

## Insights

# FRAUD CASES: HONG KONG COURT'S JURISDICTION ON THE GRANT OF VESTING ORDERS

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Regrettably, internet scams are on the rise in Hong Kong, consistent with the regrettable world trend.

According to police, reports of cybercrimes in Hong Kong surged more than sevenfold during the past decade to 16,159 cases in 2021, involving monetary losses totalling more than HK\$3 billion.

One of the legal remedies available to victims of fraud is a vesting order under section 52 of the Trustee Ordinance (Cap. 29) (the “**TO**”), which entitles the victim to call for a transfer from the party holding the stolen money (usually a bank) back to the victim.

However, there have been conflicting first instance judgments resulting in some confusion as to whether a vesting order should be sought by the victim.

Some helpful clarity was provided in the recent Hong Kong Court of First Instance case *Hypertec Systems Inc v Yifim Ltd* (HCA 1308/2021, HCMP 1829/2021, 18 February 2022), which reaffirmed the Court’s jurisdiction to grant a vesting order in an email fraud case.

## BRIEF FACTS

The Plaintiff was the victim of an email fraud. The Plaintiff was deceived by fraudsters of unknown identities into paying (a) a total sum of US\$1,360,500 to the 1<sup>st</sup> Defendant and (b) a sum of US\$250,000 to the 2<sup>nd</sup> Defendant. The defrauded money ended to the bank accounts of the two Defendants in Hong Kong.

The Plaintiff commenced:-

1. First, an action for recovery of the Plaintiff’s money or their traceable proceeds from the Defendants (the “**Main Action**”); and
2. Secondly, an action seeking vesting orders, to vest in the Plaintiff the right to sue for and recover, directly from the banks pursuant to any judgment in the Main Action, the sums that had been transferred to the Defendants and which currently were standing in the Defendants’ bank accounts should be (the “**Miscellaneous Proceedings**”).

The Court handed down its judgment and made vesting orders in favour of the Plaintiff. We will discuss below the Court's reasoning.

## **(A) The Main Action: Recovery from the Defendants of the defrauded sums or their traceable proceeds**

### *The Plaintiff's application for default judgment*

Upon the Plaintiff's ex parte application, the Court granted (a) a Mareva and proprietary injunction in favour of the Plaintiff against the Defendants and (b) a disclosure order against the banks. The injunction was later continued inter partes until further order of the Court.

Subsequently, the Plaintiff filed a writ and statement of claim against the Defendants. The Defendants defaulted in entering an appearance. Therefore, the Plaintiff sought default judgment against the Defendants for the recovery of the defrauded sums or their traceable proceeds.

### *Constructive trust*

As a matter of law, a constructive trust arises by law, in the cases of fraud, out of the transfer from the victim and receipt by the recipient. It follows that the money in the recipient's bank account becomes recoverable and traceable in equity. In the present case, the Court was satisfied that a fraud had been proven by the following:-

1. The Plaintiff was deceived into causing the transfer of money to the Defendants.
2. The exact identities of the fraudsters were not known, and with whom the Plaintiff had no prior or existing business dealings.
3. The defrauded money had been credited into the bank accounts of the Defendants in Hong Kong.
4. The Defendants had no known or established business.
5. The Plaintiff had no business dealings with either of the Defendants at any time.

The Court noted that, even if the recipient is not a party to the fraud, if its state of knowledge is such as to make it unconscionable for the recipient to retain the money, the victim is entitled to a tracing remedy. In the present case, the Court was satisfied that this was a clear case of fraud, and held that the Defendants' state of knowledge that they were not entitled to receive and to retain the Plaintiff's money made it unconscionable to retain the sums.

Regarding the timing of the acquisition of knowledge, the Court said, such knowledge needs not be acquired at the time of the transfer / receipt, but can be acquired after the money reaches the Defendant's hands. In the present case, the Defendants would have acquired knowledge of the fraud by no later than the service upon them of the injunction order and the writ and statement of

claim. Notwithstanding being served with those legal papers, the Defendants did not return or make any attempt to return the money to the Plaintiff. Therefore, the Court found that the Defendants held the sums in their respective bank accounts on trust in favour of the Plaintiff.

#### *Claim for unjust enrichment*

The Plaintiff also claimed against the Defendants on the basis of unjust enrichment. Pursuant to Guaranty Bank and Trust v Zzzik Inc (HCA 1139/2016, 18 July 2016), to establish a claim for unjust enrichment, the Plaintiff must prove that: (a) the defendants have been enriched; (b) they were enriched at the plaintiff's expense; (c) the enrichment was unjust; and (d) there is no defence entitling them to the enrichment.

The present case involved a fraud and the transfers of the money to the Defendants as the first recipients. The Court held that the pleaded facts were sufficient to satisfy the elements for the Plaintiff's claim for unjust enrichment to the extent of the money received by the Defendants.

#### *Claim for conspiracy*

The Plaintiff also relied on the cause of action of there having been a conspiracy between the Defendants to commit the fraud. Conspiracy takes the form of a combination of parties to act with the intention of causing damage to a third party who thus incurs the intended damage.

In the present case, there was no direct evidence of any combination between the Defendants, or between the Defendants and the fraudsters. On the other hand, neither the Defendants nor the fraudsters had put forward any evidence that they merely were innocent parties, and neither had offered to make restitution to the Plaintiff. The Court was of the view, therefore, that the Defendants had retained the received sums for no legitimate reason. Therefore, the Court was able to draw an inference against the Defendants as being parties facilitating the perpetration of the fraud.

#### *Relief*

In the circumstances, the Court held that the claim for personal relief was established.

For the loss of the sums that had been transferred by the Plaintiff, the Court held that the Plaintiff was entitled, against both Defendants, to damages in the amount by which it was out of pocket as a result of the fraud.

Regarding the claim for declaratory relief, the Court found that, whilst declaratory relief normally would not be granted by default without a trial, that is only a general rule of practice. The Court retains the discretion to do the fullest justice to the Plaintiff to which it is entitled in the circumstances of the case.

In the present case, the Court was of the view that a monetary judgment without declaratory relief would put the Plaintiff into the category of an unsecured creditor, with the result that the Plaintiff's

proprietary entitlement to the money in question and tracing could not effectively be recognised. Declaratory relief was therefore appropriate. The declaration would cover the amounts that had landed in the bank accounts of the Defendants.

To conclude, the Court entered judgment in favour of the Plaintiff against both Defendants, respectively for the amounts each had received. The Court also granted declaratory relief to the effect that the Defendants held the Plaintiff's money on trust for the Plaintiff.

## **(B) The Miscellaneous Proceedings: Vesting orders**

The Miscellaneous Proceedings had been commenced for vesting orders pursuant to section 52 of the Trustee Ordinance (the "TO"), which provides relevantly:-

"(1) In any of the following cases, namely –

.....

(e) where stock or a thing in action is vested in a trustee whether by way of mortgage **or otherwise and it appears to the court to be expedient**, the court may make an order vesting the right to transfer or call for a transfer of stock, or to receive the dividends or income thereof, or to sue for or recover the thing in action, in any such person as the court may appoint

.....

(5) The court may make declarations and give directions concerning the manner in which the right to transfer any stock or thing in action vested under the provisions of this Ordinance is to be exercised." (emphasis added)

In 800 Columbia Project Company LLC v Chengfang Trade [2020] HKCFI 1293, which was a cyber-fraud case, the Court considered that its jurisdiction under section 52(1)(e) TO was not engaged to justify the making of a vesting order in respect of the right to recover the plaintiff's money that had been transferred due to fraud and had landed in the hands of the defendant recipients.

In the present case, the Court adopted the reasoning advanced in Wismettac Asian Foods v United Top Properties [2020] HKCFI 1504, in which the Court rehearsed the analysis in 800 Columbia and subsequent cases. In Wismettac, the Court construed the wording of section 52(1)(e) of the TO broadly. The Court's view was that this statutory provision may be invoked if the following two conditions are satisfied: (a) a thing in action is vested in a trustee whether by way of mortgage or otherwise and (b) it appears to the court to be expedient to grant a vesting order.

The first condition under section 52(1)(e) of the TO prescribes the mode of vesting as "by way of mortgage or otherwise". Section 2 of the TO provides that, unless the context otherwise requires, the expression "trust and trustee" extends to implied and constructive trusts. In considering whether the

context requires the exclusion of constructive trustee, the Court considered that the extremely broad word “otherwise” means “any other way”, and is capable of including vesting by way of operation of law.

In Wismettac, the Court ruled that a constructive trust comes into existence by operation of law when the fraudster or the subsequent recipient receives the victim’s money or its traceable proceeds in their bank account. When the Court grants a declaration in this respect, the Court merely is affirming the legal position but is not creating any trust by such order. The Court considered that there would be no good reason for regarding the constructive trust in such circumstances as something other than a true trust, and equally there would be no good reason to exclude such a constructive trustee from the meaning of trustee in the subsection. Therefore, section 52(1)(e) of the TO should apply, so that a vesting order may be made upon proof that a constructive trust arose by operation of law in respect of the money that had been extracted from the plaintiff by fraud or mistake which ended up in the recipient’s bank account now subject to the trust.

As regards the first condition under section 52(1)(e) of the TO, the Court held that this was satisfied here because the Court had ruled that there was a constructive trust by the Defendants in favour of the Plaintiff, in respect of the money standing in the Defendants’ accounts that had been transferred by the Plaintiff by reason of the fraud.

The second condition under section 52(1)(e) is that “it appears in the court to be expedient” to make a vesting order. The test of expediency would be satisfied, the Court ruled, where it is impossible or difficult to deal with the property without such an order. In the present case, the Court held that the impossibility existed and would persist where the money in the Defendant’s bank accounts could not be moved without the bank’s co-operation.

## BCLP COMMENTS

Wismettac Asian Foods v United Top Properties and the present case Hypertec Systems Inc v Yifim Ltd present welcome news for victims of fraud seeking vesting orders to assist them to secure return of their money.

## RELATED CAPABILITIES

- Litigation & Dispute Resolution

## MEET THE TEAM



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