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<td><strong>Author(s)</strong></td>
<td>Ho, LKS</td>
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Let Them Eat Cake

Insolvency situations rarely leave coupon holders in a position where they can have their cake and eat it.

The sudden collapse of Maria's Bakery in April raises new concerns over the extent to which holders of coupons are protected from the insolvency of coupon issuing companies.

In the case of cake coupons, the purchaser makes an advance payment in return for 'one dozen assorted cakes' (in practice their equivalent value) promised in the coupon. He or she has a contractual right to demand delivery of the cakes upon production of the coupon. Failure on the part of the issuer results in a breach of contract, entitling the purchaser to pursue legal redress and obtain damages.

Those who receive coupons as gifts enjoy the same right of redemption, as the issuing company has made a unilateral offer to deliver one dozen cakes to anyone who produces the coupon.

As contractual rights are personal rather than proprietary rights, if the issuing company becomes insolvent, the holder of the cake coupon is only entitled to a share of the company's assets, along with the other unsecured creditors, on a pari passu basis - unless the coupon holder can prove, inter alia, that title over some of these assets has already passed or that some of these assets are actually held by the insolvent company on trust for him or her.

Accordingly, the holder of a cake coupon may try to establish the following claims, none of which, however, offers much hope.

The first claim, relating to merchandise promised under a coupon, is that title has already passed to the purchaser of the coupon before the company's insolvency. If the holder is not the original purchaser but a donee, he has obtained title through constructive delivery (that is, delivery of the coupon) by the original purchaser.

Under s 18 of the Sale of Goods Ordinance, 'Where there is a contract for the sale of unascertained goods no property in the goods is transferred to the buyer unless and until the goods are ascertained.' As 'unascertained goods' in this section include goods to be manufactured at some future date by the seller, purely generic goods and an unidentified portion of a specified bulk, the 'one dozen assorted cakes' promised in the coupons fall within this definition.

Even though they might be subsequently ascertained, for title to pass, r 5(1) of s 20 of the Sale of Goods Ordinance provides that, subject to contrary intention, the goods must have been unconditionally appropriated; they must have been earmarked or attached to the contract in question.

Hence, in the ordinary course of business, title over the cakes does not pass until the customers have chosen the cakes and the sale assistants have removed them from the display shelves.

In any case, this argument is of no practical help where perishable items such as cakes are concerned. Nor would it be useful for consumers of services such as holders of rental coupons.

The second claim is that the purchase money is held by the company in trust for the claimant. The purchaser can argue that the issuing company receives the purchase money in a fiduciary capacity, as purchasers have placed trust and confidence in it.

This argument was rejected (almost) outright in Re Goldcorp Exchange Ltd [1995] 1 AC 74, where the Privy Council was unwilling to find any separate fiduciary duty in relation to the purchase money that is different from ordinary contractual duties.

Another way of establishing a trust over the purchase money is to assert that money paid under a contract for the sale of goods can be construed as a trust in the purchaser's favour. This may apply if there is 'either a mutual intention that the moneys should not fall within the general fund of the company's assets but should be applied for a special designated purpose, or that having originally been paid over without restriction the recipient has later constituted himself a trustee of the money': Re Goldcorp Exchange Ltd, above, affirming Quistclose Investments Ltd v Rolls Razor Ltd [1970] AC 567.

Hence, in Re Kayford Ltd (In Liquidation) [1975] 1 WLR 279, where a mail order company that was in financial difficulties put customers' deposit moneys in an account, meaning to keep them separate from its general assets, a trust was created in favour of the customers.

However, for this argument to succeed, the claimant must show that the recipient is not free to spend the purchase money as it chooses: Re Goldcorp Exchange Ltd, above.

It would thus appear that in the absence of any promise or action by the issuing company to keep the purchase money separate from its funds, it is difficult to see how the requisite trust could be established.

Furthermore, donees of coupons are unable to rely on such trusts in relation to the purchase money, as it is difficult to find any valid assignment of the beneficial interest, if any, to them.

Could it be argued that this result is too harsh on consumers? Whilst one can appreciate their predicament, protecting coupon holders by giving them proprietary rights will upset the allocation of risks that the parties have already undertaken.

By purchasing coupons, consumers should recognise that they are exchanging convenience (or price discounts) for the risk of insolvency. In this current economic climate, they should be advised to exercise the necessary caution before purchasing coupons or redeem them before it is too late.

Lusina Ho
Faculty of Law
University of Hong Kong
Hong Kong Lawyer
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