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Fraud: There are avenues for recovery

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The latest KPMG Fraud Barometer for the UK published in January shows a record value of £1.3 billion of fraud cases reaching the courts last year. According to KPMG's figures investors and financial institutions were major victims in those cases and lost around £730 million.

The credit crunch is an undoubted cause of this rise. KPMG, rightly, consider that we are yet to see its full impact and predict that the situation is getting worse. The credit crunch has resulted in a tightening of belts in all industrial sectors and a consequence has been the uncovering and better detection of business fraud.

There is a common misconception that steps taken to recover monies are costly and will take significant time to execute. However, this is not always the case, particularly if the victim acts quickly.

There are available to the victims of any fraud both a range of targets and weapons that can be used to recover losses. If used correctly they may save time and costs. The rise in the value of fraud claims reaching the courts shows an increasing willingness by victims to identify targets and use the weapons to take steps to make a recovery.

The use of trusts is particularly helpful and can form the basis for search and freezing orders.

Claims for breach of trust or assistance in a breach of trust are one of the most important ways by which a fraud victim may be able to make a successful recovery of its losses through civil proceedings. This is because it potentially broadens the range of targets for the recovery.

Businesses or individuals who receive or hold assets for the benefit of others may owe certain fiduciary duties, a breach of which may create a constructive trust. From the point that the constructive trust exists, the business or individual who received and held the assets for the benefit of others is considered to be a constructive trustee and accountable to the beneficiaries irrespective of whether it still retains the assets or not.

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A constructive trust may arise in one of two ways:

- There must be "knowing receipt" of the assets; or
- "dishonest assistance" with the assets.



Knowing Receipt

Knowing receipt involves the receipt of property which has been disposed of in breach of a fiduciary duty. The receiver of the property must have knowledge of the breach of fiduciary duty involved in the disposal of an asset and have retained the benefit of the disposal which is traceable to the breach.

It doesn't require the recipient of the asset to behave in a dishonest manner; it merely requires knowledge of the breach.

The element of knowledge may arise from:

- Actual knowledge;
- Wilfully shutting one's eyes to the obvious;
- Wilfully and recklessly failing to make such inquiries as an honest and reasonable man would make;
- Knowledge of circumstances which would indicate the facts to an honest and reasonable man; or
- Knowledge of circumstances which would put an honest and reasonable man on inquiry.

Dishonest Assistance

This involves the business or individual dishonestly assisting a third party to breach a fiduciary duty.

The test for the state of mind involved in the dishonesty is objective and the constructive trust may be created if the business or individual fails to ask the question about the business it is being asked to conduct.

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For example in the Barlow Clowes fraud in the 1980s an individual responsible for managing accounts which he strongly suspected were being used to maintain in a fraudulent manner investors funds consciously decided not to make enquiries because he preferred in his own interest not to run the risk of discovering the truth. This was sufficient to find him liable for dishonest assistance, create the constructive trust and make him accountable for the breach as the trustee.

Search Orders

This is a key weapon in the tracing of the fraudster's assets. Its objective is to prevent the fraudster from destroying incriminating evidence regarding the commission of the fraud and the concealment of its proceeds.

It is an order that is made on a without notice application and requires the permission of the court to enter premises to search and remove evidence before the fraudster has had an opportunity to put his side of the case to the court.

It is a draconian order and could cause serious damage to the defendant's reputation. Accordingly, the court will not make such an order unless it is satisfied that:

- The applicant has an extremely strong prima facie claim;
- The potential or actual damage to the applicant arising from the claim is very serious;
- The defendant has possession of incriminating evidence and there is a real possibility that it will destroy or tamper with that evidence; and
- The harm likely to be caused to the defendant by such an order is not disproportionately excessive to the legitimate object of the order.

Computers and other electronic devices, such as mobile phones, blackberries, lap tops, are often the most fruitful source of incriminating evidence especially where the fraudster is under the impression that he has deleted such information from these devices. The terms of a search order may therefore allow computer forensic experts to partake and take an image of the hard drive of any computer or any other electronic device found in the search.

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Accordingly a search order can be extremely useful for the purposes of gathering evidence to support the applicant's claim but, more importantly in tracing and identifying the proceeds of the fraud and assets of the fraudster for the purpose of policing a freezing order.



Freezing Orders

This is one of the key weapons in securing the proceeds of the fraud and the assets of the fraudster.

The UK courts are willing to freeze assets held nationally and internationally, and by individuals or businesses other than the fraudster provided they can be shown to have been obtained using the fraudster's assets and the proceeds of the fraud.

A freezing order prevents the defendant from dealing with his assets or taking steps to remove his assets from the UK or any foreign jurisdiction where the court gives the applicant permission to enforce the terms of the order.

The conditions that have to be satisfied for the purposes of obtaining such an order are as follows:

- The applicant must have a good arguable claim;
- There is a real risk that the defendant will dissipate the assets; and
- Full disclosure of all relevant facts;

If the freezing order is to apply to and be enforced against assets in a foreign jurisdiction, the court will have to be satisfied that:

- The granting of permission to enforce a worldwide freezing order abroad is just, convenient and not oppressive;
- The interests of all parties, including those likely to be joined to the foreign proceedings are balanced against each other; and
- The relief to be obtained in the foreign jurisdiction will not be superior to that given by the worldwide freezing order.

Third Party Disclosure Orders

Another key weapon in effective asset recovery is the early identification of assets. If the freezing order is to be effective the victim will need to have identified the assets, so far as is possible, beforehand. A search order is likely to produce the relevant information. However, there are other tools available,

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particularly disclosure orders against third parties, which can be used for the purposes of establishing the whereabouts and value of the defendant's assets without notice to him which can then be frozen by the Freezing Order. It is the combination of Freezing, Search and Third Party Disclosure Orders that provides such an effective international remedy for victims of fraud.

Whilst a consequence of the credit crunch has been the increase in the uncovering of business fraud, which is likely to continue in the foreseeable future, the tools are available for making successful recovery. It is clear from the increase in the fraud cases being brought to the courts that victims are prepared to use them. However the prospects of using them successfully increase if the victim acts quickly and uses them correctly in its particular circumstance.



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