PCLL Conversion Examination
June 2021
Examiner's Comments
Commercial Law

Part A

Question 1

Overall, candidates who answered this question answered well.

Question 1(a) required candidates to identify that the sale was one by description and that section 15 of SOGO applied. Breach of the condition entitled Betty to reject the bags and treat the contract as repudiated. The other option was for Betty to accept the breach and claim for damages. Candidates who answered the question well also discussed whether Betty's loss of profits could be claimed.

The issue in Question 1(b) was whether Betty was deemed to have accepted the bags. Candidates should have discussed sections 37(1)(b), 37(2)(a) and 37(4) of SOGO. Applying the facts, was it reasonable for Betty to have taken 1 month to inspect the bags? Were the defects apparent and easily noticeable such that it could be said that Betty would be deemed to have accepted the bags? Candidates should have come up with sensible and logical conclusions in this regard.

Question 1(c) required the discussion of sections 30, 33(2) and 13(3) of SOGO. This is a situation where the parties agreed that the bags would be paid by instalments and required candidates to discuss whether the contract for sale was severable. If the contract was not severable, the breach of any condition by the seller can only be treated as a breach of warranty and not as a ground for rejecting the bags so in such case, Betty must pay for all the 1,000 bags and sue Anna for damages for the second batch of defective bags. If the contract was severable, then Betty can pay for the first batch and treat the delivery under the second batch as repudiation of the second contract and not accept delivery of the same.

Question 1(d) required candidates to discuss the 2 scenarios under section 14(1)(a) and 14(1)(b) of SOGO. If the trademark claim was before the contract of sale, then Anna would not have the right to sell the bags and in this case, section 14(1)(a) of SOGO applies. Betty can repudiate the contract and she is released from paying for the bags. If the trademark claim was after the contract of sale, then section 14(1)(b) applies. There is a breach of warranty of quiet possession and Betty is entitled to sue for damages only. In this latter case, Betty still has to pay for the bags.

Question 2

Question 2(a) required candidates to discuss when the property of the car was transferred because under section 22 of SOGO, unless otherwise agreed, the goods remain at the seller's risk until the property is transferred to the buyer. So the first step was to discuss who had the property in the car and candidates should have discussed sections 18 to 20 of SOGO. Candidates should then apply the facts – the deposit was only around 5% of the purchase price and applying *Ward v Bignall* 1 QB 534

(property in specific goods to pass only on delivery or payment), George can argue that the property of the car has not passed to him and he is under no obligation to pay the price. However, section 22 of SOGO states that nothing in section 22 shall affect the duties or liabilities of either the seller or the buyer as a bailee of the goods of the other party. So even if the property in the car has passed to George, if the fire was caused by the fault of Fred or staff at his showroom, then as bailee, Fred would still be liable for the damage of the car. It was therefore important to find out the cause of the fire.

For Question 2(b), Fred's colleague had breached Edward's instruction to sell the car. The first issue to discuss was whether Fred's showroom was acting as a mercantile agent in the sale. Section 3(1) of the Factors Ordinance should be discussed and applied to the facts. It would seem that vis-à-vis Edward, Fred was only acting in his personal capacity when he agreed to help Edward sell his car. However, since Fred's showroom was in possession of the car with Edward's consent, candidates should then discuss whether Harry was acting in good faith and noticed that Fred's colleague had no authority to sell the car? Under the *nemo dat* rule and section 23(1) of SOGO, if Harry did not have title to the car, then John acquired no better title than Harry. In this discussion, candidates should also discuss section 24 of SOGO, i.e., whether sale of the car on the online website was a market overt, justifying the exception to the *nemo dat* rule.

Part B

Question 1(a)

The relationship between the bank and its customer is normally one of contractual debtor and creditor. Many students were confused about the bank and the customer's respective role under the facts.

With respect to Charlie's savings / checking account, Charlie is the creditor and the bank is the debtor. With respect to Charlie's residential flat, the bank is the creditor/ mortgagee and Charlie is the debtor/ mortgagor. With respect to the account of ABC Limited, ABC Limited is the creditor and the bank is the debtor. With respect to the revolving loan facility, ABC Limited is the debtor and bank is the creditor. The account opened for Charlie's daughter is a trust bank account, with the daughter as the beneficiary. The trust account is opened in Charlie's name as trustee and is usually styled something like "Re Chelsea, a minor" or "Charlie, in trust for Chelsea, a minor".

Question 1(b)

The bank is under a duty to adhere to the mandate of the customer, including honouring the cheques of a customer in accordance with the mandate given. A cheque is a bill of exchange, a negotiable instrument. A crossed cheque restricts negotiability. When it is marked "account payee only," it means that it can only be deposited into payee's account. The bank has obligation to pay Comfy Sofa Limited on demand on or after the date of the cheque. Post-dated cheques are acceptable in Hong Kong.

Charlie's stop payment order – Charlie is entitled to countermand negotiable instruments he made. To be an effective countermand, the communication must be capable of being authenticated by the bank. The facts did not indicate whether the communication was clear in stating the payment to the countermand. If the countermand was a proper one, the bank has breached its duty.

The bank has a duty to keep its customer's information confidential. Unless the revealing of the information falls into an exception (e.g., consent, compulsion by law, public policy etc.) the bank breached its duty to keep the information secret. No exception seems to apply based on the facts. ABC Limited's contractual obligation to provide the same information to Omega Bank pursuant to its loan application is irrelevant. The bank has breached its duty.

Alpha Bank has a right of set off – the right to combine accounts of the customer and amalgamate the amounts to reduce any debt due to the bank. However, the right to set off can only be exercised if the debit and credit balances are already due; it cannot set off its immediate liabilities to the customer (funds in Charlie's savings account) against a contingent liability (Charlie's guarantee obligations). Alpha Bank's dishonoring of the cheque was wrongful – ABC Limited is not yet in default and Alpha is not entitled to enforce Charlie's guarantee.

Debiting Chelsea's account to pay for the mortgage was also wrong since it is a trust account. Funds in that account ought to be used for the benefit of Chelsea only. Alpha

Bank is not entitled to set off a credit balance in a trust account against a debit balance on the trustee's private account.

Question 2(a)

Students should systematically compare pledges and floating charges as security interest at least in the following aspects – title, possession, control, perfection, and enforcement. Many students neglected to answer the second part of this sub-question - discuss which of the two is more favourable from the bank's point of view.

Negotiable instruments are often accepted as pledged assets by banks but not bulky tangible assets such as machinery. With machinery, the Bank needs to worry about logistical issues such as storage, maintenance, and obsolescence of the assets. Pledgees are also bailees and owe a duty of reasonable care.

Floating charge over book debts – chargor retains control over the book debts in the ordinary course of business; a floating charge over book debts is required to be registered under s335 of the Companies Ordinance within a month of the creation (many students still wrote down the old law of 5 weeks). Notice should be given to debtors per Dearle v. Hall (many students did not understand who the "debtors" are in this context). Floating charges would rank behind fixed chargees and preferential creditors in liquidation.

Which is more favorable to the bank also depends on the value of the machinery and the book debts. Any sensible discussion that reflects a correct understanding of the law will receive full credit, regardless of the conclusion.

Question 2(b)

Having a prior charge registered means that the subject asset is encumbered and a charge granted to Kowloon Bank over the same asset will very likely be subject to that prior charge. The facts did not indicate whether there is a negative pledge clause, etc. in the prior debenture. Kowloon Bank should review the prior charge document carefully and see how exactly the current proposed charge will be affected; it should inquire with GHL regarding same and explore the possibility of entering into an inter-creditor agreement with the other lender. Kowloon Bank may also consider requesting other assets as security from GHL. Discussions on crystallization, Dearle v. Hall, among other applicable concepts, were also given credit.

Question 2(c)

Floating charge over stock in trade is a specified charge that must be registered within a month of creation under s335 of CO. The main purpose of charge registration is to give notice to others that the subject assets are encumbered. However, date of registration with the Companies Registry does not determine priority.

Question 2(d)

Students should discuss the ramifications of the failure to register the charge for each party and the options available to each party. Under S337 of CO, GHL and all

responsible persons commit an offence and are subject to a fine; the specified charge is void against the liquidator and other creditors but it does not prejudice GHL's repayment obligation to the bank. The bank may, at its option (many students still wrote down the old law of automatic acceleration) accelerate the loan and make all payments immediately due. GHL may try to seek an extension to register the charge under s346 of CO, failing that, may consider negotiating with the bank to execute a new charge document and register it within one month.

Part C

Question 1

a) Answers should first have considered actual undue influence because of the suicide threat. The better answers highlighted that an advantage of actual influence is that there is no need to prove that the agreement was suspicious. Presumed undue influence should also have been considered. Was there a relationship of trust and confidence (some answers said this was automatically presumed but that would only be the case where it is alleged a parent has undue influence over a child and not as in the question where the allegation is that son had undue influence over the parent!)? Any sensible application to the facts received full credit, as was the case when considering if the agreement was suspicious. If the presumption could be established, there was nothing on the facts to rebut it.

   Finally, misrepresentation should have been considered. On the facts there was a misrepresentation as to intention regarding what Tom would do with the money. The better answers identified here that the actual misrep was that Tom was misrepresenting a fact –the state of his mind Edgington v Fitzmaurice and if this could be proved then there was a clear fraudulent mispresentation. Reliance on the misrep should then have been considered and in particular that this need only be partial. A good answer should have finished off by highlighting the main remedy for undue influence, misrepresentation,is rescission and on the facts there were no bars to rescission.

b) Too many answers simply wrote all they knew on guarantees in an unfocused way. The better answers went through each clause identifying its legal effect. The first sentence of clause 8.1 excluded the guarantor's subrogation and indemnity rights. The second sentence was a suspense account clause which has a similar effect as the guarantor's money is not being used to pay off the creditor. Answers should have explained what the rights of subrogation and indemnity were and how a suspense account works. Clause 8.2 answers should have explained the material variation rule in Holme v Brunskill and made the point that the effect of the clause was to exclude the rule. The better answers made the additional point that the wording of the clause just covered a variation and if the changes to the loan agreement were sufficiently radical to amount to a new agreement this would not be covered by the clause Triodos Bank v Dobbs.

Question 2

a) The focus of the answers should have been on the legal effect of the clauses. A general introductory point to be made was to consider whether the clauses were incorporated into the contract.
   (i) It should have been highlighted that as the clause was an attempt to exclude the remedy of a refund for breach of S16 SOGO it was an exclusion clause and under S11 (2) CECO void if the buyer was a consumer and subject to the reasonableness test if a non-consumer. A good answer should have focused on the requirements specified in S4 CECO in order for the buyer to be a consumer. It was essential to apply

these requirements to the facts. In particular, whether the buyer was buying in the course of a business when the car was wanted for a mixture of private and business use. Any sensible discussion of this received full credit.

(ii) This was poorly done. Few answers identified that the main issue here was whether the goods were <u>ordinarily</u> supplied for private use, given the fact what was being being purchased was a transit van. This is a separate requirement that must be fulfilled to be a consumer. It is not sufficient by itself that the buyer was clearly not buying in the course of a business.

(iii) Most answers correctly identified that the clause here was an attempt to exclude S5 SoS (IT) O the implied term of care and skill. This is void in the case of a consumer S8 SoS (IT) O. However, few answers identified that the contract was not just for services but also for goods –replacing a gearbox and the attempt to exclude liability for the quality of spare parts fitted would be an attempt to exclude the implied condition of merchantable quality and void if the customer was a consumer under S12 CECO. (Not S11 as a repair contract is categorised as work and materials contract not sale of goods.)

b) This question required a sound knowledge of the Pawnbrokers Ordinance Cap. 166. Most answers correctly identified the Ordinance applied and that some criminal offences had been committed e.g. S21 (2) (b) –illegal to require a bank deposit book as a security and regarding the complaint concerning lack of knowledge of the interest rate S13 requires the pawn ticket to detail the rate. However, the main focus of the answer should have been on whether the four month redemption period S17 (1) had been extended by compliance with the S17 (2) requirements. Many answers seemed unaware of the existence of this provision.