Common Litigation Mistakes

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RME Course for Law Society of Hong Kong

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Common Mistakes in Litigation

Two main categories

Procedural Law:

Examples: failing to file acknowledgment of service within time; failing to serve the Writ within 1 year after its issuance; failing to observe limitation periods; failing to adhere strictly to the RHC.

Substantive Law:

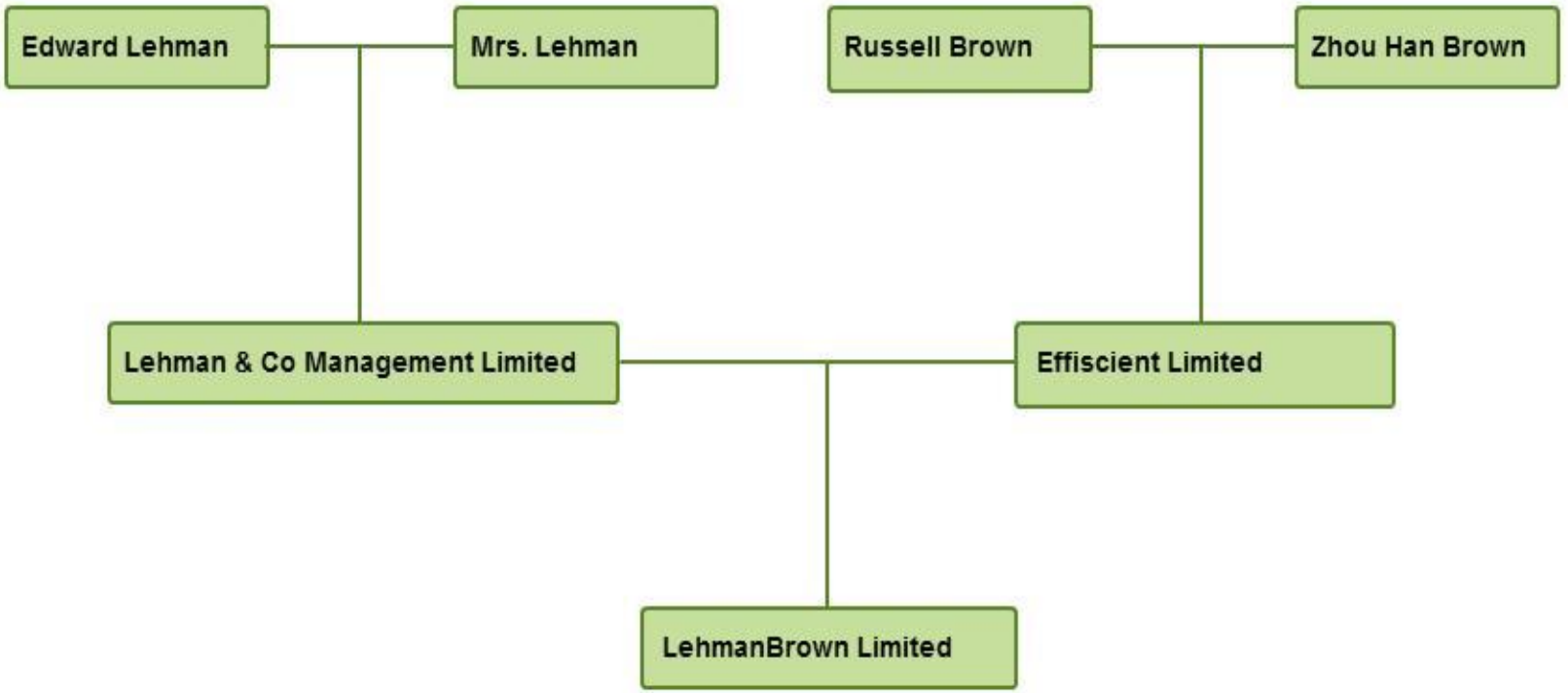
Examples: using the wrong plaintiff to sue; unaware of/mis-applying the relevant legal principles.

A Case Illustration of What Can Go Wrong in Litigation

This is a case of shareholder disputes between the two camp of equal shareholders of a company that led to litigations on multiple fronts including unfair prejudice/J&E winding-up petition, a trademark claim, a defamation claim and also related contempt proceedings. **All information is from published judgments found in the judiciary's website.** (31 published judgments)

The Company in issue, LehmanBrown Limited, was incorporated in Hong Kong in 2001.

The Company is a full service accounting firm providing audit and corporate advisory services in China.


Edward Lehman
Mrs. Lehman
Russell Brown
Zhou Han Brown
Lehman & Co Management Limited
Effiscient Limited
LehmanBrown Limited

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Background to the Disputes

(1) The Company was found by Mr. Edward Lehman (and his wife, Mrs. Karolina Lehman) and Mr. Russell Brown (and his wife, Mrs. Zhou Han Brown) in 2001.

(2) Edward Lehman is a US lawyer, then operating a mainland law firm (Lehman, Lee & Xu) ("**LLX**"), and had been in China since 1992.

(3) Russell Brown is an accountant. He had worked in Hong Kong, London, Singapore and Minneapolis between 1990 and 2001. He reached the position of Global Chief Financial Officer of a global PR firm before leaving to form the Company with Edward Lehman.

(4) Zhou Han has degrees from some Chinese universities and LSE. She worked for financial institutions in the United Kingdom between 1995 and 2000.

Background to the Disputes (cont')

(5) The parties met in 2001 and discussed the establishment of the Company.

(6) It was agreed between the parties that Russell Brown would have control of the day-to-day operations of the Company. Edward Lehman would be the financial investor, and would pay the initial expenses and to refer clients from LLX to the Company.

(7) Each would nominate one director. Lehman nominated Million Strong Limited, a company controlled by him. Brown nominated himself.

Background to the Disputes (cont')

(8) By the end of 2002, the Company was operating independently. Contrary to the initial understanding, Edward Lehman expressed his wish to "*take an active role in the management of [the Company].*"

(9) In September 2004, Edward Lehman started to demand large dividend payments. Russell Brown refused. He thought it was premature to declare dividends as the cash flow projections had not been finalised.

(10) Since October 2004, Lehman started sending emails to Brown alleging embezzlement of money and manipulation of accounts. It was also discovered Lehman took US$118,335 from the Company's bank account without authorization to secure rental payments due to LLX.

Background to the Disputes (cont')

(11) In August 2006, Brown discovered that Lehman had established a competing accounting firm in China called Lehman & Co., whose name was changed to Lehman Tax & Accounting and Lehman Bowen subsequently. It also used a webpage design that looked very similar to that of the Company.

(12) In between 2009 and 2010, Lehman started making a number of complaints to accounting regulators and the police, claiming that Brown had falsified the accounts of the Company and misappropriated client's money.

Background to the Disputes (cont')

(13) Lehman also published defamatory statements against the Company, Brown and Zhou Han by emails and web postings including:

(a) the Company's practice had violated certain rules of CIMA;
(b) Russell Brown was being investigated for ethical misconduct by CIMA;
(c) Zhou Han Brown was incompetent as an employee of the Company;
(d) the Company had tax evasion issues with the Hong Kong Commercial Crimes Bureau and Inland Revenue Department; and
(e) many other wrongdoings by the Company, Russell Brown and Zhou Han Brown.

The Trademarks Claim

- Soon after the Company was established, the parties agreed that Lehman would apply for the trademark of “LehmanBrown” for the Company in his name in Hong Kong and China, and transfer the trademark to the Company afterwards.

- However, Lehman never did so and transferred the trademarks to Home & Garden Limited, a company controlled by Karolina, his wife.

- During the later part of 2008, Lehman made complaints to the mainland authorities regarding alleged trademark infringements by the Company against trademarks owned by him, causing the Company’s premises to be raided in Guangzhou , Shenzhen, Beijing and Shanghai.

The Unfair Prejudice Claim

In September 2010, Lehman petitioned for winding up of the Company on just and equitable grounds (s.177(1)(f), Cap 32) and for alternative remedy (s.168A, Cap 32), asking for the buyout of Brown's shares in the Company.

Note: Section 168A of Cap 32 (the old Companies Ordinance and now the Companies (Winding Up and Miscellaneous Provisions) Ordinance) is now replaced by sections 723 to 726 of Cap 622.

The Situation as in September 2010

Imagine this:

(1) You represent Russell Brown, Zhou Han and Effiscient. Your clients have control of the day-to-day operations of the Company but your clients only control 50% of the shares in the Company.

(2) Your clients have 4 heads of grievance/claim against Lehman:

(a) The Competing Firm Claim

(b) The Trademark Claim

(c) The Defamation Claim

(d) The Misappropriation of Company Assets Claim

How would you proceed?

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The Unfair Prejudice Claim

The handling solicitors issued a cross-petition on 22 September 2010 (HCCW 383/2010), claiming section 168A relief, specifically for:

(1) the sale of the shares in the Company from Lehman to Brown;

(2) return of the misappropriated Fund to the Company

(3) further or other orders as the court may deem fit; and

(4) costs.

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The Unfair Prejudice Claim

- Trial took place in October 2011.
- The trial was practically a homerun for the Brown camp as the judge (Harris J) clearly disliked Lehman.
- **Thus, counsel and instructing solicitors decided to push further and ask for damages under the Competing Firms claim and the Trademark claim.**
- Judgment was handed down on 15 November 2011, granting every relief sought by **Effiscient** (Brown), including damages to be paid by Lehman Management to **Effiscient** (practically Lehman to Brown) and purchase of Lehman's shares to be valued after an expert report has been prepared (with such damages being deducted from the share purchase price).
- After getting judgment Effiscient's solicitors quickly engaged experts to assess the "damages" and the value of the share.

This sounds like a complete victory, right?

So, what went wrong?

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The Reflective Loss Principle

The Statute

Section 168A(2C) of Cap 32 (now repealed and replaced section 725 of Cap 622):

"*For the avoidance of doubt, the damages that may be ordered by the court under subsections (2)(b) and (2B)* ***does not entitle a member****, past member or then member of a specified corporation* ***to recover by way of damages any loss that is solely reflective of the loss suffered by the specified corporation which only the specified corporation is entitled to recover under the common law****.*" (emphasis added)

Note: Section 725(5) of Cap 622 is practically identical

The Mistake

- The mistake was that the loss claimed is not recoverable by Effiscient as it is solely a **reflective loss**: it is a **loss suffered by the Company, NOT its shareholders**.

- The mistake is quite glaring, as it is actually in the same section where the petition was based.

- The Court of Appeal (CACV 272/2011) allowed appeal by the Lehman camp on the damages point (i.e. no damages could be awarded because Effiscient was the **wrong plaintiff**).

- Effiscient was ordered to pay costs of the appeal and all the wasted costs for assessing “damages”.

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The Defamation Claim

The Instructing Solicitors commenced action against Edward Lehman on 28 June 2010 (under HCA 959/2010), by naming three Plaintiffs:

(1) Russell Brown;
(2) Zhou Han Brown; and
(3) Effiscient Limited.

Note: The defamatory statements by Lehman were directed at Russell Brown, Zhou Han Brown and **the Company**.

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Procedural History

- The Writ of Summons (general endorsement) was issued on 28 June 2010 seeking:
  (1) Injunction
  (2) Damages
  (3) Interest
  (4) Costs
  (5) Further and/or other relief

- After the Writ was issued on 28 June 2010, the Plaintiffs obtained leave to serve the Writ out of jurisdiction in China.

- On 23 July 2010, an interlocutory injunction was obtained against the Defendant (Lehman), restraining him from making further defamatory statements.

Procedural History

- After service, following failure by Lehman to acknowledge service, the Plaintiffs applied for default judgment on 12 November 2010 pursuant to Order 13, RHC by way of affirmation and draft order.
- The relevant parts of the affirmation:

  "*On 23 July 2010, the Honourable Mr. Justice To granted an injunction order inter alia restraining the Defendant from publishing, republishing or making Defamatory Statements about the Plaintiffs and the Company until after the trial of this action or until further order.* ***The Plaintiffs are now only left with their claim for unliquidated damages under the Writ of Summons and are hereby applying to this Honourable Court for interlocutory judgment against the Defendant for damages to be assessed and costs.***"
- A Master granted Interlocutory Judgment on 3 December 2010, for damages to be assessed.
- **Any Problem?**

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Order 13

- Rule 1: liquidated damages
- Rule 2: unliquidated damages
- Rule 3: detention of goods
- Rule 4: possession of land

Order 13

Rule 6:

(1) Where a writ is indorsed with **a claim of a description NOT mentioned in rules 1 to 4**, then, if any defendant fails to give notice of intention to defend, the plaintiff may, after the prescribed time and, if that defendant has not acknowledged service, upon filing an affidavit proving due service of the writ on him and, where the statement of claim was not indorsed on or served with the writ, upon serving a statement of claim on him, **proceed with the action as if that defendant had given notice of intention to defend**.

Proper Abandonment of Claim Outside Order 13

- Thus, a Plaintiff cannot enter default judgment under Order 13 if the claim contains or includes a claim which is not squarely within rules 1 to 4 of Order 13.

- To proceed with those claims, you have to proceed as if the defendant had given notice to defend (i.e. you should proceed under Order 19, rule 7).

- However, a Plaintiff can enter judgment under Order 13 if he **"expressly and finally abandons" every remedy or relief falling outside the scope of Order 13, rules 1 to 4** (White Book 13/6/1).

- Issue: Is the paragraph in the affirmation in support of default judgment "express and final abandonment" of the injunction claim?

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Default Judgment for a Defamation Claim

- Having woken up to the claim, Edward Lehman came back and applied to set aside the interlocutory judgment on the basis, inter alia, that it was an irregular default judgment.

- The matter was heard before Deputy Judge L Chan (as he then was) on 19 April 2012, who held that "*a reasonable reading of these paragraphs must mean that there was no other relief pending save the claim for damages to be assessed. That must also be a clear implication or indication that the claim for a permanent injunction had been abandoned.*"

- Thus, the Judge held that the judgment entered was a regular judgment.

- Lehman appealed the decision to the Court of Appeal (under CACV 119/2012).

Default Judgment for a Defamation Claim

- The Court of Appeal found that the relevant part of the affirmation in support of default judgment was NOT an express and final abandonment of claims. Nothing referred to in the paragraph indicated that the plaintiffs were intending to give up their claim to an injunction. On the contrary, it appeared to be of the view that the plaintiffs had already obtained the injunction that they were seeking (a view which was mistaken, as the injunction that had been obtained from To J was interlocutory and not final).

- But even if the injunction granted by To J had been a final injunction, the plaintiffs' approach was that having obtained the injunction, they were left only with their claim for damages. This approach did not involve any abandonment of the claim for an injunction. On the contrary, it displayed an intention to rely on that claim to keep the fruits of it, which had (at least according to affirmation, incorrect though it may have been) already been obtained. So understood, the plaintiffs were not abandoning their claim to the injunction at all, let alone expressly and finally.

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Further Complications

- More than 5 years after the action was commenced, clients went back to the pleadings stage.

  (Note: The CA heard the appeal on 13 June 2013 and 22 July 2014. CA's Judgment was handed down judgment on 29 July 2016. The decision on costs was handed down on 26 June **2020!**)

- The defamatory statements were not particularized and clients did not even have a statement of claim 4 years after the action was commenced.

  (Note: An SOC was finally filed in December 2016.)

- Believing that they have validly obtained an interlocutory judgment with damages to be assessed, the former solicitors engaged an expert to provide an opinion on the damage caused to the Company by the defamatory statements.

Methodology Adopted in the Expert Report

- The expert is a CPA who professed to be expert in litigation support and forensic accounting.

- He attempted to put a valuation on the decrease in value in Effiscient's share in the Company, as a result of the defamatory statements made by Edward Lehman on Russell Brown, Zhou Han Brown and the Company.

- He adopted a capitalisation of earnings approach and attempted to put two valuations on the Company for 2010, one assuming no defamation has taken place and another one for the actual value, on the assumption that the difference is the damage caused.

Methodology Adopted in the Expert Report

- In assessing the “no defamation” value, the expert assumed that the Company would grow at the rate predicted by management in 2009, having compared that with growth rate in the industry.

- In assessing the value after defamation, the Company’s actual income was used.

- No allowance was made for damages or diminution in value for factors other than defamation.

- **What are the problems with this report?**

Problems

- The report is completely useless.

- The difference in market capitalisation approach has been severely criticised in the English case of *Colin Stewart v Financial Times* [2004] EWHC 2337 (QB) for two reasons:

  (1) There can be many factors that affect the market capitalisation of the Company other than the alleged libel. This is too uncertain as a measure of damages in law.

  (2) The use of comparators is undesirable as it would involve the court having to investigate into the affairs of each of the comparable companies. The case would be untriable and would be a waste of resources of the court.

Assessing Damages

- **Further**, even if the interlocutory judgment was valid:

  (1) An assessment of damages could not be carried out without first having particularized (and proved) the defamatory statements.

  (2) The Defendant can fight on every single statement to challenge whether they are defamatory in nature or whether they had been made at all, the assessment of damages of hearing would in effect be a full trial.

  (3) After all, entering Order 13 default judgment on a defamation claim was a bad move as there is no practical benefit.

Reflective Loss Again …

- After the party problem has been identified in the CA in the unfair prejudice action (Effiscient cannot sue for loss of the Company), on 9 May 2013, at the time when the assessment of damages hearing was being prepared to be heard and after Deputy Judge L Chan (as he was then) held that the default judgment was regular, the Plaintiffs issued a summons to **substitute** Effiscient by **the Company**.
- In a hearing which Lehman failed to turned up, Deputy Judge Chan granted the order for substitution.
- But before the order was sealed, Lehman issued a summons asking for the matter to be re-heard, eventually this matter was also included in the appeal.
- Is it **possible to substitute parties after a default judgment was handed down ?**
- The Browns finally conceded this point in the appeal.

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Contempt proceedings - Building on Shaky Ground

- Lehman breached the interlocutory injunction order of To J and sent 9,000 defamatory emails to various parties, the Plaintiffs in HCA 959/2010 commenced contempt proceedings against Edward Lehman. Lehman apologised unreservedly in court and was ordered to pay a fine of HK$200,000 by To J on 19 April 2011. (The First Committal)

- The Second Committal:
  - During the trial of the Unfair Prejudice petition, Lehman sent out numerous defamatory statements against the Company and the Browns by email during adjournments. Effiscient commenced committal proceedings against Lehman based on To J's interlocutory injunction (HCMP 2524/2011).

  - Harris J found Edward Lehman guilty and sentenced him to jail (suspended) on 12 July 2012.

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Building on Shaky Ground

- Lehman appealed to the Court of Appeal on a new point not raised at trial.

- The submission was that the emails were sent to **recipients in England**, and in law, a defamatory statement is published where the message was read, thus Edward Lehman was not guilty of contempt.

- The Court of Appeal accepted this submission and overturned the conviction at first instance. Effiscient was ordered to pay costs. (CACV 177/2012)

- Is an appeal to the Court of Final Appeal possible? However, a more fundamental problem was noticed, as **Effiscient was not the right party in the Contempt Proceedings**, the action was bound to fail in any event

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Wrong party (again!) in a big defamation case

- In HCA 1109/2010

BAWANG INTERNATIONAL (GROUP) HOLDING LIMITED	1st Plaintiff
BAWANG (GUANGZHOU) COMPANY LIMITED	2nd Plaintiff

and

NEXT MAGAZINE PUBLISHING LIMITED	Defendant

Ps claimed against D for defamation. Damages:-

(1) Loss of profits – RMB 449m
(2) General damages
(3) Exemplary damages

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Wrong party (again!) in a big defamation case

- After a 40 day trial, the judge had little difficult finding for the Ps on liability but awarded a total of a little more than HK$3m to the Ps.
- Why?

- P1 – holding company – can't recover loss suffered for subsidiaries
- P2 – responsible for mainland sale – however, Next Magazine was strictly prohibited in the mainland. P2 failed to prove it suffered loss in mainland because of the Next Magazine article.
- Loss of sale in HK and other areas cannot be claimed as the relevant subsidiaries have not been joined.
- In assessing general damages, the court cannot take into account damage to reputation suffered by other subsidiaries.

Wrong party (again!) in a big defamation case

- 692. It is difficult to understand why the Plaintiffs have not joined HK1 and HK2 as additional claimants. **The Defendant had raised the no-reflective-loss defence at the early stage of the proceedings.** Apparently, the 2nd Plaintiff was joined as an additional claimant after considering such defence, and yet the Plaintiffs have not joined the other relevant subsidiaries as additional plaintiffs. As pointed out by Lord Millet in *Waddington*, the court has no discretion in such matter and the Plaintiffs cannot therefore claim for the loss of profits in respect of BaWang Shampoo Products outside the Mainland including Hong Kong.

- 695. The Plaintiffs also cannot claim for the loss of profits relating to the sales in Hong Kong because such loss was actually suffered by the two subsidiaries of the 1st Plaintiff, namely HK1 and HK2. As they have not been joined as the claimants in these proceedings, the existing Plaintiffs are not able to claim the loss on their behalf or to sue for the loss of the value of their shareholdings because of the no-reflective-loss principle.

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LIMITATION PERIODS – EASY TO COUNT?

- Chow Ching Man v Sun Wah Ornament (CACV 207/1995)
- New China Hong Kong (in CVL) v EY *(*HCCL 41/2004, HCCL 2/2005)
- Kensland v Tai Tang Chong [2008] HKCFA 13

- Chow Ching Man and 7 others v Sun Wah Oranment and 18 others CACV 207/1995

  - To Kwa Wan Canopy case
  - All Ps represented by one firm. Ds represented by different firms.
  - Ps' solicitors issued a writ but didn't serve within a year.
  - DOA 26 Nov 1990
  - Writ issued 23 Oct 1993
  - Application to renew and extend for one year 19 Oct 1994 (O6R8(2))

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LIMITATION PERIODS – EASY TO COUNT? (cont'd)

- Order granted on 22 Oct 1994
- Writ served in a few days
- 14 Ds applied to set aside, 2 filed Defence, others defaulted
- CFI set aside extension
- Ps appealed to CA

- "If the appeals succeed, the appellant plaintiffs will be able to pursue their claims against the respondent defendants on the merits. The failure of the appeals may mean that the plaintiffs will be left to pursue such remedy as fresh legal advisers may advise them to pursue against their present legal advisers. So the case is an unfortunate one all round." para 2, Bohkary JA

LIMITATION PERIODS – EASY TO COUNT? (cont'd)

- The law: "Where the failure to serve a writ within its normal validity period is the result of a choice, then it is necessary to decide whether the choice was made for a good reason, meaning one which supports a deliberate failure to comply with the time limit involved. And no discretion to extend the writ would arise unless the choice was made for a reason which is at least capable of amounting to a good reason."
- In fact, Ps could have been able to serve the writ within the normal period (i.e. before 22 midnight Oct 1994), albeit a bit rush, but somehow Ps chose not to do so.
- No discretion arose.
- What about the Ds who filed defence???

Case Study

- *The New China Hong Kong Group Ltd v Ernst & Young (*HCCL 41/2004, HCCL 2/2005)
  - NCHK – founded by Tsui Tsin Tong, incorporated in 1992, went into CVL in 1999.
  - Liquidators investigated and fought a number of s.221 CO summonses with EY
  - Actions commenced against EY in 2004 and Anthony Wu in 2005 (the case was heard in 2008)
  - EY was auditors for whole period, also financial adviser. Anthony Wu was lead partner.

Case Study (cont'd)

- Anthony Wu was director up to 1993, then financial adviser on the executive committee.
- Claims against EY – iro 94, 95 audited accounts, EY gave unqualified opinions (in 95 and 96) and failed to give warning of over-exposure to 7 debtors.

When did cause of action accrue?

When did cause of action accrue?

L: when the NCHK went into liquidation.

EY: when the audited reports were issued.

Answer: ?

What's the loss caused by the negligent audit?

- The full amount of the loans?
- No, it's just the chance to salvage what's left of the bad loans (by realising securities and enforcing the loan).
- Hence, cause of action accrued shortly after the issuance of the audited reports when management was supposed to take necessary action if the audited reports had not been negligently prepared and had given the necessary warnings.

Hence, primary limitation of 6 years has passed.

What about secondary limitations under s.31 and s.26 LO?

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s.31, Limitation Ordinance

(1) **This section applies to any action for damages for negligence**, other than one to which section 27 applies, **where the earliest date on which the plaintiff** or any person in whom the cause of action was vested before him **first had both—**

(a) the knowledge required for bringing an action for damages in respect of the relevant damage; and

(b) a right to bring such an action,

(referred to in this section as the "date of knowledge") **falls after the date on which the cause of action accrued.**

(2) The period of limitation prescribed by section 4(1) in respect of actions founded on tort shall not apply to an action to which this section applies.

s.31, Limitation Ordinance (cont'd)

(3) An action to which this section applies shall not be brought after the expiration of the period applicable in accordance with subsection (4).

(4) That period is either—

(a) 6 years from the date on which the cause of action accrued; or

(b) 3 years from the date of knowledge, if that period expires later than the period mentioned in paragraph (a).

(5) In subsection (1) " the knowledge required for bringing an action for damages in respect of the relevant damage " (就有關損害而提出損害賠償訴訟所需的知悉) means knowledge—

s.31, Limitation Ordinance (cont'd)

(a) of such facts about the **damage** in respect of which damages are claimed as would lead a reasonable person who had suffered such damage to consider it sufficiently serious to justify his instituting proceedings for damages against a defendant who did not dispute liability and was able to satisfy a judgment;

(b) that the damage was attributable in whole or in part to the act or omission which is alleged to constitute negligence;

(c) of the identity of the defendant; and

(d) if it is alleged that the act or omission was that of a person other than the defendant, of the identity of that person and the additional facts supporting the bringing of an action against the defendant.

s.31, Limitation Ordinance (cont'd)

Key issues:-

- only applies to negligence, not contract
- "the knowledge required for bringing an action for **damages** in respect of the relevant **damage**" – what does it mean?
- whose knowledge?

Kensland Realty Ltd v. Tai, Tang Chong [2008] HKCFA 13

- A few months before the NCHK case, these issues have been authoritatively answered in *Kensland*.
- Kensland sold a property to purchaser to be completed at 1 p.m. on 2 September 1997.
- On the completion date (2 September 1997), it (through TTC) only gave instructions on split cheques to purchaser's solicitors in less than 2 hours.
- Purchaser was 6 minutes late to deliver cheques (1:06 pm).
- Kensland, on advice on TTC, treated this as repudiation, forfeited the deposit and refused to complete.
- Purchaser immediately sued Kensland on 3 September 1997.

Kensland Realty Ltd v. Tai, Tang Chong (cont'd)

- Kensland won at First Instance (5/4/2000) but lost in CA (23/1/2001) and lost again in CFA (10/12/2001)

- After losing in CFA, Kensland turned to sue TTC for negligent advice. The action was commenced in January 2004.

- The "negligent" advice was given in September 1997. Time barred?

- Issue: under s.31 LO, when would Kensland be deemed to have "the knowledge required" to bring an action against TTC for negligent advice?

- **Answer: 3 September 1997 !**

Why? Because of s.31(5) and (7) LO

- What is required is the knowledge of “damage”, NOT legal knowledge of “liability” or “cause of action”.

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The New China Hong Kong Group Ltd v Ernst & Young (the "NCHK case")

- The Court summarised the principles in Kensland as follows:-

  (1) The knowledge which sets time running under s. 31 LO consists both of the plaintiff's actual knowledge and knowledge which is imputed to him (para. 68);

  (2) S.31 is concerned the plaintiff's knowledge relating to the damage incurred and not with the defendant's liability. The section has nothing to do with whether the plaintiff knew that the defendant's conduct amounted in law to negligence or that he had a good claim against the defendant (paras. 73, 74);

The NCHK case (cont'd)

(3) S. 31(5)(a) LO establishes a low threshold. The knowledge required to set time running is likely to be satisfied where a plaintiff becomes aware of some actual damage, provided that it is not so trivial as to be not worth bothering about (para. 79);

(4) S. 31 LO does not require the plaintiff to have detailed knowledge of all the acts and omissions set out in the particulars of his pleadings as constituting negligence. What matters is the plaintiff's knowledge of what lies at the core of the pleaded case. The requisite knowledge is not of the acts or omissions as pleaded but knowledge of the facts constituting "the essence of the complaint of negligence" distilled from such pleading (paras. 103, 105);

The NCHK case (cont'd)

(5) Knowledge of the "essence" of the act or omission is gained "the moment at which the plaintiff knows enough to make it reasonable for him to begin to investigate whether or not he has a case against the defendant": Hoffmann LJ in *Broadley v. Guy Clapham & Co.* (para. 107);

(6) The plaintiff must be shown to have actual or imputed knowledge of all the facts which are essential to the complaint which is eventually formulated as his negligence claim (para. 108).

(7) In *Kensland*, the fact that Kensland was sued immediately on 3 Sept 1997 – the next day after the "negligent" advice was given – constitute sufficient 'damage', which Kensland should be aware of.

s.31, LO (cont'd)

- Hence, it could be seen that the threshold is rather low. Further, the burden is on the plaintiff to prove that he did not have such knowledge.
- In the NCHK case, the plaintiff argued that it was only after the s.221 CO proceedings, which took a few years to conclude, and after full analysis of the transcripts, that the full extent of EY and AW's breaches of duty have become clear.
- However, the court found that whilst the s.221 CO transcripts may provide further evidence to support the claims, the essence of the claims was known long before that.

Known by whom?

- Note that the **plaintiff** in the NCHK case is the **company** acting through the liquidators, **NOT the liquidators**.
- Hence, it's the knowledge of the company that counts, NOT the liquidators'.
- What's meant by the knowledge of the company?
- Rules of attribution: knowledge of the defendants and those (within the company) who conspired with him doesn't count
- Knowledge of directors who are in a position to act would count.

The NCHK case (cont'd)

- The court held that the essential facts in this case are that:-
  - NCHK's business was conducted in a reckless manner and that the defendants failed to give the necessary warning and signed unqualified opinions of its audited accounts.
- It was found that the finance director and some other directors were aware of these facts well before the winding up of NCHK in 1999. It was not pleaded and no evidence was presented that they were in any way connected with the alleged negligent acts of EY and AW.
- Hence, NCHK and the liquidators, when they took over, were fixed with the knowledge of the essential facts through these directors.

Concealment under s.26 LO

- Can the liquidators then argue that there was deliberate concealment under s.26 LO?
- L argued that EY and AW were uncooperative in providing info, and fought a number of s.221 summonses requiring them to produce documents (in which they all lost), thus substantially lengthening the investigation process.

s. 26 LO provides:

"(1) Subject to subsection (4), where in the case of any action for which a period of limitation is prescribed by this Ordinance, either –

(a) …

(b) Any fact **relevant** to the plaintiff's right of action has been **deliberately concealed** from him by the defendant;

(c) …

the period of limitation shall **not** begin to run until the plaintiff has **discovered** the …… concealment **or** could with **reasonable** diligence have discovered it.

s. 26 LO provides:

(2) …

(3) For the purpose of subsection (1), deliberate commission of a breach of duty in circumstances in which it is **unlikely** to be discovered for some time amounts to **deliberate** concealment of the facts involved in that breach of duty.

The court in the NCHK case held:-

‘In this connection, it should also be borne in mind Lord Browne Wilkinson’s statement in *Sheldon* that “facts relevant to the plaintiff’s right of action” do not include facts which improve the plaintiff’s prospect of success. The liquidators’ complaint as to concealment of details of E&Y’s audit work; destruction of the audit working papers; or the obstruction or opposition to the section 221 proceedings, are therefore clearly irrelevant for the present purpose. They are not essential matters or “relevant facts” for the purpose of section 26(1)(b).’ (para 137)

CONCLUSION

WHAT CAUSES THE MISTAKES?

HOW COULD ONE AVOID MISTAKES?

SUGGESTIONS?

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