

**HONG KONG BAR ASSOCIATION'S FURTHER COMMENTS ON
Statute Law (Miscellaneous Provisions) Bill 2001
(Power to Give Refund of Deposit)**

Introduction

1. The Bills Committee of LegCo considered Part VII of the captioned Bill relating to the proposed legislation to give the Court power to order refund of deposit. In the course of so doing, the members made reference to sections 55(1) and 55(2A) of the New South Wales Conveyancing Act 1919. Section 55(2A) is couched in very wide terms and is comparable to section 49(2) of the Law of Property Act 1925 in England. Section 55(1) is however more restricted in scope in that it would only apply to cases where there is a defect in the vendor's title. The Bills Committee therefore sought the Bar's view on whether there are merits in amending the Conveyancing and Property Ordinance along the lines of section 55(1) of the New South Wales Act.

Section 55 of the New South Wales Conveyancing Act 1919

2. This section provides:

“Right of purchaser to recover deposit etc.

- (1) In every case where specific performance of a contract would not be enforced against the purchaser by the Court by reason of a defect in the vendor's title, but the purchaser is not entitled to rescind the contract, the purchaser shall nevertheless be entitled to recover his or her deposit and any instalments of purchaser money he or she has paid, and to be relieved from all liability under the contract whether at law or in equity, unless

the contract discloses such defect and contains a stipulation precluding the purchaser from objecting thereto.

- (2) If such undisclosed defect is one which is known or ought to have been known to the vendor at the date of the contract the purchaser shall in addition be entitled to recover his or her expenses of investigating the title.”

3. For section 55(1) to apply, the following 3 conditions must be satisfied:

- (a) There is a defect in the vendor’s title;
- (b) Because of the defect in title, the Court would not order specific performance against the purchaser; and
- (c) Although the Court would not order specific performance against the purchaser, the purchaser is not entitled to rescind the contract.

Where these 3 conditions are present then unless the contract discloses the defect in the vendor’s title and the contract also contains a stipulation precluding the purchaser from objecting to such defect in the titled disclosed, section 55(1) would operate to give the purchaser a statutory right to recover all deposit and part payment of price and also to be relieved from all liability under the contract. Hence plainly this would mean that there would be a statutory right to rescind the contract.

4. It is clear also from section 55(2) that for the purpose of the statutory right to rescind under section 55(1) the defect in title could be any type

of defects, even though it is not such type of defects which the vendor is aware of or ought to be aware of. Of course if the vendor is not aware of the defect then obviously there could not be a clause in the contract disclosing such defect and precluding the purchaser from objecting to it.

Discussion

5. There are of course many cases where the Court would not order specific performance against a purchaser even though the purchaser is in breach of the contract. The reason for the Court's refusal to order specific performance could be due to a number of reasons unrelated to any title problem. However, all these cases are not relevant for the purpose of section 55(1) because one of the requirements for the section to operate is that the reason for the Court's refusal to order specific performance is because of the defect in the vendor's title.

6. In Hong Kong it is now accepted that one of the tests of whether a good title is shown is whether the Court would order specific performance of the contract against the unwilling purchaser. Even if there is some flaws in the title of the vendor if on the whole the Court is satisfied that there is substantial performance of the contract, the Court could still order specific performance against an unwilling purchaser (see **Goldful Way Development Ltd. v Wellstable Development Ltd.** [1998] 4 HKC 679, approved by the Court of Appeal in **Wide Link Ltd. v Tam Sing Cheong & others** (unreported) CACV No. 151 of 1999. See also the Judgment of Litton NPJ in **Green Park Properties Ltd. v Dorku Ltd.** [2002] 1 HKC 121).

7. Thus the only situation which would be relevant for the purpose of section 55(1) is when (a) there is a defect in title which caused the Court to refuse to order specific performance of the contract; and yet (b) the purchaser is not entitled to rescind at common law. At common law, even in the absence of any

express term the vendor is under an obligation both to show and pass a good title (see **Active Keen Industries Ltd. v Fok Chi-keong** [1994] 1 HKLR 396). This is a very important obligation and if there is any defect in the title, it is difficult to see how the purchaser could be deprived of the right to rescind the contract unless the obligation as to title or the purchaser's rights in consequence of any breach of the obligation as to title are qualified by an express term of the contract.

8. Whatever may be the position in other jurisdiction, in Hong Kong, it is recognized and reaffirmed by the Court of Final Appeal that parties to a contract for the sale of land are free to agree on terms which would modify the common law rights. The position is best summarized in the Judgment of Lord Hoffmann NPJ in **Jumbo King Ltd. v Faithful Properties Ltd.** (1999) 2 HKCFAR 279 at 299:

“On the question of the cocklofts I agree with Litton PJ that cls. 18(e) and 19 preclude the purchaser from basing any objection to title on this ground. Ms Eu submitted that there was a rule of equity which prevented a vendor, as a matter of law, from relying on such clauses in a case in which he knows or ought to know of a defect in title. I think that is putting the matter far too broadly. Contracts for sale of land are not exceptions to the principle that parties have freedom of contract and may agree to whatever terms they like. What the cases show is that *the courts will be very reluctant to construe such a term as enabling the vendor to mislead the purchaser.* As is stated in Farrand, Contract and Conveyance (4th ed) at p. 93, such conditions are “subject to the overpowering principle that the vendor must not mislead the purchaser in any way; this means that a sufficient indication of the risk must be given before the contract is made.” This may be said to leave it

unclear whether the “overpowering principle” is an aid to construction of the contract or something which operates outside the contract. It probably does not matter, *although for my part I think it is better regarded as a matter of construction.* Thus it is inconceivable that a term will be construed as enabling a vendor to impose upon a purchaser a serious defect in title of which he actually knew. No purchaser would sign a contract which was bare-faced enough to stipulate expressly that the vendor need not disclose serious defects in title of which he had actual knowledge and, even if there was no objection on grounds of public policy, nothing less than the most express language would do. On the other hand, the position is different if the vendor did not actually know of the defect but had the means of knowledge, or if the matter was technically a defect in title, but something which a purchaser might reasonably be prepared to accept. *Prima facie, it is the duty of the vendor to deduce and then convey a good title and if he relied upon the terms of the contract to shift the risk of any defect in title to the purchaser, the language must clearly do so ...*” (emphasis added)

9. Thus in cases where there is a defect in title, the purchaser would have a right to rescind and section 55(1) would only be useful in cases where there are terms in the contract which are in language clear enough to shift the risk of defect in title to the purchaser (and hence the purchaser is not entitled to rescind) and yet the language employed is not such that (a) the particular defect in question is expressly identified in the contract itself; and also (b) there are express words which preclude the purchaser from objecting to the particular disclosed defect.

10. Hence it is clear that section 55(1) is not so much a provision to

enable the Court to exercise discretion to order the refund of deposit (or part payment of price) in exceptional circumstances. It is, in effect, a legislative provision limiting the rights of the parties to modify the vendor's obligation on good title so that any modification of the vendor's obligation on title could only take the form of expressly naming or disclosing the defect in title and providing that the purchaser shall not take objection to that disclosed defect. In all other cases or other forms of provision for modification on the obligation on title, even though the language may well be clear enough to satisfy the current common law requirements, that would not assist the vendor much because the purchaser could, under section 55(1) obtain back his deposit and any payment of the price and at the same time being relieved from any further obligation under the contract. This would in effect mean that the purchaser could rescind the contract and the vendor would not be able to benefit from such term.

11. There is of course something to be said in favour of having legislation to provide that the obligation on good title is not to be modified unless such modification is to take a specified form in compliance with certain strict criteria set out in legislation. This would have the effect of improving certainty in that one can be reasonably sure that any other form of modification would not be effective and one could thus avoid the difficulty and uncertainty which may often arise in the construction of the terms of the contract.

12. On the other hand, the Bar could not see anything wrong or unsatisfactory in the current common law position so admirably expressed and summarized in the Judgment of Lord Hoffmann in **Jumbo King**. Given the overriding matter of principle of freedom of contract, the Bar does not see why parties to a contract for sale of land should be deprived of the rights to modify the vendor's common law obligation on title in relation to defects which he is not aware of. This is because in such circumstances, section 55(1) would operate to render any such modification, however clearly expressed, to be useless, because

the defect is not disclosed (and could not have been disclosed because the vendor is not aware of it) and so the purchaser could in effect rescind the contract on account of such defect in title.

Conclusion

13. On the whole, the Bar is not in favour of having any statutory provision like section 55(1) of the Conveyancing Act 1919 of New South Wales as it is an unnecessary fetter to the principle of freedom of contract. Unlike many other contracts for the supply of consumer goods or services, formal contracts for sale of land are usually handled by solicitors and provisional sale and purchase agreements do not normally give rise to any problem in this respect because there is usually no term in the provisional sale and purchase agreements to modify the parties' obligation on title. In most of the sale of first hand property, the terms of the contract are governed by either the Consent Scheme or the Non-Consent Scheme, and could hardly be said to be inequitable. In the case of the sale of second hand property, the parties are likely to be in equal bargaining power and there is no reason why terms relating to the vendor's obligation on title negotiated through solicitors and freely entered into should not be given their proper effect.

Dated this 6th May 2002.