(1) Concerns Raised by the Construction Industry on the Proposed Arbitration Regime and (2) Comparison of Specific Provisions in the Arbitration Bill with International Arbitration Practices

I. Introduction

Following request of Members at the first meeting of the Bills Committee of the Legislative Council held on 28 July 2009, this paper sets out the following matters:

(a) the concerns raised by the construction industry on the proposed arbitration regime during the consultation period of the draft Bill; and
(b) the differences between the provisions of the Arbitration Bill and the international arbitration practices with regard to confidentiality in arbitral proceedings and the enforcement of arbitral awards.

II. Concerns raised by the construction industry

2. The major concern raised by the Hong Kong Construction Association ("HKCA") is reflected in paragraph 11.10 of the Consultation Paper on Reform of the Law of Arbitration in Hong Kong and draft Arbitration Bill ("the Consultation Paper") about the "opting-in" system in respect of domestic arbitration regime as provided in Schedule 3 of the draft Bill[1]. HKCA supported the automatic application of the opting-in provisions in sub-contracting cases. It also advocates that there should be no distinction between local and overseas sub-contractors. HKCA stated that:

> *"We fully support the idea of the Opt-in provisions for the matters set out in Schedule 3 [of the draft Bill]. We consider that these provisions are very important for stability and continuity of Domestic Arbitration in*

[1] Unless indicated otherwise, all references in paragraphs 2 - 5 and 19 - 21 of this paper are to the draft Bill attached to the Consultation Paper. Readers should refer to the Consultation Paper and the draft Bill for details. The decisions of the Administration on the issues covered in these paragraphs are reflected in the Arbitration Bill introduced to the Legislative Council on 8 July 2009.

Hong Kong.

We also support the automatic Opt-in provisions in Clause 102 [of the draft Bill] with one exception. We originally put forward the proposal that there should be an automatic opt-in so that contractors and sub-contractors would not be taken by surprise by the changes in the law. During the drafting, we were consulted as to whether the automatic opt-in could apply for a transitional period of 6 years and we agree with this. This period should give all users of arbitration sufficient time to revise their standard forms of contract and also to make them aware of the need to include express opt-in provisions in their bespoke contracts.

The exception we refer to is the exclusion from the automatic opt-in system of arbitration agreements which have international aspects to them as set out in Clause 102(2) [of the draft Bill]. We firmly believe that there should be no exception from the law for suppliers and sub-contractors who may be from overseas but nevertheless do business with Hong Kong companies. It must be assumed that those doing business in Hong Kong or supplying goods for incorporation in projects in Hong Kong will make themselves knowledgeable of Hong Kong law. If they do this then they will be free to expressly exclude the automatic opt-in provisions and this we believe is sufficient protection for them."

3. The submissions received during the consultation period are overwhelmingly against the proposal. Clause 102 of the draft Bill is criticised as creating a complicated system under which sub-contractors would be deemed to have opted-in to the provisions in Schedule 3 of the draft Bill. The reasons for objections are threefold. Firstly, it is against party autonomy. Secondly, this is unnecessary given that most of the sub-contract situations may be covered by the original Clause 101 of the draft Bill. Main contractors may also apply the Schedule 3 provisions to sub-contracts if they wish to do so by using Clause 100 of the draft Bill. Thirdly, there is an arbitrary distinction between the application of the provision to local and overseas sub-contractors.

4. The arguments for keeping Clause 102 of the draft Bill were also considered. Firstly, the whole purpose of Schedule 3 of the draft Bill is to retain the status quo of "domestic" and "international" arbitrations for sub-contractors and it should not constitute a reason against the proposal under Clause 102 of the draft Bill. Secondly, it could be argued that there is no erosion of party autonomy as Clause 102 of the draft Bill would only apply if there is an arbitration agreement in the sub-contract. Thirdly, a sub-contractor who has knowledge of the change in the law may choose to opt-out of Schedule 3 of the draft Bill.

5. It was agreed by an overwhelming majority of the members of the Working Group that Clause 102 of the draft Bill should be deleted. Having balanced the different views expressed, the Administration agreed to the recommendation of the Working Group and decided to delete Clause 102 and cross references to it in the draft Bill.

III. Differences between provisions of the Arbitration Bill and international arbitration practices with regard to confidentiality in arbitral proceedings and the enforcement of arbitral awards

Confidentiality in arbitral proceedings

6. The Model Law is silent on the issue of confidentiality. Only very few national laws have addressed confidentiality[2]. Although parties involved in international arbitration proceedings were becoming increasingly concerned over the absence of any rules in respect of confidentiality, it seems that "*there was little likelihood of achieving anything more than a rule to the effect that "arbitration is confidential except where disclosure is required by law' "*[3].

7. In Hong Kong, Section 2D of the Arbitration Ordinance (Cap. 341) enables a party to apply for the proceedings before the court to be heard otherwise than in open court. Section 2D provides that:

> *"Proceedings under this Ordinance in the Court or Court of Appeal shall on the application of any party to the proceedings be heard otherwise than in open court."*

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[2] United Nations Commission on International Trade Law (1999) *Possible Future Work in the Area of International Commercial Arbitration*, A/CN9/460, para 64.

[3] *Report of the Untied Nations Commission on International Trade Law on the Work of its 32nd Session*, Supplement No. 17 (A/54/17) (1999), para 359.

It permits the application under the Ordinance to be heard *in camera*, thus preserving privacy in the arbitration process. According to Robert Morgan, Section 2D has the following effect:

> *"It appears from the wording of this section that the relevant court has no discretion as to whether to grant an application for an in camera hearing"*[4].

8. In contrast, Clause 16 of the Bill proposes as follows:

> "*(1) Subject to subsection (2), proceedings under this Ordinance in the court are to be heard otherwise than in open court.*
> *(2) The court may order those proceedings to be heard in open court –*
> *(a) on the application of any party; or*
> *(b) if, in any particular case, the court is satisfied that those proceedings ought to be heard in open court.*"

9. The Administration has taken into account the requirement to balance the need to protect the confidentiality of arbitral proceedings as a consensual method of dispute resolution on the one hand and the public interest in having transparency of process and public accountability of the judicial system on the other. Clause 16 provides, as the starting position, that court proceedings relating to arbitration are to be heard otherwise than in open court. If enacted in its current from, Hong Kong will be the first jurisdiction to take such a step to protect the confidentiality of parties involved in arbitration. The Administration is of the view that one of the main reasons that parties choose to settle disputes by arbitration is confidentiality.

10. The Administration considers that Clause 16 is an improvement over section 2D of the Arbitration Ordinance in the following manners:

> (a) whereas the court has no discretion but to grant an application for an in camera hearing under section 2D upon an application by a party to the arbitral proceedings, the court now under Clause 16 **may** order those proceedings to be heard

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[4] Robert Morgan (1996) *The Arbitration Ordinance of Hong Kong – A Commentary*, at para [2D.03]

in open court despite the starting position provided for in that section;

(b) apart from an application of any party, the court may on its own initiative order those proceedings to be heard in open court if the court is satisfied that those proceedings ought to be heard in open court.

The enforcement of arbitral awards

11. Under the current Arbitration Ordinance (Cap 341), an award made in the Mainland by a recognized Mainland arbitral authority ("the Mainland award"), and an award made in a State or territory (other than China) which is a party to the New York Convention ("Convention award"), can be enforced as provided for in Part IIIA and Part IV respectively of the current Ordinance. An arbitral award which is neither a Mainland award nor a Convention award is enforceable at the discretion of the Court of First Instance pursuant to section 2GG of the current Ordinance[5].

12. The New York Convention is an international convention which secures to a considerable degree of uniformity the recognition and enforcement of awards in most of the important trading countries of the world. What was achieved by the New York Convention has been described as follows:

> *"The New York Convention […] was a substantial improvement [...] since it provides for a more simple and effective method of obtaining recognition and enforcement of foreign awards. The Convention […] again constitutes a substantial improvement as it gives much wider effect to the validity of arbitration agreements […]. As a result, and deservedly, the New York Convention has been praised in glowing terms. It has been described as 'the single most important pillar on which the edifice of international arbitration rests' and as a Convention which 'perhaps could lay claim to be the most effective*

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[5] Section 2GG of the current Ordinance provides as follows:

"(1) An award, order of direction made or given in or in relation to arbitration proceedings by an arbitral tribunal is enforceable in the same way as a judgment, order or direction of the Court that has the same effect, but only with the leave of the Court of a judge of the Court. It that leave is given, the Court or judge may enter judgment in terms of the award, order or direction."

instance of international legislation in the entire history of commercial law'."[6]

13. An award made under the New York Convention is enforceable in Hong Kong except for limited and exclusive technical grounds for resisting its enforcement as set out in the current Ordinance[7]. The same applied to the enforcement of Mainland awards, which are governed by rules based upon and almost identical to the New York Convention.

14. Article 35 of the Model Law deals with the recognition and enforcement of arbitral awards in an international commercial arbitration. Article 36 of the Model Law sets out the grounds on which an enforcement court can refuse the recognition and enforcement of an arbitral award. The court is obliged to recognise and enforce such an arbitral award unless one of the grounds for refusing recognition and enforcement referred to in Article 36 of the Model Law is established.

15. A comparison of the adoption of Articles 35 and 36 of the Model Law shows that some adopting states give preference to the New York Convention over the recognition and enforcement provisions of the Model Law. Examples can be found in Germany (s.1061(6) of the German Code of Civil Procedure), Lithuania and Peru. An indirect way of achieving the same result is applied by California and Texas, in the Untied States, whose arbitration laws make no mention whatsoever of recognition and enforcement of arbitral award, leaving the New York Convention as the only instrument on the issue[8]. The Administration took the view that Articles 35 and 36 of the Model Law should not apply to Hong Kong. Instead the statutory scheme under the current Ordinance, which is based on the New York Convention and the arrangement concluded with the Mainland should be adopted and retained in the Bill.

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6 Alan Redfern and Martin Hunter (2004, 4th Ed.), *Law and Practice of International Commercial Arbitration*, para 10-23.

7 The application of the New York Convention in Hong Kong is described as follows: *"The Arbitration Ordinance adopts a pro-enforcement stance towards Convention awards. With rare exceptions, the High Court exercises a discretion in favour of enforcement. The discretion will be exercised in this manner unless the rights of the party seeking to resist enforcement can be shown to have been violated in a material way […]. The object of the Ordinance, in view of the High Court, is to discourage opposition to enforcement based on unmeritorious technical points and to uphold Convention awards except where complaints of substance can be made good."* (from *Halsbury's Laws of Hong Kong* (2008 Reissue) Vol 1(2) [25.199])

8 Please see the discussion in Peter Binder (2005, 2nd ed.*) International Commercial Arbitration in UNCITRAL Model Law Jurisdictions*, Sweet & Maxwell, p 282-3. Furthermore, it is stated in Peter Binder's comparison chart that instead of the adoption of Article 35 of the Model Law, the sates of Belarus, Bulgaria, Greece and Spain only make 'reference to the 1958 New York Convention'. (*ibid*, pp. 430-1)

16. The procedures for the enforcement of Mainland awards and Convention awards under the Bill remain the same as those found in the current Ordinance. Clause 95 proposes to re-enact Section 40E of the current Ordinance which provides that the enforcement of a Mainland award shall not be refused except on any of the grounds specified in that provision. Clause 89 proposes to re-enact Section 44 of the current Ordinance which provides that the enforcement of a Convention award shall not be refused except on any of the grounds specified in that provision.

17. An application can also be made to the Hong Kong courts under section 2GG of the current Ordinance to enforce an arbitral award which is neither a Mainland award nor a Convention award. Section 2GG applies to awards made in Taiwan, Macau and other jurisdictions which are not parties to the New York Convention. The operation of Section 2GG is described as follows:

> *"Since New York Convention has no application to non-Convention awards, the presumption in favour of enforcement which underlines the enforcement of New York Convention awards under section 44 of the current Ordinance does not, however, apply. A respondent may apply to set aside the order for leave to enforce, but the Hong Kong courts will only refuse to enforce a foreign award in limited circumstances reflecting the grounds on which the Hong Kong courts will set aside an international arbitral award under Article 34 of the Model Law.*[9]*"*

18. Clause 84 of the Bill provides that an award, whether made in or outside Hong Kong in arbitral proceedings by an arbitral tribunal is enforceable in the same manner as a judgment of the Court that has the same effect, but only with the leave of the Court. It regulates the enforcement of an arbitral award made outside Hong Kong which is neither a Convention award nor a Mainland award. Clause 86 of the Bill proposes that the enforcement of such an award may be refused on any of the grounds specified in that provision. Those grounds for refusal are almost identical to the New York Convention. But Clause 86(2)(c) of the Bill proposes to give the court a discretion to refuse the enforcement of an arbitration award if 'for any other reason the court considers it just to

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[9] Hon. Mr Justice Ma (ed.) (2003*) Arbitration in Hong Kong: A Practical Guide*, Thomson, para 15-31.

do so'.

19. The draft Bill attached to *The Consultation Paper on Reform of the Law of Arbitration in Hong Kong and draft Arbitration Bill* contains a provision that has been added as Clause 85(2). That clause states that no leave shall be granted by the court unless the party seeking to enforce such award can demonstrate that the court in the place where the award is made will act reciprocally in respect of awards made in Hong Kong. The adding of the reciprocity requirement was intended to ensure that the enforcement of arbitral awards made outside Hong Kong, whether a Convention award, a Mainland award or an award which is neither a Convention award nor a Mainland award, are all granted on the same principle, namely that there would be reciprocity of enforcement of an award made by an arbitral tribunal in Hong Kong in the corresponding place, state or territory where the arbitral award sought to be enforced in Hong Kong is made.

20. It is noted that under section 2GG of the current Arbitration Ordinance (Cap. 341), the court in Hong Kong could enforce an arbitral award made in Taiwan without proof of reciprocity. There is a reciprocity requirement in the relevant Taiwan legislation for the enforcement of foreign arbitral awards. The courts in Taiwan might refuse to enforce a Hong Kong award on the ground that the requirement for reciprocity in the relevant Taiwan legislation is not met if the Bill imposes a reciprocity requirement.

21. The Working Group was of the view that the requirement for reciprocity in Clause 85(2) of the draft Bill in the Consultation Paper may carry a risk that Hong Kong arbitral awards might be refused recognition and enforcement in an overseas jurisdiction which is not a party to the New York Convention. The Working Group suggested that Clause 85(2) be deleted. The Administration agreed with the Working Group and adopted its suggestion.

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