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Panel on Administration of Justice and Legal Services

Meeting on 22 March 2021

Updated background brief on the proposed application of the United Nations Convention on Contracts for the International Sale of Goods to the Hong Kong Special Administrative Region

Purpose

This paper provides updated background information on the proposed application of the United Nations Convention on Contracts for the International Sale of Goods ("CISG") to the Hong Kong Special Administrative Region ("Hong Kong"). It also summarizes the views and concerns expressed by members of the Panel on Administration of Justice and Legal Services ("the Panel") in previous discussions on this topic.

Background

2. According to the Administration¹, CISG is a treaty which provides a set of uniform rules governing the formation, performance and remedies for breach of contracts for the international sale of goods within its scope. Its purpose is to provide a modern, uniform and fair regime for contracts for the international sale of goods, and through which to contribute to introducing certainty in commercial exchanges and decreasing transaction costs. In particular, CISG applies to contracts for sale of goods between parties whose places of business are in different Contracting States, subject to the right of the parties to opt out in whole or part of CISG. CISG has been adopted by over 90 Contracting States from diverse legal traditions and levels of economic development, which together represent over two-thirds of the global economy.

¹ Hyperlink to the Department of Justice ("DoJ")'s webpage for the United Nations Convention on Contracts for the International Sale of Goods:
<https://www.doj.gov.hk/eng/public/CISG.html> accessed on 9 March 2021.

3. On 27 May 2019, the Administration briefed the Panel about its plan to launch a three-month public consultation exercise on the proposed application of CISG to Hong Kong by outlining the key issues and arrangements of the consultation as set out in the Administration's paper (LC Paper No. CB(4)908/18-19(03)). As explained in the paper, with the number of Contracting States to CISG growing, there were views in favour of extending the application of CISG to Hong Kong for reasons that such application could potentially facilitate trade growth, prevent businesses from being subject to unfamiliar foreign laws when entering into cross-boundary transactions, improve Hong Kong's competence in resolving CISG disputes and hence enhance Hong Kong's status as an international trade and dispute resolution hub.

4. The Panel was consulted on the salient features of CISG including its key provisions and choices of opting-out and opting-in; the initial economic and legal considerations for extension of CISG to Hong Kong; interplay between CISG and Hong Kong law including differences between the two regimes and the merits and drawbacks of opting-in or opting-out; the proposed application of CISG to Hong Kong and its implementation into Hong Kong law; possible arrangements between Mainland China and Hong Kong; and the consultation arrangements and issues.

5. The public consultation exercise was launched on 2 March 2020 with the issuance of the paper titled "Proposed Application of the United Nations Convention on Contracts for the International Sale of Goods to the Hong Kong Special Administrative Region".² The original public consultation period was for three months but had been extended to end on 30 September 2020. The Administration briefed the Panel on the public consultation exercise at its meeting on 25 May 2020 and consulted members' views.

Major views and concerns of members

6. The major views and concerns of members raised at the Panel meetings on 27 May 2019 and 25 May 2020 are summarized in the ensuing paragraphs.

Reasons for Hong Kong not being a party to CISG

7. Members queried why CISG was not applicable to Hong Kong for years, while many of its top trading partners had become the Contracting States. The Administration replied that prior to 1 July 1997, CISG was not applied to Hong Kong because the United Kingdom ("UK") was not a Contracting State. During

² Hyperlink to the public consultation paper (LC Paper No. CB(4)572/19-20(01)):
<https://www.legco.gov.hk/yr19-20/english/panels/ajls/papers/ajls20200525cb4-572-1-e.pdf>

and after the transition, China had not deposited notification with the Secretary General of the United Nations for applying CISG to Hong Kong though the former was a Contracting State. The Administration advised that, given the recent trend that many close trading partners of Hong Kong had become parties to CISG, the Administration considered that the proposed application of CISG to Hong Kong could potentially promote its trade growth.

Benefits to Hong Kong and the legal profession

8. In response to members' queries about the benefits of the proposed application of CISG to Hong Kong and to the legal profession, the Administration said that based on an initial assessment, the benefits of extending CISG to Hong Kong included the potential to drive Gross Domestic Product ("GDP") and trade growth, preventing Hong Kong businesses from being subject to unfamiliar foreign laws when entering into cross-boundary transactions, improving Hong Kong's competence in resolving CISG disputes and providing freedom of contract.

9. The Administration elaborated that as almost all major trading members of the World Trade Organization and nearly half of the countries participating in the Belt and Road Initiative were members of CISG, the aim of which was to reduce legal barriers that could diminish or hamper the free flow of trade, CISG would assist in driving Hong Kong's GDP and trade growth. On the other hand, given the economic strength of Hong Kong's top trading partners, Hong Kong businesses might have difficulties in ensuring that contractual balance was kept or that a governing law familiar to them was chosen and hence might derive benefit from the default application of CISG to contracts falling within its scope. CISG could also provide a more neutral platform for trade between Hong Kong businesses and businesses from newly developing countries or economies, who might not be familiar with each other's laws.

10. In terms of potential benefits to the legal profession, as CISG cases might often be resolved by means of arbitration, the application of CISG to Hong Kong could provide an opportunity to further enhance its status as an international legal and dispute resolution services centre. Moreover, the application of CISG to Hong Kong and implementation in Hong Kong law might benefit the legal profession by increasing the opportunities for Hong Kong lawyers from the perspective of advising on relevant trade contracts and dispute resolution.

11. Members further enquired to what extent CISG would help reduce the number of disputes arising from the sales of goods contracts. They also enquired how, as Hong Kong had been a close trading partner of the Mainland for a long time, the application of CISG could benefit Hong Kong/Mainland transactions. In addition, questions had been raised on how the proposed application of CISG would help Hong Kong establish itself as the centre for

international legal and dispute resolution services in the Asia-Pacific region, which was supported under the "Outline Development Plan of the Guangdong-Hong Kong-Macao Greater Bay Area" promulgated in February 2019.

12. In response, the Administration said that given the uniform CISG rules and the relatively long history of CISG, which had entered into force in 1988, it was hoped that fewer disputes would arise between parties who had been familiar with the CISG rules. It was also hoped that, when such disputes arose, they could be resolved efficiently as the United Nations Commission on International Trade Law was maintaining a database with large number of CISG cases for reference.

Comparison of regimes for governing international sale of goods contracts

13. In response to members' enquiries regarding the major differences between CISG and the Hong Kong common law system in governing contracts for international sales of goods, the Administration advised that among other things, CISG was relatively more pro-contract than existing Hong Kong laws in the sense that its policy was to keep the contract alive, even in the case of breach, rather than allow for easy termination. The Administration also pointed out that CISG appeared to be more in line with modern commercial expectations and commercial practice in at least two important areas, namely, obligations concerning the fitness and quality of goods sold, and remedies (e.g. the right to cure, the easy ability to vary the contract, and the remedy of price reduction).

Excluding the applicability of the United Nations Convention on Contracts for the International Sale of Goods

14. Members noted that the Administration would, subject to the results of the public consultation exercise, seek the application of CISG under Article 153 of the Basic Law and the implementation of CISG in Hong Kong law by way of enacting a new stand-alone Ordinance ("New Ordinance"), which would contain provisions with the effect that CISG rules would prevail to the extent there was any inconsistency between the New Ordinance or CISG and any other Hong Kong laws.

15. Noting the effect that the various differences between CISG and existing Hong Kong laws might have on the application of CISG to Hong Kong, members enquired about the potential conflicts between CISG and the Sales of Goods Ordinance (Cap. 26). The Administration explained that, based on its own analysis it could see no fundamental conflict between CISG and Hong Kong law making it impossible for the application of CISG to Hong Kong.

16. Some members enquired how the parties to a contract could exclude the applicability of CISG and, if one of the parties to an international sales contract

wanted to exclude the applicability of CISG entirely in favour of other laws but the other party did not agree, whether the applicability of CISG could be excluded.

17. The Administration advised that as the autonomy of the parties to international sales contracts was a fundamental theme of CISG, the parties could, by agreement, derogate from virtually any CISG rule (except Article 12) or exclude the applicability of CISG entirely in favour of other laws. However, if mutual agreement could not be reached to exclude the applicability of CISG, CISG would be automatically applied to the relevant contract when the relevant conditions provided for in CISG were satisfied.

Reciprocal arrangement between Hong Kong and Mainland China

18. Members noted that CISG applied to contracts for sale of goods between parties whose places of business were in different States when the rules of private international law led to the application of the law of a Contracting State, but several Contracting States (e.g. China, Singapore and the USA) had declared under Article 95 of CISG that they were not bound by this ground as permitted by CISG. In explaining the such declarations, the Administration said that under Article 1(1)(b) of CISG, CISG applied to a contract when one of the parties or both were not Contracting States but had chosen the law of a Contracting State, say Canada, to govern the contract. However, in respect of China, since China had made a declaration pursuant to Article 95 of CISG that it was not bound by Article 1(1)(b) of CISG, CISG would not apply automatically to the contract.

19. Members asked the Administration to elaborate on its plans on considering the possibility of having a reciprocal arrangement in place between Hong Kong and the Mainland such that a sale of goods contract between businesses in the two places would be treated by both jurisdictions as if it were a contract between businesses in different contracting parties to CISG ("the reciprocal arrangement").

20. The Administration explained that since transactions between a business in Hong Kong and a business in Mainland China were within the same country, CISG (as an international treaty) did not automatically apply. However, in view of the close economic ties between the Mainland and Hong Kong and to facilitate sale of goods between businesses in the two places, the Administration proposed that, initially on a unilateral basis, the New Ordinance would contain provisions which would in effect apply the CISG rules also to Hong Kong/Mainland transactions. In the longer term, however, DoJ might explore and discuss with the Mainland the possibility to establish the reciprocal arrangement so that the CISG rules could be implemented comprehensively and systematically in respect of Hong Kong/Mainland transactions.

21. Some members wished to confirm whether, even if CISG was applicable to Hong Kong/Mainland transactions, the parties to a contract could opt out of CISG and choose either the Mainland laws or Hong Kong laws to govern the contract concerned. The Administration answered in the affirmative and added that the contractual parties could also choose the laws of other countries, e.g. UK, as the governing law of the contract.

Latest position

22. The Administration will brief the Panel on the main public views received in the consultation, the Administration's response and its recommended way forward at the Panel meeting to be held on 22 March 2021.

Relevant papers

23. A list of relevant papers is in the **Appendix**.

Council Business Division 4
Legislative Council Secretariat
16 March 2021

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List of relevant papers

Meeting	Date	Item	LC Paper No.
Panel on Administration of Justice and Legal Services	27.5.2019 (Item III)	<u>Administration's paper</u>	CB(4)908/18-19(03)
		<u>Minutes of meeting</u>	CB(4)1224/18-19
	25.5.2020 (Item VI)	<u>Background brief</u>	CB(4)583/19-20(06)
		<u>Public consultation paper by the Administration</u>	CB(4)572/19-20(01)
		<u>Executive summary of the public consultation paper by the Administration</u>	CB(4)572/19-20(02)
		<u>Minutes of meeting</u>	CB(4)872/19-20

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