Hogan Lovells

Arbitration highlights in the year of the dragon

March 2024

In the year of the dragon, attention turns to the enforcement of arbitral awards. We look at five different Hong Kong decisions where enforcement or set aside has been the central issue often involving arguments of public policy.

The precise status of a "re-arbitration" was considered in one; in another, a fast-moving change in the law prompted the remission of an award back to the arbitrator; an arbitrator's lack of attention to the proceedings was enough to persuade the court to set aside the award in the third; the fourth highlighted the high threshold for a court to look at "points of law" even where the parties have agreed this in their contract; and in the fifth, a claim that an arbitral award should be struck down as it offended Hong Kong's strict laws on third party funding, was also unsuccessful.

Face the music

In the long-running case of *G v X*, G claimed that it had been induced by fraud on the part of X to sell his interests in an online music business in the mainland at an undervalue of RMB 158 million. G sought to rescind the agreements for the transaction, claimed the return of the shares which had been transferred and asked for damages. The tribunal issued an award in favour of G in April 2021. The award included a substantial payment of damages.

In May 2021, X applied to the mainland court to set aside the award. G also applied to the mainland court for leave to enforce the award. After obtaining a Mareva injunction and disclosure order against X from the Hong Kong court in July 2021, G applied for leave to enforce the award in Hong Kong. X opposed G's application, claiming he had been unable to present his case in the mainland arbitration and that the award had dealt with a difference or dispute which did not fall within the terms of the submission to arbitration and that enforcement would be contrary to public policy.

On 23 September 2022, the mainland court issued a notice notifying CIETAC that the tribunal in the arbitration had collected two pieces of evidence of its own accord which the parties had not been allowed to examine. CIETAC decided to hold what the court referred to as a "re-arbitration" following which the mainland court issued a ruling in October 2022 to terminate the setting aside application.

Hearings were held on the scope of the re-arbitration and the award in the re-arbitration was issued on 17 November 2023. The new tribunal held that X remained liable to pay damages and that the new tribunal could only re-arbitrate the issue which had been identified in the notice. Finding the evidence to be "true, legal and relevant", the new tribunal declined to make any adjustments to the findings made by the original tribunal.

On 29 September 2023, X sought to rely on the developments on the mainland, including the notice and the re-arbitration decision, as a ground to resist enforcement of the award, contending that as a consequence, the award was either not "binding" or had been "suspended" under the mainland law, pursuant to section 95(2)(f) of the Arbitration Ordinance, (Cap. 609) (the Ordinance).

Under PRC law, enforcement proceedings are only suspended after the commencement of re-arbitration, but a party may apply to resume the enforcement proceedings after the tribunal rectifies the defect identified in the notice when the re-arbitration was ordered.

The Honourable Madam Justice Mimmie Chan in *G v X* [2023] HKCFI 3316 referred to the Privy Council decision in *Carter (t/a Michael Carter Partnership) v Harold Simpson Associates (Architects) Ltd* [2005] 1 WLR 919 in which the court rejected the argument that the effect of an order for remittal is to nullify the original award. The tribunal pointed out that the re-arbitration was dependent on the setting aside application and was limited in scope to the issues identified in the notice, since the original award had not been set aside by the mainland court and *"still has the force of res judicata"*.

A so-called re-arbitration only concerns corrects or mistakes in an arbitral award and is not considered a separate arbitration. *"The scope of a re-arbitration under Article 61 of the [mainland] Arbitration Law is generally limited to the flaws or defects in the arbitral proceedings as determined by the Mainland Court, rather than a re-arbitration of the entire matter. The purpose is to eliminate procedural defects identified in the award"*.

Takeaways

The decision goes to highlight the finality of an arbitral award. As Lord Sumption observed in earlier authority[1], *"an arbitration award is prima facie conclusive. The court has only limited powers of intervention. It exercises them on well-established grounds such as ....the arbitrator's failure to deal with some matter falling within the submission. The reopening by the arbitrators of findings which there were no grounds for remitting and which they had already conclusively decided would therefore have been contrary to the scheme of the Arbitration Act."*

1 *Sans Souci Ltd v VRL Services Ltd* [2012] UKPC 6

Return to sender

The ability to challenge on a point of law was also examined by the court in *G v N* [2023] HKCFI 3366. Here, a separate Hong Kong court decision had changed the law on a key point relied upon in the arbitration just days before the arbitration hearing took place. And that was enough for the judge to send the case back to the arbitrator to reconsider whether the award should be set aside.

G was a BVI-incorporated, wholly-owned subsidiary of a Hong Kong listed company. G was a shareholder in N, also a BVI entity which was a real estate developer and operator conducting its main business in the PRC mainland. An American investment fund IsZo Capital LP (ISZ) was also a shareholder in N and objected to plan agreed by the management to purchase more land in the PRC.

N arranged for an allotment of shares with a view to defeating a no-confidence vote planned by ISA and on 5 October 2020, N and G entered into a Securities Purchase Agreement (SPA) for a placement known as "PIPE" (a private investment in public equity). The SPA contained an HKIAC arbitration clause.

Upon application by ISZ, the BVI Commercial Court set aside the placement on the grounds that it was not in N's best interests, made for an improper purpose, and would be in breach of the relevant section of the BVI Business Companies Act. The decision was upheld by the BVI Court of Appeal.

G commenced arbitration against N in Hong Kong seeking restitution of the monies it had paid for the placement. During the arbitration, G was granted an interim preservation order restraining N for disposing of US$90 million of the consideration monies it was holding in a Hong Kong bank account. N argued it in its defence that G should not be allowed to recover the consideration monies since the placement was illegal and relying on the principle of unclean hands.

The arbitrator issued a first partial award on liability in which he found that the placement was illegal and dismissed G's claims, relying on the English case of *Tinsley v Milligan* [1994] 1 AC 340. He also upheld counterclaims lodged by N meaning that N was permitted to retain both the consideration it was paid and to recover damages from G. G asked the court to set aside the awards as being contrary to the public policy of Hong Kong.

Just a few days before the arbitral award was handed down, the Hong Kong Court of Appeal had handed down its decision in *Monat Investment Ltd (滿利投資有限公司) v All Person(s) in Occupation of Part of No 16 Ma Po Tsuen* [2023] 2 HKLRD 1311. In *Monat*, the Court of Appeal held that the UK Supreme Court decision in *Patel v Mirza* [2017] AC 467 represented the true state of the law on illegality in Hong Kong and that *Tinsley* should no longer be followed.

The *Patel / Monat* approach gave the court the discretion to consider a range of factors when considering whether the court should allow relief in restitution even if the underlying contract was unenforceable as it involved an illegal act such as

(i) the underlying purpose of the prohibition which has been transgressed;

(ii) any other relevant public policies which may be rendered ineffective or less effective by the denial of the claim; and

(iii) keeping in mind the possibility of overkill unless the law is applied with a due sense of proportionality.

According to *Patel*, consideration of illegality involves two stages, the first to decide whether there is any illegality in law and the second a determination of the consequences of any illegality found. The Privy Council in *Betamax v State Trading Corp* [2021] UKPC 14 had made it clear the first stage was not open to review by the court.

Counsel for G pointed out that it is open to the Court to review the decision of the arbitrator on public policy. He highlighted the fact that the question of illegality involves two distinct stages. The first stage involves the tribunal making findings of facts, and applying the law to the facts to ascertain if there is any illegality in law. The second stage then involves ascertaining the consequences of the illegality found and the court must assume jurisdiction to determine whether the award is in conflict with the public policy of the jurisdiction of the supervisory court.

The finality of the award is not affected when the role of the Court is simply to decide whether there is any conflict between public policy and the award, on the findings of law and fact made by the arbitrator which are not reviewed. Here, the arbitrator did not apply the approach advocated in *Patel v Mirza* on the basis that it was not part of Hong Kong law. The court, rather than coming to a conclusion as to whether the awards should be set aside as contrary to public policy, suspended the set-aside proceedings for three months and remitted the matter back to the arbitrator.

Takeaways

The decision in *G v N*, drawing as it does on both recent English and Privy Council authority on the interpretation of the illegality defence, underlines the long tradition of Hong Kong courts in respecting the finality of awards.

However, where a party makes an application under section 81 of the Ordinance (applying Article 34 of the Model Law) to set aside an award, or under either section 86(2)(b), 89(3)(b) or 95(3)(b) of the Ordinance to resist enforcement of an award, it is open to (and incumbent on) the party to show to the court that the award or enforcement thereof is contrary to the public policy of Hong Kong.

When such a contention is made, the court is bound to consider and decide the claim, applying the authorities which define the narrow scope of such a claim. It is not against the spirit or principles of the New York Convention or the Ordinance to do so.

Going for a song

When an arbitrator doesn't pay attention to the proceedings before him, they are at risk of having any award successfully challenged in the Hong Kong courts. That's the message from decision by the Honourable Justice Mimmie Chan J in *Song Lihua v Lee Chee Hon* [2023] HKCFI 2540.

The respondent applied to set aside enforcement of arbitral award made by the Chengdu Arbitration Commission on the grounds, among other, that it would be contrary to public policy to enforce the award in Hong Kong under section 95 of the Ordinance. The parties' lawyers and two of the three arbitrators, had attended the second hearing in person. The third arbitrator, named Q in the judgment, attended by video conference.

The respondent complained that Q had not meaningfully participated in the second hearing, moving from one location to another, indoors and outdoors. He had "eventually left his premises, and travelled in a car, without giving his undivided attention to the hearing."

The arbitrator could be seen *"inside a vehicle which appeared to be a private car as he was sitting in the front seat and adjusting his seatbelt."* At one stage, he said *"he had no reception as he was on or proceeding to the high-speed railway."* He was offline for periods of time and *"obviously could not hear what was being said by the parties' lawyers or by the other members of the tribunal"* and appeared not to be wearing an earpiece.

He was seen talking and gesturing to other people and did not seem to be paying attention to the proceedings on screen. On at least two occasions when members of the tribunal or the secretary of the tribunal attending the hearing had spoken to ask if Q could hear them, or was online, Q had made no answer at all, nor had he made any indication or gesture that he had heard the questions.

On 28 December 2022, the respondent Lee had applied to the Chengdu Intermediate People's Court to resist Song's application to enforce the award. On 16 March 2023, the mainland court rejected his application, in essence finding that Q's conduct in the arbitration caused a defect in the procedure, but did not have any actual impact on the hearing.

The right to be heard is an important procedural right under the rules of natural justice going directly to the question of fairness. Lee argued that such right to be heard encompasses not only the litigant's right of access to the courts, but also the court actually hearing the litigant.

Chan J said, having carefully reviewed the video of the second half of the second hearing, that *"the manner of Q's attendance of the 2nd hearing, by going outdoors where reception was poor, was obviously disruptive of the proceedings, to say the least."* According to Chan J, there is no apparent justice and fairness, when a member of the decision-making tribunal was not hearing and focused on hearing the parties in the course of the trial. The court granted the set aside application, despite the supervisory court on the mainland not having set aside the award and permitting its enforcement on the mainland. However, the Hong Kong courts apply their own standards of what constitutes a violation of Hong Kong public policy, which is different to public policy of the mainland.

It was argued that Lee's lawyer who attended the hearing had waived any irregularities, particularly by confirming to the tribunal at the end of the hearing that he had no objection to the procedures of the arbitration and there was no objection to the tribunal with regard to Q. The waiver argument was dismissed as the lawyer representing Lee had not noticed that Q had been moving from place to place, and had not noted all the activities of Q on the screen. Even if Lee's lawyer had failed to raise any objection at the hearing, the court held that the

ground of public policy can be raised and relied upon by the court, if it appears to the court, under s.95(3) of the Ordinance, that it would be contrary to the public policy of Hong Kong to enforce the award.

Takeaways

This is a pro-arbitration decision that upholds due process and the integrity of the arbitral proceedings. The court was of the view that the conduct of the hearing fell short of the high standards expected by the Hong Kong courts for a fair and impartial hearing, which gives recognition to the parties' fundamental and basic rights.

Public policy is often relied upon to resist enforcement of an award. The court made clear there must be *"a substantial injustice arising out of an award which [is] so shocking to the court's conscience as to render enforcement repugnant"* – which is a high standard to meet. The principle is that public confidence can only be maintained in the arbitral process where the fair and reasonable observer can see that due process has been observed in the arbitration. That is a prerequisite before the court can enforce the award as a judgment of the court.

In this case, if Q was not properly participating in the arbitration, an objective observer would have reasonable doubts as to whether Q had already made up their mind without hearing the parties and had no interest in what the parties had to say on the matter and as such, confidence in the arbitrator's judgment could be impaired. It is interesting that the mainland supervisory court had not set aside the award.

In *Hebei Import & Export Corp v Polytek Engineering Co Ltd* ([1999] 1 HKLRD 665, which also concerned the enforcement of a mainland award in Hong Kong, Litton PJ observed that *"[t]he expression public policy … is a multi-faceted concept. Woven into this concept is the principle that courts should recognise the validity of decisions of foreign arbitral tribunals as a matter of comity, and give effect to them, unless to do so would violate the most basic notions of morality and justice. It would take a very strong case before such a conclusion can be properly reached, when the facts giving rise to the allegation have been made the subject of challenge in proceedings in the supervisory jurisdiction, and such challenge has failed."*

The Court of Appeal decision *Gao Haiyan v Keeneye Holdings Ltd* [2012] 1 HKLRD 2012 illustrates a Hong Kong court's narrow and stringent interpretation of the public policy ground for refusal of enforcement of arbitral award, and deference to the supervisory court. In that case, the Court of Appeal observed that due weight must be given to the decision of the Xian Court refusing to set aside the award.

The waiver analysis by the court was also interesting. In most institutional rules, parties are deemed to have waived any procedural irregularities if they fail to object promptly. For example, Article 32.1 of the HKIAC Administered Arbitration Rules provides as follows: *"[a] party that knows, or ought reasonably to know, that any provision of, or requirement arising under, these Rules (including the arbitration agreement) has not been complied with and yet proceeds with the arbitration without promptly stating its objection to such non-compliance, shall be deemed to have waived its right to object."*

In *Gao Haiyan,* the Court of Appeal ruled that the party objecting to enforcement had waived their right to complain about what happened in the Shangri-la Hotel (the mediation that took place, and alleged bias). Parties are advised to object promptly to any procedural irregularities.

The construction of construction

An arbitration regime commonly used in the construction industry was at the centre of the disputes in *Employer v Contractor* [2023] HKCFI 2911. The award covered 24 disputes as to the contractor's entitlement to payment for items of work, the amount that should be paid in respect of those items and quantum disputes. The employer sought for leave to appeal in respect of seven points of law arising out of two of the disputes.

Under section 6(1) of the Schedule, an appeal to the court on a question of law arising out of an award may not be brought by a party to arbitral proceedings except with leave of the court. Leave to appeal will be granted only if the court is satisfied that

(a) the decision of the question will substantially affect the rights of one or more of the parties;

(b) the question is one which the tribunal was asked to decide; and

(c) on the basis of findings of fact in the award,

  (i) the decision on the question is obviously wrong; or

  (ii) the question is one of general importance and the decision of the arbitral tribunal is at least open to serious doubt (section 6(4)). The court will normally determine an application for leave to appeal without a hearing, and so a decision on these questions has to be based on what is readily apparent on the face of the award and the limited papers filed.

The seven points concerned the proper construction of General Conditions of Contract 61(1)(b) and (c), GCC 63 and GCC 50. The employer / plaintiff and respondent in the arbitration claimed that these were all standard form contract provisions used in the local construction industry, such that questions on their interpretation are matters of general importance to the industry, and that the relevant test for grant of leave to appeal should be *"at least open to serious doubt"*, a lower threshold than *"obviously wrong"*.

In deciding between the two, the courts distinguish between "one off contract" situations (where there is no general point of interest beyond the rights and liabilities of the parties concerned) and "standard term" situations (where parties have incorporated into their contracts standard terms which benefit from a uniform construction and without the need for detailed discussion or negotiation). The threshold for the latter will be the lower "open to serious doubt" test.

The Honourable Madam Justice Mimmie Chan found that the decision of the arbitrator on the questions identified could not be said to be either obviously wrong, or giving rise to "serious doubt" on the lower threshold should it be applicable. The application was dismissed.

Takeaways

It is not possible generally to appeal against arbitration awards in Hong Kong. The fact that an error of law may have been made does not provide a valid ground to refuse enforcement of an award or set it aside. Parties may however "opt in" to allow appeals on points of law by setting out in their arbitration agreement that sections 5-7 of Schedule 2 to the Ordinance will apply. The ability to appeal is not assured. A party must first obtain leave from the Court of First Instance (section 6(1) of Schedule 2). If the leave is refused, the decision may only be challenged if the question is one of "general importance" or there is some other "special reason" (section 6(6) of Schedule 2).

High maintenance

An international law firm defeated a challenge to an arbitral award where the defendant claimed the award should be set aside as being against the public policy of Hong Kong in that it involved litigation funding and therefore contravened the principles of maintenance and champerty.

In *BB v KO* [2023] HKCFI 2661, KO applied to set aside a court order granting leave to BB to enforce an arbitral award made in Chicago, Illinois, United States (U.S.) for nearly US$50 million owed in legal fees.

The enforcement order provided for leave to KO to apply to set aside the enforcement order within 28 days after service of the enforcement order on him. No application for setting aside was made within the period of 28 days, and on 29 December 2020, judgment was entered in Hong Kong in terms of the award. KO took no action until September 2022, claiming that he was not aware of the option to set aside the order until early 2023, that he had changed his lawyers and had been unwell.

Despite it being open to KO to challenge enforcement of the award in Hong Kong, without first seeking to appeal against the award or to set it aside in the U.S., it was KO's own considered decision to focus on his appeal and the proceedings in the U.S. to challenge the award, and to leave aside the resistance to enforcement proceedings already initiated by BB from March 2020 (when the Enforcement Order was made), to December 2020 when the judgment was entered. This was notwithstanding the fact that there were steps taken and orders obtained by BB in Hong Kong on the basis of the judgment, namely the Charging Order Nisi in May 2021, and the Garnishee Order in June 2022.

KO claimed that it would be contrary to the public interest of Hong Kong to enforce the award since the fees agreement related partly to litigation in Hong Kong and that the agreement was therefore champertous (the payment of costs in litigation in exchange for a share of the proceeds).

The Honourable Madam Justice Mimmie Chan J rejected the challenge since the challenge was more than two years out of time and that in any event, the client had failed to discharge the burden of proving that enforcement would be contrary to public policy.

If the arrangement were illegal or contrary to public policy, then that was something which should have been raised long before the hearing, and not in counsel skeleton submissions. KO's reliance at the hearing on the existence of Hong Kong litigation amounted to an ambush, since BB had not been given a reasonable opportunity to respond to the allegations.

Counsel for BB also argued that BB's entitlement to the contingency fee related solely to the successful outcome of the U.S. litigation commenced in the courts of Nevada. There were *"no concerns that either KO or BB would be encouraged (by reason of the agreement) to maintain, intermeddle with or game on the outcome of any judicial process in Hong Kong"*. Nor was there any clear evidence as to the status of any litigation in Hong Kong the time the agreement was made.

The court noted the words of Ribeiro PJ in *Unruh v Seeberger* [2007] 2 HKLRD 414 that *"the totality of the facts must be examined asking whether they pose a genuine risk to the integrity of the court's processes."*

Under section 89(2) of the Ordinance, it was for KO to prove that one or more of the grounds set out in section 89(2) exist, and in order for him to invoke section 89(3), KO must at least establish and prove the facts on which the court may find that enforcement of the award would be contrary to public policy. Without the necessary facts as to how the Hong Kong litigation affected the agreement, it

was *"simply not possible for the Court to evaluate and determine whether there was a genuine risk to the integrity of the process of the Court in Hong Kong"*. It was also for KO to discharge the burden of proving that enforcement of the award would be contrary to Hong Kong public policy.

Takeaways

The length of time that KO allowed to pass before bringing the challenge in Hong Kong ultimately contributed to the failure of the application. Whilst the court does have discretion to extend the time limit for challenge, it will only do so with good reason and after careful examination of the merits.

The time limit given in the Hong Kong order must be respected and it is immaterial whether challenges are being brought elsewhere in the world. Parties should bear in mind they should resist enforcement of an award promptly where enforcement applications are made, without first waiting to set it aside in the seat of arbitration.

The decision also goes to highlight the importance of ensuring that engagement letters are properly structured – had the potential litigation in Hong Kong been addressed separately, it is likely the challenge may never have got off the ground.

Contacts

James Kwan
Partner, Hong Kong
T +852 2840 5030
james.kwan@hoganlovells.com

Damon So
Partner, Hong Kong
T +852 2840 5018
damon.so@hoganlovells.com

Byron Phillips
Partner, Hong Kong
T +852 2840 5960
byron.phillips@hoganlovells.com

Janice Cheng
Partner, Hong Kong
T +852 2840 5010
janice.cheng@hoganlovells.com

Zoe Dong
Counsel, Hong Kong
T +852 2840 5610
zoe.dong@hoganlovells.com

Joyce Leung
Counsel, Hong Kong
T +852 2840 5078
joyce.leung@hoganlovells.com

Nigel Sharman
Senior Knowledge Lawyer, Hong Kong
T +852 2840 5637
nigel.sharman@hoganlovells.com

Alicante
Amsterdam
Baltimore
Beijing
Berlin
Birmingham
Boston
Brussels
Budapest*
Colorado Springs
Denver
Dubai
Dublin
Dusseldorf
Frankfurt
Hamburg
Hanoi
Ho Chi Minh City
Hong Kong
Houston
Jakarta*
Johannesburg
London
Los Angeles
Louisville
Luxembourg
Madrid
Mexico City
Miami
Milan
Minneapolis
Monterrey
Munich
New York
Northern Virginia
Paris
Philadelphia
Riyadh
Rome
San Francisco
São Paulo
Shanghai
Shanghai FTZ*
Silicon Valley
Singapore
Sydney
Tokyo
Warsaw
Washington, D.C.

*Our associated offices

www.hoganlovells.com