

Arbitration—set aside—illegality—common mistake—Hong Kong public policy (AI v LG II LG III)

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Arbitration analysis: The plaintiffs (the claimants in the arbitration) in the case made an application before the Court of First Instance requesting the setting aside of arbitral awards on the grounds under Article 34(2)(a)(ii), (iii) and Article 34(2)(b)(ii) of the Model Law) claiming the tribunal failed to deal with issues regarding the underlying agreements were claimed to be void for illegality or common mistake. Written by Andrew Rigden Green, partner, head of International Arbitration, Greater China at Stephenson Harwood at Stephenson Harwood.

The court found no conceivable basis to set aside the awards and dismissed the application. The following principles were applied:

- the applicant needs to meet a high threshold for challenging an award on the basis that the tribunal had failed to give reasons for its decision. There is no need for the tribunal to give reasons to deal with each and every argument presented and sufficient if the award explains the basis of material findings
- as for a claim that the tribunal had failed to deal with an issue, the court's approach is to read the award generously, so as to remedy only meaningful and readily apparent breaches of the rules of natural injustice which can cause actual prejudice
- if a party had been taken by surprise by a new stance or issue raised by the tribunal, the court may find that the party has been deprived of a fair opportunity to be heard, but not if a party is given the opportunity but fails to recognise it. It is usually sufficient if the 'essential building blocks' of the tribunal's reasoning is in play in relation to an issue

AI v LG II LG III [2023] HKCFI 1183

What are the practical implications of this case?

Firstly, the case reinforces the principle that courts will generally adopt a pro-arbitration approach when considering challenges to arbitral awards, as referred by the court as the policy of 'minimal crucial intervention'. This means that courts will be reluctant to interfere with the decisions of arbitrators and will only do so in limited circumstance where there is a serious breach of the rules of natural justice which can cause actual prejudice.

Secondly, the case demonstrated the high threshold that must be met for an award to be challenged on the grounds that the tribunal (1) failed to give sufficient reasoning for its decision or (2) failed to deal with an issue. Lawyers should carefully consider whether the tribunal's failure to provide adequate reasoning or address an issue is sufficiently clear from the award before challenging it under Article 34(2)(a)(ii) and (iii) of the Model Law.

Lastly, the case highlights the importance of carefully drafting arbitration agreements to ensure that they are clear and unambiguous, and cover all relevant issues that may arise during the arbitration process. Lawyers should ensure that the scope of the arbitration agreement is clearly defined and covers disputes related to jurisdiction and the interpretation of contract clauses (eg events of default clauses), even if the parties in these documents did not submit to arbitration. This will help to avoid jurisdictional disputes and ensure that all relevant issues are addressed during the arbitration process.

What was the background?

The case involves a dispute between a group of plaintiffs and two defendants over the purchase and sale of investment units in various trade finance funds.

Between April and June 2019, the parties entered into certain agreements (the 'Agreements') for the sale and purchase of finance fund units in exchange for two promissory notes with a combined face value of US\$500m (the 'Notes'), where part of the units transferred were distressed assets.

It was agreed that the defendants would retain security interests in the assets transferred pending payment of the entire sums under the Notes. The plaintiffs were to deliver certain documents as a condition to closing (the 'Deliverables'), but some of the Deliverables were not provided to the defendants despite the defendants' various demands.

As a result, in April 2020, the defendants declared the events of default, which resulted in the acceleration of payment under the Notes.

On 10 April 2020, the plaintiffs commenced the arbitration, alleging that the agreements were part of an unlawful scheme to conceal the defendants' losses. The plaintiffs claimed that the agreements were illegal and subject to rescission, and that the defendants had engaged in misrepresentation, contractual breaches, and tortious acts. The defendant denied the allegations and maintained that the plaintiffs had knowledge of the risks in the unit funds and of the regulatory investigations at the time when they entered into the Agreements.

In the award, the tribunal found the Agreements were not void or unenforceable by reason of illegality or common mistake. The tribunal found that there was no basis for rescission of the Agreements (whether on the ground of misrepresentation or breach of contract) and that the event of defaults had occurred under the Notes.

The plaintiffs then applied to the court to set aside the arbitral award under Article 34(2)(a)(ii) & (iii) and on the ground that the award is in conflict with public policy of Hong Kong.

What did the court decide?

The court found no conceivable basis to set aside the award on the grounds under Article 34(2)(a)(ii), (iii) or Article 34(2)(b)(ii) of the Model Law.

- the court rejected the plaintiffs' arguments that the tribunal failed to provide adequate reasonings and failed to deal with the issue of foreign illegality:
 - the court applied *R v F* [2012] 5 HKLRD 278 that an applicant has high threshold to meet when an award is challenged on the basis that the tribunal had failed to give reasons for its decision. There is no need for the tribunal to give reasons to deal with each and every argument presented. It is sufficient if the award explains the basis of material findings
 - as for a claim that the tribunal had failed to deal with an issue, the court emphasized that the approach is to read the award generously, so as to remedy only meaningful and readily apparent breaches of the rules of natural injustice which can cause actual prejudice
- the court found the 'essential building blocks' of the tribunal's reasoning were in play and rejected plaintiffs' argument they had not been given an opportunity to present their case regarding the issue of domestic illegality. The court stated that if a party had been taken by surprise by a new stance or issue raised by the tribunal, the court may find that the party has been deprived of a fair opportunity to be heard, but not if a party is given the opportunity but fails to recognise it
- the court also found the plaintiffs' argument of the tribunal adopting wrong legal test for the issue of misrepresentation was argument of error of law and that does not show that the plaintiffs did not have the opportunity to present their case, nor that the award is against public policy or outside the scope of the submission of arbitration

- regarding the plaintiffs' argument of the tribunal failing to address their claim on the defendants breaching the warranty clause regarding illegality, the court stated that the plaintiffs were not deprived opportunity to present their case as they chose not to refer to the clause in their post-hearing brief. Even if the claim had not been abandoned, the tribunal had already found there was no evidence to establish the illegality of the Agreements

finally, the court agreed with the tribunal's findings that it had jurisdiction to determine whether the event of default (ie whether there was a breach of the security agreements which were submitted to exclusive jurisdiction of Cayman Court) in the Notes had occurred, as it is a decision based on its interpretation of the provisions of the Notes, and therefore fell within the scope of the arbitration agreement contained therein.

Case details

- Court: High Court Hong Kong
- Judge: Mimmie Chan
- Date of judgment: 08 May 2023

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