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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

UNITED STATES OF AMERICA,
Plaintiff,
vs.
\$175,982.21 IN U.S. CURRENCY,
Defendant

CASE NO. 2:11-cv-08852-CBM (JCx)
FINDINGS OF FACT AND
CONCLUSIONS OF LAW
AFTER BENCH TRIAL

I. PROCEDURAL OVERVIEW

The Court, having previously made findings that the government has met its initial burden of probable cause to institute seizure and that by a preponderance of the evidence that the property is subject to forfeiture, held a bench trial on the issue of whether Claimants have made out an “innocent ownership” defense by a preponderance of the evidence. [Docket No. 56 at 6:23-7:1.]

II. FINDINGS OF FACT

A. Internal Revenue Service Investigation

1. Claimant Kristian Kratz (“Kratz”) has owned and operated the business known as Pacific Coast Hydroponics, Inc. (“PCH”) since 2005. (Exh. 22.) PCH

1 sells equipment utilized for the indoor cultivation of plants, including marijuana.
2 PCH's customers prefer to pay for their purchases with cash.

3 2. As part of an investigation by the Internal Revenue Service, IRS
4 investigators executed search warrants on Mr. Kratz' business premises and his
5 residence on June 3, 2011. At Mr. Kratz' home IRS investigators found
6 \$175,982.21 in U.S. currency in the master bedroom and found an indoor
7 marijuana grow in a detached garage and shed behind the house. The currency was
8 located as follows: \$5,030.00 on top of a dresser in the master bedroom;
9 \$138,413.00 in a safe located inside of the closet in the master bedroom; and
10 \$32,539.21 leaning against the safe. (Pre-Trial Conference Order ("PTCO") at
11 2:25-3:5.)

12 3. The Drug Enforcement Administration was contacted for assistance and
13 DEA Special Agents seized approximately 36 marijuana root bulbs growing in the
14 shed on Kratz' property (weighing approximately 8.46 kilograms), approximately
15 70 marijuana root bulbs growing inside the garage (weighing approximately 2.80
16 kilograms), and approximately 3.53 kilograms of dried marijuana, also found in
17 the garage. (PTCO at 3:6-12.)

18 4. No paraphernalia related to the distribution or use of marijuana, including
19 scales, packaging materials, baggies, customer lists, shipment or delivery records,
20 cash counting machines, was found on the premises.

21 5. The IRS later dropped its investigation of Mr. Kratz and his business.
22 (PTCO at 3:17-18).

23 6. On February 8, 2013, the government moved to dismiss, with prejudice,
24 \$32,539.21 of the defendant currency. [Doc. No. 64.] On February 14, 2013, the
25 Court ordered that amount be dismissed, and indicated that the government seeks
26 to forfeit the remaining \$143,443.00 of defendant currency. [Doc. No. 68.]
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i. Claimant's Business and Tax Records

1 7. PCH makes large cash deposits weekly to the bank and keeps the remaining
2 cash on hand. (PTCO at 3:20-3:23.)

3 8. All cash payments received from PCH customers are recorded by cash
4 registers at PCH's store and reported through "Z Reports" on a daily basis, (Exh.
5 32), and then reported as "Tender Received - Cash" in the S01 Cash Report, (Exh.
6 33). Kratz testified that he takes the daily cash receipts to his residence, where he
7 has a safe. Kratz then prepares the cash sales for deposit to PCH's bank account
8 and takes the cash to the bank more or less on a weekly basis. (*See also* Exhs. 28,
9 30.)

10 9. Kratz's bank records for his California Bank & Trust "Calbank Business
11 Adv" Account lists the account owner as "Pacific Coast Hydroponics," which
12 Claimant testified is his primary account, shows that from February 1, 2010
13 through December 31, 2010, he made total cash deposits of \$1,598,477.10. (*See*
14 Exh. 28.) Claimant's bank records also show that he made cash deposits to that
15 account totaling \$683,347.83 from January 1, 2011 through June 3, 2011. (*See*
16 Exh. 30.) Therefore, from February 1, 2010 through June 3, 2011, he made total
17 cash deposits to his account in the amount of \$2,281,824.93.¹

18 10. A "Quick Report," Exhibit 29, which is a report generated by Claimant's
19 business accounting software and are prepared by Claimant, shows a total of
20 \$2,034,518.33 in cash deposits to the bank for February 1, 2010 through June 3,
21 2011.² (*See* Exh. 29.)

22 11. At trial, Claimant testified that the "Quick Reports" (Exh. 29) directly
23 correspond with the California Bank & Trust statements (Exhs. 28, 30). However,
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26 ¹ The Claimant testified that the total cash received from his business minus the cash deposited
27 in his bank between July 16, 2009 and May 22, 2011 accounts for the currency found at his
28 home. However, the California Bank & Trust business account statements begin at February
2010, not July 2009.

² Exhibit 29 covers the period between July 16, 2009 and May 22, 2011.

1 there is a difference between the amount transferred to the bank as indicated in the
2 Quick Reports and the cash deposited in California Bank & Trust account for
3 February 1, 2010 through June 3, 2011:

\$2,281,824.93 Cash Deposits from Bank Statements
- <u>\$2,034,518.33</u> Cash Deposits from Quick Report, Exh. 29
= \$ 247,306.60

7 12. Exhibit 33 is a Quick Report that shows PCH's sales between July 15, 2009
8 and June 2, 2011. This Quick Report shows that between February 1, 2010
9 through June 2, 2011, PCH made cash sales in the amount of \$2,191,353.40. (*See*
10 Exh. 33.) The total deposits in the bank account as reflected in the Bank
11 statements for the same period are \$2,281,824.93. (*See* Exhs. 28 & 30.)

12 13. PCH reported cash assets of \$459,286 at the end of the year on its 2009 tax
13 return. (Exh. 24, at 345, line 1(d)). Claimant Kratz testified that this amount
14 constitutes money in his bank accounts and also money on hand at the end of
15 2009. Claimant had a bank balance of \$291,705.09 as of December 31, 2009 (*Id.*
16 at 344). The difference between the cash assets and the bank balance as of
17 December 31, 2009, which is the amount of cash on hand:

\$459,286.00 Cash Assets at end of 2009
- <u>\$291,705.09</u> Bank Balance at end of 2009
= \$167,580.91 Cash on Hand at end of 2009

21 14. Parties stipulated that during 2010, Pacific Coast deposited \$1,614,344.24
22 cash in its bank account and reported another \$86,560.88 in cash sales that were
23 not deposited in its bank account. (PTCO at 3:26-4:1.)

24 15. For the year ending December 31, 2010, PCH reported to the IRS that it
25 earned ordinary business income of \$395,704 on gross sales of \$2,305,473, and
26 had cash assets of \$372,187. (PTCO at 3:23-4:1.)

27 16. Claimant Kratz testified that the cash assets on the 2010 tax return
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1 constituted the money in his bank accounts and also the money in cash at the end
2 of 2010. Claimant had a bank balance of \$133,035.63 as of December 31, 2010
3 (Exh. 28). The difference between the amount in Claimant's bank account and
4 cash assets as reported to the IRS, which is the amount of cash that Claimant had
5 on hand as of the end of 2010 is:

\$372,187.00	Cash assets at end of 2010
-	<u>\$133,035.63</u> Bank balance at end of 2010
=	\$239,151.37 Amount of cash at end of 2010

9 17. The Court finds that there is a discrepancy between the amount of cash on
10 hand at the end of 2010 that parties stipulated to (\$86,560.88) and the amount
11 calculated (\$239,151.37). The Court will rely upon the stipulated figure for any
12 further calculations.

13 18. From January 1, 2011 to June 2, 2011, Claimant reported \$626,214.20 in
14 cash sales from PCH. (See Exh. 33.) During the same period, Claimant deposited
15 \$683,347.83 in the bank. (See Exhs. 28, 30.)

16 19. Using the stipulated amount, \$86,560.88, and adding it to the amount of
17 cash sales as of June 2, 2011, \$626,214.20, less the amount deposited in the bank
18 equals the amount of cash on hand as of June 2, 2011:

\$ 86,560.88	Stipulated amount at the end of 2010
+ <u>\$626,214.20</u>	Cash Sales between Jan. and June 2, 2011
= \$712,775.08	
- <u>\$683,347.83</u>	Cash deposits made between Jan. and June 2, 2011
29,427.25	Amount of cash on hand as of June 2, 2011

24 20. Kratz refused to answer questions regarding the indoor marijuana grow on
25 his property, invoking Fifth Amendment protections. These questions included
26 whether Claimant was growing marijuana at his home on the day of the IRS
27 search or anytime between 2009 and 2011, and the nature of the marijuana grow
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1 found at his home.

2 21. Kratz testified under oath that he did not sell marijuana between 2009 and
3 2011, which includes the period immediately preceding the IRS investigation of
4 Claimant's home.

5 22. At trial, the government offered into evidence a note by Claimant. (*See* Exh.
6 17.) Kratz testified that he recognized the note and that the line "get house @
7 2K/month and grow" means to grow as a person and that he had a garden.
8 Additionally, Kratz testified that the reference to "seeds" refers to seeds for
9 vegetables such as tomatoes, which Kratz testified he grows in his garden.

10 23. The government questioned Claimant about Exhibit 18, a note written by
11 Kratz and prepared eight years ago. He responded to questions regarding the
12 meaning of the phrase "need safe address to receive mail and packages," by
13 answering that he needed a secure location to receive the expensive equipment
14 that PCH sells. The Court finds Kratz's responses to questions regarding both
15 Notes to be credible.

16 III. CONCLUSIONS OF LAW

17 24. The facts, insofar as they may be conclusions of law, are hereby
18 incorporated by reference.

19 25. CAFRA, 18 U.S.C. § 983, governs forfeiture proceedings commenced after
20 its effective date, August 23, 2000. This applies to actions instituted pursuant to
21 21 U.S.C. § 881(a)(6) and 18 U.S.C. § 983(c). *See* 18 U.S.C. § 983(i)(1).

22 26. 21 U.S.C. § 881(a)(6) provides for the forfeiture of "[a]ll moneys...or
23 other things of value furnished, or intended to be furnished by any person in
24 exchange for a controlled substance...all proceeds traceable to such an exchange,
25 and all moneys...used or intended to be used to facilitate any violation of this
26 subchapter."

27 27. 18 U.S.C. § 981(a)(1)(C) provides for the forfeiture of "[a]ny property,
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1 real or personal, which constitutes or is derived from proceeds traceable to...any
2 offense constituting ‘specified unlawful activity’... or a conspiracy to commit
3 such offense.” “The government may... institute a forfeiture action if it can
4 demonstrate probable cause for doing so, based upon untainted evidence.” *United*
5 *States v. \$186,416.00 in U.S. Currency*, 590 F.3d 942, 948 (9th Cir. 2010) (citing
6 *United States v. \$493,850.00 in U.S. Currency*, 518 F.3d 1159, 1169 (9th Cir.
7 2008)).

8 28. The Ninth Circuit uses the “aggregate of the facts test” to determine
9 whether the government has the requisite probable cause to institute forfeiture.
10 *United States v. Currency, U.S. \$42,500.00*, 283 F.3d 977, 980-82 (9th Cir. 2002).
11 Under this test, the government has met its burden if “the aggregate of facts gives
12 rise to more than mere suspicion that the property was exchanged for or intended
13 to be exchanged for drugs.” *United States v. \$5,644,540.00 in U.S. Currency*, 799
14 F.2d 1357, 1363 (9th Cir. 1986). The presence or absence of any single fact is not
15 dispositive. *Id.* The Government may rely on circumstantial evidence to meet its
16 burden. *United States v. Real Prop. Located at 22 Santa Barbara Drive*, 264 F.3d
17 860, 872 (9th Cir. 2001).

18 29. After meeting this initial burden, “the burden of proof is on the Government
19 to establish, by a preponderance of the evidence, that the property is subject to
20 forfeiture.” 18 U.S.C. § 983(c)(1). The government may rely on evidence used in
21 supporting probable cause, as well as additional evidence gathered after the filing
22 of the complaint. *See \$493,850.00 in U.S. Currency*, 518 F.3d at 1170 (citing 18
23 U.S.C. § 983(c)(2)).

24 30. Once the Government has met the burden of probable cause to institute the
25 proceeding, and has met the burden of preponderance of the evidence that the
26 assets are subject to forfeiture at trial, only then does the burden shift to the
27 claimant to show that he is an “innocent owner” by a preponderance of the
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1 evidence. 518 F.3d at 1170; 18 U.S.C. § 983(d).

2 31. An innocent owner defense is an affirmative defense in which the claimant
3 bears the burden of proving that he is an innocent owner by a preponderance of
4 the evidence that the owner who either “did not know of the conduct giving rise to
5 forfeiture” or “upon learning of the conduct giving rise to the forfeiture, did all
6 that reasonably could be expected under the circumstances to terminate such use
7 of the property.” 18 U.S.C. § 983(d); 518 F.3d at 1170.

8 32. The law of the Ninth Circuit states that where the claimant proves, by a
9 preponderance of the evidence, “an alternate theory of origin for the currency,” he
10 has shown an innocent owner defense. 518 F.3d at 1170.

11 33. Claimant asserts that he is an innocent owner because the currency comes
12 from a legitimate source, his hydroponics business, and thus offers an “alternate
13 theory of origin for the currency.” 518 F.3d at 1170.

14 34. The Court received into evidence Quick Reports and bank statements
15 indicating that some of the defendant currency came from a legitimate business.

- 16 ○ Exhibit 29, PCH’s internal accounting “Quick Reports” showing cash
17 deposits made to the bank, is given less weight. (*See* Finding #11.) The
18 Court gives more weight to the California Bank & Trust Statements,
19 (Exhs. 28, 30), which cover the period of February 2010 through July
20 2011. Due to this difference, the Court relied on the bank statements.
- 21 ○ The Court compared the bank account statements with the cash received
22 from cash sales at PCH for February 2010 through July 2011. Parties had
23 previously stipulated that Claimant had \$86,560.88 of cash on hand at the
24 end of 2010. As calculated in Finding #19, Claimant had \$29,427.25 in
25 cash from a legitimate source as of the date of the seizure, June 2, 2011.

26 35. Claimant testified that some of the currency came from the legitimate
27 business, as follows.

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- 1 ○ That it was his practice to keep un-deposited cash in his safe at home
- 2 from his cash-intensive business;
- 3 ○ That he would not deposit all of the cash from his business because he
- 4 would be charged for deposits to his bank account in excess of a certain
- 5 amount;
- 6 ○ That he did not engage in the sale of marijuana during the relevant time
- 7 period;

8 36. The Court finds Claimant has shown by a preponderance of the evidence, of
9 a legitimate source for some of the currency found at his home. The Court further
10 finds that Claimant has satisfied its burden of proof as to an “alternate theory of
11 origin” for the \$29,427.25 of the Defendant currency the government seeks to
12 forfeit. *\$493,850.00 in U.S. Currency*, 518 F.3d at 1170.

13 37. The Court will also not draw an adverse inference from Claimant’s
14 invocation of the Fifth Amendment since he may be the subject of a future
15 criminal investigation. Although Claimant has been informed that he is no longer
16 the subject of a criminal investigation regarding federal tax liabilities, the
17 Government has not indicated whether Kratz is the subject of a future criminal
18 investigation regarding the marijuana at his home. *See U.S. v. Bodwell*, 66 F.3d
19 1000, 1001 (9th Cir. 1995).

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1 The Court finds, therefore, that Claimant has met his burden as to the
2 “innocent owner” defense and therefore the Government improperly forfeited
3 \$29,427.25 of the Defendant Currency obtained from Claimant’s home, and is
4 hereby ordered to return that amount with interest to claimant. The Government
5 therefore properly forfeited the remaining \$114,015.75 of the Defendant Currency.
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7 **IT IS SO ORDERED.**



8 DATED: August 14, 2013

CONSUELO B. MARSHALL

UNITED STATES DISTRICT JUDGE

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