

Hong Kong court upholds arbitral award where arbitration agreement said to be a sham (*X v Jemmy Chien*)

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Arbitration analysis: An application was made to the Hong Kong Court of First Instance by the unsuccessful party (X) to a Hong Kong arbitration to set aside the resulting awards on the bases that—(i) there was no arbitration agreement between the parties, as the named party (JC) was in reality the agent of another party (PC) who had engineered this arrangement to circumvent his fiduciary duties under Taiwanese law, and (ii) enforcement of the award would be contrary to public policy as the agreement was a sham and to do so would facilitate breaches of Taiwanese law. The court dismissed the set-aside application and awarded JC indemnity costs. Written by Andrew Rigden Green, partner, co-head of arbitration in Asia at Stephenson Harwood, Hong Kong.

X v Jemmy Chien [2020] HKCFI 286, [2020] HKEC 356 (not reported by LexisNexis@UK)

What are the practical implications of this case?

In this judgment, and the related security for costs judgment in the same case, the court has made clear that it will not allow the set-aside or challenge procedure to be used as a backdoor appeal process, rerun of the case, or challenge to the arbitrator's findings of fact. Any abuse of this process will incur indemnity costs.

In considering challenges to jurisdiction the court will confine itself to true questions of jurisdiction only and will not be drawn into considerations of the merits.

The grounds of public policy will be narrowly construed. There is a balance between non-enforcement of awards and other interests—(i) upholding arbitration agreements, (ii) facilitating the enforcement of arbitral awards, (iii) observing obligations under the New York Convention.

However, the question of whether an illegal contract or one that requires an illegal act is contrary to public policy has been left open.

What was the background?

The dispute referred to arbitration involved an underlying service agreement subject to the law of the People's Republic of China (PRC law) where JC agreed to provide product, marketing and promotion services to X. The services were delegated to and performed by PC. X claimed that JC was a party to the service agreement only to conceal that the true party was PC who was the vice president of a third party with competing business. PC therefore had a conflict of interest and entering into the service agreement would be a breach of his fiduciary duties under Taiwanese law. Therefore, the service agreement and the arbitration agreement contained in it were a sham.

In the resulting award on the merits, the arbitrator found that, pursuant to PRC law, JC was the true party to the service agreement. The arbitrator also analysed the position as if Hong Kong law applied and found also that JC would have been the true party to the agreement under Hong Kong law.

Factors that were considered important by the arbitrator were:

- JC signed in his own name
- payments under the service agreement were made to JC's bank account
- requisitions for payments were made in the name of JC
- notice of termination was given to JC without copy to PC, there was no request that PC be informed
- JC was not held out to be another party's representative

X applied to the Hong Kong court to set aside the award on the merits and an award on interest and costs. JC cross-applied to set aside those awards.

What were the issues before the court?

The court considered the following issues:

- when considering whether or not the arbitrator was correct in ruling on his own jurisdiction, what is the scope of the court's review?
- what should be taken into consideration when deciding whether or not to set aside an arbitration award on the grounds of public policy

What did the court decide?

Jurisdiction

The standard of review is one of correctness (see *Dallah Real Estate and Tourism Co v Ministry of Religious Affairs of the Government of Pakistan* [2011] 1 AC 763 applied in *S Co v B Co* [2014] 6 HKC 421) but this does not mean an unwarranted and unlimited view of the findings made by the tribunal. The courts are to be circumspect in their consideration of the correctness of a ruling of an arbitral tribunal on its own jurisdiction, recognizing its limited and narrow role confining its intervention to 'true questions of pure jurisdiction only' (see *Z v A* unreported HCCT 8/2013, 30 January 2015, at para [21]).

There was no dispute that the service agreement was governed by PRC law and the arbitration agreement by Hong Kong law.

X argued that as JC was not the true party to the arbitration agreement, but merely the agent of PC, there was therefore no arbitration agreement between X and JC and the award was unenforceable.

The court emphasised that the findings of fact by the arbitrator as to who was the true party to the agreement were made after hearing evidence from both X and JC. The decision on whether JC was a party to the arbitration agreement is a finding of law based on the facts as found by the arbitrator. Further the court held that it was not its role to review the merits of the correctness of the arbitrator's findings of credibility and of fact. Therefore, the court concluded that the arbitrator had jurisdiction to make the award.

Public policy

X's arguments in support of its contention that the award should be set aside for public policy reasons were framed in two ways:

The service agreement (and hence the arbitration agreement)

- was a sham as it was in reality between X and PC, not X and JC. This argument was set out in X's Originating Summons and supporting affidavit
- should not be given effect as the object of the parties was, under cover of this agreement, to commit illegal acts in Taiwan. This was not set out in X's Originating Summons

The court ruled that:

- allegations of fraud or illegality of the underlying agreement do not render an arbitration agreement null and void. The arbitration clause could be objectively construed as an independent arbitration agreement that any dispute between the parties as to their capacity under the service agreement should be submitted to arbitration. To enforce such an agreement would not be the enforcement of a sham, whatever the findings in respect of the service agreement
- the purpose of the Originating Summons and supporting affidavit is to frame the party's case—facts and grounds relied on should be set out precisely with particulars. No mention was made in X's evidence that the service agreement was illegal under Taiwanese law, or that its performance would require an illegal act in Taiwan
- a distinction should be drawn between a breach of fiduciary duty under civil law and a criminal act. No clear expert evidence was adduced to show that the performance of the service agreement would involve a criminal act in Taiwan
- accepting X's application to resist enforcement of the award would be tantamount to permitting X to rely on its own wrongdoing to avoid its obligations
- indemnity costs should be paid to JC

Case details

- Court: High Court of Hong Kong, Court of First Instance
- Judge: Hon Mimmie Chan J in Chambers
- Date of judgment: 4 March 2020

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