

# Hong Kong Court Finds Police Action to Freeze Bank Accounts Unlawful

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In a significant legal development, the Hong Kong Police's practice of issuing "*letters of no consent*" to informally freeze suspicious funds was held to be unlawful by the Hong Kong court in a judgment handed down in December 2021.

In this update, we:

- take a look at the reasons given by the Court that the practice of issuing "letters of no consent" lacks a legal basis; and
- consider how this judgment impacts businesses (in particular financial institutions) that face money-laundering risk in the course of business.

## RE-CAP OF THE "NO CONSENT" REGIME

Under Hong Kong law, where a person suspects or knows that property (i.e. money) represents the proceeds of an indictable offence (i.e. the proceeds of crime), they are required to report the suspicion to law enforcement agencies. Such Suspicious Transaction Reports ("STRs") are typically filed with the Joint Financial Intelligence Unit of the Hong Kong Police. Once a suspicion has been formed, it is an offence to deal in the relevant suspicious funds save for where the reporting party is given consent to deal in the funds by the Police.<sup>1</sup>

In the context of this legislative framework, the Hong Kong Police developed a practice of responding to STRs by issuing a letter to the reporting party either giving consent to deal in the funds, or giving "no consent" where an investigation was pending. Where a reporting party received a letter of no consent ("LNC"), the funds would effectively remain frozen until further notice by the Police. This practice has now been held to be unlawful.

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<sup>1</sup> See sections 25 and 25A of the Organized and Serious Crimes Ordinance (Cap. 455) ("OSCO").

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**THE DECISION IN *TAM SZE LEUNG & ORS V. COMMISSIONER OF POLICE* [2021] HKCFI 3118**

By way of factual background, the applicants in [Tam Sze Leung](#) were subject to an investigation by the Securities and Futures Commission (“SFC”) for suspected stock market manipulation. The SFC referred the matter to the Police for an investigation of suspected money laundering. As a result, the Police alerted the relevant banks of the investigation and directed the banks to file STRs and LNCs were subsequently issued by the Police.

In a judicial review, the applicants challenged the legality of the No Consent regime on six grounds, of which three were accepted by the Court. We summarise these below:

**Ground 2: The Operation of the No-Consent Regime Is Ultra Vires**

The judge (Coleman J) considered whether sections 25 and 25A of OSCO empowered the Police to informally freeze assets. The judge decided that, where OSCO provides other express freezing powers, such as a restraint order and confiscation order, section 25A of OSCO was not intended to empower the Police to operate the No Consent Regime as an “*informal freezing regime*”. In reaching this decision, the judge also took into account the peculiarity in cases such as the present one, in which the financial institutions had no knowledge or reason to file STRs if not for the Police informing them of their investigation, leading to the LNCs being issued and eventual freezing of the accounts.

In the absence of a statutory basis to freeze assets, the Police were acting beyond their powers (“ultra vires”).

**Ground 3: The No-Consent Regime Is Not Prescribed by Law**

On the flip-side to the Police acting beyond their powers (ultra vires), the Court also held that:

- OSCO does not provide sufficient clarity as to the scope of the power and the manner of the No Consent regime which could adequately be accessible and formulated with sufficient precision to enable citizens to regulate their conduct; and
- the law does not currently provide adequate effective safeguards against abuse.

In making this finding, the court took account of the fact that there was a lack of clarity in relation to the No Consent regime in the Police’s own procedural manual and that the failure to adhere to the Police procedural manual by individuals was an indication of the

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“systemic problems” with the No Consent regime. The judge was also unconvinced that civil proceedings by persons whose property is affected by LNC against financial institutions are an appropriate remedy or safeguard against such Police action.

#### **Ground 5: The Operation of the No-Consent Regime Is Disproportionate**

As with other common-law jurisdictions, decisions and actions by the government are subject to a well-established proportionality test. This public law doctrine was upheld and developed by the Court of Final Appeal in the case of *Hysan*<sup>2</sup>, which also concerned the government’s duty to protect private ownership rights.

In the present case, the applicants argued that the No Consent regime resulted in an indefinite and disproportionate interference with fundamental rights, lacks a clear scope of power, and most critically lacks proper safeguards against abuse.

In considering the proportionality of the No Consent regime, the Court accepted that the practice had a legitimate purpose of deterring criminal activity, but the Police had “myriad alternatives” to take a proactive role in combatting money laundering. In finding that the No Consent regime failed the proportionality test, the Court found that it operated “without temporal limitation yet with only internal intermittent review of justification” with the judge observing “I do not think that a reasonable balance has been struck between the societal benefits of the encroachment and the inroads made into the constitutionally protected rights of the individual, asking in particular whether pursuit of the societal interest results in an unacceptably harsh burden on the individual”.

#### **IMPLICATIONS OF THE DECISION**

At a time when the rule of law in Hong Kong has been the subject of widespread media commentary, this decision is a welcome example of the individuals’ rights and freedoms protected under the Basic Law being upheld by the courts.

Further, subject to the decision being successfully appealed, the ruling has several practical implications for businesses that routinely file STRs, particularly financial institutions:

- Historically, where a financial institution has submitted an STR, it has been able to rely on LNCs to protect themselves from complaints by customers.

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<sup>2</sup> *Hysan Development Co Ltd and Others v Town Planning Board* (FACV 21/2015).

- The number of STRs submitted to the JFIU has been on a general upward trend (37,188 in 2014 to 51,832 in 2021) of which the vast majority were filed by financial institutions. The JFIU has previously commented that some STRs were of a “lower quality” and lacked a rigorous assessment of whether there were grounds to suspect the funds that were the subject of the STR were the proceeds of crime.
- The decision in *Tam Sze Leung* does not change the requirements under OSCO to report knowledge or suspicion that funds represent the proceeds of crime or the statutory prohibition on dealing in suspicious funds. However, financial institutions will no longer be able to rely on LNCs to protect themselves from not complying with a customer’s instructions to transfer funds. If a financial institution fails to comply with a customer’s instructions and lacks a proper basis to suspect that the relevant funds are illegitimate, the financial institution could be subject to complaints or claims for breach of the customer contract.
- Accordingly, businesses that routinely file STRs may wish to review the following:
  - Internal procedures for determining whether there are sufficient grounds for filing an STR to ensure that the process is sufficiently rigorous and any decision to not comply with a customer’s instructions can be defended. Any decisions to decline executing customer instructions should be reviewed periodically.
  - Record-keeping policies to ensure that a paper-trail is kept to evidence decisions to file STRs and not comply with customer instructions.
  - Customer contracts to ensure that there is sufficient discretion to decline executing customer instructions where a determination has been made that the funds are suspicious.

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Please do not hesitate to contact us with any questions.

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