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Legal Update

Charting the Path: Major Developments in Hong Kong Arbitration Law in 2023

In this review, we reflect on significant developments in the field of arbitration in Hong Kong over the past year.

Key developments in 2023 included:

1. Multi-tiered dispute resolution clause – compliance with pre-arbitration conditions is *generally* a matter of admissibility to be ultimately determined by the tribunal and not subject to court review.
2. Lingering uncertainty remains as to the interplay between arbitration clauses and winding-up proceedings.
3. While the court continues to adopt a pro-arbitration approach, cases show it is also prepared to refuse enforcement when appropriate, demonstrating commitment to due process.
4. Hong Kong International Arbitration Centre (HKIAC) received more than 100 applications for issuing letters of acceptance under the Mainland-Hong Kong Interim Measures Arrangement.

Compliance with Pre-arbitration Procedures in Multi-tiered Dispute Resolution Clauses: The Court or Tribunal Has the Final Say?

Nowadays, it is common for commercial contracts to contain multi-tiered dispute resolution clauses which usually necessitate parties to engage in certain actions – such as attempting good faith negotiations, or mediation within a specified timeframe after a dispute has arisen – before a party can submit the dispute to arbitration.

In the landmark case of ***C v. D*** [2023] HKCFA 16, the dispute resolution clause in a contract regarding operation of a jointly-owned broadcasting satellite required parties to attempt to resolve the dispute through "good faith negotiations" before referring it to arbitration if the dispute could not be resolved through negotiations after 60 days.

In the arbitration, C objected to proceedings going forward on the ground that such pre-arbitration requirements had not been complied with. The Tribunal held that pre-arbitration conditions had been duly observed in its partial award (Partial Award).

Dissatisfied with the Partial Award, C brought court proceedings to set it aside pursuant to Article 34(2)(a)(iii) of the UNCITRAL Model Law (given effect by virtue of section 81(1) of the Arbitration Ordinance (Cap. 609) ("AO").

In gist, C contended that the Partial Award *"[dealt] with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contained matters beyond the scope of the submission to arbitration*", as the good faith negotiations requirement had not been complied with. It should therefore be set aside accordingly.

The Court of Final Appeal (except Gummow NPJ) adopted a distinction between a challenge to the **admissibility** of a particular claim and the challenge to a tribunal's **jurisdiction**. It ruled that the court may review a tribunal's ruling on its own jurisdiction (under Article 16 of the UNCITRAL Model Law (given effect by virtue of section 34(1) of the AO)) or Article 34(2)(a) of the Model Law (given effect by virtue of section 81(1) of the AO), but **not** a tribunal's ruling on admissibility of a particular claim.

Applying this distinction, Ribeiro PJ (whom Cheung CJ, Fok PJ and Lam PJ agreed with) held that *absent an agreement by the parties* that compliance with pre-arbitration conditions is amenable to review by the court, the issue of whether there was such compliance is generally a matter of admissibility of the claim in question, rather than an issue of the tribunal's authority to arbitrate (which goes to jurisdiction).

In this case, nothing in the contract suggested an intention to confer jurisdictional status on the pre-arbitration conditions. Therefore the Partial Award was **not** amenable to review by the court and C's application to set aside the enforcement order was dismissed.

As Fok PJ pointed out, this jurisdiction/admissibility distinction is widely recognised in various major international arbitration jurisdictions including England & Wales, Singapore and New South Wales, Australia. This decision has therefore brought Hong Kong in line with international practice and maintained Hong Kong's attractiveness as a major seat of international arbitration.

As an example of a true question of jurisdiction, in ***R v. A*** [2023] HKCFI 2034, Mimmie Chan J set aside a partial final award which declared that a third party non-signatory to an arbitration agreement is the "true principal" of one of the signatories; and therefore a proper party to the arbitration agreement under section 34 of the AO (which allows the court to review the tribunal's ruling on its own jurisdiction if the tribunal decides that it has jurisdiction).

In this regard, her Ladyship held that the issue of joinder of a non-signatory is a jurisdiction issue susceptible to the court's review.

Lingering Uncertainty over the Interplay between Arbitration Clauses and Winding-up Proceedings

In its landmark decision in ***Guy Kwok-Hung Lam v. Tor Asia Credit Master Fung LP*** [2023] HKCFA 9, the Court of Final Appeal addressed the issue of the court's discretion to decline jurisdiction in a bankruptcy petition (which is otherwise properly presented) where the underlying dispute about the petition debt is the subject of an exclusive jurisdiction clause (EJC) of New York courts.

The CFA held that in the ordinary case of an EJC, absent countervailing factors – such as the risk of insolvency affecting third parties and a dispute that borders on the frivolous or abuse of process – the petitioner and the debtor ought to be held to their contract (known as the "Guy Lam Approach").

In other words, the court should normally dismiss the bankruptcy petition when the underlying debt is subject to an EJC and in absence of countervailing factors. This contrasts with the traditional approach, which requires the debtor to demonstrate a bona fide defence on substantial grounds to defeat a bankruptcy petition in cases that do not involve an EJC.

An important question is whether the Guy Lam Approach – decided in a bankruptcy case involving an EJC – applies to winding-up proceedings involving an arbitration clause. In this regard, there have been inconsistent decisions in the Court of First Instance by company judges:-

1. On one hand, in ***Re Simplicity & Vogue Retailing (HK) Co., Ltd*** [2023] HKCFI 1443 and in ***Re NT Pharma International Co., Ltd*** [2023] HKCFI 1623, Linda Chan J held that the Guy Lam Approach does not apply to arbitration clauses and made winding-up orders against both companies.
2. However, in ***Re Shandong Chenming Paper Holdings Limited*** [2023] HKCFI 2065, Harris J held that the Guy Lam Approach does apply to arbitration clauses. In a footnote of the judgment, Harris J expressly indicated his agreement to the company submission that the Guy Lam Approach should be equally taken to the application of an arbitration clause.

   Nonetheless, leave was granted for the petitioner to appeal to the Court of Appeal. When granting leave, Harris J noted that "*it is highly undesirable that there are conflicting first instance decisions*".

Subsequently in ***Sun Entertainment Culture Limited v. Inversion Productions Limited*** [2023] HKCFI 2400, DHCJ Le Pichon observed the differences between Linda Chan J and Harris J but did not state a definitive stance. Instead, her Ladyship held that even if the Guy Lam Approach is applicable, the respondent company's alleged defence was frivolous, which is a recognised countervailing factor against staying or dismissing the winding-up petition. Her Ladyship made a winding-up order against the company.

Given the conflicting decisions, there is lingering uncertainty whether the Guy Lam Approach applies to arbitration clauses in which, if applicable, a creditor-petitioner bound by arbitration agreement will have to demonstrate countervailing factors set forth under the Guy Lam Approach in attempting to obtain a winding-up order.

Enforcement of Awards: Due Process Remains Crucial despite Pro-enforcement Approach

Like other prominent international arbitration jurisdictions, Hong Kong has traditionally adopted a pro-arbitration and pro-enforcement approach.

This general approach remained unchanged in 2023. For example, in ***AI & Ors v. LG II (as General Partner, and on behalf of Fund A)*** [2023] HKCFI 183, one of the grounds relied on in applying to set aside an award was alleged failure by the tribunal to deal with an issue submitted by the parties. In judgment, Mimmie Chan J reaffirmed the policy of minimal curial intervention and reiterated that the court approach should be to read the award generously – so as to remedy only meaningful and readily apparent breaches of the rules of natural justice which can cause actual prejudice – rather than comb an award to assign blame or find fault in the process. The setting aside application was dismissed.

However, the following cases serve as recent reminders that in appropriate cases where something went seriously wrong in the underlying arbitration, the Court is prepared to refuse enforcement.

FAILURE TO INDEPENDENTLY DEAL WITH DEFENCES

In ***Canudilo International Company Limited v. Wu Chi Keung & Ors*** [2023] HKCFI 700, Canudilo obtained an enforcement order to enforce a Final Award against Wu and other guarantors of an alleged debt owed by a borrower company.

The underlying arbitration proceedings were bifurcated. Arbitrator 1 first dealt with the liability between Canudilo and the borrower company in an earlier interim final award (the Interim Award) against the borrower company (but not the guarantors). Arbitrator 1 subsequently resigned and arbitrator 2 continued with the second part of the arbitration between Canudilo and the guarantors, making the Final Award against the guarantors.

The guarantors applied to set aside the enforcement order on the grounds that arbitrator 2 had, *inter alia*, exceeded its mandate and jurisdiction by failing to determine the issues in dispute; that the arbitration was not conducted in accordance with the arbitration agreement and/or the agreed arbitration procedures; that the guarantors did not have a reasonable opportunity to present their case; and that enforcement of the award would be contrary to public policy of Hong Kong.

Mimmie Chan J reiterated that when the court is called upon to set aside or refuse enforcement of an arbitral award, the fact that the tribunal had erred on facts or law is not a ground for the court to interfere. The court looks only at the structural integrity of the arbitral process, stepping in when there is an error so egregious that it would shock the conscience of the court to allow the award to stand and permit its enforcement.

In this case, arbitrator 2 rejected the guarantors' various grounds of defence largely on the basis that he was bound by the Interim Award, without seriously and independently considering the merits of such defences.

By doing so, Mimmie Chan J held that arbitrator 2 had failed to independently determine the issues in dispute, unfairly and unjustly depriving the guarantors of reasonable opportunity to present their case as to whether they were bound by the Interim Award and the findings therein.

The conduct of the arbitration by arbitrator 2 was found seriously flawed or egregious, such that due process was denied. The enforcement order was therefore set aside.

DEFECTS IN SERVICE OF THE NOTICE OF ARBITRATION

In ***G v. P (Arbitral Award: Setting Aside)*** [2023] 4 HKLRD 563, G obtained an arbitral award against P in a Hong Kong arbitration and subsequently an enforcement order from the court.

P applied to set aside the enforcement order on the grounds that there was no valid arbitration agreement between the parties, and it was not given a reasonable opportunity to present arguments in the arbitration.

Mimmie Chan J found there was a valid arbitration agreement in the underlying loan agreements, but set aside the enforcement order on the ground that the Notice of Arbitration was purportedly served via an email address different from that stated in the agreement. As such, there was no valid service of the Notice of Arbitration and G was not given notice of the arbitration – therefore not given an opportunity to present his case before the award was made against him.

This case is a reminder of the importance of properly serving documents pursuant to the underlying agreement. This is even more important where the opponent does not participate in the arbitration. It is prudent to play safe by making further efforts in ensuring good service has been effectively delivered.

DEPRIVATION OF THE RIGHT TO A FAIR HEARING

In ***Song Lihua v. Lee Chee Hon*** [2023] HKCFI 2540, Song obtained an arbitral award against Lee in a Mainland arbitration and subsequently an enforcement order in Hong Kong.

Lee applied to set aside the award itself in the Mainland but his application was dismissed by the Mainland court. Lee also applied to set aside the enforcement order in Hong Kong on various grounds pursuant to section 95(2) of the AO, including the conduct of one of the three arbitrators (Q) depriving him of the right to a fair hearing, which is contrary to public policy.

Specifically, the complaint about Q was he did not meaningfully participate in the 2nd (and last) hearing of the arbitration, as he was seen moving between different locations and did not give his undivided attention to the hearing. He was even off-line for periods and could not possibly hear what was said by parties' lawyers and other tribunal members.

Mimmie Chan J held that even though the supervisory court (Mainland court) refused Lee's application to set aside the award, it does not mean the enforcement court (Hong Kong court) cannot take the view that enforcement of the award is contrary to public policy in Hong Kong – after all, each jurisdiction has its own public policy. In this regard, her Ladyship made it clear that a fundamental principle for enforcement is that the award is made as a result of due process, and recognised rules of natural justice have been observed in the arbitration – including the principle that justice must not only be done, but must be seen to be done.

Given that Q did not hear the parties and was not focused on the trial during the 2nd hearing, her Ladyship held that there was a lack of apparent justice and fairness. Therefore the 2nd hearing fell short of the high standards expected by the Hong Kong court for a fair and impartial hearing, which upholds the parties' fundamental and basic rights. Consequently, the enforcement order was set aside.

This case shows that while the threshold for setting aside an enforcement order on the ground of public policy is generally understood to be high, the court is prepared to do so where serious issues arise in the arbitral process which are "*contrary to the fundamental conceptions of morality and justice*" in Hong Kong.

Mainland-Hong Kong Interim Measures Arrangement

The Arrangement Concerning Mutual Assistance in Court-Ordered Interim Measures in Aid of Arbitral Proceedings by the Courts of the Mainland and the Hong Kong Special Administrative Region came into effect on 1 October 2019.

Under this arrangement, any party to arbitrations seated in Hong Kong and administered by the HKIAC or other qualified arbitration institution (such as CIETAC Hong Kong, ICC Hong Kong), can apply to a competent Mainland court for interim measures in accordance with relevant Mainland laws and regulations.

Interim measures include, *inter alia*, preservation of assets, evidence or conduct. The party seeking an interim measure from a Mainland court shall submit a letter from the relevant arbitration institutions certifying the institution's acceptance of the arbitration case.

In October 2023, the HKIAC announced that it had received the 100th application[1]; and further reported that as of 27 December 2023[2] it had issued Letters of Acceptance in respect of 105 applications. Of these, 99 applications were made for preservation of assets, two for preservation

[1] https://hkiac.org/news/hkiac-receives-100th-application-under-prc-hk-interim-measures-arrangement

[2] https://www.hkiac.org/arbitration/IMA-FAQs, Q5

of evidence, and four for preservation of conduct. Among the recent applications, one was made by our team for the preservation of assets in the Mainland.

Outlook for 2024

2024 will likely be equally, if not more, exciting. One notable aspect is the anticipated Court of Appeal clarification (and possibly Court of Final Appeal) regarding applicability of the Guy Lam Approach in winding-up cases that involve an arbitration agreement.

Additionally, HKIAC statistics for 2023 are expected to be published in early 2024, likely reaffirming the popularity of Hong Kong as a preferred seat for international arbitration.

For more information about the topics raised in this Legal Update, please contact any of the following lawyers.

Vincent Law
+852 2843 2479
vincent.law@mayerbrown.com

Raymond Yang
+852 2843 2295
raymond.yang@mayerbrown.com

Johnson Ng
+852 2843 4248
johnson.ng@mayerbrown.com

Emily Chen
+852 2843 4272
emily.chen@mayerbrown.com

For more information, please contact your usual Mayer Brown contact of the Hong Kong Litigation and Dispute Resolution Team.

Terence Tung
+852 2843 4428
terence.tung@mayerbrown.com

Billy Lam
+852 2843 4392
billy.lam@mayerbrown.com

Tom Fu
+852 2843 2520
tom.fu@mayerbrown.com

Nancy Leung
+852 2843 4510
nancy.leung@mayerbrown.com

Alan Linning
+852 2843 2231
alan.linning@mayerbrown.com

Wilson Fung
+852 2843 2404
wilson.fung@mayerbrown.com

Jason Leung
+852 2843 4259
jason.leung@mayerbrown.com

Geoffrey Chan
+852 2843 4200
geoffrey.chan@mayerbrown.com

Menachem Hasofer
+852 2843 2384
menachem.hasofer@mayerbrown.com

Mei Ling Lew
+852 2843 2491
meiling.lew@mayerbrown.com

Vincent Law
+852 2843 2479
vincent.law@mayerbrown.com

Raymond Chan
+852 2843 4394
raymond.chan@mayerbrown.com

Raymond Yang
+852 2843 2295
raymond.yang@mayerbrown.com