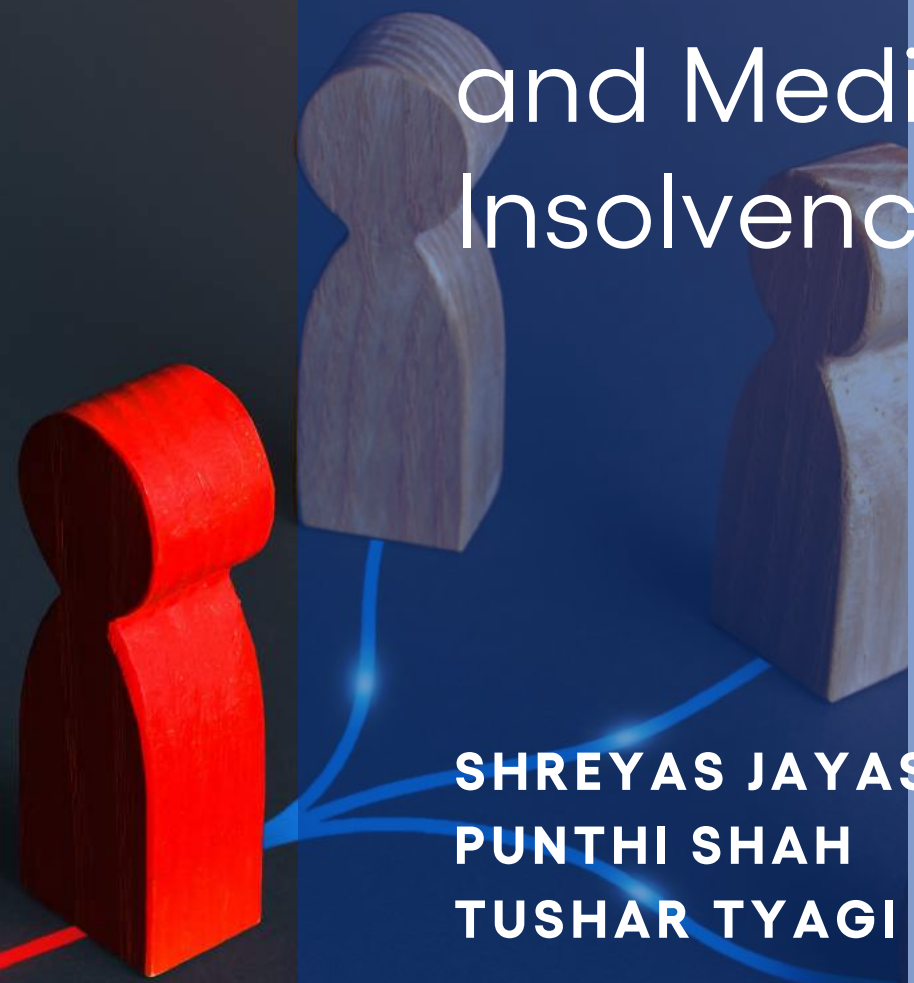
process of the Regulator to be able to recover their losses, turn over stones to see what is lying underneath, and have the ready ear of their local courts.

While there may be a price to pay – some loss of control of the process of recovery/enforcement and in particular the pace of such process, and the inevitable feeling of "being left in the dark" that may ensue – a regime that is regulator driven, that provides a concerned party with a relatively easy "in" with the local court, and which can be used to investigate and pursue wrongdoing might, in the right circumstances, be just the mechanism a concerned investor requires.

In this context, it should be noted that a relatively small offshore jurisdiction can have its advantages. In Guernsey, we have a regular dialogue with all the team at the Regulator's Department and, indeed, often represent them in some of the more challenging court applications. As a result, good professional relationships develop, and a good exchange of information is consequentially available. For the victims to know what is actually going on and when some positive steps will be taken can help enormously to ease the pain of the loss they have suffered.

ICC FraudNet
Global Annual Report 2023

Role of Arbitration and Mediation in Insolvency



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Role of Arbitration and Mediation in Insolvency

SHREYAS JAYASIMHA, PUNTHI SHAH AND TUSHAR TYAGI

Introduction

In this article, Shreyas Jayasimha, Punthi Shah and Tushar Tyagi analyze how Alternative Modes of Dispute Resolution have been gaining traction across the world as an apt alternative to litigation, including with particular reference to India. Insolvency proceedings in recent times have clashed with such alternative modes of dispute resolution, especially arbitration. In this regard, it becomes pertinent to shed light on the Insolvency and Bankruptcy Code, 2016 which has been one of the most significant national legislations on insolvency and liquidation that has yielded some outstanding results in its nascent stages. However, there exist certain grey areas within the legislation, one of which this article aims to address – the clash between imposition of a moratorium and that of an initiation/continuation of an arbitration proceeding. The article is divided in the following order –

Part I

1. Indian Perspective
   - *1.1. Arbitration as a tool for dispute resolution*
   - *1.2. The Code*
   - *1.3. Intersection between CIRP and Arbitration*
2. International Perspective

PART I: ARBITRATION AND INSOLVENCY

The Insolvency and Bankruptcy Code, 2016 ('Code') was enacted with the objective of being an umbrella legislation for the insolvency resolution of all types of entities such as individuals, corporate persons or partnership firms. The enactment of this Code was a watershed moment in the history of insolvency and bankruptcy in India. The Code sought to regulate and ensure a time-bound manner of insolvency processes with the aim of maximization of value of assets among other aspects.

Considering that the 'maximization of value of assets' is one of the most prominent aims of the Code, it has the tendency to affect other areas of law, including arbitration. Only the imposition of a moratorium under Section 14 of the Code is where the problem arises with respect to arbitration proceedings. Due to a lack of judicial precedents in this regard, the entire conflict between arbitration and Corporate Insolvency Resolution Process ('CIRP') or liquidation remains a grey area. Albeit there is a complete stay on arbitration proceedings among other proceedings under Section 14 (1)(a), there are multiple interpretations of the same by the Indian Courts which have resulted in more confusion which needs to be addressed.

1.1. Arbitration as a tool for Dispute Resolution

Arbitration is an alternative mode of dispute resolution wherein the parties submit their dispute to one or more arbitrators who is/are a neutral third party, who passes an arbitral award which is binding on both parties. It is crucial to note that arbitration can only happen upon the consent of both parties and they also appoint their arbitrators. Usually, the parties who submit their dispute to arbitration have a pre- existing agreement which has

an arbitration clause in case of future disputes or a binding arbitration agreement.

1.2. The Code

The Insolvency and Bankruptcy Code, 2016 seeks to revive distressed companies and protecting the interests of creditors by preventing credit/lending and financial risks. It classifies creditors into two categories namely, operational creditors[1] and financial creditors[2], who can both initiate CIRP[3] against the corporate debtor who has at least 1 Crore[4] of outstanding dues. Further, the corporate debtor can initiate a CIRP on their own in case of a default being committed as a corporate applicant.[5] An application under either of these categories shall be made to the Adjudicating Authority, i.e., the NCLT, which shall either accept or reject the application upon being satisfied of the existence of debt. In case it is accepted, the Adjudicating Authority will initiate a CIRP over the corporate debtor by appointing an Interim Resolution Professional who shall have full control to manage the affairs of the corporate debtor over the course of CIRP.[6] Post this, a public announcement will be made regarding the initiation of CIRP against the corporate debtor along with a call for claims of various creditors to whom the corporate debtor owes debt to. A moratorium is then imposed for the continuation of or institution of suits/arbitration proceedings among other actions.[7] It is important to note that once the CIRP begins, the order of moratorium so declared by the Adjudicating Authority shall exist till the completion of the CIRP process.

1.3. The Intersection Between CIRP and Arbitration

This section aims to identify the exact point of overlap between the Code

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[1] Section 5(20) of the Code
[2] Section 5(7) of the Code
[3] Sections 7 and 9 of the Code
[4] As amended by the Notification under Section 4 of the Code
[5] Section 10
[6] The interim resolution professional later gets replaced by the resolution professional
[7] Section 14 – the following are prohibited during the period of moratorium –
(a) the institution of suits or continuation of pending suits or proceedings against the corporate debtor including execution of any judgment, decree or order in any court of law, tribunal, arbitration panel or other authority;
(b) transferring, encumbering, alienating or disposing of by the corporate debtor any of its assets or any legalright or beneficial interest therein;
(c) any action to foreclose, recover or enforce any security interest created by the corporate debtor in respect ofits property including any action under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002;
(d) the recovery of any property by an owner or lessor where such property is occupied by or in the possessionof the corporate debtor

and the process of arbitration, i.e., the imposition of a moratorium upon the admission of an application for CIRP by the Adjudicating Authority.

1.3.1. Moratorium

A moratorium is a suspension or stay on any legal action against a corporate debtor, giving them a chance to pay off their debts. This provision awards the debtor an opportunity to assess the risks, liabilities and profits without the imposition of any legal debt recovery mechanisms by the creditor. The moratorium period begins from the date of initiation of CIRP and ends upon the completion of the CIRP process, barring all proceedings during this period.

However, the Code is silent on what types/classes of proceedings that shall not be barred, leaving it to judicial interpretation. While Courts have attempted to interpret the scope of Section 14, there is neither a conclusive order which can be followed nor has the Code been amended to remove the ambiguity.

1.3.2. Outcome of Moratorium on Arbitration Proceedings

To discuss what the outcome of an order of moratorium on arbitration proceedings, it can be classified further into the following:

1.3.2.1. Filing an application for CIRP when Parallel Arbitration Proceedings are underway.

In the case of *Fourth Dimension Solution Ltd. v. Ricoh India Ltd*[8]., the Court gave an order for the operational creditor of the corporate debtor to go ahead with arbitration proceedings despite approval of the resolution plan by the CoC and the Apex Court. Moreover, in *K. Kishan v. M/s. Vijay Nirman Company*[9], the Supreme Court held that an arbitral award falls under the ambit of a valid evidence of operational debt so long as it is undisputed.

Therefore, it is evident that there is no express bar against filing an application for CIRP when parallel arbitration proceedings are going on because a claim under an arbitration agreement does not fall under the definition of debt under the Code; However, if the claim independently falls under the scope of

[8] Civil Appeal No. 5908 of 2021.

[9] Civil Appeal No. 21824 of 2017.

financial or operational debt, an application for CIRP may be made.

1.3.2.2. Foreign Seated Arbitration in which One of the Parties is an Indian Corporate Debtor Undergoing CIRP

In a situation where there is an ongoing foreign seated arbitration proceeding and one of the parties happens to have a CIRP case ongoing in India, then such a party may request for a stay on the arbitration proceeding; However, where an award has already been passed foreign arbitration tribunal against foreign assets, then such an award shall have no prejudice against it having an effect on the Indian assets.

1.3.3. **Judicial Precedents**

Coming to judicial precedents, it is imperative to distinguish the views of courts. It is noticeable that there are 2 issues that courts have dealt with previously:

(a) Continuation/Initiation of Arbitration Proceedings when CIRP is admitted; and

(b) Arbitrability of Insolvency Proceedings.

In the case of *Alchemist Asset Reconstruction Co. Ltd. v. Moser Baer India Ltd.*, the Court held that any proceeding initiated post the initiation of CIRP including those of arbitration, are considered 'non-est' in law. This landmark case resolved the question of whether arbitration clauses can be invoked after the initiation of CIRP. However, in this case, the question of invoking the arbitration clause arose at the stage of debt recovery. This was perhaps the rationale behind the judgement being made. However, this may not be the case for all stages of arbitration.

Further, in the case of *Power Grid Corporation*[10], the Court held has that so long as a proceeding is beneficial to the corporate debtor and has no adverse impact on the assets of the corporate debtor, then such proceeding shall not be barred under Section 14 of the Code, extending to even arbitration proceedings. An opposing view was held in the recent case of Indus Biotech Private Limited v. Kotak India Venture Fund[11] wherein the Court relied on two principles to decide the arbitrability of insolvency proceedings.

[10] Power Grid Corporation of India Ltd. v. Jyoti Structures Ltd. 246 (2018) DLT 485.
[11] 2021 SCC Online SC 268.

1.3.3.1. Firstly, the aspect of the Code having an overriding effect. As per Section 238 of the Code, the provisions of the Code have an overriding effect over any other law or statute for the time being in force, which essentially takes after the maxim *generalia specialibus non derogant*. Therefore, if two special statutes have clauses which are in conflict, the clauses of the statute enacted later will have an overriding effect over the former.

1.3.3.2. Secondly, the principle of *Right in Rem* v. *Right in Personam*. In order to examine the issue of arbitrability, the court took heed of the precedent laid down in the Vidya Drolia[12] case which stipulated that insolvency/CIRP proceedings become a right *in rem* only after they are admitted. Seeing as post the admission all creditors to whom the corporate debtor owes a debt to become interested third parties, the admission or acceptance of the CIRP application thereof results in an '*erga omnes*' effect.

Insolvency proceedings being *erga omnes* is essentially true because a corporate debtor seated in one jurisdiction may have transactions with multiple jurisdictions, who will all be affected if the corporate debtor goes into liquidation or undergoes an insolvency. Therefore, even in the Swiss Ribbons Case[13], the Court held that as soon as the CIRP initiated, they become *in rem* cases.

In order to understand why post-admission insolvency case becomes right *in rem*, it is crucial to examine the case of Indus Biotech Case wherein the Court made a distinction between the *in rem* and *in personam* stages of an insolvency proceeding. Before the application is admitted, the proceedings are only between the debtor and creditor, hence it is *in personam*. The NCLT only needs to establish the existence of default. Once the application is admitted, it becomes *in rem*. Additionally, this case addressed the arbitrability of insolvency proceedings in detail, wherein the Supreme Court allowed the case to be settled *via* arbitration as the dispute does not constitute a valid '*debt*' under the Code.

[12] Vidya Drolia and Ors. v. Durga Trading Corporation, MANU/SC/0939/2020.
[13] Swiss Ribbons Pvt. Ltd. v. Union of India, (2019) SCC Online SC 73

In spite of the previously settled precedents, there is a lack of clarity regarding which insolvency proceedings can be settled through arbitration and the initiation or continuation of arbitration proceedings.

2. International Perspective

India is not the only country which imposes a stay on arbitration proceedings during an ongoing insolvency/liquidation. This is to ensure that all the creditors to whom the corporate debtor may owe a debt are treated justly. While it may be possible to settle certain insolvency issues through arbitration, there are some core insolvency issues which cannot be arbitrated (for example verification of claims of creditors, initiation of insolvency, winding up, etc.). A clear distinction between arbitrable and non-arbitrable insolvency issues has been brought about due to the sheer volume of international insolvency laws. In the Canadian case, *Petrowest Corp. v. Peace River Hydro Partners*[14], the court-appointed receiver set aside the competence-competence principle of arbitration (one that gives precedence to arbitration) and concluded that the arbitration agreements of this case were ineffective because several arbitral proceedings would conflict with the Bankruptcy and Insolvency Act's goals of an orderly and effective resolution of the receivership.

2.1. United Kingdom

Relying on the various precedents laid down by English courts, it can be ascertained that so long as third-party rights or public policies are not infringed, parties involved in insolvency disputes may settle their dispute through arbitration.[15] In a case where the creditors are not satisfied with the method of resolution of debts by the appointed liquidator they may mutually agree upon settling the issue through arbitration as opposed to approaching a court of law. Post liquidation, the effect of moratorium equates to automatically suspending or staying all actions against the corporate debtor unless otherwise expressly approved by the courts.

2.2. Australia

As such there are no divisions pertaining to core and non-core issues in the Australian set-up. The adjudicating authorities generally refuse to grant a stay order if they are of the opinion that the rights of the

[14] Petrowest Corp. v. Peace River Hydro Partners, 2022 SCC 41.

[15] This was held in the case of Fulham Football Club v. Richards, [2010] EWHC 3111 (Ch)

parties do not stem from the statute but arise from a contract. Additionally, the arbitrability of insolvency matters depends heavily on public policy considerations.

2.3. USA

Unlike many nations, the jurisprudence surrounding this conflict in the US is a little more cemented and substantial in nature. There have been a few cases wherein the courts have upheld that it is not possible to subscribe to concerns which places bankruptcy laws in a superior position to that of the Federal Arbitration Act superiority between bankruptcy laws and the Federal Arbitration Act was therefore clarified in this case. In the McMahan case, the Court laid down the test: "the party challenging the arbitral award must show/establish the Congress's intention to make an exception to the FAA's mandate either by establishing the (i) text of the Statute, (ii) legislative history of the Statute or (iii) inherent conflict between arbitration and the statute's underlying purposes."[16] In non-core matters, US bankruptcy courts lack jurisdiction, hence arbitration must be required in such circumstances. Even while the majority of essential insolvency concerns should be decided by the courts, some issues may not necessarily contradict or undermine the core purpose of the bankruptcy code and can be resolved through arbitration.

3. Road Ahead

The clash between insolvency laws and arbitral laws in India require some clarity when it comes to their application based on each case. The ultimate goal of creditors/adjudicating authorities/courts is to ensure that there is an effective debt recovery that happens, because if not, over a period of time, it will eventually affect the economy of the country. Creditors need to consider the bundle of rights each corporate debtor has, which includes that of issues pertaining to insolvency likely to be resolved through arbitration.

This comparative study of different countries gives the criteria that must be taken into account when deciding the arbitrability of insolvency issues; certain countries have adopted a severe stance, while others are more

[16] Shearson/American Express v. McMahon, 482 U.S. 220, 242 (1987).

tolerant. While some nations make decisions on a case-by-case basis, some have advanced legislative frameworks with clear structures, to some extent.

Therefore, it is up to the Indian courts to arrive at a possible solution which clears the mist surrounding this grey area that exists. Until such time, debates over the superiority of the Code over arbitration agreements or clauses will persist.

4. Conclusion

Different spheres of laws often intersect and overlap. However, each law only ensures justice for the party which suffers losses by fulfilling the aim behind which it was enacted for. Often times, multiple legislations need to be applied, resulting in the conflicts between these laws. During liquidation or insolvency proceedings, the corporate debtor is already facing hurdles to pay off their debt, therefore imposing additional proceedings/suits through arbitration or in a court will only aggravate their existing burden. On the other hand, an agreement entered into by two parties based on trust will be breached when one party does not honour it merely because of undergoing insolvency/liquidation. The judiciary must take a very neutral stance on the issue of insolvency/liquidation and the initiation /continuation of proceedings in other forums of law. In this light, many cases have seen the courts applying the following neutral rule: so long as the arbitration proceedings, which may run parallel, are not aimed at debt recovery, they can continue with the same as this has no effect on the pool of assets of the corporate debtor. While this is the most neutral solution which the Courts have come up with, it is still not entirely cohesive. This can be rectified through an amendment to Section 14 of the Code which clearly lays down which categories of proceedings are barred or not. Additionally, arbitration agreements can have clauses which deal with situations in the case either of the parties goes into insolvency. Such steps can be taken for the better implementation of the provisions of the Code as clauses contained within arbitration agreements.

PART II: MEDIATION AND INSOLVENCY

Mediation is another mode of Alternative Dispute Resolution which is informal in nature wherein a mediator (a neutral third-party) assists, oversees and facilitates the two parties who have agreed to mediate their dispute to reach an amicable solution. Unlike in arbitration, the mediator does not have any adjudicative powers. Invariably, any agreement reached upon will not be binding upon either of the parties. Mediation is at a very nascent stage in India, especially when it comes to insolvency related disputes.

The Code was enacted to deal with the rising Non- Performing Assets in a timely manner. While the Code is more successful than its predecessors, it is heavily reliant on the traditional courts for its functioning. This inevitably leads to inordinate delays due to litigation between different parties during the CIRP process. Despite multiple amendments to the Code, there are inefficiencies in the time bound resolution of disputes. Inevitably, the purpose of the preamble of the Code stands defeated. This part of the article aims to explore the aspect of using mediation as an effective tool to combat this issue. Additionally, the article shall also analyze the Indian position along with a cross-jurisdictional comparison of the effective use of mediation in insolvency issues. Finally, the article shall suggest a few approaches which may assist the creditors as well as the corporate debtor in resolving disputes through mediation including amicably framing strategies for payment of debt, restructuring among others. .

1. Indian Perspective

1.1. Benefits of Mediation

Given that mediation is mostly based on the concept of mutually negotiating to come to an amicable solution, it would increase the likelihood of arriving at a promising solution for both parties involved. Further, the corporate debtor would have some control over their assets as opposed to an Insolvency Resolution Professional having total control over the pool of assets. Additionally, there is scope for deciding on a comprehensive resolution plan which addresses the interests of all the concerned parties. Such a resolution is more than a mere debt recovery mechanism since it also helps the debtor to effectively rehabilitate. Furthermore, despite the time period provided for completion of the CIRP process, it inevitably gets delayed. By using mediation, it is possible to reduce the burden on the courts by eliminating the long procedural complexities. Mediation also helps to protect the reputation of the corporate debtor owing to the confidentiality of the proceedings. They have an added benefit of being extremely convenient because they can be held at the ease of both parties. Finally, the relationship that exists between a creditor and debtor does not get damaged

when they enter into a mediation, thereby ensuring their cooperative nature persists for future transactions.

1.2. Objectives

Mediation insolvency processes can act as a tool for alleviating corporate distress by ensuring there is a conducive environment benefitting both the parties for insolvency negotiations.

1.2.1. A significant problem that arises when it comes to insolvency proceedings is with respect to the distribution of the assets of the corporate debtor to all the creditors involved from the estate. As per the Code, a waterfall mechanism is followed but this may not be equal distribution of assets or even the entire amount of what a creditor may be entitled for. Hence, mediation could be an effective tool in this regard whereby parties themselves can come to a common conclusion as to the most efficient way of distribution of assets of the corporate debtor.[17]

1.2.2. Another pertinent issue that arises is with respect to the restructuring plan. A restructuring plan is essentially a multi-party agreement which enables the most optimal method to revive the company/solve the distress it faces for all the parties involved. What happens generally is that the corporate debtor convinces the creditors of the benefits of revival of the company as opposed to liquidation of the company. However, it is not always that creditors are satisfied with this approach because they do not trust the corporate debtor's capabilities to manage the distress. Even in the event of an acceptance of the motion, the next major challenge is that of coming up with an apt restructuring plan, which requires a lot of capital in itself – such as hearings, expert opinions, etc. However, should mediation be used for the same, there would be a more satisfactory result. The confidentiality aspect of mediation further bolsters more open communication between the corporate debtor as well as the creditors involved. Additionally, the mediation process gives the parties the chance to develop a rescue strategy that adheres

[17] For instance, Bankruptcy mediation is formally part of the judicial system in Canada. In addition of being privately available, Article 105 of the Canadian Bankruptcy and Insolvency general rules (C.R.C., c. 368) prescribes mandatory mediation to resolve two type of disputes: (a) Mediation for surplus income, which can beinitiated both by the trustee, or one or more creditors, in case of disagreement with the amount of surplus income to be paid by the bankrupt, according to art. 68(8) Canadian Bankruptcy Act; (b) and mediation in case of creditors' opposition to bankrupt's discharge, according to art. 170.1(2) Canadian Bankruptcy Act. Canadian bankruptcy regulation is available on the Justice Laws website: http://laws- lois.justice.gc.ca/eng/acts/B3/index.html.

more closely to their true interests; in addition, parties can gather a variety of information to ensure performance and to monitor future behavior. That said, there is always an iota of risk involved when it comes to restructuring plans and therefore, all relevant aspects should be considered while mediating, failing which there would be adverse consequences.

1.2.3. Finally, mediation can be used to even prevent insolvency. Instead of using it as a last resort, mediation should be employed in the initial stages of the proceedings when the parties are most likely to find common ground. They may even recognize other previously unidentified issues and prevent them from occurring.

2. International Perspective

2.1. Singapore

The Committee to Strengthen Singapore as an International Centre for Debt Restructuring proposed using insolvency mediation to resolve disputes in 2018, and the Singaporean Ministry of Law accepted their recommendation. The following cases have been approved for the use of insolvency mediation for the following purposes: resolving individual creditor disputes with a debtor in a multi-creditor restructuring; managing multiple creditor disputes of the same nature; and achieving agreement between a debtor and its creditors on the restructuring plan.[18] The Insolvency law of Singapore also provides for statutory recognition under the Insolvency to arbitration and other alternate disputes resolutions. Under the Insolvency, Restructuring and Dissolution Act 2018, the Official Assignee can refer the disputes to arbitration, or compromise all debts, claims and liabilities between the bankrupt and any person who may have incurred any liability to the bankrupt.[19]

2.2. United States of America

Under Chapter XI of the Bankruptcy Code, the US has a strong mediationprocess.[20] Either a party requests insolvency mediation, or the court orders it. It hasbeen utilized successfully in a number of high-profile instances, including the Lehman Brothers case,

[18] https://www.lexology.com/Commentary/insolvency-restructuring/singapore/oon-bazul-llp/alternative-dispute-resolution-in-insolvency-and-restructuring-proceedings

[19] Section 387 of Insolvency, Restructuring and Dissolution Act 2018

[20] Gert-Jan Boon, Maciek Bednarski, Carlotte Dessauvagie & Milan Pastoors, *The Mediator in Insolvency Law:Exploring New Terrain*, leidenlawblog

when only 4 of the 77 finalized mediation processes were discontinued.[21]

3. **Way Forward**

Simply suggesting the use of mediation as a tool to prevent insolvency is not substantial; it is crucial to also resolve various issues which surround the context of using mediation in insolvency such as-

(a) Whether to group creditors with their myriad of interests under different brackets, each with their own representative;
(b) Who gets to initiate the process - be it the corporate debtor, creditor, or both;
(c) Who decides upon the mediator;
(d) Enforcement of any settlement reached at in a particular mediation proceeding, etc.;

Insolvency mediation may not be ideal to resolve every insolvency matter. However, it provides a platform for prevention of disruption of corporate entity, which should ideally be the goal of any insolvency process. Further, seeing as maximization of value of assets is one of the primary motives of the Code, mediation also helps by expedited manner of solving cases. The judiciary and parliament should consider incorporating mediation into the Code, this will promote flexible and cost-effective resolutions of insolvency matters. While all cases may not require a mandatory pre-litigation mediation, amending the Code to incorporate those cases which fall under a specific classification to undergo a pre-litigation mediation would not only expediting process but reduce burden on courts.

Conclusion

Following the analysis in both parts of this article , it can be concluded that the Code has a long way to go to becoming a clear and potent law. Despite the numerous challenges that have cropped up - especially during the pandemic - the Code provided the most feasible solutions to aggrieved persons. The introduction would not only dispel the mist surrounding the clash between a moratorium and arbitration, but also increase the rate of success in terms of disposal of cases and debt recovery and asset distribution.

[21] Kayjal Dasan & Samuel Seow, Seminar Review: Mediation in International Insolvency, International Arbitration http://www.internationalarbitrationasia.com/mediation_in_international_insolvency_disputes

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Freezing Orders in South Africa

Challenges and Opportunities
A Recent Case Study

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Freezing Orders in South Africa- Challenges and Opportunities: A Recent Case Study

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Abstract

In this article, John Oxenham, Michael-James Currie, Jemma Muller and Tyla Lee Coertzen of Primerio provide an analysis of the use of freezing orders as a civil remedy in South Africa available to victims of fraud and cross border scams in order to identify and recover assets. In doing so, the authors provide an overview of the requirements and advantages of the use of freezing orders, as well as a synopsis of a recent case in which they were involved wherein freezing orders were successfully used to recover funds lost as a result of fraudulent misrepresentations.

Introduction

South Africa is considered one of the most notorious jurisdictions for money laundering and fraud offences. It has been estimated that South Africa forfeits up to USD25 billion in illicit financial flows annually.[1] The prevalence of money laundering in South Africa and its failure to implement various international

[1] Matt Smith, Cheska Lozano, "South Africa banks face growing risks as anti-money laundering deadline looms" (31 August 2022) <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/south-africa-banks-face-growing-risks-as-anti-money-laundering-deadline-looms-71794924> accessed 11 January 2023.

benchmarks with regards to money laundering and other financial crimes, resulted in South Africa being placed on the 'grey list' by the Financial Action Task Force ("FATF") on 24 February 2023.[2]

In the Prudential Authority's "Assessment of money laundering, terrorist financing and proliferation financing risk in the banking sector, July 2022"[3] ("Risk Assessment"), various risks and vulnerabilities within the banking sector which contribute to financial losses caused by financial crime and scams were identified.[4] These included, *inter alia*, fraud and illicit cross-border flows, the failure of banks to procure beneficial ownership information, interactions with and the onboarding of clients without face-to-face interactions, data issues and the absence of a holistic view of clients in circumstances where a client has various accounts and business relationships within the same bank.

Employing effective detection and recovery mechanisms has become more important than ever. Effectively recovering assets (which are proceeds of crime) for purposes of complying with FATF obligations rests with the State. We consider the civil mechanisms available to victims of cross border scams in order to identify and recover assets. We do so with reference to a case study the authors were recently involved in and highlight challenges and opportunities in pursuing civil freezing and recovery actions in South Africa.

In this regard, the starting point of any recovery effort is to track and trace the assets or funds. Once this is done, and in order to swiftly protect such assets while parallel proceedings are instituted, it is vital to obtain an anti-dissipation interdict, also known as the "Mareva Injunction" or "Freezing order".

We discuss the legal requirements and practical aspects of this process from a South African perspective.

Anti-dissipation interdicts in South Africa

[2] Financial Action Task Force, "Jurisdictions under Increased Monitoring" (24 February 2023) https://www.fatf-gafi.org/en/publications/High-risk-and-other-monitored-jurisdictions/Increased-monitoring-february-2023.html accessed 29 March 2023. In its "Mutual Evaluation Report of South Africa", the FATF accurately described South Africa's exposure and notorious reputation as a country popular for money laundering both within and through the country to other jurisdictions. See the "Anti-money laundering and counter-terrorist financing measures South Africa: Mutual Evaluation Report" accessible at https://www.fatf-gafi.org/media/fatf/documents/reports/mer4/Mutual-Evaluation-Report-South-Africa.pdf.

[3] Prudential Authority, "Assessment of money laundering, terrorist financing and proliferation financing risk in the banking sector" (July 2022) <https://www.resbank.co.za/content/dam/sarb/publications/media-releases/2022/pa-assessment-reports/Banking%20Sector%20Risk%20Assessment%20Report.pdf> accessed 10 January 2023.

[4] *Ibid*, para 1.2, page 2.

An anti-dissipation interdict (also known in South Africa as an interdict *in Securitatem debiti*) is an interlocutory order which prohibits a respondent from dissipating his or her assets. It is an urgent application which can, provided certain requirements are met, be granted on an *ex parte* basis.[5]

A South African court will grant such an order where there is reasonable belief that a respondent may deliberately be dissipating or concealing his or her assets, in order to ensure that when the applicant eventually obtains judgment against the respondent, the respondent will have no assets to satisfy such judgment debt.[6] It often happens that a defendant will ensure that his or her assets have either been transferred abroad or transferred into someone else's name when being made aware that a plaintiff has or intends on instituting proceedings against such a defendant, and such proceedings have a good prospect of success. By dissipating or concealing such assets, the defendant causes irreparable harm to the plaintiff as any judgment which the plaintiff may obtain will be effectively hollow.

Requirements to obtain an anti-dissipation interdict

The onus is on the applicant to prove the following requirements in order to obtain an anti-dissipation interdict:

(a) there are assets of the respondent within the jurisdiction of any court in South Africa;

(b) there is a reasonable belief that the respondent will dissipate the assets, or conceal the assets and transfer them abroad (i.e., there is a reasonable risk of disposal of the assets);

(c) the purpose of the above-mentioned dissipation or concealment is in order to frustrate the anticipated judgment obtained by the applicant in either existing proceedings or proceedings about to be instituted; and

(d) a well-grounded *prima facie* cause of action exists against the respondent.

In addition to the above, it is worth noting that the court has the power to grant ancillary orders which are viewed as necessary for the interdict (such as, *inter alia*,

[5] This is particularly relevant in in cases where the disclosure of the application to the defendant would likely result in the defendant expeditiously dissipating his or her assets before such an order can be made. An *ex parte* application, while despite being instituted without notice to the defendant, will make provision for the defendant in due course to approach the court to either discharge or amend the order after being served with the order.

[6] The precedent setting case as to when a court will grant an anti-dissipation interdict is the case of *Knox D'Arcy Ltd and Others v Jamieson and Others* 1994 (3) SA 700 (W); 1995 (2) SA 579 (W) (on appeal) 1996 (4) SA 349 (A).

the disclosure of bank account records).[7] Not only does this ensure that any interdict granted is effective, but it can also serve as a useful investigative tool by allowing access to additional information which can be used to trace the remainder of the funds which are to be recovered.

A recent case study

In 2022, an international company based in the Philippines transferred funds into a South African bank account as a result of a fraudulent misrepresentation. Various anti-dissipation interdicts were successfully utilized to swiftly freeze, trace funds already dissipated by the protagonists into other bank accounts, and ultimately recover most of the funds transferred as a result of the fraudulent misrepresentation.[8]

This case was a good example of how to "chase the money" as three urgent applications were brought and heard within a period of two days and more than 7 bank accounts were frozen as the funds were moved between different bank accounts.

The anti-dissipation interdict was commenced on an urgent and *ex parte* basis.[9] The applicant was thus not only required to demonstrate urgency in its papers, but also convince the Court's registrar that the matter is sufficiently urgent as to warrant a hearing within a few hours (the urgent application was filed within six hours from obtaining instructions and the hearing was held after hours). In the authors' view, this is in practice a common hurdle faced by legal practitioners. There are no set legal rules on how one sufficiently demonstrates urgency to a registrar, nor what the threshold for urgency is. Much will depend on the relevant registrar and his/her views on whether the matter is urgent or not.

The applicant *in casu* was able to demonstrate the urgency of the matter and expeditiously (within just a few hours) freeze the account, whilst not alerting the main protagonists to the intention to request the court to freeze the account.

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[7] The court in *Knox D'Arcy* accepted the principle in English law that: "*if a Mareva injunction is likely to be rendered ineffectual or unworkable without discovery of certain facts or documents, the Court has an inherent common-law power to make such orders for discovery of facts or documents as may be necessary to ensure the injunction will be effectual and workable*". *Knox D'Arcy Ltd and Others v Jamieson and Others* (1994) 4 All SA 171 (W), page 178.

[8] This was achieved by the team at Primerio Law Incorporated, who were able to successfully obtain four urgent applications over the course of ten days.

[9] The applicant sought the relief on an urgent and *ex parte* basis for two main reasons:

(i) It would not have been possible to serve the application on the respondents timeously; and

(ii) There was a well-grounded apprehension that if the application came to the attention of the main protagonists, they would immediately transfer the funds out of the bank account.

As a consequence of the matter being brought on an urgent and *ex parte* basis, the anti-dissipation interdict operated as an interim order, allowing the respondent to represent its case (if any) to the court on a return date given by the court.

Due to the fact that South African banks will only disclose account information following a court order, the applicant used the application for an anti-dissipation interdict to pre-emptively compel the bank to provide certain information in addition to freezing the account. In particular, the applicant sought information on the relevant account balance, know-your-client information, and bank statements. As mentioned above, this is possible as the court has the power to grant ancillary orders which are viewed as necessary for the interdict.

Absent a request for additional information, an applicant risks being granted an anti-dissipation interdict, without subsequently being able to ascertain whether the account in fact has any funds. If the account has little or no funds, the interdict is essentially meaningless and hollow. This is another shortcoming in obtaining anti-dissipation interdicts and greatly undermines its purpose and effectiveness. By requesting additional information together with the freezing order (i.e., account balances, account holder information, transaction history and bank statements), an applicant can not only ascertain the amount actually frozen, but also receive vital information which the applicant can use to trace the funds in the event of it already having been transferred into different bank accounts prior to obtaining the interdict. This is, however, assuming the bank recorded accurate and sufficient account holder information, an obligation identified by the Prudential Authority in the Risk Assessment as one which is not always adhered to by banks.[10]

The importance of requesting such additional information simultaneously with an anti-dissipation interdict was demonstrated *in casu*. The information the applicant received from the initial bank to which the funds were transferred revealed: (i) that half of the funds had been transferred out of the account; (ii) where the funds had been transferred; and (iii) relevant information on the account holder.

This information enabled the applicant to successfully obtain further urgent interdicts, freezing each South African account to which the funds were subsequently transferred, together with compelling such banks to provide certain information in relation to the accounts. Again, since the application was brought on an urgent *ex parte* basis, the respondents were provided with a return date where they could demonstrate their case (if any) to the court, and in particular motivate why the frozen funds should not be returned to the international company.

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[10] Prudential Authority, "Assessment of money laundering, terrorist financing and proliferation financing risk in the banking sector" (July 2022) <https://www.resbank.co.za/content/dam/sarb/publications/media-releases/2022/pa-assessment-reports/Banking%20Sector%20Risk%20Assessment%20Report.pdf> accessed 10 January 2023 at para 1.1, page 3.

Additionally, the information could be useful for law enforcement authorities in investigating the matter, and could greatly assist in expediting their investigation. *In casu*, the applicant provided law enforcement authorities with the information, prompting them to open an investigation into the matter.

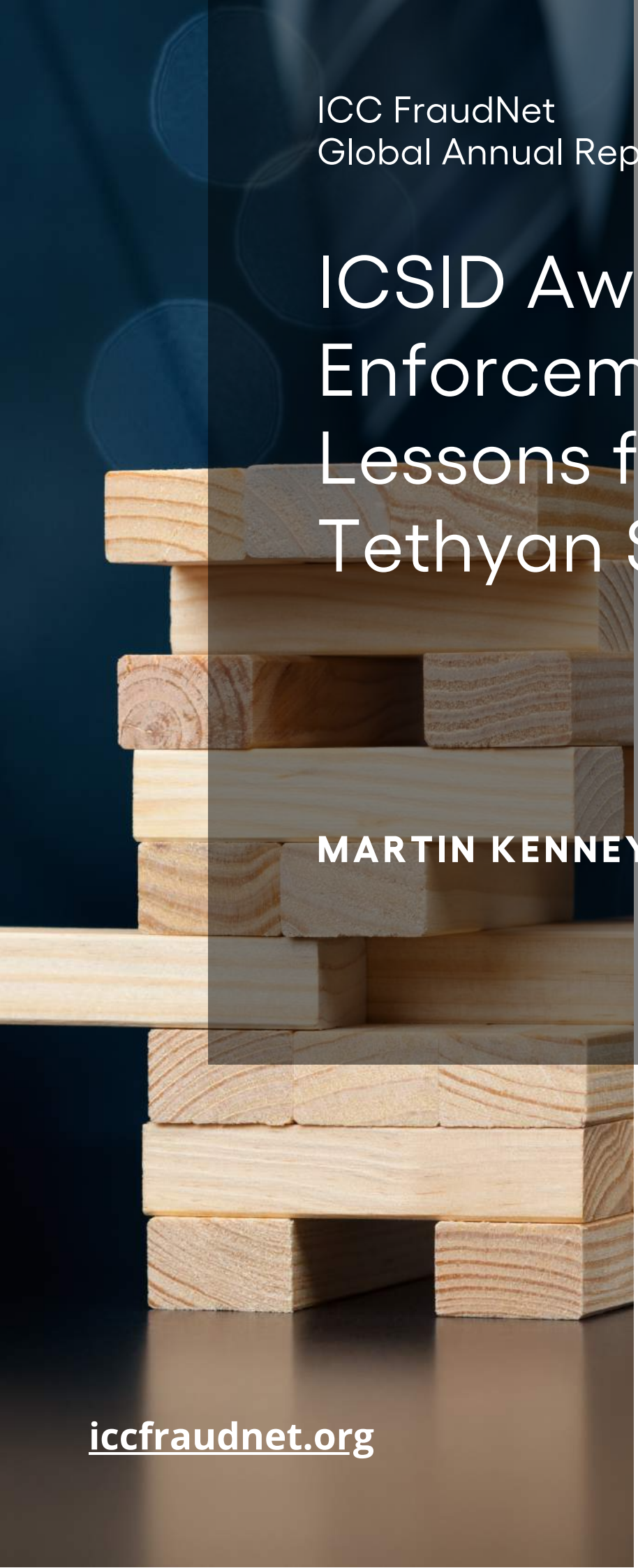
The majority of the funds 'frozen' by the applicant were ultimately frozen and returned to the applicant as the respondents failed to oppose the application (not surprisingly, given that they would be exposing their identities).

Conclusion & Practical Considerations

The use of the anti-dissipation interdict is not without difficulties. It can, however, be effectively used. Critical to the effectiveness of such a litigation tool is to move expeditiously. The team of lawyers need to have the skill set, capacity and relationship with the court's registrars to prepare, file and move an urgent application in the space of a few hours. Taking too long to deliberate on whether to proceed or not risks the funds being very quickly moved (often offshore) and fragmented making the asset recovery process more complex, costly and less likely to obtain recovery.

A key practical consideration which South African policy makes need to consider is the role and obligation on banks to take steps to freeze accounts prior to a court order being obtained. Currently banks require a court order before taking any such steps. This clearly undermines the efficacy of freezing orders because even the most expeditious freezing orders will take some time and are not immediate. Whether banks could be held liable for failing to freeze accounts despite being alerted to such fraud is a subject for another paper.

In conclusion, while our State institutions have demonstrated great difficulty in swiftly moving to detect and preclude fraudulent funds flowing in or offshore, the civil rules and courts in South Africa do provide some relief for victims of such fraud, if they react promptly and decisively.



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ICSID Award Enforcement Risk: Lessons from the Tethyan Saga

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ICSID Award Enforcement Risk: Lessons from the Tethyan Saga

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Abstract

In this article, Martin Kenney examines how a decade of multi-jurisdictional arbitral and enforcement proceedings ("the Tethyan saga") provides a case study in the consequences of ICSID award enforcement risk.

Introduction

States tend to comply with arbitral awards rendered under the ICSID Convention, the leading international treaty governing the resolution of investment disputes by arbitration.[1] The content of the ICSID (International Centre for Settlement of Investment Disputes) Convention and the incentive framework it creates, leaves little room for award-debtors to challenge awards. Despite this pro-enforcement posture, ICSID awards are always exposed to some measure of enforcement risk. The Tethyan saga, a decade of multi-jurisdictional arbitral and enforcement proceedings, provides a case study in the quantity and consequences of ICSID award enforcement risk.

The ICSID Convention was designed to robustly promote state compliance with

[1] Anastasiia Filipiuk, *Enforcement of Arbitration Awards and Sovereign Immunity*, Central European University, 15 April 2016, https://www.etd.ceu.edu/2016/filipiuk_anastasiia.pdf; Mayer Brown, *Enforcement of Awards in ICSID Arbitration*, December 2011, https://www.mayerbrown.com/en/perspectives-events/publications/2011/12/enforcement-of-awards-in-icsid-arbitration.

ICSID awards. Article 54 of the Convention requires all contracting states to recognise awards rendered and enforce pecuniary obligations. Article 52 of the Convention substantially limits the scope of award-debtor interference with enforcement. Pursuant to Article 52, the ICSID annulment process, unlike the annulment process of some non-ICSID investor-state arbitrations, is self-contained and autonomous from domestic law, ensuring that ICSID arbitrations are not subject to the supervisory jurisdiction of state courts.

Despite the robust ICSID pro-enforcement posture, there is still substantial scope for dilatory/guerrilla tactics that increase enforcement risk. The rate of Article 52 annulment applications, for instance, has increased dramatically over the past decade. From 2010-2019, the increase in the rate of annulment proceedings outpaced the increase in the rate of ICSID awards by 77%.[2] Generally, such enforcement risk is largely dependent on the identity of the award-debtor. In respect of annulment proceedings, Argentina, Venezuela, and Spain account for 44% of all annulment applications submitted by states.[3] As the Tethyan matter demonstrates, dilatory tactics reduce the certainty of recovery, and incentivise post-award settlement to the detriment of the award-creditor.

The Tethyan saga

The Tethyan arbitration saga provides a counterexample to the broader trend of ICSID award-debtor compliance, and demonstrates the consequences of state resistance to award recognition and enforcement.

In 2000, Tethyan Copper Company (TCC) – an Australian 50-50 joint venture between Barrick Gold Corporation of Australia and Antofagasta PLC of Chile – created a subsidiary in Pakistan. Tethyan engaged with Balochistan, a Pakistani province, in a joint venture agreement (CHEJVA) for exploration of mineral deposits. In 2011, after investing more than US$220 million and discovering substantial gold and copper deposits, Tethyan applied for a mining licence. Balochistan denied the application.

Tethyan appealed the administrative decision denying the application, but was unsuccessful despite exhausting domestic remedies. Ultimately, the Supreme Court of Pakistan held that CHEJVA, the Tethyan-Balochistan joint use agreement, was void on the grounds that (1) Balochistan had exceeded its powers, and (2) the

[2] Johannes Koepp, Yarik Kryvoi and Jack Biggs, *Empirical Study: Annulment in ICSID Arbitration*, 2021, The British Institute of International and Comparative Law (BIICL) and Baker Botts LLP, https://www.biicl.org/documents/10899_annulment-in-icsid-arbitration190821.pdf.
[3] Johannes Koepp, Yarik Kryvoi and Jack Biggs, *Empirical Study: Annulment in ICSID Arbitration*, 2021, The British Institute of International and Comparative Law (BIICL) and Baker Botts LLP, https://www.biicl.org/documents/10899_annulment-in-icsid-arbitration190821.pdf.

agreement was contrary to public policy.[4]

In arbitral proceedings, Tethyan had greater success on the same facts. In 2014, it obtained a favourable preliminary ruling in an ICC (International Chambers of Commerce) arbitration claim based on the Tethyan-Balochistan joint use agreement.[5] In July 2019, Tethyan obtained a partial award in an ICC arbitration seated in London.[6] Beginning in 2011, Tethyan pursued an ICSID claim against Pakistan, alleging a breach of the fair and equitable treatment, expropriation, and non-impairment obligations under the Australia-Pakistan Bilateral Investment Treaty (BIT).[7] In the ICSID proceedings, Pakistan objected on the grounds of jurisdiction, admissibility, and alleged corruption. The tribunal rejected all objections. The tribunal found for Tethyan on the merits, awarding more than US$5.9 billion in compensation, interest, and legal costs.[8]

In contrast to its considerable success in obtaining favourable arbitral awards, Tethyan faced an uphill battle to enforce its ICSID award. It prevailed in enforcement proceedings in the US, but only after lengthy litigation. After the ICSID tribunal issued the award in the Tethyan matter, Tethyan petitioned the US District Court for the District of Columbia to recognise and enforce the award. Pakistan then sought two remedies before ICSID – annulment of the award, or revision of the award. These proceedings precipitated a stay of enforcement by ICSID.[9]

In response, the US District Court for the District of Columbia itself stayed proceedings. Upon expiry of the ICSID stay, Pakistan petitioned the District Court to continue to stay enforcement of the award. The District Court dismissed Pakistan's petition, holding that, *inter alia*, Tethyan had already waited over a decade for compensation, and Pakistan had provided no guarantee that it would not use the stay to deplete its US assets.[10] Despite its ultimately favourable outcome, Tethyan was prejudiced by the delay in enforcement caused by the US District Court's stay in proceedings, which changed the negotiating posture of the parties to a prospective post-award settlement.

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[4] *Maulana Abdul Haque Baloch & others v. Government of Balochistan thr. Secy. Industries & Mineral Development & others* [2013] SCMR 511, [2013] SCP 53.
[5] *Province of Balochistan v Tethyan Copper Company Pty Ltd,* [2021] EWHC 1884 (Comm), 24.
[6] *Province of Balochistan v Tethyan Copper Company Pty Ltd,* [2021] EWHC 1884 (Comm), 2.
[7] ICSID, *Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan (ICSID Case No. ARB/12/1)*, https://icsid.worldbank.org/cases/case-database/case-detail?CaseNo=ARB/12/1.
[8] ICSID, *Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan (ICSID Case No. ARB/12/1)*, https://icsid.worldbank.org/cases/case-database/case-detail?CaseNo=ARB/12/1.
[9] ICSID, *Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan (ICSID Case No. ARB/12/1)*, https://icsid.worldbank.org/cases/case-database/case-detail?CaseNo=ARB/12/1.
[10] *Tethyan Copper Co. Pty Ltd. v. Islamic Republic of Pakistan*, 590 F. Supp. 3d 262 (D.D.C. 2022).

Enforcement proceedings in the BVI

Tethyan was less successful in enforcement proceedings in the British Virgin Islands ('BVI'). After moving to enforce the ICSID award, the BVI first instance court granted Tethyan an *ex parte* order against the state of Pakistan, and against a range of other entities associated with the state of Pakistan. These associated entities included Pakistan International Airlines ('PIA'), which was incorporated in the BVI.

The *ex parte* orders included the recognition and enforcement of the US$6 billion ICSID Award, and a provisional charging order over the BVI assets of PIA, which included estimated US$1 billion of assets in contest held by PIA's BVI holding company. Through several layers of vertical subsidiaries, this holding company owned the titles to a luxury hotel in Paris, and to the Hotel Roosevelt in New York City, which occupies a city block next to Grand Central Terminal.

In seeking and obtaining these *ex parte* orders, Tethyan relied on the Privy Council decision in *La Générale des Carrières et des Mines v. FG Hemisphere Associates LLC* [2012] UKPC 27 (Gécamines) for the proposition that PIA was so closely associated with the state of Pakistan as to be the proper source for the enforcement of an award against the state of Pakistan. The effect of the charging order was to treat PIA as assimilated into the state for all purposes, and thus a valid source of recovery.

In a return date hearing, the BVI Commercial Division of the Eastern Caribbean Supreme Court set aside the original *ex parte* orders on several grounds.[11] The Court held that *Gécamines* did not support enforcement of the Tethyan award against PIA. The Privy Council in *Gécamines* established that, *inter alia*, there was a strong presumption that separate corporate identity should be respected, and enforcement against an entity related to a state was only proper where that entity and the state had "no separate effective existence".[12] In the Tethyan matter, the BVI Court held that PIA did have a separate corporate identity, and the strong presumption of separate identity was not rebutted because PIA was publicly traded and had private shareholders, and thus PIA did have "separate effective existence" from the state of Pakistan.[13]

Further, in the return date hearing, Tethyan argued that Pakistan had waived immunity and submitted to enforcement jurisdiction by agreement to the ICSID Convention. The BVI Court disagreed:

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[11] *Tethyan Copper Company Pty Limited v Islamic Republic of Pakistan et al.* (BVIHC (COM) 2020/0196).
[12] *La Générale des Carrières et des Mines v. FG Hemisphere Associates LLC* [2012] UKPC 27.
[13] *Tethyan Copper Company Pty Limited v Islamic Republic of Pakistan et al.* (BVIHC (COM) 2020/0196).

> "TCC advanced a new case at the substantive return date that there was a submission by agreement in the ICSID Convention itself. This is said to be clear from all the textbooks and the case law. However, the ICSID Convention is a treaty that can have no effect under domestic law in and of itself. That includes, for present purposes, the United Kingdom position on state immunity…"[14]

The BVI Court's reasoning applied a narrow construction of the terms of the ICSID Convention. The Court appeared to have limited its inquiry to the question of Pakistan's obligations pursuant to the ICSID Convention, rather than inquiring whether, as a consequence of ICSID, award-debtor states agree that other parties to the ICSID Convention have jurisdiction to enforce an ICSID award. The reasoning of the BVI Court in this respect was roundly criticised in a subsequent New Zealand High Court decision:

> "I do not agree with the analysis of the British Virgin Islands High Court in *Tethyan Copper Company Pty Ltd v Islamic Republic of Pakistan and Anor*. The Court there concluded that art 54(1) of the ICSID Convention placed no international obligation on Pakistan, and accordingly could not involve a waiver of its immunity. But it is not a matter of identifying whether the state who is a party to the award itself has an obligation under art 54(1) of the ICSID Convention or not. It is a matter of identifying what that state has agreed are the obligations of other states, implemented in their judicial systems. Such agreement is clear from the articles as a whole …".[15]

Despite some surprising and unfavourable results in enforcement proceedings, Tethyan was able to obtain a relatively attractive provisional settlement. The March 2022 provisional out-of-court settlement provided the Tethyan Copper Company joint venture co-parties with various sums.

Antofagasta Copper will receive $900 million, while Barrick Gold will be authorised to extract the mineral deposits discovered in 2011. Barrick Gold will also make a US$3 billion investment in Pakistan in order to engage in this extraction. As of 9 December 2022, the Supreme Court of Pakistan has approved the settlement agreement, holding that it did not violate the Supreme Court's prior verdict, which had voided the original Tethyan-Balochistan joint use agreement.

[14] *Tethyan Copper Company Pty Limited v. Islamic Republic of Pakistan et al.* (BVIHC (COM) 2020/0196), para. 50.
[15] *Sodexo Pass International SAS v Hungary* [2021] NZHC 371 (10 December 2021), para. 28.

Conclusion

Tethyan presents a useful case study in award-creditor enforcement risk for parties to ICSID arbitration. As Tethyan discovered through extensive enforcement proceedings, the inherent uncertainty of multi-jurisdictional litigation, and the nature of the award-debtor's foreign-held assets, can limit the recoverable scope of ICSID awards. Despite the pro-enforcement posture of the ICSID Convention, and the incentive structure that the Convention creates, ICSID awards remain vulnerable to award-debtor resistance to enforcement.

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Are Banks Liable for "Ponzi Schemes"?

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Are Banks Liable for "Ponzi Schemes"?


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Abstract

This article will refer to AML requirements imposed on banks, the supervisory body of banks, and their potential controlling measures and will present the Hungarian liability rules including contractual and delictual liability with special regard to banks' responsibilities. Here, Gábor Damjanovic and Réka Bali approach the question of what can be done if banks cause financial damages to private individuals by their breach of AML obligations. In the course of this, we analyse a recent case which could be relevant for establishing liability of banks.

AML requirements

In line with the provisions of Act LIII of 2017 on the Prevention and Combating of Money Laundering and Terrorist Financing ('AML Act'), banks must identify their clients, the proxy thereof, the person with the right of disposal acting with the banks and the representative acting with the banks, and must also perform a verification of their identity. Additionally, banks must require the presentation of documents to verify the clients' and the ultimate beneficial owners' ('UBO') identity and ensure that clients' data is valid and up to date.[1]

Banks must continuously monitor the business relationship – including the analysis of transactions performed during the existence of the business relationship – to determine whether the transactions are in accordance with the

[1] Section 7 of AML Act and Section 12 of AML Act

data available to the banks regarding the client and dictate whether it is necessary to perform measures against the client in the scope of preventing money laundering.[2]

Generally speaking, if a bank employee suspects a high money laundering risk of their client in connection with a transaction, the bank employee must apply risk mitigation measures and further identify the client including the analyses of the client's ownership structure in registers available or request a statement regarding the source of funds and assets (in particular, a contract or other official document deriving from the inheritance, proof of income, document related to exchange rate gains, prizes, dividend).

Bank employees must promptly make a report to a person in charge of any data, fact or circumstance indicating money laundering that originates from a crime. Subsequently, a person in charge must forward the report on behalf of the bank to the financial intelligence unit which is a specific organisational unit of the National Tax and Customs Administration.[3]

Non-compliance with AML rules

Can lost funds be recovered in civil procedures? What if the bank fails to comply with its AML obligations determined above as a result of which the fraudulent investment operation remains undetected and thereby private individuals suffer loss. In the following passages, we assess the possibility of a civil lawsuit being brought against the bank by the scammed investors with the aim of establishing the bank's responsibility based on non-compliance with AML rules and awarding compensation to the scammed investors.

First of all, we need to look at what the supervisory body of Hungarian banks can do if it detects the infringement of AML rules.

Failing to duly perform the AML obligations, the supervisory body may apply measures (such as warnings, fines and/or suspension of activity) proportional to the severity of the infringement.[4] In Hungary, the Hungarian National Bank ('MNB') is the supervisory body of banks. [5]

In the following passages, we describe a recent example of the MNB's supervision activity.

[2] Section 11 of AML Act
[3] Section 30 – 31 of AML Act
[4] Section 69 of AML Act
[5] Section 5 point a) of AML Act

In 2022, the MNB found weaknesses in OTP Bank's[6] internal control and information system due to improper operations. MNB established that the bank's filter system was not functioning properly as the filtering criteria for the detection of unduly large and cumulatively significant cash withdrawals and were not able to detect unusual transactions. Therefore, the bank did not become aware of suspicious transactions that would have had indicated a reporting obligation. As a result, the bank was not able to fulfil its AML obligations or identify cases where further risk mitigation measures - such as obtaining proof of funds or refusing to execute further transactions - were warranted.

Due to the non-compliance with AML rules, the MNB: (i) imposed a fine of HUF 2.200.000 (approximately EUR 5,500) on the bank; (ii) obliged it to further develop and review its AML reporting, monitoring, and source of funds verification practice; and (iii) obliged it to conduct an internal investigation to assess the effectiveness of the above systems.[7]

Although the amount of the fine and the obligation may not seem significant, the finding of an AML infringement by the MNB may create an opportunity for individuals to enforce their claims against the bank.

Contractual and delictual liability rules

The Hungarian civil law liability for extra-contractual (delictual) damages and the liability for damages caused by breach of contract (contractual) are separated from each other and are regulated independently. The essence of this separation is that while liability for breach of contract is based on the concepts of foreseeability and the sphere of interest, the liability for extra-contractual damage is still based on the fault of the tortfeasor. Contractual liability differs from extra-contractual liability in two respects: in the stricter exculpation[8] and in the scope of damages to be compensated.[9]

Due to this distinction, it is important to clarify which form of liability applies if an individual wishes to claim damages against a bank for a breach of AML rules. Since, in this case, the individual does not have a contractual relationship with the bank but only with the fraudster who committed the Ponzi scheme and used a bank account for the fraud, the individual can only bring an action against the banks' unlawful conduct under the rules of extra-contractual liability.

[6] OTP Bank Group is the largest commercial bank of Hungary providing banking services for private individuals and corporate clients.
[7] MNB's Decision No. H-PM-I-B-2/2022.
[8] Section 6:142 of the Act V of 2013 on the Civil Code (**Hungarian Civil Code**)
[9] Section 6:143 of the Hungarian Civil Code

The Hungarian Civil Code clearly states the general prohibition of causing damages, and therefore, with statutory exceptions, all tort is unlawful. As a result of this rule, if the injured party proves that his/her damage was caused by the tortfeasor's conduct, the unlawfulness of the tort is presumed by law and the burden of proving the lawfulness of the tort lies with the tortfeasor.

However, an important limitation of liability for damages is that there must be a causal link between the damage and the harmful conduct. The tortfeasor is not liable for damages that are distant from the harmful conduct. Causation cannot be established for damage that the tortfeasor did not foresee and could not have foreseen. The Supreme Court of Hungary (‘the Curia’) set out in one case that the question is whether the initiator of the series of events leading to the harm saw or could have seen the result that would occur. It is important to note that the tortfeasor does not need to foresee the full causal process leading to the damage, but only to recognise the nature and extent of the damage that the conduct or omission may cause. The test here is not the consciousness of the given tortfeasor, but what a person acting with due care could foresee. Liability for damages arises when a reasonably diligent person, having regard to the likelihood of such a risk, must have assumed it.

For example, there was a case in Hungary initiated by a person who was diagnosed with a highly aggressive tumour caused by his exposure to asbestos while he was living 50 meters away from a factory that used this harmful substance between the early 1970s and 1990s. The case resulted in a multi-round court proceeding, where the Curia eventually ordered a retrial. At the first time, the first instance court dismissed his statement of claim, but subsequently, in the repeated procedure ordered by the Curia, it ruled against the owner of the factory, the Hungarian State and established the liability on the ground that - within the framework of neighbour rights - the owner is obliged to refrain from unlawful conduct that unnecessarily disturbs the neighbours.

To exclude liability, the Hungarian Sate had to prove that it did not know or, even with due care, should not have known that asbestos entering the air and polluting the environment in connection with the activity carried out on its property is harmful to health and is carcinogenic. The Hungarian State did not dispute the causal link between the damage and the harmful conduct on the scientific level but from the legal perspective. The Hungarian State stated that the causal link would only exist if the defendant could foresee the occurrence of the serious, possibly fatal illness at the time of the damage.

Regarding causation, the court highlighted that it only expects probability that cannot be challenged beyond a reasonable doubt. The court stated that early

knowledge of asbestos and its harmful effects were known by the defendant in 1975 and embodied in the defendant's legislation. The lack of precise knowledge in the course of the damaging process does not make the damage "unforeseeable", so it does not interrupt the causal link. Hence, the defendant foresaw, or was able to foresee, that the use of asbestos could infringe the personal rights of others.

Knowing the harmful effect of asbestos, the question arises as to what the defendant has done to prevent endangering the workers or the citizens. In the present case, there was no data indicating any preventing measures, designating protective distance areas, or relocating playgrounds away from the factory site.[10]
One may ask how this very sad case relates to banks' liability for damages ari áll cég sing from non-compliance with AML rules. In our view, the importance of this decision may be that even in cases where the link between the damage and the conduct of the tortfeasor seems at first sight distant and the damage is caused by negligence, liability for damages may be established.

What can make it difficult to establish the bank's liability is how to prove to the court that the bank has actually breached its money laundering obligations. This is where the MNB's supervisory activities can help, because if the MNB has found that a bank has not complied with money laundering rules during the period relevant to us, this can be strong evidence against the bank in a court case.

Conclusion

In closing, let us imagine a fictive case where a private individual is a victim of a Ponzi scheme which is generated by a fake company fraudulently obtaining and laundering money through bank accounts. The question is whether the victim can bring and win a lawsuit against the bank? Based on the previously presented case and discussion, we believe that there is a chance of winning such a case, although, the question is very complex and compound for the following reasons. The relationship is extra-contractual / delictual between the bank and the victim in the absence of a contractual relationship. Hence, providing proof that the damage was caused by the bank to support the bank's responsibility could be difficult but a decision establishing the bank's negligence in complying with AML obligations could help to win the case – such as the MNB's decision establishing the bank's negligence due to non-compliance.

[10] Metropolitan Court's Decision No. 38.P.20.956/2019/37

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Serious Fraud Litigation in Malaysia – Trends and Relief

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Serious Fraud Litigation in Malaysia – Trends and Relief

LEE SHIH & NATHALIE KER

Abstract

In this article, Lee Shih and Nathalie Ker of Lim Chee Wee Partnership, Kuala Lumpur, discuss the recent tr ends in fraud litigation in Malaysia. They provide an overview of the various facets of large-scale fraud litigation, from interim relief such as freezing and search orders, to concurrent investigations by law enforcement authorities and tracing of stolen monies.

Introduction

In recent years, large-scale fraud litigation matters in Malaysia have been constantly in the news. We will touch on recent trends, interim relief available in Malaysia, the involvement of law enforcement authorities, and how tracing of monies is carried out in Malaysia. We further set out briefly the various methods of enforcement in Malaysia.

Recent Trends in Fraud Litigation

Malaysia's fraud litigation arena has recently seen a number of serious fraud matters with claims in the hundreds of millions. The infamous 1 Malaysia Development Berhad ('1MDB') case and the subsequent criminal conviction of

Malaysia's ex-prime minister Najib Abdul Razak,[1] was just the beginning of a slew of cases where directors and ex-employees were sued for fraud involving mismanagement of monies on a large scale.

In December 2021, the High Court finally handed down judgment in one of the longest-running fraud cases in Malaysia. Damages of more than USD $44 million was awarded to the plaintiff, Toyota Tsusho (M) Sdn Bhd ('Toyota'), after 5 years of litigation. This was a matter where a senior manager in Toyota, a plastics trading company ultimately owned by public-listed Toyota Tsusho Corporation in Japan, had been secretly siphoning monies out of the company. Toyota had been paying for what were fake super engineering plastics, and where an intricate web of deceit involving fake payment documentation and cancellation of invoices made it seem as if inventory was moving when it was not. The web of deceit extended to various employees, suppliers, and other associates of the main fraudster.[2] The suit is currently on appeal in the Court of Appeal.

Also in December 2021, a suit was filed by Johor Corporation, the state-owned conglomerate of Johor, against its previous Chief Executive Officer ('CEO') and other defendants. The suit is ongoing and is for approximately USD $53 million for alleged fraud which spanned 12 years. The alleged fraud is regarding monies invested by Johor for a development of a 'global logistics system' which was never commercialised. Monies were allegedly dissipated to various international entities in Ireland, Switzerland and the United States of America.[3]

In mid-2022, Malaysia's largest development bank, Bank Pembangunan Malaysia Berhad ('BPMB'), filed a suit for more than USD $141 million against its former President and Group CEO and 26 other defendants for alleged bribery and fraud. This is in relation to the disbursement of loan monies to a company for a telecommunications network project which was allegedly never completed.[4]

Interim Relief in Malaysia

[1] See "Najib Razak: Malaysia's ex-PM starts jail term after final appeal fails", BBC News, 23 August 2022 <https://www.bbc.com/news/world-asia-62642643> (last accessed on 3 January 2023).
[2] For the related criminal proceedings, see "More charges slapped on ex-company manager", The Sun Daily, 17 January 2017, https://www.thesundaily.my/archive/2129714-ATARCH421661 (last accessed on 3 January 2023).
[3] For the related criminal proceedings, see "Former head of GLC JCorp charged with nearly RM10m investment fraud", Malay Mail, 22 March 2022 <https://www.malaymail.com/news/malaysia/2022/03/22/in-johor-former-jcorp-president-accused-of-investment-fraud-totalling-nearl/2048811> (last accessed on 3 January 2023).
[4] See "Bank Pembangunan sues former MD and 26 others for alleged fraud, bribery", The Edge Markets, 29 June 2022, <https://www.theedgemarkets.com/article/bank-pembangunan-sues-former-md-plus-26-others-fraud-and-bribery> (last accessed on 3 January 2023).

There are a number of available urgent reliefs which may be obtained in the Malaysian courts in aid of fraud litigation. These include freezing and search orders, Bankers Trust discovery orders, and Norwich Pharmacal discovery orders. More recently, the High Court granted a Norwich Pharmacal order against a cryptocurrency exchange with an office in Malaysia. This was in aid of an investigation by liquidators of the wound-up New Zealand cryptocurrency exchange, Cryptopia Limited.[5] The liquidators had applied for the order to assist in recovery efforts of stolen cryptocurrency of more than USD $41 million, where some of the cryptocurrency had been traced into Malaysia.

Investigations by Law Enforcement Authorities

In most instances in Malaysia, the initiation by a victim of investigations into fraudulent conduct will involve and proceed concurrently with the investigation by law enforcement authorities.

The authority in charge of investigation and prevention of corruption and abuse of power is the Malaysian Anti-Corruption Commission ('MACC').[6] Separately, the Royal Malaysia Police ('RMP') conduct their own investigations where police reports have been made. There are also efforts made by the MACC to engage and corporate with international law enforcement agencies where the fraud extends outside of Malaysia. For example, where targets reside outside of Malaysia or where funds are traced to sources out of the jurisdiction.

Concurrent Criminal and Civil Proceedings

Where either the MACC or the RMP recommend a matter for prosecution to the Attorney General of Malaysia, the Attorney General may choose to bring criminal proceedings against the alleged fraudsters. Again, this is often done concurrently with civil proceedings.

The courts in Malaysia have an inherent discretion to stay civil proceedings in light of concurrent criminal proceedings. One of the factors which would be considered

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[5] See "Liquidators' Eighth Report on the State of Affairs of Cryptopia Limited (in Liquidation)", 12 December 2022 <https://www.grantthornton.co.nz/globalassets/1.-member-firms/new-zealand/pdfs/cryptopia/eighth-liquidators-report_cryptopia.pdf> (last accessed on 3 January 2023). For an article on the hack and liquidation of Cryptopia Limited, see "Liquidation of hacked cryptocurrency firm Cryptopia heading towards $15m", 3 January 2022, <https://www.stuff.co.nz/national/127401736/liquidation-of-hacked-cryptocurrency-firm-cryptopia-heading-towards-15m> (last accessed on 3 January 2023).

[6] See the MACC's website at <https://www.sprm.gov.my/index.php?id=21&page_id=75&articleid=463> (last accessed on 3 January 2023).

by the courts would be whether there is a real danger of injustice in the criminal proceedings.[7]

Information and evidence which could be useful for the civil litigation may sometimes arise from the criminal proceedings. Where necessary, an application to the court in the civil proceedings may be made to admit evidence such as statements made by the accused in the criminal proceedings.

Tracing of Funds – the Role of Professionals

Where the matter is a complex one, which is generally the case for serious fraud, there is a need for a team of different professionals to ensure that the best strategy for civil recovery is adopted. In Malaysia, a forensic consultant is usually employed at the very start in order to unearth the various facets of the fraud. The information from the investigation forms the building blocks of the civil litigation. The flow of funds may be further unearthed through information obtained from Bankers Trust orders and other discovery orders. This information would then be fed to the forensic consultant for analysis. Private investigators in Malaysia and overseas are sometimes engaged in order to supplement the information on targets and assets.

Enforcement in Malaysia

Once a judgment is obtained from the civil court, the victim may proceed to enforce the judgment. The most common enforcement options in Malaysia include garnishee proceedings, writs of seizure and sale, bankruptcy and winding up proceedings. Generally, and depending on the amount of monies left in the target bank accounts, the low-hanging fruit would be a garnishee order. Garnishee proceedings in the Malaysian courts are fairly straightforward and efficient. The victim may file a court application to garnish the bank accounts belonging to the judgment debtor. The banks or garnishees would have a chance to object to the garnishee order. Where there is no objection, the order becomes absolute and the banks would have to pay the sums over to the victim.

Conclusion

Serious fraud litigation continues to be on the rise in Malaysia. Litigators, forensic consultants and other professionals will need to form a cohesive team in order to tackle the

[7] See *Suruhanjaya Sekuriti v Datuk Ishak bin Ismail & Anor* [2017] 3 MLJ 478.

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Can the EU Commission's AML Action Plan Reduce Cross-Border Financial Crime within EU Member States?

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Can the EU Commission's AML Action Plan Reduce Cross-Border Financial Crime within European Union Member States?

DIANE BUGEJA & PETER MIZZI

Abstract

In this article, Diane Bugeja, Senior Associate, and Peter Mizzi, Compliance and AML Advisor at Camilleri Preziosi Advocates, assess the upcoming thorough and sweeping changes to be made at EU level with regards to combatting financial crime related to the Money Laundering and Funding of Terrorism. In particular, they examine how the different legislative proposals, such as the introduction of harmonised EU single rulebook and a stand alone AML/CFT supervisor will strengthen the fight against financial crime within the bloc.

Introduction

On 20 July 2021, the European Commission (the 'Commission') formally announced its proposal (the 'Proposal') for a regulation of the European Parliament and of the Council on the prevention of the use of the financial system for the purpose of Money Laundering or Terrorist Financing ('ML/FT')[1]. The proposal consists of an aspiring package that seeks to overhaul the current

[1]COM/2021/420 final

European Union ('EU') Anti-Money Laundering and Countering the Financing of Terrorism ('AML/CFT') regime, focusing on the consolidation and harmonisation in an attempt to overcome existing gaps and loopholes in the current framework, most prominently at the cross-border level. This article will mainly focus on the introduction of new rules, updates and reforms, particularly relevant to reducing cross-border crime among Member States ('MS'), originating from the following legislative proposals;

- this proposal for a Regulation on the prevention of the use of the financial system for the purposes of ML and FT;
- a proposal for a Directive establishing the mechanisms that Member States should put in place to prevent the use of the financial system for ML/TF purposes, and repealing Directive (EU) 2015/849[2];
- a proposal for a Regulation creating an EU Authority for anti-money laundering and countering the financing of terrorism ('AMLA')[3]; and
- a proposal for the recast of Regulation (EU) 2015/847 expanding traceability requirements to crypto-assets[4].

Shortcomings with the existing EU AML/CFT framework

Illicit flows emanating from financial crime represent a severe threat to the reliability and stability of the EU economy and the financial system, as well as to the safety and security of EU citizens. Estimates from Europol, indicate that around 1% of the EU's Annual Gross Domestic Product is 'detected as being involved in suspect financial activity'.

This comes as no surprise when considering the major scandals that have rocked the Union over the last decade. In particular, the Danske Bank[5], Deutsche Bank AG[6] and Latvia ABLV Bank AS[7] scandals have seriously damaged the integrity and reputation of the EU as a financial services hub.

This was further corroborated by the Commission in 2019, which revealed that criminals have long exploited disparities in AML/CFT regimes among MS. Thus, EU action is warranted to ensure a fair playing field throughout the Union, with obliged entities in all Member States subject to a consistent and harmonised set of

[2] COM/2021/423 final
[3] COM/2021/421 final
[4] COM/2021/422 final
[5] https://www.nytimes.com/2019/02/20/business/danske-bank-estonia-money-laundering.html
[6] https://www.fca.org.uk/news/press-releases/fca-fines-deutsche-bank-163-million-anti-money-laundering-controls-failure
[7] https://www.govinfo.gov/content/pkg/FR-2018-02-16/pdf/2018-03214.pdf

AML/CFT obligations. Moreover, given the cross-border nature of financial crime, it is critical that member states, national supervisors, and Financial Intelligence Units ('FIUs') cooperate and coordinate with each other in sharing and dissemination of intelligence.

1. ***A regulation establishing an EU AML/CFT authority (in the form of a decentralised EU regulatory agency)***

The proposal for a Regulation creating the Anti-money laundering authority ('AMLA') establishes an integrated, EU-level supervisor for combatting ML/FT whilst also acting as a support and cooperation framework for FIUs (which takes the form of a Directive as seen below).

Following the successful implementation of the EU AML single rulebook (discussed hereunder), the AMLA will be at the heart of a revamped EU AML/CFT supervisory system, directly supervising the highest-risk financial institutions that operate in a large number of MS. Through the AMLA's coordination of national supervisors, it will indirectly supervise the remaining financial and non-financial entities that fall under the EU AML/CFT framework.

The AMLA will possess the power to act on its own behalf if it is found that the local supervisory regime is not enforcing EU law. Therefore, it is anticipated that regulatory emphasis will shift toward those MS where local regulators have been traditionally less active or effective. Further where an entity, not directly supervised, is exposed to very substantial ML/TF risk, then financial supervisors need to provide formal notification to the AMLA.

With respect to FIUs (national regulators), the AMLA will be able to obtain relevant information and documentation for it to perform its tasks, as well as issue guidelines and recommendations. AMLA is also expected to provide technical advice on the development of standards and future rules to the European Parliament, European Council and the Commission.

The aforementioned proposals provide the AMLA with the ability to bolster AML/CFT compliance among MS, directing its attention to high-risk areas and situations where national supervision is lacking, as necessary.

2. *A new regulation on AML/CFT, containing directly applicable rules, include revised EU list of entities subject to AML/CFT rules (known as Obliged Entities)*

Data extracted from Commission reports in 2019, confirmed the necessity for the introduction of harmonised regulations across the internal market. These studies found that, while the provisions of Directive (EU) 2015/849 and Directive (EU) 2018/843 are broad, their lack of direct applicability, and delayed transposition, resulted in various interpretations and fragmentation across MS. Consequently, issues with the existing EU AML/CFT frameworks has made it difficult to tackle cross-border financial crime. The Commission notes that scandals across MS disrupt the functioning of the single market and leading to reputational damage. In a bid to avoid regulatory divergences and other aforementioned issues, going forward AML/CFT rules applicable to obliged entities will take the form of regulation as opposed to a directive.

However, the proposal does not merely mean a transfer of existing provisions from AML/CFT directives to a regulation but rather several changes of substance are made in order to bring about uniformity and convergence in the application of AML/CFT rules across the EU.

Increased scope of obliged entities:

Crypto-Asset Service Provides ("CASPs"), unregulated crowdfunding platforms, creditors for mortgage and consumer credits and associated intermediaries as well as investment migration operators are now considered obliged entities and thus subject to the AML/CFT framework. In addition, AML/CFT requirements will no longer apply to person trading in goods. On the other hand, dealers in precious metals and stones are often considered high risk in terms of ML/FT and shall continue applying AML/CFT obligations.

Internal Policies, controls and procedures:

Building on existing EU AML/CFT legislation, the new requirements provide clarity on how obliged entities are to identify, analyse, mitigate and monitor ML/FT risks through the implementation of AML/CFT policies, controls and procedures. Management is to ensure that compliance functions and roles are adequately resourced and take responsibility to ensure that staff are properly trained and aware of the AML/CFT obligations.

Customer due diligence measures:

Most of the existing Customer Due Diligence ('CDD') requirements will take the form of regulatory technical standards provided by the AMLA and will be transferred from the current AML/CFT rules. Despite this, several proposals will provide transparency and further detail on CDD obligations. Harmonised and uniform rules on CDD will reduce national divergence, allow for consistent application and thus create a level playing field across MS that is harder for criminals to misuse or redirect their efforts towards the weakest link in the chain. However, obliged entities are to ensure the application of CDD requirements following a risk-based approach, through evidence-based decision-making processes that target ML/FT risks more efficiently and effectively.
Specific and detailed provisions are laid down on identification and verification processes for natural persons, legal entities, trusts and other legal arrangements, whereas conditions for the use of electronic identification will be clarified. Obliged entities will be required to obtain information on both the source and destination of funds, the estimated amount and economic rationale behind the transactions or activities.

Furthermore, the application of Simplified Due Diligence ('SDD') and Enhanced Due Diligence ('EDD') will be covered in detail, whereas the threshold for applying CDD measures for occasional transactions will be reduced from €15,000 to €10,000, thus triggering additional CDD requirements for entities.

Beneficial Ownership:

Building on existing EU AML/CFT legislation, the proposals for updated beneficial ownership rules will streamline the process of transparency among MS[8]. The concept of holding adequate, accurate and current beneficial ownership information seeks to address the lack of granularity, which allows criminals to exploit divergent application of rules. To mitigate risks of criminals hiding behind nominee arrangements, new disclosure requirements are introduced for nominee shareholder and nominee directors.

[8] The Court of Justice of the European Union ruling delivered on 22nd November 2022 on access to beneficial ownership registers is unlikely to impact transparency in practice, as member states, supervisory authorities and obliged entities will retain their access – only the general public are hereby restricted from unfettered access to beneficial ownership registers.

3. *A proposal for a Directive establishing the mechanisms that Member States should put in place to prevent the use of the financial system for ML/FT purposes, and repealing Directive (EU) 2015/849*

The Regulation creating the AMLA and its accompanying Directive provide a support and collaboration system for FIUs, whereby the AMLA will ensure consistent reporting, assist FIUs with a comparative analysis of STRs and also host the FIU.net platform.

The AMLA will create, exchange, and promote intelligence on ways for detecting and analysing suspicious transactions aimed at enhancing the reporting processes and procedures. Furthermore, to facilitate the understanding and collaboration between obliged entities and FIUs, the AMLA will conduct specialised training and provide assistance to both FIUs and obliged entities. Thus, obliged entities will receive assistance and know-how with respect to detecting suspicious activities/transactions and details on how such are to be report to the respective FIUs. Standardised templates and models will be introduced, to enhance and expedite the reporting process and sharing of information between FIUs at a cross-border level. Obliged entities that operate in multiple MS and tasked with reporting several FIUs stand to benefit the most from standardised reporting procedures and templates.

The AMLA will also be tasked with promoting coordinating and collaborating FIUs efforts in MS. The main goal is to enhance knowledge, share best practice examples, and improve threat/vulnerability assessment all of which will contribute to the publications of studies on ML/FT threats, risks, typologies, and methodologies.

As joint analysis and investigations become more commonplace, the Directive clarifies that variations in MS national laws should not affect the capacity of an FIU in cooperating with another EU counterpart. Should an FIU reject to participate in an inquiry must provide justification to the AMLA. As a result, obliged entities can anticipate an increase in FIU requests for customer information.

The Commission will be tasked with the management, maintenance and hosting of FIU.net platform, until the AMLA is fully up and running. Furthermore, the Directive requires MS to sustain and consolidate information and metrics in relation to the function of their AML/CFT frameworks. In particular, data and information pertaining to the number of reports made to the FIU and the underlying predicate offences.

The lack of feedback provided to obliged entities by FIUs following the submission of a suspicious transaction reports has long been an issue. In response, FIUs will be guided on how they are to respond and provide feedback on ML/FT threats, trends and typologies.

Furthermore, the introduction of centralised automated mechanisms will allow FIUs with direct access to the identity information of payment and bank account holders. Accordingly, the Directive pronounces that such mechanisms will be linked to a single access point administered by the Commission and available to all MS.

Such reforms will be of paramount importance toward resolving the challenges of cross-border information transmission. However, in view of increased sharing of information, obliged entities must ensure that information submitted to the FIUs is of sufficient and accurate quality. Overall, these changes will provide obliged entities with much needed cross-border intelligence which can in turn be used to improve internal ML/FT policies, controls, and procedures.

4. Third-country policy and ML/FT threats from outside the Union

The persistent nature of significant strategic deficiencies emanating from third countries outside the Union, poses a significant threat and thus requires a unified mitigating response at the Union level. The updated strategy proposed by the Commission seeks to implement a harmonised and uniform approach at the Union level as well as a detailed determination of external threats on a risk-based manner. Harmonising EU level mitigating measures seeks to protects MS by providing a framework that is directly applicable, consistent and thus reducing national divergencies, which would expose the entire Union's financial system to risks that are continuously evolving.

Hence, obliged entities should be required to apply the whole set of available EDD measures to business relationships and occasional transactions that involve those high-risk third countries to manage and mitigate the underlying risks.

The AMLA will monitor specific risks, trends and methods to which the Union's financial system is exposed and will communicate with the Union's obliged entities about external threats. Guidelines that define external threats will be provided on regular basis to obliged entities.

In an attempt to reduce ML/FT threats from third countries, the Commission will either follow Financial Action Task Force (‘FATF’) standards in relation to third

countries or carry out its own independent assessment. Third countries so identified by the Commission will be subjected to two different sets of consequences, proportionate to the risk they pose to the Union's financial system:

(i) Third countries "subject to a call for action" by the FATF, informally referred to as the 'blacklist' will be identified as high-risk third countries by the Commission. EDD measures, as well as country-specific countermeasures, will be used to them to appropriately minimise the danger.

(ii) Third-country AML/CFT regimes with compliance deficiencies, defined as "subject to increased monitoring" by the FATF and informally referred to as the 'greylist', will be identified by the Commission and subject to country-specific EDD measures proportionate to the risks.

Furthermore, the Commission may also identify third countries, which are not listed by the FATF, but which pose a specific threat to the Union's financial system and which, on the basis of that threat, will be subject either to country-specific EDD measures or, where appropriate, to all EDD measures and to countermeasures.
Prospectively, additions to the EU's list are expected to align with that of the FATF and hence most obliged entities will already have such jurisdictions classified as high risk. However, they may not currently automatically trigger EDD and thus obliged entities must prepare for more of their customer base to require automatic EDD.

5. A recast of the 2015 Regulation on Transfers (Regulation 2015/847)

The recast of Regulation 2015/847 is closely connected with the proposal for an EU AML/CFT Regulation, whereby crypto-asset service providers will be obliged to conduct due diligence on their customers. In addition, anonymous crypto-asset wallets will be prohibited in the EU.

Present EU rules on the regulation of money transfers have excluded the facet of crypto assets. The Commission notes that ML/FT risks are increasing due to the lack of traceability of these assets. The proposal intends to address this gap by following Recommendation 16 (Travel Rule) of the FATF. Going forward, Crypto-Asset Service Providers ('CASPs') must supplement crypto-asset transfers with information on the sender and beneficiary. This information must be fully shared with its counterpart in the transaction and be readily available in case of requests from competent authorities.

The Regulation requires that, for transfers of crypto-assets, identifiable information must be held on the originator (for example name, address and place and date of birth) and the beneficiary (name and account number) of the transfer. The CASP of the originator needs to verify the accuracy of the information on the originator using an independent reliable source before executing the transfer. The CASP will not be able to execute any transfer of crypto assets until this information has been obtained. This requirement seeks to ensure effective and full traceability of crypto transfers.

The Regulation requires the CASP of the beneficiary to verify the accuracy of the information on the beneficiary using an independent reliable source, before making the crypto-assets available to the beneficiary (for transfers exceeding €1,000, either single or linked). For transfer values below €1,000, the CASP must verify beneficiary information when payment is made in cash, via anonymous electronic money, or where the CASP has reasonable grounds for suspecting ML/FT.

In cases where the information outlined above is incomplete or missing, the CASP of the beneficiary will be required to make a risk-based determination regarding whether to execute or reject a transfer of crypto-assets. The CASP of the beneficiary will be required to report failures to verify accurate information.

Conclusion

The Commission's plan is extensive, ambitious and seeks to completely overhaul the existing AML/CFT legislative framework in a manner that is substantial when compared to its predecessors. The proposals acknowledge that the cross-border nature of ML/FT requires a coherent and consistent approach across MS, based on a single set of rules in the form of a single rulebook. Seeing as the present proposal does not adopt a maximum harmonisation approach, several cross-border loopholes were present throughout the Union, exposing the financial system to risks.

Shifting the form of AML/CFT rules to a Regulation, with more detail than at present in the EU Directive, will promote convergence of application of AML/CFT measures across MS. Such will be based upon a consistent framework against which AMLA will be able to monitor the application of such rules in its function as a direct supervisor of certain obliged entities.

This being said, the application of a risk-based approach remains fundamental to the nature of the EU's AML/CFT regime. In areas where specific national risks

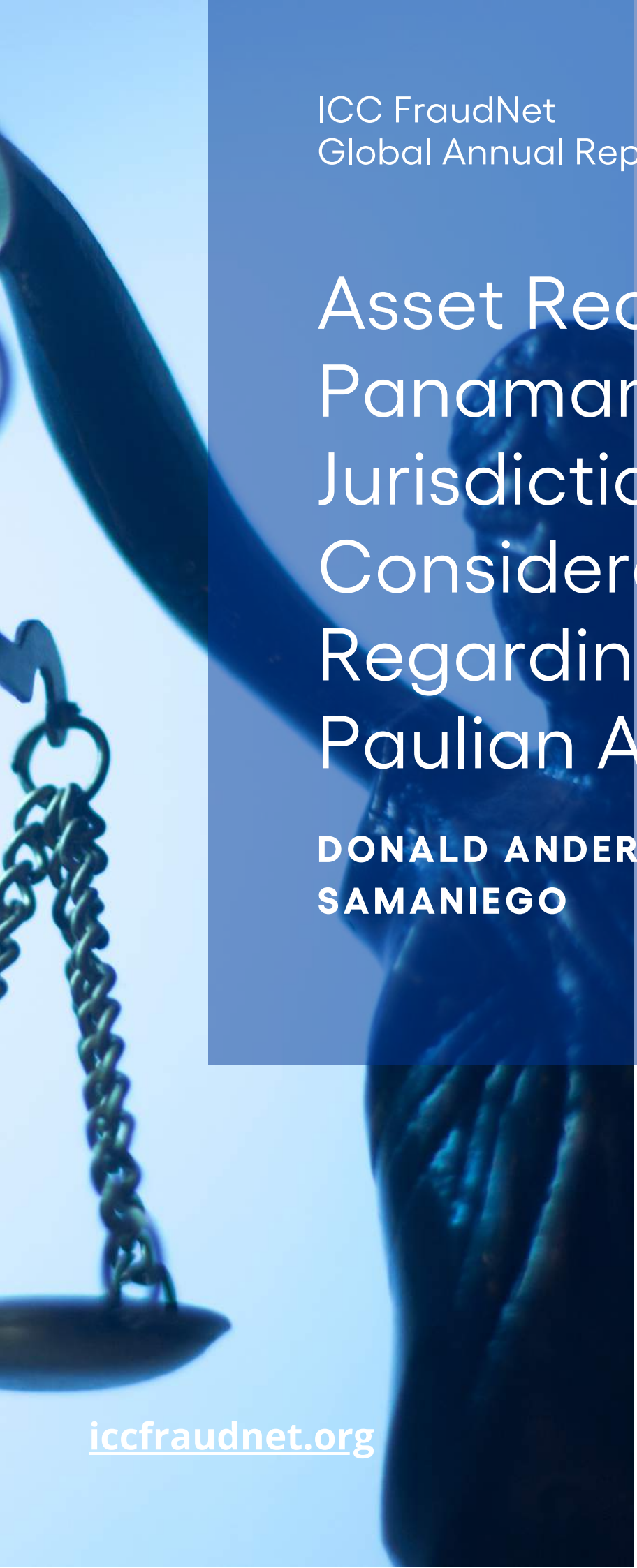
justify it, MS remain free to introduce rules going beyond those laid out in the present proposal. It can be argued that the notion of the risk-based approach may defeat the purpose of having a set of harmonised rules, however, it is anticipated that the application of a risk-based approach will be closely monitored by national supervisors and the AMLA.

The plan to establish a separate, well-resourced EU supervisor promises to increase consistency, uniformity, standards, and degree of AML/CFT supervision across the bloc. AMLA will work toward ensuring that national supervisors apply the single rulebook is applied in a consistent manner.

Nonetheless, obliged entities and FIU may encounter potential compliance challenges such as a lack of cooperation among competent authorities, both at a domestic and cross-border level, creating loopholes that can be misused by criminals. Additionally, these proposals may come into conflict with other key pieces of legislation namely data privacy acts. Obliged entities will be faced with the improbable challenge of complying with conflicting regulations, whereas AML/CFT requires the processing of personal data, data protection regulations restrict such.

In conclusion, providing a harmonised approach to key areas such as the CDD process, identification of beneficial ownership, reporting procedures as well providing clearer rules for AML/CFT risk management, improving cooperation among authorities, the interconnectivity of bank account registers, the traceability of crypto-assets and increased scope of obliged entities, superseded by consistent application by competent authorities and regulators is highly likely to reduce the cross-border element of financial crime.

The final texts of the legislative proposals are subject to change and refinement, as other EU bodies and stakeholders provide feedback. Therefore, MS, national regulators and obliged entities are strongly encouraged to closely monitor the developments in this space.



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Asset Recovery in Panamanian Jurisdiction: Considerations Regarding the Paulian Action

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Assets Recovery in the Panamanian Jurisdiction: Considerations Regarding the Paulian Action

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Abstract

In this article, Donald Sáez Samaniego, associate lawyer at the MDU LEGAL Law Firm in Panama, addresses the conceptual framework of the *Paulian* or *Revocation Action* in the Republic of Panama, as a mechanism for tracing and recovering assets. In addition, he explains the requirements that must be observed and other important elements for these actions to succeed. Based on his professional experience and legal research, the author presents an overview of the applicable law and the procedure of *Paulian Actions* before the courts of the Republic of Panama.

The Paulian action as a method of asset recovery

It tends to happen with some degree of frequency, that a plaintiff presents a pecuniary claim before the Courts of Panama and, after an extensive and exhausting process, the defendant defeated in court, skillfully transfers, or disposes of all his assets, in his search to evade the payment obligation established in a final court ruling.

Such is the case where the debtor's assets are transferred through donations or simulated sales in favor of relatives or partners, with the aim of freeing them from an imminent execution by the victorious claimant and defraud the creditor(s). That is why, in order to do justice to the defrauded creditor, the Panamanian legislator has provided an exceptional formula so that, in cases in which the insolvent debtor

releases his assets in order not to pay his creditor, ownership can be returned or restored to the debtor and then, the defrauded can collect his credit. Likewise, the mechanism entitles the defrauded creditor to exercise all the rights and actions of the fraudulent debtor for the same purposes. This remedy is what the Panamanian legislation understands as *Paulian Action* (or revocation), regulated through its Civil Code.

Conceptually, the Jurisprudence[1] of the First Superior Court of Panama,[2] has defined the *Paulian Action* as: "*the one that is incumbent on creditors to request the revocation of all fraudulent or malicious acts carried out by the debtor to the detriment of his rights*."

In Panama, the legal figure of the *Paulian Action* is regulated by article 996 of the Civil Code, in the following terms:

> "Art. 996: Creditors, after having pursued the assets in possession of the debtor to perform what is owed to them, can exercise all the rights and actions of the debtor for the same purpose, except those that are inherent to his person; They can also challenge the acts that the debtor has carried out in fraud of his right."

The scope of these requirements has been interpreted by the jurisprudence of the Supreme Court of Justice. In view of this, they must be observed by whoever intends to exercise this type of action before the courts of Panama.

Reasons to request for a *Paulian Action* process

This type of process becomes a legal alternative for those creditors who have been defrauded by their debtors. In other words, this action can contribute to the payment of the debt, since what is sought is the revocation of all those fraudulent acts that the debtor has carried out to free himself from his assets and rights and thus render the debt uncollectible. If the action is considered proven, the fraudulent transfers of assets or rights of the debtor can be annulled or revoked, in order to make them available to the creditor to execute the seizure or exercise the rights of the debtor in order to recover his credit.

[1] Judgment of November 13, 1992 issued by the First Superior Court of Panama, within the Ordinary Process proposed by Anselmo Ortega vs. Placido Castillo and others.
[2] The First Superior Court of the First Judicial District is a Court with, among other functions, hearing appeals in certain civil processes that arise in the provinces of Panama, Panama West, Colón, Darien and the Guna Yala Region (all of these include the First Judicial District). It is clarified that the Republic of Panama, judicially, is divided into four (4) judicial districts.

Requirements that must be observed to bring the *Paulian Action* before the courts of Panama

Article 996 establishes the purpose of the *Paulian Action* and the requirements that must be observed to bring to the court this type of action. It is important to point out that the requirements for its filing have been specified in a better way, through the jurisprudence of the Supreme Court of Justice of Panama.

Thus, and from the analysis of article 996 cited, the following can be deduced:

1. Insolvency of the debtor: a first requirement to observe for this action to proceed is to demonstrate that the debtor is insolvent and that he does not have assets that serve to collect the debt pending payment. Even though there is no unanimity of criteria, the idea seems to prevail that insolvency or lack of assets is not necessary to prove it in a previous or separate process, but rather, it can be proven in the same process where the *Paulian Action* is filed.

2. Subsidiary nature: in accordance with the previous requirement, the nature of the *Paulian Action* is merely subsidiary, that is, it only proceeds when the creditor cannot collect due to the fraudulent actions of the debtor to free himself from his assets with the purpose of not facing his debts.

Regarding the subsidiary nature of this type of action, by means of a Judgment of June 27, 2001, the Civil Chamber of the Supreme Court of Justice of Panama ruled in the following terms:

> "What has been asserted is also related to its reason to be, which leads us to refer again to the subsidiary nature of the Paulian or Revocation Action but from another perspective, that is, as an action whose exercise is subject to the fact that the creditor can not, in another way collect what is owed, where we consider fair that the law places in the hands of the creditor this other alternative to collect his credit, undoing or revoking those acts that fraudulently tend to prevent the fulfillment of an obligation".[3] (Emphasis added).

In accordance with the above, it is very important to establish that this is a last resort remedy for the defrauded creditor. As such, the courts are very cautious to verify that the circumstances really warrant granting this action. Of course, what is sought by not making indiscriminate use of this measure is to guarantee the principle of legal certainty.

[3] This is a liberal translation of an extract of the Judgment.

3. Fraud: A third element is to demonstrate that the acts that give rise to the transfer or disposal of assets are done fraudulently to evade payment of an obligation. This fraud, according to doctrine and case law, can occur when the transfer of goods or rights is carried out free of charge, or when, having been done for a fee (in exchange for consideration), the bad faith of the third party is verified.

4. Very personal rights or actions: although the rule authorizes the creditor to exercise the rights and actions of the insolvent debtor (for the purpose of collecting the debt), it is not possible when the debtor's rights or actions are of a personal nature or have an '*intuite personae*', that is to say, those inherent to the person that cannot be transferred either because his own nature does not allow it, or because it is legally impossible.

Conclusions and Considerations

In accordance with the norm that regulates the *Paulian Action* and jurisprudence, its primary purpose is the annulment or revocation of fraudulent acts when it is shown that the debtor has done so with the aim of becoming insolvent and avoiding his obligations to the creditor. However, we reiterate that this is a subsidiary process that, effectively, only proceeds when there are no other assets or rights of the debtor with powerful collection, in which case such insolvency must be demonstrated before the Courts.

Although this action is regulated in our legal system and can be legally requested, these processes are not common, and they tend to be very casuistic. This implies that its admission and concession may be subject to the reasoning of each judge, for which it is recommended that when filing a process of this type, the plaintiff makes sure to provide strong evidence that can create sufficient conviction in the judge, that the debtor has stripped himself of his assets to defraud his creditor.

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New AML Regulations on Crypto Assets in Poland

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New AML Regulations on Crypto Assets in Poland

JOANNA BOGDAŃSKA

The article provides information on the latest developments in anti-money laundering regulations for crypto assets in Poland. These changes are not only aimed at bringing Polish regulations in line with those of the EU, but also reflect the will of the legislator to introduce greater control over the flow of crypto assets. The legislator has also decided to impose strict penalties for non-compliance with the new standards, obviously with a view to achieving a preventive effect.

On May 15, 2021, an amendment to Poland's AML laws came into force. Its purpose was to implement into the Polish legal order the solutions of Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purpose of money laundering or terrorist financing and amending Directives 2009/138/EC and 2013/36/EU. The changes that were introduced largely affect the cryptocurrency market in Poland.

Project authors referred in their explanatory memorandum to the European Commission's "zero tolerance policy" towards inadequate or incomplete implementation of EU legislation. Polish legislator assures as well that the project's priority is to replicate the requirements of AMLD5 as closely as possible, not only in terms of content, but also when it comes to the layout of drafting units or the conceptual grid used by the EU legislator. Bearing in mind the deadlines that the European Union has set for member states to implement the provisions, that being

January 2020, Poland's legislature seems, however, to have disregarded them, since the work on the project began in February 2020.

As of 31 October 2021, the activity of virtual currencies is a regulated activity under the provisions of the Law of 6 March 2018, the "Law of Entrepreneurs". This means that such activity can be carried out, but only after obtaining an entry in the register of virtual currency activities. The register is maintained by the Director of the Tax Administration Chamber in Katowice, while its establishment is expected to contribute to increasing the transparency of the cryptocurrency market in Poland.

The register of virtual currency activities is clearly not an initiative of the Polish legislator. It stems from the need to implement the recommendations of the Financial Action Task Force ('FATF') on virtual assets[1]. Indeed, FATF stated that the activities of virtual asset service providers should be licensed or at least registered.

As of January 2023, almost 600 entities have been listed since November 2021.
The new regulations do not apply to all entrepreneurs whose activities involve cryptocurrencies. This provision identifies entrepreneurs engaged in virtual currencies activities consisting of:

- exchange between virtual currencies and means of payment,
- exchange between virtual currencies,
- intermediation in the above-described exchange, and
- maintaining accounts for virtual currencies.

This means that under the Polish AML Law, "virtual currency business" is a narrower concept than in the colloquial sense.

What's more, additional requirements have also been introduced for persons who can engage in virtual currency business, in the above narrower sense. Thus, such activity may be conducted by:

- a natural person who has not been validly convicted of an intentional crime against the activities of state institutions and local self-government, against the administration of justice, against the credibility of documents, against property, against economic turnover and property interests in civil law

[1] See: https://www.fatf-gafi.org/en/publications/Fatfrecommendations/Guidance-rba-virtual-assets-2021.html

transactions, against money and securities trading, an offence committed for the purpose of financial or personal gain, or an intentional fiscal offence;
- a legal person or an organizational unit without legal personality, in which the partners entrusted with the conduct of the affairs of the company, or authorized to represent the company, or members of the management bodies have not been validly convicted of an offence referred to the above or an intentional fiscal offense.

Further, natural persons, both running crypto business themselves and management of the legal entity engaged in such business, should have knowledge or experience relating to the business of virtual currencies. Proper knowledge and experience shall follow from a training course or programme covering legal or practical issues related to the virtual currency business, or from practice, i.e. performing, for a period of at least one year, relating to activities in the field of virtual currencies. This experience should be documented.

An entity or person engaged in virtual currencies activities without obtaining registration in the register of virtual currencies is subject to a fine of up to PLN 100,000 (c.a. EUR 20,000).

Comparing with other sanctions set forth in the AML Law, this penalty seems relatively small. However, it should be remembered that virtual currency operators have the status of mandatory institutions just like banks or financial institutions. This mean that they are required to apply financial security measures accordingly to occasional transactions equal to or exceeding EUR 1,000. As a reminder, until now the threshold was EUR 15,000.

So, in order to make a transfer of cryptocurrencies in an amount higher than the equivalent of EUR 1,000, it is now necessary to apply to the client a full catalog of financial security measures (including establishing personal data, citizenship, PESEL number or date of birth, information on identity documentation or address, establishing the data of the real beneficiary - that is, the person actually in control of the client, establishing the data of the proxy, and verifying all this data, as the AML Law prescribes).

Failure to comply with these requirements carries a number of sanctions, including criminal liability for members of governing bodies. It is worth notice that penalties imposed in the control process performed by Polish authorities are considerably higher. In the case of individuals, it can be up to almost PLN 21 million, and in the case of other entrepreneurs - up to EUR 5 million or up to the value of 10% of the company's annual turnover.

Outlook

Although it is obvious that the changes in the law have been forced by EU regulations and are aimed at tightening the system in general, one cannot help feeling that they will primarily affect the activities of cryptocurrency exchange offices. Cryptocurrency exchanges have long been considered in Poland, but also worldwide, to be the riskiest in terms of money laundering. The extension of the obligations of customer identification and verification combined with the obligation to obtain an entry in the register of cryptocurrency exchange offices enforces placing particular emphasis on maintaining up-to-date AML procedures and risk assessments of the services provided by the exchange office in terms of AML.

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Metaverse Disputes – Navigating Jurisdictional Issues in the Metaverse

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Metaverse Disputes – Navigating Jurisdictional Issues in the Metaverse

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Abstract

The Metaverse involves a confluence of cutting-edge technologies and is touted to become as revolutionary as the Internet when it was first brought into the mainstream. With a projected 25% of the global population spending at least an hour a day in the Metaverse and the size of the Metaverse market expecting to reach USD 758 billion by 2026,[1] fraud in the Metaverse is inevitable. In this article, Danny Ong, Jason Teo, and Stanley Tan of Setia Law LLC consider some of the jurisdictional issues that could arise in the Metaverse which victims of fraud are likely to grapple with when seeking relief.

Introduction

The Metaverse brings together a gamut of cutting-edge technologies and has the potential to revolutionise how we fundamentally interact, learn, work, play, and live as a society.[2] With the confluence of virtual reality, artificial intelligence,

[1] Meghan Rimol, "Gartner Predicts 25% of People Will Spend At Least One Hour Per Day in the Metaverse by 2026" (Gartner, 7 February 2022); Don-Alvin Adegeest, "Global Metaverse market to be worth 758.6 billion dollars by 2026" (19 February 2022).
[2] Matthew Ball, "The Metaverse will Reshape Our Lives. Let's Make Sure It's for the Better" (Time, 18 July 2022); Matthew Ball, *The Metaverse: And How It Will Revolutionize Everything* (Liveright Publishing, 2022).

blockchain, spatial, and cloud technology,[3] the Metaverse is poised to usher in a new era of possibilities for commerce and development.

Yet, echoing the challenges faced with the advent of the Internet and cryptocurrency, the Metaverse is likely to form a new battleground and hotbed for fraud and criminal activity. This article considers some of the challenges that victims of fraud are likely to face in seeking redress, before discussing possible solutions to overcoming them.

What is the Metaverse?

No universal definition of the Metaverse yet exists.[4] Indeed, given its nascence and the lack of clarity as to what forms and functions it will ultimately take and adopt, the Metaverse could be said to be currently incapable of precise definition. Nonetheless, one author, William G. Burns III,[5] offers the following neat encapsulation of what the Metaverse is likely to be: "*a collective virtual shared space, created by the convergence of virtually enhanced physical reality and physically persistent virtual space, including the sum of all virtual worlds, augmented reality, and the Internet*."[6]

As Burns notes, no single Metaverse currently exists.[7] However, various online platforms like Meta Platforms Inc's "*Horizon Worlds*" and VRChat Inc's "*VRChat*" could be described as early constituents of a Metaverse which users access through virtual reality equipment to interact, play games, and conduct business. While these platforms are operated by a central authority (i.e. the platform developer) in a relatively traditional manner, also on the rise are decentralised platforms like *Decentraland*, which operates through a Decentralised Autonomous Organisation ('DAO') without any central control.[8]

A decentralised Metaverse platform operated through a DAO makes decisions and implements platform policy and changes through a voting process involving the

[3] Stylianos Mystakidis, "Metaverse", Encyclopedia 2022, Vol. 2(1), 486-497.
[4] Cathy Hackl, "Defining the Metaverse Today" (Forbes, 2 May 2021).
[5] William G. Burns III has been recognised by Forbes as a "*Metaverse veteran*" (see, *supra* note 4) and his profile and experience with the Metaverse can be found at <https://www.linkedin.com/in/wgburns/> accessed on 29 March 2023. William G. Burns III is also the co-author of a journal article titled "*3D Virtual Worlds and the Metaverse: Current Status and Future Possibilities*", ACM Computing Surveys, 2013, Vol. 45:3, 1-38.
[6] William Burns III, "Everything You Know About The Metaverse Is Wrong" (26 August 2017), <https://www.linkedin.com/pulse/everything-you-know-metaverse-wrong-william-burns-iii/> accessed on 29 March 2023; See also *supra* note 4.
[7] William Burns III, "Everything You Know About The Metaverse Is Wrong", *supra* note 6.
[8] See Decentraland, "Building the foundations for a decentralized virtual world" (19 February 2020), <https://decentraland.org/blog/announcements/building-the-foundations-for-a-decentralized-virtual-world/> accessed on 29 March 2023.

owners of crypto-tokens associated with the platform. For example, in *Decentraland*, any change to the platform has to be proposed by an owner of crypto-tokens known as MANA, NAMES or LAND, presented to the other owners of these crypto-tokens, and put to a vote.[9] Proposals that have been passed by a majority are thereafter enacted by a "*DAO Committee*", which comprises trusted individuals appointed by the DAO and tasked with "*enacting any passed votes with a binding action*".[10] The DAO committee members are capable of effecting these changes because they have access to the DAO's Smart Contracts which are essentially the programmes responsible for running the *Decentraland* platform.[11]

The remainder of this article will consider the "Metaverse" in the forms outlined above.

Establishing Jurisdiction over Fraudsters in the Metaverse

Victims of fraud typically have to urgently commence a claim against the fraudster, and may seek freezing and/or proprietary injunctions against him. These typical asset recovery steps face unique challenges in the Metaverse.

As Metaverse platforms today generally allow their users to operate anonymously through avatars, identification of the fraudster presents a victim's first challenge. If the platform operator requires disclosure of users' real identities on account creation, pre-action discovery against the platform operator may be viable. However, many platforms have little or no user identification requirements, in which case victims will need to resort to commencing claims against "unknown defendants".

[9] See Decentraland, "Participation Requirements" (28 March 2023), <https://docs.decentraland.org/player/general/dao/overview/what-do-you-need-to-participate/> accessed on 29 March 2023 and Decentraland, "DAO User Guide" (28 March 2023), <https://docs.decentraland.org/player/general/dao/dao-userguide/>, accessed on 29 March 2023.
[10] See Decentraland, "How the DAO works" (28 March 2023) <https://docs.decentraland.org/player/general/dao/overview/how-does-the-dao-work/> accessed on 29 March 2023.
[11] See Decentraland, "What is the DAO" (28 March 2023), <https://docs.decentraland.org/player/general/dao/overview/what-is-the-dao/> accessed on 29 March 2023 and Decentraland, "The DAO Smart Contracts" (28 March 2023), <https://docs.decentraland.org/player/general/dao/overview/what-smart-contracts-does-the-dao-control/> accessed on 29 March 2023.

In this regard, numerous jurisdictions like Canada,[12] Hong Kong,[13] Malaysia,[14] Singapore,[15] the United Kingdom[16], and the United States of America[17] already permit claims and injunctions to be obtained against unknown persons. The recent Singapore decision of *Janesh s/o Rajkumar v Unknown Person ("CHEFPIERRE")* [2022] SGHC 264 also allowed a claimant to identify the unknown defendant by his twitter pseudonym in the court action. By extension, it may be possible for victims of Metaverse fraud to identify the fraudster by his pseudonym, avatar, or any other unique identifying trait.

Service of process, which is often necessary to confer jurisdiction on the court to determine the claim,[18] presents the next challenge for our hypothetical victim.[19] Many Metaverse platforms do not require their users to provide any contact details, much less verify their true identities. For example, in the case of Decentraland, a user only needs to provide a private cryptocurrency wallet address before being allowed to enter and trade on the platform – no email, phone number, or other contact details are required.

Nevertheless, the unique features of this space provide opportunity for unique solutions. For instance, in *D'Aloia v Person Unknown and others* [2022] EWHC 1723 (Ch), the English Court allowed a claimant to effect service of the court papers on a defendant by sending a Non-Fungible Token ('NFT') containing the court documents to the defendant's wallet address. This method of service was also employed in *LCX AG v. John Doe Nos.* 1-25, No. 154644/2022 (N.Y.Sup.Ct. June 2, 2022).[20]

Establishing jurisdiction over a fraudster operating in virtual space presents a further challenge. Victims will need to persuade a court that it is the appropriate

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[12] Jackson v Bubela [1972] 5 WWR 80; Golden Eagle v International Organization of Masters [1974] B.C.J. No. 614; Busseri v John Doe [2014] O.J. No. 605; Voltage Pictures LLC v John Doe [2015] 2 F.C.R. 540

[13] University of Hong Kong v Hong Kong Commercial Broadcasting Co Ltd [2016] 1 HKLRD 536; MTR Corporation Ltd v Unknown Persons [2019] 5 HKC 260.

[14] Zschimmer & Schwarz GMBH & Co Kg Chemische Fabriken v Persons Unknown & anor [2021] MLJU 178.

[15] *CLM v CLN* & others [2022] SGHC 46.

[16] *Cameron v Liverpool Victoria Insurance Co Ltd* [2019] 3 All ER 1 at [13]; *AA v Persons Unknown* [2020] 4 WLR 35 ("*AA*") at [75]; *Ion Science Limited v Duncan Johns* [2020] EWHC 3688 (Comm) ("*Ion Science*") at [23].

[17] Jim Wagstraffe, "To Doe or not to Doe in Federal Court" (LexisNexis, 2020).

[18] See, for example, section 16(1) of Singapore's Supreme Court of Judicature Act (2020 Rev Ed).

[19] See, for example, Order 6 rule 4 of the Singapore Rules of Court 2021, Rule 6.5 of the UK Civil Procedure Rules, or Order 10 rule 1 of the Hong Kong Rules of the High Court.

[20] See LCX AG v John Doe Nos. 1-25, Index No. 154644/2022 (N.Y. Sup. Ct. 2022), <https://www.hklaw.com/-/media/files/generalpages/lcx-ag-v-doe/ordertoshowcause_15.pdf?la=en> accessed 29 March 2023. The relevant NFT containing a hyperlink to the court documents can be accessed here: <https://etherscan.io/nft/0xdc9ec0c966c3d3a552a228b3fe353848ce2f25f4/1> accessed 29 March 2023

court to determine their claims, notwithstanding the fact that jurisdiction is traditionally determined by "*territorial connecting factors*",[21] which are less than apparent in the Metaverse.

That said, courts around the world have grappled with issues of jurisdiction in the virtual space before, and the legal principles established from resolving jurisdictional disputes in Internet and cryptocurrency disputes might assist in resolving those same issues in the Metaverse. For example, a victim of fraud in the Metaverse who wishes to establish the jurisdiction of the Singapore Court might be able to argue that the damages are suffered in Singapore if he resides or is domiciled in Singapore,[22] or lost assets in the Metaverse that were funded by a Singapore bank account.[23] The victim might also be able to rely on how the fraudster has property in Singapore[24] if, for example, it is uncovered that the fraudster has assets and/or had transferred the stolen proceeds to a cryptocurrency exchange whose central management and control is based in Singapore.[25]

Establishing Jurisdiction Over Metaverse Platform Providers

As alluded to above, victims of Metaverse fraud might also need to establish jurisdiction over Metaverse platform providers to seek disclosure orders, and later, to get assistance with enforcing a judgment against the fraudster.

While establishing jurisdiction against Metaverse platform providers operated by a central corporate entity would be relatively straightforward, difficulties arise when the Metaverse platforms are operated by a DAO because DAOs are not recognised as separate legal entities like corporations which can be sued in their own name, and their legal status remains a novel and unsettled issue[26] in most jurisdictions.[27]

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[21] Andrew Dickinson, "Cryptocurrencies And The Conflict Of Laws" in David Fox & Sarah Green (eds), Cryptocurrencies in Public and Private Law (Oxford University Press, 2019) at [5.08].
[22] See paragraph 63(3)(f)(ii) of the Singapore Supreme Court Practice Directions 2021; *Ion Science*, *supra* note 16 at [13]; *Tulip Trading v Wladimir Van Der Laan and others* [2022] EWHC 667 at [145];
[23] *Ion Science*, *supra* note 16 at [13]; *AA supra* note 16 at [68].
[24] See paragraph 63(3)(a) of the Singapore Supreme Court Practice Directions 2021.
[25] Andrew Dickinson *supra* note 21 at [5.109]; The Society of Trust and Estates Practitioners (STEP) UK Technical Committee, "STEP Guidance Note: Location of Cryptocurrencies – an alternative view" (3 September 2021); UK Law Commission, "Digital Assets: Consultation Paper" (28 July 2022) at p. 219.
[26] See the UK Law Commission's public call for evidence about how DAOs can (and should) be characterised at The UK Law Commission "Decentralised Autonomous Organisations (DAOs)", <https://www.lawcom.gov.uk/project/decentralised-autonomous-organisations-daos/> accessed on 29 March 2023. See also, Cointelegraph, "The impact and rise of DAOs in the legal industry" at <https://cointelegraph.com/daos-for-beginners/impact-in-legal-industry> accessed on 29 March 2023.
[27] The states of Wyoming and Tennessee in the United States of America have passed legislation recognising DAOs as separate legal entities, see Counsel for Creators LLP, "Wyoming DAOs as LLCs" (25 May 2022), <https://counselforcreators.com/log/wyoming-

Furthermore, as decisions of a DAO are made through a voting process involving the owners of the crypto-tokens associated with the Metaverse platform, control over the platform might be said to be vested in *all owners* of the relevant crypto-token. Commencing a claim against all owners of the relevant crypto-token and seeking orders compelling them to pass a proposal enabling disclosure or enforcement against a fraudster's Metaverse assets, is far from practical for a multitude of reasons, not least because the owners of these crypto-tokens are likely to be constantly in flux as these tokens are usually publicly traded.

One potential solution is to seek recourse against the specific crypto-token owners tasked with enacting proposals that have been passed by the DAO (the 'DAO Committee Members'). As mentioned above, these individuals have access to the Smart Contracts which enable the functioning of the Metaverse platform, and they are therefore technically capable of "controlling" the platform in a way that enables them to comply with a Court order to, for example, transfer assets owned by the fraudster on the platform to the victim.

However, while these individuals might have the ability to access and transfer ownership of crypto-tokens associated with a Metaverse platform (like LAND in Decentraland)[28], they are unlikely to have access to other assets in the fraudster's private wallet address.

In addition, considerable expertise might be needed to alter the Smart Contracts of the platform to carry out a court order for disclosure or transfer of assets. If the relevant DAO Committee Members lack such expertise or willingness to do so, victims may need to engage their own independent expert to devise a code or program to make the necessary alterations, in which case the DAO Committee Members would only be ordered to execute the relevant code or program.[29]

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daos/#:~:text=Wyoming%20Senate%20Bill%2038%2C%20titled,the%20bill%20in%20July%202021> accessed on 29 March 2023 and Matthew S. Miller & Spencer Green, "Beyond a Reasonable DAOubt: Tennessee's Limited Liability Statute for Decentralized Autonomous Organizations (DAOS)" (4 August 2022), <https://www.natlawreview.com/article/beyond-reasonable-daoubt-tennessee-s-limited-liability-statute-decentralized> accessed on 29 March 2023.

[28] See Decentraland, "Allow the DAO to recover lost assets" (25 August 2021) <https://governance.decentraland.org/proposal/?id=3f890970-052f-11ec-a4d1-8d5d2cba0825> accessed on 29 March 2023.

[29] See David Goldman, "Apple's case against the FBI won't be easy" (25 February 2016), <https://money.cnn.com/2016/02/25/technology/apple-fbi-court-case/index.html?iid=EL> accessed on 29 March 2023.

Conclusion

As we work towards achieving the exciting possibilities that the Metaverse offers, we should also remain grounded and be prepared for the reality that fraud and criminal activity will ride on the coattails of the Metaverse's success. Regulation of the Metaverse may eventually materialise to address these issues, but as was seen in the early days of cryptocurrency, it may come too slowly to provide adequate redress for victims, particularly early adopters of this new technology. Regulation may also prove to be of limited effectiveness in the case of decentralised Metaverse platforms, given their lack of a central governing entity. Nonetheless, as we have illustrated above, victims can take comfort in how Courts around the world are alive to the unique problems posed by novel technology and are willing to adopt equally innovative solutions.

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What About Volatility? Enforcement Of Crypto-Related Decisions in Spain

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What About Volatility? Enforcement Of Crypto-Related Decisions in Spain

HÉCTOR SBERT, PH.D

Abstract

This article deals with the possibilities at the disposal of a judgment or award creditor to obtain the refund in kind of crypto assets and digital assets during enforcement proceedings in Spain. We explore the enforcement orders that Spanish Courts may issue and the existing alternatives when those orders fail to provide with the return in kind of the digital assets. In particular, we will cover the risk of volatility and the instruments at the disposal of the creditor to reduce it according to Spanish law.

1. Request for Legal Opinion: a case study

CryptoABC obtained an international arbitration award against the Spanish company XYZTechno.[1] In that award, XYZTechno was ordered to return to CryptoABC a certain amount of digital assets, consisting of cryptocurrencies and various types of tokens, which CryptoABC had provided as interest-free funding to XYZTechno.

CryptoABC has asked for our opinion about the possibility to enforce such award in Spain. CryptoABC is interested in tracing and recovering those digital assets,

[1] This article refers to an actual case that is the subject of an international arbitral award issued in 2022 and administered by one of the world's leading arbitral institutions. For reasons of confidentiality, the reference to the award is omitted. For the same reasons, the names of the parties and references to the products and services covered by the cryptographic platform have been modified and anonymized.

wherever they may be. Bearing in mind that the arbitral award ordered XYZTechno to those digital assets in kind -and not their monetary equivalent-, CryptoABC has asked us to consider whether Spanish courts may issue disclosure and attachment orders, addressed both to the debtor and to third parties that may lead to: (i) ascertaining the crypto exchange where those digital assets may be deposited (ii) making sure that those digital assets are returned to CryptoABC. CryptoABC is also interested in learning more about the enforcement alternatives under Spanish law, in case the disclosure and attachment orders fail, i.e., they do not lead to the tracing and recovery of the digital assets. Also, and crucially, CryptoABC is asking what protection Spanish law has to offer against the risks arising from the volatility of such assets, meaning, who bears the risk of potential loss in value of those digital assets between the date when they were delivered to XYZTechno and the time when those same assets will be possibly returned to CryptoABC.

In this article, we explore the Spanish legal framework to the extent necessary to answer those questions and provide insight in this particularly topical area.

2. Background

CryptoABC is a crypto exchange, i.e., a company dedicated to the trade and custody of cryptocurrencies and other digital assets. As such, it enjoys a solid reputation as a safe and reliable operator in the market.

XYZTechno is a market leader delivering liquidity solutions to blockchains. In this capacity, it reached an agreement with CryptoABC to provide market maker services[2] on one of the cryptocurrency exchange platforms developed by CryptoABC, called "ABC SuperExchange".
To help it launch its services as a market maker, CryptoABC provided XYZTechno with interest-free funding (via the signature of several Loan Agreements)

[2] "*The term market maker refers to a firm or individual who actively quotes two-sided markets in a particular [asset], providing bids and offers (known as asks) along with the market size of each. Market makers provide liquidity and depth to markets and profit from the difference in the bid-ask spread. They may also make trades for their own accounts, which are known as principal trades.*", *Market Maker Definition: What It Means and How They Make Money*, Investopedia (Dec 8, 2022), https://www.investopedia.com/terms/m/marketmaker.asp. This begs the question, why are market makers necessary? A market maker serves as a middleman or broker between the demand and supply for digital assets. Market makers provide liquidity in markets of digital assets, which ensures there is enough orders to buy and sell, while cryptocurrency exchanges offer the infrastructure that allows traders to operate. Market makers ensure traders can quickly and easily liquidate their holdings. Market makers are also necessary because they maintain price stability in a market with a somewhat small bid-ask spread. In addition to being seen as reputable and trustworthy by cryptocurrency traders, a market with price stability is an indication of significant liquidity, since it means that many participants are transacting, which in turn increases the market maker's profit.

consisting of exact quantities of cryptocurrencies and digital assets (payment and utility tokens)[3] that XYZTechno would have to return.

At one point, CryptoABC requested TechnoXYZ to return the exact quantities of the cryptocurrencies and digital assets loaned at TechnoXYZ's account in ABC SuperExchange. TechnoXYZ failed to comply with this request, which led the parties to arbitration. A sole arbitrator was appointed to handle the dispute.

3. The Object of the Refund: Digital Assets, or its Equivalent Initial Value in Fiat Currency?

This was one of the critical issues of the dispute. CryptoABC argued it provided funding in the form of an exact quantity of digital assets. CryptoABC further claimed that XYZTechno had to restitute this interest-free funding in the exact same quantities as received, in conformity with the parties' intention that the funding should always remain the property of CryptoABC and that XYZTechno would bear the risk of losing it.

XYZTechno argued that funding had to be repaid based on its initial value in Euro, and not token-for-token.

The consequences of one option or the other are obvious. If the sole arbitrator was to order that the funding had to be refunded based on its initial value in fiat currency (the currency used was Euro), the volatility risk of the digital assets would be borne by the funder, insofar as that initial Euro value would be equivalent, at the time of repayment, to an amount different from that which was the initial subject of the funding.

If, on the other hand, the sole arbitrator was to rule that the funding had to be repaid in the exact amount of digital assets originally received, the volatility risk would be borne by the borrower since, if it did not hold the digital assets received, it would have to purchase them on the market at their equivalent price in Euro at the time of repayment.

4. What the Award Rules

The award rules that the parties intended the return of the digital assets on a token-for-token basis, and not on a monetary value basis. It further considered that the

[3] "Payment tokens" are issued with payment medium functions on a given blockchain, while "utility tokens" grant the right to claim the provision of a service from issuers. There are also "security tokens", which have equivalent functions to financial instruments (i.e. Initial Coin Offerings (ICOs) or other crypto-assets that represent tradable financial instruments, such as shares, bonds or rights to investment contracts).

parties agreed on an obligation to return the funding received in the same asset and in the same quantity as received.

5. Can a Spanish Court issue Disclosure and Attachment Orders to the Debtor and Third Parties in relation to Digital Assets?

Considering that the award orders the restitution of digital assets in kind (and in the exact amount initially received), CryptoABC needs to know whether a Spanish court can, during enforcement of the award, issue disclosure and attachment orders to the award debtor and to third parties – aimed at learning about the whereabouts of such digital assets and to make them available to the Spanish court, for their delivery to the award creditor.

The answer to this question of Spanish law is affirmative. A Spanish court may, according to the Spanish Code of Civil Procedure, issue disclosure orders to the award debtor and to third parties. First off, the Spanish court may order the award debtor to disclose whether it keeps the received digital assets and where they are deposited; the Spanish court may also order the award debtor to make these digital assets available to the court for delivery to the creditor.
To third parties (e.g., cryptocurrency exchange platforms, where the digital assets may be under custody), the Spanish court may also request them to disclose whether they deposit those assets and, if applicable, to make them available to the court for delivery to the award creditor.

6. Limitations on the Effectiveness of Disclosure and Attachment Orders Addressed to the Award Debtor and to Third Parties

Even though it is possible to issue orders both to the debtor and to third parties, the effectiveness of both types of order is potentially different, particularly in matters related to cryptocurrencies, whose place of deposit can be anywhere in the world.

On the one hand, the award debtor is fully subject to the jurisdiction of the enforcement court and must comply with its orders. If he fails to do so, the Spanish court may impose coercive fines on him. In addition, repeated non-compliance with judicial disclosure orders, as well as incomplete or mendacious responses to such requests, may be criminal offences under the Spanish Criminal Code.

However, in the case of third parties and, particularly, in the case of crypto exchanges, one can expect that it will only be materially possible to force them to comply with the Spanish court's orders if their domicile is Spain. If their domicile is not Spain (as is usually the case for most crypto exchange platforms), there are

generally no international instruments that would allow Spanish courts to force the third party to comply with such order. In any case, the few legal instruments that may be considered are very difficult to apply in practice. This is a considerable limitation to international asset tracing and recovery affecting all types of assets, both digital and non-digital.

7. What Enforcement Options does the Award Creditor have if the Debtor of Third Party fails to comply with the Orders issued by the Spanish Court?

To answer this question, it is first necessary to analyse the legal nature of cryptocurrencies (which Spanish legislation names "virtual currencies") and other digital assets (which Spanish legislation names "crypto assets").

In relation to the former, Spanish regulations define them as "a digital representation of value, not issued nor guaranteed by a central bank or public authority, and not necessarily associated with a legally established currency, which does not have the legal status of currency or money, but which is accepted as a medium of exchange and can be transferred, stored or traded electronically". What is noteworthy about this definition is that virtual currencies do not have the legal status of “currency” or money under Spanish law.

As for digital assets or "crypto-assets", Spanish financial regulations define them as the "digital representation of a right, asset or value that can be transferred or stored electronically, using distributed ledger technologies or other similar technology". It follows from this definition that crypto assets are purely electronic and decentralised assets. It also follows that digital assets are fungible and, as such, likely to be used as a medium of exchange in economic transactions.

We must therefore conclude that the cryptocurrencies and other digital assets that are the object of the award have the legal nature, under Spanish law, of non-cash and fungible assets (as opposed to the so-called "NFTs" or Non-Fungible Tokens, which, by definition, have a different legal nature). Therefore, the enforcement of any court or arbitral decision whose object is cryptocurrencies and other fungible digital assets will follow the legal regime of non-monetary enforcement and, specifically, that of the enforced delivery of generic or indeterminate assets. In other words, the delivery of cryptocurrencies and digital assets has the same legal procedural treatment as that of a kilo of rice or potatoes (also generic or indeterminate assets); as opposed to the regime of delivery of a Picasso painting (which would be a specific movable asset, non-fungible and, therefore, the legal-procedural equivalent of an "NFT"...).

7.1. Option 1: Attachment of the debtor's assets to pay for the acquisition of the fungible digital asset

When the debtor has refused to comply with the order to deliver fungible (i.e., generic, or indeterminate) assets, Spanish law allows the award creditor to acquire such assets at the debtor's expense. For this purpose, the creditor may request the court to empower him to acquire them, ordering at the same time the attachment of sufficient assets of the debtor to pay for the acquisition.

Naturally, the attachment of sufficient assets will be made in the fiat currency governing the enforcement; typically, in Spain, such currency will be Euros, but it could be any other of legal tender.

Therefore, an interesting question is what value, or "exchange rate" in fiat currency, will be used to determine the exact amount of the debtor's assets that will have to be seized to finance the acquisition of the cryptocurrencies and other fungible digital assets that are the object of the award. Some of the (countless) possibilities could be: (i) the exchange rate at the time when they were delivered to the borrower; (ii) at the time when the breach occurred; (iii) at the time of the arbitration claim; (iv) at the time of the award; (v) at the time of enforcement; (vi) or at the time of the award creditor's acquisition of such cryptocurrencies and digital assets.

The correct answer under Spanish law is the latter: the debtor's assets will be seized according to their value in fiat currency at the time of acquisition of the digital assets by the award creditor during the enforcement of the award. In this way, the risk of volatility of the digital assets will rely on the award debtor and not on the award creditor. The creditor will receive value in fiat currency of the digital assets at the time of purchase and can therefore buy the same exact number of cryptocurrencies and digital assets that were borrowed at the time by the award debtor.

7.2. Option 2: Request that the non-delivery of the digital assets be replaced by the payment of a fair monetary compensation

Spanish law also contemplates the possibility of it becoming impossible to purchase the generic or indeterminate asset. This possibility is relevant in the case of cryptocurrencies and digital assets, one of whose characteristics, in some instances, is their lack of liquidity. In certain cases, such lack of liquidity may make it impossible to find buyers and sellers of the cryptocurrency or digital asset in question (hence the importance of the "market maker" services that XYZTechno undertook to provide on the CryptoABC platforms).

In these cases, Spanish law provides that the impossibility to deliver the asset should be replaced by the payment of a fair pecuniary compensation. What should the amount of such compensation be? In our opinion, the compensation should cover, on the one hand, the value in fiat currency of the undelivered cryptocurrencies and digital assets (at the time when such compensation is calculated, i.e., at the time of the failed attempt to purchase them). On the other hand, the compensation should cover any other demonstrable damages that the creditor has suffered because of the non-delivery of the cryptocurrencies and digital assets (i.e., direct and indirect damages). To this end, the Spanish Code of Civil Procedure provides for a specific proceeding for the creditor to assert and prove the totality of damages suffered.

8. Conclusion

Spanish procedural law has not undergone any modification to adapt to the enforcement of court and arbitral decisions on the return of cryptocurrencies and other digital assets. However, the current regulation is already relatively well-suited to certain aspects relating to the enforcement of judgments and awards involving the delivery in kind of such assets. Spanish law provides that, in the absence of return in kind, the creditor may acquire the digital (fungible) assets at the debtor's expense, seizing his other assets for the value, in fiat currency, necessary to purchase such assets at the time of the acquisition during the enforcement. If this is not possible, Spanish law provides that the creditor may claim a fair monetary compensation from the debtor. In either case, Spanish law protects the creditor against the inherent volatility of digital assets, allowing the creditor to recover the exact amount of digital assets recognised in the enforceable title, to be calculated in fiat currency at the time of the enforcement.

In this case, paradoxically, the latter option in the enforcement stage would reach the opposite solution to the one envisaged in the award, which rejected that the return of the digital assets could be made in fiat currency instead of being made in kind. However, one must acknowledge there are no alternatives to the impossibility of recovering the digital assets in kind, other than converting them into their fiat currency value, be it to attach the debtor’s assets to assist in the purchase, or to pay to the award creditor a fair monetary compensation. Therefore, the basic element to consider is protection for the award creditor against the volatility in the value of cryptocurrencies and digital assets. As we have seen, Spanish law contemplates what seems a fair solution to this problem.

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U.S. Fraudulent Transfer Law: Legal Issues and Practical Considerations

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US Fraudulent Transfer Law: Legal Issues and Practical Considerations

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Abstract

The U.S. has a well-developed body of law concerning the prosecution and recovery of fraudulent transfers. Fraudulent transfer law is a type of creditors' rights law that seeks to claw back two types of transfers: (i) transfers made with actual intent to hinder, delay, or defraud creditors and (ii) transfers made for less than reasonably equivalent value while the debtor was in dire financial circumstances. As with most areas of law, fraudulent transfer law often involves complex issues. Questions such as whether the transferee provided reasonably equivalent value, whether the recipient of a transfer acted in good faith, or which jurisdiction's law governs the proceeding frequently involve fact-intensive inquiries. In this article, Joe Wielebinski and Matthias Kleinsasser identify common issues in this area and also provide practical considerations for practitioners.

1. Introduction

The U.S. has a well-developed body of law concerning the prosecution and recovery of fraudulent transfers. Fraudulent transfer law is a type of creditors' rights law that seeks to claw back two types of transfers: (i) transfers made with actual intent to hinder, delay, or defraud creditors and (ii) transfers made for less than reasonably equivalent value while the debtor was in dire financial circumstances. As such, fraudulent transfer litigation is one of the most important tools used to address fraud and recover assets for victims of such fraud. Fraudulent transfer law

is unique in that the party committing the prohibited act – the transferor – is generally not the defendant in the lawsuit. Instead, a fraudulent transfer lawsuit is typically commenced against the initial transferee of the assets, and, where applicable, subsequent transferees. Fraudulent transfer lawsuits are regularly filed in state and federal court not only by creditors, but also by equity receivers and bankruptcy trustees. As such, a thorough understanding of this area of law is essential for any U.S. asset recovery professional.

As with most areas of law, fraudulent transfer law often involves nuanced issues. Questions such as whether the transferee provided reasonably equivalent value, or whether the debtor acted with actual intent to hinder, delay, or defraud, can prove to be complex, fact-intensive inquiries. This article identifies many of these issues and also provides practical considerations for practitioners involved (or considering becoming involved) in fraudulent transfer litigation.

2. Basics of U.S. Fraudulent Transfer Law

a. History

U.S. fraudulent transfer law traces its roots to the Fraudulent Conveyances Act 1571, commonly referred to as the Statute of 13 Elizabeth, an act of the English Parliament that laid the foundation of modern fraudulent transfer law. At the time, creditors were frequently the victims of fake sales of assets by debtors intended to hinder collection efforts. The Statute of 13 Elizabeth effectively voided certain transactions not made in good faith or without sufficient consideration. The most famous case decided under the Statute is known as *Twyne's Case*,[1] in which the Queen's Star Chamber set aside a purported conveyance of sheep because the debtor farmer did not transfer the sheep to the purchaser and continued shearing them. Accordingly, the sheep remained available for seizure by the farmer's creditors. Thus, this case established the basic principles of modern fraudulent transfer law.

All U.S. states have some version of fraudulent conveyance law. In 1918, the original model law titled the Uniform Fraudulent Conveyance Act was enacted. Forty-five U.S. states subsequently adopted the 1984 Uniform Fraudulent Transfer Act ("UFTA"). In 2014, the UFTA was amended with the new model law being named the Uniform Voidable Transactions Act ("UVTA"). The logic behind the UFTA's name change is that some transactions that are voidable under the Uniform Fraudulent Transfer Act, such as constructive fraudulent transfers, do not require a showing of fraudulent intent. The UVTA has been adopted by several states, including California and New York. In addition, the U.S. Bankruptcy Code, codified

[1] (1601) 76 ER 809, 3 Co. Rep. 80b.

in Title 11 of the U.S. Code, contains fraudulent transfer law provisions that generally parallel the provisions under the state model laws.[2]

b. Actual Fraudulent Transfer Claims

U.S. fraudulent transfer law distinguishes between actual fraudulent transfer claims and constructive fraudulent transfer claims. An actual fraudulent transfer occurs when a debtor transfers an asset with the intent to hinder, delay, or defraud a creditor.[3] By its very nature, fraud is secretive, making it sometimes difficult to determine whether a debtor had the requisite intent to hinder, delay, or defraud.[4] Therefore, U.S. fraudulent transfer law recognizes multiple badges of fraud, the presence of which suggest that an actual fraudulent transfer occurred. These badges include that the transfer was made to a related party (called an "insider"), that the debtor absconded afterward, that the debtor was recently sued or had a judgment entered against it, and that the transfer was made for less than reasonably equivalent value, among others.[5] The more badges of fraud that are present, the more likely it is that the debtor committed an actual fraudulent transfer. The badges of fraud underlying any fraudulent transfer statute are not exhaustive.

c. Constructive Fraudulent Transfer Claims

Constructive fraudulent transfer claims are a bit of a misnomer, insofar as actual intent to hinder, delay, or defraud is not required.[6] A constructive fraudulent transfer occurs when the debtor transfers assets or grants a security interest without receiving reasonably equivalent value in exchange for the transfer and one of three conditions is present: (i) the debtor is insolvent or becomes insolvent as a result of the transfer, (ii) the debtor is undercapitalized with respect to a business or transaction that the debtor is engaged in or is about to be engaged in, or (iii) the debtor intended to incur, or believed it would incur, debts beyond the debtor's ability to pay.[7] The transferor's intent is irrelevant. In essence, constructive

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[2] *See* 11 U.S.C. §§ 548, 550.

[3] In addition to including asset transfers, a "transfer" is also defined to include the granting of a lien or other security interest, since the granting of a security interest, like an asset transfer, diminishes the amount of assets held by the debtor that can be seized by unsecured creditors. *See, e.g.*, Tex. Bus. & Com. Code § 24.002(12).

[4] Strictly speaking, an actual fraudulent transfer claim, like a constructive fraudulent transfer claim, does not require the presence of actual intent to defraud. Intent to merely hinder or delay creditors' collection efforts is sufficient. *See, e.g.*, Tex. Bus. & Com. Code § 24.005(a)(1).

[5] *See, e.g.*, Tex. Bus. & Com. Code § 24.005(b).

[6] For this reason, the most recent uniform law in the U.S. is titled the Uniform Voidable Transactions Act, not the Uniform Fraudulent Transfer Act.

[7] *See, e.g.*, Tex. Bus. & Com. Code §§ 24.005(a)(2), (b), 24.006(a). U.S. fraudulent transfer law also provides a cause of action to recover a transfer to an insider (i.e., a related party) for an antecedent debt while the debtor was insolvent. Strictly speaking, this cause of action is generally termed a claim

fraudulent transfer law seeks to prevent a debtor in dire financial circumstances from putting its creditors in a worse position by transferring assets or granting security interests to others without receiving reasonably equivalent value in exchange.

d. Who Can Be Sued?

Unlike most lawsuits, a fraudulent transfer suit is generally not brought against the transferor, the party accused of the prohibited conduct. Instead, suit is generally filed against the initial transferee – i.e., the party who received the asset from the debtor. If the initial transferee transferred assets to other parties (termed subsequent transferees), those parties can also be sued, subject to the defenses described below.[8] The creditor may generally recover either the asset transferred (to the extent the asset is non-fungible, such as real property) or the asset's value.[9] A creditor typically may not recover more value than what it is owed by the debtor.[10]

e. Affirmative Defenses

U.S. law generally defines an affirmative defense as a defense on which the defendant bears the burden of proof. There are no affirmative defenses to constructive fraudulent transfer claims. Either the plaintiff creditor can establish the elements, or he cannot. However, affirmative defenses do exist on actual fraudulent transfer claims. With respect to an actual fraudulent transfer claim, the initial transferee is free from liability if he or she can show they received the asset in good faith and for reasonably equivalent value.[11] In other words, even if the debtor transferred the asset with actual intent to hinder, delay, or defraud a creditor, if the initial transferee did not know (and reasonably should not have known) of the debtor's bad intention, then the initial transferee is protected – assuming they provided reasonably equivalent value. Even if the initial transferee did not provide reasonably equivalent value (and therefore cannot claim to be wholly free from liability), so long as the initial transferee acted in good faith, it can deduct the amount of whatever value it did provide from the amount of the adverse judgment.[12]

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to recover a preferential transfer, as opposed to a fraudulent transfer claim. Preferential transfer recovery is also an integral part of insolvency litigation in the U.S.

[8] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(b).

[9] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(b).

[10] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(b).

[11] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(a).

[12] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(d).

Subsequent transferees can rely on two defenses: First, if the initial transferee prevails on its "good faith + reasonably equivalent value" defense, all subsequent transferees are free from liability.[13] Second, even if the initial transferee cannot establish this affirmative defense, a subsequent transferee that took the assets for any value (as opposed to reasonably equivalent value) is free from liability if the subsequent transferee acted in good faith.[14]

3. Legal Issues in Fraudulent Transfer Cases

a. Who Has Standing to Bring the Claim?

Generally, a fraudulent transfer claim is brought by a creditor of the debtor. A creditor is broadly defined as a person who has a claim, which is virtually any right to payment of money, whether disputed, unliquidated, contingent, or otherwise.[15] In other words, a creditor need not obtain a judgment against the debtor prior to filing a fraudulent transfer lawsuit. Whether the creditor held a claim at the time of the fraudulent transfer can be relevant under certain factual circumstances. For example, to bring an actual fraudulent transfer claim, or to bring a constructive fraudulent transfer claim based on the debtor not paying its debts as they become due or undercapitalization, the creditor's claim must arise before the time of the transfer or within a reasonable time thereafter.[16] To bring a constructive fraudulent transfer claim based on insolvency, on the other hand, the creditor must have had a claim at the time of the transfer.[17] If the claim arose later, the creditor is prohibited from pursuing this particular type of constructive fraudulent transfer claim.

Standing to assert fraudulent transfer claims is different in a bankruptcy or receivership than in normal debtor/creditor litigation. Upon the filing of a bankruptcy petition, creditors initially lose standing to bring fraudulent transfer claims. Instead, the bankruptcy trustee (or, in a Chapter 11 case, the debtor-in-possession, which is essentially the debtor who is charged with fiduciary obligations to the bankruptcy estate) obtains standing to bring these claims.[18] In large bankruptcy cases, the Official Committee of Unsecured Creditors, or, less commonly, individual creditors may request that the bankruptcy court confer standing upon them to bring fraudulent transfer claims for the benefit of all creditors. If the debtor-in-possession is disinclined to bring fraudulent transfer claims (e.g., because it would require suing the debtor's principals or affiliates),

[13] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(a).
[14] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(b).
[15] *See, e.g.*, Tex. Bus. & Com. Code § 24.0092(3).
[16] *See, e.g.*, Tex. Bus. & Com. Code § 24.005(a).
[17] *See, e.g.*, Tex. Bus. & Com. Code § 24.006(a).
[18] 11 U.S.C. § 544(b)(1).

then the bankruptcy court will often confer standing upon the Committee or the requesting individual creditor to pursue such claims.[19]

In an equity receivership, the receiver is generally granted standing to bring fraudulent transfer claims for the benefit of the receivership estate and its interested parties.

b. What is Value – *Janvey v. Golf Channel*

Value is broadly defined under U.S. fraudulent transfer law as the transfer of property or the securing or satisfaction of an antecedent debt.[20] Reasonably equivalent value does not have a precise definition, but it does include the range of values for which the transferor would have sold an asset in an arm's length transaction.[21] However, reasonably equivalent value does not require dollar-for-dollar equivalency.[22]

An interesting opinion on the issue of value in recent case law is the Texas Supreme Court's decision in *Janvey v. Golf Channel*.[23] In that case, the equity receiver for Stanford International Bank sued the Golf Channel television network for return of $5.9 million in payments for advertising on the Golf Channel. The Receiver argued that the advertising provided no objective value to the receivership estate and merely furthered the Ponzi scheme. Accordingly, the Receiver argued that Golf Channel should not be allowed to rely on the "good faith + reasonably equivalent value" defense. The Texas Supreme Court disagreed, holding that the services provided by Golf Channel did not need to preserve the debtor's estate so long as they had objective value, and the fact that they were provided to a Ponzi scheme did not change the inquiry. Since the advertising services had objective value at the time they were provided, Golf Channel was permitted to retain the $5.9 million. This decision is controversial and is not followed in some states, which retain the more commonly accepted principle that services to a Ponzi scheme merely further the fraud and provide no value to creditors.

c. Establishing Actual Fraud – the Ponzi Scheme Presumption

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[19] *See, e.g., Official Comm. of Unsecured Creditors of Cybergenics Corp. ex rel. Cybergenics Corp. v. Chinery,* 330 F.3d 548, 583 (3d Cir. 2003) (*en banc*); *Fogel v. Zell*, 221 F.3d 955, 965 (7th Cir. 2000); *Canadian Pac. Forest Prods. Ltd. v. J.D. Irving, Ltd. (In re Gibson Group, Inc.),* 66 F.3d 1436, 1440-41 (6th Cir. 1995); *La. World Exposition v. Fed. Ins. Co.,* 858 F.2d 233, 247-48 (5th Cir. 1988).
[20] *See, e.g.*, Tex. Bus. & Com. Code § 24.004(a).
[21] *See, e.g.*, Tex. Bus. & Com. Code § 24.004(d).
[22] *See Brown v. Douglas (In re Dual D Health Care Operations, Inc.)*, 2021 Bankr. LEXIS 1934, *27 (Bankr. N.D. Tex. Jul. 21, 2021).
[23] 487 S.W.3d 560 (Tex. 2016).

Fraudulent transfer litigation frequently occurs in the context of a Ponzi scheme. A Ponzi scheme – so named after Italian businessman Charles Ponzi who defrauded thousands of people out of over $10 million – is an investment scheme in which money from new investors is used to pay prior investors. In other words, the investment scheme generates no real value by its business operations, and simply misappropriates new investor funds for the benefit of earlier investors, thereby prolonging the scheme.

Because a Ponzi scheme is, by its very nature, fraudulent, many courts in the U.S. presume that funds paid out of a Ponzi scheme to investors were made with actual intent to hinder, delay, or defraud creditors.[24] In other words, once a creditor (or receiver or bankruptcy trustee) files an actual fraudulent transfer suit and establishes that the operation in question is a Ponzi scheme, the issue of actual intent to hinder, delay, or defraud is established without further evidence. In such case, the burden shifts to the transferees to establish affirmative defenses if they wish to retain the funds they received. Clearly, the Ponzi scheme presumption is a huge advantage to a creditor/receiver/trustee pursuing actual fraudulent transfer claims. While it is generally still followed in most jurisdictions that have adopted it, the presumption has been subject to recent criticism. The Minnesota Supreme Court has held that the Ponzi scheme presumption does not apply under Minnesota law and the Texas Supreme Court has raised questions as to its validity.[25]

d. The Netting Principle

Another principle applicable to Ponzi scheme fraudulent transfer litigation is the netting principle. The netting principle operates based on the policy that transfers made from a Ponzi scheme should be clawed back to evenly distribute recovered funds among the victims, regardless of when someone invested in the scheme. The trustee or receiver nets the amount transferred to an investor from the Ponzi scheme against the amounts invested by that individual within the relevant limitations period. If the result is positive, the investor has liability as a "net winner" from the scheme. If the result is negative, the investor is not liable and may receive distributions on its claim from the receivership or bankruptcy estate.[26]

e. Establishing Good Faith – Inquiry Notice and the Duty to Investigate

A finding that a transferee acted in good faith is a valuable finding under U.S. fraudulent transfer law. An initial transferee who provides reasonably equivalent

[24] *See, e.g.*, *Donnell v. Kowell*, 533 F.2d 762, 770 (9th Cir. 2008).
[25] *Finn v. Alliance Bank*, 860 N.W.2d 638 (Minn. 2015); *Janvey v. GMAG, L.L.C.*, 592 S.W.3d 125 (Tex. 2019).
[26] *See, e.g.*, *Donnell*, 533 F.2d at 771-72.

value in exchange for the transfer and acts in good faith has a complete affirmative defense to an actual fraudulent transfer claim.[27] A subsequent transferee has a complete affirmative defense if it acts in good faith and provides any value at all.[28] Even an initial transferee who provides some value but not enough to meet the reasonably equivalent value standard can offset the amount of value provided against its liability if the transferee acted in good faith.[29]

So what is good faith? Generally, the concept is defined in U.S. fraudulent transfer law as conduct that is honest in fact, reasonable in light of known facts, and free from willful ignorance of fraud.[30] There are two types of notice that will vitiate good faith. Actual notice means that the transferee is actually aware of fraud or other inequitable conduct at the time of the transfer. Inquiry notice means that the transferee was aware of facts that would have caused a reasonable person to investigate whether fraudulent conduct is present.[31]

In *Janvey v. GMAG, LLC*,[32] the Texas Supreme Court was again called upon to interpret the Texas Uniform Fraudulent Transfer Act, this time in the good faith context. The issue before the court was what a transferee on inquiry notice is required to do to show good faith. The court held that a transferee on inquiry notice is required to conduct a diligent investigation of its suspicions to attempt to uncover fraudulent conduct if it wants to establish good faith. Importantly, the court held that this investigation requirement holds even if a hypothetical investigation may not have uncovered the fraud, thereby providing transferees a strong inventive to investigate.[33]

f. Whose Law Controls?

Fraudulent transfer claims frequently involve transactions that take place across multiple states (or countries). While fraudulent transfer law across U.S. states is reasonably uniform, seemingly small differences between or among states can prove material in the right case. For example, even when the vast majority of U.S. states had adopted the Uniform Fraudulent Transactions Act, New York, a major commercial center, retained the prior Uniform Fraudulent Conveyance Act. More recently, an increasing number of states have adopted the Uniform Voidable Transactions Act, while others continue to hold to the Uniform Fraudulent

[27] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(a).
[28] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(b).
[29] *See, e.g.*, Tex. Bus. & Com. Code § 24.009(d).
[30] *See GMAG*, 592 S.W.3d at 129.
[31] *Id.*at 129-30.
[32] 592 S.W.3d 125 (Tex. 2019).
[33] *Id.*at 131-32.

Transactions Act. Therefore, choice of law issues can prove to be important determinations.

Until the promulgation of the Uniform Voidable Transactions Act, courts generally used the following procedure to determine which state's law should apply:[34]

1) The court would apply the choice of law principles of the state in which it sits to determine how to conduct the analysis.
2) Because fraudulent transfer claims are torts, most UFTA states would apply the "most significant relationship test" found in the Restatement (Second) of Conflict of Laws that is generally used to address tort conflict of laws issues. This is an intensive, multi-factor test that considers elements such as where the injury occurred, where the conduct causing the injury occurred, the location of the parties, and other factors.
3) Before applying this test, the court would compare the laws of the respective states to determine if a true conflict exists between them. The court would also consider whether, even if the laws conflict, they would nevertheless produce the same result and whether each state's policies would be furthered by applying its laws. If no conflict exists, the same result would obtain regardless of which state's law applied, or one state's policies would not be furthered by applying its law, then a true conflict does not exist. If a true conflict does exist, the court would perform the fact-intensive analysis under the most significant relationship test.

The Uniform Voidable Transactions Act streamlines this process significantly by applying the law of the state where the transferor was located when the transfer occurred. An entity is located at its principal place of business. If it has more than one principal place of business, then the entity is located where its Chief Executive Office is located.[35] In other words, if the fraudulent transfer suit is filed in a state that adopted the UVTA, then the analysis is simple. If suit is filed in a UFTA state, it may be a much more complex analysis.

4. Practical Considerations

a. Investigate Before Filing Suit

To the extent possible, it is best for a potential fraudulent transfer plaintiff to conduct as much pre-suit investigation work as possible prior to filing suit. This should include public record searches (e.g., prior court filings or lien searches),

[34] *See Mukamal v. Nat'l Christian Found., Inc. (In re Palm Beach Fin. Partners)*, 2014 Bankr. LEXIS 5418 (Bankr. S.D. Fla. Dec. 10, 2014) (applying this analysis).
[35] *See, e.g.*, Cal. Civ. Code § 3439.10 (2016).

internet searches using a search engine, and a review of social media accounts. In particular, social media searches frequently turn up information that can later be used in a lawsuit to uncover fraudulent conduct. The applicant may wish to consider hiring a private investigator in this regard. If the applicant already has access to a significant amount of financial information relating to a business, the applicant should consider hiring a forensic accountant to determine if assets have been fraudulently transferred or other suspicious circumstances are present. Some jurisdictions also permit pre-suit discovery (e.g., a pre-suit deposition under Texas Rule of Civil Procedure 202), although the benefits of formal pre-suit discovery when fraudulent conduct is possible are often outweighed by the risks inherent in tipping off a fraudster that litigation is being evaluated. In short, while a pre-suit investigation can have drawbacks, a party should, at a minimum, conduct internet searches and review social media postings.

Because the U.S. permits liberal discovery once a lawsuit has been filed, uncovering fraudulent conduct becomes much easier once a lawsuit is commenced. The problem, of course, is that merely filing a lawsuit does not prevent a fraudster from dissipating assets while it is pending without some kind of additional equitable relief in place, like a preliminary injunction or the appointment of a receiver. Obtaining either of these types of equitable relief measures requires more than mere suspicion that fraudulent conduct has occurred. Frequently, the best course of action for a party that has sufficient evidentiary support to file a lawsuit, but not sufficient evidence to obtain a preliminary injunction or a receiver, is to file suit and seek expedited discovery, which may be authorized by the court in most jurisdictions.[36]

b. Injunctive Relief

An injunction is an equitable remedy under which a court orders the enjoined person or persons not to do something. Temporary injunctions, also known as preliminary injunctions, operate to preserve the *status quo* until a case can proceed to trial. Temporary restraining orders remain in place for only a brief period, generally until the temporary injunction hearing.

U.S. fraudulent transfer law specifically provides for a court to order injunctive relief in appropriate circumstances. Temporary restraining orders can often be obtained on an *ex parte* basis, while temporary injunctions typically require a lengthy hearing on the following elements: (1) proof of a cause of action (e.g., actual fraudulent transfer); (2) a likelihood of recovery; (3) probable, imminent,

[36] Under Federal Rule of Civil Procedure 11 and its state law equivalents, a litigant must ensure that allegations in the lawsuit have evidentiary support, or at least are likely to have evidentiary support after a reasonable inquiry.

and irreparable harm if the injunction is not granted; (4) the injury that will occur outweighs any injury that will result from granting the injunction; and (5) the injunction serves the public interest.[37] Irreparable injury is present if damages will not suffice to compensate the applicant.[38] If the enjoined person violates the injunction, he or she may be held in contempt of court.

c. Making Use of Receiverships and Creditors' Committees

Equity receiverships and Chapter 11 bankruptcy proceedings can be useful proceedings for recovering fraudulently transferred assets. As discussed in Section 3.a above, an equity receiver is generally provided the right to prosecute fraudulent transfer claims for the benefit of the receivership estate and its creditors. Similarly, Unsecured Creditors' Committees are often granted a similar right in Chapter 11 bankruptcies, particularly when the debtor's management may have a conflict of interest that would prevent them from diligently prosecuting fraudulent transfer actions. In addition, equity receivers and Creditors' Committees are granted broad investigative powers including, in the latter case, under Rule 2004 of the Federal Rules of Bankruptcy Procedure which authorizes an expansive examination regarding the debtor and its financial affairs.

d. Cross-Border Matters

Fraudulent transfer litigation frequently requires recovering transfers made as part of cross-border transactions. Cross-border litigation can be particularly difficult where laws between jurisdictions differ, especially if the transfers involved jurisdictions that are generally unfriendly to asset recovery. In such situations, identifying and retaining qualified counsel and other skilled asset recovery professionals (e.g., members and strategic partners of ICC FraudNet) in the respective foreign jurisdiction is often a critical step to increase one's chances of recovery.

If the matter involves a non-U.S. insolvency proceeding, it is strongly worth considering seeking to have the foreign proceeding recognized under Chapter 15 of the U.S. Bankruptcy Code, which is based on the Model Law for Cross-Border Insolvency. If recognition is granted to the foreign proceeding, the U.S. bankruptcy court can provide a forum for asset recovery efforts in the U.S. Another good option that is available regardless of whether an insolvency proceeding is pending in another jurisdiction is to file an application under 28 U.S.C. § 1782 to obtain information from the U.S. to assist a foreign tribunal. U.S. federal courts regularly

[37] *Paulsson Geophysical Servs. v. Sigmar*, 529 F.3d 303, 309 (5th Cir. 2008); *Butnaru v. Ford Motor Co.*, 84 S.W.3d 198, 204 (Tex. 2002).
[38] *Butnaru*, 84 S.W.3d at 204.

grant these applications to permit discovery to proceed in the U.S. to obtain evidence for use in another country.

5. Conclusion

Fraudulent transfer litigation is a critical tool for creditors to recover assets improperly transferred by a fraudster. Therefore, it is important to understand the law governing fraudulent transfers. Fortunately, the U.S. has a well-developed body of law concerning fraudulent transfers, the principles governing such claims and the practical implications involved in fraudulent transfer litigation. A thorough understanding of this area of law is critical for any U.S. asset recovery professional.

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How the UK Courts are Seeking to Police the Cryptocurrency 'Wild West' with Novel Orders

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How the UK Courts are Seeking to Police the Cryptocurrency 'Wild West' with Novel Orders

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Introduction

A review of recent case law on the English courts' response to the recognition of digital assets as property indicates that the law can respond quickly to impose order on this new virtual territory and demonstrates that the common law can be flexible, albeit given a strong steer.

The Legal Statement published by the UK Jurisdiction Taskforce of the LawTech Delivery Panel (UKJT) in November 2019 ('the Legal Statement') did not have the force of law in the sense of creating binding precedent but its conclusions on the legal status of cryptoassets have, nonetheless, been enthusiastically adopted by the English courts in tackling fraud related to such digital assets and in recovering them. Whilst some legal questions remain, the civil courts in England have not merely accepted that cryptocurrencies such as Bitcoin and other digital assets, are indeed 'property' for various legal purposes but continue to develop novel interim and final orders to take account of digital assets' unique features. Whether cryptoassets are property is vitally important because that issue defines the nature of rights, liabilities and remedies in English law in disputes concerning them. Indeed, although the criminal law was expressly excluded from the scope of the Legal Statement, the criminal courts have begun to recognise the proprietary nature of cryptoassets both in the substantive law and in the law relating to restraint and confiscation of assets. In this way, and without the benefit of any legislation, the English courts have, since the Legal Statement, demonstrated a

flexibility and willingness to police the world of virtual assets and prevent this jurisdiction becoming a 'Wild West', bereft of meaningful remedies.

The Legal Status of Digital Assets prior to the Legal Statement

In *Your Response Limited v. Datateam Business Media Limited*[1], the Court of Appeal held that an electronic database was not a form of property capable of possession. Lord Justice Moore-Bick held that recognising possession of such a thing would be a departure from existing case law and that, if such intangible property that was not a 'chose in action' was to be so recognised, it would require legislation. He thought there was *"a powerful case for reconsidering the dichotomy between choses in possession and choses in action and recognising a third category of intangible property, which may also be susceptible of possession and therefore amenable to the tort of conversion*[2]*"*. If that case were accepted, the judge thought that *"it would have the beneficial effect of extending the protection of property rights in a way that would take account of recent technological developments"*. Parliament did not act, however, and the English courts[3] were at risk of being left behind the technological developments arising from digital assets. Other common law jurisdictions did not feel so constrained. In New Zealand in *Dixon v. The Queen*[4], the Supreme Court had held that digital files comprising CCTV footage held on a computer system were more than mere information and could be 'property' for the purposes of the New Zealand Crime Act. The NZ Supreme Court considered *"that the fundamental characteristic of "property" is that it is something capable of being owned and transferred…"* and that the digital files had that characteristic. In *B2C2 Ltd v. Quoine Pte Ltd,*[5] in the Singapore International Commercial Court the judge was satisfied that cryptocurrencies met all the requirements of the classic definition of a property right set down by the House of Lords in *National Provincial Bank v. Ainsworth*[6], namely that they are *"definable, identifiable by third parties, capable in its nature of assumption by third parties, and hav[ing] some degree of permanence or stability."* On appeal, however, the question whether cryptocurrencies were a form of property was left open[7].

Technological Developments

In the meantime, in the growing world of cryptoassets there were, perhaps inevitably, fraudsters willing to exploit the new technologies – particularly their

[1] [2014] EWCA Civ 281
[2] At [27]. That case being made by Prof. Sarah Green (who sat on the UK Jurisdiction Taskforce and is now a Law Commissioner) and John Randall KC in 'The Tort of Conversion'
[3] Feeling themselves bound by *OBG Limited v. Allan* [2007] UKHL 21
[4] [2015] NZSC 147
[5] [2019] SGHC(I) 03
[6] [1965] 1 AC 1175
[7] [2020] SGCA(I) 02

speed and scope for anonymity - for their own gain and to others' detriment. Bitcoin were introduced in 2008 and increased in popularity before the use of cryptocurrencies became widespread in 2017. They were, at least initially, used predominantly as a medium of exchange for unlawful and/or secret purposes.

The English courts' response to the Legal Statement

A prime example of the use of Bitcoin for nefarious purposes is the case that led to the first reasoned judgment deciding that Bitcoins are property in English law, *AA v. Persons Unknown*[8], a decision of Mr. Justice Bryan. The claimant was the insurer of the victim of a hack and ransom demand. The victim was required to pay the ransom in Bitcoin. The claimant raised proprietary claims and sought, among other orders, a proprietary injunction in respect of the Bitcoin that had been paid over. Bryan J, influenced by the Legal Statement, accepted that crypto assets such as Bitcoin were property, albeit they are neither 'choses', or 'things' in possession or things in action. As did the first instance judge in *B2C2 Ltd v. Quoine Pte Ltd,* they met the criteria for 'property' in *National Provincial Bank v. Ainsworth*. The interim proprietary injunction was granted. The case signifies a key development. It began a number of cases which have, collectively, provided a degree of confidence in the ability of the English legal system to engage with crypto-related fraud. Subsequently, the English courts, in order to assist claimants who have been dispossessed of their cryptoassets, have been prepared to grant proprietary injunctions, asset preservation orders, freezing orders and information/disclosure orders in respect of cryptocurrencies.

In *Ion Science Ltd v. Persons Unknown*[9], the Commercial Court granted an interim proprietary injunction and a worldwide freezing order against unidentified defendants in respect of Bitcoin that had been dissipated by the wrongdoers following a fraud. The Court also granted permission to serve *Banker's Trust* disclosure orders against the exchanges that processed the transactions in order to help locate the missing digital assets and identify the wrongdoers. In the final judgment, and to assist enforcement of it, the Court granted the first third-party debt order in respect of Bitcoin.

The claimants in *Fetch.ai Ltd v. Persons Unknown Category A*[10], were granted a worldwide freezing order and proprietary injunctive relief against unknown fraudsters in addition to a *Norwich Pharmacal Order* allowing the claimants to obtain information from the cryptocurrency exchange that would, in turn, assist them to trace assets.

[8] [2019] EWHC 3556 (Comm)
[9] unreported, 21 December 2020
[10] [2021] EWHC 2254 (Comm)

In *Nicholls v. Little*[11] investors in cryptocurrency obtained a freezing and preservation order over the cryptoassets of an individual who claimed to be a specialist in investing in cryptocurrency and who had refused to return their assets to them. The claimants had obtained a default judgment against him, and the Court granted a freezing order to enable them to seek enforcement of it.

The New Zealand High Court in *Ruscoe v. Cryptopia Ltd (in Liquidation)* held that cryptocurrencies are a form of property that are capable of being held on trust. In this jurisdiction, *Wang v. Darby*[12], *Jones v. Persons Unknown*[13] and *LMN v. Bitflyer Holdings Inc & Ors.*[14] proceeded on the same basis. Indeed, in *Cryptopia* the court decided that the digital assets held by the Cryptopia exchange were also held on express trust on behalf of its customers. Whether cryptoassets can be held on trust is important because it determines the availability of certain proprietary claims in respect of cryptoassets (e.g., tracing) might be available following a breach of trust. *Osbourne v. Persons Unknown Category A*[15] involved the theft of valuable non-fungible tokens (NFTs) and is believed to be the first occasion when the court permitted service on the defendants solely by NFT.

The English criminal courts' response

The effect of the Legal Statement has been felt in the English criminal law too, which was beyond its initial ambit.

The editors of Archbold, in chapter 21-52, dealing with 'intangible property' for the purposes of the Fraud and Theft Acts, cite *AA v. Persons Unknown* in support of their commentary that *"Cryptocurrency is intangible property"*. In *R v. Wright*[16] the appellant in person, in a renewed application for leave to appeal against his conviction for blackmail, sought to persuade the Court of Appeal (Criminal Division) that it was at least arguable that his demands for Bitcoin would not have amounted to a 'gain' for him for the purpose of the offence. His reasoning was that 'gain' is confined by the Theft Act 1968 "only to gain or loss in money or other property"[17] and that "property includes money and all other property, real or personal, including things in action and other intangible property.[18]" In can be seen that the definition of 'property' in the Theft Act 1968 is, in any event, and by contrast to the definition of gain, non-exhaustive. The Court of Appeal rejected the

[11] [2022] EWHC 2344 (QB)
[12] [2021] EWHC 3054 (Comm) (although no trust was held to exist on the facts)
[13] [2022] EWHC 2543 (Comm)
[14] [2022] EWHC 2954 (Comm)
[15] [2023] EWHC 39 (KB)
[16] [2022] EWCA Crim 882
[17] Section 34(2)(a)
[18] Section 4(1)

ground of appeal, however, expressly in reliance on the decisions in *AA v. Persons Unknown*, *Ion Science v. Persons Unknown*[19] and *Fetch AI Limited v. Persons Unknown*[20]. Although *Wright* is not itself of the highest authority, it can be anticipated that the Court of Appeal (Criminal Division) will adopt a similar approach if asked to decide whether cryptocurrencies are property for the purposes of criminal offences.

Reflecting the approach taken by the civil courts in respect of freezing orders, Mr. Justice Fordham in *DPP v. Briedis*[21], an unopposed application for a 'Property Freezing Order' under Part 5 of the Proceeds of Crime Act 2002 (POCA), was *"… satisfied that cryptocurrency, as cryptoassets, fall within the wide definition of "property" in section 316(4)(c) ("other intangible … property"), especially when viewed in the light of the purpose of these statutory powers. It would be a serious lacuna if cryptoassets fell outside the reach of this statutory scheme."* The judge cited the decision in *AA v. Persons Unknown* and, indeed, the Legal Statement itself in support of his conclusion on the definition of 'property' for the purposes of Part 5. The definition in s.316(4)(c) is the same as that which is applied generally in POCA (e.g., in ss.84(1)(c) and 340(9)(c)) and so Fordham J's conclusion is likely to be adopted more widely to the provisions of POCA dealing with restraint and confiscation orders and to offences under POCA of laundering the proceeds of crime. Mitchell, Taylor and Talbot on Confiscation and the Proceeds of Crime write, at 03.034, "*Cryptoassets constitute "property", including for the purposes of a property freezing order. The same analysis is thought to apply for the purposes of a restraint order.*"

Unresolved Issues

Some questions remain. In respect of jurisdiction, *Tulip Trading Ltd v. Bitcoin Association for BSV*[22] took a different approach to the 'lex situs' of a cryptoassets than had been taken in *Fetch.ai Ltd*. In his speech on 24 February 2022[23], Sir Geoffrey Vos MR suggested that the Civil Procedure Rules may be amended to deal with the issue of jurisdiction in cryptoassets disputes. The Law Commission's Digital Assets Project will consider whether such assets are capable of being 'possessed'. As the law currently stands, only physical objects can be 'possessed'. This has implications for how digital assets can be transferred and secured, for example. The Law Commission will also be looking at whether the dichotomy between 'things in possession' and 'things in action', which prevented substantial development of the law in relation to digital assets prior to the Legal Statement, remains valid.

[19] (Commercial Court, 21st December 2020)
[20] [2021] EWHC 2254 (Comm)
[21] [2021] EWHC 3155 (Admin) at [10]
[22] [2022] EWHC 667 (Ch)
[23] At the launch of the UKJT's 'Smarter Contracts' report

The Court of Appeal, in either its criminal or civil division, has not yet provided a definitive judgment on the legal status of cryptoassets. Most of the first instance decisions have been interlocutory.

The Overall Picture

Nonetheless, as the plethora of cases at first instance dealing with digital assets shows, the English courts have enthusiastically embraced the opportunity – or steer - given to them by the Legal Statement. The cases show the flexibility of the common law. In the absence of legislation, the courts have to a great extent furthered the objective of the Master of the Rolls and the government for the English law to adapt to the challenges presented by digital assets and the potential for fraud in relation to their use.

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Asset Recovery as a Tool to Combat Investment Fraud – a view from Ireland

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Asset Recovery as a Tool to Combat Investment Fraud – a View from Ireland

BARRY ROBINSON

Abstract

In this article, Barry Robinson of BDO discusses Ponzi Schemes, Binary Options fraud and the collapse of FTX. He also discusses asset recovery in an ever-changing world of global investments and the continued rise of cryptocurrencies, including a recent Irish Court decision to "pierce the corporate veil" for the first time in that jurisdiction.

Introduction

Investment fraud occurs when someone "knowingly misleads an investor using false information for the purpose of monetary gain"[1]. There are many different types of investment fraud with one thing in common: they often involve perpetrators contacting individuals promising high returns and convincing them to invest in schemes or products that are worthless or do not exist. Once the perpetrators have received payment, they often cease contact with their victims.[2] Many such schemes include Affinity Fraud, Advance Fee Fraud, Binary Options Fraud, High Yield Investment Programs, Internet and Social Media Fraud, Microcap

[1] Beals, M., M. DeLiema and, M. Deevy (2015). 'Framework For a Taxonomy of Fraud,' Stanford Center on Longevity Working Paper. Palo Alto, CA.

[2] Investment fraud | Action Fraud (no date). Available at: https://www.actionfraud.police.uk/a-z-of-fraud/investment-fraud. (Accessed 17 April 2023)

Fraud, Ponzi Schemes, Pre-IPO Investment Scams, Pyramid Schemes, "Prime Bank" Investments, Promissory Notes and 'Pump and Dump' Schemes.[3]

In this article, Barry Robinson considers three types of investment fraud (Ponzi schemes, Cryptocurrency and Binary options) and identify the scale of these frauds, particularly during the Covid-19 Pandemic. Furthermore, it discusses the asset recovery tools that are available to investors to recover funds and discuss two recent cases from Ireland, both of which assisted victims of alleged fraud to recover funds. Finally, the article discusses what asset recovery tools are likely to be needed in an ever-changing world of global investments, the continued evolution of technology and the continued rise of cryptocurrencies.

Traditional Ponzi Schemes

A Ponzi scheme is an investment fraud that pays existing investors with funds collected from new investors[4]. Charles Ponzi first committed the first known fraud of this type in the 1920s, promising high returns for investments in stamps[5]. Ponzi scheme organisers often promise to invest funds and generate high returns with little or no risk. However, in many Ponzi schemes, little or no money is invested by the perpetrators. Instead, perpetrators of Ponzi schemes typically pay those who invested earlier by "recruiting" new investors, and have been known to keep some of the investors' funds for themselves[6].

Ponzi schemes require a constant flow of new money to thrive. When it becomes difficult to find new investors, or when large numbers of existing investors withdraw their funds or "cash out", such schemes tend to collapse, leaving later investors with significant losses. One such well-known scheme, perpetrated by Bernie Madoff, is estimated to have defrauded investors by up to $65 billion. On March 12, 2009, Madoff pleaded guilty to 11 federal felonies and to date approximately $4 billion out of the $65 billon originally invested has been returned to investors[7].

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[3] Types of Fraud | Investor.gov (no date). Available at: https://www.investor.gov/protect-your-investments/fraud/types-fraud (Accessed 17 April 2023)

[4] Ponzi Scheme | Investor.gov (no date). Available at: https://www.investor.gov/protect-your-investments/fraud/types-fraud/ponzi-scheme. (Accessed 17 April 2023)

[5] Trozze, A., Kamps, J., Akartuna, E.A. *et al.* Cryptocurrencies and future financial crime. *Crime Sci* **11**, 1 (2022)

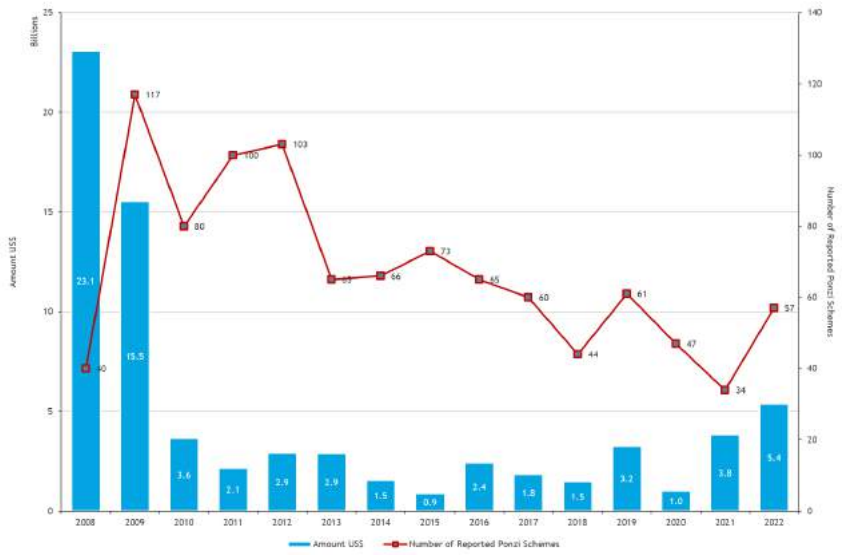
[6] *Ponzi Scheme | Investor.gov* (no date b). Available at: https://www.investor.gov/protect-your-investments/fraud/types-fraud/ponzi-scheme. (Accessed 17 April 2023)

[7] *Justice Department Announces Total Distribution of Over $4 Billion to (2022)*. Available at: https://www.justice.gov/opa/pr/justice-department-announces-total-distribution-over-4-billion-victims-madoff-ponzi-scheme . (Accessed 17 April 2023)

During Covid-19, investment fraud was prevalent across the globe, including in the USA where deceptive advertising was undertaken by some companies which claimed to have developed alleged "miracle cures" for COVID-19. Such advertising promised exponentially high growth in the value of an investment if the victim invested in a company marketing false pills that claimed to prevent coronavirus infections[8]. Such schemes portrayed many traits of a Ponzi scheme, including promises of high returns based on false premises.

An analysis by BDO of the Ponzi Scheme database[9] (a collection of publicly reported Ponzi schemes and their reported values), shows that since the financial crash of 2008, the value and volume of reported Ponzi schemes has significantly decreased (from US $23 billion of losses in 2008 to US $4 billion of losses in 2021). As can be seen from the graph below, the scale of reported Ponzi schemes in 2021 is at a similar level to 2010 and has remained constant over the past 11 years. This suggests that Ponzi Schemes are still big business for perpetrators of such schemes and investors should be wary of any investment schemes offering unusually high returns.

Figure 1: BDO's analysis of Ponzi schemes by volume and value 2008 to 2021 (based on data published in the "Ponzi Scheme database")[10]



[8] Murrar, F. (2022), "Fraud schemes during COVID-19: a comparison from FATF countries", Journal of Financial Crime, Vol. 29 No. 2, pp. 533-540

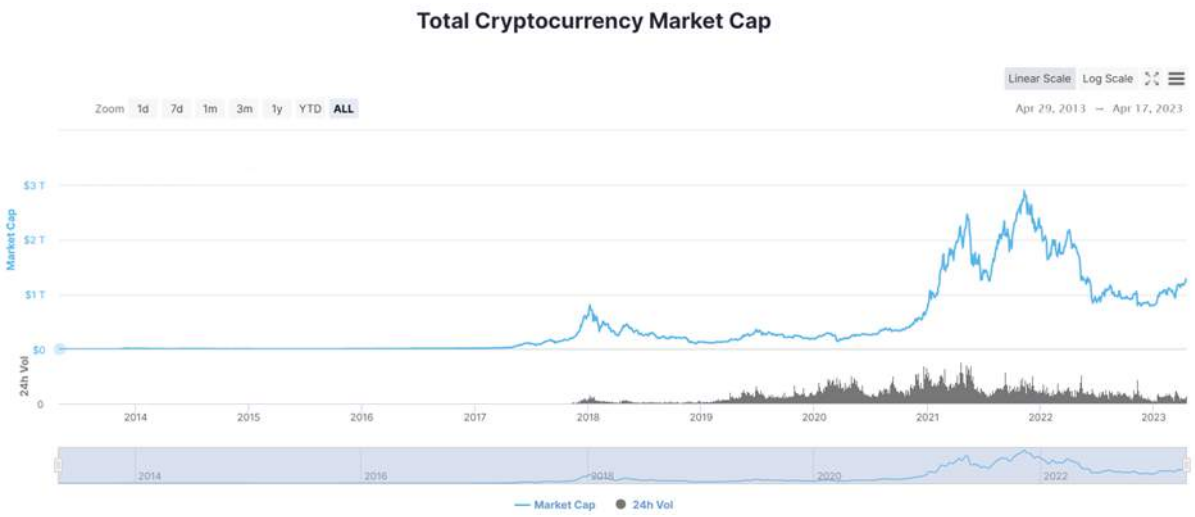
[9] Ponzi Scheme Database — Ponzitracker (no date). Available at: https://www.ponzitracker.com/ponzi-database (Accessed 17 April 2023)

[10] *Ponzi Scheme Database — Ponzitracker* (no date). Available at: https://www.ponzitracker.com/ponzi-database (Accessed 17 April 2023)

Cryptocurrency Ponzi Schemes

During 2008 to 2021, there has been an increase in the the global value of cryptocurrencies, which has has significantly increased from zero in 2010 to approximately $3 Trillion in November 2021. From the graph below we can see that there was significant growth in the volume and value of all cryptocurrencies during 2020, 2021 and 2022, which coincided with the Covid-19 Pandemic.

Figure 2: Market Cap and 24hr volume of all cryptocurrencies 2013 to 2023 (Source: coinmarketcap.com)[11]



An academic study carried out 2020 by Corbet et al (Corbet et al, 2020)[12], identified that significant growth in both returns and volumes traded indicated that large cryptocurrencies acted as a store of value during this period of exceptional financial market stress, which coincided with the Covid-19 Pandemic. Furthermore, cryptocurrency returns were found to be significantly influenced by negative sentiment relating to COVID-19. The study also found that investors perceived Cryptocurrencies as not only providing diversification benefits for them, but results suggested that digital assets acted as a safe-haven similar to that of precious metals during historic crises.

Cryptocurrency losses

[11] *Global Cryptocurrency Market Charts | CoinMarketCap* (no date). Available at: https://coinmarketcap.com/charts/ (Accessed 17 April 2023)

[12] Corbet, S., Hou, Y. G., Hu, Y., Larkin, C., & Oxley, L. (2020). Any port in a storm: Cryptocurrency safe-havens during the COVID-19 pandemic. Economics Letters, 194, 109377.

Unfortunately, the rise in investments in cryptocurrency has also given rise to an increase in investors losing large sums of money through fraudulent cryptocurrency investment schemes. Several investment schemes involving cryptocurrencies such as Bitcoin have been suspected to be Ponzi schemes, for example, the "Bitcoin Savings and Trust"[13] ,"Forcount"[14] and "IcomTech".[15] which have been the subject of investigations by the United States Department of Justice ("DOJ").

Perhaps the two most recent high profile cases involving allegations of a cryptocurrency being used to perpetrate fraud on investors is that of the collapse of the FTX Exchange in the Bahamas and Celcius Network LLC. The recent bankrputcy of FTX and related entities was quickly followed by the arrest and extradition to the USA of its founder. It is suspected that up to $8 billion of investors' funds have been lost relating to FTX[16]. FTX's founder has been charged with perpetrating a multibillion-dollar fraud through the FTX Group. To date, FTX's co-founder and Chief Technology Officer, the CEO of a related entity Alameda Research[17], and an FTX Senior Executive[18] have all pled guilty to charges arising from their participation in schemes to defraud FTX's customers and investors.

FTX follows the collapse of other high-profile cryptocurrency companies (TerraLuna, Three Arrows Capital (3AC), Voyager Digital and Celsius Network) in 2022 which has become known as the "crypto winter".[19] Issues at Celcius Network LLC came to light in July2022, when it announced a pause on withdrawals, swaps, and transfers on its platform and ultimately filed for Chapter 11 bankruptcy in the USA. Its ex-CEO has recently been sued by the New York State Attorney General

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13 *Texas Man Sentenced For Operating Bitcoin Ponzi Scheme* (2016). Available at: https://www.justice.gov/usao-sdny/pr/texas-man-sentenced-operating-bitcoin-ponzi-scheme. (Accessed 17 April 2023)

14 *U.S. Attorney Announces Fraud And Money Laundering Charges Against* (2023). Available at: https://www.justice.gov/usao-sdny/pr/us-attorney-announces-fraud-and-money-laundering-charges-against-additional (Accessed 17 April 2023)

15 *U.S. Attorney Announces Fraud And Money Laundering Charges Against* (2022). Available at: https://www.justice.gov/usao-sdny/pr/us-attorney-announces-fraud-and-money-laundering-charges-against-founders-and-promoters (Accessed 17 April 2023)

16 *CFTC Charges Sam Bankman-Fried, FTX Trading and Alameda with Fraud and Material Misrepresentations* | CFTC (no date). Available at: https://www.cftc.gov/PressRoom/PressReleases/8638-22 (Accessed 17 April 2023)

17 https://www.justice.gov/usao-sdny/pr/united-states-attorney-announces-extradition-ftx-founder-samuel-bankman-fried-united

18 *CFTC Charges FTX Co-Owner with Fraud by Misappropriation and Aiding and Abetting Fraud Related to Digital Asset Commodities* | CFTC (no date). Available at: https://www.cftc.gov/PressRoom/PressReleases/8669-23 (Accessed 17 April 2023)

19 *Opening Statement of Commissioner Kristin N. Johnson Regarding Global Markets Advisory Committee* | CFTC (no date). Available at: https://www.cftc.gov/PressRoom/SpeechesTestimony/johnsonstatement021323. (Accessed 17 April 2023)

for allegedly defrauding investors out of billions of dollars' worth of cryptocurrency.[20]

As many economies recover from the Covid-19 Pandemic, it is yet to be seen just how many more victims of cryptocurrency-related frauds that may have occurred during the Pandemic will come to light in 2023.

Binary Options

As investors sought high returns on their investments post the 2008 financial crash, many turned to alternative investments including "binary options" as a way of making higher returns than conventional investments. A binary option is a type of options contract in which the pay-out will depend entirely on the outcome of a yes/no proposition, for example whether the price of a stock will rise of fall below a specified amount[21]. In recent years there have been numerous warnings issued by financial regulators about the prevalence of unregistered binary options investment schemes. One of the largest ever binary options fraud schemes involving up to $186 million recently came to light in a legal case in the Irish Courts involving an investor, William Thomas Powers against an Irish registered company, *Greymountain Management Limited (in Liquidation) & Others*[22]. In the opening paragraph of his judgment, Mr. Justice Twomey stated:

> "The following sad and very personal email is what Irish corporate fraud looks like in real-life terms: "**Can anybody help me with the withdrawing of €210,882** and wire it to my Beobank account; see attachment. Please understand that **my life has become unbearable**; **daily I am having stress**; I can't believe this is happening… **these were all my savings** from myself and my children. Please proof me that all of this is not **a scam.**" (Emphasis added)"

The case was of significant importance insofar as it was the first legal case in Ireland to "pierce the corporate veil" to identify the relevant individuals involved in operating and assisting the alleged fraudulent investment scheme and to make those individuals personally liable for the investors' losses, including two directors of the Irish company, whom the Court found to have been involved in

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[20] *Attorney General James Sues Former CEO of Celsius Cryptocurrency Platform for Defrauding Investors* (2023). Available at: https://ag.ny.gov/press-release/2023/attorney-general-james-sues-former-ceo-celsius-cryptocurrency-platform-defrauding (Accessed 17 April 2023)

[21] *CFTC/SEC Investor Alert: Binary Options and Fraud* | CFTC (no date). Available at: https://www.cftc.gov/LearnAndProtect/AdvisoriesAndArticles/fraudadv_binaryoptions.html (Accessed 17 April 2023)

[22] William Thomas Powers -v- Greymountan Management Limited (in Liquidation) & Ors [2021] IEHC 243

"impropriety" and responsible for the investors' losses as a result of a "derelict of their duties".

Asset recovery tools to recover fraudulent losses

As can be seen with the recent cases discussed in this article, there are a number of asset recovery tools available to investors to recover investment losses. Such tools include bringing legal proceedings against the investment vehicles and those individuals believed to be responsible for any alleged fraud. Once a Judgment can be obtained against a company or individuals, it may be possible to seek mutual recognition of that Judgment in multiple jurisdictions. Often the appointment of an insolvency practitioner and forensic accountants to investigate and initiate legal proceedings against the promoters and those entities involved in any alleged fraud can be very effective in the efforts to recover losses. In another recent case before the Irish Courts in 2022, an EU national was successful in legal proceedings brought in Ireland against a number of parties to have receivers appointed over assets to recover funds they invested. In that case, a Judge appointed receivers over and made permanent various freezing orders against several assets linked to various defendants in those proceedings, including property, yachts and bank accounts.[23]

Future developments in the fight against investment fraud

As more cases are expected to become known, there will be a greater need for effective tools in the fight against investment fraud, including cryptocurrency expertise alongside forensic accounting. Mutual recognition of judgments and court orders such as disclosure orders and freezing orders will also be required. It is anticipated that the Council of the European Union's recent decision for the EU to accede to the 2019 Hague Convention on the recognition and enforcement of foreign judgements in civil or commercial matters will lead to a greater ability for investors to recover losses as it will enable recognition and enforcement of judicial decisions from non-EU States within the EU. For victims of fraud, it is hoped that recovery of funds lost through fraudulent schemes will become easier across the globe and that investment frauds in the future will no longer be able to hide behind the corporate veil or anonymous usernames in unidentified jurisdictions.

[23] Healy, T. (2022) "High Court says French actor Dany Boon entitled to €4.87m over fraud," Independent, 14 December. Available at: https://www.independent.ie/business/irish/high-court-says-french-actor-dany-boon-entitled-to-487m-over-fraud-42217701.html. (Accessed 17 April 2023)

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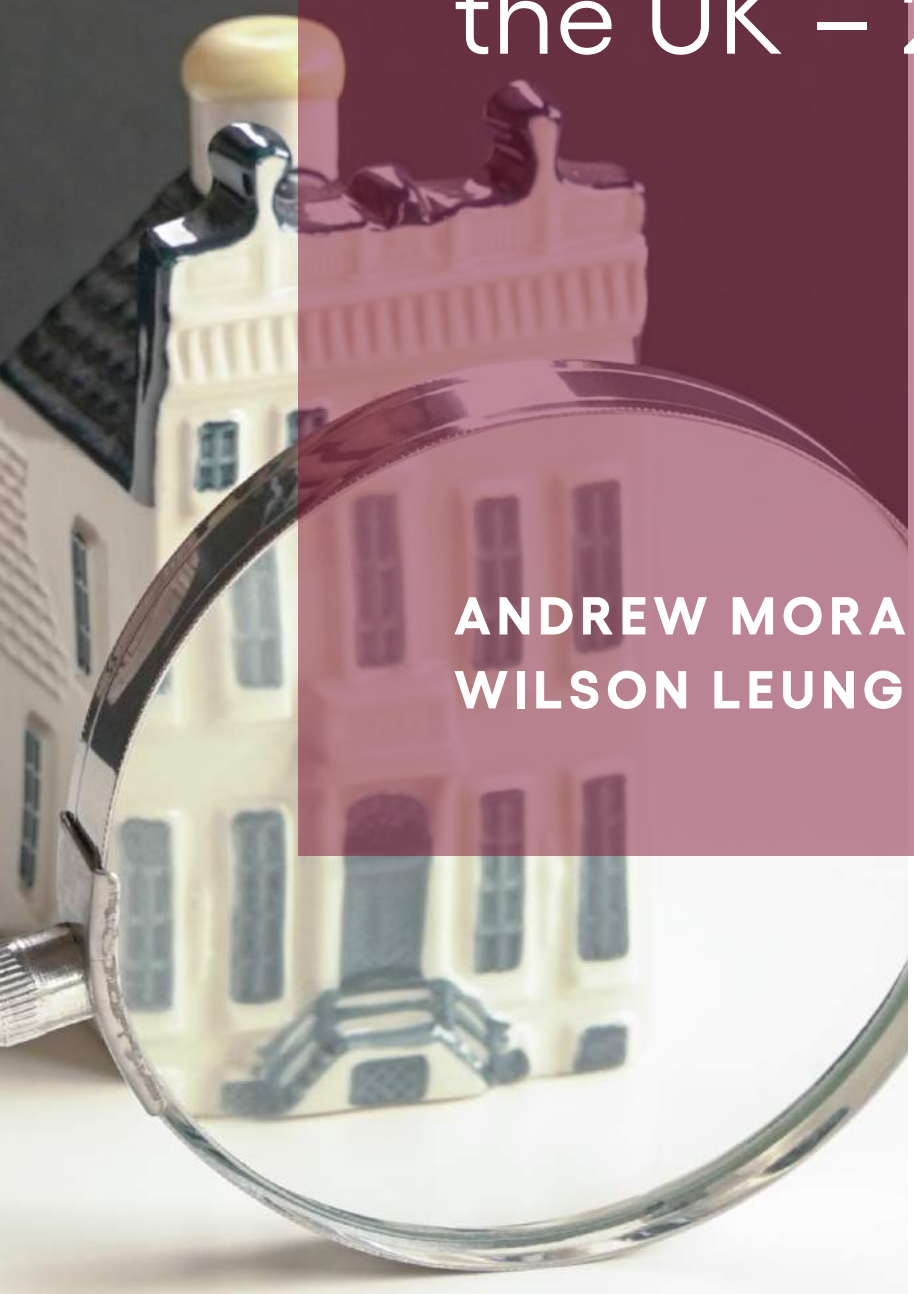

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Unexplained Wealth Orders in the UK – 2022

ANDREW MORAN KC AND WILSON LEUNG

Abstract

In this article, Andrew Moran KC and Wilson Leung, barristers at Serle Court, provide an overview of the background, structure, and operation of the Unexplained Wealth Order ('UWO') regime in the United Kingdom. The article also considers recent amendments made in 2022 and the mechanism's prospects as an effective tool.

Background

A UWO is a civil investigation tool used in the UK to assist enforcement authorities in building evidence to combat money laundering. A UWO compels a person holding particular property to explain the nature and extent of his interest in it, and how he obtained it. The objective is to provide the authorities with information to aid their assessment of whether the assets were illegitimately obtained. UWOs are particularly aimed at situations where a person has property that is disproportionate to his known income. UWOs are potentially a valuable tool for authorities to obtain information, especially because the threshold requirements for obtaining such orders are relatively low.

Historically, the UK has been an attractive destination for those who seek to launder illicit proceeds. UWOs were introduced in the UK via the Criminal Finances Act 2017, and inserted into Part 8 of the Proceeds of Crime Act 2002 ('POCA').

Under the then existing provisions of POCA, UK enforcement agencies frequently had grounds to suspect that assets within the UK were the proceeds of crime (including crimes committed abroad), but were unable to freeze or recover those assets due to an inability to obtain evidence, often due to a foreign jurisdiction's lack of cooperation.[1] This might occur, for example, where the ruling regime of the country where the crime was committed has close ties with the perpetrator. UWOs were intended to ameliorate that. The provisions came into effect on 31 January 2018.[2]

Applying for a UWO

An application for a UWO can only be made by specified enforcement authorities. In England and Wales, these are:[3]

- National Crime Agency ('NCA')
- Serious Fraud Office
- HM Revenue & Customs
- Financial Conduct Authority
- Director of Public Prosecutions.

Other agencies cannot apply for UWOs: if they want a UWO to be pursued, they would have to refer the case to one of the above authorities.[4]

The application is made to the High Court.[5] The application must specify the property in respect of which the order is sought, and the person who is believed to hold the property (i.e. the respondent).[6]

UWOs applications are generally made without notice, and heard by the court in private (indeed, this is the "presumptive starting point").[7] However, the court has power to order a public hearing and/or refuse to make an anonymity order, especially where the desirability of open justice outweighs any privacy concerns.[8]

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[1] Criminal Finances Act 2017, Explanatory Notes, at para 12
[2] Criminal Finances Act 2017 (Commencement No 4) Regulations 2018 (SI 2018/78). See also Ali Shalchi (April 2022), *Unexplained Wealth Orders*, House of Commons Library Briefing Paper no. 9098, London: House of Commons Library, §1.3. <https://commonslibrary.parliament.uk/research-briefings/cbp-9098/> Accessed on 20 November 2022.
[3] s 362A(7). Unless otherwise indicated, all references to sections are to sections in POCA. For the sake of brevity, this article will refer to sections within Part 8 of POCA as they pertain to England and Wales (there are similar provisions in Part 8 which pertain to Scotland and Northern Ireland).
[4] Shalchi, *Unexplained Wealth Orders* (supra), at p 10.
[5] s 362A(1)
[6] s 362A(2)
[7] s 362I(1); *NCA v Hussain* [2020] 1 WLR 2145, at [88] (Murray J)
[8] *NCA v Mrs A (Ruling on Anonymity)* [2018] EWHC 2603 (Admin) (Supperstone J)

Requirements for a UWO

The threshold requirements for obtaining a UWO are:

> (1) There is reasonable cause to believe that: (a) the respondent holds the property; and (b) its value is greater than £50,000.[9]
>
> (2) There are reasonable grounds for suspecting that: (a) the known sources of the respondent's lawfully obtained income would have been insufficient to obtain the property; or (b) the property has been obtained through unlawful conduct.[10]
>
> (3) Either (a) the respondent is a "politically exposed person" ('PEP');[11] or (b) there are reasonable grounds for suspecting that the respondent (or a person connected with him) has been involved in "serious crime".[12]

If the threshold requirements are fulfilled, then the court "may" make an UWO – in other words, the court has a discretion.[13]

(1) The respondent holds the property and its value is greater than £50,000

"Property" is expansively defined: it encompasses "money"; "all forms of property, whether real or personal, heritable or moveable"; and "things in action and other intangible or incorporeal property".[14] Moreover, it does not matter where in the world the property is situated.[15] The respondent may be situated anywhere in the world.[16]

There is also a wide definition of "holding" property. Property is "held" by a respondent if he holds an interest in it.[17] An interest includes (where land is concerned) any legal estate, equitable interest, or power; and (where non-land property is concerned) a right.[18] Property is also held if the respondent has effective control over the property; is the trustee of a settlement by which the property is

[9] s 362B(2)
[10] s 362B(3); see also s 242
[11] s 362B(4)(a)
[12] s 362B(4)(b)
[13] s 362A(1); *NCA v Baker* [2020] EWHC 822 (Admin), at [22] (Lang J)
[14] ss 362H(6), 414(1)
[15] ss 362H(6), 414(1)
[16] s 362A(2)(b)
[17] ss 362H(6), 414(3)(za)
[18] ss 362H(6), 414(3)(b), 414(3)(d)

held; or is a beneficiary in relation to such a settlement.[19] Thus, the definition is broad enough to cover circumstances in which property is held in trust or owned in a complex corporate structure arrangement.[20] It also covers anyone who is in possession of the property.[21] A person can hold property irrespective of whether there are other persons who also hold it.[22] The broadness of these provisions makes sense, as proceeds of crime will often be held through corporate, trust, or other structures designed to obscure the true ownership.

The applicable test here is "reasonable cause to believe".[23] This does not require the enforcement authority to prove the requirements set out at (1) above, whether to the criminal or civil standard of proof. It does require the enforcement authority to show that the fact is (subjectively) believed to be true, and that there are "objectively reasonable grounds" for that belief.[24] "Belief" does not require a firm conviction, though it is "a more positive frame of mind than suspicion."[25]

(2a) The respondent's lawfully obtained income would have been insufficient to obtain the property

The basic exercise here is to compare the respondent's known financial circumstances (insofar as this is derived from legal sources) with the value of the property.

In considering this question, the court is bound by the following guidelines:

> (i) The court must consider whether a mortgage (or other type of security) might have been available to enable the respondent to obtain the property;[26]
>
> (ii) The property should be assumed to have been bought at market value;[27]
>
> (iii) The legality of the means by which income was obtained is to be assessed by reference to the laws of the country where the income arose.[28]
>
> (iv) The "known" sources of income to be taken into account are those "*reasonably ascertainable from available information"* at the time of the

[19] s 362H(2)
[20] Criminal Finances Act 2017, Explanatory Notes, para 71
[21] *NCA v Hussain* (supra), at [29]
[22] s 362B(5)(a)
[23] s 362B(2)
[24] *NCA v Baker* (supra), at [24]-[25]; *NCA v Hussain* (supra), at [31]-[34]
[25] *NCA v Hussain* (supra), at [31]-[34]
[26] s 362B(6)(a)
[27] s 362B(6)(b)
[28] s 362B(6)(c)

application, including earnings from both employment and assets[29] (and presumably including any capital gains[30]). This might include, for instance, data available from internet searches and company registry records.

The UK authorities' code of practice states that the applicant authority should be able to explain its suspicion by reference to disclosable intelligence or information about, or specific behaviour by, the person concerned (including open source material from overseas where there are public registers relating to property and public officials' income).[31]

In some cases, the fact of a foreign criminal conviction may be adduced to meet this requirement. But the circumstances of the conviction might be such (and would be such, if there were a breach of *jus cogens* norms) that it could not form a proper ground for reasonably suspecting that the respondent's lawful income was insufficient to obtain the property.[32]

The threshold here is "reasonable grounds for suspecting". The phrase appears elsewhere in POCA as well as in other statutes (notably in connection with powers of arrest). The case law on the latter make clear that the threshold is a low one and a "very limited requirement" which could be satisfied where, for example, someone "could possibly" be associated with a robbery.[33] One may be dealing with a preliminary stage of an investigation and it is not necessary even to have formulated a *prima facie* case.[34] In short, the question is whether the enforcement authority's (subjective) suspicion, viewed objectively and in the round, is one which a reasonable person could hold.[35]

(2b) The property has been obtained through unlawful conduct

This is an alternative ground, introduced by the 2022 reforms (see below), which is based on examining whether the property has been obtained through unlawful conduct (as opposed to whether the respondent's income would have been sufficient to obtain the property). Again, the threshold here is "reasonable grounds for suspecting".

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[29] s 362B(6)(d)
[30] See: Code of Practice issued by the UK Home Secretary under s 377 of POCA, last updated 31 December 2021, at para 182. <https://www.gov.uk/government/publications/proceeds-of-crime-act-codes-of-practice-june-2021/code-of-practice-issued-under-the-proceeds-of-crime-act-2002-investigations-accessible-version> Accessed on 20 November 2022.
[31] Code of practice issued by the UK Home Secretary under s 377 of POCA (supra), at para 176
[32] *NCA v Hajiyeva* [2020] 1 WLR 3209, at [38] (Lord Burnett CJ, Davis and Simon LJJ) (Hajiyeva-CA)
[33] *Parker (aka Michael Barrymore) v Chief Constable of Essex Police* [2017] EWHC 2140 (QB) at [32] and [37].
[34] *NCA v Baker* (supra), at [37]; *NCA v Hussain* (supra), at [38]; *O'Hara v Chief Constable of the Royal Ulster Constabulary* [1997] AC 286, at 293.
[35] ***NCA v Hussain*** (supra), at [39]

(3a) The respondent is a PEP

The notion of a PEP derives from EU anti-money laundering legislation. It refers to an individual who is, or has been, "entrusted with prominent public functions" by an international organisation or any state other than the UK or an European Economic Area ('EEA') country[36]; or a family member or known close associate of, or person otherwise connected with, such an individual.[37] The logic is that, because of their position, PEPs are higher risk in terms of being involved in corruption overseas and money laundering in the UK.[38]

The definitions of being entrusted with prominent public functions, family member, and known close associate are each expanded by reference to the EU's Fourth Anti-Money Laundering Directive.[39] Consequently, PEP encompass not only legislators, senior government officials, and senior officials of international organisations, but also senior management of state-owned enterprises.[40] A state-owned enterprise would likely include any business in respect of which the government had a majority shareholding and ultimate control.[41]

(3b) The respondent (or a person connected with him) has been involved in serious crime

The alternative ground is that the respondent is involved in serious crime (or is connected with a person so involved). "Serious crime" is defined by reference[42] to an expansive list in Schedule 1 of the Serious Crime Act 2007, including *inter alia* fraud, organised crime, bribery, drug and people trafficking, and terrorism. The serious crime may have been committed anywhere in the world; but if outside the UK, the conduct must be criminal both under UK law and the law of the place where it occurred.[43]

Being "involved" in serious crime includes not only committing such an offence, but also extends to facilitating another's commission of an offence, and even to where the respondent "has conducted himself in a way that was likely to facilitate

[36] The concept of PEP continues to exclude public officials in EEA countries, notwithstanding that the UK itself has now left the EEA as a result of Brexit.
[37] s 362B(7)
[38] Criminal Finances Act 2017, Explanatory Notes, at para 13; and Shalchi, *Unexplained Wealth Orders* (supra), at p 10
[39] Article 3 of Directive 2015/849/EU dated 20 May 2015. See s 362B(8)
[40] ***Hajiyeva-CA***, at [16], [25]-[29]
[41] ***Hajiyeva-CA***, at [32]-[33]
[42] s 362B(9)(a)
[43] s 2(5), Serious Crime Act

the commission by himself or another person" of a serious offence.[44] "Facilitating" is a broad term which includes 'making easier', and there is no fixed list of conduct which would fall within it.[45]

The concept of being "connected" with someone involved in serious crime has a complex meaning derived from s 1122 of the Corporation Tax Act 2010,[46] but includes for example spouses, relatives, and business partners.

The applicable threshold here is again "reasonable grounds for suspecting".[47]

(4) Discretion

If the threshold requirements are met, the court has a discretion to make a UWO. Among other things, the court will have regard to human rights considerations, given that a UWO involves a degree of intrusion into the respondent's right to private life (which is protected by Article 8 of the European Convention on Human Rights). Thus, the court will seek to ensure that any use of UWO powers is proportionate to the outcome being sought; this will involve considering whether the necessary objectives could be achieved by less intrusive means.[48] The court may also take into account any risk of prosecution (whether in the UK or abroad) that the respondent could be exposed to by having to comply with the UWO.[49]

The UWO

A UWO requires the respondent to explain: (i) the nature and extent of his interest in the property; (ii) how he obtained the property (including, in particular, how costs incurred in obtaining it were met); (iii) in cases where the property is held by the trustees of a settlement, such details of the settlement as may be specified in the order; and (iv) other specified information and documents.[50] The respondent must provide the information within a specified time.[51] The court would likely require the order to be drafted in a clear and specific manner, given that non-compliance could attract serious consequences for the respondent (see below).

Non-compliance with UWO

[44] s 2(3)-(4), Serious Crime Act
[45] *NCA v Baker* (supra), at [52]; *NCA v Hussain* (supra), at [54]
[46] s 362B(9)(b)
[47] s 362B(4)(b)
[48] *NCA v Baker* (supra), at [64]-[65]
[49] *Hajiyeva-CA*, at [52]
[50] s 362A(3), (5)
[51] s 362A(6)

If the respondent fails, without reasonable excuse, to comply with the requirements of a UWO within the time specified, then the property is (rebuttably) presumed to be recoverable property for the purposes of civil recovery proceedings under Part 5 of POCA.[52] In other words, the court will presume that the property is the proceeds of unlawful conduct and therefore make an order that it be confiscated, unless the respondent can show (on the balance of probabilities[53]) otherwise.

As long as the respondent *purports* to comply with the UWO, he will not have failed to comply with it (and so the presumption will not arise).[54] It is debatable what degree of answer is needed from the respondent to constitute 'purported' compliance. The UK government's own code of practice apparently reflects this uncertainty: on the one hand, the code states that if a respondent provides "a poor or limited response",[55] that could amount to a failure to comply; on the other hand, the code suggests elsewhere that providing "the bare minimum of information" needed to address a UWO's requirements would suffice to be purported compliance.[56]

In addition to the presumption, the court can also secure compliance with a UWO by attaching a penal notice and thereby raising the possibility of committal proceedings.[57] It is possible that the court could enforce compliance in other ways too, for example, by making an order for cross-examination on a statement given in purported compliance with a UWO (by analogy with the practice in freezing orders[58]).

It is a criminal offence to knowingly or recklessly make a false or misleading statement in purported compliance with a UWO, punishable by a term of imprisonment of up to two years or a fine.[59]

Generally, an answer given in response to a UWO cannot be used as evidence in criminal proceedings.[60] This "use immunity" provision is included to compensate

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[52] s 362C(1)-(2)
[53] This is the standard of proof which applies to civil recovery proceedings under Part 5 of POCA: *Serious Organised Crime Agency v Gale* [2011] 1 WLR 2760, at para 123 (Lord Dyson JSC)
[54] s 362C(5)(a)
[55] Code of practice issued by the UK Home Secretary under s 377 of POCA (supra), at para 189.
[56] Code of practice issued by the UK Home Secretary under s 377 of POCA (supra), at para 185 and fn 55.
[57] *NCA v Hajiyeva* [2018] 1 WLR 5887, at [94]-[97]. Supperstone J rejected the contention that s 362C, by implication, ousts the court's power to attach a penal notice to a UWO and enforce non-compliance through committal proceedings.
[58] See, for example, *Jennington International v Assaubayev* [2010] EWHC 2351 (Ch)
[59] s 362E
[60] s 362F(1)

for the fact that the UWO regime restricts the usual privilege against self-incrimination.[61] There are some limited exceptions: for example, the answer can be used in confiscation or restraint proceedings under Part 2 of POCA.[62]

Interim freezing orders

When granting a UWO, the court may concurrently make an "interim freezing order" ('IFO'). An IFO prevents the respondent (and any other person with an interest in the property) from dealing with the relevant property in any way.[63] The aim is to prevent property being dissipated pending the respondent's provision of information ordered by the UWO.[64]

An IFO may only be granted where the court is satisfied that an IFO is necessary to avoid the risk of any subsequent recovery order being frustrated.[65]

The court has power to exclude certain property from an order, which includes doing so to enable the respondent to meet his reasonable living expenses, or to carry on his trade, business, profession, or occupation, or to meet legal expenses.[66]

After a respondent complies (or purports to comply) with a UWO, the enforcement authority will have to decide if any further enforcement or investigative proceedings are to be taken. If an IFO is in place, such determination must be made within 60 days of the date of compliance (which is extendable to 186 days).[67] The court must discharge an IFO if it is notified by the enforcement authority that it does not intend to pursue further proceedings[68] or else two days after the deadline for the enforcement authority's consideration.[69] Apart from that, the court may also vary or discharge an IFO at any time.[70]

UWOs' track record and 2022 amendments

UK enforcement authorities have had some success in using UWOs, such as:

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[61] *Hajiyeva-CA*, at [45], [51], [54]. See also: Shalchi, *Unexplained Wealth Orders* (supra), at §2.7
[62] s 362F(2)
[63] s 362J
[64] Shalchi, *Unexplained Wealth Orders* (supra), at p 13
[65] s 362J(1)-(2)
[66] s 362L(3) & (5)
[67] ss 362D(2), 362DA(5)
[68] s 362K(5)
[69] ss 362K(3)-(4). This applies unless there are any outstanding applications for property freezing orders, interim receiving orders, or restraint orders.
[70] s 362K(1)

(1) *NCA v Hajiyeva* [2018] 1 WLR 5887, upheld on appeal [2020] 1 WLR 3209:[71] This was the first UWO granted in the UK. The NCA obtained the order against the wife of a jailed chairman of an Azerbaijani state-owned bank, on the strength of evidence which included her extravagant spending at Harrods department store in London (over £16 million). After receiving the required information, the NCA brought forfeiture proceedings against her (which, as of June 2022, were ongoing).[72]

(2) *NCA v Hussain* [2020] 1 WLR 2145: The NCA obtained a UWO against a suspected money launderer for criminal gangs in northern England; it also obtained an IFO against him and six companies he owned. This led, ultimately, to him agreeing with the NCA to forfeit assets worth £10 million, even without being convicted of any criminal offence.[73]

But there has been at least one high-profile failure: *NCA v Baker* (supra). The NCA obtained UWOs in relation to several London properties. It was alleged that the properties were purchased to launder the illicit funds of a former Kazakh senior official. However, the respondents successfully applied to set aside the orders. The court held that the NCA's case was deficient and relied on unjustified assumptions. Among other things, the court decided that it was unable to infer that the money to purchase the properties had come from the former official.[74] The court also observed that, although the properties were held through complex offshore structures, this was not in itself a reason to assume that wrongful purposes were involved, because such structures could be used for privacy, security, or tax reasons.[75]

In any event, it is clear that UWOs have not been used with anywhere near the frequency originally pledged by the UK government. When introducing UWOs, the government estimated that there would be around 20 orders made per

[71] In December 2020, the UK Supreme Court refused to grant leave to further appeal: see Shalchi, *Unexplained Wealth Orders* (supra), at p 16
[72] Martin Bentham, "£16m Harrods big spender 'should be given her jewels back'", *Evening Standard* (14 June 2022) <https://www.standard.co.uk/news/london/harrods-big-spender-zamira-hajiyeva-jailed-banker-husband-jewellery-b1005995.html> Accessed 20 November 2022.
[73] Dominic Casciani, "Unexplained Wealth Orders: Suspected money launderer gives up £10m of property", *BBC News* (7 October 2020) <https://www.bbc.co.uk/news/uk-54442979> Accessed 20 November 2022.
[74] [100], [167], [197], [209], [215]
[75] [96]-[97]

year.[76] However, as of February 2022, a total of only nine UWOs had been made, relating to a mere four investigations.[77] No agency other than the NCA had utilised them. This has led the UK Parliament's Foreign Affairs Committee to describe the mechanism as "spectacularly unsuccessful".[78]

The lack of use has prompted efforts to reform the regime. In 2022, the UK government passed the Economic Crime (Transparency and Enforcement) Act, introducing a suite of measures targeted at money laundering. These included several amendments to Part 8 of POCA, aimed at making UWOs more effective:

> (1) Creating a new category of persons against whom a UWO can be made, namely, "responsible officers" of a respondent.[79] This is to enable enforcement authorities to obtain information more easily from officers of legal entities who have control over an asset, and thereby make it more difficult for individuals to hide behind complex ownership structures.[80]
>
> (2) Expanding the use of UWOs to cases where there are reasonable grounds for suspecting that the property has been obtained through "unlawful conduct" (as an alternative to scrutinising whether the respondent's lawful income would have been sufficient).[81]
>
> (3) Limiting enforcement authorities' liability for costs, such that costs will not be ordered against an authority unless its conduct has been unreasonable, dishonest, or improper.[82] This was to address a concern that UWOs' lack of use was partly caused by enforcement authorities' fear of adverse costs orders;[83] in the failed case mentioned earlier[84], the NCA had been ordered to pay £1.5 million in legal costs (reportedly half of the agency's annual budget).[85]

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[76] Criminal Finances Bill, Impact Assessment (by UK Home Office), 20 June 2017, para 16. <https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/621205/Impact_Assessment_-_UWOs.pdf> Accessed on 20 November 2022.
[77] Shalchi, *Unexplained Wealth Orders* (supra), at p 4
[78] UK Parliament, House of Commons, Foreign Affairs Committee, *The cost of complacency: illicit finance and the war in Ukraine* (HC 2022-23 168), 14 June 2022, para 12. <https://committees.parliament.uk/committee/78/foreign-affairs-committee/news/171796/morally-bankrupt-billionaires-using-the-uk-as-a-safe-deposit-box/>. Accessed on 20 November 2022.
[79] s 362A(3) and (8)
[80] Economic Crime (Transparency and Enforcement) Act 2022, Explanatory Notes, at para 335; and Shalchi, *Unexplained Wealth Orders* (supra), at p. 11
[81] s 362B(3)(b)
[82] s 362U
[83] UK Foreign Affairs Committee, *The cost of complacency* (supra), para 12.
[84] *NCA v Baker* (supra)
[85] Nicola Sharp, "Can UWOs shake their 'spectacularly unsuccessful' label?", *FT Adviser* (2 August 2022) <https://www.ftadviser.com/opinion/2022/08/02/can-uwos-shake-their-spectacularly-unsuccessful-label/> Accessed 20 November 2022; and Colette Kelly & Robert Payne, "Unexplained wealth orders: where are we now?" (*Wealth Briefing, 22 July 2022*) <https://www.wealthbriefing.com/html/article.php?id=195125> Accessed 20 November 2022.

(4) In cases where an IFO has been granted, increasing the time (from 60 days to a maximum of 186 days) for enforcement authorities to review the material provided in response to the UWO before having to decide whether to take further proceedings.[86]

Whether these reforms will have the desired effect remains to be seen. It is quite possible that they will increase the public's interest in UWOs and enforcement authorities' readiness to consider using them. The protection against adverse costs orders, in particular, may stimulate enforcement authorities' appetite for UWOs. However, a fact sheet issued by the UK government regarding the amendments conceded that it was difficult to pinpoint the extent to which the changes would increase the use of UWOs (albeit argued that "even a single UWO will have a high impact").[87] Meanwhile, the experience of other jurisdictions presents an unclear picture: although the UWO regime in Ireland has had notable success, the track record in Australia has been "mercurial at best".[88]

Ultimately, the success of UWOs may depend on factors other than the legislation itself. Even if the statutory mechanism is soundly designed, enforcement agencies will not be able properly to utilise it unless they are allocated sufficient funding so as to have the requisite financial, technical, and legal expertise.[89] As observed by the UK Foreign Affairs Committee: "Recent changes…seek to make it easier to apply for UWOs, but a law is only as effective as its enforcement."[90]

A 2017 report by the Royal United Services Institute argued that the UK authorities' success in leveraging the UWO mechanism would depend on four factors: expertise, inter-agency cooperation, resources, and political will.[91] It is to be hoped that these factors will shift in a positive direction. If so, we may see UWOs incrementally increasing in effectiveness and utility – even if they fall short of the success that had originally been promised.

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[86] s 362DA(5)
[87] UK Treasury, Home Office, and Department for Business, Energy and Industrial Strategy, Policy paper, "Fact sheet: unexplained wealth order reforms", 4 March 2022 <https://www.gov.uk/government/publications/economic-crime-transparency-and-enforcement-bill-2022-overarching-documents/factsheet-unexplained-wealth-order-reforms-web-accessible#key-reforms> Accessed 20 November 2022.
[88] Shalchi, *Unexplained Wealth Orders* (supra), p 20
[89] UK Foreign Affairs Committee, *The cost of complacency* (supra), para 12. See also Kelly & Payne, "Unexplained wealth orders: where are we now?" (supra).
[90] UK Foreign Affairs Committee, *The cost of complacency* (supra), para 12.
[91] Shalchi, *Unexplained Wealth Orders* (supra), p 21

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Blockchain Analysis: A Powerful Early Warning System for Crypto Insolvencies

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Blockchain Analytics: A Powerful Early Warning System for Crypto Insolvencies

SEAN ANDERSON & ELEANOR WARNICK

Abstract

In this paper, Sean Anderson and Eleanor Warnick consider how greater use of blockchain data analytics can complement the traditional asset recovery toolkit, by reference to some recent high-profile crypto cases.

Introduction

While cryptocurrency gained traction as an alternative asset class in 2021 and 2022, many fundamental questions about how crypto fits into the processes and standards of the fiat financial system remain unresolved. The ongoing wave of crypto insolvencies has provided a new sense of urgency to those open issues, particularly regarding due diligence and asset recovery.

The announcement by a leading accounting firm in December that it was suspending all work with crypto clients illustrates the extent to which those investing in the crypto space are operating without the safeguards, tools and assurances customary in financial markets. Fortunately, new analytic techniques using blockchain data can indicate reserves held by the business, provide early warning signs of impending financial distress and establish a foundation for

mapping and recovering assets after an insolvency. Indeed, over the past two years, more sophisticated software, more experienced investigators, and more aggressive government enforcement actions and private litigation cases have helped debunk the myth that the movements of crypto assets are untraceable.

Leveraging blockchain's transparency

The ability to analyse the solvency of a crypto enterprise in real time stems from the transparency of crypto transactions on the blockchain. Blockchain analytics firms and independent observers on social media first identify crypto addresses associated with major exchanges and hedge funds. Blockchain analytic software then makes it possible to identify irregular flows of funds out of exchanges. These fund flows can signal the crypto equivalent of a bank run, in which customers sense or hear that a crisis is looming and attempt to withdraw their funds before the exchange collapses. In November 2022, before declaring bankruptcy, FTX faced USD 6 billion in withdrawals in short succession in part due to concerns raised on social media by Changpeng Zhao, the head of rival exchange Binance.[1] Crypto holders promptly pulled their funds out of what was previously seen as a "safe" exchange—leading FTX to first freeze withdrawals and later admit it was insolvent. FTX's collapse was accelerated when users on social media, monitoring FTX's known addresses, encouraged other users to get their funds out before the addresses were eventually emptied.

In addition to crypto bank runs, investors can also observe sudden changes in behavior that could be a sign of financial distress. By watching for mispriced transactions—where a hedge fund, for example, might have overpaid to ensure a transaction took place quickly, or sold a token at a loss due to inadequate liquidity when selling the position over time may have avoided the loss—analysts can flag funds that are rushing to repay loans or cover positions. For example, the collapse of crypto hedge fund Three Arrows Capital was presaged by panicked trades, uncharacteristic OTC deals and hasty deposits to cover positions or add collateral—all of which were visible to trained observers.[2]

The ability to analyse developments in real time is particularly critical given the speed at which crypto insolvencies can occur. Part of crypto's appeal lies in its ability to execute transactions near instantaneously, without the security controls,

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[1] Source: Chaopeng Zhao's Twitter account @cz_binance https://twitter.com/cz_binance?ref_src=twsrc%5Egoogle%7Ctwcamp%5Eserp%7Ctwgr%5Eauthor, 'How Binance Played a Key Role as FTX Collapse Unfolded', *the Guardian*, 11 November 2022, theguardian.com/technology/2022/nov/11/binance-ftx-collapse-cryptocurrency-exchange-changpeng-zhao, accessed 29 December 2022

[2] 'On-Chain Forensics: Demystifyting stETH's "De-peg,"' *Nansen*, 29 June 2022, https://www.nansen.ai/research/on-chain-forensics-demystifying-steth-depeg?utm_source=twitter&utm_medium=social&utm_campaign=stETH_report_29June2022

oversight and other constraints that can slow down fiat currency transactions. As recent events have illustrated, however, frictionless efficiency is a double-edged sword: When things go south in the crypto world, they can do so with blinding speed. On the decentralised lending platforms on which many crypto companies were leveraging positions, there are no human managers from whom a trader could request an extra hour to meet a margin call. Instead, the platforms' code liquidates positions based purely on collateral requirements and price. And those liquidations can occur at any time of the day or night, without the buffer provided by the need to wait for the market to open.

Further, because many crypto companies use highly volatile cryptocurrency or tokens as collateral, a sudden drop in the value of that collateral can quickly snowball into a cascading series of potential liquidations or margin calls. FTX, for example, collateralised its loans with its own token, FTT[3]—of which FTX held roughly 80 percent of FTT's total supply, while affiliated hedge fund Alameda Research held roughly 40 percent of its USD 14.6 billion in assets in FTT.[4] Once the price of FTT began to drop, it created a crisis for both FTX and Alameda, which were suddenly unable to meet loan obligations, and the public nature of their financial distress only further drove down the price of FTT and other cryptocurrencies associated with the exchange and its founder, Samuel Bankman-Fried.

Asset recovery: Following the crypto

Just as analytical techniques give investors and others important tools to evaluate the soundness of crypto enterprises, those techniques may also be able to help in the asset recovery process after insolvencies by identifying assets that may have been improperly funnelled to entities or addresses controlled by the founders, their alter egos or even third-party attackers. For example, as FTX was entering insolvency, an unauthorised user began transferring and laundering cryptocurrency, which online analysts have already traced through a mixer to an exchange. In addition, Ethereum (ETH)[5] addresses associated with Alameda began swapping remaining crypto through instant exchangers, and eventually mixers. At the same time, some insiders appear to have received forewarning that Celsius and

[3] FTT stands for FTX token

[4] 'Blockchain Analysis: The Collapse of Alameda and FTC,' published on 17 November 2022, Nansen, nansen.ai/research/blockchain-analysis-the-collapse-of-alameda-and-ftx, accessed on 29 December

[5] Ethereum is a blockchain predominantly used for decentralised financial applications. Its native cryptocurrency is called Ether. Ether is the second largest cryptocurrency in terms of market capitalisation, after Bitcoin. An Ethereum wallet is a piece of hardware or software that stores the private cryptographic key which controls one or more specific Ethereum addresses. An Ethereum address is a public string of letters and numbers and its balance and previous transactions can be publicly seen on the Ethereum blockchain.

FTX would soon be insolvent, and withdrew their assets before those implosions. Other users—particularly in the Bahamas—were able to make withdrawals after authorities froze assets on FTX. Observers on social media have alleged that Bahamian account holders were using NFT sales to help users withdraw frozen crypto. In some of these cases, blockchain investigations will help the trustee identify individuals who received these funds.

Law firms, investigators and other advisors are likely to be sifting through the fallout of last year's crypto frauds and insolvencies for the foreseeable future. These cases will require sophisticated blockchain analysis to trace and recover cryptocurrency holdings, but will also involve the standard suite of asset recovery tools. In addition to cryptocurrency, investigators and lawyers will be pursuing private equity investments, revenue flows, third party debt and other tangible assets like yachts and mansions.

Regaining trust

In the midst of the current turmoil, crypto's future is far from clear. However, if it is to regain any of the momentum it once had, it will be essential to create a stronger system of validation for centralised crypto companies. Existing efforts to provide a "proof of reserves," crypto's analogue to the traditional audits of the fiat world, proved too easy to manipulate and lacked standards to allow less technical users to trust these claims. Here too, blockchain analytics offer a potential path forward.

Currently, the independent monitoring of crypto assets is a two-step process, in which third-party observers first identify ownership addresses and then track fund flows in and out of those addresses. However, exchanges could become active participants in that process by publicly identifying cold wallets where reserves are stored and maintaining a publicly facing ledger of those assets. To prove ownership and control, institutions can also sign smart contracts or engage in other on-chain transactions to demonstrate they actually control the private keys for the addresses. From there, blockchain analytics firms and investigators can monitor the stability of the exchanges' holdings and analyse trading patterns, as they do now.

While this approach should provide a more trustworthy tally of assets, the challenge of fully accounting for liabilities, including those in off-chain collateral agreements, remains. As such, there will always be the need for a third party to attest to proof of reserves. New cryptocurrency-focused auditing companies with the expertise to handle on-chain assets, while also conducting a larger audit of traditional assets, may fill the gap left by larger auditors. Over time, new expertise

and tools—or acquiring the companies that have them—may allow the larger auditing firms to more comfortably re-enter the cryptocurrency space.

Although it is difficult to accurately value crypto's market capitalisation, one estimate places it at roughly $900 billion as of the start of 2023. While that figure represents only a sliver of global assets—and a third of what it was only recently—it is still substantial enough to warrant the efforts of accounting firms, developers, investigators, regulators and independent observers to build an infrastructure that allows for greater accountability. Although there is much work to be done to provide future users with greater insight into the risk of platforms they use, blockchain analytics provide a solid foundation on which to begin.

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Intelligence vs. Evidence: From the Perspective of An Investigative Firm

DC PAGE

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Intelligence vs. Evidence: From the Perspective of An Investigative Firm

DC PAGE

In this article, DC Page of V2 Global analyses the important question of the distinction between intelligence and evidence, with particular reference to practical considerations in the investigative setting.

As an investigative firm, it is necessary to always explain to clients our investigative methodology not only to manage expectations and to be cost effective, but also to provide a roadmap on how to best utilize the results of the investigation. One of the concepts that often gets discussed with clients are the differences between *intelligence and evidence* and the benefits or limitations of each.

Evidence is a body of facts or information that can be used in a court of law to prove whether a fact has happened with a certain degree of probability. It has the power to validate any intelligence that may be gathered within an investigation. In a U.S. or UK criminal case, the degree of probability would be "*high beyond the reasonable doubt proof"* or "*clear and convincing evidence"*. While in a civil case the degree of probability would be 50% more probable than not (*preponderance of the evidence* type of proof).

Intelligence is information, generally confidential, gathered and analyzed during the course of an investigation around the subject matter. An advantage when gaining intelligence is utilizing trustworthy sources familiar with the content. For it to be valuable, it must be relevant and reliable. The goal is to acquire as much reliable information as possible on the subject matter to advance and further the investigation and/or to negotiate with a third party pre or post action. Intelligence

does not need to be actionable but mainly inferential based on logic and reasoning; it is part of an analytical process that gives a perspective on the subject matter.

One *difference between intelligence and evidence* is that evidence must generally be disclosed to the accused or opponent in a litigation, while intelligence does not necessarily need to be unless it will be used as leverage during settlement negotiations. Another difference is that evidence would need to be admissible in court (which would depend on the jurisdiction, type of case and the nature and scope of the evidence itself). Although intelligence may or may not become evidence, it is important that all intelligence be gathered legally within the legislative and procedural parameters of the applicable jurisdiction.

At first glance, someone may infer that evidence is more important than intelligence and, as a result, the main objective of an investigation should be to gather evidence, not intelligence. That is not necessarily true. Intelligence will provide an assessment on the costs and time necessary to proceed with a legal action and, most importantly, on the probability of success. Intelligence will also provide clues or leads on how to best manage, conduct and plan the investigation efficiently and some of the intelligence may eventually become court-admissible evidence and/or a powerful tool during settlement negotiations.

In gathering and *converting intelligence* into evidence, it is important to understand the legal framework in all applicable jurisdictions involving the subject matter. Close attention should be paid to privacy and secrecy, asset recovery, seizure laws, the judicial framework and the conflicts of laws that may have to be overcome in multi-jurisdictional cases.

Instances when intelligence may well be converted to evidence can include using practices such as open-source research, discovery, and interviews. That is why it is imperative that investigators are partnered with an experienced and reputable counsel. Other investigative techniques that are helpful when converting intelligence into evidence include surveillance, garbology, social media, and deep cyber research.

Evidence is more difficult to collect than intelligence, but evidence is necessary to succeed in a court of law. That does not mean, however, that intelligence is less valuable. There would be no evidence without intelligence.

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KYC for Investigators in Polarized Times – Your Client's Client's Client

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KYC For Investigators in Polarized Times – Your Client's Client's Client

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Abstract

In this article, Craig Heschuk of GreyList Trace and Calvin Chrustie of the Critical Risk Team consider KYC for investigators in an environment where the identity and motives of the ultimate client may be obfuscated. They review the evolving risk environment and highlight some recent cases in this area. In doing so, they provide insights, recommendations and suggestions for client KYC checklists.

Introduction

It's a story as old as the investigation business itself: the client that hires the investigator turns out to have ulterior motives and is working for an undisclosed third party. Film noir, from The Maltese Falcon to Chinatown, has played on the subject to create not only superb dramatic and ethical tension – but also exquisite, duplicitous romantic tension with the arrival of a mysterious femme fatale. The deception is predictable from the first client interview. It won't end well for the investigator, client, or both – but it is cinematic magic.

Reputable investigators, due diligence and intelligence advisors and lawyers know the landscape. In the real world, with the increasing nefarious influences of geopolitics and threats of foreign state actors, it may not be as melodramatic, but

the risk is real and the stakes are high. Professionals know that they need to do adequate due diligence on the real nature of the matter they are being asked to investigate. The risks include breach of professional ethical obligations, potential civil liability, criminal exposure and becoming unwittingly engaged in national security threats. Now this risk environment is becoming even more acute. The manipulation of investigators by organized crime and hostile foreign state actors is bringing heightened attention to this otherwise niche due diligence space.

The Emerging Threat Landscape

In the last several years the world we live in has become more polarized and adversarial. Perhaps in the past we had the luxury of believing that criminal infiltration of society writ large is a problem for "other countries". However, a new reality has arrived where the illicit activities of nefarious state actors and their transnational organized crime networks are cascading into our communities. These influence campaigns in the business, legal and political communities are becoming well-known – but manipulation strategies are also being exercised covertly via risk management firms, private investigators, business intelligence agencies and security companies.

Public institutions that have been built up to protect us are now being leveraged by foreign states and transnational crime groups in a sophisticated and strategic manner to undermine the very society that depends on them. This phenomenon as it relates to the public sphere is prominent in the news today.[1] But the application of such strategies is more wide-reaching than just at the "macro" government and corporate levels. Foreign influence operations, illicit intelligence operations and 'hit' and 'kidnap' squads are surfacing more frequently in the domain of the private sector.

China, Russia, Iran, and others have all been identified operating in this new space.[2] Headlines across the world in 2022-23 concerning China's use of "Police" offices operating in western democracies have called attention to the alarming extent to which some foreign states will interfere in other countries.[3] Several years ago, Huawei was embroiled in an international fraud, sanctions evasion and national security scandal that included transfer of technology to Iran. Huawei's command and control is now widely understood to flow directly from the PRC government. Over a several year period, Huawei contracted multiple law firms who

[1] See: https://www.nbcnews.com/politics/national-security/garland-hold-news-conference-significant-national-security-cases-rcna53702
And https://www.cbc.ca/news/politics/foreign-interference-csis-china-allegations-1.6783031
[2] See: https://www.ctvnews.ca/politics/cybersecurity-agency-calls-out-four-countries-as-the-greatest-strategic-threats-to-canada-1.5194491?cache=yes
[3] See: https://www.nytimes.com/2023/04/17/nyregion/fbi-chinese-police-outpost-nyc.html

were in partnership with research, security, investigative and risk firms. During this time, state-backed hackers and espionage threat actors had physical and cyber access to the law firms' systems. The "clean up" exercise is enormous and fraught with potential legacy infiltration risk given the sophistication of the hacking. All this growing out of an ostensible case of "litigation support", due diligence and private sector investigations.

For the private sector, these cases are more than just cautionary tales. They are existential threats and they mean that a compliance regime must include efforts to understand a new client's ultimate client. The damage of misunderstanding the real reason work is being contracted can extend to criminal exposure. The consequences of not knowing the "who" as both the client and the subject of interest have made international headlines attracting the attention of the global law enforcement, intelligence and legal community.

Recent Cases In The Press

Operation Fox Hunt is a well-known and ongoing example. Michael McMahon, a former NYPD sergeant turned private investigator undertook surveillance operations of a Chinese national on behalf of a client. Mr McMahon insists he had no knowledge that the ultimate client was the Chinese government, and they were working to coerce the Chinese citizen to return to the PRC. But he has been charged by the FBI with acting as an illegal agent for the Chinese government.[4]

In 2021, we saw a high-profile case of Iranian intelligence agencies hiring private investigators to gather information and conduct research for a kidnapping plot to target Americans, Canadians, and British citizens. Iranian intelligence operatives were arrested, and the complicit supporting cast of private security and investigators suffered the consequences of potentially having failed to adequately follow a "know your client" process. As Lisa Monaco, the Deputy Attorney General said in the context of this case, the US has increasingly seen "the blending of national security and criminal threats, as rogue nations and criminal organizations make common cause and share capabilities".[5]

In early 2023, the arrest of a former high ranking FBI agent hired by the Russians to "to investigate and gather intelligence" on behalf of a Russian oligarch grabbed headlines – a depressing case where an FBI agent was acting for the other side just as nations seek to bring Russia's criminal business elite to account.[6]

[4] See: https://www.nytimes.com/2022/11/13/nyregion/china-iran-private-detectives.html
[5] See: https://www.nytimes.com/2023/01/27/us/politics/masih-alinejad-doj-assassination-plot.html
[6] See: https://www.axios.com/2023/01/23/doj-mcgonigal-sanctions-oligarch-deripaska

These are several recent examples making headlines and catching the attention of governments regarding the growing concern of foreign threat actors operating within western democratic borders. The existence of foreign hostile actors from Russia, China, and Iran are not new. What is new is the escalating of use of violence and leveraging the western democratic private sector capabilities to carry out their nefarious national security mandate that includes, kidnappings, murder, extortions.[7]

Recommendations for Your Client KYC Checklist/Risk Assessment

With the above discussion in mind, the following are some recommendations based on best practices and drawn from our professional experience:

1. Secure basic information such as business address and nature of business activities etc (including government ID if there is a suspicion about the true identity or nationality of the client), seek references from professional associates, consider employment verification.

2. Obtain a statement of the legitimate interest that the client is pursuing in requesting the investigation.

3. Consider geopolitical indicators in the Risk Assessment - ie potential connectivity to high risk networks or state actors particularly China, Russia, Iran and North Korea.

4. If you see or suspect geopolitical risk indicators - consider securing advisory services that are versed in these more 'acute' risks and have experienced researchers in the area of national security.

5. Always use open source intelligence ('OSINT') and in very large or suspicious cases leverage tools that assist and support OSINT including "big data" and AI tools. Note: Absence of or minimal social media and internet presence could be a flag - this includes a "recent-only" presence.

6. Look out for indicators such as a client starting with a very small matter and then expanding quickly to larger and more expensive assignments or clients that seem to have surprisingly large budgets.

[7] See footnotes 3 and 4. See also the case of Jamal Khashoggi: https://www.bbc.com/news/world-europe-45812399

7. Once a relationship is established, continue checking and assessing if there were high risk indicators and / or suspicious flags.

8. Read Malcolm Gladwell's "Talking To Strangers", an entertaining and compelling examination of how we have a pre-disposition to believing the people we interact with – a "default to truth" as Gladwell puts it. Even the best security practitioners are prone to being deceived – even when, in hindsight, the warning lights were flashing. Gladwell talks at length about Ana Montes, the "Queen of Cuba", one of the most damaging spies in U.S. history. It was not brilliant tradecraft that allowed her to work undetected for the Cuban government for decades. The reason she thrived as a mole at the Defence Intelligence Agency was that her colleagues liked her and unconsciously turned a blind eye to the tell-tale indications of deceit.

Conclusion

The malign actions of foreign state actors may be focussed on pursuing a discrete case against an individual or they may be part of a strategic effort to fundamentally damage another society. In either case, such covert attacks corrupt our entire society as the system and networks we rely upon become compromised as a result of being used in conspiracies to harm others. The methods employed range from exposing IT systems to top-tier hackers; allowing physical access to corporate board rooms which can be compromised by electrical devices; recruiting insider threats through honeypots and financial incentives; etc. Investigators, attorneys and other professional advisors can become an unwitting pawn in these efforts. The onus is on us to be aware that our firms are highly likely to be targeted and potentially compromised. The ramifications of complacency in knowing who your client really is are potentially severe.

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Unpacking the Complexities of Third-Party Liability Claims for Aiding and Abetting Fraud

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Unpacking the Complexities of Third-Party Liability Claims for Aiding and Abetting Fraud

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Abstract

Third-party claims are an increasingly important tool in the fight against fraud and corruption. When it comes to recovering assets that have been fraudulently taken, it is essential that all potential parties who may have assisted in the wrongdoing be held accountable. This article will unpack the complexities of third-party liability claims for aiding and abetting fraud and outline the legal framework for such claims.

What is a Third-Party Liability Claim?

In the context of asset recovery, third-party liability claims are civil claims brought against individuals or entities who have facilitated the wrongdoing of the primary defendant. Such claims are most commonly made against banks, lawyers and other intermediaries who have knowingly or negligently acted to facilitate a fraud or corruption and can include *Quincecare* claims, aiding and abetting fraud, aiding and abetting breach of fiduciary duty, etc. In some cases, the person or entity accused may not have directly benefited from the wrongdoing but may have known or ought to have known about it and failed to act.

The purpose of third-party liability claims is to ensure that anyone who has facilitated the fraud or corruption is held accountable and to ensure that victims of fraud and corruption can seek full restitution for their losses. It is also an important tool for deterring future wrongdoing from both fraudsters and their enablers and encouraging good corporate governance.

Aiding and Abetting Fraud

Aiding and abetting fraud is a form of intentional misconduct in which one person assists another to commit a fraudulent act. This type of conduct is often referred to as "assisting" or "associate" liability, and it is an offence that could lead to both civil liabilities and criminal sanctions depending on the jurisdiction.[1] Aiding and abetting fraud is a serious offence and can result in significant penalties, including imprisonment and fines.[2]

Impact of Third-Party Liability on Asset Recovery

Third-party liability claims are an important tool for victims of fraud and corruption seeking to recover stolen assets. While criminal sanctions can be an effective deterrent for fraud and corruption, civil asset recovery is often the only way for victims to recover their losses.

Additionally, third-party liability claims allow victims to seek restitution from the parties who facilitated the primary defendant's fraud or corruption. This can include banks, lawyers, and other intermediaries who have knowingly or negligently acted to enable the wrongdoing. By targeting these enablers and facilitators, claimants expand the universe of potential recovery strands and improve the chances of restitution.

The Legal Framework for Third-Party Liability

The legal framework for third-party liability claims is based on common law principles. For an aiding and abetting fraud claim, a claimant needs to prove: (a)

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[1] See 18 U.S.C. § 2. To uphold a conviction for aiding and abetting under 18 U.S.C. § 2, the Government must prove that the defendant associated with a criminal venture, purposefully participated in the criminal activity, and sought by his actions to make the venture successful. *United States v. Polk,* 56 F.3d 613, 620 (5th Cir.1995) (citations omitted). A defendant associates with the criminal venture if he shares in the criminal intent of the principal. *United States v. Jaramillo,* 42 F.3d 920, 923 (5th Cir.), *cert. denied,* 514 U.S. 1134, 115 S.Ct. 2014, 131 L.Ed.2d 1013 (1995). A defendant participates in the criminal activity if he has acted in some affirmative manner designed to aid the venture. *Id.*

[2] United States Attorney's Office. (February 16, 2023). *Hopkins County Company Guilty of Aiding and Abetting Document Fraud* [Press Release]. ("[Defendants] has agreed to pay forfeiture of $5 million" and "face up to six months in federal prison at sentencing"). https://www.justice.gov/usao-edtx/pr/hopkins-county-company-guilty-aiding-and-abetting-document-fraud.

the existence of an underlying fraud; (b) the third party had knowledge of the fraud (c) and the third party provided substantial assistance to facilitate the fraud.[3] This can be difficult to prove, as the third party may not have been directly involved in the underlying wrongdoing.

For example, to plead knowledge in an aiding and abetting fraud claim, it has been held the claimant must allege sufficient facts to support a "strong inference of fraudulent intent" by either (a) showing a motive for participating in the fraud and an opportunity to do so or (b) identifying circumstances indicative of conscious behavior.[4]

In bank fraud cases, courts have recognized "atypical banking procedures" as a basis to infer knowledge that the bank was aiding in the fraud.[5] And the United States Court of Appeals for the Second Circuit has stated that "proof of a defendant's knowledge or intent will often be inferential."[6] Keep in mind though that allegations that a bank merely suspected fraudulent activity does not satisfy this requirement.[7]

Given the high standard of showing actual knowledge, in many jurisdictions the law requires claimants to prove that the third party acted in a manner that was "unreasonable" or "reckless" to be held liable.[8] This means the third party must have acted in a way that was objectively unreasonable or reckless considering the known circumstances. Reckless disregard is not just suspicion, but rather behavior that "highly unreasonable and constituting an extreme departure from standards of ordinary care."[9]

Additionally, the plaintiff must show sufficient evidence demonstrating that the defendant substantially assisted the underlying fraud. Commentary to the RESTATEMENT (SECOND) OF THE LAW OF TORTS § 876 identifies several relevant factors for evaluating whether encouragement or assistance was "substantial" including: (1) the nature of the act encouraged; (2) the amount and kind of assistance given; (3) the defendant's relation to the tortious actor; and (4) the defendant's state of mind.[10]

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[3] *Wight v. Bankamerica Corp.,* 219 F.3d 79, 91 (2d Cir.2000) (citing *Fidelity Funding of Calif., Inc. v. Reinhold,* 79 F.Supp.2d 110, 122 (E.D.N.Y. 1997)).
[4] *In re AHT Corp*., 292 B.R. 734, 746 (S.D.N.Y. 2003), *aff 'd*, 123 Fed. Appx. 17 (2d Cir. 2005).
[5] *Neilson v. Union Bank of California, N.A.*, 290 F. Supp. 2d 1101, 1120-1121 (C.D. Cal. 2003) (citing *Aetna Cas. & Sur. Co. v. Leahey Constr. Co.*, 219 F.3d 519, 536 (6th Cir. 2000)).
[6] *Rolf v. Blyth, Eastman & Dillon & Co.*, 570 F.2d 38 (2d Cir. 1978), *amended*, 1978 WL 4098 (2d Cir. May 22, 1978), *cert. denied*, 439 U.S. 1039 (1978).
[7] *Dubai Islamic Bank v. Citibank N.A.*, 256 F. Supp.2d 158, 166 (S.D.N.Y. 2003).
[8] *See Tew v. Chase Manhattan Bank, N.A.*, 728 F. Supp. 1551 (S.D. Fla. 1990), *amended on reconsideration*, 741 F. Supp. 220 (S.D. Fla. 1990).
[9] *Levine v. Diamanthusel, Inc.*, 950 F.2d 1478, 1484 (9th Cir.1991).
[10] RESTATEMENT (SECOND) OF THE LAW OF TORTS § 876 cmt. d (1979).

There are similar causes of action – *e.g.*, aiding and abetting fiduciary duty or a *Quincecare* claim – that can also be alleged depending on the facts and the jurisdiction.

Challenges in Bringing Third-Party Liability Claims

Bringing a successful third-party liability claim can be difficult. While the burden of proof in civil cases is by a preponderance of the evidence (*i.e.*, there is a greater than 50% chance that the claim is true), the claimants must show that the third party had knowledge of the fraud or corruption and acted to facilitate it. This can be difficult to prove, as the third party may not have been directly involved in the wrongdoing.

Additionally, there is the *in pari delicto* doctrine and the Second Circuit's *Wagoner Rule* to consider. A common fact pattern for third-party claims, especially against financial institutions, involves a bankrupt corporation that formerly operated as a fraudulent enterprise. After the fraudsters have left the bankrupt company, the bankruptcy trustee commonly uncovers that third parties enabled the fraud.
In pari delicto is a Latin phrase which means "in equal fault" and is a doctrine that states that there is a bar to a claimant recovery of damages for a wrong in which the plaintiff participated.[11] If the claimant is at least equally at fault as the defendant in the wrongdoing, the court will not involve itself in resolving one side's claim over the other. Courts are understandably reluctant to award relief to plaintiffs who have "unclean hands," and this doctrine serves as an equitable defense.

In the Second Circuit, a bankruptcy trustee standing in the shoes of a debtor corporation lacks standing to sue third parties for damages "when a bankrupt corporation has joined with [the] third party in defrauding its creditors."[12]

However, *in pari delicto* and the *Wagoner Rule* are not a sure-fire defense for enablers of fraud. In a bankruptcy setting, the doctrine applies primarily to a bankruptcy trustee as a representative of the "debtor" under the U.S. bankruptcy code, and not to the trustee in its status as a representative of the "creditor."[13] As

[11] Merriam-Webster. (n.d.). in pari delicto. In *Merriam-Webster.com dictionary*. Retrieved February 1, 2023, from https://www.merriam-webster.com/legal/in%20pari%20delicto
[12] *Shearson Lehman Hutton, Inc. v. Wagoner*, 944 F.2d 114, 118 (2d Cir. 1991); see *Wight v. BankAmerica Corp.*, 219 F.3d 79, 87 (2d Cir. 2000)("[M]anagement's misconduct is imputed to the corporation, and because a trustee stands in the shoes of the corporation, the *Wagoner* rule bars a trustee from suing to recover for a wrong that he himself essentially took part in.").
[13] *See* 11 U.S.C § 544(a)(1).

such, if it can be effectively argued that the claim stems from the creditor's rights as opposed to the debtor's, then this hurdle can be overcome.[14]

The *Wagoner Rule* also has an additional narrow but important exception. It does not bar a bankruptcy trustee's claim against third parties where the bankrupt corporation's management "acted entirely in his own interests and adversely to the interests of the corporation."[15] The exception is narrow: management "must have totally abandoned" the corporation's interests[16] or engaged in "outright theft or looting or embezzlement . . . i.e., where the fraud is committed against a corporation rather than on its behalf."[17] And the exception does not apply if a corporation "receives any benefit from the fraud . . . even if the fraud ultimately causes the corporation to suffer harm in the long term, and even where the insider intended to benefit himself at the corporation's expense."[18]

The final challenge with third-party liability claims is that they can be expensive and time-consuming. While not unique to third-party liability claims, defendants may have access to a larger war chest and claimants may not be able to finance the claim themselves and will need to seek litigation funding.

Strategies for Bringing Third-Party Liability Claims

In order to bring a successful third-party liability claim, it is important to have a clear strategy in place. Claimants should start by gathering evidence, such as documents and other materials that demonstrate the third party's knowledge of the fraud or corruption and their role in facilitating it.

Claimants should also seek legal advice early. Third-party liability claims are complex and the issues presented can be tricky and entangled. Claimants and their counsel should be aware of the legal framework for third-party liability claims to properly consider whether their claim is likely to be successful. This will help claimants to make an informed decision about whether to proceed with the claim and how best to pursue it.

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[14] *See Wagoner*, 944 F.2d at 120 ("[a] claim against a third party for defrauding a corporation with the cooperation of management, accrues to creditors, not to the guilty corporation"); *see also In re Bennett Funding Grp., Inc.*, 336 F.3d 94, 102 (2d Cir. 2003) ("In short, we hold that the defrauded investors and not the bankruptcy trustee are entitled to pursue the claims arising from the fraud.").
[15] *Wight*, 219 F.3d at 86.
[16] *In re CBI Holding Co.*, 529 F.3d 432, 449 (2d Cir. 2008) (citing *Center v. Hampton Affiliates, Inc.*, 66 N.Y.2d 782, 784 (1985)).
[17] *Kirschner v. KPMG LLP*, 15 N.Y.3d 446, 466-67 (2010).
[18] *Cobalt Multifamily Inv'rs I, LLC v. Shapiro*, 857 F. Supp. 2d 419, 428 (Bankr. S.D.N.Y. 2012) (citing *Kirschner*, 15 N.Y. at 468-69).

Finally, claimants should consider the funding options available. Properly evaluating a third-party claim and – if feasible – the ensuing litigation, can be expensive and funding can be an effective way of financing a third-party liability claim, as it allows claimants to access the funds needed without having to pay the full cost upfront.

Conclusion

Third-party liability claims are an important tool in the fight against fraud and corruption. By holding those who facilitate such wrongdoing accountable, victims of fraud and corruption can seek full restitution for their losses. This article has unpacked the complexities of third-party liability claims for aiding and abetting fraud and outlined the legal framework for such claims. It has also outlined the challenges in bringing such claims and strategies for pursuing them. By understanding the legal framework and the strategies for bringing such claims, claimants can make an informed decision about proceeding with a third-party liability claim.

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Crypto Regulation in Offshore Financial Centres – How Much is Enough?

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Crypto Regulation in Offshore Financial Centers – How Much is Enough?

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Digital assets, particularly cryptocurrencies, have rapidly transformed the financial landscape. They have the potential to revolutionize how we conduct financial transactions, but at what cost to the unsuspecting, or unsophisticated, consumer and investor?

The regulation of these assets remains a complex and challenging issue, particularly in jurisdictions such as the Cayman Islands, the British Virgin Islands, and other island nations in the Caribbean region. In recent years, Offshore Financial Centers ('OFC's') have, with varying degrees of success, invested heavily in the battle to change a common perception that OFCs are the natural habitat for tax cheats, kleptocrats, fraudsters, and the generally corrupt.

OFCs that can boast a clean bill of health on the international stage are able to attract new service providers and benefit from the investment in local resources that follows. Finding the right mix of innovation, incentive, and regulation is a delicate equilibrium but one that any jurisdiction must find if it is to avoid reputational disaster that comes with international financial scandals. Scandals like those that have tarnished reputations of Caribbean nations, arguably unfairly and on a disproportionate scale, than those of more so-called developed countries, leaving many jurisdictions gun-shy or paralyzed when it comes to supervising and enforcing the industry.

While offshore jurisdictions are often known for favorable regulatory environments and economic stability, these same qualities have made them an attractive location for digital asset companies, highlighting the need for strong regulations to protect consumers and investors, and prevent financial crimes such as money laundering. Digital asset regulation in offshore jurisdictions is still in its infancy, with significant challenges that must be addressed.

One of the most significant issues is the lack of clear laws and regulations. While some territories have implemented strict regulations for digital assets, some jurisdictions are still striving to establish clear guidelines for the industry, creating uncertainty for companies operating in the digital asset space and making it challenging for investors to understand and evaluate the associated risks.

The pace of innovation and market volatility that are distinguishing characteristics of the digital asset sector amplify the challenges faced by regulators worldwide. These can have a more significant impact on smaller jurisdictions, where attracting and maintaining resources and technical expertise can be demanding.

Even in some jurisdictions where regulation has been implemented, an absence of consistent oversight and enforcement enables bad actors to take advantage of those gaps and makes it easier to avoid or bypass those safety barriers. Consequently, the digital asset industry experienced a wave of prominent and far-reaching collapses during the "crypto winter" of 2023.

Occasionally, and more by good luck than good management, the reluctance or inability for a regulator to approve an application pushes the applicant elsewhere, sparing that jurisdiction from the spotlight and furor of the ensuing meltdown. Sadly, this “do-less” approach keeps out the good as well as the bad, to the ultimate detriment of that country.

So, where is the balance between the “head in the sand” approach and a regulatory regime that is so tight that if a company is allowed through the gates, their operation and innovation is so restricted as to be prohibitive? The answer, clearly, is somewhere in between and must include a comprehensive approach to digital asset regulation.

While many offshore jurisdictions have established regulations for specific areas of the digital assets industry, such as exchanges or initial coin offerings, a more comprehensive approach is needed to effectively regulate the industry as a whole.

The digital asset industry is multifaceted and is constantly evolving, encompassing various aspects such as tokenization, fintech, blockchain, and so on. While

regulation of specific areas is a step in the right direction, a more comprehensive framework that ties into anti-money laundering, cybersecurity, market manipulation, custody of digital assets, and much more is needed. A comprehensive approach will create a more stable, secure, and transparent environment for the industry. This will help to ensure that regulation does not stifle innovation.

To do this, governments should focus on regulating the activities, not the assets. This means that governments should focus on regulating the people and businesses that are involved in the digital asset ecosystem, rather than regulating the digital assets themselves.

Regulators must consider where their highest duty lies. If that duty is ultimately to protect investors and consumers, then a risk-based approach to regulation is apt. This means the focus of their regulatory efforts must be on the activities that pose the greatest risk to consumers and investors. For example, governments should focus on public facing service providers like exchanges and other businesses that are involved in the trading of digital assets.

Achieving these aims requires collaboration between regulators and industry stakeholders - a vital component of effective digital asset regulation. Ideally, government-to-government collaboration to coordinate regulatory efforts across borders would help to reduce the drive for businesses or investors to seek out the least regulated jurisdiction. In practice, this kind of international cooperation is complicated and unlikely to fully take root, national interests will never fully align, however, the greater the commonality between regulations across the globe, the more obvious it becomes when spotting jurisdictions offering a weaker regime.

Advances have been made in allowing entrants to set up under a regulatory "sandbox", a safe, controlled environment where projects and businesses can function while regulatory frameworks are developed.

Regulators can use the sandbox to observe and assess potential risks associated with participating companies and the broader industry, striking a balance between consumer protection, and fostering innovation. This approach helps oversight bodies to develop regulations and share information and best practices to ensure that regulations remain relevant and effective.

Similarly, regulators and the private sector can collaborate in different ways to assist under-resourced governments in enhancing the rigor of existing laws and regulations that affect the digital asset market. Proactively, this can be as simple

as sharing expertise, industry knowledge, and best practices around digital asset regulation via training programs, workshops, and seminars.

In a more hands-on way, private sector companies can offer technical assistance to governments in the form of tools, technologies, and resources that can bolster their capabilities in monitoring and enforcing digital asset regulations. This can include software solutions, data analytics tools, and cybersecurity expertise.

Reactively, public-private sector collaboration on investigations is not new. With the rapid evolution and expansion of technology and structures being used in the sector, it will often be the private sector that is exposed to these before a regulator in a smaller territory.

Regulators and private sector firms can collaborate on joint investigations to identify and address potential violations of digital asset regulations. By pooling resources and expertise, they can work together to investigate and prosecute cases of non-compliance, or more serious and damaging misconduct.
The regulation of digital assets is a complex and challenging issue. There is no one-size-fits-all approach, and each jurisdiction will need to develop its own regulatory framework in light of its own specific circumstances. However, it is clear that offshore jurisdictions are committed to regulating digital assets in a way that promotes economic growth and innovation while also protecting consumers and investors.

Ultimately, offshore jurisdictions must recognize and confront their realities truthfully. They must recognize and address their shortcomings in this area to ensure the effective regulation of the industry, protect investors, and create an enabling environment for innovation and growth. As the digital asset industry continues to evolve, it is essential for regulators to remain proactive and adapt to these changes to ensure the continued success and safety of the industry.

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Another Corporate "Failure to Prevent" Offence: Fraud

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Another Corporate "Failure to Prevent" Offence: Fraud

DR DOMINIC THOMAS-JAMES

Abstract

In this article, Dr Dominic Thomas-James, Consultant and Director of Publications at ICC FraudNet, Barrister, Goldsmith Chambers, and Research Associate at Fitzwilliam College, Cambridge considers proposed legislation currently going through the UK Parliament that seeks to create a corporate failure to prevent fraud offence. The article considers the effect of this legislation, the extent to which it is suitable in the area of fraud, and details some questions that remain unresolved.

Overview of the legislation

Within the increasingly complex economic crime landscape, so-called "failure to prevent" offences have become a familiar standard. A corporate failure to prevent fraud offence is currently making its way through the UK Parliament. The Economic Crime and Corporate Transparency Bill[1] takes aim at large businesses or organisations and whether their systems to prevent fraud on the part of their people, are adequate.

We are, of course, familiar with this type of "failure to prevent" offence in the areas of bribery and tax evasion – with section 7 of the Bribery Act 2010 providing an offence of failure of corporate organisations to prevent bribery, and the failure to prevent the facilitation of tax evasion per part 30 of the Criminal Finances Act

[1] See: UK Parliament, Parliamentary Bills, 'Economic Crime and Corporate Transparency Bill', available at: https://bills.parliament.uk/bills/3339 (accessed 22 May 2023).

2017. There have been those campaigners making calls to transpose this model into a broader failure to prevent economic crime offence.[2]

The mechanics of the proposed law appear quite straightforward in that it takes aim at large corporate organisations, partnerships, non-profits and charities under restrictive criteria. Entities must fit two of three criteria, namely, employing over 250 people; making more than £36 million turnover per year; or holding assets of more than £18 million. The legislation targets an organisation that did not have reasonable measures in place to prevent fraud on the part of an employee or agent, and that may have benefited from the fraud. The fraud itself and related offences include offences under the Fraud Act – namely, section 2, 3 and 4: fraud by false representation; fraud by failing to disclose information; and fraud by abuse of position. It also includes a section 9 fraud offence, namely participating in a fraudulent business. It further includes Theft Act 1968 offences, namely the section 11 offence of obtaining services dishonestly, the section 17 offence of false accounting, and the section 19 offence of the making of false statements by company directors. It includes an offence under the Companies Act 2006, namely the section 993 offence of fraudulent trading, and finally it includes the common law offence of cheating the public revenue (*R v Hudson* [1956] 2 QB 252).

Companies and organisations to which the legislation applies will need to demonstrate that they have reasonable fraud prevention procedures in place. Indeed, companies may have a defence if they can demonstrate that it had reasonable measures in place – as per the defences we see relating to other corporate "failure to prevent" offences. What is to be considered as "reasonable procedures" is yet to be defined and Government guidance on this is awaiting publication. For companies and organisations unable to demonstrate the same; on conviction liability is an unlimited fine. Importantly, prosecutors will not need to prove that the company or organisations' senior figures knew about the fraud, or directed it.

Impact

This offence, much like those others in the areas of bribery and tax evasion facilitation, appears to be aimed at general deterrence and bringing the "fraud" discussion firmly within the corporate governance environment. As such, and for the area of fraud, it brings organisations' role as potential "facilitators" rather than "victims" in this regard, into the compliance framework.

Of course, in English criminal law, for fraud to be proven, dishonesty needs to be shown (*Ivey v Genting Casinos* [2018] AC 391). In the criminal setting, this is to a high standard and the prosecution must prove that the defendant committed fraud beyond reasonable doubt – in other words, the jury must be satisfied so that they are sure. This can be contrasted with the civil setting, whereby the claimant has

[2] See, for example: Baroness Bowles of Berkhamsted's amendment to the Economic Crime and Corporate Transparency Bill, Amendment number 91, available at: https://bills.parliament.uk/bills/3339/stages/17398/amendments/94608 (accessed 22 May 2023).

the burden of proving the same on the balance of probabilities – in other words, that it is more likely than not that the defendant committed the fraud.

For offences under sections 2, 3 and 4 of the Fraud Act 2006 (i.e. fraud by false representation, failing to disclose information, or abuse of position), it must be proven that the defendant's conduct was dishonest, and that it was their intention to make a gain, or cause a loss or the risk of loss to another. The *actus reus* requirement for fraud in this regard is less than for theft. It need not be shown that a gain or loss actually occurred. The maximum prison sentence for a criminal fraud conviction under these provisions is 10 years.

Dishonest intent is the underlying feature of such fraud offences in the criminal context. In the case of fraud by false representation, it must be shown that the defendant made a false representation dishonestly and knowing that the representation was, or might be, untrue or misleading. In the case of fraud by failing to disclose information, the defendant must have failed to disclose information when they were under a legal duty to, and dishonestly intended, by failing to disclose that information, to make a gain or cause a loss or risk thereof.

Yet, for a corporate to commit the new "failure to prevent" fraud offence, prosecutors do not need to show that there was a "directing mind". Prosecutors do not need to prove that officials orchestrated the fraud, conspired, or knew about it – which may have ended up benefiting the organisation.

The proposed legislation clearly focuses on systems – or the lack thereof. What the legislation achieves with not having this requirement of proving knowledge on the part of officials, is to eradicate the possibility or risk of wilful blindness on the part of the organisation or its officers. In other words, formerly, liability would have rested on the part of – say – the rogue employee. Now, it will not be sufficient for companies to rely on rogue elements or one-offs in the absence of reasonable fraud prevention procedures being fully implemented and operational.

Putting the focus on the organisation, even without the requirement of proving knowledge or a directing mind, appears to have at its core general deterrence. It also creates a non-optional awareness-raising function within the organisation's operations and, therefore, inevitably ought to have an effect on culture and corporate governance. Given that fraud and its methods are ever-evolving, particularly with the use of technology and systems, awareness and understandings of fraud require constant monitoring. The legislation may well serve this aim.

While standardisation will inevitably be required in terms of guidance on what are considered to be "reasonable procedures"; in practice much will depend on particular risk-profiles of organisations and the type of measures they will aver are adequate. Indeed, even the UK Government's Factsheet acknowledges that for some entities it may be reasonable to have no fraud prevention procedures when it

has an extremely low risk of fraud.[3] Of course, guidance will have to take account of fraud's complexity. The fact remains that fraud is the crime to which we are most likely to fall victim, and represents some 41% of all crime against individuals in England and Wales.[4] Understanding fraud remains an essential, but difficult, endeavour particularly for companies strategizing on measures to prevent it. If we truly understood the risks of and from fraud, the forms that fraud takes, the environments and circumstances fraudsters pray in, and, importantly, fraudsters' motivations, then one would think that the above figure would be somewhat less.

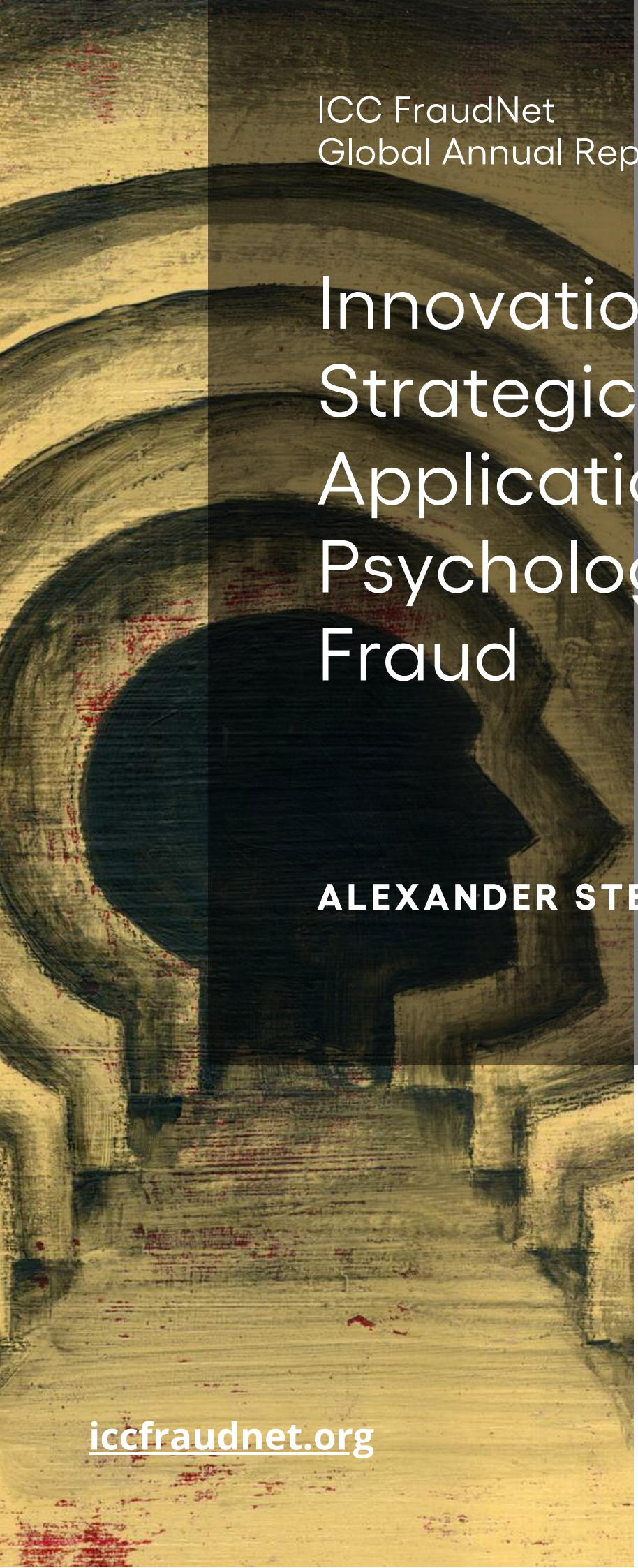
The elephant in the room arguably is the type of company or organisation concerned. With more and more "failure to prevent" offences, there is considerably more attention on issues relating to corporate governance, responsibility and compliance than ever before. For larger organisations, the sort caught by this legislation, it is not unreasonable to assume that the majority will put considerable effort and resources into both ascertaining what are "reasonable" fraud prevention measures in their case, and implementing the same to comply with this legislation. Even though "reasonable procedures" is still lacking guidance and definition; many such organisations will already have gone through similar processes to comply in areas such as failing to prevent bribery and failing to prevent the facilitation of tax evasion. For these, and now for fraud, many will of course engage specialist compliance personnel and legal representatives to ensure compliance. The proposed legislation targets large organisations – given their risk profile. It does not target smaller organisations – partly due to concerns about proportionality. Therefore, the targets under the legislation are those organisations that are perhaps better resourced to implement and monitor such measures. Surely this, taken with the familiarity of the work required to comply with similar measures already in place, will make the prosecutor's task all the more difficult in proving that procedures were not reasonable.

Concluding thoughts

Robert Peel, in his policing principles, evoked the notion that an effective law enforcement does not have high arrest rates; but rather, its community has low crime rates. It is not unreasonable to assume that most entities to which the legislation applies, will likely retain legal and compliance experts to assist and advise them on devising procedures that will be considered "reasonable" for the prevention of fraud; based on the legislation's guidance and on their particular business, activities and risk profile. With Peel's principle in mind, how will the legislation's effectiveness be measured? It could be argued that it rests on a more nebulous, conceptual basis, rather than high numbers of criminal fines. Bringing fraud awareness-raising more visibly under the corporate governance spotlight ought to serve a deterrent function. Yet, given the likelihood that large entities will comply and implement reasonable measures, as well as the difficulty prosecutors

[3] UK Government Policy Paper: Factsheet: Failure to Prevent Fraud Offence, 11 April 2023, available at: https://www.gov.uk/government/publications/economic-crime-and-corporate-transparency-bill-2022-factsheets/factsheet-failure-to-prevent-fraud-offence (accessed 22 May 2023).
[4] See: UK House of Lords (12 November 2022) "How do we break the fraud chain?", available at: https://ukparliament.shorthandstories.com/breaking-fraud-chain-committee-report/index.html (accessed 22 May 2023).

may therefore have in proving that the measures were "unreasonable"; it remains unclear whether this will translate to prosecutions and convictions – or whether the function of this legislation rests more in the area of awareness-raising and corporate culture, backed up by the threat of a criminal fine and the reputational harm that may ensue for non compliance. Of course, the question remains as to whether this legislation will prevent fraud at a substantive level, or is it is just another exercise in corporate box-ticking, which may yield little by way of measurable results?



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Innovations and Strategic Applications in the Psychology of Fraud

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Innovations and Strategic Applications in the Psychology of Fraud

DR ALEXANDER STEIN

Abstract

Fraud is a crime of relationships. It involves dishonesty, deception, betrayals of trust and abuses of power and is predicated in ubiquitous human propensities to be hoodwinked and manipulated. Despite its centrality, the psychological dimension of fraud and fraudsters has been historically misconstrued and domain relevant expertise underutilised in the ferocious psychological battle to recover victims' losses and bring fraudsters, kleptocrats, and other corrupt actors to justice. In this article, Alexander Stein Ph.D., redresses that by elaborating on the complex psychodynamics at play across the entire psycho-social ecosystem in fraud matters and delineating psychologically sophisticated tools for actionably leveraging psychodynamic intelligence to assist fraud litigators and allied asset recovery professionals.

Introduction

"Fraud is committed by people, not numbers."
— Joseph Wells, Founder and Chairman, Association of Certified Fraud Examiners[1]

[1] Joseph Wells' keynote address, ACFE 25th Annual Global Fraud Conference, San Antonio, Texas, June 2014

The standard definition of fraud is *deceit, trickery, sharp practice, or breach of confidence perpetrated for profit or to gain some unfair or dishonest advantage*. Fraudsters use these methods to induce victims to unwittingly become deprived of dominion over substantial sums of money or other valuable assets.[2]

The ostensible goal in most cases is personal enrichment. To this end, fraudsters continually innovate and creatively adapt to new technologies and environments. They exploit disruptive macro-social events and loopholes in markets and financial instruments, capitalize on inadequate regulatory oversight or reform, and weaponise investor greed and lackadaisical due diligence.

But above all else, fraud is a crime of relationships. It involves dishonesty, deception, betrayals of trust and abuses of power and is predicated in the ubiquitous human propensities to be hoodwinked and manipulated.

In this view, recovering the *fructus sceleris*—the fruit of ill-gotten gains—and pursuing justice on behalf of victims involves more than adroitly navigating judicial procedures and coordinating complex trans-national legal, banking, accounting, and investigative expertise. Contemporary asset recovery cases are, at core, a ferocious psychological battle with corrupt actors who operate under radically disparate moral, ethical, and behavioural codes, dismiss the rule of law, and abide antisocial notions of justice, consequence, and accountability.

That conflict is waged primarily between the fraudster, his affiliates, operational workforce, and knowing co-conspirators and facilitators (as well as many unwitting enablers, including family members), on the one side, and the array of asset recovery professionals—investigators, litigators, prosecutors, litigation funders, and other subject matter experts—on the other.

But an expansive view of the human ecosystem must also include two additional constituencies: the victims and other impacted stakeholders, and the judiciary—triers of fact and law—legislatures, regulators, and policy-making institutions as well as the social and cultural structures that enable them.

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[2] The umbrella rubric "fraud" is used here for brevity's sake and is intended to incorporate by reference its many forms and varieties. Other common frauds include false claims of scientific discovery or intellectual property ownership. While these may result in undeserved gains to the fraudster and unjust losses to the victims, they comprise different classes of fraud which will not be directly taken up here. The dominant focus here is asset recovery in the context of economic fraud. For more detail, see for example, Martin Kenney's useful enumeration of 15 common types of fraud in the chapter titled *Serious Fraud* in *Asset Tracing and Recovery – The FraudNet World Compendium, 1st Edition*, pp. 8-14. For a thorough survey of Ponzi schemes, see Kathy Bazoian Phelps & Hon. Steven Rhodes, *The Ponzi Book: A Legal Resource For Unraveling Ponzi Schemes* (LexisNexis® 2012).

Whatever their functions, these groups are psycho-social systems, each subject to and governed by powerful psycho-social forces and dynamics. In addition, the antagonist and his cohort will inevitably unleash psychological warfare to frustrate, stymie, or nullify the professional campaign directed to bringing them to book.

In short, fraud professionals routinely confront the roiling impact of all manner of unscrupulous behaviour—deception, psychological manipulation, abuses of trust and power—as well as a dizzying array of dense issues involving individual and social psychology, family systems, and organizational dynamics.

In the 5th century BC, Chinese military strategist and philosopher Sun Tzu opined that "the opportunity of defeating the enemy is provided by the enemy himself."[3] This axiom is no less applicable in 21st century fraud cases where sophisticated analyses and actionable intelligence concerning the mind and behaviour of the fraudster and his confederates together with insight into the psychological dynamics of all the constituent human systems open a third dimension on case management, strategy, and prosecution, and provide unique guidance for the litigation and recovery operation.

What follows is an introductory overview of these ideas, briefly updating historical and conventional understandings of the psychology of fraud as a prelude to providing a contemporary and more robust psychodynamic perspective. This is followed by a delineation of the primary applications and methods for leveraging expertise in human psychology, and family, organisational, and social systems in asset recovery work.

Psychology in Jurisprudence and Fraud—The Imperative of Updating Historical Perspectives

Efforts to understand and explain the psychological underpinnings of criminally deviant behaviour have entwined with the development of Western jurisprudence for more than four hundred years. Common law guidelines on criminal liability have, in simplest terms, historically relied on establishing intent, motive, and forethought to explain why people defy prevailing rules of law and codes of normative civil ethics and conduct.

Most English law jurisdictions require establishment of *mens rea*, the guilty mind, as a necessary element of a criminal offence accompanying *actus reus*, the guilty act. Codified by Edward Coke in the 17th century, the notion *actus non facit reum nisi*

[3] "Art of War," Chapter 4

mens sit rea—the act does not make a person guilty unless the mind also be guilty—remains jurisprudentially influential to this day. Another related psycho-legal concept is *Dolus*, which describes an accused person's intention at the time an alleged crime is committed. It has two forms: (i) *Dolus directus* (direct intention), where it is determined that the accused intended a certain act or result; and (ii) *Dolus eventualis* (indirect intention) where the possibility of a particular consequence or circumstance is foreseen but there is a reckless disregard as to whether it ensues or not. Both forms establish that the accused understood that his actions or the consequences of them were wrong. Similarly, establishment of a*nimus nocendi*—criminals' (or organizational decision-makers') *a priori* knowledge of illegality and intent to harm—is a requisite condition to courts' determinations of penalty and liability for constructive dishonesty, knowing assistance, recklessness, negligence, and aiding and abetting breaches of fiduciary duty.

Societies and courts have long relied on consensual acceptance of these concepts. In support of that, psychologists' and psychiatrists' expert opinions are enlisted in cases involving psychiatric issues, requiring extensive knowledge of mental health law, in jury selection, or in presenting relevant psychiatric concepts and diagnostic findings in language that courts can understand and use in instructing juries and rendering sentencing. This includes determining a defendant's mental fitness or capacity relating to criminal intent, mental competency, or statutory thresholds of legal insanity; attesting to a defendant's state of mind and how it affected his ability to author or commit certain acts in concurrence with the alleged criminal wrongdoing; or testifying as to the symptoms and conditions of a crime victim's post-traumatic duress.

Research on the psychology of fraud occupies a distinct category in the studies of criminal types,[4] historically relying, in the main, on psychiatric diagnoses to explain why people commit fraud.

Arguably the most influential schematic understanding has been the Fraud Triangle. Devised by Donald R. Cressey in the 1950's, it established a triumvirate of simultaneous factors needed for an "ordinary" person to commit fraud: opportunity, rationalisation, and pressure (or incentive).

Another popular mid-20th century view examined similarities between classic symptoms of antisocial personality disorders, particularly criminal psychopathy, and the markers of leading economic criminals. While not a formal diagnostic classification in the DSM (Diagnostic & Statistical Manual of Mental Disorders),

[4] Including, inter alia, mass- and serial-killers, sociopaths, sex offenders, terrorists, kidnappers, drug lords, organized crime capos, tyrants, dictators, authoritarians, and malfeasant executives and assorted white-collar offenders.

psychopathy overarchingly refers to APD (anti-social personality disorder), a serious condition characterised by virulently aggressive and disinhibited antisocial behaviour, feckless disregard, diminished empathy, and absence of remorse. The work of several psychiatrists profoundly influenced clinical, diagnostic, and criminological parameters of psychopathy, most prominently Hervey M. Cleckley, an American psychiatrist and pioneer in the field of psychopathy whose 1941 book *The Mask of Sanity* provided the most influential clinical description of psychopathy in the twentieth century, and Robert D. Hare, a Canadian forensic psychologist who developed the Hare Psychopathy Checklist used to assess cases of psychopathy. Building on that earlier work, William and Joan McCord, a husband-and-wife team who specialised in the study of criminal delinquency, co-authored *The Psychopath: an essay on the criminal mind* (1964), a seminal work which became a leading reference to the legal profession. These and other similar works ignited popular imagination and found easy favour with courts and juries, cementing psychopathy as far and away the most widely accepted explanation for fraud.

Other established views emphasised fraudsters as principally motivated by an unquenchable hunger for power, rapacious greed, or unrestrained opportunism. Additional explanations proposed that fraudsters utilise "techniques of neutralisation" which reduce the offender's ability to modulate or abort destructive, amoral, or anti-social impulses to greater degrees than the average person. A related view suggested that fraudsters possess an unusual capacity for rationalisation—a psychological mechanism by which an individual seeks to replace the actual socially, ethically, and emotionally reprehensible motivations for his actions with a more palatable though fictive explanation.

Even the most systematic scientific research has tended to narrowly classify fraudsters as remorseless sociopaths or psychopaths—predatory men devoid of empathy who prey on victims ill-equipped to protect themselves and their assets. Studies such as Edwin H. Sutherland's 1939 "*Principles of Criminology"* which promulgated Differential Association and Differential Reinforcement Theory—the notion that criminal behaviour is learned—are still referenced today. Some studies located the origins of criminally delinquent behaviour in organic (brain) disorders, while others assigned the complex calculus of predispositions and psycho-social factors driving the commission of fraud to a wide range of causes, including low self-esteem, arrogance and egocentricity, a poorly developed code of ethics, emotional instability, a desire to beat the system, and taking pleasure in manipulating others.

Even as a separate matter from the relative plausibility or fractional correctness of any of these formulations, the historically entrenched focus on fraudsters wholly in terms of psychopathology is simplistic. It inadequately explains the salient

characteristics, psychological constituents, and dynamic catalysts of offenders and their criminal schemes. And the conventional view of fraud as an asymmetrical bipolar event between fraudster as dominant figure and victim in a hapless subordinate position—while omitting all other involved parties—is insufficient in the aggregate.

One legacy of these approaches has been to compress fraudsters into a universally accepted taxonomy that purportedly explains all typical characteristics and motivations as a single diagnosable psychopathology. This has detrimentally influenced generations of litigators in crafting prosecution and asset recovery strategies, jurists, and policy-making bodies in determining sentencing guidelines and designing prevention and recidivism reduction programs, and biased journalists, authors, and filmmakers in producing mythologised narratives about fraud and fraudsters now ensconced in culture and the popular mind.

But the most significant adverse consequence in the context of this article is that it provides scant practical value to asset recovery professionals. Recalling the premise that fraud is fundamentally a psychological crime, it follows that expansive, contemporised conceptualisations of the psychological dimensions involved demonstrably enhance developing and pursuing third party liability claims against fraudsters and their knowing assistants and facilitators leading to the recovery of assets wrongfully taken from victims. Working models must move beyond inert post-facto psychiatric diagnoses for single-actor wrong-doing. And professionals in the field can only benefit from access to sophisticated psychodynamic intelligence gathering and analytics to add to the array of established legal and accounting instruments and practices.

What follows redresses these shortcomings on two fronts. One is to introduce a magnified multi-dimensional understanding of the complex psychodynamics at play across the entire human ecosystem of a fraud case. This includes mapping the matrix of people in a dynamically interacting constellation of relationships—a field populated by the primary antagonist's family and others in his personal sphere together with all those in his professional world such as executives, associates, and front-line personnel in his various entities, bankers, accountants, lawyers, property agents, and all others with knowledge of his financial dealings, holdings, and corporate structures. The multijurisdictional team of asset recovery professionals forms another group, and the judiciary, regulatory bodies, and legislatures yet another. The stakeholders and participants comprising these constituencies are considered independently as well as in direct and indirect connection to each other.

The second presents robust methods for actionably leveraging psychodynamic intelligence and soft and shadow data analysis in case strategy, management, prosecution, and settlement negotiations.

The Fraudster: General Profile, Psychological Components, Talents, Vulnerabilities

> "Society is a masked ball where everyone hides his real character
> and reveals it by hiding."
> — Ralph Waldo Emerson[5]

The psycho-historical origins and mental substructures of criminal fraudulence, driven by individualistic predilections and idiosyncratic circumstances and decisions, are complex, meaningfully vary for every offender, and defy broad-brush theorizing. A comprehensive taxonomy of fraudster psychology encompassing all constituents and underpinnings of every type of fraud is infeasible here. Each fraud case is unique and must ultimately be understood in its own context.

That said, there is a substantial body of evidence-based scholarship explicating the array of psychological devices used and abused by those who commit fraud. Only a fraction of that will be referenced here.

Everyone is a Fraudster

We are unique among species in calling up psychological mechanisms even in the complete absence of any actual external threat. We preserve in our minds vivid phantoms of abusive, traumatising, humiliating, impinging, terrifying, invasive, overwhelming experiences, relationships, and environments of early life. The psychological systems and early response patterns developed to survive some early life circumstance extend into contemporary life as unconscious reflexes—internal responses triggered without awareness or control and that cannot be modulated or aborted at will—and solidify as fixed, embedded features of character. We draw on batteries of such devices—denial, negation, disavowal, repression, suppression, dissociation, splitting, projection, among others—to protect ourselves from feeling, thinking, remembering, or even knowing things about ourselves, and to control people and situations to help us feel safe, powerful, and important.

[5] "The Conduct of Life" (1860)

With gradations and variations across cultures, these are all essential psychological dispositions and devices shared by everyone. They are normal parts of the human condition.

They are also all elemental in fraud. Therefore, in a sense, and in radical departure from constricted historical psychiatric classifications fixated on criminal psychopathy, everyone is (or can be) a fraudster. Or a potential victim.

But of course, not everyone is a malicious felon. Precise reasons why some individuals respond to certain trauma with asocial miscreance or criminality rather than living with quotidian psychological scars are difficult to detail in the abstract. Typical differentiating factors are age, severity, seriality, and response. Serial trauma in very early life usually gives rise to more acute psychological deformations than comparatively less shattering or isolated episodic experiences in later maturational stages. Still, there are countless variables, and developmental trajectories do not follow pre-set formulations. It is not unusual for survivors of severe relational trauma—childhood victims of emotional or sexual abuse, domestic violence, pathologically narcissistic, manipulative, and other toxically disordered and dysfunctional households—to escape those early injuries and lead reasonably healthy and productive lives. But for others, those who grow-up to become fraudsters or predatory power abusers, forming relationships differentiated from their formative experience and developing self-modulated ethical, pro-social decision-making and behavior, is an impossibility. Normal coping and survival mechanisms become weaponized and other people exist only, or primarily, as functional opportunities, recalling the definition of fraud, to profit or gain some unfair or dishonest advantage.

The presenting details of an individual's psychohistory will elicit different responses or have a different function depending on the context. In social relationships, it might prompt compassion—or a hasty retreat; in a therapeutic setting, it should lead to an initial diagnosis and treatment strategy; and in a legal psychiatric context, such data will inform a baseline evaluation to guide sentencing or predict rehabilitation or recidivism.

The utility here is different. These psychological devices developed in the protagonist's life are his weapons. Understanding them is important to formulating a three-dimensional profile—telling us who he is, how he thinks, and what motivates him; how he relates to risks, threats, and other people; clarifies his aims, aspirations, values, and tolerances; reveals potential vulnerabilities, and helps accurately forecast his probable responses and decisions in various future scenarios.

Lies & Deception

Deception abounds across the natural world. Many animals and organisms use an ability to camouflage, feign, disguise, lure, or outwit to live another day, secure sustenance, prevail in conflict, or traverse, escape, or defeat threat and adversity.

Deceit, misrepresentation, dishonesty, evasiveness, and duplicity serve similarly important functions for people. Far from patently undesirable or pathological, most theories of human development consider the child's first lie an important milestone. Lying—the overt, conscious, intentional effort to evade the truth or to present an untruth—is something every human being, including people who are (or claim to be) unwaveringly honest, has done[6]. Everyone employs contrivance and emotional deception as a coping device or for self-preservation.

Innocuous falsities are mandatory mainstays of social life. Diplomacy, minimisation, and white lies facilitate workable relations, and intentional feints, half-truths, and artful obfuscations are accepted requisites of diplomatic rhetoric, political stagecraft, negotiations, interrogations, and corporate deal-making.

Lies can be a form of denial, substituting something private or shame- or guilt-inducing with something less threatening. We conceal or obscure aspects of ourselves—thoughts, feelings, desires, impulses, vulnerabilities—to avoid scrutiny, humiliation, or punishment, or to preserve emotional homeostasis—to feel alright—with others, within ourselves, and in environments we perceive or experience as unsafe.

Another type, common among young children and others with under-developed skills in lying, is negation, in which the object of the lie is expressed in its negative: "I'm not doing something." "There's nothing here." "This is not what you think it is." "You have nothing to worry about."

People will also transform a statement they cognitively recognize as a lie (or probable falsification) into a truth they prefer. Known as wilful denial, fraudsters liberally use this to self-justify their thoughts and actions, and it is also common among fraud victims (and other traumatised individuals) to neutralise emotional pain.

Imposturousness

[6] For a penetrating examination of lying, see "Lying: Moral Choice in Public and Private Life" by Sissela Bok. Vintage; 2nd ed. (1999)

Many fraudulent schemes employ psychological elements related to imposter fraud even if they do not typically use identity disguise.

Imposturous tendencies are universal. The true impostor assumes multiple false identities to deliberately deceive. He passes himself off incognito (which is often the only way he can function) in delinquent or other criminal ways as actually possessing an identity of someone other than himself. One notorious example is Hargobind Punjabi Tahilramani, an Indonesian national dubbed the "Con Queen of Hollywood" who perpetrated an elaborate, long-running con by impersonating powerful female entertainment executives before being apprehended by the FBI.[7] Other prominent cases include Anna Sorokin, a Russian immigrant from a middle-class family, whose frauds pivoted on transforming herself into the persona of Anna Delvey, a non-existent wealthy German heiress. Or, the Colombian imposter Anthony Gignac who convinced people he was a rich Saudi prince named Khalid bin al-Saud, though he was actually a poor street kid from Bogotá who had been adopted and raised by a couple from Michigan.

Many con artists experience themselves as most authentic when they are acting imposturously and often feel as though they are being artificial and phoney when they are themselves. A professional impostor might never fear exposure when swindling but will feel like an impostor if he did honest work.

While seemingly similar to "imposter syndrome" popularised by social psychologist Amy Cuddy's 'fake it until you make it' 2012 Ted Talk, relating to people who fear their insecurity or underpreparedness will be disastrously exposed, criminal impostors commit identity fraud by deliberately pretending under the literal cover of a fictive persona. They are frequently motivated by an unconscious need for punishment, not merely a defence against the dreaded exposure of inadequacy. The drive to produce illusion rather than substance may contain a neurotic fear that healthy, acceptable activities will be mistaken for monstrous crimes for which he would not want to risk being caught. Deceit and artifice, it must be noted, are also critical to the normal promotion of illusion, as in art and play.[8]

The appearance of excessive empathy and a dazzling ability to pass themselves off as having impressive expertise or capacities are other key attributes. They can seem

[7] For more on the psychology behind Tahilramani's con: the bonus episode of the 2020 podcast "Chameleon: Hollywood Con Queen," hosted by Josh Dean and Vanessa Grigoriadis and produced by Campside Media and Sony Music, https://podcasts.apple.com/us/podcast/bonus-episode-1-the-psychology-of-the-scam/id1532225667?i=1000500309399

[8] It is relevant to note that fraud litigators, members of law enforcement and other asset recovery personnel frequently use techniques and instruments of fraud or deception in the normal course of advancing a case, though with entirely different legal aims and motivations, and implemented within rigorous ethical and judicial guidelines.

remarkably attuned to others, quickly and intuitively catching on to what somebody is thinking and feeling, and disarmingly anticipating others' expectations. But all of that is, more accurately, a form of gas-lighting—inauthentic, self-serving, and the antithesis of empathy. It is also typically limited and selective. As keen and sharp as their responses may be in picking up details and certain nuances in the needs and desires of others, particularly those they target, they may also be staggeringly obtuse and emotionally tone-deaf in other relationships.

Betrayal, Manipulation & Abuses of Trust

Betrayal, manipulation, and abuses of trust are standard tools of the fraudster's trade; he could not employ them masterfully without knowing them intimately. He could only have been horribly scarred—a victim—in his own life.

That would likely be denied and even seemingly contradicted by his high functionality and life as a powerful, successful, respected titan of business. Self-deception in inventing an idealised creation myth—a fabricated narrative that childhood was caring, loving, and stable, with parents who praised, encouraged, and provided a strong moral compass—is common in pathogenic trauma.

But psychological evidence, inferred or extrapolated through behavioural symptoms and shadow data—trace information dispositive of mental constructs and predispositions—suggests a different story. The experience of severe betrayal catalyses a host of natural reactions, cross-culturally. These include depressive collapse, dissociative impassivity, chronic anxiety, and violent retaliatory outrage. It is, among all else, laceratingly painful.

Emotional betrayal involves sudden unexpected withdrawals of affection, love, or attention. Availability and interest are doled out intermittently, unpredictably, and in constricted packets. In contingent, insecure attachments, children can become cognitively and emotionally disorganized, and may adopt the artifice of pseudo-empathy and social poise to cover their low self-esteem, insecurity, and powerlessness. The persistent anticipation of instability and dread of disempowerment impels a callous disregard for people and social norms and, in threating situations, can unleash aggressive, disruptive behaviour or an icy catatonic unemotionality.

Criminality

All criminal acts are intrinsically psychological events. As a separate matter from legal, environmental, socio-cultural, and other considerations, criminality is

always a behavioural expression of the actor's internal world destructively or coercively inflicted on others.

But the underpinnings of prohibited, harmful behaviour are, like the elements of fraud, intrinsically normative. Fantasies, urges, and floridly conceived campaigns of brutality, violence, glorious vengeance, the easy acquisition of vast wealth, power, and adoration, lurid and forbidden sexual bacchanals, assorted rampages unencumbered by remorse or concern for consequence, are all commonplace.

Each of us can readily imagine illegal, socially impermissible, morally reprehensible, inhumane, destructive, and viciously repugnant acts. Such mental doings can have various purposes, for example to contend with emotional distress or disturbance or imaginatively satisfy an unrealizable craving. But these are typically transient and containable thoughts which rarely escalate into enactment or committing an actual crime. The imaginary drama is a continuous obsessive rehearsal, not a true factory of scenes and situations. Most of these thoughts and attendant feelings are psychologically digested and dismissed without transgressive action.

The line between criminal fantasy and actual commission is crossed when the thoughts and feelings become so powerfully consuming that working them over mentally is insufficient. The drive for release through action is an imperative that eclipses all else. Abetted by delusional self-rationalisation and dismissal of possible adverse consequences, enactment becomes unstoppable.

Thus, a signal attribute of many criminals is an inability to appropriately self-regulate, manage or contain—reconsider or walk back—primitive urges in harmless fantasies or other nondisruptive outlets, or, like the renegade entrepreneur, harness and transpose adversity or other difficult personal experiences into socially productive law-abiding ventures.

But until that line is crossed, the psychological substructures are ubiquitous human phenomena.

Chief Executive & Master Strategist

The foregoing can be concisely distilled to two main points with important relevance to asset recovery work:

(1) The psycho-historical elements giving rise to fraud are cross-culturally intrinsic to the human condition, not in themselves evidence of severe psychopathology;

(2) A formative life experience organized around knowing the world as abusive and untrustworthy, while creating a constellation of injurious maladaptations, also gives rise to tactical occupational advantages. Analogous to world-class athletes whose mental, muscular, and respiratory systems are perfectly and naturally suited to their sport, fraudsters' primary instinctual reflexes are optimised and seamlessly calibrated for their enterprise.

With rare exception, high-value cross-border fraud is operationally sophisticated. It is the antithesis of the work of the petty criminal. Elite fraudsters are creative, intellectually gifted, and voraciously ambitious. They are superior abstract thinkers with quick intuitive abilities to grasp hidden relationships, often with minimal or incomplete information, and frequently exhibit an unparalleled ability to remain preternaturally poised even under extreme duress.

On this view, and putting ethics and law momentarily aside, some fraudsters are CEOs of complex, effectively organised businesses and can be seen as masterful corporate strategists and organisational leaders. But for the fact that its mission is destructive, illegal, and in the service of malfeasance, their formal business may be structured as any legitimate venture (indeed, ultimate beneficial ownership may be concealed within a labyrinth of seemingly legitimate puppet or nominee entities). In most instances, these organisations are staffed with a senior management team of superior quality and capability.

These organisations, like many others, are also susceptible to myriad quotidian challenges. There will be frustrated and disaffected employees; difficulties with absenteeism, squabbling, and sub-par performance; grumbling lieutenants with stymied aspirations and uncontrollable personal problems (including, not uncommonly, various addictions and abusive relationships), communication quagmires, cultural and inter-departmental friction, and operational and personnel breakdowns of all stripes.

While the principal traits and competencies comprising so-called "great leadership" are not definitionally fixed and remain debated (despite a vast literature devoted to assertions to the contrary), the intense pressures and challenges of the chief executive role are well established. Even the CEOs of the world's highest-performing and most profitable companies have blind spots and invariably stumble.

But any similarities between corrupt and legitimate business leaders should not be mistaken as an equivalence. Authoritarian leanings, malevolent creativity, and

indifference to competitive fair play are nontrivial differentiators. Others include shameless rejection of integrity and honesty, an absence of conscience and pro-social responsibility, and brazen disregard for compliance controls, regulatory legalities, fiduciary legitimacy, and the rule of law.

While the fraudster's playbook engenders certain advantages, voluminous management research demonstrates irrefutable correlations between tyrannical leadership, ethical indifference, and normed institutional corruption with high rates of organisational turmoil and dysfunction.[9] In addition, many large-scale fraudulent enterprises are either literal or de facto family businesses in which numerous family dynamics and dysfunctions distort best practices. The internal cultures of these ventures can closely resemble organized crime syndicates, even if not formally classifiable as such.

In sum, it is critical to understand that the visible persona of individuals who commit high-value cross-border fraud—powerful, successful, shrewd business titans, pillars of moral integrity and paragons of civic largess—is a fiction, its own fraud. Their malevolent brilliance and super-functionality operate only within a narrow spectrum. Beneath the cloaks and veils, they are psychologically damaged and emotionally stunted. They live in a world defined by fear, impotence, betrayal, retribution, threat, and punishment, bound by concerns of humiliation and inferiority, and preoccupied with stratagems for defiance, domination, and retaliation. They are ruthless power-abusers, wedded to vengefulness, devastating others through subterfuge, contrivance and manipulation.

These perspectives are in the aggregate like a psychological X-Ray, providing insight into an array of individual and organizational vulnerabilities that, once amassed and properly understood, can be advantageously leveraged against the protagonist and his confederates.

Victims: Psychological Characteristics & Propensities, and Role in the Fraud and its Aftermath

> *"Every magic trick consists of three parts. The first is The Pledge. The magician shows you something ordinary. The second is called The Turn. The magician takes the ordinary something and makes it appear extraordinary. Now you're looking for the secret … but you don't really want to know. You want to be fooled. But you wouldn't clap yet. Because*

[9] A startling 2015 Harvard Business School study ("Toxic Workers" by Michael Housman and Dylan Minor, https://www.hbs.edu/faculty/Pages/item.aspx?num=50046) found that "toxic workers are much more productive than the average worker" and that while "there is a potential trade-off when employing an unethical person—they are corrupt—they excel in work performance."

> *making something disappear isn't enough; you have to bring it back. That's why every magic trick has a third act … the part we call The Prestige."*
> — Christopher Priest "The Prestige"[10]

Understanding fraud as a total event entails looking not only at why certain people commit it but why some become victims. Of additional practical importance in expanding the asset recovery toolkit is leveraging insight about the victim's role in the criminal proceedings and aftermath as material witness, first order data source, and fiduciary stakeholder in the recovery operation.

Fraud differs from crimes of threat or force. Few people on the wrong end of a weapon will defy a perpetrator's demand to hand over their valuables. Victims of fraud and other cons, by contrast, must play an active part in what happens. Fraud exists in relationships and arrangements between people, and pivots on complicitous confluences of power, needs, desires, and individual histories and tendencies. Trust cannot be breached until it has been given or established.

As fraudsters have been narrowly categorised as sociopaths, so too have victims of fraud been mischaracterised. They have as a class been considered greedy, witless, or gullible patsies, susceptible to manipulation and deception. Allowing oneself to be bamboozled was taken as *prima facie* evidence of naïveté.

Legal systems have been (and many still are) riven with this bias. Historically, courts of law and of public opinion responded to victims of fraud as they have to victims of sexual assault or domestic violence, apportioning culpability to the victim for causing the crime or failing to avert it.

Consequently, fraud victims have suffered the additional indignities of social stigma and obstruction to appropriate legal and financial remedy, injuries further compounded by victims' own shame, embarrassment, and self-castigation for having been duped. But unwitting participation does not change that they are victims in the truest sense: harmed or adversely affected by another's wrongdoing.

As Material Witness and First Order Data Source—Marked by Psychological Fingerprints

Misconceptions about victims have also influenced asset recovery professionals' interactions with them, unintentionally contributing to overlooking or foreclosing critical intelligence and primary evidentiary material.

[10] "The Prestige" by Christopher Priest (1995), Tor Books

However unique each incident is, every victim of fraud shares a common experience: the dual trauma of betrayal and loss. Victims are also typically shocked, humiliated, ashamed, weak, vulnerable, furious, and untrusting. They may be despondent, disinterested, defeated, or resigned, as well as agitated or bellicose, stressed, and distressed. Depression and suicidality are common.[11] Fissures can form in personal and professional relationships leading to divorce, partnership dissolutions, and acrimony with friends and relatives.[12] They may be bankrupt; even if not, they will likely be financially anxious and risk averse.

This is not merely a complex evidentiary field. It is a roiling cauldron of emotionality. The victim may be psychologically haemorrhaging even if he appears intact. And notwithstanding a willingness to help—he is after all a primary stakeholder in assisting the asset recovery professionals in bringing the fraudster to book and, hopefully, being repatriated with some of his stolen assets—he may be too overwhelmed, humiliated, guarded, and mistrustful to think clearly, speak coherently, or productively engage in discovery interviews.

But victims are uniquely important sources of information. They are to be considered akin to a crime scene. Grifters, hucksters, and sundry con artists colloquially call victims "marks" (among other terms like sucker, rube, and stooge). It is uncannily apt. Victims bear the mark of the perpetrator. Analogous to physical evidence, fraudsters leave psychological fingerprints—impressions, emotional traces, and other fragments of soft data. These can be culled from victims' accounts of their experience in interviews and from which potentially useful intelligence about the malicious actor and the mechanics of the enterprise can be extrapolated.

But as noted, this information can be challenging to access through the static of victims' distress or could be overlooked in the fast-moving larger-scale project of harvesting diverse evidentiary material. Expertise in victim interviewing and specialised soft intelligence gathering—including compassion, patience, and sensitivity—are important.

Roles & Functions in Relation to Fraudsters

[11] For additional information on the topic of red collar crime—white-collar crime leading to physical violence and/or death (whether homicide or suicide)—see Brody RG, Kiehl KA. "From White-Collar Crime to Red-Collar Crime." J. Financ Crime. 2010;17(3):351-364; Perri, Frank S. "Red Collar Crime." Intl J Psych Studies Archives 2016; 8(1):61-84; Perri, Frank S. "Fraud detection suicide: the dark side of white-collar crime." J. Financ Crime 2016 23(4) 786-797).

[12] See The White-Collar Wives Project, Lisa Lawler, Founder, for information and resources around the the catastrophic legal, economic, and emotional fallout to innocent spouses and families of fraudsters and perpetrators of clandestine economic crimes: https://www.thewhitecollarwivesproject.org/.

While some individuals are more susceptible to being scammed than others, no one is immune. Anyone can play into a fraudster's ploy. There is no definitive victim profile. That said, there is a recurrent fundamental in every fraudulent scenario: desire.

Both victim and fraudster share the want of something—the fulfilment of a wish or need. The fulcrum of economic crime is of course money or some other valuable asset, though this is often merely an incidental vehicle used by both fraudster and victim for the attainment of other aims—for instance, power, status, recognition, admiration, love, validation, social elevation, retribution, or any of a host of other para-economic interests.[13] Like any talented entrepreneur, the fraudster identifies a desirable commodity or service that he will, in essence, bring to market. Part of the fraudster's work is to make his offering appear concordant with victims' interests.

An obvious factor distinguishing fraudulent from legitimate enterprises is that its business model is intentional deception and harm. While aspects of that grotesquely inequitable transaction are the fraudster's responsibility, the victim must be sufficiently motivated to overcome (or dispense with) due diligence best practices, sound judgment, experience, good counsel, even intuition. Some may abandon rationality and reason altogether. Denial and magical thinking, mentioned above, allow victims to dismiss red flags and delusionally believe that all will be well—*he might be capable of stealing from others*, the victim tells himself, *but he won't steal from me*.

People also tend to follow group or mob mentality. Ponzi artists, for example, enlist victims as unwitting sales associates; in bragging or touting their investment success, each successive group of marks grease the machinery that will entice new recruits to voluntarily participate.

Recall the pseudo-attunement to others discussed above. Successful fraudsters keenly pinpoint and then exploit people's propensities and vulnerabilities, enticing or duping them to yield to the con of their own accord.

But despite their apparent impunity, fraudsters are, ironically, always in a relationship of dependency to others. Unlike criminals who use weaponry or force,

[13] There is abundant criminal case law grounded in McNally v. United States, 1987, wherein the U.S. Supreme Court held that in order to constitute fraud, the object of a scheme must be to deprive a victim of money or property. U.S. criminal law insists on a clear legal distinction between fraud and mere deceit or deceptive conduct, and repeatedly concludes that not all deception is fraud. The discussion here focuses on active psychological elements which operate indifferently to the narrow parameters of legal and judicial determinations.

or stealth and tactical brilliance, the fraudster's success is contingent on victim participation.

No matter any scheme's payday, flipping the polarities of power in a relationship, abusing and betraying trust, inflicting psychological pain are fraudsters' actual drivers. That goal can only be attained with the help of another.

This, ultimately, is his Achilles Heel.

Judiciary and Legislature

"*Not everything that is legal is right*."
— Judge Theodor Seidel[14]

Since the 15th century, the main iconography of justice has been *Justicia*, a blindfolded woman carrying a double-edged sword symbolising reason (or truth) and fairness, in one hand, while balancing the scales of a case's competing claims, in the other. The notion that "justice is blind" is meant to convey a court's impartiality and objectivity.

Judiciary officers, sovereign legislative bodies, regulators, government officials, and other law makers comprise an important constituency in the ecosystem of a fraud case. Their decisions and interventions can facilitate or hinder investigations and recovery initiatives and influence legal strategy and case management decisions. They can also serve as de facto enablers to fraudsters, money launderers, and other corrupt actors. Jurisdictions that offer products, services, and laws such as bank secrecy, impenetrable asset protection vehicles, and short statutes of limitations in which to file claims, among other mechanisms will appeal to or even facilitate wrongdoing.

Certain jurisdictions are hotbeds of corruption and under-the-table deal-making. In certain locales, jurisprudence, politics, economics, and social or religious ideology openly comingle. Judicial and legislative decisions and policies are the products of individuals' ideologies, philosophies, and personal predilections, not just case law and precedent. Some jurists and policy architects are unabashed activists, will exceed their authority, or are allergic to impartiality. Their decision-making might favour political agendas, socially promulgated morals, or cultural and religious values. Or, such may hold greater allegiance to placating special

[14] From Judge Theodor Seidel's sentencing pronouncement in the February 1992 case against East German soldier Ingo Heinrich, on trial for shooting and killing Chris Gueffroy in 1989 as he tried to climb the Berlin Wall.

interest groups and influential business leaders than advancing socially just regulatory policy. Jurists no less than fraud victims are susceptible to corruption.

Experienced cross-border asset recovery professionals accept the potential for these issues to influence case disposition, often as unavoidable forces beyond control. While certain factors may indeed be untouchable, important benefits derive from closely examining and developing sophisticated proactive responses and workarounds to this dimension of a case.

Asset Recovery Team

"Only a few know how much one must know to know how little one knows"
— Werner Heisenberg[15]

Asset tracing and recovery in high-value cross-border cases requires the coordinated collaboration of professionals across a range of disciplines. Collectively, this consortium is the asset recovery team ('ART').

There is a vast literature on optimising team performance and effective project management. A deep review of those and other affiliated research in application to asset recovery work is beyond the scope of this article. Instead, this section presents a concise overview of psychodynamic concepts and tools specifically relevant to asset recovery and fraud litigation[16].

ARTs engage with both allies and antagonists across the case ecosystem and, as already noted, contend with circumstances and issues involving individual and social psychology, organizational dynamics, and family systems. Attempting to assess or act on such matters without domain-relevant expertise, armed only with *de minimus* lay understandings, is an avoidable handicap that places offenders in a significant advantage over the professionals attempting to defeat them. By analogy, forensic criminology was transformed by the introduction of microscopy, DNA analysis, and other technologies that empowered the collection and analysis of previously invisible physical evidence. Similarly, there is a wealth of psychodynamic data beyond hard facts and evidence which can measurably advance a case.

Actionable Tools & Applications of Psychodynamic Intelligence Analysis

[15] Werner Heisenberg, theoretical physicist (1901-1976)

[16] See also, *"Multi-Jurisdictional Concealed Asset Recovery: Managing the Risks"* by Martin S. Kenney, Alex D. Moglia, and Alexander Stein, Journal of International Banking Law and Regulation, Vol 1, 2015; "*Leadership and Management of People In Asset Recovery*" by Martin S. Kenney, Alexander

"*Never interfere with the enemy while he is in the process of destroying himself.*"
— Napoleon Bonaparte[17]

Fraud weaponises human psychology. Psychology can be used as a countermeasure.

As certain martial arts redirect an attacker's strength against him by leveraging physics and tactical savvy, the force of psychodynamic intelligence analysis enables insights regarding the fraudster's psychological vulnerabilities and other psycho-social dimensions of the malicious enterprise to be turned against him.

In conventional management consulting, assessments of organisational and leadership challenges are a point of entry to implement a go-ahead action plan for enhanced functionality, sustainability, and profitability. By contrast, stress points and dysfunctions identified in the fraudster's organisation through investigation and other intelligence gathering, can be pried apart and exploited to advance the pursuit of justice.

The array of deployment areas and methods for leveraging psychological expertise include:

- Developing dynamic predictive behavioural models of primary and ancillary actors and their networks of affiliates, collaborators, and organizations.
- Creating actionable pinpoint profiles and analyses of the opposition's personal life and professional operations, including executive team, front-line personnel, and organisational strengths and vulnerabilities.
- Providing psychologically sophisticated counter-offensive tactical planning.
- Boosting human systems intelligence gathering and strengthening both victim and other involved stakeholder interviewing to enhance the interpretation and application value of information obtained.
- Providing precision forecasts and expert counsel regarding the entire human ecosystem of the case in preparation for settlement negotiations, pre-trial

Stein, Alex D. Moglia, and D.C. Page, unpublished whitepaper presented at The C5 30th Fraud, Asset Tracing & Recovery Forum, Miami, Florida, October 2015; and "*Cross-Disciplinary Collaboration in Fraud and Asset Recovery*" by Martin S. Kenney and Alexander Stein, unpublished whitepaper presented at The ACFE 25th Annual Global Fraud Conference, San Antonio, Texas, June 2014.

[17] Authorship indeterminate but usually attributed to Napoleon Bonaparte, French military commander and political leader, 1769-1821.

meetings, arbitration hearings, settlement discussions, and court proceedings.

Conclusion

"Every human being's life in this world is inevitably mixed with every other life and, no matter what laws we pass, no matter what precautions we take, unless the people we meet are kindly and decent and human and liberty-loving, then there is no liberty. Freedom comes from human beings, rather than from laws and institutions."

— Clarence Darrow[18]

Criminal fraud is a perversion of natural, universal human psychological systems, and a radical deformation of societally productive entrepreneurship. The building blocks and predispositions both to commit fraud and become victim of it are endemic to the human condition, and many aspects of the world's economic and social systems enable, abet, or are indifferent to the corruption and abuses of power that engender large-scale fraud.

Even if fraud cannot be wholly eliminated, more effective detection, deterrence, prevention, and recovery mechanisms can and must be brought to bear. Providing more robust and sophisticated tools and resource to the professionals dedicated to bringing fraudsters and kleptocrats to justice and recovering and repatriating value wrongfully taken from victims must be a priority. Crucial to that, as has been argued here, is clarifying the wide-ranging simplifications and misunderstandings of the psychological dynamics and psycho-social elements at play across the spectrum of involved parties as well as elevating the utilisation of specialist expertise in the human dimensions of fraud in asset recovery case work.

[18] From Darrow's closing argument in People v Henry Sweet, 1926

ICC FraudNet
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The Boundaries of Arbitration Exclusion in the EAPO Regulation

DR CARLOS SANTALÓ GORIS

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Abstract

The European Account Preservation Order consists of an interim measure at the EU level. It allows the temporary attachment of debtors' funds in cross-border civil and commercial claims. The EAPO Regulation states that it does not apply to 'arbitration'. The meaning of 'arbitration' is not a settled question among scholars and national courts. In this article, Dr Carlos Santaló Goris explores the underpinning debate surrounding the arbitration exclusion, focusing on the interpretation some national courts have made of it.

A. Courts interim measures in arbitration proceedings

1. National procedural systems generally permit courts to grant interim measures in support of civil claims brought before arbitral courts. The fact that the parties decide to bring a civil claim before an arbitral court does not necessarily exclude them from measures granted by ordinary courts. For instance, the German Code of Civil Procedure (*Zivilprozessordnung*) states that 'an arbitration agreement does not preclude a court from ordering, at the request of a party, an interim or conservatory measure with respect to the subject matter of the arbitration before or after the commencement of the arbitration'.[1] A similar provision can be found in the Spanish

[1] Section 1033 German Code of Civil Procedure (*Zivilprozessordnung*)

Code of Civil Procedure (*Ley de Enjuiciamento Civil*).[2] The 2010 Irish Arbitration Act, referring to the UNCITRAL Model Law on International Commercial Arbitration,[3] acknowledges that it 'is not incompatible with an arbitration agreement for a party to request, before or during arbitral proceedings, from a court an interim measure of protection and for a court to grant such measure'.[4]

2. Regulation No 655/2014 introduced the European Account Preservation Order ('EAPO'), which is the very first cross-border civil interim measure at the European Union level.[5] It applies in all EU Member States but Denmark.[6] It permits courts of the EU Member States where the EAPO Regulation applies to order the provisional attachment of the funds in the bank accounts located in other Member States.[7] The EAPO can be used only in civil and commercial claims with a cross-border dimension.[8] Creditors can apply for the EAPO *ante demandam*, during the proceeding on the merits or once they have already obtained an enforceable judgment, authentic instrument or court settlement.[9] Moreover, creditors who have a title, enforceable or not, by the time they submit an EAPO application can also request the investigation of the debtors' bank accounts.[10] One of the EAPO's most attractive features is that is always granted *ex parte*,[11] so debtors are only informed about the attachment of their bank accounts once it has already happened.

3. Can the EAPO be included among those interim measures that courts can grant to secure a claim before an arbitral tribunal? In this regard, it should be noted that the EAPO Regulation states that 'arbitration' is an excluded subject matter.[12] Depending on how arbitration exclusion is interpreted, one could argue that an EAPO may or not be granted to secure a claim brought before an arbitral court. This

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[2] This possibility also features in Art. 722(1) Spanish Code of Civil Procedure (*Ley de Enjuiciamiento Civil*). The Spanish Arbitration Act reiterates this possibility: Art. 11(3) Act 60/2003 of Arbitration (*Ley 60/2003 de Arbitraje*).
[3] Article 9 UNCITRAL Model Law on International Commercial Arbitration 1985 (With amendments as adopted in 2006)
[4] Article 10 Irish Arbitration Act.
[5] Regulation (EU) No 655/2014 of the European Parliament and of the Council of 15 May 2014 establishing a European Account Preservation Order procedure to facilitate cross-border debt recovery in civil and commercial matters, OJ L 189, 27.6.2014, p. 59–92 ('EAPO Regulation').
[6] Recital 51 EAPO Regulation.
[7] For a more exhaustive overview of the EAPO Regulation, see the previous edition of the FraudNet Global Annual Report: Carlos Santaló Goris, 'Searching for the Debtors' Bank Accounts across the European Union: the EAPO Regulation Information Mechanism' FraudNet Global Annual Report (2022), 231.
[8] Art. 2 EAPO Regulation. The EAPO Regulation defines a cross-border claim as one where the creditors' domicile or the court that grants the EAPO is in a different Member State than the bank account to be attached is located: Art. 3 EAPO Regulation.
[9] Art. 5 EAPO Regulation.
[10] Art. 14(1) EAPO Regulation.
[11] Art. 11 EAPO Regulation.
[12] Art. 2(1) EAPO Regulation.

article explores the different interpretations of the arbitration exclusion, relying on the contributions scholars have made to the topic and the approaches followed by some national courts.

B. The boundaries of the arbitration exclusion

4. Among scholars, there are different interpretations of what the 'exclusion of arbitration' means.[13] Nonetheless, the most prevalent view is that the moment there is an arbitration clause that compels the parties to bring their claim before an arbitral court, they can no longer apply for an EAPO.[14] This broad interpretation was seemingly embraced by the European Commission, which in the Proposal of the EAPO Regulation it stated that 'even though there might be a case for allowing parties to an arbitration to have recourse to the European procedure, the inclusion of arbitration would entail complex questions which have not yet been addressed by EU law, e.g. under which circumstances arbitral awards can be put on an equal footing with judgments and it did not seem appropriate to address them for the first time in this instrument'.[15]

6. There are some authors who have a more restrictive view of the arbitration exclusion. For *Hilbig-Lugani*, it is possible to obtain an EAPO before initiation of the arbitration proceedings, even when there is an arbitration clause compelling parties to bring their claim before an arbitral court.[16] The arbitration exclusion would only operate once the arbitration proceeding begins. For *Schumacher,* once the arbitration proceeding has come to an end and there is an arbitral award, the

[13] For an extensive overview on the different interpretations that scholars have made of the EAPO's arbitration exclusion, see: Denise Wiedemann, 'The European Account Preservation Order' in Jan von Hein and Thalia Kruger (eds.), *Informed Choices in Cross-Border Enforcement. The European State of the Art and Future Perspectives* (Intersentia 2021) 109 – 114.

[14] Burkhard Hess, 'Art. 2 EuKoPfVO' in Peter Schlosser and Burkhard Hess (eds.), *EU-Zivilprozessrecht* (5th edition C.H. Beck 2021), margin no. 3; Pilar Jiménez Blanco, 'La Orden Europea de Retención de Cuentas: Avances y limitaciones' Anuario español de Derecho internacional privado (2014/2015) 245 – 245; Martin Klöpfer, 'Art. 2 Verordnung (EU) Nr 655/2014' in Reinhold Geimer and Rolf A Schütze (eds.), *Internationaler Rechtsverkehr in Zivil- und Handelssachen* (CH Beck 2016), margin no. 7; Franz Mohr, *Die vorläufige Kontenpfändung. EuKoPfVO* (LexisNexis 2014), margin no. 34; Miguel Teixeira de Sousa, 'O Reg. 655/2014 sobre o Procedimento de decisão europeia de arresto de Contas: uma apresentação geral' Revista da Ordem dos Advogados (2019) 194 – 195; Martin Trenker, 'Vorläufige Kontenpfändung: Überblick und ausgewählte Fragen' in Bernhard König and Peter G. Mayr (eds.), *Europäisches Zivilverfahrensrecht in Österreich IV* (Manz 2015) 129; Marcin Walasik, 'Article 2' in Elena D'Alessandro and Fernando Gascón Inchausti (eds.), *The European Account Preservation Order. A Commentary on Regulation (EU) No 655/2014* (Edward Elgar 2022), paras. 2.26-2.30; Nora Wallner-Friedl, 'Artikle 2 EuKoPfVO' in Andreas Geroldinger and Nora Wallner-Friedl (eds.), *IZVR Praxiskommentar Internationales Zivilverfahrensrecht* (LexisNexis 2021), margin no. 13; Denise Wiedemann, 'Artikel 2 EU-KpfVO' in Thomas Rauscher (ed.), *Europäisches Zivilprozess- und Kollisionsrecht* (5th edition Otto Schmidt 2022), paras. 12 - 18.

[15] COM/2011/0445 final, 5.

[16] Katharina Hilbig-Lugani, 'Art. 2 EuKoPfVO' in Thomas Rauscher and Wolfgang Krüger (eds.), *Münchener Kommentar zur Zivilprozessordnung. Band 3* (6th edition C.H. Beck 2022), margin no. 9.

arbitration exclusion would no longer operate.[17] Creditors could apply for an EAPO to guarantee the enforcement of an arbitral award.

C. The CJEU approach towards the exclusion of arbitration in the Brussels system: is this of any relevance for the EAPO Regulation?

7. The EAPO Regulation is not the only EU civil procedural instrument for which arbitration is excluded. The European Enforcement Order, the European Small Claims Regulation and the Brussels I bis Regulation all contain a similar reference excluding arbitration.[18] Under the two predecessors of the Brussels I bis Regulation, the 1968 Brussels Convention and the 2001 Brussels I Regulation,[19] the CJEU has rendered several key judgments interpreting the arbitration exclusion.[20] Part of this case-law was codified to the Preamble of the Brussels I bis Regulation.[21]

8. Among of the judgments rendered by the CJEU on the arbitration exclusion, C-391/95, *Van Uden* is the most relevant for the EAPO Regulation.[22] In this case, the CJEU was asked to determine whether, given the arbitration exclusion, is possible to use the jurisdictional rules of the 1968 Brussels Convention to obtain an interim measure.[23] In this judgment, the CJEU affirmed that what was relevant to decide 'whether the 1968 Brussels Convention could apply to a procedure on interim measures was the 'nature of the rights which they serve to protect'.[24] Therefore, as long as the claim does not concern the arbitration procedure as a subject manner, claimants could still rely on the 1968 Brussels Convention.[25] For instance, claims

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[17] Hubertus Schumacher, 'Art. 2 EuKoPfVO' in Hubertus Schumacher, Barbara Köllensperger and Martin Trenker (eds.), *Kommentar zur EU-Kontenpfändungsverordnung EuKoPfVO* (MANZ 2017), margin no. 65.

[18] Art. 2(2)(d) Regulation (EC) No 805/2004 of the European Parliament and of the Council of 21 April 2004 creating a European Enforcement Order for uncontested claims OJ L 143, 30.4.2004, p. 15–39; Art. 2(2)(e) Regulation (EC) No 861/2007 of the European Parliament and of the Council of 11 July 2007 establishing a European Small Claims Procedure, OJ L 199, 31.7.2007, p. 1–22; Art. 1(2)(d) Regulation (EU) No 1215/2012 of the European Parliament and of the Council of 12 December 2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast), OJ L 351, 20.12.2012, p. 1–32 (Brussels I bis Regulation).

[19] 1968 Brussels Convention on jurisdiction and the enforcement of judgments in civil and commercial matters, OJ L 299, 31.12.1972, p. 32–42 (1968 Brussels Convention); Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters OJ L 12, 16.1.2001, p. 1–23 (Brussels I Regulation).

[20] C-190/89, 25 July 1991, *Marc Rich*, ECLI:EU:C:1991:319; C-185/07, 10 February 2009, *West Tankers*, ECLI:EU:C:2009:69; C-536/13, 13 May 2015, *Gazprom*, ECLI:EU:C:2015:316; C-700/20, 20 June 2022, *London Steam-Ship Owners' Mutual Insurance Association*, ECLI:EU:C:2022:488.

[21] Recital Brussels I bis Regulation.

[22] C-391/95, 17 November 1998, *Van Uden*, ECLI:EU:C:1998:543.

[23] C-391/95, 17 November 1998, *Van Uden*, ECLI:EU:C:1998:543, para 18.

[24] C-391/95, 17 November 1998, *Van Uden*, ECLI:EU:C:1998:543, para 33. Something that the CJEU had already determined in previous judgments: C-143/78, 27 March 1979, *De Cavel (I)*, ECLI:EU:C:1979:83, paras. 7 – 9; C-120/79, 6 March 1980, *De Cavel (II)*, ECLI:EU:C:1980:70, para. 9; C-25/81, 31 March 1982, *C.H.W.*, ECLI:EU:C:1982:116, paras. 6 – 8.

[25] Fernando Gascón Inchausti, 'Artículo 35' in José Pedro Pérez-Llorca, Pilar Blanco-Morales Limones, Federico Francisco Garau Sobrino, María Luz Lorenzo Guillén, Félix J. Monteiro Muriel (eds.), *Comentario al Reglamento (UE) nº 1215/2012 relativo a la competencia judicial, el reconocimiento y la*

by arbitrators for the payment of their fees would be excluded.[26] At the same time, the CJEU state that 'where the parties have validly excluded the jurisdiction of the courts in a dispute arising under a contract and have referred that dispute to arbitration, there are no courts of any State that have jurisdiction as to the substance of the case for the purposes of the Convention'.[27] However, courts could still rely on Art. 24 (now Art. 35 of the Brussels I bis Regulation) which stated that other courts than those with jurisdiction to decide on the merits of the claim can render interim measures.[28] It should be noted that, unless the CJEU decides the opposite, *Van Uden* remains applicable to the Brussels I bis Regulation unless the CJEU decides to the contrary.[29]

9. Can the *Van Uden* solution be transposed to the EAPO Regulation? When an EAPO is requested before the creditor has obtained an enforceable title, and the debtor is not a consumer, the jurisdiction to issue the EAPO 'shall lie with the courts of the Member State which have jurisdiction to rule on the substance of the matter in accordance with the relevant rules of jurisdiction applicable'.[30] These relevant rules on jurisdiction include the Brussels I bis Regulation.[31] However, only the rules on jurisdiction of the Brussels I bis Regulation that permit 'to rule on the substance of the matter' can be used. Since there is an arbitration agreement, there would be no courts with jurisdiction to decide on the merits.[32] Art. 35 of the Brussels I bis Regulation would also be excluded since it only serves to grant 'provisional, including protective measures' but not to decide on the merits.[33]

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ejecución de resoluciones judiciales en materia civil y mercantil. Reglamento Bruselas I (Aranzadi Thomson Reuters 2016), 713.

[26] Gilles Cuniberti and Sara Migliorini, *The European Account Preservation Order Regulation: A Commentary* (Cambridge 2018), 27.

[27] C-391/95, 17 November 1998, *Van Uden*, ECLI:EU:C:1998:543, para. 24.

[28] C-391/95, 17 November 1998, *Van Uden*, ECLI:EU:C:1998:543, para. 29.

[29] In C-186/19, *Supreme Site Services*, the CJEU stated that the case law on Art. 24 of the 1968 Brussels Convention 'can be transposed to the interpretation of the equivalent provisions in Article 35 of Regulation No 1215/2012 (Brussels I bis Regulation)': C-186/19, 3 September 2020, *Supreme Site Services*, ECLI:EU:C:2020:638, para. 50. In TOTO, the CJEU referred to C-391/95, *Van Uden* when interpreting Art. 35 of the Brussels I bis Regulation: C-581/20, 6 October 2021, *TOTO*, ECLI:EU:C:2021:808, para. 52.

[30] Art. 6(1) EAPO Regulation.

[31] Pietro Franzina, 'Article 6' in Elena D'Alessandro and Fernando Gascón Inchausti (eds.*), The European Account Preservation Order. A Commentary on Regulation (EU) No 655/2014* (Edward Elgar 2022), paras. 6.07 – 6.08.

[32] In this regard, *Leandro* remarks that 'a distinction may be proposed between a "court" having jurisdiction on the merits (and, accordingly, for granting the EAPO) and a "court" which would have had jurisdiction on the merits, absent a valid arbitration agreement, which may nonetheless grant an EAPO': Antonio Leandro, 'Arbitration and European Account Preservation Order' Kluwer Arbitration Blog (2016), available at: <http://arbitrationblog.kluwerarbitration.com/2016/04/04/arbitration-european-account-preservation-order/> accessed on 15 January 2023.

[33] Katharina Hilbig-Lugani, 'Art. 6 EuKoPfVO' in Thomas Rauscher and Wolfgang Krüger (eds.), Münchener Kommentar zur Zivilprozessordnung. Band 3 (6th edition C.H. Beck 2022), margin no. 7; Denise Wiedemann, 'Artikel 6 EU-KpfVO' in Thomas Rauscher (ed.), *Europäisches Zivilprozess- und Kollisionsrecht* (5th edition Otto Schmidt 2022), margin no. 5.

Therefore, the *Van Uden* solution would not fit in the jurisdictional regime of the EAPO Regulation.[34]

D. National courts' approach towards the arbitration exclusion: from Lithuania to Luxembourg passing by Poland

10. The extension of the arbitration exclusion is no longer a merely theoretical question. Domestic case law on the EAPO Regulation shows that courts in at least three different Member State have already dealt with this issue. One of these courts was the Lithuanian Court of Appeals (*Lietuvos apeliacinis teismas*). It was asked to clarify whether District Court of Vilnius (*Vilniaus apygardos teismo*) could grant an EAPO in a case pending before the Vilnius Commercial Arbitration Court (*Vilniaus komercinio arbitražo teisme*).[35] First, the Lithuanian Court of Appeals (*Lietuvos apeliacinis teismas*) found that the above-mentioned judgment C-391/95, *Van Uden*, did not apply to the EAPO Regulation.[36] Therefore, it determined that under the Brussels I bis Regulation Lithuanian courts did not have jurisdiction to grant an EAPO in a claim pending before an arbitral court.

11. Since the Brussels I bis Regulation was not applicable, the Lithuanian Court of Appeals (*Lietuvos apeliacinis teismas*) explored whether it would be possible to grant the EAPO relying on the domestic rules on jurisdiction.[37] It needs to be recalled that the jurisdiction to grant an EAPO 'lie with the courts of the Member State which have jurisdiction to rule on the substance of the matter in accordance with the relevant rules of jurisdiction applicable'.[38] Those 'relevant rules of jurisdiction' include not only the Brussels I bis Regulation but also domestic rules on jurisdiction.[39] In this case, the Lithuanian Court of Appeals (*Lietuvos apeliacinis teismas*) wondered if Article 27(2) of the Lithuanian Act on Commercial Arbitration could provide the jurisdiction to grant an EAPO. This provision states that 'a party shall be entitled to request Vilnius Regional Court to take interim measures or require to preserve evidence before the commencement of arbitral proceedings or the constitution of an arbitral tribunal'. Nonetheless, the Lithuanian legislation implementing the EAPO Regulation states that the court with jurisdiction to decide

[34] Burkhard Hess, 'Art. 2 EuKoPfVO' in Peter Schlosser and Burkhard Hess (eds.), *EU-Zivilprozessrecht* (5th edition C.H. Beck 2021), margin no. 3.
[35] Lietuvos apeliacinis teismas, 28.11.2017, byla e2-1387-178/2017, para 21.
[36] Lietuvos apeliacinis teismas, 28.11.2017, byla e2-1387-178/2017, para 21.
[37] Lietuvos apeliacinis teismas, 28.11.2017, byla e2-1387-178/2017, para 23.
[38] Art. 6(1) EAPO Regulation.
[39] For instance, in Slovakia, the District Court Žilina (*Okresný súd Žilina*) of determined that Slovakian courts had jurisdiction to grant an EAPO against the bank accounts of a debtor domiciled in the USA based on the Slovakian domestic rules on jurisdiction, more precisely on the 1963 Czechoslovakian Act on International Private and Procedural Law (*Zákon o medzinárodnom práve súkromnom a procesnom*): Okresný súd Žilina, 13.08.2020, 50Cb/38/2020, ECLI:SK:OSZA:2020:5120208691.1.

on the merits is the only competent to grant the EAPO.[40] Therefore, Lithuanian Court of Appeals (*Lietuvos apeliacinis teismas*) concluded if the claim is brought before an arbitral court, under Lithuanian law, there would not be a competent court to grant the EAPO.[41]

12. In Poland, the Court of Appeal in Rzeszów (*Sąd Apelacyjny w Rzeszowie*) also found that the domestic rules of jurisdiction could serve to grant an EAPO in support of claim brought before an arbitral tribunal.[42] More precisely, this court referred to Art. 1166 of the Polish Code of Civil Procedure, which states that 'subjecting the dispute to the arbitration court does not exclude the ability of the court to secure the claims which are brought before the arbitration court'.

13. Using the domestic rules on jurisdiction can be a solution to circumvent the limitations of the Brussels I bis Regulation. Nonetheless, there is an aspect of the EAPO Regulation that Lithuanian and Polish courts should have considered that would prevent granting an EAPO when a claim is brought before an arbitral court. The EAPO Regulation requires that the procedure on the substance of the matter has to be conducted before a court.[43] This leads to the question: does an arbitral court fit in the category of a court that decides on the merits of the claim? In this regard, the CJEU has stated that, in principle, arbitral courts do not enter in the category of courts that can make a preliminary reference under Article 267 of the Treaty on the Functioning of the European Union.[44] Relying on this definition, an arbitral court cannot be a court that decides on the merits of the claim in an EAPO procedure.[45] Against this argument one could wonder whether the definition of a court that decides on the merits needs to match the definition of court that can make a preliminary reference.[46] This is an open question that only the CJEU can

[40] Art 30(18) Law of the Republic of Lithuania on the Implementation of European Union and International Legal Acts Regulating Civil Procedure (*Lietuvos Respublikos civilinį procesą reglamentuojančių Europos Sąjungos irtarptautinės teisės aktų įgyvendinimo įstatymas*)
[41] Lietuvos apeliacinis teismas, 28.11.2017, byla e2-1387-178/2017, para 23.
[42] On this case see: Grzegorz Pobożniak and Paweł Sikora, 'The Admissibility of a European Account Preservation Order in the Event of an Arbitration Clause' Czech (& Central European) Yearbook of Arbitration (2018) 226 – 227.
[43] Art. 10(3) EAPO Regulation.
[44] C-284/16, 6 March 2018, *Achmea* ECLI:EU:C:2018:158, 54 – 56. Only an arbitral court which 'had been established by law, its decisions were binding on the parties and its jurisdiction did not depend on their agreement' could make a preliminary reference: C-377/13, 12 June 2014, *Ascendi Beiras Litoral e Alta, Auto Estradas das Beiras Litoral e Alta*, ECLI:EU:C:2014:1754, para. 28.
[45] Wiedemann (n 13), 111.
[46] In this regard it should be noted that in the CJEU case C-551/15, *Pula Parking*, Advocate General Bobek relied on the notion of 'court' entitled to make a preliminary reference under Art. 267 of the TFEU to examine the notion of 'court' in the Brussels I bis Regulation. On the one hand, he considered 'it inappropriate to import wholesale definitions that have been developed in different contexts of other instruments of secondary law' (para. 98). Nonetheless, the criteria to determine that a court can make a preliminary reference under Art. 267 of the TFEU can be a term of reference to establish the notion of court under the Brussels I bis Regulation: Opinion AG Bokek in C-551/15, Pula Parking, ECLI:EU:C:2016:825, paras. 82 – 107.

answer. In the meantime, as a matter of caution, a coherent interpretation of both notions would be preferable.[47] It would be up to the CJEU to decide differently (if it ever has that chance).

14. Luxembourg was the third Member State where a court dealt with an arbitration exclusion. In this case, the creditor already had an arbitral award and requested an EAPO before the District Court of Luxembourg (*Tribunal d'arrondissement de Luxembourg*) to secure its enforcement.[48] The court granted the EAPO. Subsequently, the debtor requested before the same court the revocation of the EAPO under Article 33 of the EAPO Regulation.[49] The debtor argued, among other reasons, that the claim fell within the arbitration exclusion. The court did not examine whether the claim did or did not fall within that arbitration exclusion.[50] In the court's view, since the EAPO had not attached any funds, the debtor did not have an interest (*interet d'agir*) to obtain the revocation of the EAPO. In other words, the debtor lacked the locus standi required by Luxembourgish law.[51]

15. The critical point of this case is the reason why the District Court of Luxembourg (*Tribunal d'arrondissement de Luxembourg*) issued an EAPO to secure the enforcement of an arbitral award. The EAPO Regulation only acknowledges three kinds of titles that can be used to apply for an EAPO: judgments, court settlements, and authentic instruments.[52] The EAPO Regulation defines 'judgment' as 'any judgment given by a court of a Member State'.[53] This means that an arbitral award cannot be a judgment unless an arbitral court is considered to be 'a court of a Member State'. An arbitral award is neither an authentic instrument nor a court settlement. Therefore, if an arbitral award does not fit within any of the three categories of titles, why did the District Court of Luxembourg grant the EAPO? Luxembourgish law requires arbitral awards to be declared enforceable by a court before seeking their enforcement.[54] Perhaps the District Court of Luxembourg (*Tribunal d'arrondissement de Luxembourg*) considered that the judgment declaring an arbitral award enforceable to be a 'judgment' that can be used to apply for an EAPO.[55] The influence of domestic practice on the enforcement arbitral awards might offer another explanation. Luxembourgish courts often grant

[47] Wiedemann (n 13), 111.
[48] Tribunal d'arrondissement de Luxembourg, Ordonnance du 24 septembre 2021 (unpublished).
[49] Art. 33 EAPO Regulation.
[50] Creditors can only request the revocation of the EAPO under a limited number of grounds. One of those grounds is that 'the conditions or requirements set out in this Regulation were not met', which includes that the claim the EAPO seeks to guarantee falls under the arbitration exclusion: Art. 33(1)(a) EAPO Regulation.
[51] Cour de cassation, arrêt n° 2594 du 12 février 2009, N° JUDOC: 99865114.
[52] Art. 5(b) EAPO Regulation.
[53] Art. 4(8) EAPO Regulation.
[54] Art. 1241 Luxembourgish Code of Civil Procedure (*Nouveau Code de Procedure Civil*).
[55] *Cuniberti* and *Migliorini* consider that the judgments declaring the enforceability of arbitral awards can be used to apply for the EAPO: Cuniberti and Migliorini (n 26), 31.

national attachment orders (*saisie-arrêts*) to secure the enforcement of arbitral awards. The District Court of Luxembourg (*Tribunal d'arrondissement de Luxembourg*) might have addressed the EAPO application as it would have done with a national provisional attachment order requested to secure the enforcement of an arbitral award. Regardless of the reasons that led the District Court of Luxembourg (*Tribunal d'arrondissement de Luxembourg*) to grant the EAPO based on an arbitral award, it is difficult to reconcile such a solution with the text of the EAPO Regulation.

16. Overall, case law shows that national courts seem keener towards a more limited interpretation of the arbitration exclusion than most scholars.

E. Concluding thoughts: A need to shed light on the EAPO arbitration exclusion

17. The existence of different interpretations concerning the arbitration exclusion among courts and scholars reveals that this is not a settled question and needs to be clarified. One could hope that a national court decides to submit a preliminary reference to the CJEU about this. That would allow the CJEU to address the arbitration exclusion as it was able to do with the Brussels I bis Regulation. However, considering the scarce use of the EAPO that statistics show,[56] the probability of a national court referring a question on the EAPO Regulation's arbitration exclusion is slim. Another option is that in the case of a reform of the EAPO Regulation, the EU legislator decides to include a specific provision in the Preamble explaining the boundaries of the arbitration exclusion, as was done in the Brussels I bis Regulation. Until one of these possibilities occurs, the controversy surrounding the arbitration exclusion will continue.

[56] Marco Buzzoni and Carlos Santaló Goris, *Report on practices in comparative and cross-border perspective* (2022), 64 – 65, available at: <https://efforts.unimi.it/research-outputs/reports/report-on-practices-in-comparative-and-cross-border-perspective/> accessed on 15 January 2022.

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BDO is an international network of public accounting, tax and advisory firms which perform professional services under the name of BDO.

Drumcliffe is a private investment management firm dedicated to funding and managing the recovery of stolen assets for the victims of global fraud and corruption. Their mission is to return the proceeds of crime to governments, insolvent companies, and victims while creating non-correlative returns for their investors.

Highgate is a global market leader in dispute resolution. They shape the environment outside the courtroom to help win disputes. Working with legal advisers and investigators, Highgate deploys creative and intelligence-driven strategies to bring the other side to the negotiating table.

Grant Thornton is one of the world's largest professional services networks of independent accounting and consulting member firms that provide assurance, tax and advisory services to privately held businesses, public interest entities, and public sector entities.

GreyList Trace Limited is a UK based fintech company that has developed artificial intelligence risk screening technology. Its cutting-edge proprietary algorithm software can legally and non-invasively identify any one or two-way connections between any pair of email addresses.

Mintz Group is a corporate investigations firm that gathers information before hiring, before transactions, during litigation disputes and after frauds, all over the world.

Serle Court is a leading set of barristers' chambers offering genuine expertise across a broad range of both chancery and commercial disciplines. Including commercial litigation, offshore litigation, fraud and general chancery work.

V2 Global provides risk mitigation and strategic solutions on a global scale. Focusing on the acquisition and synthesis of information, they specialise in crisis and risk management, investigatory and strategic advisory services in areas of business intelligence, cyber and data security and forensics.

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