



Hong Kong Institute of
Certified Public Accountants
香港會計師公會



Qualification Programme

Module 10

Business and Company Law

Pilot Examination Paper

Time Allowed	3 hours
Examination Assessment Allocation	
Written Questions	100 Marks All questions are compulsory

Do not open this question paper until instructed by the supervisor.

You should answer Written Questions in the Script Booklet. In the Script Booklet, you should start **EACH** question on a **NEW** page.

This question paper must not be removed from the examination centre.

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Module 10 – Business and Company Law

You should allocate approximately 3 hours in total for SEVEN compulsory written questions.

Suggested time allocation (by marks):

Marks	Approximate time in minutes
1	2
2	3
3	5
4	7
5	9
6	11
7	12
8	14
9	16
10	18
11	20
12	21
13	23
14	25
15	27
16	29
17	30
18	32
19	34
20	36

WRITTEN QUESTIONS (Total: 100 marks)

Answer **ALL** of the following questions. Marks are indicated at the end of each question. Together they are worth 100% of the total marks for this examination.

Question 1 (40 marks – approximately 72 minutes)

Thomas had been working as the managing director in Yellow River Ltd for almost ten years. He resigned from Yellow River Ltd three weeks ago, and then immediately formed a new company named Golden Cow Ltd with Carmen and Kate. The parties were close friends where they had known each other for more than ten years. Their respective shareholdings in Golden Cow Ltd are: Thomas (40%), Carmen (30%) and Kate (30%). They executed a shareholders' agreement. It stated that all of them shall be appointed as directors and also actively participate in the company's management. Both Yellow River Ltd and Golden Cow Ltd are property developers.

The employment contract of Thomas in Yellow River Ltd included a restrictive provision which prohibited him from engaging in the same business and soliciting the clients from Yellow River Ltd within one year after his employment with Yellow River Ltd. Thomas believed that his previous connections and reputation in the industry would be helpful in his new business. Therefore, Thomas asked his secretary, Angela, in Golden Cow Ltd to contact his old clients concerning his new business. Thomas later on received a call from John, his very wealthy old client. John said that he was very interested to sign a new contract with Golden Cow Ltd. Thomas agreed and he reminded John that the contract would be executed by his newly formed company but not himself, so it would not violate the restriction imposed on him from his previous employment.

There is an objects clause in the articles of Golden Cow Ltd stating that the company shall only engage in the business of property development. Thomas has been recently negotiating a joint venture contract on behalf of the company with Silver Hill Ltd to develop a new type of smart phone. Thomas believes that it can help diversify the business of the company.

Kate opposed the joint venture contract but the proposal was supported by Carmen. Thomas and Carmen thought that Kate would become a hurdle in the company. Therefore, Thomas and Carmen convened a general meeting and removed Kate from her directorship. Thomas and Carmen also raised the directors' remuneration and ceased the payment of dividends to shareholders.

Thomas so far only received a single call from John but no others. Thomas thought that it may be owing to the laziness of Angela in helping him to contact his old clients. Thomas therefore terminated the employment of Angela summarily without payment in lieu of notice.

Required:

- (a) Analyse whether Thomas was in breach of the restrictive provision of the employment contract with Yellow River Ltd. (You can assume that the restrictive provision itself is valid.) (10 marks)
- (b) (i) Analyse whether the joint venture contract would be void. (7 marks)
- (ii) Analyse what kind of legal action would be available to Kate in relation to the contract under the Companies Ordinance (Cap.622). (3 marks)
- (c) Analyse the appropriate legal actions available to Kate in protecting her interest as a minority shareholder. (15 marks)
- (d) Analyse whether the termination of Angela's employment contract was lawful. (5 marks)

Question 2 (10 marks – approximately 18 minutes)

- a) Louisa wanted to sue Carrie for breach of contract and the case will be pending for trial in the Court of First Instance. The solicitor of Louisa handed her two cases for reference. The first case is from the Court of First Instance, and the second case is from the Court of Appeal. Both cases have similar facts and legal issues as the case of Louisa. However, Louisa is wondering whether both cases are equally applicable to her upcoming trial.
- b) Richard is a businessman from England and he wanted to sue a company in Hong Kong. Richard learned that a recent judgment from the House of Lords will be very helpful to his claim, but he is not sure whether a decision from England can be applicable in the courts of Hong Kong.
- c) Ivan is a social worker. Ivan recently helped his client in a family case before the Court of Appeal. Ivan noticed that the judge made several suggestions on the administrative matters in the judgment. Ivan felt that the suggestions from the judge were very useful but he was not certain whether these suggestions would be binding on the other courts as well.

Required:

Analyse the legal principles behind the following cases:

- (a) Louisa. **(6 marks)**
- (b) Richard. **(2 marks)**
- (c) Ivan. **(2 marks)**

Question 3 (15 marks – approximately 27 minutes)

Chris has a sausage factory in Yuen Long. The sausage factory routinely uses the water from a nearby river in its production process. Super Tech Ltd is a chemical factory located at the upper section of the same river. Last month, an explosion occurred in Super Tech Ltd which damaged its pipes and caused a leakage of waste water. The problem was fixed hours later but almost three tons of chemical substances were flushed into the river. Two days after the explosion, Chris found that all the sausages in his factory were polluted by certain chemical substances and no longer consumable. Chris was forced to abandon all the remaining sausages which cost him over HK\$1 million. Since Super Tech Ltd is the only factory located on the upper stream of the river, it is very likely that the chemical substances were from Super Tech Ltd. Chris decided to sue Super Tech Ltd for compensation.

Required:

Analyse whether Chris can file a claim against Super Tech Ltd for compensation. (You can ignore any statutory liability concerning water pollution or nuisance.)

(15 marks)

Question 4 (15 marks – approximately 27 minutes)

- a) Orange Ltd is a computer software company. The company recently posted a statement in the newspaper and vowed that their newly invented anti-virus programme can 100% protect the operation system from all kinds of computer viruses. The company guaranteed anyone who installed their programme but is still being infected with a computer virus can claim HK\$1,000 as compensation from them. In order to show their seriousness, the company already deposited HK\$1,000 in its own bank account for possible payment. Richard used the anti-virus programme but his operation system was seriously infected. Richard wanted to claim the money from Orange Ltd but the company told Richard that the statement was an advertisement only.
- b) Elsie wanted to buy a piano from Anna. The parties subsequently agreed on the terms and signed a sales contract at the purchase price of HK\$10,000 on 15 June 2019. The contract provides, *inter alia*, that the seller shall retain the ownership until the buyer fully settled the payment not later than 30 June 2019. The piano was delivered to Elsie immediately after the conclusion of the contract. However, Elsie failed to settle the payment on time. Anna was really upset and thought that she still retained the ownership of the piano.

Required:

- (a) Analyse whether Richard has any legal ground to file a claim against Orange Ltd.**

(10 marks)

- (b) Analyse whether the ownership of the piano has been transferred to Elsie.**

(5 marks)

Question 5 (10 marks – approximately 18 minutes)

- a) Mary works as a branch manager in Kowloon Bank and Robert is her superior. Yesterday, Robert asked Mary to help him deposit HK\$5 million of cash into his own account. Robert told Mary that the money would be used for some future transactions in one of his clients whose identity was not to be disclosed. Robert refused to disclose any further information concerning the client or the money and he asked Mary to just follow his instructions. Mary had been working as a branch manager for ten years. Mary knew very well the banking procedures but she had never seen such a huge cash transaction sum. Despite all her queries, Mary followed the instructions of Robert without making any query.
- b) William is a fresh graduate from a lower class family. William is presently working as a liaison officer in the Department of Justice. William's monthly salary is HK\$20,000. William owns two diamond Swiss watches and a top model BMW. William has also recently rented a top services apartment in Central which cost him a monthly rental payment of HK\$25,000. William's supervisor reported him to the Independent Commission Against Corruption, but William thinks that he has done nothing wrong by having a living style better than the average person.

Required:

- (a) Analyse the possibility that Mary may have committed any offences under the Organized and Serious Crimes Ordinance (Cap.455). (5 marks)
- (b) Analyse the possibility that William may have committed any offences under the Prevention of Bribery Ordinance (Cap.201). (5 marks)

Question 6 (5 marks – approximately 9 minutes)

Big Rock Ltd is a Hong Kong public company and its main business is property development. The company has been involved in several business projects and is now in urgent need of funds. In a recent board meeting, one of its directors, Michael, proposed to the board that the company should offer debentures to the public for fund raising. Michael's understanding is that raising funds by offering shares to the public will trigger the legal requirements in preparing the prospectus and the disclosure of various financial information. Michael thought that all of these requirements are not relevant in the issuance of debentures.

Required:

Analyse whether the issuance of debentures will trigger the legal requirements in preparing a prospectus, and if so, what will be the required contents. (5 marks)

Question 7 (5 marks – approximately 9 minutes)

Bobby, Candy and Danny are the only shareholders and directors of Quick Profit Ltd. The articles of the company state that the managing director can act on behalf of the company to sign a contract up to the limit of HK\$200,000. Prior approval from the board is a must if a contract beyond the stated sum needs to be executed.

Bobby learned that Danny had represented himself as the managing director (without formal appointment) and concluded a contract on behalf of the company which involved the sum of HK\$300,000. Bobby knew that the board had never approved such a contract. Bobby thought that Danny was not properly authorised by the board and thus the contract shall not be binding on the company.

Required:

Analyse whether the contract signed by Danny is binding on the company.

(5 marks)

* * * END OF EXAMINATION PAPER * * *

Module 10

Business and Company Law

Answers

The suggested answers are longer than what candidates are expected to give in the examination. The purpose of the suggested answers is meant to help candidates in their revision and learning. The suggested answers may not contain all the correct points and candidates should note that credit will be awarded for valid answers which may not fully covered in the suggested answers.

WRITTEN QUESTIONS (Total: 100 marks)

Unless otherwise stated, all references to statutory provisions herein are made to the Companies Ordinance (Cap.622).

Answer 1(a)

A company is a separate legal entity. This means that a company is a different entity altogether from its shareholders and directors.

This principle was firmly established in the case "*Salomon v Salomon [1897]*". In this case, Mr Salomon at first operated a shoe business as a sole proprietor. Later on, Mr Salomon sold his business to a company incorporated by himself and his family members. The business subsequently declined and the company went into liquidation. Most of the creditors received nothing in the liquidation. The creditors sought to set aside the transfer of business from Salomon to the company, and maintained that the business still belonged to Salomon and so did the debts. The court ruled that the company is in law a different person, even after incorporation the business is precisely the same as it was before, the company is not in law the agent of its owner but a separate legal person in entirety.

Based on the principle of *Salomon v Salomon*, Thomas and Golden Cow Ltd are two separate legal entities. That said, the restrictive provision in the employment contract of Thomas shall not be applicable to Golden Cow Ltd regardless of their relationship. In addition, Thomas also reminded John that the contract with John would be executed by Golden Cow Ltd but not Thomas. *Prima facie*, Thomas was not in breach of the restrictive provision.

The concept of separate legal entity can be rebutted. The general principle is that the corporate veil can be pierced if there are any special circumstances indicating that the company (the corporate form) is a mere façade concealing the true facts behind (*Toptrans Ltd v Delta Resources Co Inc [2005] 1 HKLRD 635*); or there are impropriety or improper motive in the use of corporate form (*Winland Enterprises Group Inc v Wex Pharmaceuticals Inc [2012] 2 HKLRD 757*).

A notable example is for a party to use the corporate vehicle to evade an existing legal obligation. In *Gilford Motor Co v Horne [1933] 1 Ch 935*, the defendant was previously employed by the plaintiff as a managing director in selling motor vehicles. There was a restrictive covenant in his employment contract which prohibited him from working in the same business in certain places over a specific period of time. The defendant resigned later and set up his own company to engage in the motor vehicle business through his wife and friends. The court held that the company was established because of the defendant's fear that he might otherwise breach the restrictive covenant if he carried on the business by himself. The court further stated that the company was formed as a device in order to mask the effective carrying of the business of the defendant. The purpose was to enable the defendant under a sham to engage in business which might be intervened by the plaintiff. The court finally granted an injunction to both the defendant and his company not to act in breach of the restrictive covenant.

In our case, Thomas was under a restrictive covenant of Yellow River Ltd not to work in the same business nor to solicit the clients within one year after his employment with Yellow River Ltd. Thomas had committed a breach of the covenant by setting up a new corporate vehicle and tried to conclude a contract from his old client (John). Based on the principles from the Gilford Motor case, the corporate veil (Golden Cow Ltd) shall be pierced by the court, and Thomas and his company may still be liable for breaching the restrictive covenant.

Answer 1(b)(i)

Under the traditional common law principle, the capacity of a company is limited and restricted by the objects clause in its articles if any. Under the "*Ultra Vires Rule*", an act done by the company beyond its objects clause shall be void. The act cannot be ratified by the members of the company even with unanimous consent, this means that the company shall be incapable of performing an *ultra vires* act at all.

In *Ashbury Railway Carriage & Iron Co Ltd v Riche [1875] LR 7 HL 653*, the articles of the company said that its objects were "to make and sell, or lend on hire, railway carriages.". The company at first agreed to give Riche a loan (which is beyond the stated object of the company), but later on refused. Riche sued for execution of the loan and the company pleaded the defence of *ultra vires*. The court held that the company was pursuing an act beyond its object and would become *ultra vires*. It was further stated that an *ultra vires* was clearly against the written law and shall not be ratified even by the unanimous consent of the whole corporation.

In accordance with s.115(1), an objects clause is no longer compulsory. A company has the capacity, rights, powers and privilege of a natural person of full age. Nevertheless, a company can still have an objects clause, and the general principle is that if a company does have an objects clause, then the company shall not do anything against it (ss.116(1) and (2)). However, what really matters is that an act shall not become invalid only because the act violated its objects clause (s.116(5)). Preliminary speaking, the joint venture contract is not necessarily invalid merely because it may violate the stated objects clause.

An *ultra vires* act may become invalid if the outsider has actual knowledge of the objects clause. S.120 states that a person is not to be regarded as having notice merely because the matter is disclosed in the articles and being public. It basically abolished the common law concept of constructive notice. Therefore, in order to argue that the joint venture contract is void on the ground of *ultra vires*, it must be proven that Silver Hill Ltd has actual knowledge that the development of the smart phones is against the company's stated objective.

Besides that, s.117 also states that if a person is dealing with a company in good faith, then the power of the company's directors to bind the company is to be regarded as free of any limitation under the articles of the company.

Answer 1(b)(ii)

Under s.116(3), any dissenting members of the company have the power to restrain the directors to act against the stated objects clause by bringing a proceeding in court. Yet, it does not include an act which had already been executed or accomplished (s.116(4)). Therefore, if Silver Hill Ltd had no actual knowledge concerning the objects clause of Golden Cow Ltd, then the only option available to Kate shall be to initiate a court action against Thomas for his doing of an act in contravention of s.116(1) before the execution of the joint venture contract.

Answer 1(c)

Kate may bring a court proceeding against Thomas and Carmen on the ground of "unfair prejudice". The governing law is stated in Division 2 of Part 14 (ss.723 to 727). Under s.724(1), a member of a company may apply to the court for remedies under unfair prejudice where: (1) the company's affairs are conducted in a manner unfairly prejudicial to the interests of the members generally or of one or more members; or (2) an actual or proposed act or omission of the company is or would be so prejudicial.

Kate has been removed from her directorship, but it should have no impact as to her legal capacity to institute the proceeding as a current member. A petitioner can only make a successful application of unfair prejudice if he or she can prove the relevant conduct in issues are both "unfair" and "prejudicial". It is a two fold approach, it means both elements must be proved.

Prejudicial – It was explained in *Re Taiwa Land Investment Co Ltd [1981] HKLR 297* as meaning of "injury, detriment or damage" to the financial interests of the member or anything that may negatively affect their other interests in their capacity as members. It may include the diminishing of shares value (*Nicholas v Soundcraft Ltd [1993] BCLC 360*) or infringement of their rights under laws or articles.

Unfair – The court held that unfair means "not fair or unjust" (*Taiwa Land Investment Co Ltd*). The court shall apply the concept of "unfair" judicially and in accordance with the rational principles (*Wong Man Yin v Ricacorp Properties Ltd [2003] 6 HKCFAR 265*) and in its commercial context (*O'Neil v Phillips [1999] 1 WLR 1092*). It usually refers to the situation where there are some breaches of the terms agreed upon on how the affairs of the company shall be conducted, or having disputes in using the rules in a manner contrary to good faith or equity.

In order to determine whether Kate can apply for reliefs on the ground of "unfair prejudice". The following must be satisfied. Firstly, it is necessary to identify any possible prejudicial acts by Thomas and Carmen. This means whether the financial interests or rights of Kate have been infringed. Secondly, it is essential to see whether there is anything unfair between the parties. That is whether there are any breaches of understanding or agreement on the administration of the company. Thomas and Carmen raised the remuneration of the directors and ceased the payment of dividends to shareholders. Kate as a sole member without directorship is actually excluded from sharing any profit of the company. Besides that, Thomas and Carmen hold over 50% of the shares and can remove Kate from her directorship in the general meeting in accordance with the Companies Ordinance, it still breached the terms as agreed in the shareholders' agreement as well as the mutual understanding between the parties to manage the company together as a quasi-partnership. By considering the situation as a whole, Kate has suffered financially and also by being excluded from the management. The allegation of unfair prejudice is able to be established.

S.725(1) states that the court may "make any order that it thinks fit for giving relief". This means the court has wide discretion to do what it considers to be fair and equitable thus to put right and cure (*Re Bird Precision Bellows [1986] Ch 658, 669*). S.725(2) lists out certain orders that can be granted by the court:

- a) to require the company to do or refrain from doing certain things;
- b) to order proceedings to be brought in the company's name;
- c) to appoint receiver or manager;
- d) to regulate the conduct of the company's affairs;
- e) to purchase shares; and
- f) to award damages and interest.

Amongst all the remedies available, the most commonly sought one is the "buy out order". It is an order for the purchase by the majority of the minority's shares at a fair price (s.725(2)(a)(iv)). This order is particularly suitable if mutual trust no longer exists between the parties and there are impracticalities to further the company's affairs (*Re Dalkeith Investments Pty Ltd [1984] 9 ACLR 247*).

The "buy out order" can be made against any member or even the company itself. Its application is not limited to buying out by the majority, and it is possible to order the minority to buy the majority's shares. It is very rare to have such an order, and it will usually be a buy out of the minority's shares as it allows the minority to realise their investment and to have a clean break with the parties who are in control but unable to co-operate together. The court will take into account whether there is bad faith or impropriety on the part of the majority and then decide the suitability in granting the buy out order.

Alternatively, Kate may also consider winding up the company on the ground of "just and equitable" in accordance with s.177(1)(f) of the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap.32) ("CWUMPO").

This is a statutory provision but its principles are largely derived from equity. One of the well accepted grounds for application is quasi-partnership. In *Ebrahimi v Westbourne Galleries Ltd [1973] AC 360*, the court held that considerations in granting the winding-up order may arise if the company is formed on the basis of personal relationship and mutual trust, and at the same time there is an agreement or understanding that all members shall participate in the administration of the company have been breached.

It is a drastic action to wind up a company and the winding-up order shall only be granted at the last resort. S.180(1A) of the CWUMPO also stipulated that the winding-up order shall be denied if the respondents can demonstrate an alternative remedy and the unreasonableness on the part of the petitioner to pursue for a winding-up order.

Answer 1(d)

An employee may be summarily dismissed without notice or wage in lieu of notice if he or she breaches the contract fundamentally. S.9 of the Employment Ordinance (Cap.57) sets out the following grounds for summary dismissal:

- The employee wilfully disobeys a lawful and reasonable order;
- The employee misconducts himself or herself, such conduct being inconsistent with the due and faithful discharge of his or her duties;
- The employee is guilty of fraud or dishonesty; or
- The employee is habitually neglectful in his or her duties.

There is no universal standard in deciding the meaning of disobedience, neglect and the degree of misconduct which will justify summary dismissal. It depends on the nature of the business and the facts. The general rule is that if the employee does anything which is seriously incompatible with the due or faithful discharge of his or her duty then he or she may be dismissed summarily without notice. The court usually considers that summary dismissal is a very serious measure and will not easily allow it.

In our case, Thomas alleged that Angela was only lazy, so it was neither related to fraud nor disobedience. Thomas therefore must prove that Angela was in serious misconduct or habitually neglectful in her duties to justify the summary dismissal. If Angela was only being "lazy" in relation to a single event, then it may not be sufficient to dismiss her summarily.

Answer 2(a)

The doctrine of judicial precedent is the cornerstone of the common law system. It means judges shall decide cases in accordance with the decisions handed down by the court in previous cases if the same or similar issue arises. The doctrine is also referred to as *stare decisis*, which means "keep to what has been decided". The doctrine of precedent must follow the hierarchy of courts. It means a decision shall only become binding on the same or lower level of courts in accordance with their relative ranking. This principle can be illustrated by vertical and horizontal *decisis* in our court system.

Vertical *decisis* – In Hong Kong, the Magistrates, various tribunals and the District Court act as the lowest trial court. The Court of First Instance acts as both trial and appellate court. The Court of Appeal acts solely as an appellate court, and the Court of Final Appeal acts as the court for final adjudication. The principle of vertical *decisis* is that all courts exercising trial jurisdiction must follow the decisions of the courts exercising appellate and final adjudicating jurisdiction. Therefore, the decisions of the Court of Appeal are binding on the Court of First Instance. It means Louisa can refer to the case from the Court of Appeal for reference.

Horizontal *decisis* – This refers to the situation that a judge shall be bound by the decisions of the previous cases at the same level in the hierarchy. The actual operation is a matter of the court's practice. For example, the Court of Final Appeal is not bound by itself, the Court of Appeal is bound by its prior decisions, and the Court of First Instance is not bound by its own decision. That said, the case from the Court of First Instance may not be applicable to the upcoming case of Louisa.

Answer 2(b)

Overseas decisions – Strictly speaking, overseas decisions, even from other common law countries are not in the same hierarchy as the courts in Hong Kong, so they are not binding to the local courts. However, Hong Kong courts still highly regard the decisions made by the courts in other common law countries especially those from Britain. Article 84 of the Basic Law also allows local courts to refer to the decisions made by other common law countries.

In our case, even the decision from the House of Lords may not necessarily be binding for Hong Kong courts, but it may have persuasive authority for the local courts and Richard can still take reference from it.

Answer 2(c)

Ratio – Not everything mentioned in a judgment shall become a binding precedent. Only the legal reasons handed down by the court shall be binding, and we call it the *ratio decidendi*. This refers to the legal reasons given by the court in resolving a particular case or dispute. The opposite of *ratio decidendi* is *obiter dicta*. This means something being mentioned by the judge but they are not related to the judgment. *Obiter dicta* shall not be treated as a precedent.

In our case, since the suggestions made by the court were related to administrative matters only (*obiter dicta*), so it shall not be binding for other courts.

Answer 3

Chris can sue Super Tech Ltd in tort of negligence. In order to prove the liability of the defendant (Super Tech Ltd), the plaintiff (Chris) has to prove four elements:

1. The defendant owed a duty of care to the plaintiff;
2. The defendant breached the duty of care;
3. The plaintiff's injury or damage must be caused by the defendant; and
4. The plaintiff must suffer damage.

The first element is duty of care. This duty requires a person to use reasonable care to avoid doing any harm to the others. The leading case is *Donoghue v Stevenson [1932] AC 562*, where it laid down the principles on duty of care. The plaintiff bought a bottle of ginger beer from the defendant, where she found certain remains of a snail inside. The plaintiff claimed to have suffered from stomach illness and wanted to have compensation. The court explained duty of care as "a duty to take reasonable care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour" and "persons who are so closely and directly affected by my acts that I ought to have them in contemplation as being so affected when I am directing my mind to the acts or omissions which are called in question.". This can be summarised as the "neighbour test". In a nutshell, it means that a duty of care is owed to people one ought reasonably to foresee will be affected by one's conduct. Therefore, the first thing for Chris has to do is to prove that he is the one that Super Tech Ltd could reasonably foresee when it was handling its waste water.

The second element is breach of duty. The assessment here is that the conduct in issue falls below the standard regarded as normal or desirable. The first test here is "foreseeability". This somehow means predictability. That is the scope of the risk and the likelihood on the occurring of certain events. The second test is the "reasonable man test". The test here is to judge the action of the defendant with the standard of a reasonable man (a normal individual) in his or her position. The standard may vary. For example, the standard shall be different if one is a professional. Therefore, the breach of duty is determined by whether a reasonable person in a particular circumstance with his or her own particular background would foresee such a risk. The relevant factors for the determination include the magnitude of risk involved, the purpose of that particular act or activity and the difficulty of taking precautions to avoid such a risk. Generally, the higher and more serious the risk involved, more shall be done for its avoidance (*Yu Yuk-Fung v Pui Kee Iron Works [1970] HKLR 73*). Chris needs to prove that the leakage of pipes and the pollution caused by the chemical substances were in breach of duty as a reasonable owner of a chemical factory and the harm to Chris would be foreseeable.

The third element is causation. Causation refers to the connection between the act of the defendant and the plaintiff's damage or injury. A defendant is not liable for negligence unless the plaintiff's loss was caused by the defendant. The courts will usually adopt the concept of the chain of causation, to see if there is an unbroken chain of events between the act and the damage caused. The plaintiff must also prove both causation in fact and causation in law. The former concerns whether the act of the defendant was the cause of the plaintiff's loss in fact. That said, the plaintiff's loss would not occur if not for the defendant's act. The latter focus is on whether the defendant's negligence was recognised by the law as the cause of the damage. The test is on fulfilling the legal requirements not merely the factual connection. Chris has to prove that his loss is the direct result from the chemical substances flushed into the river by Super Tech Ltd.

The final element is damage. Damage is the actual harm, injury or loss suffered by the plaintiff. The underlying principle in tort is to restore the plaintiff to its former status before the tortious act of the defendant. This legal principle being known as "*restitutio in integrum* (full compensation)". Apart from proving damages from the defendant, the plaintiff also needs to consider the extent of loss which is recoverable. The court will adopt the concept of remoteness of damage, where it will limit the kind of damage which was unforeseeable or occurred in an unusual way. This means some damage will be treated as too remote and shall not be borne by the defendant. Finally, Chris must show to the court that the chemical substances from Super Tech Ltd caused real losses to him because merely proving the occurrence of such an event is not enough, Chris needs to prove damages.

Answer 4(a)

The basic elements in forming a valid contract are intention, consideration, offer and acceptance. Supposing all the other elements exist, then a contract shall be concluded once an offer is duly accepted. Therefore, the first element we need to look for is a valid offer. A valid offer is one which can be readily acceptable. An offer can be easily mixed up with an invitation to treat.

An invitation to treat is a proposal and its purpose is to invite the other party for further negotiation. It shows the willingness of a party in entering a contract at a later stage. It is not yet an offer because it does not contain all the necessary elements making it readily acceptable. It usually refers to the preliminary stage of a contractual negotiation.

In contrast to an invitation of treat, an offer is an expression of willingness to contract on certain terms, made with the intention that it shall become binding as soon as it is accepted by the person to whom it is addressed. An offer must be very clear, and it must contain all the necessary elements for a contract to be concluded.

There are two main types of contract: a bilateral contract and a unilateral contract. A bilateral contract refers to the situation where the contractual parties are specified and know each other. A unilateral contract is one where only one party makes an express promise, or undertakes a performance without first securing a reciprocal response from the other party. This means, the offeror is making an offer to some unknown parties (the whole world).

In *Carlill v Carbolic Smoke Ball [1893]*, a pharmaceutical company posted an advertisement and claimed that their smoke balls (a drug) could cure flu. The company promised to offer HK\$200 to anyone who used their products but still caught influenza. The company later argued that their statement was only a bluff without legal meaning. The court rejected their arguments and ruled that the advertisement included all the necessary information needed for an offer. More importantly, it clearly stipulated the conditions to be accepted by anyone who was willing to act on the offer. Therefore, it is a valid offer and shall be binding once accepted.

In our case, Orange Ltd clearly stated that anyone who used their anti-virus programme can be free from infection, and they were willing to pay compensation to uphold their promise. The statement also clearly stated the necessary conditions in accepting such an offer. Based on the principles of the Carbolic Smoke Ball case, it is a unilateral contract with an open offer to anyone who is willing to use their software. Richard used their software and accepted their offer, so he should be entitled to file a claim against Orange Ltd.

Answer 4(b)

S.19 stated that where there is a contract for the sale of specific or ascertained goods, then the time of transfer shall depend on the intention of the parties. Relevant factors such as the terms of the contract, the conduct of the parties and circumstances of the case shall also be considered.

Though, a seller of goods is given the power to reserve the ownership (title) of the goods under s.21(1). Therefore, if the seller has imposed certain conditions on the transfer of ownership of the goods, then the seller may reserve the right of disposal of the goods until all the conditions are fully fulfilled.

In our case, the sales contract clearly stated that the seller can retain the ownership of the piano until the buyer could fully settle the payment on or before the due date. Since Elsie failed to pay on time, this means the conditions imposed were not properly satisfied. Therefore, according to s.21(1), Anna still owned the title.

Note: The references to the above provisions are made to the Sales of Good Ordinance (Cap.26).

Answer 5(a)

Mary may commit money laundering contrary to ss.25 and 25A.

S.25 states that a person commits an offence if, he knowing or having reasonable grounds to believe that any property in whole or in part directly or indirectly represents any person's proceeds of an indictable offence, and he deals with that property. S.25A states that where a person knows or suspects that any property in whole or in part directly or indirectly represents any person's proceeds of; was used in connection with; or is intended to be used in connection with, an indictable offence, he shall as soon as it is reasonable for him to do so, disclose that knowledge or suspicion, together with any matter on which that knowledge or suspicion is based, to an authorized officer.

According to s.25, a person will be convicted of money laundering if he knew or even had reasonable grounds to believe the money is related to a crime but he still deals with it. Whereas a person shall also report any suspicious money transactions in accordance with s.25A.

In our case, even though Mary did not know the source and final purpose of the money from Robert, but at least she should have doubted its legality. This is because Mary has been working as a branch manager for 10 years, and she must be noticed that depositing such a huge sum of cash without disclosing the name of the client or its source and purpose were utterly abnormal. Despite all the doubts, Mary still assisted Robert in handling the money and also did not report such a suspicious money transaction. Since it is not a must to convict a person on his or her actual knowledge of the crime-related money but only a reasonable doubt about it shall suffice. It is very likely that Mary will be convicted on both counts.

Note: The references to the above provisions are made to the Organized and Serious Crimes Ordinance (Cap.455).

Answer 5(b)

William may have committed an offence for either maintaining a standard of living above his remuneration or possessing unexplained property under s.10.

S.10 of the POBO states that any person who being a prescribed officer (William is employed by the government): (a) maintains a standard of living above that which is commensurate with his present or past official emoluments; or (b) is in control of pecuniary resources or property disproportionate to his present or past official emoluments, shall, unless he gives a satisfactory explanation to the court as to how he was able to maintain such a standard of living or how such pecuniary resources or property came under his control, be guilty of an offence.

In our case, William is a fresh graduate and he is from a lower class family, but he was able to rent a top services apartment in Central where the monthly rent exceeded his monthly salary, which is contrary to s.10(1)(a) for maintaining a standard of living above his present or past remuneration. William also owns two luxury diamond Swiss watches and a top model BMW, which is contrary to s.10(1)(b) in possessing properties disproportionate to his present or past emolument. The law requires a prescribed officer who has violated the above requirements to give a satisfactory explanation to the court or otherwise he shall be guilty. William cannot argue that he is just merely having a good standard of living and then shirk the responsibility of proof to the enforcement.

That said, William's supervisor is right to report him to the Independent Commission Against Corruption for his living style, and he will be convicted unless he can provide a satisfactory explanation.

Note: The references to the above provisions are made to the Prevention of Bribery Ordinance (Cap.201).

Answer 6

The answer is affirmative. Public companies can offer shares or debentures to the public for the purpose of fund raising. However, a company must not issue any forms of application for debentures / shares to the public unless it has been issued with a prospectus in accordance with the law. The governing law is the amended Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap.32). Therefore, Michael's understanding was wrong.

A prospectus is defined as any prospectus, notice, circular, brochure, advertisement or other documents offering debentures / shares to the public or calculated to invite offers by the public to acquire the same. It includes any written documents serving the abovementioned purpose.

The contents of a prospectus can be summarised into four main areas:

- Firstly, basic information concerning the company and the offering in accordance with Schedule 3.
- Secondly, disclosure in accordance with Schedule 18 of Part 1 on the particulars of shares or debentures, financial condition of the company and the nature of the shares or debentures, company and the likely subscribers.
- Thirdly, various reports in accordance with Schedule 3 of Part 2. It includes auditor's report concerning financial condition of the company, accountant's report if the funds raised will be used in purchasing a new business or to acquire an undertaking and also a valuation report if the company holds land or buildings with a value of not less than HK\$3 million or 10% of company's value.
- Fourthly, if the prospectus included an expert's statement, then a written consent from that expert must be included for its authentication.

Note: The references to the above provisions are made to the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap.32).

Answer 7

Prima facie, Danny had neither been duly approved to be the managing director nor having the right to sign a contract beyond the limit of HK\$200,000. It is apparent that Danny had breached the requirement of the articles and he had no authority to enter into this contract of HK\$300,000.

However, the company may still be bound by the contract signed by Danny if the outside party argues that Danny was acting as the agent of the company in exercising his apparent or ostensible authority. The outside party could argue that Danny had been held out as the managing director of the company, and they were in reliance on this holding to enter the contract with the company. The general position is that the outside party has no duty to verify the internal affairs or regulations of the company.

Besides that, s.117 also states that if a person is dealing with a company in good faith, then the power of the company's directors to bind the company is to be regarded as free of any limitation under the articles of the company.

In our case, the contract made by Danny may therefore be binding on the company even though he may have acted in breach of his authority.

* * * END OF EXAMINATION PAPER * * *