GAY CONSTRUCTIONS PTY LTD & ANOR v CALEDONIAN TECHMORE (BUILDING) LTD (HANISON CONSTRUCTION CO LTD, THIRD PARTY) - [1994] 2 HKC 562

HIGH COURT
KAPLAN J

CONSTRUCTION LIST NO 23 OF 1993

17 November 1994

Arbitration -- Stay of proceedings -- Whether art 7(2) of the Uncitral Model Law complied with -- Whether record of agreement has to refer specifically to an arbitration clause -- Relevant considerations

Words and Phrases -- 'Statement of claim and claim' -- Uncitral Model Law art 7(2)

The third party (the applicant) was the main contractor and the defendant (the respondent) was a nominated sub-contractor in a standard form contract which contained an arbitration clause. The contract was signed by the third party but not the defendant. Prior to the commencement of the works, the defendant submitted a form of tender and referred to the standard form contract.Works commenced and, thereafter, the parties exchanged correspondence which made reference to a number of the clauses in the contract. In opposing the third party's application for a stay of the third party proceedings under s 6 of the Arbitration Ordinance (Cap 341), the defendant contended that there had been no compliance with art 7(2) of the Uncitral Model Law (the Model Law) as the defendant did not sign the contract and none of the correspondence actually referred to the arbitration clause.

Held, granting a stay of the third party proceedings:

(1) It was possible to comply with the last sentence of art 7(2) without an explicit reference to the arbitration clause. To require a specific reference to the arbitration clause would be far too restrictive and, clearly, was not intended by those drafting the Model Law.
(2) There was no reason why the phrase 'statements of claim and defence' in art 7(2) should be read as referring only to pleadings in the formal sense.
(3) When arbitration proceedings commenced, the claim document of the defendant would either be treated as the statement of claim or form the basis of another document which would incorporate all of its contents.
(4) Very strong grounds need to be made out to deprive a party of his contractual bargain of arbitration over litigation. In the present case, a stay ought to be granted.

Obiter

If the defendant wished to sub-contract the works, it was his responsibility to ensure that he imposed an arbitration clause upon his sub-contract. If there were back-to-back arbitration clauses, with this being a domestic arbitration, there would be ample scope for an application for consolidation under s 4 of the Arbitration Ordinance (Cap 341).

Cases referred to

Astell-Peiniger Joint Venture v Argos Engineering & Heavy Industries Co [1994] 3 HKC 328 (to be reported in

[1994]HKC 3

Taunton-Collins v Cromie [1964] 1 WLR 633

Telford Development v Shui On Construction A 1946/87 (A1946/87, unreported)

Wharf Properties v Eric Cumine Associates [1984] HKLR 211

Legislation referred to

(HK) Arbitration Ordinance (Cap 341) ss 2(1), 4, 6, Sixth schedule (UN docs A/CN 9/264, A/40/17)

Other legislation referred to

BrochesCommentary on the Model Law p 41 -

Holtzmann & Neuhaus Guide to the Uncitral Model Law pp 263-264 -

Kaplan, Spruce & Cheng Hong Kong Arbitration --Cases and Materials p 26 -

Kaplan, Spruce & Moser Hong Kong and China Arbitration -- Cases and Materials p 746 para 8Uncitral Model Law art 7(2)

Application

This was an application by the third party for a stay of third party proceedings under s 6 of the Arbitration Ordinance (Cap 341). In opposing the application, the respondent contended that art 7(2) of the Uncitral Model Law had not been complied with. The facts appear sufficiently in the following judgment.

Peter Graham (Herbert Smith) for the applicant.

Stephen Franklin (Robin Bridge & John Liu) for the respondent.

Glenn Haley (McKenna & Co) for the plaintiffs.

KAPLAN J

On 11 November 1994, I granted the third party (Hanison) a stay of the third party proceedings under s 6 of the Arbitration Ordinance (Cap 341). I said that I would briefly reduce my reasons into writing, which I now do.

Hanison was the main contractor appointed by China Dyeing Holdings Ltd to undertake the construction of a dyeing factory at Yuen Long in the New Territories. The defendant was a nominated sub-contractor for the design and supply of structural steel frames and external cladding. This work was sub-contracted by the defendant to the first plaintiff, Gay Constructions Pty Ltd, who appeared to have sub-contracted some or all of this work to the second plaintiff.

The contract between the first plaintiff and the defendant was in writing and was signed by Hanison on 12 March 1992. It was not signed by the defendant. It contained an arbitration clause.

Prior to entering into the agreement with Hanison, the defendant submitted a form of tender to Hanison and signed it on 10 December 1990.

Paragraph 1 of this tender states:

> Having inspected the site, examined the drawings, conditions of sub-contract, conditions of main contract and specification for the execution of the abovenamed sub-contract works, I/we offer to execute, complete and maintain the whole of the said of the sub-contract works in conformity with the drawings, conditions of sub-contract, conditions of main contract (insofar as they refer to nominated sub-contractors) and specification for the sum of dollars thirty seven million,

> one hundred eighty three thousand and thirty only ($37,183,030.00) or such sum as may be ascertained in accordance with the conditions of sub-contract and relevant conditions of main contract.

Paragraph 4.01 of the form of tender provided as follows:

> 'The standard conditions of sub-contract' means the standard conditions of sub-contract together with its appendix issued under the sanction of the Hong Kong Institute of Architects, the Royal Institution of Chartered Surveyors (Hong Kong Branch) and the Society of Builders, Hong Kong, First RICS (HK Branch) edition 1986 for use where the sub-contractor is nominated under the standard form of building contract for Hong Kong.

This form of contract contains an arbitration clause.

In due course, the sub-contract was signed by Hanison but not by the defendant. Works commenced and, thereafter there are copious references in the correspondence passing between Hanison and the defendant which make ample reference to a number of the clauses in the written sub-contract.

As a preliminary point, Mr Franklin, for the defendant, contends that there has been no compliance with art 7(2) of the Uncitral Model Law (the Model Law) which by virtue of s 2(1) of the Arbitration Ordinance has application equally to domestic as to international cases.

Article 7(2) provides as follows:

> The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the parties or in an exchange of letters, telexes, telegrams or other means of telecommunication which provide a record of the agreement or in an exchange of statements of claim and defence in which the existence of an agreement is alleged by one party and not denied by another. The reference in a contract or a document containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause part of the contract.

Clearly, the agreement is not signed by both parties and the issue is whether there are exchanges of letters which provide a record of the agreement and whether there is an exchange of a statement of claim in which the existence of the agreement is alleged and not denied.

Mr Franklin's short point is that none of the references in the correspondence actually refer to the arbitration clause contained within the written agreement and thus, he submits, art 7(2) cannot possibly be complied with.

This raises the question whether a reference to clauses of the written agreement are sufficient even though they do not specifically refer to the arbitration clause.

The first of the Sixth Schedule documents to which the court may have regard in interpreting the Model Law is a report of the Secretary General of Uncitral dated 25 March 1985 and entitled *Analytical Commentary on Draft Text of a Model Law on International Commercial Arbitration*(United Nations document A/CN 9/264) and the second of the Sixth Schedule documents is a report of the United Nations Commission on International Trade Law on the work of its eighteenth session (3-21 June 1985) (United Nations document A/40/17). A commentary on art 7(2) in the analytical commentary can be found at p 746 in Kaplan, Spruce & Moser *Hong Kong and China Arbitration -- Cases and Materials*published by Butterworths in May 1994. Paragraph 8 states:

> The second addition, contained in the last sentence, is intended to clarify a matter which, in the context of the 1958 New York Convention, has led to problems and divergent court decisions. It deals with the not infrequent case where parties, instead of including an arbitration clause in their contract, refer to a document (eg general conditions or another contract) which contains an arbitration clause. The reference constitutes an arbitration agreement if it is such as to make that clause part of the contract and, of course, if the contract itself meets the requirement of written form as defined in the first sentence at para (2). As the text clearly states, the reference need only be to the document; thus, no explicit reference to the arbitration clause contained therein is required.

Holtzmann & Neuhaus in their *Guide to the Uncitral Model Law* comment on this point at pp 263-264 where they state:

> 4 *Reference in a written contract to a document containing an arbitration clause if the reference makes the clause part of the contract*. This sentence was added to make clear that when an arbitration clause is not contained in a written contract but rather a document referred to therein -- such as general conditions of contract or another contract -- the arbitration agreement may be deemed to be 'in writing'. The contract containing the reference must be in writing. This probably means that it must meet the requirements contained in the second sentence of the paragraph. That is, the contract probably must be either signed or contained in an exchange of letters, telexes, etc. Otherwise, as already noted, the parties could, merely by placing the arbitration clause in a separate document, avoid the requirements of a written assent from each party.
>
> The meaning of the requirement that 'the reference (be) such as to make (the arbitration) clause apart of the contract' may raise questions. The working group made clear that it did not mean the contract had to make explicit reference to the arbitration clause itself. The requirement was adopted as a middle ground between two positions: one view was that the text of the arbitration agreement had to 'be before both parties' in order to bind them; another view was that only a 'reference' in the contract
>
> *[1994] 2 HKC 562 at 566*
>
> to general conditions or other documents containing the arbitration clause was enough.The language adopted appears to mean that the general conditions, prior contract or other document must have been intended to be incorporated into the contract and not merely referred to in, for example, a 'whereas' clause or as background to the agreement.

Aron Broches in his *Commentary on the Model Law* states at p 41:

> 11Thirdly, they clarified the effect of a reference in a contract to another document which contains an arbitration agreement provided the contract is itself in writing and the reference is such as to make that clause part of the contract. In adopting this language at his final session, the working group agreed that it should not be understood as requiring an explicit reference to the arbitration clause in the other document.

In *Astell-Peiniger Joint Venture v Argos Engineering & Heavy Industries Co Ltd* [1994] 3 HKC 328 , I dealt with a similar point and referred to the same materials as I have set out above. I am quite satisfied that it is possible to comply with the last sentence of art 7(2) without an explicit reference to the arbitration clause. To require a specific reference to the arbitration clause would be far too restrictive and clearly was not intended by those drafting the Model Law.

On the facts of this case, it is perfectly obvious that although the defendant did not sign the written agreement, it relied upon various parts of it to support the various claims that it was making and no doubt denying claims that were being made against it. I have no doubt on the facts of this case that there are ample exchanges of letters which provide a record of the agreement. However, the matter does not end there. In due course, the defendant put in a contractual claim for loss and expense to Hanison in December 1992. This is a detailed and complex document and attached to this claim document are a number of provisions of the sub-contract including, interestingly enough, the arbitration clause itself. This document which was sent to Hanison provides the clearest possible record of the written agreement and reference to the arbitration clause itself. I have no difficulty in concluding that despite its length, this document when sent to Hanison comes within the definition of a letter. If I were wrong about that, I would be prepared to hold that this document was in fact an exchange of statements of claim in which the existence of the agreement was alleged by the defendant themselves and certainly, never denied by Hanison. The phrase 'statements of claim and defence' in art 7(2) of the Model Law is not defined and I see no reason why they should be read as referring only to pleadings in the formal sense once an arbitration has commenced. This claim document is headed 'contractual claim for loss and expense' and I have no doubt that when arbitration proceedings commence, it will either be treated as the statement of claim or form the basis of another document which will incorporate virtually all of its content. In this case, the defendant had ample knowledge in advance that the form of sub-contract contained

[1994] 2 HKC 562 at 567

an arbitration clause and when it came to making its claim, it actually included the arbitration clause as part of its documentation. To conclude that art 7(2) had not been complied with would be an absurdity on the facts of this case. I am, therefore, quite satisfied that Mr Franklin's short preliminary point fails and that art 7(2) has been complied with.

I now turn to consider Mr Franklin's submissions which were intended to persuade me not to exercise my discretion in favour of granting the stay.

The law on this subject was carefully reviewed and set out by Mantell J in *Wharf Properties Ltd v Eric Cumine Associates* [1984] HKLR 211 , where the learned judge observed, in a similar situation, that a person in the position of the defendant has to show a very strong or very good reason why the matter should not be referred to arbitration. The circumstances of the case should be considered by the court with a strong bias in favour of maintaining the bargain between the parties.

This case raises a point which frequently arises in practice. There can be an arbitration clause in the contract between the employer and the main contractor but not one between the main contractor and the sub-contractors. The same arguments are wheeled out every time. It is contended that there could be inconsistent findings of fact and there would be multiplicity of proceedings. The answer in most of these cases is that parties entering into sophisticated agreements of this nature, which involve more than two parties, should take care to ensure that there is a common thread in the dispute resolution mechanisms agreed upon. If A and B enter into a detailed contract containing an arbitration clause, why should B be deprived of that bargain merely because A has entered into another contract relating to the same project but which does not contain an arbitration clause. When this point arises, there is frequent reference to the case of *Taunton-Collins v Cromie* 1964 1 WLR 633. That was very much a special case and had nothing to do with the sort of sophisticated and complex building contract with which I am dealing with in this present case.

I do not wish to get involved in a discussion about the perceived advantages of arbitration over litigation. However, there are certain obvious advantages in arbitration which I am quite certain parties have in mind when they enter into complex construction contracts. The first is that an arbitration clause enables them or an appointing authority to agree upon a technical arbitrator rather than a judge, if the circumstances are appropriate. Secondly and, perhaps, most importantly, and not a factor which appears to have been taken account of in the previous cases, is that one can only appeal against an arbitral award with leave of the court. Since 1982, when the leave to appeal provisions were introduced in Hong Kong, there have only been three or four successful applications for leave. That means that in almost all cases where an arbitrator has rendered an award, that award is final. This is, of course, in sharp contradistinction to the situation which pertains in litigation. There are no restrictions on appeal in litigation

whether of interlocutory or final decisions of a first instance judge. It is possible that a final decision will be appealed to the Court of Appeal and there is provision in cases involving more than $500,000 for an appeal to the Privy Council as of right. A third point which often arises but which may not be so relevant in this case is that an arbitration clause usually gives power to the arbitrator to open up, revise and review certificates and directions of the engineer whereas there is strong authority to support the view that the court has no such similar power.

I have chosen these three factors which are not intended to be exclusive. However, they are all actual or perceived advantages which the arbitral process enjoys over litigation. It seems to me that very strong grounds indeed need to be made out to deprive a party of his contractual bargain of arbitration over litigation. I am not to be taken as saying that there can never be cases where it would be appropriate to refuse a stay. In *Telford Development Ltd v Shui On Construction Ltd* default (A1946/87, 21 February 1989, unreported) reported at p 26 of Kaplan, Spruce & Cheng *Hong Kong Arbitration -- Cases and Materials,* Godfrey J (as he then was) refused to grant a stay relying upon multiplicity of proceedings and inconsistent findings of different tribunals. However, with great respect to that learned judge, he failed to consider all the various matters which I have referred to and I am bound to say that the points that he relied upon must inevitably arise in every multi-partite case where the party who has the means to exercise control has failed to ensure that there are back-to-back dispute resolution provisions.

I think that the above comments are sufficient to indicate the reasons why I felt constrained to exercise my discretion in favour of granting the stay. Mr Graham, who appeared on behalf of Hanison, also relied upon the unfairness which would attach to his clients if they were forced to remain in the proceedings, bearing in mind that the hearing was fixed for May 1995 and, it is going to be very difficult for his clients to get ready in time and there was also the possibility of joining other parties. I do not think that this is a matter of which I can really take much notice. It is either right or it is not right for me to grant a stay. Had I not granted a stay and the matter remained in court, then, it would be up to the judge in charge of the construction and arbitra-

tion list to decide whether any unfairness would be suffered by Hanison if they had to keep to the present timetable. I am quite confident that if Hanison were able to show a risk of unfairness or prejudice, the judge would make an appropriate order.

Finally, I ought to deal with the suggestion which was made in the written argument on behalf of the defendant, namely, that the third party had no defence and, therefore, there was nothing to go to arbitration. The claim made against Hanison is for an indemnity in the event that the defendant should be held liable (which the defendant denies). I agree with Mr Graham when he says that this is manifestly not a case where the

claimant can clearly show that the third party has no grounds for disputing the claim.

In all the circumstances, therefore, I was quite satisfied that this was an appropriate case to exercise my discretion under s 6 and stay these proceedings as the parties have agreed upon arbitration. I am also quite satisfied that art 7(2) has been fully complied with.

I conclude this judgment with the following observation. Time and time again, this court has been faced with a similar problem. The problem is simply that those responsible for drafting multi-partite contracts do not appear to focus on the importance of having dispute resolution clauses in the various linked contracts which are not inconsistent with each other. In this case, Hanison was the main contractor and the defendant was a nominated sub-contractor on a standard form of contract which contained an arbitration clause. If the defendant then wishes to sub-contract the works, it surely is his responsibility to ensure that he imposes an arbitration clause upon his sub-contractor so that the present problem is avoided. If there were back-to-back arbitration clauses, with this being a domestic arbitration, there would be ample scope for an application for consolidation under s 4 of the Arbitration Ordinance.

There is no need to make any directions on the third party proceedings. After hearing counsel, I ordered the defendant to pay Hanison's costs of this application for a stay.