Letterhead of THE LAW SOCIETY OF HONG KONG

2nd February, 2000

Our Ref : SG/FA/1092
Your Ref :
Direct Line :

The Hon. Ms. Margaret Ng,
New Henry House, 10/F.,
10 Ice House Street,
Central,
Hong Kong.

Dear Margaret,

Re: Section 12 of the Conveyancing and Property Ordinance

Further to our discussion on Friday of last week the Law Society has been looking further at the complaint made by Mr. Justice Godfrey concerning the absence of any equivalent of Section 49(2) of the Law of Property Act in Hong Kong legislation. Initially our Property Committee felt that this was a matter that occurred infrequently and that it did not justify a change in the law. The Committee was, however, divided over the issue. I have since asked the Chairman of the Property Committee John Morgans for his views and I now attach these as he has prepared a very useful paper which may assist the LegCo Panel meeting although it only represents his views. However, the Law Society is looking at the matter again particularly in the light of the research that John Morgans has done and it may be that there will be a change of position.

We shall attend the Panel meeting on the 15th.

Yours sincerely,

Patrick Moss
Secretary General

Encl.
PM/ff

TO: Patrick Moss, The Law Society of Hong Kong

CC: Christine W. S. Chu, The Law Society of Hong Kong

FROM: John Morgans, Baker & McKenzie

E-MAIL: john.morgans@bakernet.com **DIRECT DIAL:** (852) 2846 1737

DATE: 31 January 2000

RE: s. 12 Conveyancing and Property Ordinance & s. 49 (2) Law of Property Act

Executive Summary and Recommendation

This memorandum has set out the positions in Hong Kong, where there is no equivalent to s. 49 (2) of the LPA, and in England and Australia where such provisions exist to provide purchasers in default with a means of relief from forfeiture of their deposits. Factors have been considered both for and against the existing law.

Reasons to change the law are as follows:

1. In cases where the law is ambivalent, the purchaser is unable to decide whether to accept the vendors' title. An innocent refusal to complete based on the law may result in the loss of a deposit in the event that the courts decide against the purchaser.

2. At times, the conditions of sale, if interpreted rigidly, can cause an unfair result to a purchaser who is forced to accept an interest which is different than what he reasonably thought he was contracting for.

3. Often, independent third parties, or factors beyond the control of the purchaser are to blame for failure to complete. In such a circumstance it is unjust to deny the purchaser a remedy.

4. The existing equitable jurisdiction to grant relief from forfeiture is inadequate to meet the requirements of creating a fair and equitable conveyancing system.

Reasons not to change the law are as follows:

1. Giving such a discretion to the courts may encourage a floodgate of litigation.

2. Changes to the law as proposed diminishes the sanctity of the contract.

3. Changes to the law may result in the laws becoming uncertain and unpredictable.

4. The UK provisions do not bar a vendor from seeking damages after relief is given to the purchaser through return of the deposit.

In conclusion, it is strikingly odd that Hong Kong is one of the few jurisdictions with a common law system in which there is no equivalent of s. 49 (2) of the LPA. Moreover, there do not seem to be a plethora of cases in the other jurisdictions in which this cause of action has arisen. Given the complexity of modern conveyancing transactions, and the complexities of the laws which govern them, the law does not always provide definitive answers to certain problems. Granting the courts a certain degree of flexibility in dealing with vendor-purchaser summons is generally a good thing which is to be encouraged. Also, there are many situations in which the absence of s. 49 (2) of the LPA could produce a grossly unfair result. Reform would be a positive step and the Australian system sets a good model as it is more detailed in its provisions which place restrictions on the relief. Moreover, the Australian authorities which extend the discretion of the courts, even in situations where the parties have contracted that time is to be of the essence, are positive developments as they are based on the principle that unconscionable conduct should provide a basis to allow the courts to over-ride strict contractual provisions. The Australian model should be studied in greater detail with possible reforms in Hong Kong along similar lines.

Introduction

This memorandum seeks to address a criticism of the existing state of s. 12 of the Conveyancing and Property Ordinance (the "CPO") which has been voiced by Godfrey JA on two separate occasions during the course of his judgments. The criticism is essentially this, whereas s. 49 (2) of the English Law of Property Act (the "LPA") contains the following provision:

> Where the court refuses to grant specific performance of a contract, or in any action for the return of a deposit, the court may, if it thinks fit, order the repayment of the deposit;

the Hong Kong equivalent of s. 49 of the LPA, s. 12 of the CPO, contains no such provision. S. 49 (2) of the LPA has the effect of giving the court the discretion to order the vendor to return the purchaser's deposit in a situation where the vendor is not in breach of the contract. This discretion has been exercised in a wide variety of cases where it is the purchaser that is in breach of the contract for the sale of any interest in land.

In this memorandum, the position in Hong Kong will be analyzed through consideration of the cases prior to, and in which it has been proposed that s. 12 of the CPO be amended to bring it in line with its English equivalent. This will have the effect of demonstrating the problems which arise in a system where the courts have no discretion similar to that granted

by virtue of s. 49 (2) of the LPA. The limitations of the existing equitable jurisdiction of the courts to grant relief from forfeiture will also be examined to determine whether it is a sufficient discretion to alleviate against the types of injustices which may arise in vendor-purchaser disputes. Focus will then be shifted to the various range of situations in which the English courts have applied s. 49 (2), so as to consider whether such situations are relevant in the context of Hong Kong. Various criticisms of s. 49 (2) will also be considered so as to demonstrate that in the event that the legislation in Hong were to be changed, it would not be without its own problems. Finally, some mention will be made of s. 55 (1) of the New South Wales Conveyancing Act 1919, a provision which deals with the purchaser's right to recover his deposit and which differs from the English s. 49 (2) in material respects.

(1) The Position in Hong Kong and the Existing Equitable Remedy of Relief from Forfeiture

Ng Check-kok v. Kiu Wai-ming [1992] 1 HKLR 5

At the outset, a clear distinction needs to be made between the equitable remedy of relief from forfeiture, which has been available from the earliest of times and which is not confined to a select number of categories, and a statutory action for the return of a deposit by the purchaser in a situation where it is the purchaser that is at fault, such as an action under s. 49 (2) of the LPA. In the former case, relief is granted on the grounds that it is the vendor who is in some way at fault. In the latter situation, the vendor is perfectly within his strict legal rights and yet the purchaser seeks the return of his deposit in a situation where he himself is in breach. This distinction was pointed out in the early case of Ng Check-kok v. Kiu Wai-ming, by Clough J:

> Where however a vendor exercises a right to forfeit a deposit (which is an earnest of the performance of the contract by the purchaser) upon the default of a purchaser the forfeiture is not a penalty and its retention had been said to be liquidated damages....We know of no case reported or unreported in the English courts where a normal deposit in a conveyancing transaction has been the subject of relief from forfeiture by a vendor (as distinct from recovery under s. 49 (2) of the LPA 1925) and it seems to us to be a most unlikely occurrence...

The inherent jurisdiction of a court of equity to grant relief against forfeiture arises where the vendor, having some legal right, avails himself of such a right for the purposes of fraud, oppression, harsh or vindictive injury. The general nature of the court's jurisdiction in this area was reviewed by Lord Wilberforce in Shiloh Spinners Ltd. v Harding [1973] AC 691, where he stated that the grounds for equity's intervention included areas where there was fraud, accident, mistake or surprise. If the purchaser then, is able to bring himself within the parameters of this general jurisdiction of the courts, he will be able to sustain an action against the vendor for relief from forfeiture, without the need for recourse to such statutory provisions as s. 49 (2) of the LPA. This general equitable jurisdiction of the courts has always been available in Hong Kong and may perhaps represent one of the reasons why the CPO does not contain a provision similar to s. 49 (2) in the LPA, since it was believed that

the equitable jurisdiction of the courts was generally available in cases where the vendor had acted unconscionably in forfeiting the purchaser's equitable interest in the land. Despite the existence of this general equitable discretion, it will be seen from what follows that there are a wide variety of situations in which a purchaser defaults, through no fault of his own, and cannot avail himself of the equitable relief from forfeiture owing to the fact that the vendor is squarely within the ambits of his legal rights.

In Ng Check-kok v Kiu Wai-ming it was further noted that the courts have tended to grant relief from forfeiture clauses (regarded as creating penalties which it would be unconscionable to retain) in cases where a purchaser has contracted to purchase land by installments under an agreement making time of the essence and the vendor has rescinded the contract and forfeited one or more earlier installment payments upon default by the purchaser in respect of a subsequent payment of an installment. One clear example of this was the case of Zeta Estates Ltd. v. Li Mang-Wah and Another [1979] HKLR 501 where the vendor attempted to rely on a forfeiture clause giving the vendor the right to forfeit all monies paid by the purchaser (ie being one initial deposit and part payments by installment for the balance over the course of 20 years) in the event of the purchaser's failing to pay to the vendor the purchase price and interest reserved at the place and time and in manner provided in the agreement. This was held to be a penalty clause and therefore the court had an equitable discretion to grant relief from forfeiture to the purchaser.

To sum up, the equitable jurisdiction of the courts seems to be limited to those cases where there is unconscionable conduct on the part of the vendor, or if the forfeiture clause is construed as a penalty, in which case it will be struck down by the courts. Nevertheless, the mere finding that a forfeiture clause is in the form of a penalty will not be sufficient to lead a court to find in favour of the purchaser. This point is plainly evident from the next case to be considered in which Godfrey J., (as he then was), first alluded to the benefit to be derived from incorporating the equivalent of s. 49 (2) of the LPA into the Hong Kong CPO.

Gladflow Limited v Grandland Development Limited [1993] 2 HKLR 494

The case of Gladflow Limited v Grandland Development Limited was a very significant case in the development of the law relating to the court's discretion in granting the purchaser relief from forfeiture in cases where it was the plaintiff who was in breach of the contract. In this case, the purchaser (the "Plaintiff") entered into an agreement to purchase a property from the vendor ("Vendor"). The agreement provided for the payment of two initial deposits, representing 10% of the purchase price, on or before the signing of the agreement, a further sum on a specified date prior to completion, and the balance on completion. Although the Plaintiff paid the two initial deposits being 10% of the purchase price, she failed to pay the further sum on the date specified prior to completion. The Defendant exercised its right to determine the agreement and forfeit the deposit. The Plaintiff sought specific performance of the agreement and a refund of the deposit. Godfrey J. stated that in light of the Plaintiff's breach of contract in failing to make a payment on the date stipulated, the availability of specific performance would depend on whether the court would relieve the Plaintiff from the forfeiture of its interest.

The issue of whether relief from forfeiture was available depended, as noted above, on whether the forfeiture clause in the agreement could be regarded as a penal provision, in which case the courts would have a well established discretion to grant relief from forfeiture.

Notwithstanding the use of the words "unliquidated damages" in the forfeiture clause, on its true construction it was held to be a penal provision which would, prima facie, give rise to the right to relief. The court decided, however, that the mere *availability* of the relief was not decisive to the question of *whether* that relief should be granted. Because the agreement provided that time was to be of the essence, the decision of the Privy Council in Steedman V. Drinkle [1916] AC 275 , which clearly established the principle that the right to relief (specific performance) would not be available in cases where there was an express time stipulation in the agreement between the parties, was applied leading the court to decline from granting an order for specific performance. Moreover, the court held that the payment of a mere 10% of the purchase price could not be considered as a penalty giving rise to the right to forfeiture (ie although, as noted above, it was held that the provisions in the forfeiture clause for "forfeiture of all installments of purchase monies already paid"- did amount to a penal provision), and thus no relief along such lines was allowed.

The decisive factors in this case was the principle from Steedman V. Drinkle that the courts would not allow specific performance where the parties had expressly agreed that time was to be of the essence and that a deposit of 10% in the context of the sale and purchase of an interest in land is a liquidated sum, able to be forfeited on the purchaser's default, a principle derived from the Privy Council's decision in Linggi Plantations Ltd. v. Jhgatheesan [1972] 1 MLJ 89. From this it follows that a purchaser would be hard pressed to argue that a deposit of 10% of the purchase price was a penal provision entitling him to relief against forfeiture, and equally beyond the aid of the courts if the contract provided that time was to be of the essence. These twin Privy council cases demonstrate the limitations of equitable relief, as it exists in Hong Kong, as such relief is to give way to the principles of the sanctity of the contract between the parties and sanctity of the 10% deposit in conveyancing transactions.

In the face of these two obstacles to equitable relief, Godfrey J. noted that an alternate mode of relief might have been available to the defaulting Plaintiff if there were a Hong Kong equivalent to s. 49 (2) of the LPA by which jurisdiction is conferred on the court in England and Wales to order, if it thinks fit, the return of the purchaser's deposit in any action brought, unsuccessfully, by the purchaser for specific performance. This avenue was closed and thus this case demonstrates a common situation in which relief against forfeiture is insufficient to do justice between the parties. It seems unfair that a purchaser, ready and willing to make payment just 20 days after the payment due date, as in the Gladflow Limited case, should be denied equitable relief in any form. This case was the first harbinger of the need for reform in Hong Kong. The present system ties the hands of the courts and leads to the vendor obtaining a windfall for a minor breach on the part of the purchaser.

Nevertheless, before leaving the case, it is necessary to note Godfrey's comments on the controversial decisions of the High Court of Australia in Legione v. Hately (1983) 152 CLR 406 and Stern v. McArthur (1988) 165 CLR 489, at the end of the Gladflow Limited case. In Legione, the majority held that the court had jurisdiction to grant relief to a defaulting purchaser against the forfeiture of his interest in the land, and go on to make an order for specific performance, even though he had failed to comply with a condition whereby time was of the essence. In goes without saying, that this decision flies in the face of the authority of the Privy Council decision in Steedman. The basis of this jurisdiction, and the condition precedent to the courts invoking it, was relief against the unconscionable conduct [of the vendor], even in a situation where the purchaser was at fault for failure to honor the strict contractual provisions. The following principles were set out as criterion in the determination

of whether unconscionable conduct had been established:

(1) Did the conduct of the vendor contribute to the purchaser's breach?
(2) Was the purchaser's breach (a) trivial or slight, and (b) inadvertent and non willful?
(3) What damage or other adverse consequences did the vendor suffer by reason of the purchaser's breach?
(4) What is the magnitude of the purchaser's loss and the vendor's gain if the forfeiture is to stand?
(5) Is specific performance with or without compensation an adequate safeguard for the vendor?

The implication of this case is that there is room for the expansion of the court's equitable jurisdiction to grant relief against forfeiture, notwithstanding that the purchaser was in default as to a stipulation that time was to be of the essence, beyond the tried and tested route of demonstrating that the forfeiture clause is in essence a penal provision which can be struck down. Without amending the CPO, the courts of Hong Kong could follow the Australian lead in taking the five factors noted above into consideration in determining whether, despite the purchaser's breach of contract, the vendor had been guilty of some unconscionable conduct. However, in all fairness it should be noted that such expanded jurisdiction would still not have helped the Plaintiff in the Gladflow case since the vendor's conduct did not fall to such a level as to establish the jurisdictional basis of the relief. Moreover, as the final two Hong Kong cases to be discussed will illustrate, unfair results can arise through no fault of either party when it is the law itself which is to be blamed for its inconsistency, leaving the purchaser without any equitable locus standi upon which to found a claim for relief. It is the next two cases which clearly demonstrate the inadequacy of the existing legislation in Hong Kong to meet unseen vicissitudes which can arise in a conveyancing transaction.

Ip Foo Keung Michael, Chan Ling Wen Elaine v. Chan Pak Kai (Civil Appeal No. 273 of 1999) (the "First Case")
Wu Wing Kuen v. Leung Kwai Lin Cindy (Civil Appeal No. 240 of 1999) (the "Second Case")

It is the outcome of the First Case which led Godfrey JA. to refer to the failure of the legislature in Hong Kong to incorporate a provision similar to s. 49 (2) of the LPA into the CPO as a "disgrace", in which his previous pleas for the incorporation of such a provision (ie as noted in the Gladflow case) had "fallen on deaf ears".

Both of these cases were appeals from the Court of First Instance in which the purchasers (the "Purchasers") sought, inter alia, the return of their deposits which had been forfeited by the vendors (the "Vendors"), when the Purchasers refused to complete the purchase of the various properties on the grounds that the Vendors had failed to show good title. Both cases centered on the issue of whether s. 13 of the CPO, on its proper construction, allowed vendors to introduce secondary evidence in the process of *showing* good title (ie there was clear authority that such secondary evidence would be permitted at the stage of *giving* or *proving* good title). If such secondary evidence was admissible, then the Purchasers were not entitled to rescind the agreements and should not be entitled to the return of their deposits.

The Court of Appeal decided that s. 13 of the CPO did not preclude the introduction of secondary evidence at the stage of *showing* good title to the property. The legislative intention behind s. 13 was not to make life more difficult for vendors, but simply to facilitate

conveyancing by reducing the length of time for which the vendor had to prove his title.

In the First Case, the Purchaser's appeal was dismissed since it was not in dispute that if secondary evidence was admissible, then the evidence provided had been sufficient. In the Second Case, the appeal was allowed on the grounds that the majority found that the evidence provided was not sufficient. What was common to both cases was the fact that given the state of the law on the matter, it was impossible to say with certainty which way the decision would go. There were no less than 12 authorities on the subject of whether secondary evidence was admissible under s. 13, six of which indicated that such evidence was admissible, while the other six were decided in the opposite way. Now given such a deadlock prior to the decision of the cases and a long trawl by the parties through the litigation process, it was impossible for the solicitors of the parties to offer definitive advice as to whether the Purchasers had a right to question the title of the Vendors. Some of the cases indicated that showing title based on secondary evidence was adequate while others decided that such a title was shaky. Under the circumstances, although the purchasers were in breach for failing to accept the evidence of title offered, the law worked against them in that it stood in the position of a deadlock or stalemate. This was no fault of the Purchasers nor could the Vendors be accused of unconscionable conduct. The law was, in a sense, to blame for the First Purchaser's loss of his deposit. The law was equally impotent to offer relief to the Purchaser in breach since there was no unconscionable conduct on the part of the vendor, the deposit was not a penal clause, nor was there any other room for equitable relief. S. 49 (2) of the LPA, as Godfrey JA. pointed out, would have offered an avenue for relief. These cases present a strong and cogent argument for legislative reform in Hong Kong.

(2) The English Authorities on s. 49 (2)

Charles Hunt Limited v. Palmer [1931] 2 Ch 287

Premises were sold at an auction and were sold subject to certain special conditions of sale, one of which provided that the leases of the premises might be examined at the office of the vendors' solicitors before the sale and that the purchaser, whether or not he inspected the same, should be deemed to have bought with notice of the contents thereof. The premises had been described in the sale as "valuable business premises". The purchaser (the defendant) was the highest bidder, paid a deposit and proceeded to sign the necessary documentation of sale, without inspecting the conditions in which the above stipulation was made. In the course of investigating title, it came to the defendant's knowledge that the premises were subject to restrictive covenants under which they could only be used for one particular trade. The defendants refused to complete the purchase and sued for return of the deposit. The vendors' action for specific performance failed and by virtue of their discretion under s. 49 (2) LPA, the court ordered that the defendant's deposit be returned. The reasons for the decision was that despite the special condition of sale, describing the premises as "valuable business premises" was a misleading misrepresentation since in fact the premises could only be used for one purpose.

This case demonstrates that in a situation where the parties have made a bargain to be bound by certain conditions, the court nevertheless has a discretion to interfere if it would be in the greater interests of justice to do so. In effect, the purchaser was bound by contract not to make any objection in respect of any matter contained in the original lease. The court argued

that although the purchaser had contracted to take a particular title, the result of granting specific performance would be forcing him to take something which he did not contract to buy. A court of equity would not enforce a contract against the purchaser which was different from that which he had entered into. Thus the court was not bound to refuse to order the return of the deposit even if the vendor was protected at law by the conditions of sale.

If this situation were to arise in Hong Kong, and such examples of misrepresentation are not uncommon, the court would have no discretion to order the return of the deposit given the strict contractual provisions. The most that a Hong Kong court could do would be to decline an order for specific performance. On the other hand, is it desirable to give the court a power to override the conditions of sale?

Universal Corporation v. Five Ways Properties [1979] 1 All E. R. 552

This was a landmark case on the proper interpretation of the court's discretion under s. 49 (2). Prior to this case, no suggestion had ever been made that the subsection could be invoked by a purchaser who had committed a repudiatory breach of contract, in order to recover his deposit from a wholly blameless vendor. In this case it was contended that the subsection conferred an unfettered jurisdiction on the courts to order the return of deposits. The purchaser was a Liberian corporation which had planned to finance the purchase of a property with funds from Nigeria. With a change in the relevant exchange control regulations of Nigeria, the necessary funds could not be remitted either by the completion date or by the time limit specified in a notice to complete. As a result, the purchaser was unable to complete on the completion date. Accordingly, the vendor proceeded to rescind the contract and forfeited the deposit while the purchaser sought recovery of the deposit under s. 49 (2). On appeal, the Court of Appeal held that the subsection could only be interpreted such that it did indeed confer an absolutely unfettered discretion to order the return of deposits. It was held that a purchaser can invoke the section even though he has committed a repudiatory breach of contract and has thus been entirely responsible for the rescission of the contract. The true construction of s. 49 (2) was that it was designed to do justice between the vendor and the purchaser. The discretion was to be exercised judicially and with regard to all of the relevant circumstances, including the terms of the contract.

The unique feature of this case is that it was essentially a no-fault case in which both the purchaser and the vendor had come with clean hands. The obstacle to completion had been as the result of factors beyond the control of both of the parties. The purchaser had no way of knowing that a sudden change in exchange control regulations from the country of purchase would hamper its ability to complete on the agreed date. If the situation had arisen in Hong Kong, an innocent purchaser would have been deprived of its deposit as there would have been no grounds upon which to do justice between the parties. Another striking feature of the case is its relevance to Hong Kong as an international finance center. It is not hard to imagine that in the sale and purchase of large commercial properties in Hong Kong involving syndicated loans and international financing arrangements, such a situation could easily arise in which the parties were adversely effected by events beyond their control. With the present state of the law in Hong Kong, the courts are handicapped from just intervention in such a situation to ensure a fair result to both parties concerned. This case presents a strong argument in favour of s. 49 (2) in that it clearly demonstrates the type of no-fault situations which the section was designed to circumvent.

Dimsdale Developments (South East) v. De Haan [1983] 47 P. & C. R. 1

In this case, the purchasers, having paid a deposit of about 10 %, failed to complete the contract on time and also failed to comply with what was held to be a valid notice to complete. The vendors rescinded the contract and resold the property for about 15% more than the contract price with the original purchasers, having suffered losses of about half the amount of the deposit by way of costs, fees and bank interest. Having failed in their contention that the notice to complete was invalid, the purchasers sought the recovery of their deposit. The judge, who happened to be Gerald Godfrey Q. C sitting as deputy High Court Judge, held that although this was an appropriate case for exercise of the discretion under s. 49 (2), there was no reason why the purchasers should not pay damages to the vendor for losses occasioned by the purchasers' breach of contract. He ordered the return of the deposit to the purchasers on the condition that they either submit to a deduction from the deposit to cover the vendors' losses, or an inquiry as to damages in that regard. This case established beyond all doubt that despite the fact that the purchaser has committed a repudiatory breach of contract and has therefore been entirely responsible for the vendor's rescission of the contract, he may nevertheless seek recovery of his deposit under s. 49 (2) so as to prevent a vendor who has fully complied with all of hi contractual obligations from retaining any more of the deposit other than his provable damages for breach of contract.

Country and Metropolitan Homes Surrey Ltd v. Topclaim Ltd. [1997] 1 All ER

This case need only be mentioned in the context of the situation where the parties attempt, in the contract, to expressly exclude s. 49 (2) LPA from the contract. In this case, it was the vendor who was at default when he attempted to rescind the contract for the purchaser's failure to complete. For this reason, despite the express exclusion of s. 49 under the terms of the contract, this did not alter the ordinary position at law, namely that the fate of the deposit, in a situation where the contract is not completed, depends on which party is to blame for not completing the contract. For this reason, the vendor could not rely on the express exclusion of s. 49 to prevent the purchaser from reclaiming his deposit.

The result of these three English authorities seem to suggest that they do have scope for operation in Hong Kong and that the circumstances in which they were decided are not far removed from the type of situations which might arise in Hong Kong. This is particularly true of the Hunt case and the Universal Corporation case which clearly demonstrate situations where other intervening factors render an unsatisfactory result if court is left without the necessary discretion to step in and do justice.

(3) Criticisms of s. 49 (2) LPA

s. 49 (2) LPA is not, however, without problems of its own. Essentially the problems which it introduces are fourfold.

(1) If purchasers are assured that they have a fallback provision which gives the court an unfettered discretion to order the return of the deposit, even if they are at fault, this may encourage litigation and create a situation in which defaulting purchasers abuse the provisions of s. 12 of the CPO as a last attempt to win back their deposit. Excessive litigation has never been encouraged by the courts and the judiciary in

Hong Kong has often criticized the abuse of the vendor-purchaser summons. Given the fact that the discretion is so wide, it might cause solicitors acting for purchasers to take risks which they would not attempt under the present regime with the knowledge that they have a fallback position.

Another negative consequence which may follow from the tendency to encourage parties to litigate is that the enactment of a similar provision in Hong Kong would have the effect of undermining the sanctity of the 10% deposit in conveyancing transactions. As Lord Macnaghten pointed out in Soper v. Arnold (1889) 14 App Cas 429 (HL) :

> "Everybody knows what a deposit is. The purchaser did not want legal advice to tell him that. The deposit serves two purposes- if the purchase is carried out it goes against the purchase money- but its primary purpose is this, it is a guarantee that the purchaser means business; and if there is a case in which a deposit is rightly forfeited it is, I think, when a man enters into a contract to buy real property without taking the trouble to consider whether he can pay for it or not."

But by allowing the courts such a wide discretion, it may have the effect of undermining the significance of the deposit as a guarantee that the purchaser means business. The effect of decisions such as Universal Corporation and Dimsdale Developments is to limit the vendor's right to forfeit the deposit to his provable claims for breach of contract, and thereby mitigating the power of the deposit to force the parties to take their arrangements seriously.

(2) Another negative result of s. 49 (2) of the LPA is that it has the effect of diminishing the sanctity of a contractual arrangement between the parties. This principle is clearly evident from the Hunt case in which the court overruled the express conditions of sale so as to enable a purchaser to claim back his deposit. If a purchaser contracts to buy whatever title the vendor is able to give, it seems only just that the courts should encourage parties to abide by the terms of their agreement without recourse to special discretionary powers designed to alleviate the hardship of the strict letter of the law. This principle of the sanctity of the contract was a strong factor in the Steedman case of the Privy Council in which the courts refused to exercise their discretion in light of the strict contractual provisions to the contrary that time was to be of the essence. Although the High court of Australia have declined to follow this precedent in the Legione case, it may be a preferable course of action to uphold the sanctity of the contract in Hong Kong which has, traditionally, been very much of a laissez faire society.

(3) A third negative result of s. 49 (2) is that it would introduce an element of uncertainty into conveyancing transactions. Under the present system, parties are relatively clear that it is the defaulting party which will lose the deposit in the event of a dispute. By allowing a greater discretion to the courts in this area, the parties would be left on less sturdy ground as to the extent of their rights and responsibilities. Because the categories of the discretion are never closed to a select number of situations, parties

would be unable to discern with certainty what type of decision a court, empowered with a huge discretion, might be inclined to make.

(4) Finally, one further weakness of this provision is that it does not bar the vendor's action against the purchaser for damages. The court is therefore unlikely in practice to order the return of the deposit except in a case where its value exceeds the vendor's claim for damages. This principle is evident from the Dimsdale Developments case in which the purchaser, although being allowing to reclaim his deposit, was nevertheless obliged to deduct the amount of the vendors' losses.

In this sense, the parallel provision in Australia is superior in the sense that it has taken this problem into consideration. The New South Wales Conveyancing Act 1919 s. 55(1) not only gives the purchaser the right to recover his deposit in a case in which specific performance is refused against him, but relieves him of any liability under the contract "whether at law or in equity". It is to the Australian equivalent of s. 49 (2) of the LPA to which we now turn.

(4) **The Position in Australia**

S. 55 of New South Wales Conveyancing Act 1919 is significantly different from its UK equivalent and deserves consideration for its novelty. The provision is in the following terms:

55 (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 deposit and any installments of purchase money he 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 expense of investigating the title.

(2A) In every case where the court refuses to grant specific performance of a contract, or in any proceeding for the return of a deposit, the court may, if it thinks fit, order the repayment of any deposit with or without interest thereon.

(3) On the application of the purchaser the court may order the payment under this section and declare and enforce a lien in respect thereof on the property the subject of the contract.

The rationale of s. 55 (1) was explained by Long Innes J in Bennett v Stuart (1927) 27 SR (NSW) 317:

"As I understand it, the object of the section was to enable a purchaser to recover his deposit in a case in which, though he had contracted to accept such a title as the vendor had, or had otherwise precluded himself from relying upon a defect in the vendor's title, the Court of

Equity would not by reason of a defect in the vendor's title have enforced specific performance of the contract against the purchaser. It consequently has no application to a case where the Court finds in fact that there is no defect in the vendor's title; nor, as it seems to me, to a case in which the Court of Equity would refuse to decree specific performance because the title was too doubtful."

In order for the purchaser to succeed on an action brought under s. 55 (1), the court must be satisfied that:

1. There is a defect in title; and
2. The contract does not disclose the defect or the contract does not contain a stipulation precluding the purchaser from objecting to the defect in title: and
3. The court would not enforce specific performance of the contract;
4. The purchaser is not entitled to rescind the contract (eg through a fundamental breach on the part of the vendor)

The advantage of this provision is that it strikes a balance between honouring the contract which the parties have agreed to while preventing a vendor from foisting a faulty title onto the purchaser. Also, as mentioned above, it relieves the purchaser from "all liability both at law and in equity" which precludes the vendor from claiming damages at common law.

S. 55 (2A) is, of course, identical to s. 49 (2) of the LPA. As noted above, this section has been liberally interpreted and it is not necessary for the court to find inequitable conduct on the part of the vendor. In exercising the discretion the court should look at whether in all the circumstances it is unjust and inequitable to permit the vendor to retain the deposit forfeited on termination. In Australia, the onus lies on the purchaser to show that it is just and inequitable to permit the vendor to retain the forfeited deposit on termination. One situation in which the section has been applied in Australia is where the purchaser is ready and willing to perform but has lost the opportunity due to the inadvertence of those he had properly employed to act for him. Unlike the position in Dimsdale Developments where the court limited the purchaser's right to reclaim the full deposit, in Australia, the section does not give the court an overall discretionary supervision of monetary adjustments between the parties to a contract under which a deposit had been paid but terminated.

Finally, in the recent Australian case of Gogard Pty Limited v. Satnaq Limited [1999] NSWSC 1283 (23 December 1999), relief under s. 55 (2A) was denied to a purchaser. The case sets out the various factors to be weighed in determining whether relief should be granted. They are as follows:

(1) The conduct of the parties, especially the applicant, the circumstances that brought about the termination and forfeiture, and the amounts at stake. The court considers matters connected with the contract as well as the conscionability of the conduct of the parties after the contracts are exchanged;
(2) Whether the purchaser took a risk in structuring its financial dealings in such a way that at the time when completion was to occur, the purchaser was unable to finance the purchase;

(3) Did the purchaser do everything in his power to complete with the fault lying with the solicitors of the purchaser;
(4) Would the purchaser have had a defence to an order for specific performance if an order requiring such were sought by the vendor;
(5) Was the deposit in the nature of a penalty; and
(6) Has the vendor resold the property to a third party for a higher price than that agreed between the vendor and the original purchaser: did the vendor seek, by the resale, to make a windfall profit at the expense of an innocent purchaser.

By taking such factor as these into consideration, the courts will ensure that justice is done between the parties and that neither party is enriched at the expense of the other.

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