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The Commercial Unit, Civil Division
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What's inside

Editorial

We feature three articles in this edition.

The first article talks about the concept of novation in the law of contract, and explains how it differs from assignment and variation.

The second article provides an overview of the new licensing regime for virtual asset service providers under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) and HKMA's consultation conclusion on the regulation of stablecoins published in January 2023.

The third article outlines the main features of the Inland Revenue (Amendment) (Taxation on Specified Foreign-Sourced Income) Ordinance which introduces a new foreign-sourced income exemption regime for passive income and requires adequate economic substance for preferential tax treatment.

We also feature three case reports in this edition.

In the first case, the CFI had to consider whether cryptocurrency is "property" which can form the subject matter of a trust.

In the second case, the CFA held that the unauthorised closure of a bank account by a bank and the payment of money out of the bank account to an unauthorised person would not discharge the debt owed by the bank to the account-holder and that time would not begin to run for limitation purposes until demand for payment is made by the account-holder.

The third case is about the application of s.42 of the Companies Ordinance (Cap. 622) in which the CFI ordered the removal of certain documents registered at the Companies Registry which contained wrong information as to the true identity of the relevant companies' officers, directors, shareholders and address of registered office.

YUNG Lap-yan

Novation of Contract

Introduction

Novation is an act whereby, with the consent of all parties, a new contract is substituted for an existing contract and the latter is discharged.[1] Usually, but not necessarily, a novation takes the form of the introduction of a new party to the new contract and the discharge of a person who was a party to the old contract.[2]

This article gives an overview of the concept of novation in contract law and explains how novation differs from assignment and variation.

Effect of novation

By novation, an original contract is extinguished and replaced by a new contract so that the rights and obligations under the original contract are assumed by a new party under the new contract. A novation does not merely assign or transfer a right or liability to another party, it extinguishes the original contract and replaces it with a new one.[3]

Requirements for novation

(a) Consent of all parties

Novation takes place where two contracting parties agree that a third, who also agrees, shall stand in the relation of either of them to the other.[4] Since novation involves the creation of a new contract, the consent of all parties involved is necessary.[5] In the absence of express consent to novation, consent may be inferred from conduct. For instance, acceptance of novation may be inferred from acts and conducts that amount to the performance of obligations of the agreement novated.[6] A party asserting novation must "clearly establish" it by evidence.[7]

(b) Intention to novate

Apart from obtaining all parties' consent, it is crucial to establish an intention to effect a novation. As said by Viscount Haldane in *Morris v Baron & Co*[8], "*[w]hat is, of course, essential is that there should have been made manifest the intention in any event of a complete extinction of the first and formal contract, and not merely the desire of an alteration, however sweeping, in terms which still leave it subsisting.*"

(c) Consideration

Since a new contract is formed under novation, the new contract should be supported by valuable consideration unless it is made by way of deed. Where the contract between the two original parties is executory on both sides, the consideration for the discharge of the obligation as between them lies in the mutual surrender of rights to performance. The consideration for the contract between the remaining original party and the new party lies in the mutual exchange of promises.[9]

Novation by implication

A contract can be novated by express agreement (whether oral or written) or by implication. The test to determine whether a novation can be implied is set out in the judgment of *Evans and SMG Television Limited*[10], where Lightman J said "*...whether that inference is necessary to give business efficacy to what actually happened. The inference is necessary for this purpose if the implication is required to provide a lawful explanation or basis for the parties' conduct.*" Evidence of subsequent conduct is also relevant to establish whether there has been a novation by conduct.[11]

The test was illustrated by a recent English case of *Gama Aviation (UK) Limited & International Jet Club Limited v MWWMMWM Limited*[12], where a novation was found to be implied by conduct.

In *Gama,* a contract ("Original Contract") was entered into by an aircraft service provider and the defendant to provide services for the defendant's aircraft. As a result of a merger, the plaintiff took over the aircraft service provider's role to provide services to the defendant. When the defendant stopped paying for the services, the plaintiff sought to recover the unpaid sums from the defendant on the basis that the Original

1 Para. 115.390, Halsbury's Laws of Hong Kong, Vol. 7, Contract.
2 Hong Kong Bilingual Legal Dictionary, Novation.
3 22-092, Chitty on Contract, 34th Ed., Vol. 1.
4 Ibid.
5 *Far East Consortium Ltd v Airedale Ltd* (Kaplan J), [1991] 1 HKC 325.
6 *Enterprise Managed Services Ltd v Tony McFadden Utilities Ltd* [2011] 1 BCLC 414 at [24].
7 Per David Steel J, in *The Tychy (No. 2)* [2001] 1 Lloyd's Rep 10, at [24].
8 [1918] AC 1.
9 Para. 115.426, Halsbury's Laws of Hong Kong.
10 [2003] EWHC 1423 (Ch), para. 181.
11 *Capita ATL Pension Trustees Limited v Sedgewick Financial Services Limited* [2016] EWHC 214 (Ch), para. 21.
12 [2022] EWHC 1191 (Comm).

Contract was impliedly novated to the plaintiff and hence the plaintiff was entitled to payment for the services. The Court considered that the facts that the defendant had asked the plaintiff for assistance, received invoices in the name of the plaintiff and paid the plaintiff for two years lent support to the plaintiff's claim that there was a novation by implication.

Differences between novation and assignment

Under contract law, assignment (of rights) refers to a process where a party transfers his rights and benefits under a contract to another party. Despite some similarities, novation and assignment are two distinct legal concepts.

An assignor can assign its rights in a contract to a third party without the consent of the other party, unless such consent is required in the contract. A novation, however, essentially requires the consent of all parties.[13]

Assignment involves the transfer of the assignor's rights under the contract to the assignee without extinguishing the original contract. The assignor still owes obligations to the original party under the contract. The assignor can still be held responsible for failure to perform the contract. As for novation, a novation typically extinguishes the original contract and replaces it by another.[14] The original parties will no longer be required to perform the original contract.

A novation transfers both rights and liabilities to the new party, in an assignment only the benefit of the contract can be transferred.[15]

Assignment does not require consideration, while novation, which involves the creation of a new contract, requires consideration, unless it is made under deed.[16]

Differences between novation and variation

The parties to a contract may vary the terms of that contract. Similar to a novation, a contract variation requires the consent of all parties.[17] A variation may be made by express agreement or may be implied by conduct.[18]

However, unlike a novation which creates a new contract, a variation only involves effecting changes to an existing contract without replacing that contract with a new one.

Where parties agree to alter an existing contract by bringing in a third party, it may not necessarily be a novation.[19] For example, in *Trustees of Saunders v Ralph*,[20] the Court held that having regard to the parties' intention, the original tenancy agreement had merely been varied by adding an additional tenant and there was no novation.

Conclusion

Novation enables the incoming party to assume the rights and obligations under the original contract by extinguishing the original contract and replacing it with a contract upon obtaining consent from all parties. Novation, assignment and variation are different contract law concepts. While novation involves the creation of a new contract, assignment and variation do not.

Tommy Lau

13 *Budana v Leeds Teaching Hospitals NHS Trust* [2017] EWCA Civ 1980, [2018] 1 W.L.R. 1965 at [48], [115].
14 22-092, Chitty on Contract, 34 Ed., Vol. 1.
15 22-093, Chitty on Contract, 34 Ed., Vol. 1.
16 22-094, Chitty on Contract, 34 Ed., Vol. 1.
17 Para. 115.407, Halsbury's Law of Hong Kong.
18 Ibid. And see *Wong Bei-nei v A-G* [1973] HKLR 582, [1973] HKCU 50.
19 22-095, Chitty on Contracts 34th Ed., Vol. 1.
20 (1993) 66 P. & C.R. 335.

New Regulatory Regime on Virtual Assets

The virtual asset ("VA") industry and stablecoin trading have flourished across the globe in recent years, with a substantial increase in participating institutions and investors.

VA (e.g. Bitcoin, Ethereum) is a cryptographically secured digital representation of value expressed as a unit of account or a store of economic value; that can be transferred, stored or traded electronically; and either:

(a) is used for the payment for goods or services, discharge of a debt and/or investment; or
(b) provides rights to vote on the affairs in connection with such digital representation of value.

Stablecoin is "a crypto-asset that aims to maintain a stable value relative to a specified asset, or a pool or

basket of assets". It may be used for investment or payment purposes. As a result of stablecoin's growing potential as a means of exchange between cryptocurrencies and currencies (e.g. USD, RMB, EURO), stablecoins have a growing interconnectedness with the traditional financial markets.

As an international financial centre, Hong Kong has attracted a wealth of talent and start-ups in the VA sector as well as crypto retail operators offering the trading of stablecoins. To ensure orderly development and operation of this front, the Government recently introduced a licensing regime for the VA service providers ("VASPs") under the Anti-Money Laundering and Counter-Terrorist Financing Ordinance (Cap. 615) ("AMLO"). Consultation on the regulation of stablecoin is underway for potential implementation of a stablecoin regulatory regime in the near future.

Licensing regime for VASPs under AMLO

In response to the latest Financial Action Task Force standards on anti-money laundering and counter-terrorist financing, a new licensing regime for VASPs was introduced on 1 June 2023 to regulate persons engaging in VA service.

Any person who engages in VA service shall apply for licence from SFC. VA service means operating a VA exchange to provide services through electronic facilities, whereby binding transactions of selling or buying VA will form, or people are introduced or identified so that they may negotiate or conclude such binding transactions; and in providing such services, the service provider will directly or indirectly possess client money or VA.

To catch up with the rapid development in the VA sector, the scope of VA and VA service may be varied by the Secretary for Financial Services and the Treasury by notice published in the Gazette.

Nature and management of licensed VASPs

Both locally incorporated companies and non-Hong Kong companies registered under the Companies Ordinance (Cap. 622) with a place of business in Hong Kong are eligible as applicant for VASP licence with SFC.

VASP licence applicant shall have at least two responsible officers to oversee the operation of the business of VA service and to ensure compliance with anti-money laundering/counter-terrorist financing requirements. To be approved by SFC as a responsible officer of a VASP, it is a pre-requisite that the person is a representative licensed by SFC. Only representatives licensed by SFC may carry out regulated functions on behalf of VASPs.

SFC may grant licence if it is satisfied that the VASP licence applicant, its responsible officers and representatives are fit and proper persons.

Retail access to licensed VA trading platforms

Given the strong public support for allowing VASPs to provide VA services to retail investors, SFC has allowed retail access to licensed VA trading platforms, subject to compliance with a range of robust investor protection measures covering onboarding, governance, disclosure and token due diligence and admission.

SFC's role and powers

Licensed VASPs are subject to SFC's supervision and are required to submit audited accounts and financial information to SFC regularly. Where a VASP is found guilty of misconduct or not fit and proper, SFC is empowered to take disciplinary actions, including suspension or revocation of licence.

SFC is also empowered to enter business premises of licensed VASPs for conducting inspections and investigations; and to appoint auditors to look into the affairs of licensed VASPs.

To protect client assets of licensed VASPs in case of emergency, SFC has intervention powers in relation to the operation of licensed VASPs where circumstances require, e.g. SFC may require licensed VASPs to conduct business only in a specified manner; and may restrict licensed VASPs from disposing of client assets.

Offences

A person who is not a licensed representative but performs any regulated function of providing VA service; or holds himself out as such commits an offence. Carrying on a business of providing VA service without licence; or non-compliance with anti-money laundering/counter-terrorist financing requirements, also constitute an offence.

Regulation of stablecoins

Regulatory ambit

To ensure financial stability and consumer protection, HKMA published a consultation conclusion on regulation of stablecoins in January 2023. In the consultation conclusion, HKMA indicated that it would focus on regulating the following aspects of

stablecoins:

(a) establishment and maintenance of rules governing stablecoins;
(b) creation[21], issuing[22] and destroying[23] of stablecoins;
(c) stabilisation of stablecoins; and
(d) secured storage of stablecoins.

HKMA will adopt a "same risk, same regulation" approach to regulate relevant entities and activities. Whether the entities are authorized institutions under the Banking Ordinance (Cap. 155) or not, they should be allowed to issue stablecoins as long as they could satisfy relevant licensing and regulatory requirements.

Licensing requirements

The following activities are proposed to be subject to licensing requirements:

(a) conducting a stablecoin activity in Hong Kong;
(b) actively marketing a stablecoin activity to the public of Hong Kong;
(c) conducting an activity which concerns a stablecoin that purports to reference to the value of the Hong Kong dollar, even if the activity is not caught by (a) or (b); or
(d) conducting an activity which HKMA is of the opinion that should be so regulated, having regard to matters of significant public interest.

Conclusion

With a solid legislative framework for regulation of the VA sector underpinned in the AMLO and forthcoming regulation of stablecoins, it is hoped that a comprehensive regulatory system would be put in place to allow VA businesses to thrive in Hong Kong progressively and sustainably.

Angel Li

[21] E.g. by mining (using high-end computers to solve cryptographic equations through which miners earn reward in the form of new stablecoins) or minting (providing validation services such as adding new transaction blocks to a blockchain through which validators earn reward in the form of new stablecoins).

[22] I.e. distributing stablecoins to investors and/or initial coin offering to list stablecoins on a crypto exchange.

[23] I.e. permanently removing stablecoins from circulation.

Inland Revenue (Amendment) (Taxation on Specified Foreign-Sourced Income) Ordinance 2022

Introduction

The Inland Revenue (Amendment)(Taxation on Specified Foreign-Sourced Income) Ordinance 2022 ("the Ordinance"), enacted in December 2022, introduces a new foreign-sourced income exemption ("FSIE") regime for passive income.

The Ordinance brings Hong Kong in line with the prevailing international tax standard of requesting adequate economic substance for preferential tax treatment and also addresses the concerns of the European Union on the risks of double non-taxation arising from the general non-taxation of foreign-sourced passive income within Hong Kong's territorial source principle of taxation.

This article outlines the major features of the Ordinance.

Covered income and covered taxpayers

Under the new FSIE regime, foreign-sourced income that is interest, intellectual property ("IP"), dividend or disposal gains from the sale of certain equity interests (hereinafter collectively referred to as "specified foreign-sourced income") will be deemed to be sourced from Hong Kong and chargeable to profits tax if –

(a) the income is received in Hong Kong[24] by a person that is, or acts for an multinational enterprise group[25] or an entity included therein ("MNE entity") carrying on a trade, profession or business in Hong Kong ("covered taxpayer") irrespective of its revenue or business or asset size; and

(b) the recipient entity fails to meet the economic substance requirement (see below) if the income is non-IP income, or fails to comply with the nexus approach (see below) if the income is IP income.

[24] Income is regarded as "received in Hong Kong" if (i) it is remitted to, or is transferred or brought into Hong Kong; (ii) it is used to satisfy any debt incurred in respect of a business carried on in Hong Kong; or (iii) is used to buy moveable property, and the property is brought into Hong Kong.

[25] An multinational enterprise group means a group that includes at least one entity or permanent establishment that is not in the jurisdiction of the ultimate parent entity of the group. "Permanent establishment" under the Inland Revenue Ordinance, Cap. 112 ("IRO") includes 'a branch, management or other place of business'.

Save for the above and unless otherwise provided under the IRO, other foreign-source income will continue to be exempt from tax in Hong Kong under the existing territorial source principle of taxation.

Interest, dividend and disposal gain generated by regulated financial entities, such as authorized banks or insurer, from the carrying on of their regulated businesses will not fall within the scope of the FSIE regime.

Economic substance requirement

Specified foreign-sourced income that is not IP income and is received in Hong Kong by a covered taxpayer will be exempt from profits tax if the covered taxpayer conducts substantial economic activities with regard to the relevant income ("relevant activities") in Hong Kong, such that:

(a) for a taxpayer that is not a pure equity-holding company, the relevant activities will include making necessary strategic decision, and managing and bearing principal risk, in Hong Kong in respect of any assets it acquires, holds or disposes of;

(b) for a taxpayer that is a pure equity-holding company, a reduced substantial activities test can be applied such that the relevant activities will only include holding and managing its equity participations, and complying with the corporate law filing requirements in Hong Kong;

(c) with regard to (a) and (b) above, outsourcing of the relevant activities will be permitted provided that the taxpayer is able to demonstrate adequate monitoring of the outsourced activities and that the outsourced activities are conducted in Hong Kong; and

(d) to meet the economic substance requirement, the taxpayer will need to meet an adequacy test in terms of employing an adequate number of qualified employees and incurring an adequate amount of operating expenditures in Hong Kong in relation to the relevant activities.[26]

Nexus approach for IP income

As far as foreign-sourced IP income is concerned, the nexus approach will apply in determining the extent of such income to be exempted.

Under the nexus approach, only income from a qualifying IP asset can qualify for preferential tax treatment based on a nexus ratio which is defined as the qualifying expenditures as a proportion of the overall expenditures that have been incurred by the taxpayer to develop an IP asset. The proportion of research and development ("R&D") expenditures is a proxy for substantial economic activities. This ensures that there is a direct nexus between the income receiving benefits and the expenditures contributing to that income.

Participation exemption for dividends and disposal gains

Foreign-sourced dividends and disposal gains of an MNE entity, can be exempted from tax even if it is unable to comply with the economic substance requirement provided that –

(a) the MNE entity is a Hong Kong resident person or a non-Hong Kong resident person that has a permanent establishment in Hong Kong;

(b) the MNE entity holds at least 5% of the shares or equity interest in the investee company during the year of accrual of the relevant income; and

(c) the MNE entity holds the shares or equity interest in the investee company for at least 12 months immediately prior to the accrual of the relevant income.

Anti-abuse rules

If a covered taxpayer enters into an artificial arrangement with an intent to avoid the deeming provisions and in turn the profits tax charge on any relevant foreign-sourced income, the general anti-avoidance rules as set out in sections 61 and/or 61A[27] of the IRO will be applicable. Under these provisions, the assessor or the assistant commissioner is able to disregard the artificial arrangement and assess the relevant income accordingly.

Double taxation relief

It is possible that a covered taxpayer fails to meet the exemption conditions of the new FSIE regime but has nonetheless already paid tax (e.g. withholding tax) in respect of the specified foreign-sourced income. In this circumstance, a tax credit will be provided to Hong Kong resident persons in respect of the income concerned to avoid double taxation. Foreign tax paid by non-Hong Kong resident persons on the specified foreign-sourced income may be deductible under

[26] The Inland Revenue Department ("IRD") will also consider other relevant factors, such as the nature of business and scale of operation.

[27] These sections empower IRD to disregard the use of fictitious, artificial or contrived arrangements to avoid or reduce tax liability.

s.16(1)(ca)[28] of the IRO.

Facilitation measures for ease of compliance

Taxpayers are permitted to apply for an advance ruling on whether the adequacy test is satisfied. IRD has published administrative guidance to help taxpayers ascertain their tax liabilities.

David Wan

Re Gatecoin Ltd (in liquidation) [2023] HKCFI 914

Facts

Gatecoin Limited ("Gatecoin"), a Hong Kong-incorporated company operating a cryptocurrency exchange platform, was wound up by the court in March 2019. Joint and several liquidators ("Liquidators") were appointed.

The Liquidators applied under s.200(3) of the Companies (Winding up and Miscellaneous Provisions Ordinance (Cap.32) (the "CWUMPO") for directions concerning, inter alia, the characterisation of cryptocurrencies held by Gatecoin.

Issues

In order to ascertain whether Gatecoin held the currencies, including cryptocurrencies, deposited by its customers on trust, the Court had to consider whether cryptocurrency is "property" which can form the subject matter of a trust. This Commentary will focus on the Court's discussion and decision on whether cryptocurrency is property.

Decision

The definition of property

S.197 of the CWUMPO imposes an obligation on a liquidator to take into custody all "property" upon a winding-up order. The meaning of "property" is defined under s.3 of the Interpretation and General Clause Ordinance (Cap.1) to "*[include] (a) money, goods, choses in action and land; and (b) obligations, easements and every description of estate, interest and profit, present or future, vested or contingent, arising out of or incident to property as defined in paragraph (a) of this definition*". The question is whether cryptocurrency falls within the said meaning of "property".

The requirements for "property" were stated in *National Provincial Bank v Ainsworth*[29] as "*…it must be definable, identifiable by third parties, capable in its nature of assumption by third parties, and have some degree of permanence or stability.*"

It was noted by the Court that an academic debate on whether cryptocurrencies constitute property took place in *Legal Statement on Cryptoassets and Smart Contracts*[30]. The debate stems from the traditional view that "property" can only be choses in possession and choses in action (see *Colonial Bank v Whinney*[31]). In *Legal Statement*, it was stated that the courts have found no difficulty in treating novel kinds of intangible assets as property, on that basis, while a crypto asset might not be a thing in action, that does not mean that it cannot be treated as property.

The Court also observed that Hong Kong courts have previously granted interlocutory proprietary injunctions over cryptocurrencies without any party suggesting that cryptocurrencies were not "property".

How cryptocurrencies are categorised in other jurisdictions

The Court then considered relevant case law in other jurisdictions and observed that they all recognise the proprietary nature of cryptocurrencies:-

(1) England and Wales
In *AA v Persons Unknown*[32], the learned Judge adopted the reasons identified in *Legal Statement* and held that Bitcoin meets the criteria set out in *Ainsworth*.

(2) The BVI
In *Joint Liquidators of Torque Group Holdings Ltd (In liq) v Torque Group Holdings Ltd (In liq)*[33], the learned Judge followed the conclusions in *Legal Statement* and *AA*, and held that crypto assets are assets for the purposes of liquidation.

(3) Singapore
In *CLM v CLN & Ors*[34], the court concluded that cryptocurrencies satisfy the definition of a

[28] This section permits a deduction for tax paid in a territory outside Hong Kong by any person who carries on a trade, profession or business in Hong Kong during the basis period for the year of assessment in respect of profits chargeable to tax under Part 4 of the IRO.

[29] [1965] AC 1175, 1247-1248
[30] November 2019
[31] (1885) 30 Ch D 261
[32] [2019] EWHC 3556 (Comm)
[33] BVIHC (Com) 0031 of 2021, 2 July 2021
[34] [2022] SGHC 46

property right in *Ainsworth* and could be protected by a proprietary injunction.

(4) Canada
In *Shair.Com Global Digital Services Ltd v Arnold*[35], the court was satisfied that the plaintiff had a claim to a proprietary interest in the digital currencies purchased by defendant.

(5) United States
The US courts held that cryptocurrencies are properties in various decision. For instance, in *BDI Capital v Bulbul Investments LLC*[36], the court held that Bitcoins are sufficiently identifiable to be considered "specific intangible property" and hence are capable of being the subject of a conversion action under Florida law.

(6) Australia
In *Australian Federal Police v Bigatton*[37], the court granted a freezing order over the defendant's property including cryptocurrencies.

(7) New Zealand
In *Ruscoe v Cryptopia*[38], the learned Judge concluded that cryptocurrency satisfies the four criteria for "property" as explained in *Ainsworth* and is a type of intangible property in that: -

(1) It is definable as the public key allocated to a cryptocurrency wallet[39] is readily identifiable and sufficiently distinct;
(2) It is identifiable by third parties in that only the holder of a private key[40] can access and transfer the cryptocurrency from one wallet to another;
(3) It is capable of assumption by third parties in that it can be and is the subject of active trading markets; and
(4) It has some degree of permanence or stability, as the entire life history of a cryptocurrency is available in the blockchain[41].

Conclusion: Cryptocurrency is "property" and capable of forming the subject matter of a trust

The Court noted that like other common law jurisdictions, our definition of "property" is an inclusive one and intended to have a wide meaning. Hence, the Court held that it is appropriate to apply and follow the reasonings in the *Legal Statement* and *Ruscoe v Cryptopia*, and their conclusion that cryptocurrency is "property", which is capable of forming the subject matter of a trust.

Molly Wong

PT Asuransi Tugu Pratama Indonesia Tbk (formerly known as PT Tugu Pratama Indonesia) v Citibank N.A. [2023] HKCFA 3

Facts

The Appellant opened an account (the "Account") with the Respondent bank (the "Bank") in 1990. The mandate of the Account provided that any two officers who opened the Account could give instructions regarding the Account. From 1994 to 1998, two such officers instructed the Bank to pay out an aggregate of US$51.64 million from the Account to themselves and to two others through 26 transfers, all of which were purportedly authorized by instructions. The Court of First Instance ("CFI") found that the sole purpose of the Account was to serve as a temporary repository of funds en route from the subsidiaries of the Appellant to the four individuals' own pocket. In 1998, the two officers gave the Bank the final instruction to transfer the balance to them and close the Account afterwards. The Bank executed such instruction.

In 2006, the Appellant informed the Bank that the final instruction and all 26 transfers were dishonestly authorised and demanded payment. In 2007, the Appellant commenced proceedings further to that demand on the basis that the Bank ought to have known that the transfers were not in the ordinary course of business of the Appellant and were only for the personal benefit of the transferees. The Appellant pleaded that the debit entries from the 26 transfers and the Account's closure instruction shall be of no effect, and that the Account shall remain in existence by 'reversing' those entries, which amounted to a claim in debt. It was the Appellant's further or alternative claim that the Bank shall compensate the Appellant the same amount as the claim in debt as damages for breach of duty of care owed in contract and/or tort by recklessly giving effect to the transfer instructions, which a reasonable and prudent banker would consider there being a real possibility that the Appellant might be defrauded, and would not act on without making inquiries or informing the Appellant's

[35] [2018] BCJ 3114
[36] 446 F.Supp.3d 1127 (2020)
[37] [2020] NSWSC 245
[38] [2020] NZHC 728
[39] Each user of a cryptocurrency network owns a "wallet". Each wallet has a unique address and is associated with 2 distinct keys: a "public key" (akin to a bank account) and a "private key" (akin to a PIN).
[40] The private key is used to transfer cryptocurrency from a user's wallet to the wallet of another user.
[41] Cryptocurrency is a digital asset based on blockchain technology, which records transaction data in a list of records (a block) with a time stamp, and one block is linked to the next by cryptography.

independent directors.

CFI's decision

CFI held that the Bank breached its duty since it did not inquire about the transfers when a pattern had emerged at the third out of the 26 transfers, indicating improper operation of the Account, which a reasonable and prudent banker would have been put on inquiry. However, CFI found that the Account closure instruction given in 1998 was duly authorised and the six-year limitation period for the Appellant's cause of action under the Limitation Ordinance (Cap. 347) started to run at that time. Hence, the Appellant's claim was statute-barred when the proceedings commenced in 2007.

The Court of Appeal ("CA")'s decision

CA dismissed the appeal on slightly different grounds. It held that the closure of the Account in 1998 was unauthorized and repudiatory. That said, such closure was effective to bring the banker-customer relationship to an end; and it was irrelevant that the Bank's repudiation was not accepted by the Appellant. It followed that the cause of action for the Bank's wrongful transfers arose at that time. Accordingly, the Appellant's claim had been statute-barred when the action commenced.

At both CFI and CA, the Bank further advanced a case of contributory negligence. Both courts held that contributory negligence would have lain if not for the fact that the claim had failed for being statute-barred.

The Court of Final Appeal ("CFA")'s decision

CA granted leave to the Appellant to appeal to CFA on two issues, (i) whether a cause of action for deposits debited to the Account without authority arose upon its closure in 1998 without the need for a demand; and (ii) on the footing that the Appellant's claim was not statute-barred, whether such claim to recover the balance of the Account ought to sound in debt, to which contributory negligence could not be a defence.

Issue (i)

CFA considered that the closure of the Account was unauthorized and was a repudiation of the relationship. In the absence of the Appellant's acceptance of repudiation and any exceptional reasons which entitle the Bank to unilaterally end the contract between the Appellant and the Bank, the contract had continued, which entitled the Appellant to claim the balance undiminished by the 26 unauthorized transfers as debt, without limit of time. There was no reason why the Appellant should be deprived of such right given the Bank's wrongful conduct in its failure to inquire when pattern of improper operation of the Account emerged at the third transfer, which fell short of the standard as a reasonable and prudent banker.

Furthermore, whether the closure of the Account was authorised or not, no principle of law would entitle the Bank to unilaterally discharge a debt without paying it. On the footing that the debt had not been discharged, it still subsisted in 2006 when it was demanded, and time did not begin to run for limitation purposes until then. Accordingly, these proceedings which began in 2007 were not statute-barred.

Issue (ii)

On the footing that the Appellant's claim was not statute-barred, CFA proceeded to consider whether the claim could be abated by the Appellant's contributory negligence. CFA considered the Appellant's claim a claim in debt, rather than a claim for damages for the Bank's breach of duty of care owed in contract and/or tort. Accordingly, it did not fall within the scope of s.21 of the Law Amendment and Reform (Consolidation) Ordinance (Cap. 23), which provides that for a claim in respect of damage arising from the fault of both the claimant and other person(s), such contributory negligence shall reduce the damages recoverable to such extent as the court thinks just and equitable.

CFA held that the defence of contributory negligence was not available to the Bank and unanimously allowed the appeal in favour of the Appellant. Judgment was entered for the Appellant for the aggregate amount from the third unauthorised transfer onwards, the point in time when the Bank should have been put on inquiry.

Lawrence Li

Noble Crest Limited v Chau Yuet Ching Brenda and Others [2023] HKCFI 115

Facts

Noble Crest, Full Honest, East Victory and Million Globe (collectively the "Plaintiff Companies"), sought orders pursuant to s.42 of the Companies Ordinance (Cap. 622) ("CO") that certain documents filed in the Companies Registry be expunged ("Impugned Documents"), and that the information in the documents be rectified and removed.

Up until 12 January 2016, the 1st Defendant ("Madam Chau"), together with her son ("Chau Junior"), were directors of Noble Crest, East Victory and Million Globe when on that date she resigned as director of these companies. Furthermore, up until 14 September 2016, Madam Chau was the sole shareholder of the Plaintiff Companies when on that date she transferred her share in each of the Plaintiff Companies to a company called Pink Diamond. As a result, Chau Junior became the sole director and Pink Diamond became the sole shareholder of the Plaintiff Companies.

The Impugned Documents later came to be signed by Madam Chau (when she was no longer a shareholder or director of the Plaintiff Companies), the 2nd Defendant (purportedly as company secretary) and the 4th Defendant ("William") and filed with the Companies Registry in November and December 2016 and February and March 2017 respectively, without the knowledge or approval of Chau Junior or Pink Diamond. The Impugned Documents included: (1) certain forms in respect of each of the Plaintiff Companies indicating that at the material times (a) Chau Junior ceased to act as director; (b) Madam Chau was appointed as director and then ceased to act as director; (c) William was appointed as director; and (d) changes of company secretary and registered office; and (2) annual returns of Noble Crest, East Victory and Million Globe indicating that Madam Chau was the sole director and shareholder. It was alleged that the Impugned Documents were based on certain resolutions of the Plaintiff Companies ("Underlying Resolutions"), which were passed by Madam Chau purportedly as the sole shareholder and director of each of the Plaintiff Companies when in fact she was neither.

The Law

S.42 of CO provides as follows:

(1) The Court of First Instance ("Court") may, on application by any person, by order direct the Registrar of Companies ("Registrar") to rectify any information on the Companies Register (as defined in s.2 of CO) or to remove any information from it if the Court is satisfied that—

  (a) the information derives from anything that—
    (i) is invalid or ineffective; or
    (ii) has been done without the company's authority; or
  (b) the information—
    (i) is factually inaccurate; or
    (ii) derives from anything that is factually inaccurate or forged.

…

(4) The Court must not order the removal of any information from the Companies Register under subsection (1) unless it is satisfied that—

  (a) even if a document showing the rectification in question is registered, the continuing presence of the information on the Companies Register will cause material damage to the company; and
  (b) the company's interest in removing the information outweighs the interest of other persons in the information continuing to appear on the Companies Register.

The threshold for removal rather than rectification is not high. If there is a prospect of damage being caused to the company by the information on the Companies Register, that would justify removal. The continued presence of incorrect information may give rise to a real risk that the persons dealing with the company would question the identity of the shareholders and directors, creating confusion, uncertainty, and time and cost on the part of the companies in dealing their affairs. (See *Sterling Payment Services Ltd v Registrar of Companies & Another*[42] applied).

Decision

The Court decided that there was no arguable defence to the Plaintiff Companies' claim under s.42(1) of CO for the reasons below:

(a) The Underlying Resolutions which were the basis for the Impugned Documents were signed by Madam Chau, purportedly as shareholder and director of the Plaintiff Companies, when in fact she was neither. The information in the Impugned Documents regarding the appointment of directors and changes of company secretary and address of registered office derived from something that was invalid and effective (*cf.* s.42(1)(a)(i)).

(b) The Impugned Documents were signed or presented by one or more of Madam Chau, the 2nd Defendant and William, without the knowledge or approval of the Plaintiff Companies' sole director (i.e. Chau Junior) or shareholder (i.e. Pink Diamond) at the material times. The information in the Impugned Documents derived from something done without the Plaintiff Companies' authority (*cf.* s.42(1)(a)(ii)).

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(c) The information in the Impugned Documents regarding the appointment of directors, changes of company secretary and address of registered office, and identity of shareholder was factually incorrect (*cf*. s.42(1)(b)(i)).

The Court held that the removal of the information in the Impugned Documents was justified under s.42(4) of CO:

(a) Even if a document showing rectification was registered in the Companies Registry, the continuing presence of the wrong information as to the identity of the Plaintiff Companies' officers, shareholder and address of registered office would cause material damage to the Plaintiff Companies because they could cause confusion to third parties dealing with the Plaintiff Companies as to the true identity of the shareholder and officers of the Plaintiff Companies. There was a real risk that this could happen in the present case.

(b) The Plaintiff Companies' interest in removing the information in the Impugned Documents outweighed the interest of the Defendants in the information continuing to appear on the Companies Register.

The Court ordered that the Registrar should remove the Impugned Documents from the Companies Registry. In view of the removal order, there was no need to make any rectification order.

Ida Chan

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