World Scientific Research Journal (WSRJ) ISSN: 2472-3703
www.wsr-j.org

The implications of Hong Kong arbitration for the establishment of "One Belt and One Road" arbitration institutions.

Zhi Qiao

City University of Hong Kong, China

qiaozhi89@gmail.com

Abstract: On January 23rd 2018, Xi Jinping, general secretary of the CPC Central Committee, President of the State, presided over the second meeting of the Leading Group for Deepening Overall Reform of the 19th Communist Party of China Central Committee. "The guideline on setting up a dispute-solving mechanism and institution among Belt and Road countries" has been considered and adopted at the conference. The meeting stressed: to establish the dispute settlement mechanism and institutions of "the Belt and Road", we should adhere to the principle of joint negotiation, establishment and sharing, rely on existing judicial, arbitration and mediation institutions in China, absorb and integrate domestic and foreign legal service resources, and establish a pluralistic dispute resolution mechanism that effectively links up litigation, mediation and arbitration, to properly resolve trade and investment disputes of "the Belt and Road" in accordance with the laws, and protect equally the legitimate rights and interests of both Chinese and foreign parties, thus creating a stable, fair and transparent business environment of legalization. So, how should this institution and mechanism be established? What are the areas to be paid attention to when designed and organized? Perhaps the current practice in Hong Kong can serve as a reference. As an important financial centre in the world, Hong Kong has a sound financial system, a favorable legal environment, an excellent talent pool and a free and open business environment. According to the official statement of the Hong Kong Government, Hong Kong is one of the major dispute resolution centres in the Asia-Pacific region. Hong Kong's advantage as a regional centre for dispute resolution include a sound legal system, a wealth of expertise, a superior geographical location, close networking with the mainland and governmental support. Therefore, this paper mainly focuses on the dispute settlement mechanism in Hong Kong, which focuses on the jurisdiction of Hong Kong arbitration as an example, combing the issues that should be paid attention to during the arbitration in Hong Kong.
Keywords: arbitration, Hong Kong.

1. UNDERSTANDING OF DISPUTE SETTLEMENT MECHANISM IN THE NEW ERA

In his report of the 19th CPC National Congress, Xi pointed out that comprehensively putting forward the rule of law is a profound revolution when govern the country, which shall persist in enforcing the rule of law, promoting scientific legislation, strict law enforcement, judicial justice, and compliance with laws among all the citizens. Xi also stressed the importance of opening up. He said, opening up will bring progress, while closure will inevitably make us lag behind. China's open doors will not be closed but will only grow larger. We should focus on the construction of "the Belt and Road", pay equal attention to both bringing in and going out, abide by the principle of co-discussion and co-construction and sharing, strengthen the opening and cooperation of innovation capabilities, and form an open pattern of inside and outside linkage between the land and sea and mutual aids between the east and the west. Xi's important speech organically unifies the comprehensive implementing the rule of law and accelerating modernization of national governance system and governance ability. It has pointed out the direction for us to advance the modernization of national governance system and governance capacity on the track of rule of law and realize the overall goal of comprehensively deepening the reform.

At present, the legal system of the socialism with Chinese characteristics has already been formed. Generally speaking, all aspects of the national life and social life have laws to abide by. The writer thinks that to comprehensively implementing the rule of law is the essence and crucial guarantee for developing socialism with Chinese characteristics. It is related to the governance by our Party and the prosperity of our country, the happiness and living standards of people, as well as the career development of the Party and the country. Legal construction will fulfill more missions and act more important roles than before[1].

At present, we are focusing on the construction of the legal system of socialism with Chinese characteristics and building a law-based socialist country. Under the principles of social justice and fairness, we've actively taken measures to reform and have gained major progress. For this, dispute settlement mechanism ADR is vital in legal practice. Traditional dispute settlement ADR usually refers to all the methods to settle a dispute besides lawsuit and arbitration. The methods include: negotiation, consultation, mediation, conciliation, and so on. It is a major procedure for legal governance of the country. Therefore, the selection of mechanism will affect the whole process of dispute settlement and will assert profound impact on the rights and interests of the parties concerned.

2. DISPUTE RESOLUTION CLAUSE

The dispute resolution clause is a clause in which the parties resolve the dispute in any way when the disputes occur, which reflects the embodiment of the party's autonomy. The precise and effective dispute settlement clause is an important part of the contract content, which can save the litigation cost and effectively protect the rights and interests of the parties when the contract content is in dispute.

In most contracts, the fact that the parties may disagree out of default on the either an expressed or implied term of contract. In such instances, it is upon the drafters to provide for alternative means of dispute resolution before considerations of enforcement of legal rights arising from

contracts. Alternative dispute resolution, "ADR" mechanisms have been widely appreciated as means of dispute settlement. The term alternative means that they will be alternative to the action for damages, injunction or any other court-sanctioned relief. This is often necessary to ensure trade facilitation and the conservation of relationship between parties to a contract amidst a disagreement.

The common processes that are often provided for range from Mediation, Arbitration, Litigation, and some other hybrid processes. Of these processes, Mediation is the most commonly used in commercial contracts, and it involves the introduction of a neutral third party referred to as the mediator with a primary focus on the interest of parties as opposed to the legal entitlement. The conciliatory process helps in reaching a consensus between the parties in the event of the success of its application.

A survey of corporate attitudes to international arbitration conducted by the School of International Arbitration, Queen Mary College, University of London, and PricewaterhouseCoopers in 2006 found that, of the 73% of respondents who preferred international arbitration as their dispute resolution mechanism of choice, approximately two-thirds preferred to use arbitration "in combination with ADR mechanisms in a multi-tiered, or escalating, dispute resolution process" [2].

Drafters may also consider the hybrid processes of Mediation-Arbitration to ensure that the matter is taken to a neutral third party first with an intention that should it fail, the matter be referred to an Arbitral Tribunal. In some circumstances, a narrower, more internationally recognized definition of this term refers to situations in which a party decides to employ the processes of both mediation and arbitration in a single case [3]. Craig Tevendale et al. in the article "Use of Mediation with Arbitration" has further expanded the mandatory provisions of a dispute resolution clause [4]. The authors discussed the need for an escalation clause or a multi-tiered clause as sub clauses of the dispute resolution clauses of the contracts which. This helps the parties to sort out problems arising from disputes based on the validity or the existence of the settlement agreement. Hong Kong Courts recognize Mediation-Arbitration as legitimate, given that it is provided for in the UNCITRAL Model law which is reflected in s.33(4) of the Arbitration Ordinance[5].

In addition, compared with litigation, the arbitration procedure is more flexible and convenient. The parties can choose arbitral procedures, avoid red tape and resolve disputes in a timely manner. Secondly, the tribunal hearing of arbitration is not open to the principle, that is, as long as there is no special stipulation or agreement, the arbitration is not open to public. This fully embodies the protection of commercial secrets of the parties, the maintenance of the parties' business reputation, and the principle of respecting the parties. Litigation, on the contrary, should be tried in public without a special agreement.

In some circumstances, the concern is that without proper drafting of the clauses in contracts, the objectives of coming up with a solution that is acceptable and binding upon the parties may not be met. The question, therefore, is what are the norms that the drafters ought to use in ensuring a proper dispute resolution clause in contracts? Additionally, the problem is what the

court-approved guiding principles in the drafting of dispute resolution clauses for disputants. The analysis below mainly presents a review of recent arbitration and litigation cases in Hong Kong to show the significance of the resolution clause in business contracts.

3. LITIGATION OR ARBITRATION

When drafting dispute resolution clauses, Litigation and Arbitration are the two most common approaches of dispute resolution. These clause (also known as "split clauses") are enforceable at least as a matter of Hong Kong, having been held to be a sufficiently clear submission to arbitration[6].

In the case, PCCW Global Ltd (formerly Beyond the Network Ltd) v Interactive Communications Service Ltd (formerly Vectone Ltd)[7], it was not clear on whether the parties were subject to an arbitration agreement. There was evident contradiction within the contract which demanded parties to handle their disputes through court proceedings in a way to establish whether the jurisdiction was to be affected in Hong Kong or London in clause 4.3. Clause 5 stated that, in case there is a dispute between the contracting parties, the case can only be solved by bringing the dispute to the Hong Kong courts for resolution. On the other hand, it referred disputes to arbitration on New York as provided in clause 11.3. There arose a conflict between the provisions of clause 5 and clause 11.3 since both Hong Kong and London courts and an arbitrator had jurisdiction to resolve the dispute between the two parties Beyond and Vectone.

The Court of First Instance held that, the parties agreed to submit their billing disputes to exclusive jurisdiction of courts in Hong Kong. Vectone made an appeal to the courts, with the principle point focusing on whether there was an agreement to arbitrate. The Court of Appeal held that, clause 11.3 gave a leeway for enforceable arbitration. The judge also noted that, it was evident for courts not to usurp the arbitrators' role unless the point was evidently clear and then the matter should have stayed to arbitration[8].

Pursuant to clause 11.3 which was not a binding arbitration agreement and rejected to stay in the court proceedings arguing that, although the party required the dispute to be arbitrated, there was no obligation on the other parties to accede to invitation to arbitration. The judge opined that, subject to clause 4.3, the requirements aimed at resolving the dispute effectively within a reasonably acceptable period included referring the disputes to arbitration under Clause 11.3. Since Vectone's request for arbitration came late, a period of more than 5 months after the dispute had started, the judge considered it that, Vectone had waived any of the available rights under Clause 11.3 to arbitration[9]. Vectone's application to stay litigation was also dismissed in the case.

This case highlights on the role of ensuring clarity in regard to the choice of litigation or arbitration. Whilst parties are not always mindful of the risk of disputes when negotiating and drafting their contracts, the failure to think ahead and deal with these possibilities with precise clauses could expose the parties to complex procedural arguments when disputes subsequently arise[10].

4. ENFORCEMENT OF CLAUSE

A good drafter of a dispute resolution clause must be cognizant of the difference between a legally binding clause and a clause that is enforceable on the other hand. Drafting a multi-tiered dispute resolution clause requires specific care because of various mechanisms within different steps and when drafted without sufficient consideration they bear the risk of being unenforceable because of the lack of certainty[11].

Although arbitration is a dispute resolution system based on the parties' agreement, it has its binding effect due to the legal regime consisting of international conventions, national

arbitration laws and institutional arbitration rules which improve the enforceability of both arbitration agreements and arbitral awards[12]. Article 14 of the UNCITRAL Model Law provides that upon reaching a contract, for dispute resolution, a clause should be entered describing the agreed method for the enforcement of the settlement agreement terms. This is evident in the case of *Xu Yi Hong v. Chen Ming Han & Others*[13]. That presents a case where the parties agreed to clause 9 of the contract that any dispute arising from the agreement should be referred to arbitration. The parties further provided for the arbitrator to be Xiamen Commission whose decision was to be binding on the parties.

Another typical case is Hyundai v Vigour Appeal.[14] In this case, the parties had entered into a construction contract whereby they had arbitration agreements. Dispute over the certification of the architect arose. The contractual parties verbally to settle the issue by Vigour refused the idea of negotiation except if Hyundai agrees to sign an undertaking that that would help to pursue arbitration or formal court proceedings. Due to the ultimatum, Hyundai agrees to sign the agreement form made by Vigour which stated that the contacting parties will do arbitration and will not take any case to court forever and nobody will have any right to sue the other and that parties will be mutually discussing their disputes as they arise. Having convinced Hyundai to sign the agreement that he had prepared, Vigour went block settlement negotiations making Hyundai to lose confidence that Vigour is in anyway has an intention to settle any dispute that would arise with their contract. Hyundai the commenced court proceedings seeking the declaration to the meaning of the agreement he signed.

In the first instance Reyes J held that arbitration would still hold in the arising dispute between Vigour and Hyundai, having his reasons grounded on the following: the agreement made on March was not clear that would do away with the arbitration between the contractual parties. Furthermore, the wordings of the agreement could not construe the rights of the parties to litigate in a court of law. In fact according to Reyes J held, it was n agreement to refrain from arbitration. Reyes J held, further said that the agreement signed by Hyundai in March was unenforceable. On that ground, Reyes J held Vigour did a repudiatory breach which released Hyundai from the promise to forbear arbitration.

Court of appeal later affirmed that arbitration still exist between the parties and that the agreement was signed prior was unenforceable. The decision of the Court of Appeal ascertained that bare agreement to negotiate in Hong Kong is unenforceable. Similarly, a mediation agreement which does not have well spelled out procedures is just an agreement to agree and thus is unenforceable. Hence, in order for an agreement not to arbitrate or litigate there are higher chances that such an agreement can be enforceable without more.

Some of the lessons that can be learnt from this judgment are: if any of the contractual parties wish to enforce an agreement so that it can either negotiate or mediate they he or she needs to include enough certainty of the meaning within the agreement. Additionally, one has to think so vigilantly, about the wording of the agreement.

5. PLACE OF ARBITRATION AT SPECIAL SCENARIO: HONG KONG OR MAINLAND CHINA?

In drafting the dispute settlement terms, a particular condition is the interpretation of "China" — Hong Kong or Mainland China. Since China resumed its sovereignty over Hong Kong in 1997, there is no doubt that Hong Kong is part of China, but the Basic Law also allows it to retain its legal system.[15] For arbitration, there are arguments that, the procedural laws in Hong Kong and the Mainland of China are different, and the different levels of the corresponding courts lead to different enforcement and supervision of arbitration awards. To some extent, although the arbitration agreement, prima facie, have explicitly agreed on the place of arbitration, what should be done about the issue of "China"? *Z v A and others*, is a typical case to deal with the problem.[16]

The plaintiff and the defendant have two contracts one after another, named CKD and Agency Agreement ("CKD Agreement") and Technical Cooperation Agreement respectively ("TC Agreement"). There are dispute resolution clauses referring to arbitration, in both two agreements. The CKD Agreement states that:

"In case of breach of any of the Articles of this agreement by either of the parties, both Parties agree to put best efforts to remedy by negotiations. Otherwise, those Parties agree to arbitration as per the International Chamber of Commerce and held in CHINA…"

Whereas the TC Agreement submits that:

"Any dispute, controversy or difference which may arise between the parties out of or in relation to this Agreement or for the breach thereof shall be settled amicably by the parties, but in case of failure, it shall be finally settled in CHINA by arbitration pursuant to the Rules of the International Chamber of Commerce whose award shall bind the parties hereto."

As to governing law, both agreements contain the adoption of Chinese law or the law of the People's Republic of China, with the parties being no dissent.

Then, defendant initiated the arbitration because disputes between the parties had arisen. According to the disputes resolution clauses in the agreement, the respondents filed the request for arbitration with the International Court of Arbitration ("ICC Court") of the International Chamber of Commerce ("ICC"). In the request, the defendants give three main reasons——(1)Hong Kong is a part of China; (2) an arbitration award made by ICC in Hong Kong can be enforced in Mainland China; and (3) the arbitration shall be governed by the laws of the People's Republic of China——thus, the place of arbitration should be the Hong Kong special administrative region.

The plaintiff opposed the arbitration in Hong Kong, giving that both agreements stipulate that the arbitration should be arbitrated in China and the governing law is applicable to Chinese law, it is not necessary for the ICC International Court to designate another place of arbitration.

Obviously, notwithstanding arbitration was consensual, it was precisely because of the ambiguity of the dispute resolution clauses, which led to the contradiction about the jurisdiction between the plaintiff and defendants. It was not clear whether the "Chinese law"

referred to the laws of the Mainland of China or the laws of Hong Kong, and whether the term "China" referred to the Mainland of China or Hong Kong.

The High Court held that the present case arbitration shall commence in Hong Kong rather than Mainland China and the tribunal was properly constituted. The court gives the following four principles summarized as below[17]:

(1) The parties, as rational and rational businessman, they must be aware that, at the time of agreement, China has been restored to the sovereignty of Hong Kong, and that in law and geographically, Hong Kong is a part of China;

(2) ICC arbitration on the Mainland is valid and a Mainland court has ever enforced an ICC award made on the Mainland under the New York Convention;

(3) Rational and reasonable businessmen would not have intended by their agreement to refer their dispute to arbitration by an institution, or in a place, which would render the arbitral award unenforceable, or otherwise than binding and effective;

(4) The ICC Court is entitled to determine the place of arbitration in accordance with the provisions of article 14 (now article 18) of the ICC Rules——which the parties have expressly agreed to submit to and be bound by for the purpose of the arbitration[18].

In short, for historical reasons, the relationship between Hong Kong and Mainland China, which exists under *one country two systems*, is complicated. On the one hand, the sovereignty of Hong Kong belongs to China. On the other hand, their judicial system is completely independent. Because of Hong Kong's developed commercial trading system and the perfect mature arbitration system, most parties are keen to arbitrate in Hong Kong when disputes arise. It is important, thus, to follow the principle that draft clearly and expressly the place of arbitration whether in Hong Kong or Mainland China. From this case, we can observe that where the terms of the dispute resolution clauses are unclear about the specific meaning of "China", considering the actual facts and circumstance, Hong Kong can replace the Mainland as the place of arbitration. This also reflects the judicial utmost respect for arbitration.

6. CLARIFY COMMUNICATION ADDRESS AND MODE OF SERVICE

When drafting dispute resolution clauses, there is a seemingly unimportant detail that can not be ignored, that is, a clear delivery address. In the case *Sun Tian Gang v Hong Kong & China Gas (Jilin) Ltd*,[19] the Hong Kong Court of First Instance set aside an arbitral award that was rendered in 2007 after establishing that the plaintiff in the case did not get proper notice of the arbitral proceedings and it was not able to present due to an incarceration in Mainland China. This case highlights on the significance of emphasizing on the precise communication address and mode of service in the dispute resolution clause.

Sun entered into an agreement for sale of shares in a company owned by *Sun*. Later, *China Gas* alleged that, *Sun* was in breach of a contract of the guarantee and warranties that were provided under the agreement and therefore started arbitration. Two years before the commencement of the arbitration, *Sun* had been arrested by Mainland public security officers on suspicions of

having provided false capital, and was subsequently transferred to Jilin, where he was detained in custody.

The court set aside the Award relying on Article 3(1) of the Model Law and Article 2 of the UNCITRAL Rules. *China Gas* contended that, the notice of arbitration and the Award were validly served on Sun at three different addresses and they should have been deemed received. The evidence shows that, the 1st Address and fax number was the communication address specified for Sun under clause 10.3 of the Agreement. Clauses 10.2 provide as follows (as translated):

"10.2 Any notice to be sent shall specify the communication addresses of both parties set out in clause 10.3. Any notice which clearly specifies the communication addresses of the parties in accordance with the following rules shall be regarded as formally delivered:

(a) for personal delivery, delivery to the communication address of the other party shall be regarded as delivery;

(b) for airmail, the 7th banking business day after the date of posting shall be regarded as delivery;

(c) for dispatch by fax, the time of dispatch of the fax shall be regarded as delivery."[20]

The court analyzed three modes of service one by one and established that the plaintiff was not issued proper notice of arbitral proceedings and was not able to present the case because of incarceration. The facts in the case are exceptional and they highlight that fairness and due process is necessary in the process of arbitration and they are prerequisites for recognition and enforcement of awards in Hong Kong.

From this case, we can observe that the court has a very high standard for the service of documents. The High Court recognize that it is regrettable that, in the past few years, allegations of forgery and non-executive documentation have become commonplace in Hong Kong lawsuits. The witnesses in the court were also easy to prepare, vowing to give up documents that appeared to be their signatures. Mimmie Chan J said: "I accept that these claims have to be substantiated to the requisite high degree of proof, before they are accepted by the court."[21]

Therefore, when drafting a dispute resolution clause, the drafters must make a clear agreement on the various possible service methods. Drafters shall also make a preliminary presumption on the development and change of the parties, and list the delivery addresses in detail, so that ensure the effectiveness of the arbitration results.

7. POSTSCRIPT

Evidence from the dispute resolution cases handled above shows that, failure to keenly follow the provisions of the dispute resolution clause and failure to draft the dispute resolution clause well may easily lead to pathological problems. The amount of information contained in the arbitration clause varies from contract to contract. Some parties to an arbitration clause specified in the governing rules, the number, qualifications and experience of arbitrators, the arbitrators and arbitration procedures of the language, the locations and the seat of the

arbitration and even the service model. Clarity on these issues enhances the speedy and effective dispute resolution as well as preservation of relations between parties in cases.

The year 2018 is the first year when the guidelines of the 19th National Congress of the Communist Party of China are put into practice. This year is very crucial for establishing an all-round moderately prosperous society and implementing "the 13th Five-year plan". It is also the 40th anniversary of reform and opening up. Guo Shengkun, member of the Political Bureau of the CPC Central Committee, secretary of the Central Secretariat, and secretary of the Central Political and Legal Committee, once emphasized that: we should stick to the principles of legal governance and aim at in-depth reform; we should unswervingly adhere to the legal path of socialism with Chinese characteristics. The basic principle of "good law, good governance" should be followed so as to facilitate the legal construction in China of the new time to a new level. A few days ago, "the guideline on setting up a dispute-solving mechanism and institution among Belt and Road countries" was passed at the second meeting of the Leading Group for Deepening Overall Reform of the 19th Communist Party of China Central Committee. At the beginning of the new year 2018, the key step of legalize and institutionalize the dispute settlements related to business, trade and investment under "The Belt and Road Initiative" has been taken. With mature legal system, Hong Kong boasts leading ability in dispute settlement in the world. Its experience and practice should be well referred to.

REFERENCES

[1] See Department of Justice, The Government of Hong Kong Special Administrative Region, <https://www.doj.gov.hk/eng/public/alternative.html > accessed on 23 March 2018

[2] Simon Chapman, 'Multi-tiered Dispute Resolution Clauses: Enforcing Obligations to Negotiate in Good Faith' (2010) 27 Journal of International Arbitration, Issue 1, pp. 89–98

[3] Gu Weixia, 'The delicate art of med-arb and its future institutionalisation in China' UCLA Pacific Basin Law Journal, Spring, 2014, Vol.31(2), p.97-126

[4] Alexander Oddy, Craig Tevendale, Jan O'Neill, Hannah Ambrose and Jennifer Hartzler 'Use of mediation with arbitration' <https://www.lexology.com/library/detail.aspx?g=5639e1c3-44ed-4928-9589-398519e26a84> accessed 5 November 2017

[5] Ma Justice, Brock and Denis Arbitration in Hong Kong: A Practical Guide (3rd ed. Hong Kong : Sweet & Maxwell/Thomson Reuters Hong Kong Ltd., 2014) 209

[6] ibid 221

[7] [2007] 1 HKC 327

[8] ibid para.60

[9] ibid para.67

[10] Phillip Georgiou, 'Poorly Drafted Dispute Resolution Clauses: Hong Kong Court of Appeal Attempts to Unravel the Mess' Jones Days, July 2007

[11] Klaus Peter Berger, Law and Practice of Escalation Clauses, 22 Arb. Int'l 1 (2006).

[12] Didem Kayali, 'Enforceability of Multi-Tiered Dispute Resolution Clauses' (2010) 27

Journal of International Arbitration, Issue 6, pp. 551–577
[13] [2006] 4 HKCU 1633
[14] [2004] 2 HKC 505
[15] The Basic Law of the Hong Kong Special Administrative Region of the People's Republic of China 1997, s 8
[16] [2015] 2 HKC 272
[17] ibid [33]-[37].
[18] International Chamber of Commerce Rules of Arbitration 2017, article 18 (1) : The place of the arbitration shall be fixed by the Court, unless agreed upon by the parties.
[19] [2017] 1 HKC 69
[20] ibid para.21
[21] ibid 29