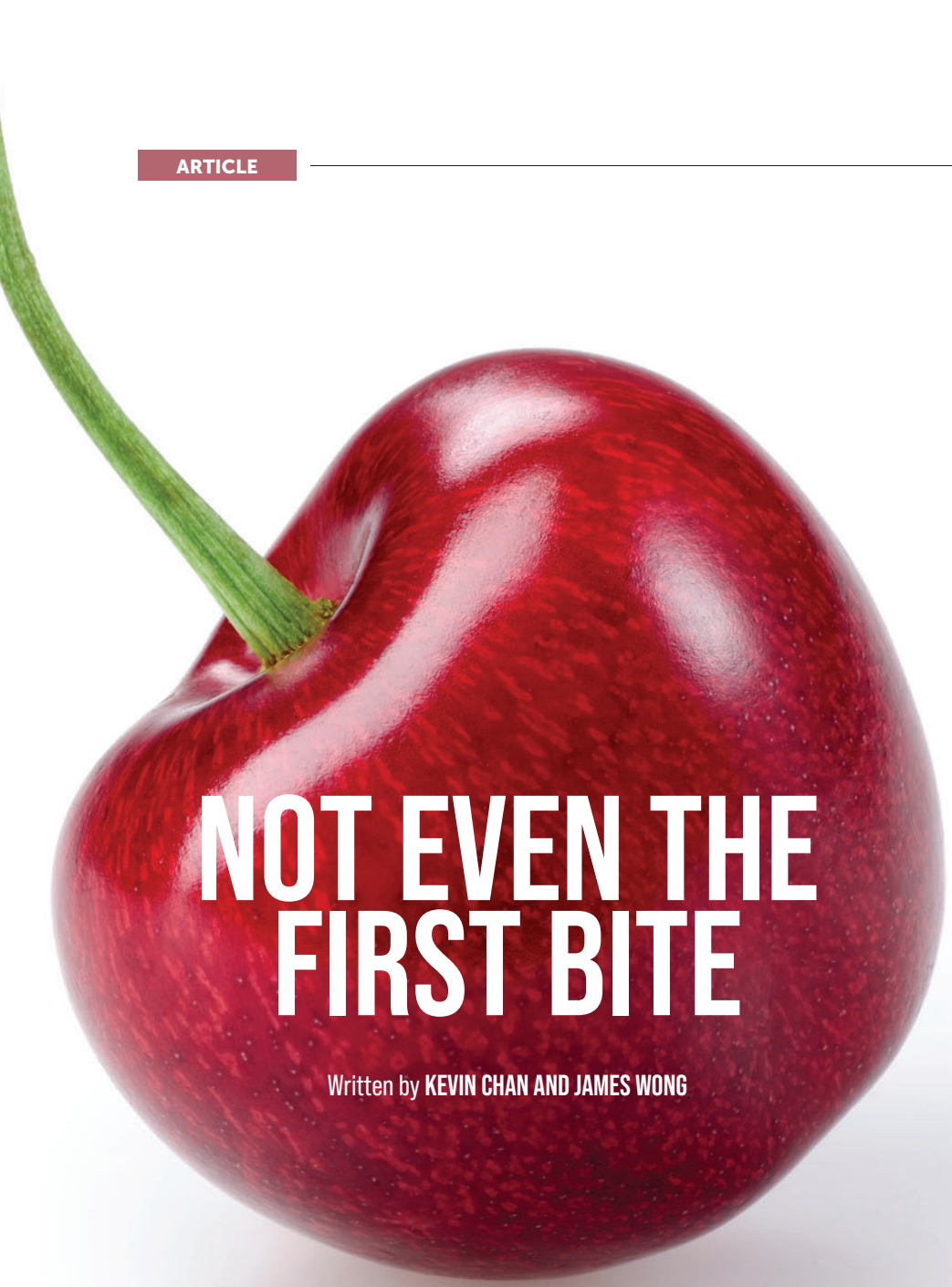

NOT EVEN THE FIRST BITE

Written by **KEVIN CHAN AND JAMES WONG**

Denial of reasonable opportunity to present case enables out-of-time setting aside of an arbitral award enforcement order

DLA PIPER

The Hong Kong Court does not refuse enforcement of an arbitral award lightly. Even errors on facts or law by an arbitrator are not grounds for the Court to deny enforcement. The Court exercises its supervisory powers by looking at the structural integrity of the arbitral process. But if the error is so egregious that it would be shocking the conscience of the Court to allow the enforcement, the Court will step in. The recent case of *Canudilo International Company Limited v Wu & Others* [2023] HKCFI 700 is an example.

The facts

Canudilo International Company Limited (CIC) (as claimant) commenced arbitration against Apennine Holdings Limited (the Company) and its guarantors (collectively, as respondents), seeking the unpaid purchase price for goods sold. CIC applied to the arbitrator (Arbitrator 1) to bifurcate the arbitration. The two parts of the arbitration are (1) CIC's claims against the Company; and (2) CIC's claims against the guarantors. Arbitrator 1 issued an interim final award for part (1) of the arbitration, ruling that the Company is liable to CIC. But Arbitrator 1 later disclosed that, on the day he made the interim final award, he received the Company's time extension application to make written submissions, notwithstanding that Arbitrator 1 had already declared the proceedings between CIC and the Company

to be closed before that. Arbitrator 1 invited the parties to decide whether to nominate a new arbitrator to continue with part (2) of the arbitration. As two of the four guarantor respondents objected to Arbitrator 1 remaining as arbitrator, Arbitrator 1 resigned. HKIAC appointed a new arbitrator (Arbitrator 2).

Arbitrator 2 directed the parties to exchange witness statements, and held an oral hearing. Arbitrator 2 made a final award, against all four guarantor respondents. CIC applied to the Hong Kong Court for enforcing the final award against the guarantor respondents, and obtained an enforcement order.

The guarantor respondents applied, out of time, to set aside the Court's enforcement order. Their reasons are that Arbitrator 2 failed to determine the issues in dispute, that the arbitration was not conducted in accordance with the arbitration agreement and/or the agreed arbitration procedures, that certain respondents did not have a reasonable opportunity to present their case, and that enforcement of the award would be contrary to the public policy of Hong Kong.

The Court's discussion

Mimmie Chan J allowed the guarantor respondents' challenge. She found it obvious from Arbitrator 2's final award that he followed Arbitrator 1's findings between CIC and the Company. She expressed her grave concerns that Arbitrator 2 had not applied his own independent mind pursuant to the mandate given to him under the arbitration agreement to decide the dispute between the parties. There were two parts of the arbitration. The findings in part (1) (between CIC and the Company) did not bind the guarantor respondents in part (2) (between CIC and the guarantor respondents). It was grossly unfair and unjust that Arbitrator 2 considered that two of the guarantor respondents had already been given the opportunity to present their evidence and make their submissions before Arbitrator 1 during part (1) of the arbitration.

Arbitrator 2 considered the four guarantor respondents were already parties of the arbitration in part (1) of the arbitration which dealt with the disputes between CIC and the Company. When the guarantor respondents sought to make submissions in part (2) of the arbitration between themselves and CIC, Arbitrator 2 considered they were seeking a '*second bite of the cherry*" which was impermissible. Mimmie Chan J disagreed. She said that they were not seeking to have a second bite of the cherry, because they "*never had the first bite*".

In conclusion, Mimmie Chan J considered that Arbitrator 2 had failed to consider and failed to decide two guarantor respondents' defences in an impartial and independent manner. He had failed to give them a reasonable opportunity to present their case on the binding effect of Arbitrator 1's interim final award, by deciding the issues on the basis that he and all the parties were already bound by that award. It would be contrary to the basic notions of justice and requirements for a fair hearing to enforce the final award. Due process had been undermined.

Time extension granted

The court's enforcement order was made on 10 August 2021, which required the respondents to apply to set aside the order within 14 days after service. But it was not until 26 April 2022 that they made their setting aside application.

Mimmie Chan J allowed the time extension application by the guarantor respondents to resist enforcement. She adopted the principles laid down by the Court of Final Appeal in *Astro Nusantara International BV v PT Ayunda Prima Mitra* [2018] HKCFA 12. Two guarantor respondents' reason for not having acted earlier was that they had grave financial difficulties in the latter part of 2021, and were not able to make the setting aside application in time.

In her judgment, bearing in mind the merits of the belated application, and the seriousness of the errors undermining the structural integrity of the final award, it was appropriate to grant the time extension.

Accordingly, Mimmie Chan J allowed the out-of-time setting aside application.

Comments

Resisting enforcement of arbitral awards is often a challenging task. The Court looks for "substantial injustice" and "egregious" errors by the arbitrator. The parties cannot overturn an award simply because the arbitrator got matters wrong on law or fact, which is a risk that '*the parties must be deemed to have undertaken"* (*A v R [*2009] 3 HKLRD 389).

To meet the threshold, Canudilo serves as a case example where deprivation of reasonable

opportunity to present one's case had undermined due process. Other examples include the respondent not receiving notice of the arbitral proceedings (such as in *Sun Tian Gang v Hong Kong & China Gas (Jilin) Ltd*. [2016] 5 HKLRD 221, where an individual was imprisoned and received no notice of the arbitration), or the award dealt with matter beyond the scope of jurisdiction (in *Wah Chang International (China) Co Ltd v Tiong Huat Rubber Factory (Sdn) Bhd* [1991] 1 HKC 28, where the awards were held not enforceable because the submission to arbitration only covered disputes on condition or quality, but the arbitrators also dealt with disputes on the alleged failure to open letters of credit).

From the perspective of an award debtor, *Canudilo* also raises a question of whether there are strategic options between (a) actively applying to the Court to set aside an arbitral award, under Section 81 of the Arbitration Ordinance (adopting Article 34 of the UNCITRAL Model Law), or (b) awaiting the award creditor to obtain and serve its enforcement order, and then applying to set aside that enforcement order. The active approach, if successful, enables the award debtor to set aside the award and remove the sword of Damocles above its head. Procedurally, there is a 3-month time limit for the application; the Court has no power to extend time (as Mimmie Chan J said in *Canudilo*), save in exceptional circumstances (such as the imprisoned individual in the Sun Tian Gang case referred to above). Alternatively, the award debtor may choose to wait and resist enforcement when the creditor applies for an enforcement order. The enforcement order will stipulate a time period for application to set it aside, as the guarantor respondents did in *Canudilo*. In this scenario, the Court has power to extend that time period, in accordance with the principles set out in *Astro Nusantara International BV v PT Ayunda Prima Mitra* [2018] HKCFA 12. In *Canudilo*, the Court allowed the time extension application in view of the strong merits of the setting aside application, the absence of evidence of prejudice to the claimant, and the overall circumstances of the case. Obviously not every award debtor can plead for mercy by referring to its "grave financial difficulties" which delayed its application to the Court.

The advantage of actively setting aside an award is to prevent (or at least delay) direct enforcement action, including a bankruptcy or winding up petition. If the award creditor issues a petition after the 3-month time limit expires, the award debtor will struggle to apply to set aside out of time and oppose the petition by relying on the ground of exceptional circumstances. From the very limited authorities in this area, it appears unless the award debtor is able to demonstrate grave injustice in the arbitration process

(such as the imprisonment case in *Sun Tian Gang*), the Court will be very slow to grant the time extension.

From the claimant's perspective, *Canudilo* highlights the importance of the proper conduct of an arbitration. Mimmie Chan J questioned the wisdom of CIC's application to bifurcate the arbitration. And the fatal points were Arbitrator 2's undue reliance on the interim final award in part (1) of the arbitration, and his denial of due process including the respondents' reasonable right to present their case, and others, all under the watch of the claimant side. A claimant and its legal representatives should ensure that an arbitration is conducted in accordance with the arbitration agreement and the agreed arbitration procedures, and that principles of due process are properly observed.

ABOUT THE AUTHORS

Kevin Chan

Kevin Chan has over 25 years' experience in civil dispute resolution. He helps clients across the banking, investment, real estate, insurance and logistics industries with a range of complex commercial and cross-border disputes, and non-contentious matters.

Kevin acts for banks, multinational companies, Chinese state-owned/private enterprises and listed companies. He has advised clients on investment, joint-venture and shareholder disputes; banking disputes involving issues on loan defaults, asset recovery, financial leasing and trade finance; real estate disputes; a wide range of logistics and transportation disputes; and all types of cross-border enforcement issues. Kevin also advises on a wide range of non-contentious matters. These include assisting financial services companies, commodity traders and insurance companies in reviewing and drafting contractual documents, standard business terms and conditions and other commercial documents.

James Wong

James Wong is a Senior Associate in the Litigation and Regulatory team of DLA Piper Hong Kong. He specialises in cross-border dispute resolution, with a focus on disputes with a China element. He has a broad practice which covers commercial litigation, shareholders' disputes, enforcement of distressed debts and securities, professional negligence, bankruptcy and corporate insolvency, product liability, and international arbitration.

James had spent one year on secondment to a Chinese SOE. He is experienced in advising creditors, debtors and corporations on projects involving distressed debts with complex security arrangement.