

Brief Overview of the Relevant Hong Kong Law

I. Introduction

1. The purpose of this brief overview is to set the scene for the comparative exercise of similarities and differences between Hong Kong law and the CISG in Chapter 2 of the Consultation Paper (“Chapter 2”). As such, this overview will focus on those areas which are studied in the comparative exercise in Chapter 2.
2. For ease of reference, the topics that will be discussed below include:
 - (1) When the Hong Kong law of sale applies and whether the Hong Kong courts will apply the CISG even under the status quo;
 - (2) Formation of a valid sales contract in Hong Kong law (offer and acceptance, consideration and intention to create legal relations);
 - (3) General principles on ascertaining the contents of the contract (i.e. interpretation of the contract, implied terms, and controls on onerous terms, including liquidated damages clauses);
 - (4) Specific contents of a contract for sale of goods (i.e. arrangements for passing of property, mandatory implied terms under the Sale of Goods Ordinance (Cap. 26) (“SGO”) and duties of the buyer and seller respectively);
 - (5) Remedies for breach of a sales contract (from the buyer’s and seller’s perspective respectively); and
 - (6) Factors vitiating or terminating a sales contract (mistake, misrepresentation and frustration).

II. Application of the Hong Kong Law of Sale

(A) Is Hong Kong law the governing law?

3. By definition, international sales involve more than one jurisdiction. As such,

the first question to be answered is “does Hong Kong law apply?” In other words, is the relevant sales agreement or dispute arising therefrom governed by Hong Kong law¹?

4. This being a conflict of laws question, the answer depends on the choice of law rules of the forum court (as courts in different jurisdictions can come to different answers even on the same factual matrix). The forum court, of course, may or may not be the Hong Kong court.
5. The analysis where the forum is not Hong Kong is beyond the scope of this overview, and is in any event a matter for foreign law.
6. If Hong Kong is the forum court, however, the principles are generally as follows:
 - (1) If the parties to the dispute do not raise the governing law as a live issue, Hong Kong law will apply by default².
 - (2) Assuming the question of governing law is raised, the Hong Kong court will first perform a process of characterisation - broadly, it will determine if the issues in dispute are contractual or proprietary in nature³.
 - (3) If contractual, the Hong Kong court will first ascertain whether the parties have made an express choice of law in the sales contract. If so, this choice is “normally conclusive”⁴.
 - (4) Failing such an express choice, the Hong Kong court will consider if the parties had impliedly agreed on a choice of law, or failing even that will assess which law has the “closest and most real connection” with the transaction⁵. These two assessments will require the court to take into account a wide range of connecting factors, including but not limited to the place of business of the parties, the place of performance of the obligations under the contract, the existence of a jurisdiction clause in the contract, etc., in which no one factor will be decisive (although the case law treats the place of the act of physical delivery as particularly significant)⁶.
 - (5) If the issue is characterised as proprietary (i.e. usually concerning validity of transfer of title), the Hong Kong court will generally apply

1 Graeme Johnston & Paul Harris, *The Conflict of Laws in Hong Kong* (3rd edn, Sweet & Maxwell 2017) para. 5.046.

2 Lord Collins of Mapesbury (ed), *Dicey, Morris and Collins on the Conflict of Laws* (15th edn, Sweet & Maxwell 2012) para. 9R-001.

3 Ewan McKendrick (ed), *Sale of Goods* (LLP Asia 2000) para. 15-002.

4 A.G. Guest (ed), *Benjamin's Sale of Goods* (10th edn, Sweet & Maxwell 2017) para. 26-006.

5 *Ibid* paras. 26-007-26-008.

6 *Ibid* para. 26-009.

the *lex situs*, the law at the place the goods are situated at the time of transfer of title⁷, as the governing law. This is subject to an exception for goods sold in transit - the situs having obviously tenuous connections with the goods in such a context, the Hong Kong court will instead apply the law with the “closest and most real connection” as per sub-paragraph (4) above⁸.

7. If, on applying the above choice of law rules, the Hong Kong court holds that a foreign law governs the relevant dispute before it, the content of such law will be considered an issue of fact and the parties are required to adduce (expert) evidence to prove it, with the added costs this would entail⁹. This can be an inaccurate exercise (e.g. the experts may be wrong, or the Hong Kong court may not be able to accurately duplicate the reasoning processes of the foreign court)¹⁰.
8. Albeit a slight digression, one issue to be discussed here is where the Hong Kong court, applying its conflict of law rules, arrives at the law of a state which is a Contracting State of the CISG. The question is whether the Hong Kong court then applies the local sales law of that state, or the CISG?
9. There is a dearth of Hong Kong authority on the point. Academic writers and foreign courts¹¹, however, suggest that this depends on whether that foreign state has made the decision to apply the CISG in priority over its domestic sales law, i.e. whether it has made any reservation under Article 95 CISG so that it will not be bound by Article 1(1)(b) CISG, which provides that “[t]his Convention applies to contracts of sale of goods between parties whose places of business are in different States: ... (b) when the rules of private international law lead to the application of the law of a Contracting State.”
10. The prevailing view appears to be that if the foreign state whose law is applicable is bound by Article 1(1)(b) CISG (i.e. the foreign state has not made an Article 95 reservation), then the CISG applies in the Hong Kong court as forum¹²; and vice versa. In gist, therefore, it is arguable that the CISG may apply in the Hong Kong courts even under the status quo¹³.

7 McKendrick (n 3) para. 15-086.

8 Guest (n 4) paras. 26-124, 26-138.

9 Richard Fentiman, *International Commercial Litigation* (2nd edn, OUP 2015) paras. 20-07-20-08.

10 *Ibid* paras. 20.48-20.57.

11 Ingeborg Schwenzer (ed), *Schlechtriem & Schwenzer: Commentary on the UN Convention on the International Sale of Goods (CISG)* (4th edn, OUP 2016) Article 1-6 para. 4; Michael Bridge, *The International Sale of Goods* (4th edn, OUP 2017) para. 10.05; CISG Advisory Council Opinion No.15, para. 3.18, available at: <http://www.cisg.law.pace.edu/cisg/CISG-AC-op15.html>.

12 *Ibid*; see also Oberlandesgericht Koblenz (Germany), 17 September 1993, at [1], translated at: <http://cisgw3.law.pace.edu/cases/930917g1.html>; Schwenzer (n 11) Article 6 para. 32.

13 Benjamin Hayward, Bruno Zeller & Camilla Baasch Andersen, ‘The CISG and the United Kingdom - exploring coherency and private international law’ (2018) ICLQ 607, 621.

(B) Sale of goods or something else?

11. Even assuming that Hong Kong law applies, the Hong Kong law on sale of goods will not be relevant if the relevant contract is determined to not involve the sale of goods. This can involve situations such as gift, barter and hire purchase¹⁴.
12. Particular problematic, however, are contracts for a mixture of services and goods (e.g. building a ship), which may be a sale of goods to which the services are incidental, or vice versa. Unless the parties have made a clear choice in the form of their agreement, the well-established test is for the court to look at “the substance of the contract”¹⁵.
13. The case law “provides no general principles that might clarify the distinction” and there are only firm decisions in certain fixed scenarios¹⁶:
 - (1) Where a chattel is to be affixed to land, the contract will usually be for work and materials (i.e. service);
 - (2) Where an article is to be manufactured for the buyer but all the raw materials are supplied by the buyer, then it is clear that what is being contracted for is the services involved; and
 - (3) Where (professional) services are provided above and beyond the goods delivered (e.g. seeing a doctor and being prescribed medicines), this is usually a contract for service.
14. Beyond these categories, it is recognised that the “substance” test presents difficulties, especially where the supply of the goods and the performance of the work cannot be easily separated as distinct elements in the bargain (e.g. building a house or painting a picture, where the whole of the skill and work involved goes into creating the end product delivered¹⁷).
15. There has been criticism of the “substance” test in Australian case law, but the Hong Kong authorities appear to refer to the key Australian case without critical evaluation¹⁸.

14 See e.g. Brian Gilchrist (ed), *Chitty on Contracts (Hong Kong Specific Contracts)* (5th edn, Sweet & Maxwell 2016) para. 20-018.

15 *Robinson v Graves* [1935] 1 KB 579, applied in Hong Kong in *Mak Ping Kui v Millionice Ltd* (unrep., HCA 940/1998, 25 April 2001).

16 Guest (n 4) paras. 1-041, 1-043-1-046.

17 *Ibid* paras. 1-042, 1-047.

18 *Mak Ping Kui* (n 15) at [48], citing without comment *Deta Nominees v Viscount Plastic Products* [1979] VR 167.

III. Contract Formation under Hong Kong Law

16. Under Hong Kong law, a contract requires at the least: (1) offer and acceptance, (2) consideration, and (3) an intention to create legal relations.

(A) Offer and Acceptance

17. The doctrine of offer and acceptance creates the agreement necessary to found any valid contract at law.
18. It is usually defined in terms of a clear “offer” being unambiguously “accepted”¹⁹. Attempts to water down the doctrine by inviting the court to look at the documents and conduct of the parties as a whole and to infer agreement therefrom have been rejected in Hong Kong²⁰.
19. An offer is an “expression of willingness to contract on specified terms made with the intention that it is to become binding as soon as it is accepted...”, with such expression assessed objectively²¹.
20. An acceptance is a “final and unqualified expression of assent to the terms of an offer” and, as with an offer, is objectively assessed²².
21. Key issues with offer and acceptance in the sale of goods context are: (1) when and how they can be made or revoked; (2) what happens if an acceptance does not perfectly correspond to an offer; and (3) can the contract be sufficiently certain if the agreement is vague?

(1) Making and revoking offers and acceptances

22. **Making offers.** The principal difficulty here is whether a particular statement is an offer or only an invitation to treat (i.e. statements made to invite an offer from the counterparty). Subject to certain well-defined situations where the statement has been classified via case law (such situations not directly relevant for sale of goods)²³, the general rule is that this depends on the court’s assessment of the statement-maker’s intention²⁴.
23. **Terminating offers.** An offer will lapse firstly where it has been rejected by

19 Michael J Fisher & Desmond G Greenwood, *Contract Law in Hong Kong* (Expanded 2nd edn, Hong Kong University Press 2011) para. 3.2.

20 *Calimpex International v ENZ* [1994] 1 HKC 191 at 196.

21 Hugh Beale (ed), *Chitty on Contracts* (33rd edn, Sweet & Maxwell 2018) para. 2-003.

22 *Ibid* para. 2-026.

23 *Ibid* paras. 2-010-2-013 (display of goods); 2-014-2-017 (advertisements), 2-019-2-023 (auctions and tenders).

24 *Ibid* para. 2-010.

the counterparty, whether by a refusal or by a counter-offer²⁵. Secondly, an offer will lapse on the expiry of a specified time or reasonable time (if no period is specified)²⁶.

24. Further, the offeror can himself revoke the offer at any time before it has been accepted; this is so even if he has expressly stated that the offer is open for a period of time, as this is a bare promise unsupported by any consideration (consideration is discussed below)²⁷.
25. The rejection/revocation must generally be communicated to the counterparty; there is no exception for postal communications as with acceptance (this “postal rule” is discussed below)²⁸.
26. **Making Acceptance.** Generally, acceptance is required to be communicated to the offeror and so silence or inactivity is normally ineffective to constitute acceptance²⁹. Further, acceptance is effective only when it actually reaches the offeror, or where the failure to acquire notice of the acceptance is due to the fault of the offeror (e.g. he failed to read a duly received message)³⁰.
27. There are two special rules concerning making acceptance. First, acceptance by post is deemed effective from when it is sent (the so-called “postal rule”); this is an exception to the general rule that acceptance takes effect when it comes to the offeror’s notice³¹.
28. Second, acceptance by electronic communications depends on whether a communications system has been defined by the offeror:
 - (1) If so, then the acceptance is effective when the electronic message is received by the designated system; and
 - (2) If not, then acceptance is effective when the electronic message comes to the knowledge of the offeror³².
29. **Revoking Acceptances by Post.** Given that acceptance generally takes effect on the offeror acquiring (actual or constructive) notice, there is usually little room for revocation of an acceptance in Hong Kong law. The exception is a potential revocation of an acceptance by the postal rule. On this point, there is no English or Hong Kong authority, and decisions from other common law jurisdictions have diverged³³.

25 *Ibid* para. 2-098.

26 *Ibid* paras. 2-102-2-103.

27 *Ibid* para. 2-094.

28 *Ibid* paras. 2-095, 2-101.

29 *Ibid* para. 2-044.

30 *Ibid* para. 2-046(3).

31 *Ibid* para. 2-047 *et seq.*

32 Electronic Transactions Ordinance (Cap. 553) section 19(2)-(3).

33 Beale (n 21) para. 2-060 *et seq.*

(2) *Where acceptance does not correspond to the offer*

30. The second issue with the Hong Kong law of offer and acceptance is the position where the acceptance does not perfectly correspond to the offer, i.e. a so-called “battle of the forms” scenario. This is particularly relevant in the sale of goods context, as each party refers to his own set of (conflicting) standard terms when contracting³⁴, and it is unclear at the end of the day whose standard terms prevail.
31. The traditional offer and acceptance approach leads to the “last shot” approach - the last party referring to his standard form makes the “winning” offer, rejecting the other party’s offer (if any) in the process, and this offer is then accepted by the other party performing the contract³⁵.
32. There are, however, glosses on this basic position. Recent case law has shown that if both parties refer to their standard terms but, viewed in the round, neither are accepted by the other, then a contract may be formed albeit on neither party’s terms³⁶. Some commentators have also detected hints of a “knock out” approach to the battle of the forms: the contract is formed based on those terms which are common to both sets of standard forms, and other terms are “knocked out” of the contract³⁷.

(3) *Vague or incomplete agreements*

33. Hong Kong law will find that an agreement is not a binding contract if there is an unacceptable degree of uncertainty in it. Such uncertainty usually arises from: (1) the terms of the contract being incomplete; or (2) the terms being complete but unduly uncertain and vague.
34. In practice, the Hong Kong courts generally strive to uphold contracts:

“Of course, once essential terms have been agreed, there will not be any lack of certainty. And where there has been part performance, the Court ‘will strain to the utmost to supply the want of certainty even to the extent of providing substitute machinery’ ... Thus, the Court may imply terms, adopt usual covenants or even determine terms by reference to concepts of reasonableness.”³⁸
35. This rule is well-evidenced in the case where the parties have failed to agree the price. In the sale of goods context, this is not necessarily fatal. Section 10

34 See e.g. *BRS v Arthur V Crutchley Ltd* [1968] 1 All ER 811.

35 Beale (n 21) para. 2-036.

36 *Ibid* para. 2-036.

37 Bridge (n 11) para. 11-11 and footnote 100.

38 *The World Wood Fair Limited v Hong Kong Island Development Ltd* [2005] 1 HKLRD 665 [7], reversed on appeal on the evidence: (2006) 9 HKCFAR 735.

of the SGO provides that the price may be left to be fixed in a manner agreed upon in the contract, or may be determined from the parties' dealings, or failing even that may be fixed at a "reasonable price", which depends on the facts of each case.

36. For completeness, it is observed that this provision presupposes that a binding contract is made (albeit without agreement on the price). Depending on the facts, the lack of agreement on price may of course point to the lack of any contract at all³⁹. In such circumstances, if the parties perform acts pursuant to a purported agreement, they may nonetheless recover from each other payment for a reasonable sum by way of common law claims in restitution for unjust enrichment and not by contractual claims⁴⁰.

(B) Consideration

37. In Hong Kong law, a promise or agreement is not generally binding as a contract unless it is made in the form of a deed, or it is supported by "consideration", i.e. "something of value in the eye of the law" given in exchange for the promise or agreement⁴¹.
38. This explains why a promise to not revoke an offer⁴² is not enforceable - there being no detriment to the offeree or benefit to the offeror, nothing of value is given in exchange for the promise; hence the promise not to revoke is not binding in law.
39. However, consideration can be executory in nature, i.e. it can be a promise to perform or forbear from performing so long as the act being promised would itself be good consideration⁴³. This explains how consideration can be found in consensual variations of contracts (which frequently occur in the sale of goods) - insofar as the parties' new agreement confers benefits on one another, the mutual promise to perform the new agreement constitutes good consideration.
40. However, this raises the possibility that a proposed variation of contract would be entirely to one party's benefit (such as where the buyer asks for more time to pay). In such circumstances, the benefiting party will be simply performing his pre-existing contractual obligations i.e. a "past consideration"; this is not good consideration⁴⁴.

39 Beale (n 21) para. 2-121.

40 *Ibid* para. 2-120.

41 *Ibid* paras. 4-001-4-002.

42 See para. 24 above.

43 Stephen Hall, *Ho and Hall's Hong Kong Contract Law* (4th edn, LexisNexis 2017) para. 3-14.

44 Beale (n 21) para. 4-026.

41. This conclusion has presented great difficulty in the context where one party cannot perform and asks for a variation wholly in his favour, and the other party (for genuine commercial reasons) wishes to allow the variation. In such cases, the Hong Kong courts have, following English case law, resorted to finding consideration in “practical benefits” (such as avoiding delay, or minimising costs in finding replacement suppliers) where no new benefit was conferred and what was offered was, in strict terms, only “past consideration”⁴⁵. This is an area of live controversy, particularly after one recent English Supreme Court case indicated that the current law on “past consideration” was “ripe for reconsideration”⁴⁶.

(C) Intention to Create Legal Relations

42. One final element for finding a binding contract in Hong Kong law is that the parties intend their agreement to be legally enforceable. The presumption in a commercial (as opposed to domestic or social) agreement, is that the parties intend it to be legally enforceable⁴⁷, due to the inherent implausibility of one businessman placing himself at the mercy of another. In practice, this presents little difficulty for contracts for the sale of goods.

IV. Ascertaining the Content of the Contract

43. What is expressly agreed in a contract may be unclear, or incomplete. In such cases, via the processes of interpretation and implication, the Hong Kong courts will flesh out the contractual content. On the other hand, there may be situations in which the Hong Kong courts consider that certain one-sided clauses in contracts to be contrary to policy goals, and will thus adopt various techniques to avoid such clauses.

(A) Contractual Interpretation

44. Contractual terms are often expressed in such a manner that their meaning is ambiguous. In such cases, the courts will interpret the term, with the aim of ascertaining not what the parties subjectively intended, but of what a reasonable person in the position of the parties would have understood the terms to mean⁴⁸. As such, the Hong Kong law approach to interpretation is primarily objective.
45. The objective approach entails looking not only at the words used, but also

45 See e.g. *UBC (Construction) Ltd v Sung Foo Kee Ltd* [1993] 2 HKLR 207.

46 *Rock Advertising Limited v MWB Business Exchange Centres Limited* [2018] 2 WLR 1603 [18].

47 *New World Development Co Ltd v Sun Hung Kai Securities Ltd* (2006) 9 HKCFAR 403, 413.

48 Beale (n 21) para. 13-043; see in Hong Kong *Jumbo King Ltd v Faithful Properties Ltd* (1999) 2 HKCFAR 279 at 296.

to the background and context of the agreement. Evidence of the subjective (or actual) intent of the parties is largely irrelevant.

46. The ordinary meaning of the words used will generally prevail (assuming it is clear) where it makes sense in the light of the relevant background and context⁴⁹. However, it is trite that the courts will depart from the plain language meaning when, viewed against the background, that meaning would be ambiguous, create an absurdity or contradict other parts of the agreement⁵⁰. In such circumstances, particularly in the context of mercantile contracts such as those for the sale of goods, the courts will strive to ascribe to the words a meaning that they can bear and that would make good commercial sense⁵¹.
47. As the interpretive exercise is aimed at making sense of what the parties objectively intended at the time the contract was made, acts subsequent to contract formation are therefore inadmissible to interpret the terms of a written agreement⁵².

(B) Implication of Terms

48. In other scenarios, the express terms of the contract may be incomplete. In such circumstances, Hong Kong law may resort to the doctrine of implied terms.
49. Terms are implied in one of three manners: (1) in law (affecting an entire class of contracts), (2) in fact (affecting an individual contract), or (3) by custom and usage. In the sale of goods context, implied terms in law are largely controlled by the SGO and will be discussed below.
50. For implying a term in fact, the operative threshold is high. Notwithstanding recent Privy Council (of the United Kingdom) authority which suggests an elision of the processes of interpretation and implication of terms⁵³, the position in Hong Kong remains governed by the Hong Kong Court of Final Appeal authority to the effect that a term will be implied only where:
 - (1) The term is reasonable and equitable;
 - (2) The term is necessary to give efficacy to the contract, so that no term will be implied if the contract is effective without it;
 - (3) The term must be so obvious that “it goes without saying”;

49 *River Trade Terminal Co Ltd v Secretary for Justice* (2005) 8 HKCFAR 95 at 107-108.

50 Beale (n 21) paras. 13-083.

51 *Ibid* para. 13-084.

52 *Ibid* para. 13-136.

53 *AG of Belize v Belize Telecom Ltd* [2009] 1 WLR 1988.

- (4) The term must be capable of clear expression; and
 - (5) The implied term does not contradict any express term⁵⁴.
51. For implying a term by custom and usage, the threshold is similarly high. There must be a general and well-known custom or usage of the particular trade or place which the contract is concluded in light of - the test traditionally applied is that the term must be “notorious, certain and reasonable”⁵⁵, and it must not contradict any express terms of the contract⁵⁶. In such circumstances, the law in implying the term is simply spelling out “what both parties know and would, if asked, unhesitatingly agree to be part of the bargain”⁵⁷.

(C) Statutory Interpretation

52. Whilst at first glance it may be odd for a section on ascertaining the contents of a contract to discuss the principles of statutory interpretation, this is apt in the sale of goods context. The default terms of any sale of goods under Hong Kong law are provided for by the SGO. Insofar as particular provisions in the SGO may be unclear, the principles brought to bear on interpretation may include those of statutory (and not only contractual) interpretation.
53. Examples of provisions in the SGO which have required statutory interpretation include the phrases “sale in the course of a business” and “goods supplied under a contract” in section 16⁵⁸.
54. Relevant general principles on statutory interpretation include the following:
- (1) The fundamental goal is to ascertain objectively the intention of the legislator as reflected in the language of the statute⁵⁹.
 - (2) The starting point is that “an Ordinance shall be deemed to be remedial and shall receive such fair, large and liberal construction and interpretation as will best ensure the attainment of the object of the Ordinance according to its true intent, meaning and spirit”⁶⁰.
 - (3) Accordingly, a purposive approach is adopted. The Hong Kong court will, at the first instance have regard to context and purpose, including the legislative materials, and not only where ambiguity

54 *Kensland Realty Ltd v Whale View Investment Ltd* (2001) 4 HKCFAR 381 at 391-392.

55 *Eggar, Forrester Offshore Ltd v Hong Kong United Dockyards Ltd* [1987] 1 HKC 318 at 331.

56 Beale (n 21) para. 14-018.

57 *Liverpool City Council v Irwin* [1977] AC 239 at 253.

58 As to the former phrase, see *Stevenson v Rogers* [1999] 2 WLR 1064; as to the latter, see Gilchrist (n 14) para. 20-101.

59 *HKSAR v Cheung Kwun Yin* (2009) 12 HKCFAR 568 at 574.

60 Interpretation and General Clauses Ordinance (Cap. 1) section 19.

arises⁶¹. The court strives to give effect to the statute's context and legislative intent and purpose, implying and reading in words if necessary, but without attributing a meaning which the language and words are incapable of bearing⁶².

- (4) Finally, and importantly, the Hong Kong courts adopt a pragmatic and commonsense approach to interpretation, and will reject interpretations which give rise to absurd results⁶³.

(D) Classification of Terms

55. To elaborate on the law on terms, Hong Kong law adopts a classification of contractual terms, whether express or implied. In effect, the law recognises that some contractual obligations are so important that breaches thereof give rise to a right to terminate the contract in addition to other remedies, whilst breaches of relatively less important terms do not confer termination rights.
56. Generally, under default Hong Kong law, a term is classified as:
 - (1) A condition, for which breach thereof will give rise to a right of termination as it would "deprive the party not in default of substantially the whole benefit" of the contract⁶⁴;
 - (2) A warranty, for which breach thereof (no matter how serious) will not give rise to a right of termination; or
 - (3) An innominate term, which cannot be classified as either a condition or warranty as it can be breached in different ways, with some breaches depriving the innocent party of the benefit of the contract and others not. As such, whether a breach of an innominate term gives rise to a right of termination depends on the seriousness of the effect of the breach.
57. The same categorisation has been expressly held to apply in the sale of goods context⁶⁵. For example, it is well-established that stipulations as to time for delivery in sale of goods contracts are presumptively conditions, whilst provisions for time for payment are presumptively not⁶⁶.
58. As to how a particular term is to be categorised, the default approach is again to look at the objective intention of the parties, i.e. an exercise in

61 *Vallejos v Commissioner of Registration* (2013) 16 HKCFAR 45 at para. 76.

62 *HKSAR v Lam Kwong Wai* (2006) 9 HKCFAR 574 at 606.

63 *Chan Ho Tin v Lo Ying Ki Alan* [2018] 2 HKLRD 7 at 35.

64 *Hong Kong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26 at 69-70.

65 *Cehave NV v Bremer Handelsgesellschaft mbh (the Hansa Nord)* [1976] QB 44.

66 Edwin Peel, *Treitel: The Law of Contract* 14th edn, Sweet & Maxwell 2015) para. 18-103.

interpretation⁶⁷. However, this can be overridden by the parties' mutual agreement on classification⁶⁸ or by statute⁶⁹.

(E) Form of Variation of Terms

59. The substantive validity of variations of contractual terms was discussed previously in the context of consideration⁷⁰. However, a different dimension to the issue of variation is whether parties can control the form of any variation.
60. In the sale of goods context (and commercial contracts in general), this issue usually concerns the enforceability of non-oral modification clauses ("NOM Clauses"), which compel the parties to make any variation to the contract in written form. The issue is difficult as it had historically been argued that any oral variation necessarily implied a waiver of the NOM Clauses. However, the English Supreme Court has recently given recognition to such clauses, albeit whilst recognising that reliance on such clauses may be precluded by estoppel⁷¹. The Hong Kong courts may follow suit.

(F) Control of Onerous Terms

61. Hong Kong law, whilst generally respecting the parties' freedom of contract, will intervene in the case of so-called onerous terms, i.e. terms which a party with superior bargaining power can impose on the other to its own advantage. Common examples in the sale of goods context are clauses excluding or limiting one party from liability in the event of breach of contract, or those providing that one party's standard terms "will prevail over any terms and conditions in the [counter-party's] order"⁷².
62. In such circumstances, Hong Kong law will regulate the onerous terms. However, in the international sale of goods context (including, as seen below, commerce between Mainland China and Hong Kong businesses), one of the most important regulatory tools of the Hong Kong law is disappplied.
63. The Control of Exemption Clauses Ordinance (Cap. 71) ("CECO") generally serves to substantially regulate terms purporting to exempt or limit parties' contractual liability (i.e. the CECO holds such terms substantially invalid/unenforceable).
64. However, section 16 of the CECO provides that it does not apply to

67 Guest (n 4) para. 10-027.

68 Hall (n 43) para. 6-182.

69 *Samsung Hong Kong Ltd v Keen Time Trading Ltd* [1998] 2 HKLRD 341.

70 See Section III(B) (Consideration) above.

71 *Rock Advertising Limited v MWB Business Exchange Centres Limited* [2018] 2 WLR 1603.

72 *Butler Machine Tools Co Ltd v Ex-Cell-O-Corporation (England) Ltd* [1979] 1 WLR 401.

international contracts for the supply of goods, i.e. (broadly) those sale of goods contracts which are “made by parties whose places of business...are in different countries or territories or are in and outside of Hong Kong”, and where the sale has an international dimension, i.e. (broadly) where “the acts constituting the offer and acceptance have been done in different countries or territories” and/or the goods are carried “from one country or territory to another country or territory”⁷³. Further, section 17(1) provides that the operative provisions of the CECO do not apply when Hong Kong law applies only by virtue of the parties’ choice of law (and where another law would govern the contract in the absence of such choice).

65. The Unconscionable Contracts Ordinance (Cap. 458) (“UCO”) is another form of statutory control over onerous contract terms. The UCO targets contracts that do not measure up to a normative standard of “good conscience”, a standard which is broadly and flexibly applied⁷⁴.
66. However, the UCO limits relief specifically for the purpose of consumer protection. As per section 5 of the UCO, it applies where one party does not enter into the contract in the course of a business or holds itself out to be doing so, and the goods or services pursuant to such contract are “of a type ordinarily supplied or provided for private use, consumption or benefit” (section 3(1) the UCO).
67. As such, it can be seen that the operative provisions of both the CECO and the UCO would rarely apply to a contract for international sales.
68. Therefore, the Hong Kong courts are left with common law methods for regulating onerous terms in such contracts. These include primarily:

- (1) **Incorporation.** The basic idea is to exclude onerous terms from the contents of the contract at all, given that such terms may not be squarely presented to the accepting party. Whilst English law distinguishes between the situation where the contract is signed by the accepting party and where it is not (with the rules for incorporating an onerous term being much stricter in the latter), there is Hong Kong case law accepting Canadian authority⁷⁵ which treats the two situations alike. Hence, onerous terms which were not read, and which the offeror knew was reasonably not read by the accepting party before its signature, would not be incorporated⁷⁶. This is similar to the rules for incorporating such a term without a

73 These phrases were newly added to the CECO by amendments in 1997. It appears that the phrase “in and outside of Hong Kong” was specifically inserted to ensure that section 16 applies to contracts between Mainland China and Hong Kong businesses even after the reunification.

74 *Chang Pui Yin v Bank of Singapore Ltd* [2017] 4 HKLRD 458 at para. 66.

75 *Tilden Rent-A-Car Co v Clendinning* (1978) 83 DLR (3d) 400.

76 See e.g. *Wing On Properties and Securities Co Ltd v Wave Front Enterprise (HK) Ltd* [2007] 2 HKC 54.

signature, which requires reasonable notice to be given to the other party⁷⁷.

- (2) **Strict Interpretation.** A second method for controlling onerous clauses is by way of interpretation. Courts will require onerous clauses to be clear and unambiguous before they can be enforced (and will read such clauses against the *proferens* in the event of ambiguity)⁷⁸, and will also strictly scrutinise their scope to ascertain if the clauses cover the subject-matter in dispute⁷⁹.

(G) Liquidated Damages and Penalty Clauses

69. Finally, by the doctrine of penalty clauses, Hong Kong law also substantively controls clauses providing for payment of pre-specified sums of money by one of the contractual parties to another in the event of breach.
70. At a high level of generality⁸⁰, if the pre-specified sum is proportionate to the party's loss in the event of breach, the clause will be enforceable as a liquidated damages clause. However, if the said sum is out of all proportion to the loss, it will be struck down as a penalty clause and unenforceable.
71. However, there is now uncertainty in the Hong Kong law as to whether it will follow the latest English decision on the subject⁸¹, which makes important technical and conceptual modifications to the doctrine. A District Court decision has approved the English position⁸² but the higher courts have not yet squarely addressed the issue.

V. The SGO

72. This section will discuss: (1) the obligations of the buyer and seller in a sale of goods contract under the SGO, (2) the scheme of remedies - under both the SGO and the common law - for breach of such obligations, and (3) miscellaneous effects of the SGO including its effect on the transfer of risk and property.

(A) Seller's Obligations under the SGO

73. The primary duty of a seller is summarised at section 29 of the SGO, namely,

77 Beale (n 21) para. 13-015.

78 *Ibid* paras. 15-008, 15-012.

79 *Ibid* para. 15-009.

80 *Ibid* paras. 26-190-26-191.

81 *Cavendish Square Holding BV v Makdessi* [2016] 1 AC 1172.

82 *Force Way Engineering Ltd v IO of Grand Court* (unrep., DCCJ 3216/2016, 19 December 2017).

that it is the duty of a seller to deliver the subject goods to a buyer in accordance with the terms of a contract of sale.

74. Delivery is defined under the SGO as the “voluntary transfer of possession from one person to another”⁸³, and it may be actual or constructive.
75. The seller’s obligations under the SGO in relation to various aspects of delivery are outlined below. Note that these default obligations can be (and are frequently) displaced by Cost Insurance and Freight (“CIF”) and Free On Board (“FOB”) terms in international sales⁸⁴. Special rules have developed in CIF and FOB cases⁸⁵.
 - (1) **Place of delivery.** The general rule is that the place and method of delivery depends on the contract of sale. Where the contract is (rarely so) silent in an international sale, a duty is imposed on the buyer to collect the goods from the seller’s place of business (if the seller has one, and if not, from the seller’s residence) rather than for the seller to send them to the buyer⁸⁶.
 - (2) **Time of delivery.** The general rule is that time for delivery is stipulated under the contract of sale. Where no time is fixed, a duty is imposed on the seller to deliver the goods “within a reasonable time”⁸⁷. What is a reasonable time is a question of fact⁸⁸. Where time is fixed but not stated whether it is of the essence, it is frequently presumed to be so in the context of commercial contracts⁸⁹.
 - (3) **Quantity of Goods.** A duty is imposed on a seller to deliver the exact quantity of goods stipulated in the contract of sale⁹⁰. The buyer may reject delivery where the quantity delivered is insufficient or excessive⁹¹ (beyond *de minimis*).
 - (4) **Description of Goods.** A duty is imposed on a seller to deliver to a buyer goods which meet (wholly) the contract specifications and descriptions⁹². The buyer may reject delivery where the goods (or a portion thereof) do not meet the descriptions. This is distinct from a seller’s duty in relation to the quality of goods.

83 SGO section 2(1).

84 The term “international sale” is used loosely as a term of commerce and not as a legal term. CIF and FOB terms can be and often are incorporated into a sale of goods contract governed by Hong Kong law. This includes contracts between Mainland China and Hong Kong businesses, so long as the contract is governed by Hong Kong law and validly incorporates the CIF/FOB terms.

85 Guest (n 4) paras. 19-009, 19-011, 19-013, 20-008, 20-016, 20-033.

86 SGO section 31(1).

87 SGO section 31(2).

88 *Protronics Co Ltd v Kouoi Vincent* (unrep., DCCJ 3234/2004, 13 April 2006).

89 *Bunge Corporation v Tradax Export SA* [1981] 1 WLR 711.

90 SGO section 32(1).

91 SGO sections 32(1) and (2).

92 SGO section 32(3).

- (5) **Expenses.** The expenses of putting the goods into a deliverable state⁹³ and the expenses of making actual delivery of the goods are borne by the seller, unless otherwise agreed⁹⁴. The expenses of receiving delivery are borne by the buyer, unless otherwise agreed⁹⁵.
- (6) **Examination on Tender of Delivery.** Unless otherwise agreed, a duty is imposed on a seller to afford a buyer, on request, a reasonable opportunity of examining the goods to ascertain whether they are in conformity with the contract⁹⁶. The buyer cannot be made liable for refusing to take delivery if the seller has not given him an opportunity to examine the goods as requested. However, the buyer's right to examination may be waived if the buyer expressly accepts the goods without first examining them or if the right is excluded by contract (for example, in a CIF sale⁹⁷). This is not to be confused with the buyer's right to examine post-delivery.
- (7) **Delivery by Instalments.** A buyer is not bound to accept - and a seller is not entitled to make - delivery by instalments, unless otherwise agreed⁹⁸. Where delivery by instalments is agreed, it is a matter for each case as to whether any defect in one instalment constitutes a repudiation of the whole contract or a severable breach⁹⁹.
- (8) **Delivery to Carrier.** Delivery to a carrier for the purpose of transmission to the buyer is *prima facie* deemed to discharge the seller's duty to deliver¹⁰⁰. However, a duty is imposed on the seller to reasonably contract with the carrier having regard to the nature of the goods and the circumstances of the case¹⁰¹. The rationale is for the reasonable prevention of the goods being lost or damaged in transit¹⁰². If the seller fails to do so, the buyer may decline to treat delivery to the carrier as delivery to himself or may sue the seller for damages.

76. Furthermore, sections 14 to 17 of the SGO imply terms as to the title, description and quality of goods into a contract of sale. Insofar as the terms are conditions, breach by the seller entitles the buyer to treat the contract as repudiated regardless of the gravity of the breach (i.e. the extent of the breach

93 SGO section 31(5).

94 *White v Williams* [1912] AC 814.

95 *Ibid.*

96 SGO section 36(2).

97 *E Clements Horst & Co v Biddell Bros* [1912] AC 18.

98 SGO section 33(1).

99 SGO section 33(2).

100 SGO section 34(1).

101 SGO section 34(2).

102 *Thomas Young & Sons v Hobson & Partners* (1949) 65 TLR 365.

and the seriousness of the effects thereof).

77. Under section 14, various undertakings as to title of goods are implied.
- (1) **Title.** There is an implied condition that the seller has a right to sell the goods¹⁰³. Where, for example, the goods in question belong to a third party¹⁰⁴ or “can be stopped by process of law from selling”¹⁰⁵, the seller would be in breach.
 - (2) **Charges and encumbrances and quiet possession.** There are also two implied warranties that the goods will be free from any charge or encumbrance in favour of a third party and that the buyer will have quiet possession of the goods¹⁰⁶.
78. Under section 15, a term as to the correspondence of the goods with their description is implied. The starting point is that goods sold by description must correspond with their description¹⁰⁷. For a sale by sample, the bulk of such goods must correspond with the sample as well as by description.
- (1) In the case of specific goods, a contract for sale is a sale by description if the buyer has not seen the goods and relies solely on a description given by the seller¹⁰⁸. Where the buyer has seen the goods, a contract for sale may still be a sale by description depending on whether the goods are sold by a description which the stated characteristics form part of¹⁰⁹.
 - (2) If the sale of goods is by sample and description, both correspondences are required under section 15(1).
79. Under section 16, conditions as to the merchantable quality and fitness of the goods are implied on the seller’s part.
- (1) **Merchantable quality.** Subject to various caveats, there is an implied condition that goods sold in the course of a business are of merchantable quality¹¹⁰. “Merchantable quality” is defined under the SGO as “fit for the purpose or purposes for which goods of that kind are commonly bought... of such standard of appearance and finish... [are] free from defects... safe... [and] durable, as it is reasonable to expect having regard to any description applied to them, the price (if relevant) and all the other relevant

103 SGO section 14(1)(a).

104 *Rowland v Divall* [1923] 2 KB 500.

105 *Niblett v Confectioners’ Material Co Ltd* [1921] 3 KB 387.

106 SGO section 14(1)(b).

107 SGO section 15(1).

108 *Varley v Whipp* [1900] 1 QB 513.

109 *William Zamara v The Shui Hing Co Ltd* (1951) 35 HKLR 1.

110 SGO section 16(2).

circumstances”¹¹¹. What quality may be expected of a particular good and whether it is of merchantable quality depends on the facts of each case¹¹².

- (2) The caveats include: where a certain defect is drawn to a buyer’s attention before the contract of sale¹¹³; where the buyer examines the goods before the contract is made and his examination ought to have revealed that defect¹¹⁴; or where sale is by sample, that defect which would have been apparent on a reasonable examination of a sample, regardless of whether the buyer actually examined the sample¹¹⁵.
- (3) **Fitness for purpose.** A second implied condition under section 16 arises where the buyer, expressly or impliedly, makes known to the seller any particular purpose for which he buys the subject goods. In that situation, it is a condition on the seller’s part that the goods are reasonably fit for that purpose, even if it is not a purpose for which such goods are commonly supplied¹¹⁶. What is “reasonably fit” is a question of fact. The more specific the buyer’s purpose, the narrower the range of goods the seller can supply to satisfy the condition¹¹⁷.
- (4) However, no condition is implied if the buyer does not rely on the seller’s skill or judgment in supplying the goods, or, even if the buyer does so rely, where it is unreasonable for him to do so¹¹⁸.

80. Under section 17, conditions in relation to a sale by sample are implied on the seller’s part.

- (1) **Correspondence.** There is an implied condition that the bulk of the goods correspond with the sample in quality¹¹⁹.
- (2) **Opportunity to compare.** There is an implied condition that the buyer must be given reasonable opportunity to compare the bulk with the sample¹²⁰.
- (3) **Free from latent defects.** There is also an implied condition that the goods are free from latent defects which would not be apparent upon

111 SGO section 2(5).

112 *Rogers v Parish (Scarborough) Ltd* [1987] 2 All ER 232.

113 SGO section 16(2)(a).

114 SGO section 16(2)(b).

115 SGO section 16(2)(c), Guest (n 4) paras. 11-070, 11-078, 11-080.

116 SGO section 16(3).

117 *Henry Kendall & Sons v William Lillico & Sons Ltd* [1969] 2 AC 31.

118 SGO section 16(3).

119 SGO section 17(2)(a).

120 SGO section 17(2)(b).

reasonable examination of the sample, but which render the goods merchantable¹²¹.

- (4) Mere display of a sample does not itself constitute a sale by sample. A term must be included in the contract for sale to that effect for section 17 to apply¹²².

81. The importance of the terms implied under sections 14 to 17 of the SGO ought not to be overstated in the context of international sales. In domestic sales, those terms are often protected from being contracted out of by section 11 of the CECO, hence taking the nature of mandatory local law. However, that protection is disappplied from international sales, including sales between Mainland China and Hong Kong businesses, under sections 16 and 17 of the same Ordinance (see paragraph 64 above)¹²³.

(B) Buyer's Obligations under the SGO

82. The primary duty of a buyer is also summarised at section 29 of the SGO. It is his duty to accept and pay for the subject goods in accordance with the terms of a contract of sale. This can be conceptualised as separate duties to: (1) accept delivery, and (2) make payment.

83. The buyer's duty to accept delivery is part and parcel with his right to examine the goods post-delivery as well as his right to reject the goods. Notwithstanding the latter right, section 37 of the SGO provides that certain conduct or inaction on the buyer's part may be deemed to constitute acceptance of the goods. The buyer's right to reject is then lost.

- (1) **Acceptance.** The buyer is deemed to have accepted the goods when he intimates to the seller that he has accepted them¹²⁴; or when the goods have been delivered to him and he does any act which is inconsistent with the ownership of the seller¹²⁵; or after the lapse of a reasonable time, he retains the goods without intimating to the seller that he has rejected them¹²⁶. What is "a reasonable time" is a question of fact and includes giving the buyer reasonable opportunity to examine the goods for defects - for section 37(2) purposes - and deciding what to do with those goods¹²⁷.

- (2) **Examine post-delivery.** The deeming provisions in sections 37(1)

121 SGO section 17(2)(c).

122 *Technology Innovation Manufacturing Ltd v Good Power International Ltd* (unrep., DCCJ 4301 and 4318/2003, 3 October 2007).

123 Section IV(F) (Control of Onerous Terms) above.

124 SGO section 37(1)(a).

125 SGO section 37(1)(b).

126 SGO section 37(4).

127 *Gilman & Co Ltd v Yau Shun Printing Press* [1977-1979] HKC 300.

and (4) are subject to the buyer's right to examine the goods after delivery. If the buyer has not examined the goods before delivery, he will not be deemed to have accepted the goods upon delivery unless he has had a reasonable opportunity of examining them¹²⁸. Where the buyer deals as consumer, his right of examination post-delivery cannot be waived or excluded by agreement¹²⁹.

(3) **Rejection.** If the buyer's right to reject is not lost and he exercises it, it is sufficient for him to intimate his rejection to the seller¹³⁰. Unless otherwise agreed, he is not bound to return the goods to the seller¹³¹.

(4) The buyer may, however, be liable in damages (and/or an action for price under section 51) for neglecting or refusing to take delivery of the goods if he does not take delivery within a reasonable time after the seller requests him to do so¹³². The basis and calculation of such damages to which the seller may be entitled are explained below.

84. The buyer's duty to pay for the goods is primarily determined by the terms of the contract for sale. Elements such as the amount, method, place and time for payment are usually agreed expressly. Where the contract does not so stipulate, the SGO and rules of the common law apply (as the case may be) to circumscribe the buyer's duty. For example, where the contract is silent on the time of payment, payment will *prima facie* be due when the seller informs the buyer he is ready and willing to deliver the goods¹³³.

(C) Seller's Remedies for Breach

85. The seller's remedies for breach can be broadly classified as either "real" or "personal". The latter are remedies for a claim for money which the seller may exercise against the buyer personally whereas the former are remedies against the goods themselves.

86. In practical terms, real remedies allow an unpaid seller to protect his interests beyond pursuing the potentially bankrupt buyer as an unsecured creditor. By implication of law and subject to the SGO, the real remedies available comprise a lien on the goods, a right of stoppage in transit, and a right of resale¹³⁴.

(1) As a preliminary point, the remedies are only available if the seller is

128 SGO section 37(2).
129 SGO section 37(3).
130 SGO section 38.
131 SGO section 38.
132 SGO section 39.
133 SGO section 30.
134 SGO section 41.

an “unpaid seller”. The whole of the contract price should be unpaid or untendered¹³⁵. For example, the seller is not an unpaid seller where a cheque received by him as conditional payment is current, and as such the real remedies are not available to him. However, they revive if the cheque becomes dishonoured.

- (2) **Unpaid seller’s lien.** The lien essentially entitles the seller in possession of the goods to retain them - thereby overriding his duty to deliver - until the buyer has paid or tendered the whole price. It arises where the goods have been sold without stipulation as to credit, or when the buyer becomes insolvent¹³⁶. Where part delivery has been made, it is nevertheless possible for the seller to exercise his lien over the remainder of the goods if the buyer cannot show the seller has waived the lien¹³⁷. The seller also loses his lien when he delivers the goods to a carrier or when the buyer lawfully obtains possession of the goods¹³⁸.
- (3) **Stoppage in Transit.** Like the unpaid seller’s lien, the right of stoppage is also intended to protect an unpaid seller whose goods have not reached the buyer. Where the goods are in transit, the seller has the right to halt the transit and resume possession of the goods if the buyer becomes insolvent¹³⁹. This is the case notwithstanding property has passed to the buyer¹⁴⁰. The right is extinguished when the goods are no longer in the course of transit, namely when the buyer takes delivery from the carrier¹⁴¹.
- (4) **Right of resale.** The right of resale is important as the contract of sale is not rescinded by the unpaid seller merely exercising either his lien or right of stoppage¹⁴². If property in the goods has passed to the buyer, the seller can only reclaim property by validly terminating the contract. For example, he may do so by reselling¹⁴³.
- (5) The seller may resell if he is entitled to exercise his statutory right of resale¹⁴⁴, or the contract expressly provides for him to do so¹⁴⁵, or he is entitled to terminate the contract under common law (for example by accepting the buyer’s repudiation). The statutory right arises where firstly, the goods are perishable or the seller gives

135 SGO section 40(1).
136 SGO section 43(1).
137 SGO section 44.
138 SGO section 45.
139 SGO section 46.
140 *Ex p Chalmers* (1873) LR 8 Ch App 289.
141 SGO section 47(1).
142 SGO section 50(1).
143 SGO section 50(2).
144 SGO section 50(3).
145 SGO section 50(4).

notice to the buyer of his intention to resell, and secondly, the buyer does not pay or tender the price within a reasonable time. If engaged, the statutory right additionally entitles the seller to sue the buyer for damages occasioned by his breach.

87. In any case, the seller may sue for personal damages against the buyer under the SGO if the buyer refuses to accept and pay. Where property in the goods has passed, the usual remedy is a claim for price under section 51. Where property remains with the seller, the usual remedy is a claim for damages for non-acceptance under section 52. An overview of the two actions is provided below, as well as the possibilities of special or consequential damages and other miscellaneous remedies.

- (1) **Claim for price.** Where property has passed to the buyer and the buyer wrongfully neglects or refuses to pay for the goods according to the terms of the contract, the seller may claim the price as a debt against the buyer¹⁴⁶.
- (2) The time when property passes to the buyer is important to section 51(1), which is a matter of construing the terms of the contract. For example, the terms governing passing of property may be different under a CIF or FOB contract. If property has not passed, the seller may not take action to claim for the price, even if the passing of property was prevented by the buyer's breach¹⁴⁷.
- (3) No mitigation on the seller's part is required under section 51 as the action is one in debt, and the rules as to remoteness do not apply.
- (4) **Damages for non-acceptance.** Where the property in the goods remains with the seller and the buyer wrongfully neglects or refuses to pay for the goods, the usual remedy is to claim damages for non-acceptance against the buyer¹⁴⁸.
- (5) The general rule for assessing damages under this action is that the quantum will be the "estimated loss directly and naturally resulting... from the buyer's breach"¹⁴⁹. However, the general rule is overridden by the "market price rule" under section 52(3). The market price rule ascertains, *prima facie*, the seller's damages by deducting the market price of the goods at the time which the buyer ought to have accepted the goods from the contract price. If no time for acceptance is expressly agreed, the market price to be deducted is that at the time of neglect or refusal to accept the goods¹⁵⁰.

146 SGO section 51(1).

147 *Stein, Forbes & Co v County Tailoring Co* (1916) 86 LJKB 448.

148 SGO section 52(1).

149 SGO section 52(2).

150 SGO section 52(3).

- (6) The application of this rule is only possible where there is an “available market” for the goods in question. Whether an available market exists depends on, for example, the existence of price fluctuations¹⁵¹, an immediate access to substitute buyers or sellers¹⁵², and market size¹⁵³ are each relevant albeit not conclusive.
- (7) The market price rule becomes difficult to apply where the goods in question have a fixed retail price. In one case, a seller was compensated by the difference between the contract price and the cost of the goods¹⁵⁴. In short, the retail price was disregarded and the seller was awarded the profits which he would have made from the sale. The market price rule was held not to apply in this scenario.
- (8) Where the market price rule is inapplicable and the general rule under section 52(2) operates, the rules on mitigation will apply *prima facie*. Damages awarded may be reduced if the seller does not limit his loss by promptly reselling them after the buyer fails to accept the goods.
- (9) **Special or consequential damages.** The unpaid seller who resells the goods by way of section 50 may also claim damages for the actual loss incurred and any expense reasonably incurred as a result of the buyer’s breach or in connection with the resale. The actual loss is the difference between the contract price and the resale price (although the seller should rely on section 52(3) instead if he has resold at a price lower than the market price).
- (10) The seller is also entitled to claim interest and special damages¹⁵⁵. This is usually confined to claiming interest on the money lost.
- (11) **Miscellaneous remedies.** Various miscellaneous remedies are available to the seller depending on the circumstances. A seller may be entitled to bring proceedings under the ordinary law of contract or tort. Declarations and injunctions might be sought.

(D) Buyer’s Remedies for Breach

88. As mentioned earlier, a buyer who has not accepted the goods has the right to reject the goods where the seller breaches the express or implied conditions of the contract.

151 *Thompson Ltd v Robinson (Gunmakers) Ltd* [1955] Ch 177.

152 *Elbingen Aktien Gesellschaft v Armstrong* (1874) 9 QB 473.

153 *Kwei Tek Chao v British Traders & Shippers Ltd* [1954] 2 QB 459.

154 *Thompson Ltd v Robinson (Gunmakers) Ltd* [1955] Ch 177.

155 SGO section 56.

89. Action(s) for damages can also be brought. The SGO and the rules of common law provide for various measures of damages which the buyer may claim.

- (1) **Damages for non-delivery.** An action may be brought for the non-delivery of the goods or for a breach in a term of the contract¹⁵⁶. The measure of damages is the same as that for the seller's claim for damages for non-acceptance under sections 52(2) and (3)¹⁵⁷. Namely, the general rule to assessment damages for non-delivery applies if the market price rule does not. Where the market price rule applies, the measure of damages is *prima facie* to be ascertained by the difference between the contract price and the market price of the goods at the time which they ought to have been delivered (or at the time of the seller's neglect or refusal to deliver). The same factors are relevant as to whether there is an "available market" for engaging the market price rule in the first place.
- (2) **Damages for delay in delivery.** Where delivery of the goods is late but the buyer nevertheless accepts the goods, he may claim for damages for delay in delivery. Although the SGO does not expressly provide for such damages to be sought, it appears to fall within the scope of section 55(2), namely as a claim for damages flowing from a breach of warranty.
- (3) Where there is an "available market" for the goods, the normal measure of damages is the difference between the market price at the agreed time and place, and the market price at the time and place which the goods were actually delivered¹⁵⁸. Where there is no available market, it may be possible to recover damages from the buyer's loss of use of the goods during the interim period¹⁵⁹.
- (4) **Damages for defective quality.** Where the seller breaches a warranty as to the quality of the goods, the buyer may claim damages for their diminution in market value¹⁶⁰. The *prima facie* rule for the measure of damages in such circumstances is the difference, assessed as at the time of delivery, between (1) the value of the goods had they complied with the undertaking as to quality, and (2) the value of the goods in their actual condition¹⁶¹. This rule may be departed from in appropriate circumstances. For example, in the case where a defect was discovered after delivery, the assessment of difference in value may take place at the time which the defect

156 SGO section 53(1).

157 SGO sections 53(2) and (3).

158 *Koufos v C Czarnikow Ltd (The Heron II)* [1969] 1 AC 350.

159 *Cory v Thames Ironworks Co* (1868) LR 3 QB 181.

160 SGO section 55(1).

161 SGO section 55(3).

was discovered, rather than at delivery¹⁶².

- (5) Where there is an “available market”, the market values to be contrasted are the relevant market prices. Where there is no available market, any relevant evidence (though not the contract price¹⁶³) will be considered in ascertaining market value.
- (6) **Special or consequential damages.** A buyer who later discovers a defect may recover special or consequential loss caused by the defect, including (but not limited to) expenses reasonably incurred as a result of the seller’s breach and within the parties’ reasonable contemplation at the time of contract¹⁶⁴ and loss of profits caused by the seller’s breach and within the parties’ reasonable contemplation at the time of contract¹⁶⁵. The buyer may not, however, recover further losses which he ought reasonably to avoid after discovering the defect¹⁶⁶.
- (7) **Miscellaneous remedies.** Various miscellaneous remedies, similar to those available to the seller, are available to the buyer depending on the circumstances.
- (8) The SGO also provides that an order for specific performance of a contract of sale for specific or ascertained goods can be made¹⁶⁷. However, the courts are usually reluctant to do so where damages would be an adequate remedy, as is frequently the case with sale. The most common exception is where the goods are unique; nonetheless, the court in such circumstances retains an overall discretion¹⁶⁸.

(E) Property and Risk

90. Additionally, the SGO prescribes rules on the transfer of property in the subject goods and the passing of risk. Whether property in the goods and the risk in them have passed may affect whether (as set out above) certain remedies are available to the parties (e.g. the action for the price).
91. The significance of property in the goods passing is that the buyer will then generally have good title in the goods even if the seller still has possession.

162 *Naughton v O’Callaghan* [1990] 3 All ER 191.

163 *Minster Trust Ltd v Traps Tractors Ltd* [1954] 1 WLR 963.

164 *Yu Fat Piece Goods Co Ltd v Peter Mercantile Co Ltd* (unrep., DCCJ 2798/2002, 14 March 2006).

165 *Croydex Ltd v Tung Shing Plastic Factory Ltd* [2007] 3 HKLRD (Yrbk) 550.

166 *Lambert v Lewis* [1982] AC 225.

167 SGO section 54.

168 Alastair C.L. Mullis, ‘Termination for Breach of Contract in CIF Contracts under the Vienna Convention and English Law; Is There a Substantial Difference?’ in Lomnicka & Morse (eds), *Contemporary Issues in Commercial Law* (Sweet & Maxwell 1997) 137 at footnotes 32-33.

The seller can then sue for the contract price if the buyer wrongfully neglects or refuses to pay for the goods in accordance with the contract¹⁶⁹.

92. Risk will *prima facie* pass when property passes¹⁷⁰. Where risk has passed to the buyer, he has to pay the contract price even if he does not receive the goods or if the goods are damaged or lost. The buyer cannot sue the seller in damages for failing to make delivery or for delivering less than the contracted quantity of goods or damaged goods. On the other hand, where risk has not passed from the seller, the buyer is entitled to reject the goods. The seller cannot compel the buyer to pay the contract price or take delivery of remaining or damaged goods, nor can he sue the buyer for damages for refusing to do so.
93. However, the parties' duties and liabilities as bailee of the goods are not affected by the operation of section 22. An action in bailment - depending on whichever party is the bailee - is independent of whether property and risk have passed.
94. As to whether property (and therefore *prima facie* risk) passes, the nature of the subject goods is a significant consideration. Whether the sale concerns specific and ascertained goods or unascertained goods determines the rules of property transfer which apply.

(1) **Specific and ascertained goods.** The general rule is that property is transferred to the buyer "at such time as the parties to the contract intend it to be transferred"¹⁷¹. Whilst the parties may expressly or impliedly agree on the time which property passes, section 20 of the SGO sets out various rules for presuming that intention where the contract is silent. For example, the time which property passes depends on whether the contract unconditionally sells the goods in a deliverable state¹⁷², or the seller is bound to put the goods into a deliverable state¹⁷³ or ascertain the price of the goods¹⁷⁴, or the goods are delivered to the buyer on approval¹⁷⁵.

(2) **Unascertained goods.** Where the subject goods are unascertained, property does not pass to the buyer "unless and until the goods are ascertained"¹⁷⁶. Where, for example, unidentified goods are transferred but deteriorated as a result of delay, property in them does not pass and the seller bears the risk of that damage¹⁷⁷.

169 SGO section 51.
170 SGO section 22.
171 SGO section 19(1).
172 SGO section 20 rule 1.
173 SGO section 20 rule 2.
174 SGO section 20 rule 3.
175 SGO section 20 rule 4.
176 SGO section 18.
177 *Healy v Howlett & Sons* [1917] 1 KB 337.

However, property passes if unascertained goods are unconditionally appropriated to the contract¹⁷⁸.

95. The *prima facie* passing of risk alongside property may be rebutted in certain circumstances. Where “control” (namely, the power of appropriation) in the goods has passed to the buyer, risk passes to him ahead of property. For example, the buyer’s acceptance of a delivery warrant, pursuant to which a third party undertakes to deliver the goods in accordance with the holder’s instructions, suffices to transfer the risk notwithstanding that property does not¹⁷⁹.

VI. Avoiding a Contract of Sale

96. This section briefly touches on various common methods in which a contract of sale can be vitiated or set aside under Hong Kong law.

(A) Mistake

97. Generally, mistakes in Hong Kong law arise in any of three varieties, including common mistakes, mutual mistakes and unilateral mistakes:

- (1) **Common mistake.** A common mistake occurs when the parties both labour under the same mistake. In other words, the parties have in fact reached consensus, albeit such consensus is based on the same wrong assumption. Not all common mistakes are legally relevant - relief only follows where the mistake is such that the adventure contracted for is impossible to perform¹⁸⁰, and also where the contract has not already expressly allocated the risk of the impossibility to one party¹⁸¹.
- (2) Common mistakes as to the existence of the subject-matter are usually sufficiently fundamental to trigger the doctrine; on the other hand, common mistakes as to quality will usually not suffice¹⁸².
- (3) In the sale of goods context, section 8 of the SGO codifies one scenario of common mistake: where goods to a contract of sale have perished without the knowledge of the seller (hence the seller is mistaken as to their existence) at the time of contract, the sale is avoided.

178 SGO section 20 rule 5.

179 *Sterns Ltd v Vickers Ltd* [1923] 1 KB 78.

180 *Great Peace Shipping Ltd v Tsavliris Salvage (International) Ltd* [2003] QB 679 at 703.

181 *Tony Investments Ltd v Fung Sun Kwan* [2006] 1 HKLRD 835.

182 Beale (n 21) paras. 6-046, 6-048.

- (4) **Mutual mistake.** A mutual mistake occurs when the parties are at cross-purposes with each other over some fundamental fact. In these cases, the parties in fact never reach agreement. However, such a mistake is legally relevant only where the court considers that the mutual mistake was made reasonably, i.e. that it was reasonable for each party to hold the belief that they did¹⁸³.
 - (5) **Unilateral mistake.** A unilateral mistake occurs when only one of the parties is mistaken as to the terms of the contract, and such mistake is known to the other party¹⁸⁴.
 - (6) Common examples of such unilateral mistake involve cases of mistaken identity, where one party mistakenly believes he is contracting with X when in fact he is dealing with Y (usually due to fraud on the part of Y)¹⁸⁵.
98. Generally, the effect of a relevant mistake being established is to show that the contract (on the terms apparently agreed) is void *ab initio*, although it has been controversially held in some cases of unilateral mistake that a contract may be formed on the terms that the mistaken party intended (but failed to express objectively), and the contract may be so rectified¹⁸⁶.

(B) Misrepresentation

99. Misrepresentations are: (1) pre-contractual statements (generally of fact, albeit in certain circumstances also of opinion or intention, such as where one party has superior knowledge or expertise of the contractual subject-matter), (2) made with the intention of inducing the other party to enter into the contract, (3) which did in fact induce the other party to so act, and (4) which are false¹⁸⁷.
100. Misrepresentations are generally categorised as fraudulent, negligent or innocent, depending on the degree of fault of the misrepresenter. Relief for each is different:
- (1) **Fraudulent misrepresentation.** The innocent party can seek to rescind (and hence avoid) the contract and make restitution of the benefits exchanged thereunder as of right (subject to common law restrictions on rescission), and can alternatively seek damages.
 - (2) **Negligent misrepresentation.** The innocent party can seek

183 *Ibid* para. 3-019.

184 *Ibid* paras. 3-022, 3-025.

185 Fisher & Greenwood (n 19) para. 10.5.2.

186 Beale (n 21) para. 3-009.

187 Hall (n 43) paras. 7-6, 7-24, 7-36.

damages (under common law or section 3(1) of the Misrepresentation Ordinance (Cap. 284) (“MO”). It may also seek to rescind the contract, but in addition to the common law restrictions is also subject to a statutory discretion under section 3(2) of the MO, which enables the court to award damages in lieu of rescission.

- (3) **Innocent misrepresentation.** The recipient of the misrepresentation can only seek rescission, subject again to the MO. The only way it may be awarded damages is if the court awards damages in lieu of rescission.

(C) Frustration

101. Frustration can be defined as “something occur[ring] after the formation of the contract which renders it physically or commercially impossible to fulfil ... or transforms the obligation to perform into a radically different obligation” from that originally bargained for¹⁸⁸. To that core definition may be added the remarks that the occurrence must be (1) unforeseen by the parties and not provided for in the contract; and (2) not the fault of either party¹⁸⁹.

102. The modern approach is “multi-factorial” and assesses the whole of the relevant factual matrix:

“Among the factors which have to be considered are the terms of the contract itself, its matrix or context, the parties’ knowledge, expectations, assumptions and contemplations, in particular as to risk, as at the time of contract ... and then the nature of the supervening event, and the parties’ reasonable and objectively ascertainable calculations as to the possibilities of future performance in the new circumstances.¹⁹⁰”

103. In the case law, common examples of frustration include:

- (1) Impossibility of performance (e.g. destruction of subject-matter, death or incapacity of the contracting parties in cases of personal contracts, impossibility of performing by a specified manner such as by shipping via a named vessel)¹⁹¹;
- (2) Failure of the jointly held commercial purpose underlying the contract (e.g. where a flat was rented to view the coronation of the King, but where such coronation was cancelled¹⁹²); and

188 Beale (n 21) para. 23-001.

189 Fisher & Greenwood (n 19) para. 14.4.

190 *The Sea Angel* [2007] 2 Lloyd’s Rep 517 [111].

191 Hall (n 43) paras. 17-8, 17-10, 17-19.

192 *Krell v Henry* [1903] 2 KB 740.

- (3) Supervening illegality¹⁹³.
- (4) Examples of frustration specifically in the sale of goods context include:
 - (a) Section 9 of the SGO, which provides that where goods specified in an agreement to sell perishes before the sale (and hence the passing of risk to the buyer), the contract is “avoided”.
 - (b) Supervening illegality due to state action, e.g. where a Hong Kong international sale of goods contract was frustrated by the supervening imposition of foreign payment controls¹⁹⁴. However, where there is no absolute embargo on the specified type of international sale but only a new requirement to obtain a licence, the seller cannot rely on frustration until he has applied for such a licence and been refused¹⁹⁵.
 - (c) Unexpected delay in completion, as in a series of cases concerning the closure of the Suez Canal in 1956 which would have forced sellers to reroute goods shipped via the Cape of Good Hope (which journey was much longer and far more costly). In line with the multi-factorial approach discussed above, whether the contract was frustrated depended on (i) whether the goods were perishable, (ii) whether a definite date of delivery (as opposed to shipment) was provided for in the contract, and (iii) whether there was sufficient shipping capacity to carry the goods via the new route¹⁹⁶.

104. The effect of frustration is that the contract is automatically discharged forthwith by the operation of law. Parties are released from further performance of the contract¹⁹⁷.

105. However, the parties may have partially performed the contract already or incurred expenses in preparation therefor prior to the frustrating event. Hong Kong law therefore empowers the courts, generally via section 16 of the Law Amendment and Reform (Consolidation) Ordinance (Cap. 23) (“LARCO”) to perform a just adjustment in such circumstances:

- (1) Section 16(2) provides that sums payable prior to the frustrating event shall cease to be payable and all sums paid before the frustrating event may be recovered.

- (2) The same section further provides that the party to whom sums were

193 Hall (n 43) paras. 17-31 *et seq.*

194 *Nam Sun Trading Co v Andersen, Meyer & Co Ltd* [1951] 35 HKLR 113.

195 Beale (n 21) para. 23-047.

196 *Ibid* para.23-048, see also *Ocean Tramp Tankers Corp v V/O Sovfracht (The Eugenia)* [1964] 2 QB 226 at 240- 243.

197 Beale (n 21) para. 23-071.

paid or payable has, before the frustrating event, incurred expenses, the court may allow him to retain or recover such payment up to the amount of actual expenses incurred.

- (3) Section 16(3) provides that where any party has obtained a valuable benefit (other than payment of money, which is dealt with in section 16(2)), the other party may recover such sum from him a sum not exceeding the value of the benefit.

106. There is some theoretical debate as to whether the principle underlying section 16 of the LARCO is the reversal of unjust enrichment, or a broader principle of loss apportionment¹⁹⁸. However, for practical purposes, what is important is that (due in part to such theoretical debates and the lack of case law) it is unclear how the discretions allowing the court to adjust the relative sums paid or retained to the parties are to be exercised¹⁹⁹.

107. Finally, in the sale of goods context, there is an important exception to section 16 of the LARCO. Section 17(5) of the LARCO provides that the loss-adjusting provisions of section 16 of the LARCO do not apply to: (1) contracts (other than charterparties) for the carriage of goods by sea, (2) contracts for the sale of specific goods which have perished before the risk has passed to the buyer i.e. those governed by section 9 of the SGO, or (3) contracts for the sale of specific goods which are frustrated by reason that the goods have perished.

- End of Annex 2.1 -

198 *Ibid* paras. 23-075, 23-081.

199 As to section 16(2), see *ibid* para. 23-081; As to section 16(3), see *ibid* para. 23-090.