CU Review Summer 2015

The Commercial Unit, Civil Division
The Department of Justice

What's inside

Attribution of Conduct or States of Mind to Companies 2

Voluntary Health Insurance Scheme – Indemnity Insurance 3

The Relative Importance of Contractual Terms and Remedies for Breach 5

Hua Tyan Development Ltd v Zurich Insurance Co. Ltd (2014) 17 HKCFAR 493 ("Hua Tyan No. 2") 7

Pathak Ravi Dutt v Sanjeev Maheshwari [2014] 3 HKLRD 597 8

Huen Wai Kei v Choy Kwong Wa Christopher (No. 2) [2014] 4 HKLRD 782 10

Editorial

We feature three articles in this edition. The first article is about the modern principles on attribution of conduct and states of mind to companies and two recent cases applying the principles.

The second article talks about the proposed Voluntary Health Insurance Scheme. The public consultation of the scheme ended in April 2015. Public responses generally show support for the scheme and legislative exercise is now under way.

The third article discusses the relative importance of a contractual term – condition, warranty or intermediate, and the remedies available to the innocent party for breach.

We also feature three case reports in this edition. The first case is a re-visit of the Hua Tyan case we reported in the Summer 2013 edition. In this edition, we report that the CFI decision discussed in the Summer 2013 edition has been reversed by the CA and CFA.

In the second case, the CFI reaffirmed the principle that a lack of understanding of the contents, meaning or effect of a document signed by a person of full age and understanding was not a ground to disown the document.

The third case is about past consideration – the existence of the defendant's debt to the plaintiff is insufficient to support the defendant's subsequent promise to put up properties as security for the debt.

YUNG Lap-yan

Attribution of Conduct or States of Mind to Companies

Introduction

Companies are legal persons, but can only act through others, such as their directors, employees or agents. Whether the conduct of an individual is to be attributed to a company depends on the legal rules of attribution. Such rules also deal with attribution of states of mind to companies. This can be important because, for example, the operation of many statutory provisions depends on the state of mind of the person in question, and such a "person" can be a company.

The modern principles on attribution are outlined below, followed by a discussion of two recent cases.

Rules of attribution

In *Meridian Global Funds Management Asia Ltd v Securities Commission*[1], the following categories of rules were set out for determining whether acts or mental states of individuals are to be treated as the company's:

1. Primary rules of attribution: These are set out in the company's constitution or implied by company law. For instance, if the articles of association provide that the directors are to exercise the company's powers of management, then a management decision of the directors would be imputed to the company based on such a primary rule of attribution. As to rules implied by company law, an example is the doctrine of unanimous consent, where a unanimous decision of the members of the company can be regarded as a decision of the company.

2. General rules of attribution: These rules apply to all persons. For instance, under agency law, the act of an agent is attributed to the principal where the agent acts within the scope of the agent's authority (such as where an authorised sales employee enters into a sales contract with a customer on behalf of the employer). These principles apply to agents of a company in a manner similar to other agents.

3. Special rules of attribution: If the above rules are not appropriate in the particular circumstances, the court may devise a special rule to determine whether the conduct or mental state of an individual should be attributed to the company for the purposes of the particular law in question. For instance, the court might decide that the conduct or knowledge of an employee is to be treated as the conduct or knowledge of the company for the purposes of achieving the policy of the particular statutory provision in question, even though such conduct or knowledge would not be attributed to the company under the primary or general rules of attribution.

Bilta (UK) Ltd v Nazir (No.2)

In *Bilta (UK) Ltd v Nazir (No.2)*[2], the directors of a company procured the company to engage in transactions to defraud the Revenue and Customs Commissioners in relation to value added tax ("VAT"). The fraudulent scheme involved the company becoming insolvent, with a VAT liability that it could not pay by reason of its insolvency. The liquidators brought proceedings on behalf of the company against its directors and others to recover compensation for breach of the directors' fiduciary duties. Two defendants sought to have the proceedings dismissed on the basis of the illegality defence. Under this defence, the court would not allow a claimant to succeed in an action that is founded on an illegal act. It was argued that the company was itself a party to the fraud and hence could not rely on its own illegality in the action against the defendants. The issue, then, was whether the fraudulent conduct of the directors would be regarded as the fraudulent conduct of the company for the purpose of the illegality defence.

The court emphasised that it is necessary to consider whether it is appropriate to attribute the individual's action or state of mind to the company for the purpose of the particular law in question[3]. The question of "whether an individual's conduct or state of mind is to be treated as the conduct or state of mind of the company for the purpose in hand" is relevant in

[1] [1995] 2 AC 500

[2] [2015] 2 WLR 1168

[3] *Ibid*, at paras. 37–44, 191

considering all of the three categories of rules of attribution[4]. The question in each case is whether attribution is required to promote the policy of the substantive rule, or (to put it negatively) whether, if attribution is denied, that policy will be frustrated. This approach applies not only in relation to statutory rules, but also to common law rules[5].

Where a third party is pursuing a claim against the company arising from the misconduct of a director, employee or agent, the primary and general (in particular agency) rules of attribution would normally be applied to attribute acts or mental states of the individuals to the company (as long as the individuals are acting within the scope of their authority)[6]. However, in a situation such as in the *Bilta* case, the policy objectives of the law of fiduciary duties would be defeated if the defaulting directors' conduct or state of mind is attributed to the company so as to prevent the company from seeking redress against its directors.

Accordingly, where a company was the victim of wrongdoing by its directors, then the wrongdoing of the directors could not be attributed to the company as a defence to a claim brought against the directors by the company for the loss suffered by the company as a result of the wrongdoing[7]. Thus, the illegality defence failed as the company would not be treated as being a party to the fraud for the purpose of the company's claim against the directors.

Moulin Global Eyecare Trading Ltd v CIR

Moulin Global Eyecare Trading Ltd v CIR[8] involved a company whose accounts were falsified (with profits overstated) by certain directors of the company. The company's tax returns were prepared on the basis of the false accounts. Subsequently, the company went into liquidation, and the liquidator applied for a refund of the overpaid taxes. The time period for the application had expired, and the company's entitlement to object to the tax assessments out of time and also to claim repayment based on errors in its tax returns depended on whether the company was attributed with the directors' knowledge of the fraud.

Under the company's articles, the directors were conferred with responsibility for preparing the company's accounts[9]. The relevant directors were the active perpetrators of the fraud in the preparation of the false accounts on which the tax returns were based. The court applied the primary rules of attribution to attribute their knowledge of the fraud to the company[10].

The court reached a different outcome compared with *Bilta* because the present case did not involve a claim by the defrauded company against the fraudulent directors[11]. Accordingly, the company was treated as having knowledge of the fraud at all times and the liquidator was unsuccessful in obtaining the tax refunds.

Stefan Lo and Ida Chan

Voluntary Health Insurance Scheme – Indemnity Insurance

The public consultation on the proposed Voluntary Health Insurance Scheme **("the Scheme")** launched by the Food and Health Bureau ended in April 2015. Public responses generally show support for the Scheme and the legislative exercise is under way. Perhaps it is time for us to understand more what the Scheme is about in preparation for its implementation, which is going to affect us all. In this article, we will discuss certain insurance law principles relevant to the proposed Scheme.

The insurance business relevant to the Scheme

Aimed at facilitating a greater use of private healthcare services as an alternative to public services through insurance protection, the Scheme intends to regulate "individual indemnity hospital insurance" (as explained below). Under the present insurance regulatory regime, a company may carry on any of the classes of insurance business as specified in the First Schedule of the Insurance Companies Ordinance (Cap.41) **("the Ordinance")** in or from Hong Kong as long as it is duly authorized by the Insurance Authority **("IA")** under the Ordinance to carry on that

4 *Ibid*, at para. 191
5 *Ibid*, at para. 197
6 *Ibid*, at para. 205
7 *Ibid,* at para. 7
8 (2014) 17 HKCFAR 218
9 *Moulin Global Eyecare Trading Ltd (in liq) v CIR* [2012] 2 HKLRD 911 at paras. 57, 64
10 (2014) 17 HKCFAR 218, at para. 130
11 *Ibid*, at paras. 131, 134

class of insurance business[12]. The type of insurance business which is relevant to the Scheme falls within the business in class 2 (sickness) of Part 3 of the First Schedule **("Class 2 business")**, which is defined as "effecting and carrying out contracts of insurance providing fixed pecuniary benefits or *benefits in the nature of indemnity* (or a combination of the two) against risks of loss to the persons insured attributable to sickness or infirmity, but exclusive of contracts falling within class D (of Part 2 of the First Schedule)" *(emphases added)*.

At present, the IA does not regulate the design of insurance products (including healthcare products falling under Class 2 business) and the level of premium payable by policy holders. Potential policy holders are free to buy whatever is available in the market that is suitable for their needs and at the price (i.e. premium) they consider reasonable. Under the proposed Scheme, an insurer, in carrying on Class 2 business, is required to comply with certain minimum requirements to be imposed by legislation if the contracts of insurance provide for benefits in the nature of *indemnity* and where the policy holder / insured person is an individual who needs in-patient treatment in a hospital. What is indemnity insurance then?

Principle of indemnity[13]

An indemnity insurance refers to an insurance where the insured will be reimbursed (i.e. indemnified) by the insurer for his actual loss; that is, the insured will be placed in the position he would have been in had the loss not occurred. The insured, however, is required to prove any loss before he can recover under the insurance policy.

Under common law, for indemnity insurance, it is lawful for a person to insure the same risk on the same interest in the same subject with two or more insurers (i.e. double insurance), even though the aggregate of all the insurances may exceed the total value of the insured's interest (i.e. overinsurance). In case of double insurance or overinsurance, if the policies do not expressly provide for the proportion of liability of each insurer, the insured can choose to recover the total loss from any one or more of the insurers. If the insured does not recover the total loss from one insurer, he may recover the balance from the other insurers. Under the principle of indemnity, however, the insured will not be allowed to recover more than his actual loss. Once the insured has recovered the total loss from one or more of his insurers, his right to indemnity ceases[14].

Medical insurance benefits in the nature of indemnity verses fixed pecuniary benefits[15]

Medical insurance falling under Class 2 business may be in the form of medical expenses cover or fixed income. Medical expenses coverage is designed to reimburse the insured's costs and expenses for his medical treatment for illness. Since this form of benefit is in the nature of indemnity, the principle of indemnity applies and the insured cannot recover more than his actual loss, despite that he may have (over-)insured himself against the same health risks under one or more policies with the same or different insurers. In fact, it is not unseen in the market that medical insurance policies expressly provide for the principle of indemnity to the intent and effect that the insured's entitlement to reimbursement of medical expenses under the policy shall be deducted by the amount reimbursed under other polices.

Under the proposed Scheme, individual indemnity hospital insurance must cover expenses for medical conditions requiring hospital admission (e.g. daily room and board charges, surgeon and anaesthetist fees), prescribed ambulatory procedures, prescribed advance diagnostic imaging tests (subject to co-insurance) and non-surgical cancer treatment. The limit of indemnity for each benefit shall meet the respective levels to be prescribed in the legislation. There shall also be restriction on cost-sharing (e.g. deductible or co-insurance) by policy holders[16].

---

[12] Sections 3, 6(1) and 8 of the Ordinance

[13] Insurance Law and Practice in Hong Kong, edited by S.H. Goo and Robert Merkin and others, 2003 edition, paras.4-6 and 16-1 to 16-6; Colinvaux's law of Insurance in Hong Kong, Robert Merkin, 2nd edition, paras.4.003, 11.005 and 11.039

[14] *Millandon v Western Marine and Fire Ins. Co. 9La 27.32 [1836]; Godin v London Ass. Co. [1758] 1 Burr. 489; 1W. BL. 105; Bank of North America v Western Assurance Co. [1884] 7 Ont.R.166 and Simcock v Scottish Imperial Ins. Co. [1902] 10 S.L.T. 286* as cited in Insurance Law and Practice in Hong Kong, para.16-1

[15] Insurance Law and Practice in Hong Kong, paras.24-61 to 24-67

[16] See Chapters 2 and 3 of the consultation document issued in December 2014 for the twelve minimum requirements under the proposed Scheme

Medical insurance covering hospitalization may also be in the form of fixed income[17]. Such cover provides for a fixed cash benefit payable for each day of hospitalization due to a sickness or accident. This type of cover is not one of indemnity and, therefore, will not be regulated under the proposed Scheme.

Critical illness cover typically provides a lump-sum cash payment if the insured is diagnosed with a disease as designated in the insurance policy e.g. cancer. The lump-sum cash payment under a critical illness cover is often seen as an advance payment of death benefit, i.e. the payment is not an indemnity of actual loss. Like fixed income benefit, this type of cover will not be regulated under the proposed Scheme. It will also not be regulated for reason that the cover is attached to or form part of a hospital insurance which provides for benefits in the nature of indemnity.

Lily Man

The Relative Importance of Contractual Terms and Remedies for Breach

It goes without saying that not all contractual terms are of equal importance. When a contractual term is breached, the remedies available to the innocent party are dependent upon the relative importance of that term in the contract in question. Generally, where a party fails to fulfil a contractual obligation, the innocent party will have the right to recover from the defaulting party damages. However, where a party fails to fulfil a more important contractual obligation, it may give the innocent party the additional right to refuse to perform his obligations and to bring the contract to an end entirely (i.e. to treat himself as discharged).

Condition vs. Warranty

Traditionally, contractual terms were classified into either conditions or warranties. The effect of such classification can be seen in the Sale of Goods Ordinance (Cap. 26) ("SOGO"). Under section 13(2) of SOGO, a condition is defined as a stipulation the breach of which may give rise to the right to treat the contract as repudiated. Warranty is defined in section 2(1) of SOGO as "an agreement the breach of which gives rise to a claim for damages, but not to a right to reject the goods and treat the contract as repudiated". Case laws show that such distinction was also accepted by the courts in considering contractual disputes involving other types of contract. Hence, the general principle is that a breach of a condition entitles the innocent party to treat the contract as coming to an end (thus freeing himself from further performance under the contract) and to claim damages for loss sustained by the breach, whereas a breach of warranty only gives the innocent party the right to claim damages but he cannot treat the contract as repudiated.

The advantage of classifying the contractual terms into either condition or warranty is that it provides certainty. The innocent party will know that if the other party has broken a condition, there is a right to terminate. However, scholars have criticised that the dichotomy of condition and warranty is rigid and unsatisfactory because some terms can be breached in more than one way and the consequences of the breach can be serious or trivial. If a term is classified by the contracting party or the court as a condition, the innocent party can repudiate the contract even if that term is breached in a trivial way and the innocent party has suffered no or only trifling loss[18].

Intermediate Term and Seriousness of a Breach

In view of the rigidity in the distinction, an alternative approach was developed by the court, under which the court would look at the nature and seriousness of the breach itself to determine the remedies available to the innocent party.

In *Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd*[19], the plaintiffs owned a ship which they chartered to the defendants and the relevant contractual term stipulated that the ship for charter would be "seaworthy". This might seem to be an important contractual term but in fact a ship can fail to be seaworthy in serious circumstances (e.g. due to a large hole in the hull) or for trivial reasons (e.g. missing a signal light bulb). The parties did not classify the seaworthiness term as condition or warranty. Despite this, the seaworthiness term was a standard clause commonly found in charter party in those days and was often described as a warranty.

---

17 For example, "hospital cash" as so called in the industry

18 *Atiyah's Introduction to the Law of Contract* (6th ed., 2005), p. 198.

19 [1962] 2 Q.B. 26.

On delivery of the ship, there were a number of defects involving the size of the crew and the crew's inability to handle the old engines on board. As a result, the ship was out of service for 20 weeks out of a two-year contract period and the defendants repudiated the contract on the grounds that the ship was not seaworthy and the plaintiffs had breached the contract.

The English Court of Appeal unanimously held that although the defendants were entitled to damages, the plaintiffs' breach did not substantially deprive the defendants of the whole benefit of the contract. The defendants were held to have wrongfully repudiated the contract. Instead of adopting the traditional classification of contractual terms into conditions and warranties, the Court of Appeal considered that there may be an "intermediate" or "innominate" class of terms which were not conditions but the breach of which might justify termination of the relevant contract provided that the consequences of the breach were sufficiently serious. If the breach of an intermediate term substantially deprived the innocent party of the whole benefit which it was intended that he should obtain from the contract, the breach was sufficiently serious to entitle the innocent party to terminate the contract.

In a line of cases which adopt the approach of *Hongkong Fir*, it was further established that a right to terminate a contract also arises where a breach of an intermediate term rendered it impossible for the parties to perform the contractual obligations[20].

Criticisms on the *Hongkong Fir* Doctrine

The approach adopted in *Hongkong Fir* has been criticized for creating uncertainty because it can be difficult to predict when the court will find a breach of contract to be sufficiently serious to entitle the innocent party to terminate the contract. Also, an innocent party may be held liable for wrongful repudiation of the contract if, after the contract was terminated, it is discovered that the breach did not deprive the innocent party substantially the whole benefit of the contract.

Thus, in some cases[21] subsequent to *Hongkong Fir*, the court considered that the distinction between condition and warranty was still valuable and remained important in the interest of certainty.

The present position seems to be that when determining whether a breach will entitle an innocent party to repudiate the contract, the court will construe the contract as a whole. Parties can expressly indicate in the contract the consequences to be attached to a particular breach to reflect their intention to treat a contractual term as a condition. But the court may not treat this as conclusive. The court will give weight to both the intention of the parties and the seriousness of the breach before deciding whether the innocent party is entitled to repudiate the contract. If the parties have clearly spelt out their intention, the court may give less weight to the seriousness of the breach.

Where the parties do not label a contractual term as condition or there is no indication that a breach of a contractual term would result in termination of the contract, in the absence of any applicable statute classifying the term (such as SOGO), the court will treat the contractual term as an intermediate term and determine the remedy available based on the seriousness of the breach. In such circumstance, the innocent party will be entitled to repudiate the contract only if the effect of breach of the intermediate term deprives the innocent party of substantially the whole benefit of the contract, or renders it impossible for the parties to perform the contractual obligations.

Fiona Lai

[20] *Chitty on Contracts, Volume I: General Principles* (30th ed., 2008), p.833

[21] *Mihalis Angelos* [1970] 3 All ER 125, *Bunge Corporation v Tradax Export SA* [1981] 2 All ER 513.

Hua Tyan Development Ltd v Zurich Insurance Co. Ltd (2014) 17 HKCFAR 493 ("Hua Tyan No. 2")

CU Review Summer 2013

Back in the issue of ***CU Review Summer 2013***, we saw how the Court of First Instance ("CFI") in *Hua Tyan*[22] ("*Hua Tyan* No.1") held that a Dead Weight Tonnage warranty ("DWT Warranty") of a marine insurance policy (the "Policy") could be rejected on the basis that it was inconsistent with the vessel that was expressly named in the Policy. The reason was to give effect to the "real intention" of the parties when considering the policy "as a whole".

Hua Tyan No.1

The plaintiff insured ("P") obtained the Policy issued by the defendant insurer ("D") covering a cargo of round logs ("Cargo"). After the vessel ("Vessel") carrying the Cargo sank, P brought a claim against D which D denied alleging that P had breached a condition that the Vessel's DWT must not be less than 10,000 and/or was guilty of material non-disclosure on this issue, which would entitle D to avoid the Policy.

The Vessel had a DWT of some 8,960 as expressed in the Policy. It was not in dispute that the DWT of a named vessel was relatively easily available through the Internet.

The CFI found that by giving effect to the named Vessel alone, but not to do so for the DWT Warranty, would enable the contractual intention of the parties to be carried into effect, namely, to provide insurance coverage for the Cargo. The CFI further remarked that had it been necessary to do so, it would have rectified the Policy by deleting the DWT Warranty.

The CFI's decision was reversed by the Court of Appeal.

Hua Tyan No.2

On appeal against the Court of Appeal's decision, the Court of Final Appeal ("CFA") dismissing P's appeal, ruled that:

(1) there is no inconsistency between the DWT Warranty and the naming of the Vessel, hence, the DWT Warranty stands;

(2) pursuant to section 33 of the Marine Insurance Ordinance (Cap. 329) (the "MIO"), if a warranty is not exactly complied with, D is discharged from liability from the date of the breach of warranty. Since the Vessel was incapable of reaching the capacity as specified in the DWT Warranty, therefore D's liability has been discharged;

(3) information that is readily available on the internet in the absence of common practice, is not equivalent to an insurer's constructive knowledge; and

(4) the factual matrix of the case could not undermine or nullify the terms of a contract when they are already clear and unequivocal[23].

No inconsistency in the policy terms

CFA sees no inconsistency in the Policy between the identification of the Vessel and the existence of the DWT Warranty because:

"The mere fact that a vessel is named in a contract of marine insurance does not mean in any way that an insurer is somehow prevented from insisting by way of warranty on that vessel possessing certain characteristics"[24].

DWT Warranty

A warranty is an affirmation of the existence of a particular state of facts. These, according to the CFA, are subject to section 33 of the MIO. When such warranties are not inconsistent, they stand to be exactly complied with, failing which, D's liability will be discharged from the date of non-compliance.

State of knowledge of D

Knowledge of parties may sometimes result in some

[22] *Hua Tyan Development Ltd v Zurich Insurance Co Ltd* [2012] 4 HKLRD 827

[23] Para. 48 of *Hua Tyan No. 2*

[24] Para. 41 of *Hua Tyan No. 2*

form of waiver or estoppel. However, in the absence of evidence to link up the use of the internet and the common practice for D to enquire into the specifications of vessels of P, the CFA held that there was no *prima facie* case for P to assert any presumption of knowledge on the part of D in the Vessel's DWT.

Waiver

In the present appeal, as the breach of a marine insurance warranty would result in the automatic discharge of an insurer's liability, reliance was placed by P on the doctrine of waiver by estoppel. A warranty will be ineffective if it is waived[25].

The relevant test is set out in *Copa Casino* and it requires three elements to be established by the party relying on it: (1) a clear and unequivocal representation by the person said to have waived rights (i.e. D in the present case), whether by words or conduct, that the representor's legal rights will not be insisted upon; (2) reliance by the representee (i.e. P in the present case) on the representation; and (3) that it would be inequitable for the representor to go back on the representation[26].

The CFA held that in the absence of clear and unequivocal representation by D that the Policy will cover the Vessel notwithstanding non-compliance of the DWT Warranty, the contention on waiver falls at the first hurdle of the above stated test[27].

The factual matrix is irrelevant when the Policy itself is clear

As for when the factual matrix is relevant to a case, CFA had this to say,

"The account that one takes of the factual matrix of a contract is to assist in arriving at the true construction of the contract and its terms. It does not have some separate life of its own to undermine or nullify the effect of a clear term of the contract. The meaning and effect of the Deadweight Warranty in the present case is clear and no assistance can be derived by reference to the factual matrix of the Contract"[28].

No rectification

P has claimed rectification by way of striking out the DWT Warranty which P contended was an error contrary to the common intention of the parties and that it is ineffective as a term of the Policy. The test for rectification of a contract as set out in *Agip SpA* was applied by CFA in considering P's claim, which provides that:

"First, there must be a common intention in regard to the particular provisions of the agreement in question, together with some outward expression of accord. Secondly, this common intention must continue up to the time of execution of the instrument. Thirdly, there must be clear evidence that the instrument as executed does not accurately represent the true agreement of the parties at the time of its execution. Fourthly, it must be shown that the instrument, if rectified as claimed, would accurately represent the true agreement of the parties at that time"[29].

Having found no basis for rectification in CFI's judgment, P's claim for rectification accordingly failed.

P's appeal was dismissed.

Vivian Cheung

Pathak Ravi Dutt v Sanjeev Maheshwari [2014] 3 HKLRD 597

This case highlights the inducement requirement for establishing misrepresentation - a false statement which does not affect the decision to make a contract is not actionable. It also shows the courts' reluctance to strike down a contract simply on the basis that the person signing it did not read or understand what he was signing.

---

25 S.34(3) of the MIO

26 Copa Casino at [39] referring to the analysis of waiver in the shipping context by Lord Goff of Chieveley in *Motor Oil Hellas (Corinth) Refineries SA v Shipping Corp of India* [1990] 1 Lloyd's Rep 391, 397(1)-399(2), see also *Kosmar Villa Holidays Plc c Trustees of Syndicate 1243* [2008] 1 CLC 307, [36]-[38] (Rix LJ)

27 Para. 54 of *Hua Tyan No. 2*

28 Para. 49 of *Hua Tyan No. 2*

29 *Agip SpA v. Navigazione Alta Italia SpA* [1984] 1 Lloyd's Rep 353, 359 (Slade LJ)

Facts

The plaintiff ("P"), an Indian national, originally worked in a diamond trading company in India. According to P, the defendant ("D") (the company owner's relative) offered to employ P as a diamond assorter cum salesman in Hong Kong, and promised to arrange for a proper employment visa for P to work for D in Hong Kong ("Offer"). P agreed to take up the Offer.

P claimed that he was asked by D to sign a Domestic Helper Contract ("DH Contract") in English, without being aware of the true nature and effect of its contents, which were not explained, read or interpreted to him. Further P claimed that D induced him to sign the DH Contract by orally representing to him that he was signing a document relating to immigration matters in relation to P entering Hong Kong and that P "would only work in relation to the diamond trade in Hong Kong" ("Representations"). According to P, after he arrived in Hong Kong, he discovered that D's Representations were untrue in that (i) the DH Contract was a contract to employ him as a domestic helper; and (ii) he was required to work as a domestic helper and also in the diamond trade.

P alleged that D failed to pay P his outstanding salary and refuse to let P return to India. P terminated his employment with D and lodged a complaint to the Hong Kong police. P signed a witness statement asserting that (i) D was his employer; (ii) he was a domestic helper but had to work in D's office; and (iii) D refused to return his passport to him. According to P, D then maliciously and without cause falsely accused P of stealing diamonds from his office. P was charged with theft but acquitted after trial. P then commenced Labour Tribunal proceedings against D for salaries owing under the DH Contract.

Subsequently, P brought an action against D for fraudulent misrepresentation, breach of contract and malicious prosecution.

Decision

The Court dismissed P's claims for the reasons set out below.

P's knowledge of the DH Contract

The Court held that a person could not disclaim a contract on the basis only that he did not know or read what he was signing; a lack of understanding of the contents, meaning, terms or effect of a document signed by a person of full age and understanding was not a ground to disown the document (the principles affirmed in *Bank of China (Hong Kong) Ltd v Fung Chin Kan*[30] and *Ming Shiu Chung v Ming Shiu Sum*[31] were applied).

Applying the above principles, the Court held that even if P did not understand the effect or meaning of the DH Contract, he could have sought explanations on it first; and by signing the contract immediately, P took his chance with the DH Contract and should be bound by what he chose, blindly or carelessly, to sign.

Whether there were any misrepresentations by D regarding the nature or effect of the DH Contract

The Court rejected P's claim that he had been induced to sign the DH Contract by D's misrepresentations. The Court considered that on the evidence, P's complaint to the police represented the truth and substance of his case: that he knew the nature of the DH Contract was for his employment as a domestic helper, and he had agreed to sign such a contract. This was consistent with P's institution of Labour Tribunal proceedings for recovery of salaries owing to him under the DH Contract.

Whether there was an oral agreement for D's employment of P as a diamond assorter or salesman in Hong Kong ("Oral Agreement")

The Court rejected P's claim that there was an Oral Agreement. The Court found that P had been informed, and had agreed, that he could only be employed by D as a domestic helper in Hong Kong, and he agreed to sign and did sign the DH Contract to obtain a visa to come to Hong Kong.

The Court went on to comment that even if the Oral Agreement was made, the Court would not have enforced it since it aimed to defeat the visa and work permit which only permitted P to work as a domestic helper in Hong Kong and the performance of it would have been illegal without a proper visa and work permit permitting P to work in relation to the diamond trade in Hong Kong.

The claim of malicious prosecution

The Judge referred to the principles pertaining to the tort of malicious prosecution, as summarized in *Jae*

[30] (2002) 5 HKCFAR 515 at 533.
[31] (2006) 9 HKCFAR 334 at 361.

Hoon Oh v Richdale[32]. The principles relevant to the present case were that (i) to establish malicious prosecution, it must be proved that the complainant had lied, or procured others to lie to the authorities in order to try to have another person prosecuted on a criminal charge; and the lie must also "at least" have influenced the authorities to prosecute; (ii) where the authorities exercised an independent discretion or judgment in investigating and deciding to prosecute, the nexus between the lie and the prosecution was broken, and the complainant would not be held to be the prosecutor; and (iii) the court would not necessarily infer from the fact that false information had been given to the police that the police investigation was tainted.

The Court was not satisfied that the prosecuting authorities did not and had not been able to exercise independent discretion or judgment in investigating the complaint of theft or in deciding to prosecute P for theft. On the facts, the police had considered various witness statements and CCTV footages of D's office at the time of the alleged theft. There was nothing to suggest that D's evidence had prejudiced either the police's investigation or the discretion to prosecute. The Court therefore held that P failed to prove malicious prosecution.

Ada Ng

Huen Wai Kei v Choy Kwong Wa Christopher (No. 2) [2014] 4 HKLRD 782

Facts

The plaintiff, Huen, ("P") and the defendant, Choy, ("D") jointly owned a company ("C"). D controlled a company ("D Company"), which owned certain properties in Residence Bel-Air (the "Properties"). In 2005, due to disagreement over the affairs of C, P and D signed an agreement whereby D would purchase all of P's shares in C for $40 million (the "Shares Agreement"). D made an initial payment of $10 million to P. A few days after execution of the Shares Agreement, P and D orally agreed that D would procure D Company to put up the Properties as security for D's liability to pay P the remaining $30 million under the Shares Agreement, and, in the event of D's default, D would procure D Company to assign the Properties to a company controlled by P ("P Company"), and the consideration for the purchase of the Properties shall be set-off against the defaulted amount (the "Security & Set-Off Agreement").

[32] [2005] 2 HKLRD 285

P and D (on behalf of P Company and D Company respectively) then signed a memorandum of agreement for sale and purchase (the "Memorandum"), which provided that D Company shall assign the Properties to P Company for a consideration of $38.4 million, and that vacant possession should be delivered to P Company free from all encumbrances upon completion of sale. P and D also signed a supplemental agreement to the Shares Agreement (the "Supplemental Agreement") stating that P and D signed the Memorandum as a guarantee of D's payment of $40 million to P under the Shares Agreement. Thereafter, P Company and D Company signed a sale and purchase agreement (the "S&P") under which D Company was to sell the Properties to P Company at $38.4 million. At that time, the Properties were mortgaged to a bank (the "Bank") for about $16 million. It was later found that P and D signed the S&P instead of a usual security to obviate the need to obtain the Bank's consent.

D defaulted in paying the $30 million balance under the Shares Agreement. Completion of sale and purchase of the Properties did not take place. P and P Company ("Ps") brought proceedings against D and D Company ("Ds") in 2006 and 2007.

At trial, the judge found D liable to P for the sum of $30 million under the Shares Agreement. The judge ruled in Ps' favour and adjudged that:

(1) D pays P $30 million (the "Judgment Sum") with interest thereon ("Order 1"); and

(2) **alternative** to Order 1, an order for specific performance of the S&P by D Company to assign the Properties to P Company and to set-off the consideration of $38.4 million against the Judgment Sum with interest thereon ("Order 2").

After the judgment was handed down in 2013, D did not pay the Judgment Sum. Meanwhile, the market value of the Properties in 2013 was double that in 2005. Having obtained a judgment with alternative remedies, Ps promptly elected to enforce Order 2 and requested D Company to assign the Properties to P Company. Ds argued that the S&P was only a security to ensure D's due payment pursuant to the Shares Agreement, and that if Ps had the right to call

on D Company to assign the Properties to P Company in lieu of asking for the Judgment Sum, Ps would get more than the amount awarded to them.

Ds appealed to the Court of Appeal ("CA") against the judgment.

Decision

The major contention of Ds' appeal was that the Security & Set-Off Agreement was unenforceable for **lack of consideration**. Order 2 was wrongly made and should not have been ordered in the alternative to the Judgment Sum in Order 1.

CA quoted Order 18, rule 7(1) of the Rules of the High Court (Cap. 4A), which stipulates that every pleading must contain a statement in a summary form of the material facts on which the party pleading relies for his claim or defence. Endorsing an old authority cited by Ds' counsel, *Clarke v Gray*[33], which held that "… in the case of an agreement, not under seal, the consideration must be stated, and no part of the entire consideration for any promise contained in the agreement can be omitted…", CA found that the Security & Set-Off Agreement was not an agreement under seal.

CA held that consideration for the Security & Set-Off Agreement was a material fact and should have been, but was not, pleaded in Ps' statement of claim, and that on the evidence there was no consideration for the Security & Set-Off Agreement. According to P, he did not offer D anything in return for the security under the Security & Set-Off Agreement, and D voluntarily offered the Properties as security. Apparently, the Security & Set-Off Agreement was only an "afterthought" to the Shares Agreement and not supported by consideration.

Applying *BCCI Finance International Ltd v Aftab Ahmed*[34], CA also held that the existence of D's debt to P was insufficient to support D's promise made on behalf of D Company to put up the Properties as security, nor was past consideration adequate to bind the parties to the Security & Set-Off Agreement.

CA agreed with the trial judge's findings that: (1) the Memorandum and the Supplemental Agreement were entered into as a result of the Security & Set-Off Agreement; and (2) the S&P did not stand alone and must be considered with the Memorandum and the Supplemental Agreement, which preceded it, and the clear intention of these documents was that the Properties (i.e. the subject matter of the S&P) were to be security for D's liability under the Shares Agreement, as agreed by P and D in the Security & Set-Off Agreement. However, since the Security & Set-Off Agreement was unenforceable for lack of consideration, the trial judge erred in granting an order for specific performance of the S&P. On this ground, CA allowed Ds' appeal and set aside Order 2.

There are additional reasons why Order 2 could not stand. CA went on to consider that, even if the Security & Set-Off Agreement were enforceable, the trial judge should not have ordered specific performance of the S&P because it was a "sham" in that the legal rights and obligations purported to have been created by it (i.e. a sale and purchase of the Properties) were different from the actual legal rights and obligations that the parties intended to create (i.e. a security by which the Properties were put up to secure the performance of D's liability under the Shares Agreement). Further, the S&P, if enforceable, would create an equitable charge or a mortgage. It is a settled rule of equity that any agreement which interferes with the mortgagor's equitable right to redeem is ineffectual. Insofar as the S&P purported to assign the Properties to P Company in the event of D's default, vesting the entire legal and beneficial ownership in P Company free from all encumbrances and thereby extinguishing D Company's right to redeem the Properties, it is invalid at law.

Christie Kwong

Editors : **Yung Lap Yan**
Beverly Yan
Ada Chen

Advice should be sought from CU before applying the information in the CU Review to particular circumstances.

33 (1805) 6 East 564 at 568.
34 [1991] 1 HKC 375.