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The Commercial Unit, Civil Division
The Department of Justice

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Editorial

Welcome to the Winter edition of the CU Review. On behalf of the Commercial Unit of the Department of Justice, I wish you all a Merry Christmas and a Happy New Year.

In this edition we feature three articles. The first article is about the Competition Bill which has recently been introduced into the Legislative Council for its scrutiny. The article summarizes some of the major provisions of the Bill. The second article is about the Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill which also has recently been introduced into the Legislative Council. This Bill reflects the requirements of anti-money laundering and counter-terrorist financing ("AML") recommended by the international AML standard setter – the Financial Action Task Force. The third article is about proposals to enhance consumer protection against unfair trade practices.

Three case reports are also included. The first case involves the Hong Kong pop group "Soler" who alleged that their agreements with their worldwide exclusive agent and manager were in restraint of trade. The second case relates to the question of whether a pay TV service contract between a pay TV licensee and its customer which provides that, in the event that the customer terminates the use of the basic services of the pay TV prior to the expiry of the term of the contract, the customer will have to pay all the monthly fees for the remaining term of the contract is valid and enforceable. The third case is about whether time is of the essence of a provisional agreement for the sale and purchase of a property.

Yung Lap-yan

Notes :

Major Provisions of the Competition Bill

In 2006, the Competition Policy Review Committee recommended that in order to ensure effective implementation of the Government's policy objective to promote competition, the Government should prepare a cross-sector competition law.

Following that recommendation, the Government has prepared a cross-sector competition law – the Competition Bill (the "Bill") which was introduced into the Legislative Council in July this year.

We summarize below some of the major provisions of the Bill.

Competition Rules

The Bill contains the following three competition rules which prohibit undertakings from adopting anti-competitive conducts:

(i) an undertaking must not make or give effect to an agreement, engage in a concerted practice, or as a member of an association of undertakings, make or give effect to a decision of the association, if the object or effect of the agreement, concerted practice or decision is to prevent, restrict or distort competition in Hong Kong (the "First Conduct Rule");

(ii) an undertaking that has a substantial degree of market power in a market must not abuse that power by engaging in conduct that has as its object or effect the prevention, restriction or distortion of competition in Hong Kong (the "Second Conduct Rule"); and

(iii) an undertaking must not, directly or indirectly, carry out a merger that has, or is likely to have, the effect of substantially lessening competition in Hong Kong (the "Merger Rule").

At present, the Bill provides that the Merger Rule will only apply to carrier licensees under the Telecommunications Ordinance (Cap. 106).

Establishment of Competition Commission (the "Commission")

The Bill provides for the establishment of the Commission which will consist of not less than five members appointed by the Chief Executive (the "CE"). In considering the appointment of a person as a member of the Commission, the CE may have regard to that person's expertise or experience in industry, commerce, economics, law, small and medium enterprises or public policy.

One of the most important functions of the Commission is to investigate conducts that may contravene the competition rules, and to bring proceedings before the Competition Tribunal ("the Tribunal") in respect of anti-competitive conducts.

Establishment of Tribunal

The Bill provides for the establishment of the Tribunal within the Judiciary as a superior court of record which will consist of the judges of the Court of First Instance (the "CFI") appointed in accordance with section 6 of the High Court Ordinance (Cap. 4), by virtue of their appointments as such judges. The President and Deputy President of the Tribunal will be appointed by the CE on the recommendation of the Judicial Officers Recommendation Commission.

The Tribunal has jurisdiction to hear and determine competition cases brought by the Commission, private actions as well as applications for the review of reviewable determinations of the Commission. The Tribunal may appoint specially qualified assessors to assist in its proceedings.

Investigative/Enforcement Powers of the Commission

Under the Bill, the Commission may conduct an investigation into any conduct that constitutes or may constitute a contravention of a competition rule either of its own volition, on receipt of complaints or on referral from the Government or the CFI. Its investigative powers include, among others, the power to require production of documents and information, the power to require attendance before the Commission to answer questions, the power to enter and search premises and the power to seize and retain evidence and property under a court warrant. The Commission must have reasonable cause to suspect that a contravention of a competition rule has taken place, is taking place or is about to take place before exercising its investigative powers.

Under the Bill, the Commission will be empowered to accept commitments from an undertaking to take or refrain from taking certain action to address the Commission's concerns about a possible contravention of a competition rule.

In addition, the Commission will be empowered, after its investigation but before bringing proceedings in the Tribunal, to issue an infringement notice to an undertaking against whom it proposes to bring proceedings, offering not to bring those proceedings on condition that the undertaking makes a commitment to pay a sum of up to $10,000,000 to the Government, and to take or refrain from taking certain action to address the Commission's concerns about a possible contravention of a conduct rule.

The Bill will also empower the Commission to enter into leniency agreements with persons who have allegedly contravened the conduct rules under which the Commission agrees not to bring or continue proceedings for a pecuniary penalty against those persons in exchange for their cooperation in the Commission's investigation or in proceedings under the ordinance in respect of other parties involved in the same contravention.

Remedies that may be Applied by the Tribunal

Under the Bill, the Tribunal will be empowered to apply a full range of remedies for contravention of the competition rules. These remedies include, among others, pecuniary penalties not exceeding 10% of the turnover (including global turnover) of the undertaking in contravention of the competition rule for the year in which the contravention occurred, declaration that a person has contravened a competition rule, injunction orders, orders for the termination or variation of an agreement, orders awarding damages to aggrieved parties, and disqualification orders against directors.

Private Actions

In addition to public enforcement through the Commission, the Bill also provides for private actions to be brought by persons who have suffered loss or damage as a result of a contravention of a conduct rule. Such private actions could either follow on from a determination of the Tribunal, the Court of Appeal or the Court of Final Appeal that the conduct is a contravention of a conduct rule, or could be "stand-alone" actions seeking a judgment on a conduct and remedies.

Exemptions and Exclusions

The Bill provides that certain parts of the Bill (e.g. the competition rules) do not apply to statutory bodies except those statutory bodies or their activities specified in regulations to be made by the Chief Executive in Council ("CE in C").

The Bill further provides that CE in C may only make a regulation with respect to a statutory body if he is satisfied that:

(a) the statutory body is engaging in an economic activity in direct competition with another undertaking;

(b) the economic activity of the statutory body is affecting the economic efficiency of a specific market;

(c) the economic activity of the statutory body is not directly related to the provision of an essential public service or the implementation of public policy; and

(d) there are no other exceptional and compelling reasons of public policy against making such a regulation.

The Bill provides that the First Conduct Rule and/or the Second Conduct Rule will not apply to any agreement that enhances overall economic efficiency, or any agreement to the extent that it is made for the purpose of complying with a legal requirement, or any undertaking entrusted by the Government with the operation of services of general economic interest in so far as the conduct rule would obstruct the performance of the particular tasks assigned to it.

The Bill will empower CE in C to make orders to exempt agreements or conducts from the First Conduct Rule and/or the Second Conduct Rule if CE in C is satisfied that there are exceptional and compelling reasons of public policy for doing so or if the agreements or conducts are required to avoid a conflict with international obligation.

As for the Merger Rule, the Bill provides that the rule will not apply to any merger that enhances overall economic efficiency. The Bill will also empower CE in C to make orders to exempt a merger from the Merger Rule if he is satisfied that there are exceptional and compelling reasons of public policy for doing so.

Yung Lap-yan

Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Bill (the "Bill")

Background

The Bill sets out customer due diligence ("CDD") and record-keeping requirements for financial institutions ("FIs") and a new licensing system to regulate remittance agents and money changers. It reflects the requirements of anti-money laundering and counter-terrorist financing ("AML") recommended by the Financial Action Task Force, the international AML standard-setter. Subject to the Legislative Council's scrutiny, the proposed commencement date of the Bill is 1 April 2012.

Financial Institutions

FIs in four different sectors will be affected by the Bill (see: Table 1). At present, the Monetary Authority, the Securities and Futures Commission ("SFC") and the Insurance Authority regulate the banking/deposit-taking, securities and insurance sectors respectively. They also supervise the AML compliance of their regulatees in accordance with their guidelines. The statutory CDD and record-keeping requirements in the Bill largely reflect the AML requirements in these existing guidelines.

	Sectors	Financial Institutions
1	Banking and deposit-taking	Institutions authorized under the Banking Ordinance, Cap. 155
2	Securities	Corporations licensed under the Securities and Futures Ordinance, Cap. 571 ("SFO")
3	Insurance	Insurers, insurance agents and insurance broker authorized/appointed under the Insurance Companies Ordinance, Cap. 41
4	Money service operation	Currently called remittance agents and money changers registered under the Organized and Serious Crimes Ordinance, Cap. 455 ("OSCO")

Table 1: FIs affected by the Bill

As regards remittance agents and money changers, they are now required to register with the Police under the OSCO. After enactment of the Bill, they will be regarded as money service operators ("MSOs"), which shall obtain licences from the Commissioner of Customs and Excise ("CCE").

CDD Measures

Under the new legislation, FIs shall adopt different CDD measures applicable to customers or transactions of different risk profiles. Table 2 highlights different risk profiles of some customers and transactions with the applicable CDD measures provided in the Bill. In general, the level of CDD measures should increase with the risk of the customers or transactions. FIs may implement CDD measures through an intermediary but the FIs will remain liable for any failure in carrying out the measures.

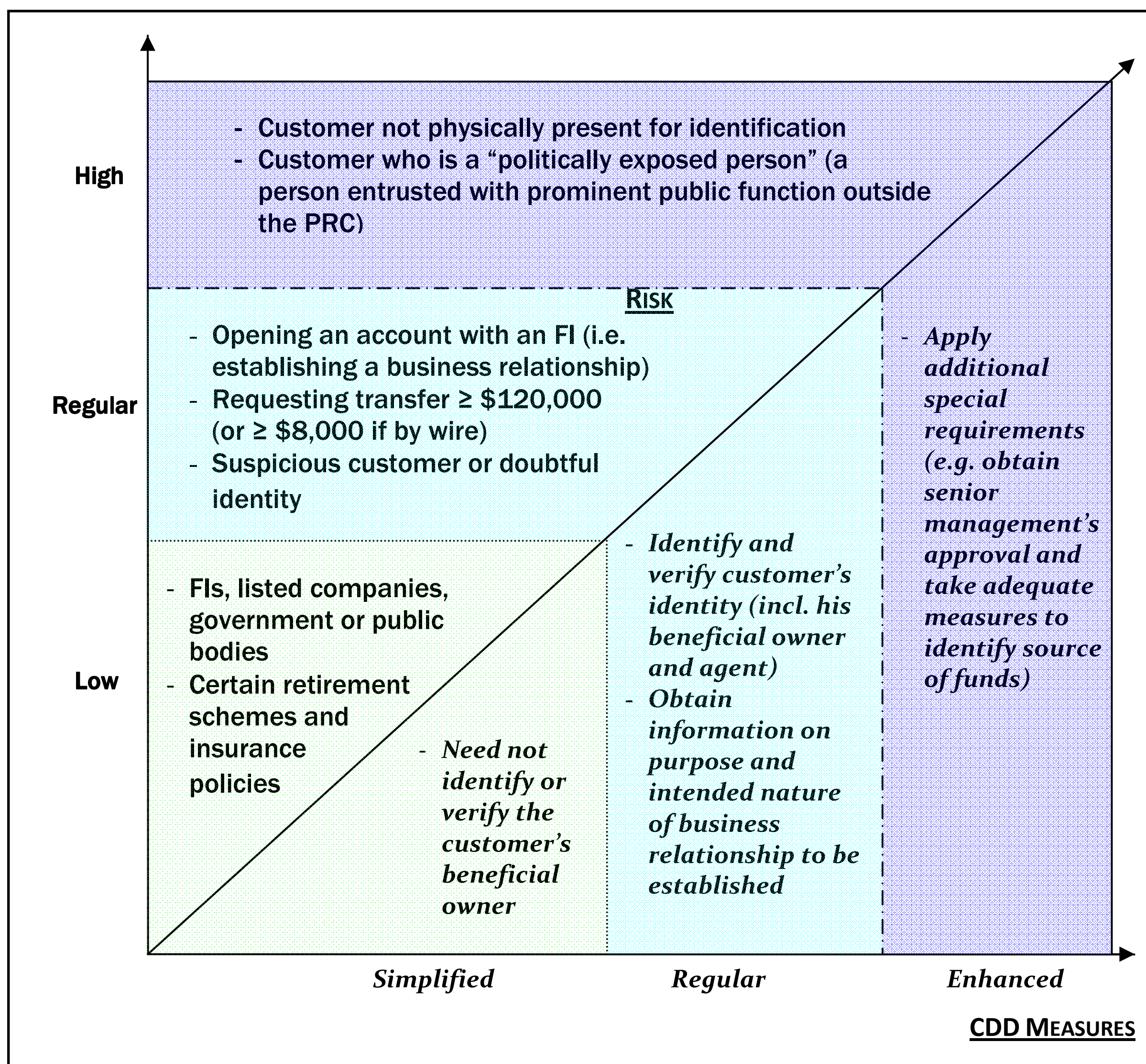

Table 2: The risk profiles of some customers and transactions and the applicable CDD measures in the Bill

Continuous CDD Obligations

The CDD obligations to be imposed on FIs are on-going. FIs should continuously ensure that CDD measures are taken appropriately and customer information is up-to-date. For anyone who is already a customer when the Bill commences, an FI should conduct CDD measures when it finds any suspicious or unusual transaction by the customer, any material change in the operation of the customer's account, or becomes aware that it lacks sufficient information about the customer.

Record-keeping Measures

In addition to CDD measures, FIs shall keep relevant records for a period of 6 years or longer if required by the relevant regulators.

Offence and Sanction

An FI commits an offence if it contravenes the statutory CDD or record-keeping requirements knowingly or with intent to defraud and the FI's directors and employees will also be criminally liable if they knowingly or with intent to defraud cause or permit the FI to contravene the requirements.

An FI may be imposed supervisory sanctions by its respective regulator for breach of CDD or record-keeping requirements, including remedial action orders, public reprimands and pecuniary penalty of up to HK$10 million.

Powers of the Regulators

The regulators will be given a range of supervisory and enforcement powers similar to those provided to SFC under Part VIII of the SFO.

The Bill empowers the regulators to compel evidence, enter FIs' business premises and inspect FIs' books and records, initiate investigations into suspected breaches, apply for court warrants for search and seizure and initiate summary prosecutions. The exercise of such powers will be subject to statutory procedural safeguards. For example, inspection can only be carried out at a reasonable time; an inspector/investigator must provide evidence of authorization; search and seizure can only be done with court warrants; and self-incriminating evidence shall not be used against a person in criminal proceedings.

Licensing MSOs

At present, MSOs need to register with the Police and keep transaction records under sections 24B and 24C of the OSCO. The Police may not refuse registration or access MSO's premises/books/records for routine compliance checks. Under the new legislation, MSOs shall obtain a licence from CCE and, like other FIs, be subject to the statutory CDD and record-keeping requirements. CCE will decide on the licensing matters and ensure MSO's compliance with the licensing requirements.

The Post Office

The Post Office provides money service similar to commercial MSOs. Hence, the Postmaster General ("PMG") shall comply with the statutory CDD and record-keeping requirements in respect of the Post Office's money business. However, unlike other MSOs, PMG may operate the money service without a licence.

Same as other MSOs and their employees, PMG and his employees will be subject to supervisory sanctions (e.g. public reprimands and remedial action orders) and criminal prosecution under the Bill. But PMG and his staff will not be subject to pecuniary penalty since they are already subject to disciplinary mechanisms applicable to government employees.

Review Tribunal

As a check and balance of the regulators' powers, an independent Anti-Money Laundering and Counter-Terrorist Financing (Financial Institutions) Tribunal ("the Tribunal") will be established to review decisions made by the regulators, including their decisions to impose supervisory sanctions and CCE's licensing decisions. The Tribunal will comprise a Chairperson (who must be a person eligible to be appointed as a judge of the High Court) and two members to be appointed by the Secretary for Financial Services and Treasury. The Chairperson and members shall not be public officers. The Tribunal's decision may be appealed to the Court of Appeal.

Beverly Yan
Boyce Yung

Legislation to enhance Protection for Consumers against Unfair Trade Practices

CITB has recently completed a public consultation exercise in relation to its proposals to enhance consumer protection by expanding the current Trade Descriptions Ordinance, Cap. 362 ("TDO") as follows:

(a) expanding the coverage of the TDO to cover *false or misleading representations in respect of services*[1]. "Services" will be widely defined but will not include rights, privileges or facilities provided under a contract of employment;

(b) creating a new offence in the TDO to outlaw *misleading omissions*;

(c) creating a new offence in the TDO to outlaw *aggressive practices*;

(d) creating specific offences in the TDO to outlaw the practices of "*bait-and-switch*" and "*accepting payment* without *intending or being able to supply*";

(e) imposing a *cooling-off arrangement* (under which consumers may cancel the contracts within a specified period) in specified types of transactions (essentially contracts of 6 months duration or more and all consumer transactions concluded during unsolicited visits to consumers' homes or places of work); and

[1] Currently, only goods are covered.

(f) enabling aggrieved consumers to institute private action.

"**Misleading**"

A commercial practice will be considered a "misleading omission" if, in the factual context, it omits or hides material information or provides material information in an unclear or ambiguous manner **and** thereby causes the average consumer to take a transactional decision[2] he would not otherwise have taken. When deciding on whether a practice is a misleading omission, all the features and circumstances of the commercial practice including the limitations of the communications medium deployed and alternative communications measures taken will be taken into account.

"Aggressive Practices"

A commercial practice will be considered aggressive if, in the factual context, taking into account all relevant circumstances, it significantly impairs the consumer's freedom of choice through the use of harassment, coercion or undue influence **and** thereby causes him to take a transactional decision he would not otherwise have taken. The TDO will include a non-exhaustive list of the factors which should be taken into account when determining whether a practice uses harassment, coercion or undue influence. These factors will include the use of threatening or abusive language or behaviour and the exploitation by the trader of any specific misfortune (of which the trader is aware) which is of such gravity as to impair the consumer's judgment or to influence the consumer's decision.

"**Bait-and-Switch**"

"Bait-and-switch" refers to the practice of traders advertising or promoting products at bargain prices or on very favourable terms to attract consumers and to switch them to purchasing more expensive products. More specifically, under the offence of ***"bait advertising",*** a person will be prohibited from advertising the supply of products at a specified price if there are no reasonable grounds for believing that he will be able to offer those products for sale at that price for a reasonable period and in reasonable quantities, having regard to the nature of the market and the nature of the advertisement.

Under the offence of "bait-and-switch", a person will be prohibited from making an offer to sell products at a specified price with the intention of promoting a different product through various tactics such as refusing to show the advertised item, refusing to take orders or to deliver the item within a reasonable time or demonstrating a defective sample of the item. The enforcement agency is required to prove the existence of an intention of promoting a substitute.

For a business acting in good faith, it will be a defence if it has taken immediate remedial action by either replenishing the stock, causing another supplier to supply the same goods or service on the same terms, offering equivalent goods or service on the same terms or it has stated clearly and truthfully in the relevant advertising materials the size of stock available at the specified price and offered all of them for sale.

"Accepting payment without the intention or ability to supply"

It is proposed to create an offence in the TDO to prohibit in consumer transactions the practice of accepting payment or other consideration with the intention, at the time of acceptance, not to supply the contracted products or to supply materially different products.

Strict Liability and Defences

The new offences will be created on a strict liability basis i.e. guilt will not be dependent upon establishing intent (except where expressly stated). As a safeguard, it will therefore be a defence for the accused to prove that the commission of the offence was due to, among other things, a mistake or information supplied by a third party or an accident, and that he had exercised due diligence to avoid committing the offence.

Enforcement

Customs and Excise Department will be the primary enforcement agency but the Telecommunications Authority and Broadcasting Authority (to be merged into a new Communications Authority under the Communications Authority Bill currently before LegCo) will enjoy concurrent jurisdiction in relation to their respective sectors.

As an alternative to prosecution, these bodies will be empowered to seek undertakings from traders to cease offending conduct. Undertakings will be published and any breach of their terms amenable to enforcement action via the courts including, at the court's discretion, by way of injunction restraining specified conduct.

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[2] "Transactional decision" means in essence any decision taken by a consumer on whether, how and on what terms to purchase, make payment for, retain or dispose of a product, or to exercise a contractual right in relation to a product.

Private right of action

Consumers suffering loss as a result of conduct which contravenes the above provisions will be entitled to obtain compensation based on a new statutory private right of action. Such action may be independent of any conviction (standalone) or follow-on from a conviction. The latter will generally be easier to pursue in court since the contravention is established by the conviction.

Exceptions

The proposed new offences will not apply to sectors subject to sector specific regulation such as financial services, property related transactions and professional services independently regulated.

Overseas Experience

The above proposals are based on similar legislation in the UK's Consumer Protection from Unfair Trading Regulations 2008 and the Australian Trade Practices Act 1974 and therefore follow a well trodden path. They are, however, relatively conservative in that more radical initiatives such as joint and several liability of credit card issuers for the misrepresentations and contractual breaches of their merchant suppliers from whom purchases are made using a credit card, as under the UK's Consumer Credit Act 1974 sections 56 and 75, have not been adopted.

Ada Chen
David Grover

Hummingbird Music Ltd. v Accounci
[2010] 1 HKLRD 587

The doctrine of restraint of trade has long been recognised as one which has been expressed with considerable generality, if not ambiguity. Even the best-known formulations contain no attempt at a definition. Rather, the doctrine is regarded as one to be applied to factual situations with a broad and flexible rule of reason. This case provides an illustration of how the doctrine is applied in a sole agency arrangement.

The case

The plaintiff, by two batches of agreements signed in 2006 and 2007, contracted with the defendants, who were two pop singers, as their worldwide exclusive agent and manager. The parties fell out and the defendants sought to rescind the agreements. The plaintiff brought proceedings seeking declarations that the agreements remained binding and enforceable against the defendants. The defendants counter-claimed alleging that the agreements were in restraint of trade. At first instance, the court decided for the plaintiff and awarded it damages for breach of contract and decided that the defendants' defence that the agreements were in restraint of trade failed on merit.

On appeal, the defendants argued that the agreements should have been regarded as being in restraint of trade as (a) they restricted the defendants from working for any person other than the plaintiff and (b) copyright in the recordings and musical works created as part of carrying out the agreements belongs to the plaintiff. The appeal was dismissed.

Two-stage test

To assess whether a contract is in restraint of trade, the court applies a two-stage test. First, it distinguishes contracts which are in restraint of trade from those which merely regulate normal commercial relations between the contracting parties. If the contract is in restraint of trade, the court will go to assess the reasonableness of such restraint. (*Panayiotou v Sony Music Entertainment (UK) Ltd*[1] applied)

To elaborate further, if a contract only ties the parties *during* the continuance of the contract and the ties are only incidental and normal to the positive commercial arrangements at which the contract aims, even though those ties exclude all dealings with others, there is no restraint of trade and no question of reasonableness arises. However, if the contract ties the trading activities of either party *after* its determination, or if one of the parties is unilaterally fettered *during* the contract, so that the contract loses its character for the regulation and promotion of trade and acquires the

1 [1994] EMLR 229

predominant character of a contract in restraint of trade, the question of reasonableness sets in[2].

Joint venture arrangement and copyrights

In deciding that the agreements between the parties were not in restraint of trade, the Court of Appeal (the "CA") took into account the joint venture arrangement between the parties as identified by the Deputy Judge in the first instance. Under the agreements, the plaintiff would devote time and resources to promote the defendant artists in exchange for the exclusive right to duplicate recordings of the defendants' performances and the right to the copyright in the recordings. The ties in the agreements were not only in alignment with the ordinary practice in the industry, they were also mutual, as opposed to unilateral, fetters on both the plaintiff and the defendants.

The CA also found that a producer's acquisition of copyrights in artists' recordings were conventional under the Copyright Ordinance (Cap. 528). Copyright was considered as a jurisdictional matter. The defendants' works would have to be sold to jurisdictions outside Hong Kong if they were to be fully and properly marketed. It would be workable only if the party responsible for arranging those sales (in this case, the plaintiff) had full control of all relevant copyright.

The actual terms of the agreements also supported the court's decision. The agreements could be automatically renewed upon expiry of the contract term unless the defendants served a termination notice. The existence of such an important right to put an end to the agreements does not appear to be able to sit well with a restraint of trade allegation.

Duress/Undue influence

In rejecting the defendants' restraint of trade allegation, the CA recapped the lower court's observation that both the plaintiff and the defendants were ''relative novices in the music industry''. This implies that the relative position or bargaining power of the parties was more or less equal. Indeed, as the lower court's judgment revealed, the defendants were in their mid-thirties ''who were able to decide what was best for them''. As such, it was hard for the defendants to argue that they had reposed trust and confidence in the plaintiff or that they had been duressed or unduly influenced into signing the agreements after all.

Lily Man

2 Esso Petroleum Co Ltd v Harper's Garage (Stourport) Ltd [1968] AC 269, per Lord Pearce

Tai Chok Man v TVB Pay Vision Ltd.
[2010] 2 HKLRD 767

In the last edition of the CU Review, we examined whether a liquidated damages clause is an exhaustive remedy under contract law. Recently, the Court of First Instance (the "CFI") in Hong Kong had the opportunity to consider whether a clause in a fixed term television service contract is a genuine liquidated damages clause or a penalty clause.

Facts

The case arose in connection with a fixed 18-month term pay television service contract entered into between TVB and the claimant which expressly provided that if the claimant terminated the use of the basic services before the contract term expired, he would have to pay all the monthly fees for the remaining term of the contract (the "Provision"). After signing the contract, the claimant informed TVB that he did not intend to continue using the service or paying the monthly fee at the expiry of 3 months. TVB responded that the claimant would still be liable to pay the fees for the rest of the contract period.

The claimant did not succeed in obtaining refund of service fees already paid under the contract in the Small Claims Tribunal and applied to the CFI for leave to appeal.

Decision

The CFI found the legal principles and background circumstances taken into account by the adjudicator in the Small Claims Tribunal accurate and correct. This included the following:

- The total service fees receivable by TVB during the 18-month contract period represent the proceeds to be received by TVB upon completion of the contract. TVB would certainly suffer loss in the event of early termination by the subscriber.

- The Provision was intended to compensate TVB for the profits that it should have obtained but for the early termination of the contract by the subscriber. The amount payable under the Provision was a genuine pre-estimate of the loss sustained by TVB in the event of a breach by a customer.

- The adjudicator ruled that the Provision was a reasonable and valid compensation clause, that the claimant was clearly aware of the Provision in the contract, and that he was bound by the contract to pay all the monthly fees for the rest of the contract period.

The CFI observed that "as a matter of the spirit of a contract and under the general principles of contract law, it is not for the court to strike down or refrain from enforcing a contractual clause merely because a party subsequently considered it unreasonable or unfair." Further, under the legal principles generally applicable to fixed-term contracts, the innocent party is entitled to demand the party who terminated the contract before its expiry to pay such sums as are payable for the rest of the contract period as damages for the breach. This being the case, the Provision was a legally valid liquidated damages clause and not a penalty clause.

The claimant's application was dismissed.

Cases cited in the judgment

The following cases were cited in the judgment:

- *Dunlop Pneumatic Tyre Co v New Garage & Motor Co Ltd*[3] and *Philips Hong Kong Ltd vs A-G of Hong Kong*[4] - As a general legal principle, where a contractual term expressly provides that the party who is in breach of the contract is to pay a fixed sum to the other party, and that sum is a genuine pre-estimate of damages representing the loss likely to flow from the breach, then the term is a liquidated damages clause and not a penalty clause.

- *Robophone Facilities v Blank*[5] – In normal circumstances, the party who alleges that the clause is a penalty clause bears the onus of proving that the clause is of an oppressive and punitive nature.

"Genuine pre-estimate"

In *Tai Chok Man* the relationship between the sum of money payable under the Provision and the loss suffered by TVB should the subscriber terminate prematurely is readily apparent. In many cases however, the task of assessing whether a liquidated damages clause amounts to a "genuine pre-estimate" is more difficult. The courts have indicated the following:

- Identifying situations where the application of the provision could result in a larger sum being recovered by the injured party than his actual loss will generally **not** result in the provision being unenforceable. In *Philips Hong Kong Ltd vs A-G of Hong Kong*, Lord Woolf delivering the judgment of the Privy Council stated: "Except possibly in the case of situations where one of the parties to the contract is able to dominate the other as to the choice of the terms of a contract, it will normally be insufficient to establish that a provision is objectionably penal to identify situations where the application of the provision could result in a larger sum being recovered by the injured party than his actual loss. Even in such situations so long as the sum payable in the event of non-compliance with the contract is not extravagant, having regard to the range of losses that it could reasonably be anticipated it would have to cover at the time the contract was made, it can still be a genuine pre-estimate of the loss that would be suffered and so a perfectly valid liquidated damage provision. The use in argument of unlikely illustrations should therefore not assist a party to defeat a provision as to liquidated damages."

- In *Alfred McAlpine Capital Projects Ltd v Tilebox Ltd*[6] Jackson J stated: "In my view, a pre-estimate of damages does not have to be right in order to be reasonable. There must be a substantial discrepancy between the level of damages stipulated in the contract and the level of damages which is likely to be suffered before it can be said that the agreed pre-estimate is unreasonable. Although many authorities use or echo the phrase 'genuine pre-estimate', the test does not turn upon the genuineness or honesty of the party or parties who made the pre-estimate. The test is primarily an objective one, even though the court has some regard to the thought processes of the parties at the time of contracting."

Josephine Ho

[3] [1915] A.C. 79, 86
[4] [1993] 1 HKLR 269
[5] [1966] 1 WLR 1428, 1447
[6] [2005] EWHC 281

Sun Lee Kyoung Sil v Jia Weili
[2010] 2 HKLRD 30

Facts

The parties in this case were vendor and purchaser who entered into a provisional agreement (the ''Agreement'') for the sale and purchase of a property at HK$24 million. Under the Agreement, the defendant purchaser had to pay an initial deposit of HK$1.2 million by cheque upon signing of the agreement which, however, did not expressly provide that time was of the essence.

The purchaser inadvertently credited the relevant sum into another account of hers, leaving an insufficient amount of funds in the correct bank account. The cheque was thus dishonoured.

Upon notification by the bank of the problem with the cheque, the defendant immediately instructed the bank to rectify the mistake by transferring the right amount of funds into the correct account. The defendant also purchased and delivered a cashier order in the said sum to the vendor's solicitor. The vendor considered that the defendant had repudiated the provisional Agreement by failing to pay the initial deposit in accordance with its terms. She rescinded the Agreement and refused to accept payment from the defendant.

The vendor applied to the Court of First Instance (the ''CFI'') for summary judgment against the defendant, claiming the initial deposit with interest thereon till the date of judgment.

Decision

The CFI began by emphasizing the uniqueness of Hong Kong land law. Relying on two appellate decisions, namely *Kwan Siu Man v Yaacov Ozer*,[1] which affirmed *Wong Wai Chi v Cheung Kwok Fung*,[2] it held that for transactions of such nature as in this case, the contractual parties were ''usually taken to have proceeded on the basis that time is of the essence of the contract, despite the fact that there is no express provision to that effect in the provisional agreement…''.[3] The court further noted that the parties contemplated an urgent transaction since they did not bother to draft a more comprehensive formal sale and purchase agreement which would usually provide that time was of the essence.[4] Finally, the learned judge justified his decision with reference to the specific facts of the case, including the sale of a flat in a large development in the secondary market, the volatility of Hong Kong's property market and the relatively short time, i.e. 9 weeks between the signing of the Agreement and completion.[5]

In the end, although the purchaser argued that the non-punctual payment of the initial deposit was a mere oversight and she all along intended to proceed with the Agreement, the CFI held that the purchaser had repudiated the Agreement and the vendor was entitled to accept such repudiation.[6]

In view of the uniqueness of Hong Kong land law and conveyancing practice and its pivotal role in the court's reaching the conclusion that it did, it is unlikely that the same principle would be readily applied to a contract for procurement of goods or services.

So, what is the position on ***time is of the essence*** under contract law? For all types of contract, time will be considered to be of the essence **if**:

(a) the parties expressly stipulate that conditions as to time must be strictly complied with, **or**

(b) the nature of the subject matter of the contract or the surrounding circumstances show that time should be considered to be of the essence,[7] **or**

1 [1999] 1 HKLRD 216
2 [1996] 3 HKC 287

3 [2010] 2 HKLRD 30 at 37
4 *Ibid* at 38
5 *Ibid* at 49
6 *Ibid* at 36, 52
7 In *Chitty on Contracts Vol. 1 General Principles (29th edition), Sweet & Maxwell* at p. 1241, the author cited some cases in which the court relied on their specific facts to conclude that time was of the essence, e.g. *Mardorf Peach & Co Ltd v Attica Sea Carriers Corp of Liberia* [1977] AC 850, where a charterparty under which the owner is given the right to withdraw the vessel

(c) the circumstances of the case show that precise compliance with stipulations as to time would fulfil the parties' intention,[8] **or**

(d) a party subjected to unreasonable delay gives notice to the defaulting party, making time of the essence.

Halsbury's Laws of Hong Kong and *Chitty on Contracts* provided some examples of contracts where time is considered of the essence. These include mercantile contracts such as cost, insurance and freight contracts and free on board contracts, as well as contracts for sale of goods where the delivery time is fixed.

As an anecdote, a party to a contract may be under a false sense of security if the contract in question has expressly stipulated that time shall be of the essence and yet he has conducted himself in a way contrary to such stipulation. A case in point is *Yue Po Engineering Co Ltd v Ocean Industrial Co*,[9] where the parties contracted for the supply and installation of commercial kitchen equipments. In this case, the contract set out the work schedule to be observed by the supplier and clearly stated time was to be of the essence. It turned out that the defendant purchaser not only delayed in furnishing a proper site for the measurement and installation of the equipment, it also failed to arrange electricity and gas supplies in time, thereby rendering it impossible for the vendor to properly discharge its contractual obligations, namely the construction, installation and testing of the equipment. Considering the purchaser's own conduct, the CFI held that it was an implied term of the contract that delay caused by the defendant in placing the site in a fit condition for the plaintiff to perform its contractual obligations ''would have excused any delay by the plaintiff occasioned by that'' and this is consistent with the expressed term of the contract that time was of the essence of the contract.[10]

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in default of "punctual payment" of hire. See also *Hua Yang Printing Holdings Co Ltd v Pure Health Publishing Co. Europe BV* (HCA 5410/1998) and *Chung Fai Engineering Co & Another v Maxwell Engineering Co Ltd & Another* (CACV 981/2000).

8 *Ibid*, where the author cited *Bunge Corp., New York v Tradax Export SA, Panama* [1981] 1 WLR 711, 729, where the buyers were required to give 15 days' notice of readiness of the vessel so that the sellers could then nominate the port for loading. The House of Lords held time to be of the essence, since performance by the buyer was a condition precedent to the seller's ability to perform his obligation.

9 HCA 3660/1995

10 *Ibid* at para 27

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