CHINA STATE CONSTRUCTION ENGINEERING CORP GUANGDONG BRANCH v MADIFORD LTD - [1992] 1 HKC 320

HIGH COURT
KAPLAN J

ACTION NO 6563 OF 1991

2 March 1992

Arbitration -- Stay of proceedings -- Scope of arbitration clause -- Whether UNCITRAL Model Law applies -- Effect of Arbitration (Amendment No 2) Ordinance 1989 s 26 -- Forum non conveniens -- Arbitration Ordinance (Cap 341) s 6A -- Arbitration (Amendment No 2) Ordinance 1989 s 26

Words and Phrases -- 'An arbitration commenced' -- Arbitration (Amendment No 2) Ordinance 1989 s 26

By a labour services agreement, the plaintiffs agreed to supply to the defendants the services of a number of Chinese construction workers to carry out works in Libya. The agreement provided that 'in case of any incompleteness of the contract, both parties shall reach settlement through friendly consultations.If settlement cannot be reached through consultations, the matter may be submitted for arbitration ...'.

A dispute arose between the parties. The defendants admitted that the amount claimed by the plaintiffs was correct but contended that it was a condition precedent that the payment would only be made after the contra-account had been settled. The plaintiff issued a writ which was duly acknowledged. The defendant issued a summons seeking a stay of the proceeding relying on the arbitration clause in the agreement and the alternative ground of forum non conveniens. The defendant having taken no steps for an interim stay, the plaintiff obtained a judgment in default. The defendant applied for setting aside the judgment and a continuation of the stay proceedings.

Held, setting aside the judment and granting the stay:

(1) The court was satisfied that the defendant had a real prospect of success as the settlement agreement was clear enough that there was a condition precedent to the payment of the claim to the plaintiff only after the contra-account had been settled. Accordingly, the judgment was set aside on the basis that the defendant paid all the costs thrown away. *The Saudi Eagle*[1986] 2 Lloyd's Rep 221 applied.

(2) The word 'incompleteness' was wide enough to cover a failure of a party to perform the contract.

(3) Once one party or the other has opted for arbitration, the other party is obliged to honour the agreement to arbitrate.If both parties agreed not to arbitrate but to litigate, they would be perfectly free to do so but the permissive word 'may' does not entitle the plaintiff to negate the defendant's wish to arbitrate. In this context, the word 'may' in effect means 'shall'.

(4) The proceedings should be stayed as this was clearly a non-domestic arbitration agreement within the meaning of s 6A(3) of the Arbitration Ordinance.

(5) The whole thrust of s 26 of the Arbitration (Amendment No 2) Ordinance 1989 was to ensure that the UNCITRAL Model Law did not apply to arbitration

agreements entered into before 6 April 1990. The three exceptions in s 26(2) do not relate to the Model Law as such but to conciliation, reporting restrictions and the rules of evidence. The phrase 'an arbitration commenced' in s 26 of the Arbitration (Amendment No 2) Ordinance 1989 has to be read as importing the meaning 'an arbitration commenced or to be commenced'. To

fail to give this interpretation would run counter to the clear intent of the legislature which was to ensure that arbitration agreements before 6 April 1990 would fall to be decided under the law which existed at the time the agreement was entered into.

(6) Had a stay under s 6A not been appropriate, the court would have granted a stay on the ground that there was some other available forum which was clearly more appropriate for the trial of this action and there were no circumstances, by reason of which justice required, that a stay should nevertheless be refused. *The Spiliada* [1987] 1 Lloyd's Rep 1 followed.

Cases referred to

Continental Corp (No 2) v Vincenzo Fedele [1964] HKLR 213

Cravat Export Co v Taiwan Power Co (USDC Eastern District of Kentucky, CA 90-11, 5 March 1990, unreported) default

Hobbs Padgett v JC Kirkland [1969] 2 Lloyd's Rep 547

Mitsubishi Case [1985]473 US 614

Saudi Eagle, The; Alpine Bulk Transport Co v Saudi Eagle Shipping Co [1986] 2 Lloyd's Rep 221

Spiliada, The; Spiliada Maritime Corp v Cansulex [1987] 1 Lloyd's Rep 1

Legislation referred to

(HK) Arbitration Ordinance (Cap 341) s 6A

(HK) Arbitration Ordinance (1990 reprint) s 31

(HK) Arbitration (Amendment No 2) Ordinance 1989 s 26

(HK) Rules of the Supreme Court O 14

Other legislation referred to

Davis, Benjamin G, ' Pathological Clauses: Frederic Eisemann's still vital criteria' Arbitration International Vol 7 No 4/1991 p 365 -

UNCITRAL Model Law art 8

Summons

This was an application by the defendant seeking to set aside of the default judgment obtained by the plaintiff and continuation of the stay of the proceedings pending arbitration. The facts appear sufficiently in the following judgment.

Mark Pierrepont (Victor Chu & Co) for the plaintiff.

Ambrose Ho (Peter C Wong, Chow, Hui Bon Hoa) for the defendant.

KAPLAN J

I have before me three summonses, two of which raise interesting points under the Arbitration Ordinance (Cap 341).

In this action, the plaintiffs claim US$119,019.12 together with interest under a labour services agreement dated 9 April 1984 by which the

plaintiffs agreed to supply to the defendants the services of a number of Chinese construction workers to carry out certain works in Libya. The defendants admit that the US dollar figure claimed is correct but contend that it is a condition precedent for the payment of the sum that payment would only be made after the

defendants' accounts with the plaintiffs' head office/management office in Libya had been settled.This is said to be the effect of a settlement agreement dated 20 February 1986.

The plaintiffs issued their writ on 29 August 1991. The defendants duly acknowledged service on 24 September 1991. On 9 October 1991, the defendants issued a summons seeking a stay of these proceedings under s 6A of the Arbitration Ordinance (the Ordinance) on the grounds that the agreement dated 9 April 1984 contained an arbitration clause. Alternatively, they sought a stay under the inherent jurisdiction of the court on the grounds of forum non conveniens.

Paragraph 3 of their summons sought a stay pending the hearing of their summons which was originally returnable on 9 January 1992.

The defendants failed to take either of two elementary steps. They failed to invite the plaintiffs to take no further steps in the action until the hearing of their summons for a stay and they further failed to apply for an interim stay to protect their position until 9 January 1992.

In the light of these omissions, it is not surprising that the plaintiffs signed judgment in default on 4 November 1991 and for this the defendants have only themselves to blame.

The first summons which I had to consider was the defendants' summons to set aside this default judgment. Applying *The Saudi Eagle*test [1986] 2 Lloyd's Rep 221, I had to be satisfied that the defendants had a defence which has 'a reasonable prospect of success'. I accept that this is higher than the O 14 (of the Rules of Supreme Court) test.

I was satisfied that the defendants had a real prospect of success. The settlement agreement which relates specifically to the main agreement appears, on its face, to provide for payment only after the contra-account had been settled. There is said to be an issue as to whether it is the Guangdong branch or head office that was a party to the settlement agreement. It is said that they are separate legal entities. Documents have been put in to substantiate this point. However, the defendants seemed unaware of the corporate distinction. Be that as it may, the settlement agreement is clear enough to argue that payment has to be made to the plaintiffs only after accounts with head office are settled. Any arguments as to whether the settlement agreement is subject to any implied term that the defendants would attempt to settle these accounts in good faith and whether in fact they have tried to do so are pre-eminently suitable for a trial. It seems clear that the main agreement has to be read with the settlement agreement which varies or supplements the terms of the main agreement.

It was for these reasons that I set aside the judgment, on the basis that the defendants paid all the costs thrown away. Although I have found that the defendants did not take certain elementary steps, they did indicate to the plaintiffs that it was their intention to seek a stay on the two grounds mentioned. It seems to me that the justice of this case requires the exercise of my discretion in favour of the defendants. I do not consider that this is an appropriate case to make any other conditions for setting aside this judgment.

The second summons issued by the defendants seek to amend their summons to stay by deleting references to s 6A of the Arbitration Ordinance and substituting reference to art 8 of the UNCITRAL Model Law which appears as the fifth schedule to the Ordinance. Nothing much turns on this because whether under s 6A or under art 8, the court is bound to stay the proceedings save in the circumstances mentioned in both provisions. I accept, of course, that both provisions are not identical. The Model Law was made part of Hong Kong's law of arbitration by the Arbitration (Amendment No 2) Ordinance 1989 and the Governor specified 6 April 1990 as the commencement date. However, the application of the Model Law was subject to the transitional provisions which were contained in s 26 of the 1989 Ordinance and this sectiion is now to be found as a footnote to s 31 of the 1 October 1990 reprint of the Arbitration Ordinance.

Section 26 provides as follows:

Transitional

> (1) An arbitration commenced, within the meaning of s 31(1) of the principal Ordinance, after the commencement of the principal Ordinance but before the commencement of this Ordinance shall be governed by the principal Ordinance as if this Ordinance had not been enacted.
>
> (2) An arbitration commenced, within the meaning of s 31(1) of the principal Ordinance, after the commencement of this Ordinance under an agreement made before the commencement of this Ordinance shall be subject to ss 2B, 2E and 14(3A) of the principal Ordinance but, subject to that, shall be governed by the principal Ordinance as if this Ordinance had not been enacted.

Mr Ho submits that, as in the present case no arbitration has commenced within the meaning of s 31 of the Ordinance, s 26 does not begin to bite and, thus, the Model Law does apply to this arbitration agreement notwithstanding that it was entered into six years before the Model Law came into force. One only has to state this proposition to see its manifest absurdity. The whole thrust of s 26 was to ensure that in relation to arbitration agreements entered into before 6 April 1990 the Model Law did not apply. The three exceptions in s 26(2) do not relate to the Model Law as such but to conciliation, reporting restrictions and the rules of evidence.Mr Ho relied upon the word 'commenced' and submitted that as this arbitration had not commenced yet, the pre-condition of the

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subsection had not been met. In my judgment, in this context, the phrase 'an arbitration commenced' has to be read as importing the meaning 'an arbitration commenced or to be commenced'. To fail to give this interpretation would run counter to the clear intent of the legislature which was to ensure that arbitration agreements entered into before 6 April 1990 would still fall to be decided under the law which existed at the time the agreement was entered into.

I am quite satisfied that the Model Law cannot apply in this case and I have to consider the matter as a non-domestic arbitration agreement to which s 6A of the Ordinance still applies. I now turn to consider the arbitration clause relied upon which states as follows:

> In case of any *incompleteness* of the contract, both parties shall reach settlement through friendly consultations. If settlement cannot be reached through consultations, the matter *may* be submitted for arbitration to the Foreign Economic and Trade Arbitration Commission of the China Committee for the Promotion of International Trade. (Emphasis added).

I am happy to record that Mr Pierrepont who appeared for the plaintiffs did not seek to take any points arising from the change of name of China's international arbitral body to the China International Economic Trade Arbitration Commission (CIETAC).

The points at issue are apparent from the two words which I have italicized.

Mr Pierrepont submits that the word 'incompleteness' should be given its natural meaning and should be taken to refer solely to clauses which may have been omitted from the contract. In other words, this clause is only applicable, if at all, if one party wishes to contend that the contract requires an additional term or terms. On this basis, Mr Ho retorted that this would give to the arbitrator the power to rewrite the contract which could not really have been the parties' intention.I must confess to finding this a daunting prospect for any arbitrator or arbitral tribunal.

Mr Ho submitted that the word 'incompleteness' is a word which is wide enough to cover non-performance or breach of the contract. I find this a much more satisfying interpretation. It avoids the arbitrator having to rewrite the contract made between the parties. I cannot believe that the parties would ever have contemplated entering into an agreement whereby the arbitrator was only to consider what was missing from the contract and not also have agreed that all disputes under the contract should likewise be resolved by arbitration. I therefore, propose to construe the word 'incompleteness' as wide enough to cover a failure to perform the contract which is the very allegation made by the plaintiffs in this case.

Mr Pierrepont's next point is that, by use of the word 'may' as opposed to 'shall', the parties have not bound themselves to arbitrate this dispute. He puts it on the basis that arbitration can only take place by consent and

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that one party cannot stop the other party from going to an appropriate court, as has happened here.

It is trite law that the terms of the agreement to arbitrate have to be sufficiently certain to be enforceable. In *Hobbs Padgett v JC Kirkland* 1969 2 Lloyd 's Rep 547 at 549, Salmon LJ (as he then was) stated that the word 'arbitration' would be a sufficient expression of intent.

A similar problem was presented to Mills-Owens J in *Continental Corporation (No 2) v Vincenzo Fedele* [1964] HKLR 213 . In that case, there were six sets of documents evidencing the sale of commodities by the plaintiffs as sellers to the defendants as buyers and each contained the clause 'arbitration: friendly arbitration in Hong Kong'. The learned judge held that it was unnecessary for an arbitration clause to take a particular form, so long as the intention was clear and that the reference to the word 'friendly' arbitration did not imply that the parties did not intend to be bound contractually to resort to arbitration. *i*t implied a resort to arbitration in preference to a resort to a court of law. At p 216, he said this:

> On the matter of vagueness or uncertainty, as it appears to me, there are two possible questions, namely, whether it is sufficiently certain that the parties intended to refer the dispute to arbitration, and whether they intended it as a matter of legal obligation. The clause appears to me to satisfy both tests. It is not necessary that an arbitration clause should take a particular form so long as the intention is clear ... The reference to 'friendly' arbitration does not, in my view, imply that the parties did not intend to be bound contractually to resort to arbitration in the event of dispute; on the contrary, it implies resort to arbitration in preference to resort to a court of law.

It seems clear to me that the parties in the case before me had agreed on arbitration as opposed to litigation in the courts in any particular country. The fact that the permissive word 'may' was used does not in the end detract from this agreement. It seems to me that once one party or the other has opted for arbitration (as by taking out this application for a stay) the other party is obliged to honour the agreement to arbitrate. It follows, of course, that if both parties agreed not to arbitrate but to litigate, they would be perfectly free to do so but I do not think the word 'may' in the context of this clause entitles the plaintiffs to negate the defendants' wish to arbitrate by the issue of court proceedings. At the end of the day, it seems clear to me that this is one of those cases where the word 'may' in effect means 'shall'. I do not think that the defendants are prevented from insisting upon arbitration merely because the plaintiffs issued their proceedings before any steps could be taken by the defendants to commence the arbitration.

Since the argument concluded in this case, I have come across an excellent article by Benjamin G Davis, entitled 'Pathological Clauses: Frederic Eisemann's still vital criteria' which appears at p 365 in the *Arbitration International* Vol 7 No 4/1991 . Mr Davis who is a senior case

officer of the International Chamber of Commerce Court of Arbitration, referred to an arbitration clause in the following terms:

> Any dispute of whatever nature arising out of or in any way relating to the agreement or to its construction or fulfillments may be referred to arbitration.Such arbitration shall take place in USA and shall proceed in accordance with the rules of conciliation and arbitration of the International Chamber of Commerce.

Mr Davis goes on:

> Recently, a US District Court (*Cravat Export Co v Taiwan Power Co* default USDC Eastern District of Kentucky, CA 90-11, 5 March 1990, unreported) was faced with this language and determined that such a clause provides for permissive arbitration until one of the parties chooses to invoke the arbitration clause. When such an election is made by a party, in the US District Court's view, then, the arbitration becomes mandatory for the parties. In the actual ICC arbitration, the party raising the jurisdiction or objection withdrew it after this decision.

I am comforted by the fact that my view of the arbitration clause before me appears to accord with the views expressed by the US District Court of Kentucky. Forester J in the *Cravat* default case remarked that several courts had rejected the interpretation, based on the word 'may', that arbitration was permissible only if both parties agreed thereto. Noting the strong Federal policy in favour of arbitration (see the *Mitsubishi* default case 473 US 614 (1985)) the learned judge went on to say this:

> The court finds the contract ... provided for permissive arbitration until one of the parties chose to invoke the arbitration process. When Taipower elected to proceed to arbitration for resolution of the dispute, arbitration then became mandatory for both parties.

I respectfully agree.

I am also satisfied that the interpretation to which I have subjected this clause accords with commercial reality and common sense as it is frequently the case that contracts between nationals of different states prefer arbitration as opposed to litigation. One of the major factors being that an arbitral award is far easier to enforce under the New York Convention than a judgment of a domestic court. At the present time, this is very much the case as between Hong Kong and China.

In conclusion, therefore, this is clearly a non-domestic arbitration agreement within the meaning of s 6A(3) of the Ordinance. Under s 6A(l) of the Ordinance, I have to grant a stay unless I am satisfied 'that the arbitration agreement is null and void, inoperative or incapable of being performed, or that there is not in fact any dispute between the parties with regard to the matter agreed to be referred'. Save as to the two points in relation to the word 'incompleteness' and the word 'may', Mr Pierrepont put forward no other reasons as to why the stay should not be granted. He

sensibly accepted that once I had decided to set aside the judgment on *The Saudi Eagle* grounds, it was not really open to him to argue that there was no dispute between the parties.

I therefore, grant the application to stay these proceedings under s 6A of the Ordinance. In view of the decision at which I have arrived in relation to the application for a stay in favour of arbitration, it is not necessary for me to go into the alternative submission made by Mr Ho, namely, that I should stay these proceedings under the inherent jurisdiction of the court on the grounds of forum non conveniens. It may however, be helpful if I indicate what my decision would have been had that been a live issue.

Mr Ho accepted that in the light of the authorities, in particular *The Spiliada*[1987] 1 Lloyd's Rep 1, the burden was on the defendants to show that China was clearly the more appropriate forum.Mr Ho contended that all the factors pointed to China as clearly the more appropriate forum and there was only one connection with Hong Kong, namely, that the defendant was a Hong Kong company. He submitted that the arbitration clause which provided for arbitration in China was some indication that Chinese law applies to this contract. This contract was made in China between the parties in relation to the supply of Chinese construction workers from China to work in Libya. Payment under the agreement was made in US currency but was to be transmitted to a Chinese bank account in China through a Hong Kong bank. The plaintiffs' witnesses all come from China and as I said, the only real connection with Hong Kong is the fact the defendents are a Hong Kong corporation. Although the plaintiffs do not have a regular place of business here, they do have an associated office here. Mr Pierrepont submitted that China was not clearly the more appropriate forum and relied on the fact that there was no reciprocal enforcement of civil judgments as between China and Hong Kong. I have in mind, of course, the various observations of Lord Goff in *The Spiliada* and bearing those in mind, I am forced to the conclusion that there is some other available forum which is clearly more appropriate for the trial of this action and that there are no circumstances by reason of which justice requires that a stay should nevertheless be refused. There is certainly no evidence, let alone cogent evidence, before me that the plaintiffs will not obtain justice in the foreign jurisdiction. In my judgment, everything connects this case with China and I would have granted a stay on this ground had I not been satisfied that it was appropriate to grant a stay under s 6A of the Arbitration Ordinance.

It follows therefore, that I dismiss the defendants' summons to amend their summons by referring to the UNCITRAL Model Law ... I grant the defendants a stay of proceedings on the grounds mentioned above.