

Shah v. HSBC – Potential Liability for Reporting Money Laundering Suspicions

Part 1



The recent case of **Shah & Anor v. HSBC Private Bank (UK) Ltd [2010] EWCA Civ 31** may have some unsettling implications for the financial community, as organisations may not be afforded protection against later civil action where they report suspicions of money laundering. The full implications of the judgment are yet to be determined and whether a bank will ultimately be accountable to its customer for the loss alleged to be suffered from making the suspicious activity reports must await the outcome of the trial.

Brief Summary of the Case

Mr Shah sought damages against his bank, HSBC, for breaches of duty and failure to follow his instructions to process transactions whilst requests for consent under the Proceeds of Crime Act 2002 were pending with the Serious Organised Crime Agency (“SOCA”).

Mr Shah and his wife banked with HSBC and were based in Zimbabwe. HSBC suspected that the funds in the account were proceeds of crime and on four occasions HSBC sought the consent of SOCA prior to processing transfer requests out of the account.

The explanation given by HSBC to Mr Shah for the delay in processing the payments was that it was “complying with its UK statutory obligations”. When Mr Shah advised one of the intended recipients of funds of this reason for delay, rumours spread that he was suspected of money laundering in the UK. Following a meeting with the head of

HSBC’s African department in November 2006 at which Mr Shah was advised that there had been investigations into Mr Shah’s affairs but that they were at an end, Mr Shah requested details of HSBC’s communications with SOCA which was refused. As a result of this refusal to provide details, Mr Shah alleged that he was unable to provide an explanation of the investigations to the Zimbabwean authorities who first froze and then seized his investments allegedly resulting in losses of over US\$300million.

Mr Shah issued proceedings against HSBC alleging breach of duty by not complying with his instructions and failing to provide information to which he was entitled, resulting in the alleged losses. HSBC argued that it would have committed criminal offences had it effected the transfers whilst there were suspicions of money laundering.

Mr Shah further alleged that the suspicions were irrational, negligently self-induced and mistaken and required HSBC to prove that it had a suspicion.

HSBC applied to strike out or seek summary judgment in respect of the claim. At first instance, on 26 January 2009, HSBC was successful in its application for summary judgment. Hamblen J dismissed all of Mr Shah’s claims.

Mr Shah appealed. He was partly successful. By its judgment dated 4 February 2010 the Court of Appeal summary judgment was set aside on 10 December 2009. Mr Shah had asserted on appeal that the claim was not sufficiently straightforward to be

summarily dismissed. He also alleged that HSBC had failed to make the reports to SOCA as soon as reasonably possible. HSBC resisted the appeal arguing that to obtain summary judgment it was sufficient to put in evidence facts sworn by a solicitor, or alternatively, that the court would not expect a bank to produce witnesses to give evidence regarding the suspicion and so a trial on the issue would be pointless as judgment would always be given in favour of the bank.

The Court of Appeal allowed Mr Shah's appeal in part but it is important to note that the judgment only considered whether Mr Shah's case was sufficiently arguable to be allowed to proceed to trial. The question of HSBC's liability, if any, would be dealt with then.

The Decision

The Court of Appeal recognised that banks are in an “unenviable” position. On the one hand they face the risk of prosecution for failing to report suspicions or proceeding without consent and on the other they risk being sued by their customers for failing to carry out their instructions. It was however made clear that the normal court procedures were “not to be sidestepped merely because Parliament has enacted stringent measures to inhibit the notorious evil of money laundering...”

The Court stated that “any claim by a customer that his bank has not executed his instructions is, on the face of it, a strong claim if the instructions have not, in fact, been executed... It is only when the bank says that it suspects the customer was money laundering that any defence to the claim begins to emerge”. It went on to say that there is no reason why the bank should not be required to prove the fact of suspicion in the ordinary way at trial by way of disclosure initially and then by calling either primary or secondary evidence from the relevant witnesses. There is a danger of injustice in deciding cases without appropriate disclosure and cross-examination.

The Court affirmed previous authorities¹ as to the meaning of the word “suspect” and its affiliates. The essential element in these concepts is “the Defendant

must think there is a possibility, which is more than fanciful, that the relevant facts exist. A vague feeling of unease would not suffice. But the statute does not require the suspicion to be ‘clear’ or ‘firmly grounded and targeted on specific facts’ or based on ‘reasonable grounds’.”

A bank will have a good defence if it actually had suspicion.

The Court also confirmed that, in principle, undue delay in making a report could be a breach of a banker's duty of care.

The judgment suggests that, as agent for Mr Shah, HSBC was obliged to consider its competing duties in relation to providing information to the customer regarding suspicious activity reports and tipping off concerns, particularly where the customer was requesting information. It was stated that there must arguably come a time when a customer is entitled to have more information about the conduct of his affairs. A blanket prohibition on the provision of information about suspicious activity reports is open to challenge. Plainly to permit such a prohibition would prevent a claimant from establishing whether an entity was acting lawfully and within the constraints of the legislation.

The Court did deal with other tipping off issues. It was held that, in the context of non-summary proceedings, tipping off issues were unlikely to continue to be relevant by the time of trial and that it would almost certainly be known at that stage whether disclosure by evidence in those proceedings would prejudice any investigation which was in fact taking place or contemplated. It was said that in those circumstances, it was appropriate for the bank and not merely its solicitor, to give direct evidence of its suspicions.

The Implications of the Court of Appeal Judgment

1. A bank facing a claim for failure to carry out a customer's instructions has a valid defence if it held a suspicion of money laundering and made a disclosure seeking consent (from SOCA in the UK and the Financial Crime Unit in the Isle of Man). However, the bank may be required to prove that it held the relevant suspicions.

¹ Rv Da Silva [2007] 1 WLR 303 and K Ltd v National Westminster Bank Ltd [2007] 1 WLR 311

2. Proof is only required of the fact of the suspicion. Provided that suspicion is not fanciful, the rationality of the belief should be irrelevant, as will be any assertions that it is negligently self-induced or mistaken.
3. This decision highlights the importance of having appropriate systems in place so that any suspicions that lead to suspicious activity reports are well documented.
4. Organisations making suspicious activity reports should ensure that they are made promptly or risk liability for any delay. In this particular case a two day period was thought to be reasonable.
5. An organisation cannot rely on tipping off concerns once there is no risk of prejudicing an investigation. An organisation will need to give careful consideration to its duties to advise a customer/client about their affairs.

organisation must comply with its anti-money laundering obligations. Staff should receive regular training (current legislation requires training to be conducted at least annually²) and be aware that they must report suspicions promptly and efficiently.

The content of this article is intended to provide a general guide to the subject matter. Specialist advice should be sought about your specific circumstances.

Should you have any questions or requests for further information please contact:

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Conclusion

This case is likely to have an impact on all who make money laundering suspicious activity reports, including banks, financial institutions, lawyers, corporate service providers and accountants.

The Court of Appeal's decision means that customers may obtain disclosure in litigation of an organisation's internal documents relating to money laundering disclosures and require them to prove at trial that they held the suspicions reported. It also leaves open the possibility that organisations may owe duties to their customers to advise them of money laundering reports made about them.

It remains to be seen what the true implications of this case will be. It can only be hoped that the final judgment will provide guidance for organisations as to how they can comply with their anti-money laundering obligations whilst meeting their duties to their customers or clients.

It is essential that money laundering reporting officers and those responsible for anti-money laundering within organisations ensure that their procedures effectively record evidence of suspicion and produce a complete paper trail leading to the ultimate report. Clients should be aware from the outset that the

² Paragraph 22 of the Criminal Justice (Money Laundering) Code 2008 (as amended).

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