SCHINDLER LIFTS (HONG KONG) LTD v SHUI ON CONSTRUCTION CO LTD - [1994] 3 HKC 598

HIGH COURT
KAPLAN J

ACTION NO 7005 OF 1991

2 July 1992

Civil Procedure -- Stay of proceedings -- Summary judgment -- Payment into court by defendant -- Payment accepted by plaintiff -- Whether defendant precluded from raising defence and counterclaim -- Whether proceedings should be stayed in favour of arbitration -- Whether there was dispute

Arbitration -- Agreement to arbitrate disputes -- Application for summary judgment -- Stay of proceedings in favour of arbitration -- Whether stay should be granted

By a main contract, the defendant as main contractor agreed to erect and construct a hotel development for the employer. By a written sub-contract, the plaintiff as sub-contractor agreed to supply, install and maintain 15 lifts at the said development. Clause 11(b) of the sub-contract provided that within 14 days of receipt by the main contractor of payment from the employer against any certificate from the architect, the main contractor shall notify and pay to the sub-contractor the total value certified in respect of the sub-contract work.

The plaintiff claimed a sum said to be due under certain certificates. The defendants said that they had not received payment from the employer because the employer had set off against the total sums due under the certificates an equal sum by way of liquidated damages. The plaintiff contended that the defendant had nevertheless received payment.

The plaintiff started its claim in August 1989. No agreement being reached, it served on the defendant a notice to concur in the appointment of an arbitrator in March 1991. Proceedings commenced on 13 September 1991, with the defendant paying into court $550,000 said to be in satisfaction of all the matters in dispute which were the subject of arbitration and after taking into account and satisfying any counterclaims which a second party may have on 2 October 1991. The payment into court was accepted by the plaintiff on 14 October 1991. This payment was paid before the defendants had served a statement of defence and counterclaim. By an agreement on 7 October 1991, the parties confirmed that it had agreed to appoint an arbitrator.

The plaintiff sought summary judgment for the sum. The defendants sought a stay of the proceedings in favour of arbitration. The plaintiff contended that by accepting the payment into court, the defendants were now precluded from raising a defence and counterclaim to these proceedings, which was open to them to raise in the arbitration, namely, a set off for damages for delay which they contend was caused by the plaintiff.

Held, granting a stay of proceedings:

(1) The arguments on the issue of 'receipt of payment' could not be characterized as being unsustainable or misconceived. It was one of those points

where there existed the reasonable possibility of differing views. Since the parties had chosen arbitration to settle their disputes and this covered the present dispute on the construction of cl 11(b), the correct procedure was that the parties should invite the arbitrator to rule on this matter by way of interim award if necessary and then leave it to the dissatisfied party to apply for leave to appeal if so advised. *Home & Overseas Insurance Ltd v Mentor Insurance Co (UK) Ltd* 1989 3 All ER 74 applied.

(2) It was arguable that the parties agreed to payment on certificate and this should also be decided by the arbitrator. If they had wanted this particular point decided by the court, they could have invited the Chief Justice to appoint a judge arbitrator under s 13A of the Arbitration Ordinance (Cap 341) or they could have agreed to waive their arbitration agreement to enable this point to be decided by the court. Since they had not agreed on either, there was nothing wrong in them being bound to honour the dispute resolution method agreed in their context.

(3) Since there was such dispute or difference, the plaintiff had no other grounds upon which to oppose the stay in favour of arbitration. Therefore, the O 14 application had to be refused.

Cases referred to

Channel Tunnel Group v Balfour Beatty Construction [1992] 2 All ER 609

Ellerine Bros v Klinger [1982] 1 WLR 1375

Hayter v Nelson Home Insurance Co [1990] 2 Lloyd's Rep 265

Home & Overseas Insurance Co v Mentor Insurance Co (UK) [1989] 3 All ER 74

Hong Kong Teakwood Works v Shui On Construction Co [1984] HKLR 235

Icos Vibro v SFK Management [1992] 1 HKC 296

On Lee General Contractor v The Garden Co (A328, 330/92, unreported) DEFAULT

Ryoden Engineering Co v Paul Y Construction Co [1994] 2 HKC 578

Schindler Lifts (HK) v Shui On Construction Co [1985] HKLR 118 (CA)

Sethia Liners (SL) v State Trading Corp of India [1985] 1 WLR 1398

Legislation referred to

(HK) Arbitration Ordinance (Cap 341) ss 4, 13A

(HK) Rules of the Supreme Court O 14, O 73

Summons

This was a summons taken out by the plaintiff seeking summary judgment for a sum due under a sub-contract and a summons by the defendants seeking a stay of the proceedings in favour of arbitration.The facts appear sufficiently in the following judgment.

John Scott (Deacons) for the plaintiff.

*Nigel Aiken (Masons)*for the defendant.

KAPLAN J

I have before me two summons. The first is taken out by the plaintiff, and this seeks summary judgment for $447,223.50 being the sum said to be due under certificates 37 and 39 dated respectively 27 June 1990 and 3 January 1991.

By their summons the defendants seek a stay of these proceedings in favour of arbitration.

By a main contract dated 12 June 1987 entered into between Kornhill Development Ltd as employer and the defendant as main contractor, the defendant agreed to erect and construct a hotel development at Pacific Place Phase 1.

By a written sub-contract entered into between the plaintiff and the defendant on or about 28 May 1988, the plaintiff as nominated sub-contractor agreed to supply install and maintain 15 lifts at the said hotel development.

One of the major issues canvassed before me was the effect of cl 11(b) of the sub-contract which provided that:

> Within 14 days of the receipt by the main contractor of payment from the employer against any certificate from the architect, the main contractor shall notify and pay to the sub-contractor the total value certified therein in respect of the sub-contract work ...

The defendants say that in relation to the sums certified, the subject matter of this action, they have not received payment from the employer because the employer has set off against the total sums due under the certificates, an equal sum by way of liquidated damages. This set off is disputed by the defendants.

The plaintiffs say that the defendant has nevertheless received payment by virtue of the set off of liquidated damages against sums due under the certificates. This issue arises quite frequently and I am sure that the industry would like an authoritative decision on this form of sub-contract. The point has not yet been decided. In *Hong Kong Teakwood Works Ltd v Shui On Construction Co Ltd* [1984] HKLR 235 , Hunter J (as he then was) in O 14 proceedings, when he gave leave to defend inclined to the view that receipt of payment imported receipt of cash. In *Schindler Lifts (HK) v Shui On Construction Co* [1985] HKLR 118 the Court of Appeal, without deciding the point, expressed the view that Hunter J was probably right.

In*Ryoden Engineering Co Ltd v Paul Y Construction* default *Co Ltd* [1994] 2 HKC 578 , the same point came before me in similar but not identical circumstances. In that case, I refused O 14 judgment and granted the stay because I was satisfied that it was arguable that the defendant could raise a common law set off against the claim for certified sums and on that basis, I did not rule on the 'pay when paid' provision although I acknowledged that a decision on the phrase was desirable.

I must, of course, be consistent with my decision in *Ryoden*unless it can be shown to my satisfaction that I was wrong. But Mr Scott for the plaintiff submits that there is, in this case, a special feature which does entitle me to decide the 'pay when paid' point without having to worry about set off. I will have to explain the chronology in order to consider his

submission. Before doing so, I should make clear that there is another issue in this case and that is, that it is the plaintiff's case that the agreement between the parties actually provided for payment on certificate and not payment when paid. This issue revolves around whether a certain document was incorporated into the contract and what precisely it meant in the light of certain questions and answers which also had contractual effect.

I should also point out that there is no authority in England on the 'pay when paid' clause because payment against certificate is the normal clause used in English sub-contracts. Mr Aiken for the defendant relied on the difference between the English and the Hong Kong phraseology as supporting his contention in relation to cl 11 in the present contract.

Relevant chronology

Between August 1989 and October 1991 the plaintiffs were advancing a claim for loss and/or expense.

In August 1989, a claim document was prepared on behalf of the plaintiffs and this was amended in April 1991.

No agreement having been reached as to this claim, the plaintiff served on the defendant a notice to concur in the appointment of an arbitrator and this notice was dated 11 March 1991.

So far as it is relevant, this notice stated as follows:

> Take notice that we hereby request and require you within seven clear days after the service of this notice on you to concur with us in the appointment of a single arbitrator to act in the above-mentioned matter for the purposes of the agreement to refer to arbitration contained in the sub-contract dated 28 May 1988 and made between Shui On Construction Ltd (as the main contractor) and Schindler Lifts (Hong Kong) Ltd (as the sub-contractor)

These proceedings were commenced on 13 September 1991.

On 2 October 1991 the defendant paid into court $550,000. The notice stated:

> The said $550,000 is in satisfaction of all the matters in dispute which are the subject of arbitration before Mr Terence Cleary and relate to the Hotel Development of Pacific Place 1 and in respect of the first party's claims. Said $550,000 is inclusive of interest and after taking into account and satisfying any counterclaims which second party may have.

By an agreement entered into between the plaintiff and the defendant on 7 October 1991, the parties confirmed that it had been agreed to appoint Mr Terence James Cleary as arbitrator. Clause 2 of this agreement stated as follows:

> The dispute referred to the award and final determination of the arbitrator arises in connection with a nominated sub-contract between the main contractor and the sub-contractor dated 28 May 1988 for the design, supply, installation, testing, commissioning and maintenance of the lift installation of the hotel
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> *[1994] 3 HKC 598 at 602*
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> development at IL 8571, Queensway, Hong Kong as are more particularized in the claim dated August 1989 and amended by letter and enclosure dated 7 May 1991 and subject to the main contractor's defences and counterclaims thereto.

On 14 October 1991 (ie within the 14-day period specified in O 73) the plaintiffs accepted the payment into court.

The payment in which was thus accepted was paid in before the defendants had served a statement of defence and counterclaim.

The issue

The plaintiff contended that by accepting the payment into court, the defendants are now precluded from raising as a defence and counterclaim to these proceedings, what was open to them to raise in the arbitration, namely, a set off for damages for delay which they contend was caused by the plaintiffs. Mr Scott has pointed out that in the claim document which was submitted some time ago, there was no mention of a claim under these certificates and indeed the claim under them did not arise until after the original claim document. Mr Scott submits that the plaintiff has been very careful to keep out any claims under certificates from the arbitration proceedings and he submits that by the payment into court in satisfaction of all of the matters in dispute in the arbitration and satisfying any counterclaim which the defendant may have this effectively precludes the defendant from raising in these proceedings any claim for set off for delay.

Mr Aiken submits that the plaintiff must have been aware and appreciated that the payment in was in satisfaction of all matters currently in dispute. He submits that the plaintiffs were well aware that the defendant intended to set off and counterclaim. He reminds me that when the second notice to concur was served the dispute with regard to the certificates had arisen. Mr Aiken further questions why the plaintiffs issued the writ at all. He said that it could not be for the purposes of obtaining the benefit of O 14 because they could always ask the arbitrator to rule as a preliminary issue on the question 'pay when paid'. He submits that the defendant could not have behaved in such a way as Mr Scott describes which would be effectively abandoning a counterclaim which they had always asserted. Mr Aiken submits that the payment in was intended to dispose of the claim on the certificates. He goes on to submit that this does not mean that the plaintiff would never be paid under this certificate because all that he is submitting is that the claim was premature. As soon as the defendant has been paid by the employer, they would then pass on to the plaintiff such part as is due to them. In fact, I was told that this is what had recently happened because in January of this year, the defendant paid the plaintiff $49,074.50 which was part of the claim of $447, 223.50 which is precisely what the plaintiffs are claiming in this action. Mr Scott submits that these stances are somewhat inconsistent. Either the payment in was intended to dispose of the claim on the certificates, once and for all or was not. It

[1994] 3 HKC 598 at 603

appears, according to Mr Scott, that the defendants are taking an inconsistent position.

Mr Scott submits that the result for which he contends is somewhat strange but it is as a result of rather strange conduct on the part of the defendant. It seems clear to me that the claim on the certificates was nev-

er part of the claim in the arbitration. The claim in the arbitration was for some $2,990,413.96 and it also seems clear to me that if this matter had proceeded, the defendant would have put in a counterclaim alleging, as they have done in the proceedings before me, although somewhat vaguely, that the plaintiff was responsible for part or all of the delay alleged. It seems to me that it is strongly arguable that the defendants have indeed precluded themselves from raising any counterclaim based on delay in the proceedings before me. The terms of the payment into court are wide enough to cover their counterclaim for delay. It is true that as at the date they paid the money in to satisfy any counterclaim which Shui On may have they had not actually put in a counterclaim but they had alleged that delay had been caused by the plaintiffs and it is difficult to see what other counterclaim could have been referred to when the payment into court was made.

That being the conclusion at which I have arrived, it follows, that the position before me now could be said to be different to that which was before me in the *Ryoden*case. On this basis, the first decision I have to make is whether I should embark upon a construction of the 'pay when paid' provision or whether I should leave that to be decided by the arbitrator taking into account, of course, that the parties have agreed to have all differences under this contract resolved by arbitration. No useful purpose can be achieved by referring to the various authorities to which I made ample reference in the *Ryoden* case. I, of course, take into account the observations of Kerr LJ in *(SL) Sethia Liners Ltd v State Trading Corp of India Ltd* 1985 1 WLR 1398, 1401-1402 and I further have regard to the observations of the Court of Appeal in *Home & Overseas Insurance Co Ltd v Mentor Insurance Co (UK) Ltd* 1989 3 All ER 74. It is also necessary to have regard to *Hayter v Nelson Home Insurance Co* default [1990] 2 Lloyd's Rep 265. In that case, Saville J referred to an observation of Templeman LJ in *Ellerine Bros v Klinger* 1982 1 WLR 1375 where he said:

> There is a dispute until the defendant admits that the sum is due and payable.

Saville J went on to say this at p 271:

> ... so that only in the simplest and clearest cases, ie where it is readily and immediately demonstrable that the respondent has no good grounds at all for disputing the claim should that party be deprived of its contractual right to arbitrate. In the context of the 1975 Act, this meant that only in such cases can
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> *[1994] 3 HKC 598 at 604*
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> the court be satisfied that there is not in fact any dispute between the parties with regard to the matter agreed to be referred.

It is implicit in the decision in *Channel Tunnel Group v Balfour Beatty Construction Ltd* default[1992] 2 All ER 609 that the Court of Appeal approved Saville J's approach. (On 11 June 1992 the appeals committee of the House of Lords gave leave to appeal in the *Channel Tunnel* default case.)

In *Icos Vibro Ltd v SFK Management Ltd & Anor* [1992] 1 HKC 296 , I had cause to consider *Hayter*and in following it I concluded that it was not inconsistent with the *Home v Overseas* default case. I have to ask myself the question whether the defence based on non-payment is misconceived. In my judgment, I cannot say that. The next question is whether after relatively short argument, I can be satisfied that the point is 'plainly unsustainable' (Parker LJ in *Home v Overseas).* default I have given this matter long and anxious consideration and I am left in this state of mind. I have formed a view as to what 'receipt of payment' means in the context of this contract. On the other hand, I cannot characterize the contrary argument as being unsustainable or misconceived. It is one of those points where there exists the reasonable possibility of differing views.

As I said in *Ryoden* I would like to decide this point given that I have formed a view as to the meaning of the relevant phrase and the fact that it is important for this point to be resolved. If there had been no arbitration clause in this case, I would have decided it. However, I am very conscious of the fact that the parties have chosen arbitration to settle their disputes and this covers the present dispute on the construction of this clause. As Parker LJ put it in *Home v Overseas* default :

> In cases where there is an arbitration clause it is in my judgment the more necessary that full scale argument should not be permitted. The parties agreed on their chosen tribunal and a defendant is entitled prima facie to have the dispute decided by that tribunal in the first instance to be free from the intervention of the courts until it has been so decided and thereafter if it is in his favour to hold it unless the plaintiff obtains leave to appeal and successfully appeals.

I believe that this passage accurately reflects the position where, as here, there is an arbitration clause. If I were to decide this point myself I would be arrogating to myself a power which the parties had by their contract vested in the arbitrator. I am not prepared to interfere with the contractual mechanism for dispute resolution having decided that the point is arguable even though I know which way I would have decided it.

I was faced with a similar situation in *On Lee General Contractor v The Garden Co Ltd* default (A328, 330/92, unreported) where I refused O 14 judgment and granted a stay in order that a point of construction should be decided by the arbitrator. Although I found the plaintiff's arguments attractive, I could not conclude that it was 'readily and immediately demonstrable that the (defendants) had no grounds at all for disputing the claim'. The point

at issue there was whether the existence of the defects liability period excluded the right to claim damages for those defects. It appeared to me that there was a point of construction which had to be decided by the arbitrator who was invested with power by the parties to resolve all disputes arising out of that contract.

The correct procedure in the present case, as it seems to me, is that the parties should invite the arbitrator to rule on this matter by way of interim award if necessary and then leave it to the dissatisfied party to apply for leave to appeal if so advised. If leave is granted then the court would be able, perfectly properly, and within the Arbitration Ordinance (Cap 341) and within the spirit of the parties' contractual arrangements to give its views on the construction of this vexed phrase.

In relation to the other point, namely, that the parties agreed to payment on certificate, I am likewise satisfied that this is arguable and this should also be decided by the arbitrator. It may well be that on this point some evidence may be required.

I have felt some concern that on two occasions I have declined to decide an important point of construction in a standard form of sub-contract in use in Hong Kong. My concern is to some extent assuaged by the fact that the parties to this dispute have themselves brought about this position. Their standard form contract contained an arbitration clause. If they had wanted this particular point decided by the court two courses of action were open to them. They could have invited the Chief Justice to appoint a judge arbitrator under s 13A of the Arbitration Ordinance (Cap 341). Alternatively, they could have agreed to waive their arbitration agreement to enable this point to be decided by the court. They have not agreed on either of these two courses of action and in those circumstances I see nothing wrong in them being bound to honour the dispute resolution method agreed in their contract.

It follows therefore that I have come to the conclusion that I must refuse this O 14 application and grant a stay of these proceedings as sought by the defendants. I should make it clear that the only ground upon which the stay was opposed was that there was no dispute or difference which needed to go to arbitration. Having decided that there was such dispute or difference the plaintiffs have got no other grounds upon which to oppose the stay in favour of arbitration. Therefore, in the exercise of my discretion under s 4 of the Arbitration Ordinance (Cap 341) I grant the stay sought.

I propose to make a costs order nisi in favour of the defendants both in relation to the plaintiff's O 14 summons and the defendants application for a stay.