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Ref : Chans advice/189

To: Transport Industry Operators

Air cargo misdelivery (II)

Remember our Chans advice/165 (reporting the Hong Kong Court of Appeal holding the Hong Kong forwarder liable to pay US\$852,339 plus costs and interest to the Indian bank in the air cargo misdelivery case)? On 19/5/2016, the Court of Final Appeal dismissed the Hong Kong forwarder's application for seeking leave to appeal. [FAMV Nos 45 & 52 of 2015]

The factual background

The factual background can be summarised again as follows:-

- (1) The Indian bank provided banking facilities in India to an Indian diamond supplier.
- (2) The Indian bank made finance available to enable the diamond supplier to acquire diamonds and other raw materials for the manufacture of finished diamonds for export.
- (3) With the Indian bank's consent, the diamond supplier sold three batches of diamonds to a buyer in Hong Kong. The payment terms were documents against acceptance 120 days after sight – i.e. the Indian bank (through its Hong Kong agent) would present drafts of 120 days' tenor (drawn by the diamond supplier on the buyer) to the buyer for acceptance, and that the buyer would only be entitled to take delivery of the goods after having accepted the drafts drawn on it. The diamond supplier agreed to pledge the diamonds to the Indian bank, which would only release them after 120 day drafts drawn by the diamond supplier on the buyer had been accepted and indorsed to the Indian bank.
- (4) The diamonds were shipped to Hong Kong by air. The diamond supplier engaged an Indian freight forwarder to make arrangements for the shipment. The shipments were effected under three House Air Waybills issued by the Indian forwarder, respectively dated 28/7/2008, 6/11/2008 and 12/11/2008. The House Air Waybills recorded the diamond supplier as the shipper, the Bank of East Asia ("BEA") (the Indian bank's agent and receiving bank in Hong Kong) as the consignee and the buyer as the notify party.
- (5) The House Air Waybills were given by the Indian forwarder to the diamond supplier, who in turn handed them over to the Indian bank. The Indian bank sent them on to BEA, but later received them back, and remained in possession of them.
- (6) According to the House Air Waybills, the Hong Kong forwarder was the contracting party in respect of the contract for carriage of the goods covered by the House Air Waybills.
- (7) After the diamonds arrived in Hong Kong, the Hong Kong forwarder released them to the buyer without having first obtained the consent of the Indian bank or BEA, and without the buyer having accepted the drafts drawn on it. As a result, the buyer was able to obtain the diamonds without paying for them, resulting in the Indian bank losing such security as it had over the diamonds.

The Indian bank's claim

The Indian bank sued the Hong Kong forwarder for conversion of the consignment of diamonds by having misdelivered them on their arrival in Hong Kong.

The decisions below

At first instance in the High Court, the Indian bank's claim was dismissed on the basis that it lacked *locus standi* to sue. The Judge thought it crucial that the AWB was not a document of title and held that

a pledge of the diamonds had not been created, so that the Indian bank did not have the right to immediate possession necessary to found an action for conversion.

The High Court's Judgment was reversed in the Court of Appeal which held, applying the Privy Council decision in *Kum v Wah Tat Bank Ltd*, that delivery of the diamonds to the carrier, consigned to the Indian bank's agent in Hong Kong, was a constructive delivery to the Indian bank of the goods which the parties had agreed should be subject to a pledge, perfecting the pledge and giving the Indian bank *locus* to sue for conversion. Damages were assessed at US\$852,339, reflecting the value of the diamonds stated on the AWB. Because the Indian bank had made a sanctioned offer to accept the lower sum of US\$850,000, applying Order 22 rule 24, the Court of Appeal ordered Hong Kong forwarder to pay (i) the costs of the trial on an indemnity basis; (ii) interest on the trial costs at half the rate of 4% over prime; and (iii) interest on the damages awarded at 4% over prime.

The application for leave on the merits

The Hong Kong forwarder sought leave to appeal both in relation to the substantive issues and the costs order.

As to the substantive merits, it formulated two questions said to be of great general or public importance, both of which had as their premise, the proposition that lack of knowledge by the carrier of the pledgee's interest in the misdelivered goods provided the carrier with a defence to an action for conversion.

However, no authority was cited in support of that proposition. The right to sue for conversion depends on the plaintiff having an immediate right to possession of the converted goods. A pledge is constituted by delivery, actual or constructive, of the goods to the pledgee who therefore has or is entitled to immediate possession and so has *locus* to sue for conversion. The position is conveniently summarised in *Chitty on Contracts, Vol II, §33-133* (omitting reference to citations) as follows:

"Until repayment, the pledgee is, by virtue of his possession and his immediate right to possession of the thing pledged, the only person who may sue a stranger for trespass or conversion; where the pledgee is deprived of possession by the tortious act of a stranger, the measure of damages recoverable by the pledgee is the full market value of the thing at the time when and the place where he should have obtained possession. (The tortfeasor cannot take advantage of the pledgee's liability upon his receiving that value, to account to the pledgor (or another) for any amount exceeding the pledgee's interest)."

In the case in question, the Indian bank and the diamond supplier entered into a contract of pledge involving a bailment by the diamond supplier of the diamonds to the Indian bank as security for repayment of its debt. As the Court of Appeal held, delivery of the diamonds to the carrier for carriage to Hong Kong, naming BEA as consignee amounted to constructive delivery to the Indian bank, perfecting the pledge. Accordingly, as pledgee, the Indian bank was entitled to immediate possession of the diamonds through its agent BEA. It was therefore entitled to sue the Hong Kong forwarder in conversion and the Hong Kong forwarder's knowledge or ignorance of the pledge arrangement between the Indian bank and the diamond supplier was irrelevant. The purported questions of law are not reasonably arguable.

Furthermore, as the Court of Appeal pointed out, the proposition that knowledge was required was never part of the Hong Kong forwarder's case in either of the Courts below. As the Court held in *Flywin Co Ltd v Strong & Associates Ltd*, and has frequently re-iterated, a party who seeks to raise a new point on appeal will be barred from doing so unless there is no reasonable possibility that the state of the evidence relevant to the point would have been materially more favourable to the other side if the point had been taken at the trial.

The state of the Hong Kong forwarder's knowledge had not been explored. The bland assertions made in the proposed questions that the Hong Kong forwarder lacked knowledge of the Indian bank's interest as pledgee could not simply be accepted. The fact that the AWB named BEA as the consignee

must of itself at least have constituted possible notice of a pledgee's interest. Even if the point were arguable, it was not one that could be taken for the first time in the Final Court.

One of the proposed questions suggested that an attornment was required to enable the Indian bank to sue. When pressed to explain, the Hong Kong forwarder asserted that an attornment by the diamond supplier was needed. The point is misconceived. As Lord Wright explained, attornment is necessary where a pledge is sought to be created over goods whose possession is not delivered (actually or constructively) to the pledgee, often because they are in a third party's, and not in the pledgor's, custody. His Lordship stated:

"At the common law a pledge could not be created except by a delivery of possession of the thing pledged, either actual or constructive. It involved a bailment. If the pledger had the actual goods in his physical possession, he could effect the pledge by actual delivery; in other cases he could give possession by some symbolic act, such as handing over the key of the store in which they were. If, however, the goods were in the custody of a third person, who held for the bailor so that in law his possession was that of the bailor, the pledge could be effected by a change of the possession of the third party, that is by an order to him from the pledger to hold for the pledgee, the change being perfected by the third party attorning to the pledgee, that is acknowledging that he thereupon held for him; there was thus a change of possession and a constructive delivery: the goods in the hands of the third party became by this process in the possession constructively of the pledgee."

The diamond supplier, the pledgor, constructively delivered the diamonds to the Indian bank, the pledgee, by consigning them for air carriage to BEA, the Indian bank's agent. The diamond supplier did not thereafter have custody of the diamonds, so that no question of any attornment by the diamond supplier arose. Attornment is simply not relevant.

The application regarding costs

Regarding costs, the Hong Kong forwarder sought leave to appeal against the Court of Appeal's order giving effect to the provisions of Order 22 which attach consequences to an efficacious sanctioned offer. The principal complaint was that the damages awarded (US\$852,339) exceeded the amount of the Indian bank's sanctioned offer (US\$850,000) by "a miniscule amount". The application was put in various ways, both as raising important points of law and as meriting leave on the "or otherwise" ground. There was, however, no basis for interfering with the Court of Appeal's exercise of discretion. The Court of Appeal were not laying down any hard and fast rules but, having considered all relevant aspects of the litigation, they held that it was not unjust for the Indian bank to rely on the offer it had made. It was a fact-specific decision that was perfectly justified as a matter of discretion.

The decision

Based on the above, the Court of Final Appeal dismissed the application with costs both on the substantive issues and the costs order.

Please feel free to contact us if you have any questions or you would like to have a copy of the Judgment.

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