

MULTI-TIER DISPUTE RESOLUTION CLAUSES AND THE DISTINCTION BETWEEN JURISDICTION AND ADMISSIBILITY – HONG KONG COURT OF APPEAL CONFIRMS APPROACH

Escalation (or multi-tier dispute resolution) clauses are commonly found in commercial contracts. For example, an agreement may require the parties to enter into good faith negotiation, mediation, conciliation and/or adjudication before an arbitration can be commenced. In the case of *C v D*, the Hong Kong Court of Appeal confirmed that, subject to the contrary agreement of the parties, alleged non-compliance with preconditions to arbitration is a matter of admissibility for an arbitral tribunal. The decision will be welcomed by parties agreeing to arbitrate their disputes in Hong Kong. It confirms that Hong Kong law is clearly aligned with the prevailing position internationally that a tribunal should decide on the admissibility of all claims before it, with narrow grounds for interference by national courts. This briefing also discusses the position in England and Australia.

BACKGROUND

The effect of an obligation to enter into negotiations prior to arbitration and the jurisdiction of a tribunal over the matters submitted to arbitration, including compliance with such obligation, is an issue that has attracted debate amongst leading academics and practising commentators in the field of international arbitration and has been considered in detail by the courts of major seats of arbitration.

A recent Hong Kong Court of Appeal decision (*C v D* [2022] HKCA 729) concerned a dispute as to alleged non-compliance with procedural preconditions to arbitration and whether non-compliance meant that the tribunal had no jurisdiction. The Court of Appeal drew a distinction between issues of admissibility and those of jurisdiction, a distinction which, the court held, is "*rooted in the nature of arbitration itself*".

Jurisdiction vs Admissibility

The distinction between jurisdiction and admissibility (as discussed in *C v D*) is as follows:

Key issues

- Subject to the contrary agreement of the parties, questions as to the existence, scope and fulfilment of preconditions to arbitration go to the admissibility of the claim and not the jurisdiction of the tribunal.
- Again subject to the contrary agreement of the parties, questions of admissibility are for the tribunal to decide. Non-compliance with preconditions to arbitration cannot lead to a successful jurisdiction challenge to an award before the court.
- It is confirmed that Hong Kong law is in line with that in England and Australia.
- Whilst escalation or multi-tier dispute resolution clauses are commonly found in commercial contracts, careful consideration should be given to their drafting.
- Parties should note that a tribunal may deem a claim inadmissible for failure to comply with preconditions to arbitration, stay proceedings for any prescribed negotiation period, and/or apply cost penalties.

- Jurisdiction concerns the power of the arbitral tribunal to hear a case.
- Admissibility concerns whether it is appropriate for the arbitral tribunal to hear a case¹ and whether the tribunal should hear the claim because it may be defective and/or procedurally inadmissible.²

Issues of admissibility include:

- Existence, scope and/or fulfilment of conditions precedent or preconditions to arbitration such as a requirement to enter into good faith negotiation, mediation, conciliation, adjudication and/or written notices or requests, time limits or requirements naming specified participants for these procedures. (In the construction context, an arbitration agreement in a building sub-contract may require completion of - or issuance of the completion certificate under - the main contract before arbitration may be commenced.³)
- Whether a claim is time-barred or the limitation period has expired.
- *Res judicata* or whether a judgment bars a subsequent action between the same parties upon the same cause of action.
- Other mootness or ripeness issues. Mootness refers to the claim becoming hypothetical or dead including because the alleged claim no longer exists or has already been resolved and ripeness refers to readiness for arbitration including a claim not resting upon a future event that has not occurred.

C v D confirmed that the admissibility of a claim is a matter for the arbitral tribunal to decide. This has the consequence that if the tribunal decides that the pre-arbitration procedural requirement is a precondition to arbitration that has not been satisfied, it may order a stay of the arbitration proceedings pending compliance with the precondition, dismiss the claim and/or impose costs sanctions.

The distinction between admissibility and jurisdiction is also relevant to the supervisory jurisdiction of the courts. If an issue goes to the admissibility of a claim as opposed to the tribunal's jurisdiction, it alone will not prevent the court from granting a stay of proceedings in favour of arbitration. (Questions of jurisdiction including the existence of an arbitration agreement, on the other hand, will be decided on a *prima facie* standard and if no arbitration agreement is found, no stay will be granted.) Further, once an arbitral tribunal has determined an issue to be one of admissibility as opposed to jurisdiction, that decision is not reviewable by the court in a setting aside application (also confirmed by *C v D*).

It is open to parties to an arbitration agreement to agree (in clear and unequivocal language) that pre-arbitral procedural requirements and other issues of admissibility are instead to go to the jurisdiction of the tribunal.

¹ See the English case of *Republic of Sierra Leone v SL Mining Ltd* [2021] EWHC 286 (Comm) and the Australian case of *The Nuance Group (Australia) Pty Ltd v Shape Australia Pty Ltd* [2021] NSWSC 1498.

² See also the Chartered Institute of Arbitrators' International Arbitration Practice Guideline: Jurisdictional Challenges.

³ See the earlier Hong Kong cases of *Kinli Civil Engineering Ltd v Geotech Engineering Ltd* [2021] HKCFI 2503 and *T v B* [2021] HKCFI 3645 in which the distinction between jurisdiction and admissibility were recognised.

C v D: THE CASE

Facts and findings

Facts

The Plaintiff C was a Hong Kong owner and operator of satellites. The Defendant D was a Thai satellite operator. C and D entered into a Cooperation Agreement for the development, building and deployment of a satellite (Satellite A). Pursuant to the Cooperation Agreement, half of Satellite A's transponders were to belong to D, which had exclusive rights to utilise the same (the Thai Payload). A dispute arose relating to content broadcast from the Thai Payload whose video signals were reaching the PRC, and this was not authorised by PRC authorities. C demanded D to cease transmission at two transponders, which D failed to do, after which C switched them off. D considered C's action to be a repudiatory breach of the Cooperation Agreement and a material default thereunder.

The dispute resolution provision in the Cooperation Agreement provided for arbitration in Hong Kong at the HKIAC in accordance with the UNCITRAL Arbitration Rules if any dispute was not resolved amicably within 60 business days of a party's request in writing for negotiation. The negotiation had to be in good faith. Either party could by written notice refer the dispute for resolution through negotiation to the Chief Executive Officers (CEOs) of the parties (or their authorised representatives), who were to meet within 10 business days of such request.

The CEO of D issued a letter to the board of directors of C referring to an earlier notice of material default served through its lawyers and invited the board to reconsider its position to reinstate the relevant transponders (December Letter). In the December Letter, D indicated its willingness to otherwise refer the dispute to the parties' senior management in accordance with the Cooperation Agreement. Ultimately, neither party referred the dispute to their respective CEOs before referring the dispute to arbitration.

Tribunal findings

A partial award was issued in favour of D (the Partial Award). The arbitral tribunal held that the Cooperation Agreement required the parties to attempt to resolve any dispute by negotiation in good faith, but reference to the respective CEOs was optional. The tribunal further found fulfilment of the condition that arbitration could not be commenced unless the dispute was not resolved within 60 business days of a party's request in writing for negotiation, with the request having been made by way of the December Letter.

C sought for the Partial Award to be set aside on the basis that the tribunal had lacked jurisdiction. C contended that reference of the dispute to the parties' respective CEOs for resolution by way of written notice was a condition precedent to any reference to arbitration, and no such notice had been given.

Court of First Instance decision

At first instance, the court referred to the distinction between jurisdiction and admissibility being recognised in court decisions (as well as academic works) in the UK and the US. Whilst the Hong Kong Arbitration Ordinance (Cap 609) does not expressly draw such a distinction, it is relevant to the construction and application of the want of jurisdiction ground for setting aside an arbitral

award under Article 34(2)(a)(iii) of the UNCITRAL Model Law on International Commercial Arbitration ("Model Law").⁴ Non-compliance with procedural preconditions to arbitration such as a requirement to engage in prior negotiation goes to the admissibility of a claim rather than the tribunal's jurisdiction and C's objection went to admissibility. It was for the arbitral tribunal to decide and not for the court to interfere pursuant to a set aside application.

Court of Appeal decision

The first instance decision was upheld on appeal. On the facts, C's objection was held not to have been that the substantive claim advanced by D could never be referred to arbitration or be arbitrated at all. Its objection was only that the reference to arbitration was premature in that some pre-arbitration requirements should first be observed. C's objection went to the admissibility of the claim rather than the jurisdiction of the tribunal. As such, the Partial Award was not subject to review by the court under Article 34(2)(a)(iii) of the Model Law.

The reasons for the Court of Appeal's adoption of this approach are as follows:

- It is consistent with the commercial purpose of arbitration agreements as explained by Lord Hoffman in the English case of *Fiona Trust & Holding Corp v Privalov* [2007] UKHL 40, which is that parties as rational businesspersons want disputes to be decided by the arbitral tribunal chosen by them, and not for some questions arising out of their relationship to be submitted to arbitration and others to be decided by national courts.
- It furthers the stated object of the Arbitration Ordinance, namely, to facilitate the fair and speedy resolution of disputes by arbitration without unnecessary expense.
- It is in line with the general trend of minimising the permissible scope of judicial interference in arbitral procedures and awards.
- It ensures that Hong Kong does not fall out of line with major international arbitration centres such as London.

The Court of Appeal further emphasised that the distinction between jurisdiction and admissibility is ultimately controlled by the agreement of the parties; arbitration is consensual and it is the parties' agreement which determines the true scope of the disputes which may be submitted to arbitration.

Even disregarding the distinction between admissibility and jurisdiction, the Court of Appeal considered it to be clear that the dispute on the question of fulfilment of the pre-arbitration requirements was a dispute falling within the terms of the submission to arbitration and there was thus no basis for setting aside the award. This is because the dispute resolution clause provided that "any" dispute which could not be resolved amicably within 60 business days may be referred to arbitration and its coverage was not confined to substantive disputes.

⁴ Adopted in section 81 of the Arbitration Ordinance, which provides that an award may be set aside if it deals with a dispute not contemplated by or falling within the terms of the submission to arbitration or contains decisions on matters beyond the scope of the submission to arbitration.

The Court of Appeal also rejected C's argument that the non-fulfilment of preconditions to arbitration meant that the arbitration procedure was not in accordance with the agreement of the parties and this second ground of appeal based on the ground for setting aside an arbitral award in Article 34(2)(a)(iv) of the Model Law was also rejected.

POSITION IN OTHER JURISDICTIONS

England and Wales

In England, pursuant to section 67 of the Arbitration Act 1996, an arbitral award may be challenged on the grounds of the tribunal's substantive jurisdiction, which may require the court to consider the scope of the matters submitted to arbitration in accordance with the parties' arbitration agreement. The Court of Appeal in the *C v D* decision found that the wording of the English provision on substantive jurisdiction is not substantially different from the corresponding Hong Kong provision and as such English case law was relevant.

In the recent case of *Republic of Sierra Leone v SL Mining Ltd* [2021] EWHC 286 (Comm), it was held that alleged non-compliance with preconditions to arbitration is exclusively a matter of admissibility for the arbitral tribunal and cannot lead to a successful jurisdictional challenge under section 67 of the Arbitration Act 1996. The arbitral award in question was challenged on the ground that the three-month negotiation period provided for by the dispute resolution clause had not expired at the date on which a request for arbitration was served. The court held that an objection that a claim was brought too soon goes to the admissibility of the claim rather than the substantive jurisdiction of the tribunal.

The *SL Mining* decision provided welcome clarification, as prior to this, the English authorities were somewhat unclear as to the effect of an obligation to enter into negotiations prior to arbitration on the jurisdiction of a tribunal.

The approach taken in *SL Mining* was applied by the court in *NWA v NVF* [2021] EWHC 2666 (Comm). In that case, a party challenged an award under section 67 on the basis that the parties had failed to comply with the provisions of a multi-tiered dispute resolution clause requiring that disputes be submitted to mediation before arbitration.

In dismissing the section 67 challenge, the court found that non-compliance with the requirement for mediation was an issue of admissibility for the tribunal rather than one of jurisdiction. In addition, failure to comply with the mediation provision did not render the arbitration agreement inoperative. The court was clear that to deprive one party of a right to refer a dispute to arbitration because of another's failure to comply with a precondition would deprive the arbitration agreement of business common sense.

Australia

The Model Law has been adopted in all the States of Australia and in New South Wales, through the Commercial Arbitration Act 2010. In *The Nuance Group (Australia) Pty Ltd v Shape Australia Pty Ltd* [2021] NSWSC 1498, the distinction between admissibility and jurisdiction was adopted and it was held that a time-bar challenge is not a challenge to jurisdiction.

CONCLUSION

C v D is a welcome decision in confirming that questions of admissibility (including the treatment of pre-arbitral requirements) fall exclusively within the remit of the arbitral tribunal unless agreed otherwise by the parties. Where issues of admissibility are for the tribunal to determine, failure to comply with pre-arbitral requirements cannot result in a successful challenge to set aside an award on the grounds of the tribunal lacking jurisdiction to hear the parties' dispute.

Irrespective of the admissibility and jurisdiction distinction, care should be taken in drafting escalation or multi-tier dispute resolution clauses, and parties should consider:

- Whether such a clause is necessary in the first place.
- The operation of the clause and whether it is sufficiently certain and not overly burdensome.
- The length of the period provided for good faith negotiation or other pre-arbitration procedures.

In addition, parties should note that in considering the admissibility of a claim, a tribunal may:

- deem a claim inadmissible for failure to comply with relevant preconditions in a multi-tiered dispute resolution clause;
- stay the proceedings for any prescribed negotiation period; and/or
- apply cost penalties.

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