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A Simple Guide to Arbitration in Hong Kong

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Introduction - What is Arbitration?

Arbitration is a method for resolving disputes between parties in private, as an alternative to litigation in the courts. The parties agree to designate an independent third party (a tribunal, comprising of one or more arbitrators) to resolve the dispute between them and to be bound by their decision.

The Arbitration Agreement

The arbitration agreement is usually incorporated as part of the contract from which the dispute arises. However, even when there is no arbitration clause in the contract in dispute, an arbitration agreement can be made after a dispute has arisen, if the parties prefer not to go to court. If there is no arbitration clause in the contract, a separate, mutual agreement is necessary, as one party cannot force another party to arbitrate a dispute, if there is no arbitration clause in the contract.

In the context of private sector building contracts, the arbitration agreement is found in clause 41.4 of the Standard Form of Building Contract (2006 Edition). For sub-contracts, the arbitration agreement is contained in clause 42.4 of the Standard Form of Nominated Sub-contract (2005 Edition).

If parties have agreed to go to arbitration, with the limited exceptions stated below, they cannot ignore the agreement by going to court, unless both parties agree. Under the Arbitration Ordinance, if one party to an arbitration agreement commences legal proceedings in any court against the other party, the latter may insist on arbitration and apply to that court to stay the court proceedings commenced.

The Hong Kong court will only refuse to stay the proceedings in one of the following situations:

- The defendant has submitted its first statement on the substance of the dispute (acknowledgement of service and application for extension of time for filing the defence not included).
- The arbitration agreement is ineffective, e.g. it is not in writing, is null and void, or is inoperative or incapable of being performed.

Common Arbitration Clauses

As stated above, to compel the other side to go to arbitration, there must be an arbitration agreement. Our experience is that much time and money is wasted if one does not have a properly drafted arbitration clause. Therefore, it is very important to get the arbitration clause right. The following clauses are commonly used :

- Arbitration clause for administered arbitration in Hong Kong:
  "Any dispute, controversy, difference or claim arising out of or relating to this contract, including the existence, validity, interpretation, performance, breach or termination thereof or any dispute regarding non-contractual obligations arising out of or relating to it shall be referred to and finally resolved by arbitration administered by the Hong Kong International Arbitration Centre under the Hong Kong International Arbitration Centre Administered Arbitration rules in force when the Notice of Arbitration is submitted. The seat of arbitration shall be Hong Kong. The number of arbitrators shall be [one or three]. The arbitration proceedings shall be conducted in [English/Chinese]."
- Arbitration clause for ad hoc arbitration in Hong Kong:
  "Any dispute, controversy or claim arising out of or relating to this contract, or the breach, termination or invalidity thereof, shall be settled by arbitration in accordance with the UNCITRAL Arbitration Rules as at present in force and as may be amended by the rest of this clause. The appointing authority shall be Hong Kong International Arbitration Centre (HKIAC). The place of arbitration shall be in Hong Kong at HKIAC. There shall only be one arbitrator. The languages to be used in the arbitral proceedings shall be [English/Chinese]."

There are many variations of arbitration clauses. Parties should seek legal advice for the drafting of tailor made clauses to suit their needs.

Hong Kong's Arbitration Ordinance

The Arbitration Ordinance (Cap 609) ("the Arbitration Ordinance") came into force on 1 June 2011. It replaced the old Arbitration Ordinance (Cap 341) ("the Old Arbitration Ordinance"). Under the Old Arbitration Ordinance, there were two distinct arbitration regimes, namely one for domestic arbitrations and the other for international arbitrations, the latter being governed by the UNCITRAL Model Law ("the Model Law"). Under the new Arbitration Ordinance, that distinction is basically abolished and there is a single regime, governed by the Model Law, subject to modifications and supplements. Arbitrations commenced before 1 June 2011 are still governed by the Old Arbitration Ordinance.

The Arbitration Ordinance is extremely user friendly, being divided into fourteen parts, which largely follow the sequence of an arbitration. Entire Articles of the Model Law are inserted into the body of the relevant section, followed by details of any modification or addition to it, so that readers can easily see whether and to what extent that Article applies in Hong Kong.

Opt-in and automatic provisions

Although the Arbitration Ordinance is largely governed by the Model Law, it does (as mentioned above) contain some additional provisions which supplement or modify the Model Law. These include, for example, provisions in Schedule 2 (which allow greater court intervention), provisions on confidentiality and provisions on arb-med.

Schedule 2 retains some of the provisions under the old domestic arbitration regime, which parties (in both domestic and international arbitrations) may opt into or which (in some circumstances) will automatically apply, unless the parties opt-out. These provisions were retained as a result of lobbying, particularly from the construction industry, which wanted to keep some of the features of the old regime. The Schedule 2 provisions will automatically apply (unless the parties expressly opt-out) to an arbitration agreement entered into before or within 6 years from commencement of the Arbitration Ordinance, if the arbitration agreement provides that it is a domestic arbitration.

The Schedule 2 provisions relate to arbitration by a sole arbitrator, consolidation of arbitrations, decisions of preliminary questions of law by the court, challenging an arbitral award on the ground of serious irregularity and appeals against arbitral awards on a question of law.

Commencement of Arbitration

The procedures to be followed to commence arbitration are frequently embodied in the arbitration agreement. Usually a written notice to the other party specifying the general nature of the dispute is sufficient. If the rules of arbitration have been chosen in the arbitration agreement, they must be followed. Unlike litigation, no special procedure is necessary for overseas service of the notice of arbitration on a foreign party. Simplicity and informality are two distinct advantages of using arbitration as a means to resolve disputes. It can be costly and time consuming to effect service of a Writ overseas. For arbitration proceedings, it is sufficient to fax or e-mail the notice, unless the arbitration agreement provides otherwise.

For example, in construction disputes, the Standard Form of Nominated Sub-Contract provides that where there is a dispute arising under the sub-contract between the main contractor and the sub-contractor, the following procedures shall be undertaken if their dispute is not settled by mediation:

- The party who wishes to refer the dispute to arbitration should give a written notice to the other party that the dispute shall be referred to arbitration in accordance with clause 42.4 of the sub-contract. The notice of the dispute will become the terms of reference of the arbitration. Care must be taken to ensure that the dispute is described in a sufficiently wide manner in the notice to enable the arbitrator to deal with all issues in dispute between the parties.

- The claimant should also propose his choice of arbitrator to the respondent for his agreement either in the notice of arbitration or by a separate notice to concur on the appointment of arbitrator.
- The respondent may counter-propose his own arbitrator. If the parties fail to reach an agreement on who to appoint or the respondent fails to respond to the notice to concur on the appointment of arbitrator, the claimant may request the appointing authority (i.e. the President or Vice-President for the time being of The Hong Kong Institute of Architects and the President or Vice-President for the time being of the Hong Kong Institute of Surveyors) to appoint an arbitrator for the parties. In other cases where no appointing authority is specified in the arbitration agreement or the appointing authority is not willing to appoint the arbitrator, the Hong Kong International Arbitration Centre (HKIAC) will make the appointment for the parties pursuant to the Arbitration Ordinance.

Unless the required qualifications and/or experience of the arbitrator are specified in the arbitration agreement, it is possible to appoint anyone (i.e. not necessarily a lawyer) as arbitrator, although a person who has training and experience as an arbitrator or experience in the field relevant to the dispute is usually preferred. If an appointment is made jointly by the Hong Kong Institute of Architects and the Hong Kong Institute of Surveyors, a surveyor or an architect who has the appropriate experience and qualifications will be appointed as arbitrator. One of our partners is on the panel of arbitrators of the Hong Kong Institute of Surveyors. For appointment by the HKIAC, an arbitrator will be appointed from their list or panel of arbitrators. Some of our partners are members on the list and panel of arbitrators of the HKIAC.

The number of arbitrators (normally one or three) is either that specified in the arbitration agreement and procedural rules adopted by the parties or, failing that, decided by the HKIAC.

Arbitration Procedures

There are no fixed procedures for the conduct of arbitration proceedings, as the process is intended to be informal. The arbitrator generally has control over the procedures. If the arbitration agreement sets out the applicable rules, the arbitrator must follow them. If none have been agreed, he may propose a well recognised set of rules to be followed by the parties. We generally recommend that parties adopt the HKIAC Domestic Arbitration Rules or the HKIAC Administered Arbitration Rules.

There is no prescribed venue for the hearing of the arbitration. The parties can agree to meet at any convenient place, such as the offices of the arbitrator or lawyers for either party. The HKIAC (at 38/F, Two Exchange Square, 8 Connaught Place, Hong Kong) also provides good facilities for arbitration hearings at reasonable charges.

The usual procedures are as follows:

- The claimant will ask the arbitrator to hold a preliminary meeting with the parties. During the preliminary meeting, the arbitrator will decide the rules to be used for the arbitration (if none have been agreed), his fee structure (if this has not already been agreed) and most importantly, the timetable for service of pleadings, exchange of lists of documents and exchange of witness statements.
- Pleadings are usually similar to those used in court proceedings, except that the style can be less formal and in many cases, supporting documents will be annexed to the pleadings to assist each party to understand the other's case. This also saves considerable time and dispenses with the need for formal discovery.
- The exchange of lists of documents can be limited to certain types of documents or can be completely dispensed with, where the parties have annexed all supporting documents to their pleadings. We normally recommend dispensing with court style discovery so as to reduce the time and cost of resolving the dispute.

- Either party may ask the arbitrator to fix a date for the main hearing at any time. It may be fixed at a directions hearing before the arbitrator. Usually, the main hearing will be fixed after the completion of document submission or whenever the parties are ready for it. It is also possible for the parties to agree to a "documents-only arbitration" i.e. without a hearing. This may be appropriate where only the law is in dispute, rather than the facts.
- It is usual in most arbitrations for evidence (both factual and expert) to be exchanged in advance of the hearing. The arbitrator may direct that the experts meet to see if there is common ground, or if facts can be agreed. The parties' opening submissions may also be exchanged in advance of the hearing. These measures can frequently reduce the time required for the arbitration hearing, with possible cost savings.
- After considering the evidence and the parties' submissions, the arbitrator will make an award, which may be provided with or without reasons, depending on the prior request of the parties. The arbitrator will also deal with the question of the costs of the arbitration after considering submissions from both parties. Typically the losing party will have to bear the costs reasonably incurred by the winning party and the arbitrator's fees. The arbitrator will take into account whether the losing party has made any settlement offer.
- The arbitrator's award is final and binding, although an appeal to the court can be made if the arbitration agreement falls within one of those types set out in sections 99 to 101 of the Arbitration Ordinance. This includes an arbitration agreement in a construction contract, in which case either party may apply for leave to appeal against the award on a question of law, unless the parties agreed to opt out of the right to appeal. It should be noted that leave to appeal will only be granted if the conditions set out in paragraph 6 of Schedule 2 to the Arbitration Ordinance are satisfied.
- Apart from an appeal, the only other recourse against an arbitral award is an application to the Court to set it aside, pursuant to section 81 of the Arbitration Ordinance (see "Challenging the Arbitration Award" below). The Court will not examine the merits of the case and the grounds for setting aside are all related to questions of procedural fairness or public policy issues.
- The legal costs awarded by the arbitrator are subject to taxation either by the arbitrator or the court. Taxation is a process used in litigation by which the court assesses a fair amount of legal costs to be paid by the losing party. As a rule of thumb, the "taxed costs" will be about two-thirds of the actual costs spent by the winning party in the arbitration. Unlike court proceedings, where generally the parties are not charged for the service of judges or the provision of the courtroom, arbitrators require the parties to pay, usually on an hourly basis. From our experience, arbitrators on average may charge HK$5,000 to HK$6,000 per hour. Until an award on costs has been made, both parties normally bear half of the interim fees of the arbitrator.

Court support but minimal intervention

The Hong Kong Government's policy has been to encourage arbitration as an alternative dispute resolution method and the Arbitration Ordinance states that its purpose is to facilitate the fair and speedy resolution of disputes by arbitration without unnecessary expense.

There is a specialist list in the High Court, Court of First Instance, called the Construction and Arbitration List which deals with applications under the Arbitration Ordinance.

One of the purposes of the Arbitration Ordinance and adoption of the Model law was to reduce court supervision and intervention and it does this by giving the arbitral tribunal as much power as possible. The Arbitration Ordinance is stated to be based on the principles that, subject to safeguards necessary in the public interests, parties are free to agree on how a dispute should be resolved and that the court should only interfere in the arbitration as expressly provided in the Ordinance.

The arbitral tribunal is empowered to grant interim measures pending determination of disputes, including injunctions to maintain or restore the status quo and preserve assets and evidence.

The Arbitration Ordinance also includes a section setting out general powers exercisable by the arbitral tribunal (unless otherwise agreed by the parties), which include:-

- Requiring a claimant to give security for costs of the arbitration.
- Directing the discovery of documents or delivery of interrogatories.
- Directing evidence to be given by affidavit.
- Directing inspection, photographing, preservation, custody, sale or sample-taking, observation or experiments on any relevant property.

What is the Court's role?

The Arbitration Ordinance states that the court cannot intervene in arbitration proceedings, except as provided for in the Ordinance. The court's role is basically limited to the following:-

- Staying court proceedings in favour of arbitration where the matter is subject to an arbitration agreement.
- Ruling on challenges to the appointment of an arbitrator.
- Granting interim protective measures, such as injunctions (although the court may decline to do so where the interim measure is currently the subject of arbitral proceedings or considers it more appropriate for the interim measure to be granted by the arbitral tribunal).
- Assisting in the taking of evidence, for example, by ordering a witness to attend arbitration proceedings to give evidence or produce documents.
- Determining the arbitral tribunal's fees in the event of a dispute.
- Granting an extension of time to commence arbitration proceedings (where an arbitral tribunal has not already been appointed).
- Determining matters under the Schedule 2 opt-in provisions (referred to above).
- Setting aside arbitral awards.
- Enforcing arbitral awards.

Challenging the Arbitration Award

The Arbitration Ordinance provides the limited circumstances in which an arbitral award may be set aside by the court, namely:-

i. incapacity of a party;

ii. invalidity of the arbitration agreement;

iii. a party not given proper notice of the appointment of an arbitrator or the arbitral proceedings or otherwise being unable to present his case;

iv. the award dealing with a dispute not falling within the terms or scope of the submission to arbitration;

v. the composition of the arbitral tribunal or the arbitral procedure not being in accordance with the parties' agreement or Hong Kong law;

vi. the subject matter of the dispute not being capable of settlement by arbitration under Hong Kong law; or

vii. the award being in conflict with Hong Kong's public policy.

The Schedule 2 opt-in provisions (referred to above) also provide for applications to the court to challenge an award on the ground of serious irregularity and for appeals to the court on questions of law.

Enforcement of the Arbitration Award

Section 84 of the Arbitration Ordinance states that, with the court's leave, an arbitration award, whether made in or outside Hong Kong may, except in very limited circumstances, be enforced in the same manner as a judgment of the High Court.

As Hong Kong is a party to the "1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards" by virtue of China's accession to that treaty, an award obtained in Hong Kong is enforceable in other countries that are signatories to the New York Convention.

If the losing party has no assets in Hong Kong but does in another jurisdiction, an arbitration award may be more valuable than a court judgment, if the country where the assets of the losing party are situated has no reciprocal judgment enforcement arrangement with Hong Kong, but is a signatory to the New York Convention. Notably, such countries include the United Kingdom, the United States of America and Japan, Hong Kong's three major trading partners.

Enforcement in Mainland China

Since 1 July 1997, when sovereignty of Hong Kong returned to China, Hong Kong arbitration awards have become domestic awards, for the purposes of enforcement within China and enforcement of awards can no longer be through the New York Convention. Accordingly, an agreement for mutual recognition and enforcement of arbitration awards between Hong Kong and Mainland China (the Agreement) was signed on 21 June 1999 which essentially reflects the provisions in the New York Convention in addition to restoring enforcement procedures in place prior to the handover.

The Supreme People's Court of China promulgated a notice for implementing the Agreement with effect from 1 February 2000. Pursuant to the notice, there are only limited grounds for refusing to enforce a Hong Kong award, which mirror the grounds for refusal in the New York Convention. The most controversial of these is that an award will not be enforced if the enforcement would be contrary to the social and public interests of Mainland China. If the losing party is a state-owned company, such a defence may be raised. However, a defendant could just as easily raise the defence of state immunity in court, so it is a problem that may have to be faced in litigation, as well as arbitration.

Applications for the recognition and enforcement of foreign arbitral awards should be filed with the Intermediate People's Court in the place where the Respondent is domiciled or has property. If the place where the Respondent is domiciled or the place where the Respondent has property falls within the jurisdiction of different Intermediate People's Courts, the applicant may apply to any People's Court, but is not permitted to apply to more than one.

One major limitation under the Agreement (which is not found in the New York Convention) is that the applicant is not permitted to file applications in both Hong Kong and Mainland China at the same time. Only when the result of enforcement of the award by the court of one place is insufficient to satisfy the liabilities, may the applicant apply to the court in the other place for enforcement of the outstanding liabilities. This restriction may pose difficulties to an applicant when choosing the jurisdiction in which to first file the application.

It should be noted that the time limits for applying to enforce arbitration awards are different in Hong Kong and Mainland China. In Hong Kong, it is 6 years from the date when the other party fails to fulfil its obligations under the award, but in Mainland China, the corresponding time limit is 2 years.

Costs and Expenses

Although legal representation is not required in arbitration, parties often retain lawyers to represent them, especially in complicated disputes. Sometimes, lawyers will be involved when interlocutory matters arise, which have to be dealt with by the Construction and Arbitration division of the High Court of Hong Kong.

As with litigation, we charge on an hourly basis. The cost of arbitration varies greatly, depending on the size and complexity of the claim and defence. In appropriate cases, we can agree to charge a fixed amount up to a particular stage of the proceedings, regardless of the actual time spent, so that clients can have a definite budget for the proceedings.

Arbitrators usually charge on an hourly basis, although during a hearing it may be on a daily basis. As discussed above, their rates normally range from HK$5,000 to HK$6,000 per hour, depending on experience and expertise. Some arbitrators also charge a lump sum fee for their initial appointment, which is not refundable, even if the dispute is later settled without involving the arbitrator.

If the appointing authorities are involved, they will charge a nomination fee. The HKIAC's current nomination fee is HK$8,000.

Some lawyers argue that arbitration is not necessarily cheaper than litigation, bearing in mind that the court does not charge substantial fees, but the arbitrator may. While we agree to a certain extent, one should note that the progress of an arbitration can be faster than court proceedings because the arbitrator's directions can be obtained more quickly than the court's directions. Applications for interlocutory matters can frequently be dealt with by correspondence, and an earlier hearing date can usually be obtained with an arbitrator. These savings in time usually mean savings in costs, and we believe arbitration is generally more cost-effective than traditional court proceedings. Also of particular importance, especially for technical disputes, is the fact that the parties are free to select their arbitrator(s), with qualifications and experience relevant to the dispute. One cannot, however, choose their own judge for court proceedings.

Hong Kong as an arbitration venue

Hong Kong is a popular arbitration venue for many reasons, including the following:-

- Hong Kong's Arbitration Ordinance, provides a user-friendly, legal framework for arbitrations which, having largely adopted the UNCITRAL Model Law, cements Hong Kong as a leading arbitration venue.
- Arbitration awards made in Hong Kong are enforceable in almost 150 countries under the New York Convention and in Mainland China under the "Arrangement Concerning Mutual Enforcement of Arbitral Awards between the Mainland and the Hong Kong Special Administrative Region."
- Hong Kong is a common law jurisdiction, which preserves the rule of law, administered by an independent judiciary.
- Hong Kong Courts are supportive of arbitration, but take a "hands off" approach.
- Hong Kong is conveniently located for Mainland China-related disputes and easily accessible from anywhere in the world. Its highly efficient airport, a 20 minute ride away on the "Airport Express" from the Central business district, makes it an easy place to travel to and from.
- Hong Kong is one of the world's leading financial centres, with a highly developed transportation network, excellent accommodation and telecommunications.
- There are minimal language difficulties, as English and Chinese are both official languages.
- There is a huge pool of multi-lingual professionals available to act as arbitrators, although parties are free to choose arbitrators from anywhere in the world.
- There are excellent facilities and support services provided by Hong Kong International Arbitration Centre ("HKIAC").

Other Alternative Dispute Resolution methods

In recent years, other methods of dispute resolution such as mediation and adjudication, have been developed as an alternative to litigation and arbitration.

Mediation is used in the Standard Form of Building Contract (2006 Edition) and in Hong Kong Government construction projects. Mediation is a voluntary procedure in which a trained and impartial third person (called a mediator) helps the parties settle their dispute. The mediator assists the parties to discuss the issues in dispute, identify their real needs and interests, explore possible settlement options and reach a settlement agreement. If the mediation results in a settlement, a settlement agreement will be drawn up containing the agreed terms and, once signed by the parties, will be legally binding. A characteristic of mediation is that the approach is not confrontational, and thus parties who wish to maintain their commercial relationship may elect to mediate. With the assistance of the mediator, parties can reach a settlement by exploring different options which may not be available in litigation or arbitration.

Since the implementation of Civil Justice Reform in Hong Kong in 2009, parties to litigation must attempt to settle their disputes by mediation. Otherwise, adverse costs orders may be made against the parties who unreasonably refused to mediate, regardless of the outcome of the litigation.

Adjudication is a dispute resolution mechanism which involves an independent third person (usually an expert) considering the claims of both parties and making a decision. Adjudication was adopted by the Airport Authority to resolve disputes under its contracts when building Hong Kong's new international airport in the 1990's. We understand that the Hong Kong Government is considering using adjudication in all of its construction contracts on the New Engineering Contract (NEC) Forms. The adjudicator issues a binding decision that may only be challenged in arbitration after completion of the works, meaning that the adjudication process has the advantage of being relatively quick and the parties need not divert too many resources from the project to resolve disputes, which could affect its progress.

Want to know more?

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