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Arbitration in Hong Kong: Immune from immunity?

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In a landmark provisional judgment in *Democratic Republic of the Congo v. FG Hemisphere Associates* FACV Nos. 5, 6 & 7 of 2010, the Hong Kong Court of Final Appeal (CFA) has held by a majority of 3:2 that absolute sovereign immunity applies in Hong Kong, with no exception for purely commercial transactions or assets. Taken with the judgment of the Hong Kong Court of First Instance (CFI) in *Intraline Resources SDN BHD v. The Owners of the Ship or Vessel "Hua Tian Long"* HCAJ 59 of 2008 in relation to crown immunity in April 2010, the CFA's judgment means that both sovereign immunity and crown immunity are absolute under the law of Hong Kong. The CFA also confirmed that immunity cannot be waived through a pre-dispute contractual waiver, with important consequences for enforcement against State assets located in Hong Kong. However, and whilst the judgment raises a number of interesting political and constitutional issues, it should not affect the choice of Hong Kong as a leading seat of arbitration when contracting with States and State entities, particularly in PRC-related contracts. In this blog, we take a look at the practical implications of this important judgment, including its impact on arbitral proceedings seated in Hong Kong and potential risks when seeking enforcement against State assets situated in Hong Kong.

Sovereign immunity is premised upon the principle that the courts of one State may not assume jurisdiction over another State without consent (i.e. unless sovereign immunity is validly waived in accordance with the principles discussed below). Accordingly, sovereign immunity in the Hong Kong context will be relevant where the counterparty is a State other than the PRC or a non-PRC State entity. Crown immunity, on the other hand, is premised upon the principle that the courts of a State may not assume jurisdiction over that State (the crown) without its consent. Accordingly, in Hong Kong, crown immunity will be relevant if the counterparty is the PRC or a PRC State entity. (Crown immunity does not apply to the Government of the Hong Kong SAR, against which actions can be brought under the regime set out in the Crown Proceedings Ordinance (Cap. 300)).

It is now clear that both sovereign immunity and crown immunity are absolute under the law of Hong Kong. There is no exception for transactions and assets which are of a purely commercial rather than a sovereign nature (in contrast to the "restrictive" doctrine of sovereign immunity which is applied by many jurisdictions). An entity entitled to immunity will be able to assert it in all transactions and in respect of all assets, regardless of their commercial or sovereign character. Whilst the position in relation to sovereign immunity is technically provisional pending the consideration by the Standing Committee of the National People's Congress (SCNPC) of certain questions referred to it by the CFA under Hong Kong's Basic Law, it seems likely that the interpretation to be rendered by the SCNPC will endorse the overall tenor of the CFA's provisional

judgment.

The CFA in *FG Hemisphere* affirmed the earlier findings of the Court of Appeal (CA) in relation to waiver of sovereign immunity, holding that any waiver must be express and "*in the face of the court*" in order to be effective. In practice, this means that the waiver must be made at the time the court is to exercise jurisdiction. Pre-dispute contractual provisions, such as a Hong Kong court jurisdiction clause or an express waiver clause, will not, therefore, suffice to constitute a waiver of immunity. Based upon the judgment of the CFI in *Intraline*, it appears likely that the same principles regarding waiver will apply to crown immunity as to sovereign immunity at any stage at which the doctrine may be invoked. Where a party is dealing with a State counterparty, it is therefore advisable not to adopt a Hong Kong court jurisdiction clause – although arbitration, including in Hong Kong, will be a viable option, as discussed below. In addition, it would be prudent not to place reliance upon express waiver of immunity clauses, although these should still be included in contracts with State counterparties wherever possible, since they will be effective in many other jurisdictions. Identifying whether or not an entity is part of the State or the crown, and therefore entitled to immunity, may not always be straightforward, and it may be necessary to seek specific advice on a case-by-case basis.

The question of sovereign or crown immunity, and therefore of waiver, does not, strictly speaking, arise in relation to the jurisdiction of an arbitral Tribunal. Arbitration is a consensual process derived from a private contract between the parties, and the authority of the arbitral Tribunal flows from that contract. The adjudication of a dispute by an arbitral Tribunal does not, therefore, involve the exercise of jurisdiction by the courts of a State over any State, whether their own State (in the case of crown immunity) or a foreign State (in the case of sovereign immunity). As the CFA stated in *FG Hemisphere*, "*when a State enters into an arbitration agreement with a private individual or company, that act does not constitute a submission to any other State's jurisdiction. It involves merely the assumption of contractual obligations vis-à-vis the other party to the agreement*." Therefore, no immunity will be engaged by the assumption of jurisdiction by an arbitral Tribunal. It is therefore strictly a misnomer to refer to an arbitration clause as constituting an implied waiver of immunity from the arbitration proceedings themselves, although they are nevertheless commonly characterised in this way (including, for example, in the judgment of the CA). What is clear is that sovereign and crown immunity will not apply to the arbitration proceedings themselves. In this regard, section 34 of Hong Kong's new Arbitration Ordinance (Cap. 609) expressly preserves the principle of "kompetenz-kompetenz", which holds that it is for the arbitral Tribunal (and not, for example, the courts of the seat) to rule upon its own jurisdiction.

Although the CFA did not itself express an opinion on the question of whether or not an arbitration clause will amount to an implied waiver of the supervisory jurisdiction of the courts of Hong Kong over an arbitration seated in Hong Kong or otherwise, it cited a leading work on State immunity by Lady Hazel Fox CMG QC, an eminent commentator on this area, which concludes that "*the exception for arbitration agreements operates… to remove state immunity from the first stage of arbitration in which the national courts exercise supervisory powers*." That conclusion had itself been quoted and approved (albeit in obiter remarks) by the CA, an endorsement which was not disturbed by the judgment of the CFA. It is therefore strongly arguable that the law of Hong Kong accords with customary international law on this issue and an arbitration clause will amount to an implied waiver of immunity in respect of the supervisory jurisdiction of the Hong Kong courts. Furthermore, court proceedings in support of arbitration are relatively rare in practice, and most arbitrations proceed from beginning to end without requiring the input of domestic courts. Moreover, in several important aspects of arbitral procedure, Hong Kong's new Arbitration

Ordinance (Cap. 609) shifts responsibility for functions which have traditionally been part of the supervisory role of the courts to the Hong Kong International Arbitration Centre (HKIAC) (for example, in relation to determining the number of arbitrators, appointing arbitrators and appointing mediators), further narrowing the circumstances in which it will be necessary to invoke the supervisory jurisdiction of the courts.

Whilst there is, of course, an unquantifiable risk that a State counterparty might take this point in any proceedings before the Hong Kong courts in support of an arbitration, Hong Kong remains a very attractive seat. This is particularly so in relation to PRC-related contracts, since Hong Kong is a readily acceptable venue for PRC counterparties who may otherwise be reluctant to agree an offshore seat. In practice, therefore, the judgments of the CFA in *FG Hemisphere* and the CFI in *Intraline* should not affect the choice of Hong Kong as a seat for arbitration.

The most significant impact of the *FG Hemisphere* and *Intraline* cases is in relation to enforcement and execution against assets belonging to a State or a State entity located in Hong Kong. The CFA confirmed in *FG Hemisphere* that an arbitration clause will not operate as an implied waiver of immunity either from enforcement proceedings in the Hong Kong courts or from execution or attachment against assets. In addition, because any effective waiver of immunity must be made "*in the face of the court*" , an express waiver clause will not be effective to waive immunity in respect of enforcement and execution either. The risk posed by immunity in respect of enforcement and execution will be relevant where State assets against which enforcement might be sought are located in Hong Kong, and particularly in cases in which they are the only such assets of the relevant State or State entity. However, the position will be the same regardless of the jurisdiction in which the relevant arbitral Award or court judgment was rendered. Accordingly, whilst immunity in respect of enforcement and execution is an important issue of which to be aware, it should not affect the choice of Hong Kong as a seat of arbitration. In addition, the combined effect of the *FG Hemisphere* and *Intraline* judgments upon dispute resolution in Hong Kong should not be overstated: the issue of sovereign or crown immunity will only apply in the case of contracts with States and State entities, and not those with purely commercial counterparties. With a modern arbitration regime under the new Arbitration Ordinance (Cap. 609), one of the leading arbitral institutions in the HKIAC, and reliable, supportive courts, Hong Kong continues to be an attractive venue for arbitration – particularly when dealing with PRC counterparties.

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