Civil and Criminal Asset Forfeiture

Issues of Default and Enforcement for Yacht Loan Agreements

Civil and Criminal Asset forfeiture relative to "In Rem" claims against vessels has a rich history in British Maritime law (Navigation Act 1660). The US Supreme Court came to embrace the concept when Majority Opinion, Associate Justice Joseph Story asserted in US v. Schooner Amistad, 40 US (15 Pet) 518 (1841):

> (A) vessel which commits the aggression is treated as the offender, as the guilty instrument or thing to which the forfeiture attaches, without any reference whatsoever to the character or conduct of the owner. (The seizure of the ship is justified by ...) the necessity of the case, as the only adequate means of suppressing the offense or wrong or insuring an indemnity to the injured party.

The reach of civil and criminal forfeiture further expanded into US law during "Prohibition Years" (1920-1933) with a celebrated period of confiscations of property, whiskey and yachts from bootleggers and mariners alike. The 1980's brought to the forefront once again the use of civil and criminal forfeitures as a weapon against the War on Drugs in the US. (Comprehensive Crime Control Act of 1984).

Today, Criminal and Civil forfeitures have become quite lucrative for authorities netting billions each year, as reported by the US Treasury and therefore are here to stay at least for a while.

The standards of proof between civil and criminal forfeiture vary from a "preponderance of evidence" to "beyond a reasonable doubt" and vary State to State. Thereafter, it gets much more complicated with an asset forfeiture as to what authority is asserting the claim and the nexus of the seized property as to the "fruits" of the criminal activity.

The concept of innocent owner defense surfaced with The Civil Asset Forfeiture Reform Act of 2000, 18 USC Sec 983(d) et sec ("CARFA").

Today, in criminal forfeiture cases, a third party who gets an interest in the forfeited property after the act giving rise to the forfeiture must show that he/she had no reason to know that the property was involved in a crime committed by another person. Thus, if the third party knows, at the time he/she acquires their interest in the property, that the previous owner of the property used it to commit a crime or was *accused* of having used the property to commit a crime, the third party cannot challenge the forfeiture as a bona fide purchaser. US v. Sokolow 1996 WL 32113 (E.D. PA. 1996).

It is immaterial whether the third party became aware of the taint on the property from first-hand knowledge, from reports in the media, or because the property was named in an indictment, *lis pendens*, restraining order, or some other action by the government. If the

information available to the third party would have put a reasonable person on notice that the property was subject to forfeiture, he/she cannot claim to be a bona fide purchaser.

In Re: Moffitt, Zwerling & Kemler, 846 F.Supp.463 (E.D. Va. 1994)

Current high-profile forfeitures involving the US Department of Justice and foreign nations actively collaborating in the civil and criminal forfeiture claims target prominent yachts of note:

1. 65m Heesen "Galactica Star" launched 2013 was taken into custody by the US government together with the Federal Republic of Nigeria asserting the proceeds used to purchase the yacht were proceeds of embezzlement of Nigerian treasury funds. Upon information and belief is being offered for sale pursuant to a judicial interlocutory sale (sealed bid May 19, 2019).

2. Cayman flagged Oceanco 91.5 motor yacht "Equanimity" impounded by Indonesia in a multi-billion-dollar corruption investigation by Malaysian financier Jho Low and subject to ongoing proceedings in US Courts.

For the marine lender, asset forfeiture claims asserted against one of its secured assets with (Preferred Ship's Mortgage) presents a host of complex issues which must be carefully examined on a case by case basis. Moreover, it may not always be clear if a cloud or threat of asset forfeiture constitutes an actionable default under a loan agreement for a marine lender's secured asset. Therefore, a lender must be exacting before asserting a default when the cloud of an asset forfeiture is presented for a vessel or borrower.

A sample "Default" clause may typically include the following language in a Marine Loan Agreement:

Events of Default. Grantor shall be in default under this Agreement, if, prior to the time that the full amount of the Obligations is completely paid, any one or more of the following events (each, an "Event of Default") occurs:

a. any receivership, bankruptcy, insolvency or similar proceedings, or any assignment for the benefit of creditors, shall be instituted by or against Grantor or Guarantor;

b. the Vessel shall be arrested, attached, levied upon, seized, or made the subject of any legal proceedings, including any civil or criminal forfeiture proceedings, or held by virtue of any lien or distress, or any notice of claim of lien on the Vessel is filed with the U.S. Coast Guard or any other applicable authority;

c. Grantor has made any false or misleading statement to Bank about any fact, including but not limited to, those in this Agreement, the Preferred Mortgage or the application for credit;

d. any other event occurs that Bank in good faith reasonably believes endangers Grantor's ability to timely pay any sum due under this Agreement or the Preferred Mortgage; or
e. any other event occurs that Bank in good faith reasonably believes jeopardizes or impairs the value of the Collateral or Bank's ability to realize that value in a foreclosure.

Let us consider a fictional set of facts whereby a beneficial owner of a single purpose entity owning a vessel is indicted for securities violations by the US Department of Justice. The vessel is subject to a loan agreement with a lender secured by a First Preferred Ship's Mortgage for amounts advanced for the purchase of the vessel at arm's length for fair and reasonable consideration the same year of alleged crime. The indictment and public notice of the same comes two years after the vessel purchase. Vessel owner has in every respect made punctual payments for the loan and now wishes to sell the vessel.

The cloud of the indictment clearly gives rise a "threat of forfeiture." Any third-party purchaser is now on notice of the indictment, and therefore is presumed not eligible for the innocent owner defense. The lender may be eligible to assert an innocent owner defense likely with presumed priority in claim pursuant to First Preferred Ship's Mortgage over any threatened asset forfeiture claim by state or federal authorities.

Is this grounds for the lender to assert a default based upon an event that the "Bank in good faith reasonably believes jeopardizes or impairs the value of the Collateral or Bank's ability to realize that value in a foreclosure?"

The "impaired value default" may not be so clear-cut as an event of Default if you consider the remedy to the Lender is foreclosure by the Preferred Ships Mortgage by way of Marshal sale. Faced with the prospect that a judicial sale of the Vessel will yield a lesser return than a commercial sale, both the Lender and borrower share in such downside. The further threat that any deficiency resulting in a judicial sale from the Guarantor is now inflamed by the indictment and asset forfeiture action. Gone are CARFA innocent owner defenses for the lender post foreclosure of the yacht in this scenario.

Does the borrower have a legitimate defense there is no default in this case above? If for example the borrower asserts the triggering of a default by the Lender based on a cloud of forfeiture actually jeopardizes or impairs the value of the vessel based on the expectation that a judicial sale or forced sale will render significantly less value for the vessel than a bargained for sale of the vessel, is this the basis of a counterclaim and damages or waiver of deficiency for the borrower?

Asset Forfeiture has become increasingly complicated for the marine lender, when the headlines everyday bring us news of more indictments in the financial world and beyond. The alarming rise in forfeiture claims and everyday use of indictments could bring pause to the

growth of the superyacht fleet. Forcing the hand of collateral disposal for a lender after an asset forfeiture starts is tricky business.

David Bohonnon

Bohonnon Law Firm, LLC

The information offered in this article is a summary in nature and should not be considered a legal opinion. David Bohonnon is a partner in the Bohonnon Law Firm, LLC., which practices extensively in Marine and Admiralty matters. Further questions may be directed to David Bohonnon at the Bohonnon Law Firm (www.bohonnon.com), (203)787-2151.