HCA 2776/2016

IN THE HIGH COURT OF THE
HONG KONG SPECIAL ADMINISTRATIVE REGION
COURT OF FIRST INSTANCE
ACTION NO 2776 OF 2016

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BETWEEN

POLYTEC OVERSEAS LIMITED （保利達國際有限公司）	1st Plaintiff
POLYTEC HOLDINGS INTERNATIONAL LIMITED （保利達控股國際有限公司）	2nd Plaintiff
and	
GRAND DRAGON INTERNATIONAL HOLDINGS COMPANY LIMITED （龍浩國際集團有限公司）	1st Defendant
GUANGDONG LONGHAO GROUP COMPANY LIMTED （廣東龍浩集團有限公司）	2nd Defendant
X	3rd Defendant

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Before: Hon Mimmie Chan J in Chambers
Date of Hearing: 8 March 2017
Date of Decision: 22 March 2017

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D E C I S I O N

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Background

1. This is an application made by the 1st and 3rd defendants in this action to stay to arbitration the proceedings issued by the plaintiffs against them, on the basis of an arbitration clause existing in an agreement made between the plaintiffs and the 1st defendant.

2. The 1st plaintiff ("**POL**") is a BVI company which is a wholly owned subsidiary of the 2nd plaintiff ("**PHIL**"), also a BVI company. The 1st defendant (Longhao HK "**LHK**") is a Hong Kong company, which is an associated company of the 2nd defendant (Longhao Guangdong "**LG**"), a PRC company. The 3rd defendant ("**X**") is a shareholder of both LHK and LG, and is also the sole director of LHK.

3. On 25 October 2016, POL and PHIL commenced proceedings against LHK, LG and X. In brief, the plaintiffs claim that LHK and LG were in breach of contract, that X was in breach of the terms of a guarantee, and that LHK and LG were in further breach of fiduciary duties owed to them. POL and PHIL seek various forms of relief, including repayment of a sum of RMB 140 million, and damages for breach of contract or for breach of fiduciary duties.

4. The background of the parties' dealings and relationship, leading to the dispute in this action, is not in dispute. What is disputed by the plaintiffs is whether there is a binding or operative arbitration agreement pursuant to which this action should be stayed.

The agreements

5. On 15 April 2008, POL and LHK entered into an agreement in writing known as the Cooperation Framework Agreement (BOT) ("**BOT**"). The BOT sets out the terms and conditions of the agreement between POL and LHK to establish a joint venture company in Hong Kong ("**JV Company**"), and to cooperate in their joint venture to develop, construct and operate highways on the Mainland ("**Highway Projects**"). POL and LHK agreed to contribute to 70% and 30% respectively of the capital of the JV Company, and to construct and operate the highways on the Mainland through one or more project companies to be established under their agreement ("**Project Companies**"). The JV Company was to act as the parent company overseeing all the Highway Projects tendered or to be tendered for the parties' management and ownership in their joint venture under the BOT.

6. There is no dispute that clause 10.1 of the BOT contains an arbitration clause ("**Arbitration Clause**"), which states that any dispute between the parties in the implementation or performance of the BOT may be submitted to CIETAC in Huanan for arbitration, if the dispute cannot be conciliated:

> "雙方因履行本協議而發生爭議，如協商不成，可向中國國際經濟貿易仲裁委員會華南分會申請仲裁。"

7. According to the Statement of Claim filed in these proceedings ("**SOC**"), an agreement dated 18 April 2008 was made between POL and the Mainland transportation authority, whereby POL was granted the right to invest in, build, manage and operate a highway in Wuhan ("**Hubei Project**"). A wholly owned subsidiary of POL was incorporated on the Mainland, as the Project Company for the Hubei Project.

8. By an agreement dated 5 February 2009 made between PHIL and the relevant Mainland authority, PHIL was in turn granted the right to invest in, build, manage and operate a highway in Hunan ("**Hunan Project**"). A wholly owned subsidiary of PHIL was incorporated on the Mainland, as the Project Company for the Hunan Project.

9. Pursuant to the BOT, X signed 2 written guarantees on 2 December 2008 and 13 March 2009 respectively. Under the guarantees, X undertook on behalf of himself and LHK various obligations in relation to the Highway Projects. The claims made against X in this action are on the basis of his breach of the 2nd guarantee of 13 March 2009 ("**Guarantee**").

10. Variations and supplements were made to the BOT.

11. On 30 May 2009, POL, PHIL and LHK entered into a supplemental agreement ("**1st Supplemental**"), to clarify and supplement the terms of their relationship under the BOT. After referring to the BOT, POL and LHK confirmed in the 1st Supplemental that their agreement to jointly invest in, construct and operate Highway Projects comprised the Hubei Project, and the Hunan Project which had already been acquired in the name of PHIL. PHIL was joined as a party to the 1st Supplemental, and under clause 3 of the 1st Supplemental, PHIL confirmed that the Hunan Project acquired under its name shall be

invested and operated by POL and LHK, on the expressed condition that POL and LHK shall comply with the BOT and the 1st Supplemental.

12. Clause 4 of the 1st Supplemental states that the 1st Supplemental is supplemental to the BOT, and has equal force and effect（“具有同等效力”）as the BOT (“**Equal Force Provision**”).

13. Clause 5 of the 1st Supplemental states as follows (“**Litigation Provision**”):

> “凡因本協議產生或有關本協議的任何爭議或分岐均應提交中國香港特別行政區法院審理解決。
>
> (Any dispute or difference arising or in connection with this agreement should be submitted to the courts of the HKSAR for resolution.)”

14. In mid-2009, POL, PHIL and LHK agreed to vary the BOT (“**Variation Agreement**”), to the effect that the requirement of setting up the intended JV Company would be dispensed with, and that the Hubei Project and Hunan Project would be directly managed and operated by the subsidiary companies of POL and PHIL. POL, PHIL and LHK would accordingly directly fund the Project Companies in the same proportion as they had intended to contribute to the intended JV Company under the BOT, ie 70% and 30% respectively.

15. Disputes arose between the parties, as a result of which works under the Hubei Project and Hunan Project were halted. It is alleged that LHK failed to pay its 30% contribution to the funding of the Project Companies as agreed under the BOT, as a result of which workers’ wages and suppliers could not be paid. The plaintiffs also claim that they were unable to exercise control over the Project Companies, as a result of the refusal by LHK, LG and X to cooperate with them.

16. On 26 January 2015, 6.5 years after the 1st Supplemental, a further agreement was made between POL, PHIL, LHK and LG (“**2nd Supplemental**”). The parties referred in the recitals to the BOT and the 1st Supplemental. The 2nd Supplemental further recites that as a result of their discussions, the parties had reached agreement on their dispute in relation to the Hunan Project and the Hubei Project.

17. Under the 2nd Supplemental, the parties set out the terms of their continued involvement in the Projects. It was agreed (inter alia) that LHK and LG would contribute 30% (the same percentage specified as LHK's contribution under the BOT to the capital of the JV Company) of the Hunan Project and the Hubei Project, and that POL and PHIL would have independent and complete management power and control over the Project Companies. The 2nd Supplemental further provides that LHK and LG would be liable for liquidated damages if they caused any suspension of works. The amounts which had been injected by POL and PHIL were confirmed, and the amounts which were outstanding from LG were set out, in the 2nd Supplemental.

18. In particular, the 2nd Supplemental (1) confirmed that LHK and LG had returned approximately RMB 1.12 billion to POL and PHIL, being part of the construction costs paid by POL and PHIL, as X had agreed orally with POL and PHIL before the making of the BOT; and (2) provided a mechanism for further and ongoing payment to POL and PHIL of part of the construction costs, as agreed and as may accrue over time ("**Construction Costs Repayment Provisions**").

19. Clause 10 of the 2nd Supplemental states that the agreement represents the final and comprehensive settlement of matters between the parties and relating to the Project Companies, and that apart from personal guarantees and undertakings, the 2nd Supplemental prevails in respect of any inconsistencies with past agreements and supplemental agreements ("**Inconsistency Provision**").

20. The 2nd Supplemental is silent as to the method of dispute resolution.

Applicable legal principles

21. The principles applicable to the determination of the application for stay of these proceedings are not disputed.

22. Section 20 of the Arbitration Ordinance ("**Ordinance**") incorporates Article 8 of the Model Law. Article 8 (1) states:

> "A court before which an action is brought in a matter which is the subject of an arbitration agreement shall, if a party so requests not

> later than when submitting his 1st statement of the substance of the dispute, refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed."

23. As the court set out in *Tommy CP Sze v Li & Fung (Trading) Ltd* [2003] 1 HKC 418, the 4 questions for the court are: (1) Is there an arbitration agreement between the parties? (2) Is the clause in question capable of being performed? (3) Is there in reality a dispute or difference between the parties? (4) Is the dispute or difference between the parties within the ambit of the arbitration agreement.

24. The onus is on LHK and X as the applicants for stay to show that there is a prima facie or plainly arguable case that the parties are bound by an arbitration clause, and unless the point is clear, the court should not resolve the issue, and the matter should be stayed in favor of arbitration for the arbitral tribunal to determine its own jurisdiction (*PCCW Global Ltd v Interactive Communications Services Ltd* [2007] 1 HKLRD 309).

25. For the stay to apply, the action before the court must be "in the same matter" that is the subject of the arbitration agreement, and not purely "related" to it or "involved" in it (HM Holtzmann & J Neuhaus, *A Guide to the UNCITRAL Model Law*). In ascertaining the "matter", the court should consider the substance of the controversy as it appears from the circumstances and evidence, and not just the particular terms in which the claimant has sought to formulate its claim in court (Merkin, *Arbitration Law*, para 8.20 and the cases cited therein). The focus is on the substance of the dispute, and not the pleadings.

The claims made in these proceedings

26. The pleadings are nevertheless relevant and should be considered, before the court can ascertain the substance of the dispute and the matter which is before the court.

27. In this action, POL and PHIL as plaintiffs claim that LHK and LG are in breach of the BOT as supplemented by the 2nd Supplemental, and that X is in breach of his Guarantee. It was argued on behalf of POL and PHIL that considered in the context of the SOC, the relief sought by the plaintiffs are sought under and on the basis of the 2nd Supplemental and the Guarantee, and not the BOT. However, if the SOC is considered in

detail, it can be seen that the plaintiffs' claims are made for repayment of amounts due under the 2nd Supplemental, as a result of the rights and obligations of LHK, LG, POL and PHIL under the BOT, as supplemented by the 2nd Supplemental.

28. As the plaintiffs plead (in paragraph 9 of the SOC), the BOT sets out the framework of the cooperation between POL and LHK in relation to the Highway Projects tendered and to be tendered on the Mainland. POL was to hold and contribute 70% of the share capital of the JV Company which was intended to hold the Highway Projects, and LHK was to hold and contribute 30% of such capital. Adjustments were to be made to the shareholding in the event of either party failing to make its share of the capital contribution. Under the BOT, LHK undertook the responsibility to organize the construction of the Project and to ensure the quality of the construction.

29. The plaintiffs claim, in paragraph 19 of the SOC, that the 1st Supplemental was entered into by POL, PHIL and LHK "to clarify and supplement the terms of their relationship under the BOT". POL and LHK agreed under the 1st Supplemental to carry out the investment, construction and operation of the Hunan Project and the Hubei Project in accordance with the BOT (as alleged in paragraph 19 (2) of the SOC), and PHIL agreed that the Hunan Project listed under the name of its subsidiary was to be jointly invested, built and operated by POL and LHK (paragraph 19 (3) of the SOC).

30. The fiduciary duties relied upon by POL and PHIL are claimed to be owed by LHK and LG as the "joint-venture partners" of POL and PHIL (paragraph 25, SOC), since POL claims that it had entered into the BOT in reliance on the expertise, experience and connections of LHK, LG and X in infrastructure and construction projects on the Mainland. The fiduciary duties were to act honestly, in good faith and in the best interests of the plaintiffs' interests in the Project Companies, and (inter alia) not to exercise the powers conferred upon them under the BOT for improper purposes (paragraph 25 of the SOC).

31. Under the BOT as varied by the Variation Agreement, LHK was liable to contribute 30% of the funding of the Project Companies. According to the 2nd Supplemental, the outstanding sum from LHK was crystallized at RMB 612,188,331.96 ("**Outstanding Amount**"), as at 16 January 2016. Under the 2nd Supplemental, it was agreed that LHK and LG may request for a loan from POL and PHIL for repaying the Outstanding Amount, but if

LHK and LG failed to settle the Outstanding Amount within 6 months from the date of the 2nd Supplemental, the parties' respective shareholding in the Project Companies would be adjusted, to reflect *pro rata* the respective actual contribution made by the parties.

32. Paragraph 40 of the SOC pleads that the 2nd Supplemental is "consistent with and reflects the spirit of clause 3.2B of the BOT", and that "at all material times since the conclusion of the (BOT), notwithstanding the subsequent interposition of the (1st Supplemental), the Variation Agreement and the (2nd Supplemental), the parties' respective obligation to fund the Project Companies has always remained unchanged".

33. POL and PHIL claim that LHK and LG breached the 2nd Supplemental, by (inter alia) failing to inject sufficient funds into the Project Companies, and that they had failed to pay the actual construction costs of the Highway Projects, which led to the suspension of the project works. They further claim that LHK and LG failed to pay the Outstanding Amount (which represented the funding contribution from LHK/LG), and further failed to comply with their obligations under the Construction Costs Repayment Provisions to make payment of a sum of RMB 140 million, accrued since the date of the 2nd Supplemental. It is also the claim of POL and PHIL that they had been denied of their right of control and management of the Project Companies.

34. On the basis of the foregoing breaches, POL and PHIL claim in the SOC that LHK and LG had committed a repudiatory breach of the BOT, as supplemented or varied by the 1st Supplemental, the Variation Agreement and the 2nd Supplemental, evincing an intention not to be bound by the same. It is alleged that given the complete suspension of the project works, there is no prospect for the Hunan Project and the Hubei Project to be completed by 30 December 2016, as warranted under the 2nd Supplemental, and that LHK and LG had committed an anticipatory breach of the 2nd Supplemental.

35. As against X, it is claimed that he is in breach of the Guarantee by failing (inter alia) to properly manage and organize the Highway Project works and to manage and supervise the Project Companies.

36. By way of relief, the plaintiffs' claim in the action are for a declaration as to the respective shareholding in the Project Companies of POL, PHIL, LHK and LG; payment

of the sum of RMB 140 million pursuant to the Construction Costs Repayment Provision, and damages for breach of contract or breach of fiduciary duties.

Is there an arbitration agreement in respect of the claims made in the action?

37. As highlighted by Senior Counsel for LHK and LG, it is not the plaintiffs' pleaded case that the BOT has in any way been superseded or replaced by the 1st Supplemental, or by the 2nd Supplemental. To the contrary, the BOT is referred to in the SOC as the basis of the parties' cooperation and joint venture relating to the Highway Projects. The 1st Supplemental is said to have been entered into by PHIL together with POL and LHK, in order to clarify and supplement the terms of their relationship under the BOT (by inclusion of the Hunan Project), and the 2nd Supplemental is claimed (in paragraph 40 of the SOC) to be consistent with and reflects the spirit of the BOT. In clause 1 as well as clause 2 of the 1st Supplemental, POL and LHK confirm that they will perform the terms of the BOT, and to complete the investment, construction and operation of the Hunan and Hubei Projects in accordance with, or on the basis of, their agreement under the BOT.

38. On my reading of the SOC and the terms of the relevant agreements referred to, the claims made by the plaintiffs against LHK, LG and X are on the basis of the BOT - as supplemented by the Variation Agreement, the 1st Supplemental and the 2nd Supplemental.

39. Having considered the substance of the claims made against LHK and X in this action, the dispute between POL, PHIL and LHK as to the amounts said to be owing and due from LHK, and as to LHK's breach of its obligations by failing to cooperate with POL and PHIL in the management of the Highway Projects, arise in the parties' performance or implementation of the BOT, and therefore fall within the ambit of the Arbitration Clause.

40. By entering into the 1st Supplemental, can the parties be said to have agreed to dispense with, or to replace the BOT with the 1st Supplemental, such that the Arbitration Clause in the BOT should be ignored by the court? This has to be considered in the light of the terms of the 1st Supplemental and in particular the Litigation Provision, and in the context of the parties' dealings and the circumstances of the case.

41. It is relevant to bear in mind that the parties had been dealing with each other since the BOT was made in 2008. There was, according to the plaintiffs, also a related oral agreement between X, POL and PHIL before the BOT was signed. The parties proceeded with their joint investment in, and management of, the construction of the Highway Projects on the basis of the whole series of the agreements made between them, signed between April 2008 and January 2015, as varied by and/or supplementing one or the other. The substance of the plaintiffs' claims in this action is that the structure of the parties' venture essentially remained the same, as set out in the BOT, despite the variations made in 2009. Even when the 2nd Supplemental was made, the plaintiffs' case on the face of the SOC is that the 2nd Supplemental simply confirmed the outstanding obligations of the parties and recorded the arrangement agreed in 2016 as to how the liabilities incurred under the BOT were to be further discharged.

42. There is no apparent dispute between the parties that the Hubei Project had been included in the BOT and the joint venture between the parties thereunder, by virtue of the 1st Supplemental.

43. It is in my judgment pertinent that the 1st Supplemental expressly states (in clause 4) that it is a supplement to the BOT, and that it has equal effect as the BOT. Any suggestion that the 1st Supplemental replaces or has superceded the BOT entirely would be contrary to the express terms of clause 4. It would also be inconsistent with the references made, in clauses 1, 2 and 3 of the 1st Supplemental, to the parties' obligations to perform the terms of the BOT, to complete the investment and construction of the Highway Projects in accordance with their agreement under the BOT, and on the basis of POL's and LHK's performance of the terms of the BOT.

44. Although the 2nd Supplemental is said to represent the "final and comprehensive settlement and resolution of matters between the parties in relation to the Project Companies", the liabilities and obligations of LHK and LG as set out in the 2nd Supplemental with respect to the 30% contribution arose out of the BOT. On the whole, I do not consider that the 2nd Supplemental can be clearly said to be a new and independent agreement, self-contained and separate from the BOT. The 2nd Supplemental in effect sets out arrangements as to how the liabilities incurred under the BOT were to be paid or financed (by loans, if necessary), as appropriate.

45. It cannot be disputed that a valid arbitration agreement can be expressed in permissive terms (as by use of "may" in the Arbitration Clause), conferring the right on LHK in this case to require the plaintiffs under the Arbitration Clause to submit the dispute to arbitration by an application for stay (*Hermes One v Everbread Holdings Ltd and Others* [2016] 1 WLR 4098).

46. According to the plaintiffs, the Litigation Provision in the 1st Supplemental is clearly inconsistent with the Arbitration Clause in the BOT, and this goes against any incorporation of the Arbitration Clause into the 1st Supplemental, despite the references it made to the BOT.

47. However, since there is no dispute resolution clause in the 2nd Supplemental, there is no "inconsistency" between the Arbitration Clause and the 2nd Supplemental, for the Inconsistency Provision in the 2nd Supplemental to apply, and to replace or supersede the BOT.

48. It is important to bear in mind the reminder from the Court of Appeal in *PCCW Global Limited v Interactive Communications Service Ltd* that at this stage, the court is simply to determine on a *prima facie* basis whether there is a valid arbitration agreement. In the judgment of Tang VP (as His Lordship then was) in *PCCW*, reference was made to the decision of the Court of Appeal in *Private Company "Triple V" Inc v Star (Universal) Co Ltd & Another* [1995] 2 HKLRD 62, in which Litton VP explained:

> "The judge said this:
>
> > There is *prima facie* evidence of a dispute between the plaintiff and D1 in relation to contract 93 RV-1034HK and an arbitrator or to be appointed to arbitrate their dispute. It will be for the arbitrator to decide the effect, if any, of the alleged subsequent agreement canceling the contract.
>
> I agree. If the judge were to go into the matter more deeply, he would in effect be usurping the function of the arbitrator. Whilst, clearly, the judge had to make a judgment as to whether there existed an underlying agreement to arbitrate, he could do no more than to form a *prima facie* view." (Emphasis added)

49. Bearing in mind the language of the Arbitration Clause, the provisions of the 1st Supplemental, the absence of a dispute resolution clause in the 2nd Supplemental, the affirmation in the 1st Supplemental and in the 2nd Supplemental as to the continuing (and

equally) binding and operative effect of the BOT, and the nature of the claims made by POL and PHIL against LHK and LG in these proceedings, my view is that LHK has adequately established a plainly arguable case, predicated on cogent and not dubious or fanciful evidence (*Pacific Crown Engineering Ltd v Hyundai Engineering Construction Co Ltd* [2003] 3 HKC 659) that an arbitration clause or agreement existed between POL, PHIL and LHK in relation to the claims made against LHK and LG under and on the basis of the BOT. I do not consider that it is clear that the BOT has been superceded or replaced. It would appear to be arguable that the parties regarded their dealings and relationship under the joint venture to be governed by the series of the BOT, the 1st Supplemental and the 2nd Supplemental, as supplementing one another. Whether and how, on construction, the Arbitration Clause can be reconciled with the Litigation Provision in the 1st Supplemental should be determined by the arbitral tribunal.

Is the Arbitration Clause inoperative?

50. The plaintiffs claim that in January 2017, they "came to know" that LHK and LG had commenced civil proceedings against the plaintiffs and another party in the Higher People's Court of Hunan on the Mainland ("**Hunan Proceedings**"). It is claimed that in the Hunan Proceedings, LHK and LG seek the return of funds they had injected into the Hunan Project Company pursuant to the BOT. The plaintiffs claim that by commencing such proceedings, the position adopted by LHK and LG is inconsistent with their application for stay of the Hong Kong action to arbitration. It is argued that by exercising the right to commence the Hunan Proceedings, LHK and LG have made a final election between their alternative and inconsistent rights to litigate in Hunan and to proceed to arbitration in accordance with the Arbitration Clause. Accordingly, the plaintiffs argue that LHK and LG are estopped from pursuing the arbitration proceedings, in the sense that they cannot re-exercise the right to the opposite effect (Handley, *Estoppel by Conduct and Election* (2nd Ed, 2016, paras 14-002 to 14-003 and 14-008), and that the Arbitration Clause is hence inoperative.

51. As illustrated in the case of *Sargeant v ASL Developments Ltd* (1974) 131 CLR 634, 646, for the doctrine of election as between two inconsistent legal rights to apply, the words or conduct ordinarily required to constitute an election must be unequivocal, in the sense that it is consistent only with the exercise of one of the two sets of rights and inconsistent with the exercise of the other. Even in the case of *The "Thor Scan"* [1999] 2

HKLRD 136 relied upon by the plaintiffs, the court emphasized that for waiver to operate, the party in question must have, by conduct, clearly and unequivocally abandoned his right or indicated that he was not exercising such right.

52. In *The "Thor Scan"*, Chan CJHC (as His Lordship then was) referred to the case of *The Kanchenjunga* [1990] 1 Lloyd's Rep 391, where Lord Goff explained the principle of waiver, and in the particular relevant context, waiver in the sense of abandonment of a right which arises by virtue of a party making an election. Chan CJHC summarized the position and explained that for the principle of waiver to operate, it must be shown that: (1) a party has a right under a contract or by operation of law; (2) he knows of the existence of the right or the facts giving rise to such right; and (3) he has, "by conduct, clearly and unequivocally abandoned his right or indicated that he is not exercising such a right".

53. Ultimately, each case must of course be considered in the context and on its own facts. In *The "Thor Scan"* itself, the appellant had commenced proceedings in the Netherlands, and pursued it to judgment or a decision being handed down by the Dutch court in the Netherlands, finding that it was not competent to deal with the claim as the principal place of business of the appellant was the Antillles. Such conduct of commencing, and pursuing, the Dutch proceedings was held by the court to be clear and unequivocal abandonment of the appellant's right to arbitrate, or clear and unequivocal indication that the appellant was not exercising the right to arbitrate.

54. In the present case, and on the evidence available at this stage, I cannot find that the conduct of LHK and LG, as relied upon by the plaintiffs, is sufficiently unequivocal. The evidence is unclear as to whether the plaintiffs have been served with the Hunan Proceedings. They only claim that after being served with LHK's application to stay this action in December 2016, they came to know, around 27 January 2017, that the Hunan Proceedings had been started. It is not clear when the Hunan Proceedings were commenced, whether it was before or after the application to stay these Hong Kong proceedings. In any event, LHK has filed evidence in this action to show that they had already applied to the Hunan court, on 12 January 2017, for leave to withdraw the Hunan Proceedings, and LHK is ready, able and willing to proceed to arbitration in respect of the claims made against it in these proceedings.

55. In my view, there is insufficiently clear evidence that LHK had clearly indicated to the plaintiffs by its conduct that LHK was unequivocally exercising its right to litigate in Hunan, and was abandoning its right under the Arbitration Clause. Just as the court should only form a *prima facie* view on the existence of an arbitration agreement, it should order the stay unless it is clear that the arbitration agreement is inoperative.

56. Having found there to be a *prima facie* case of the existence of an arbitration agreement between the plaintiffs and LHK, which agreement has not been clearly shown to be inoperative, I will grant the mandatory stay under s 20 of the Ordinance, for the matter to be referred to arbitration and for the tribunal to decide the dispute, including any dispute as to its jurisdiction and as to the existence and effect of the arbitration agreement.

The claims against X

57. As for the Guarantee, it was signed on 13 March 2009, before the 1st Supplemental containing the Litigation Provision was made on 30 May 2009. It cannot be said that the parties had intended, at the time the Guarantee was made, that the Litigation Provision would apply. On behalf of the plaintiffs, it was argued that X was not a party to the BOT which contains the Arbitration Clause, such that the plaintiffs cannot be bound to pursue their claims against X by arbitration.

58. The mere fact of X not being a party to and not being bound by the Arbitration Clause is not a sufficient basis for relieving the *plaintiffs* of their obligation under the Arbitration Clause, to submit their disputes with LHK and LG which arise in the implementation or performance of the BOT to arbitration (*New Sound Industries Ltd v Meliga (HK) Ltd* [2005] 1 HKC 41). The disputed claims made by POL and PHIL against X under the Guarantee are in fact disputes in the performance of the obligations of LHK under the BOT, to fall within the scope of the Arbitration Clause. The Guarantee does not have an arbitration clause. It is a matter of construction whether or not there has been incorporation of the Arbitration Clause by reference (*Astel-Peiniger Joint Venture v Argos Engineering & Heavy Industries Co Ltd* [1995] 1 HKLRD 300), and I agree with Leading Counsel for the plaintiffs that the mere reference to the BOT in the recitals and in clause 1 of the Guarantee is not sufficient reference to make the terms of the BOT (and in particular the Arbitration Clause) part of the Guarantee (within the meaning of Article 7 (6) of the Model Law and s 19 (3) of

the Ordinance), to constitute the existence of an arbitration agreement between the plaintiffs and X.

59. The claims made against X in this action under the Guarantee are founded on alleged breaches of LHK's obligations under the BOT, as varied and supplemented by the 1st Supplemental and 2nd Supplemental, and X, LHK and LG are all closely related. The liability of X under the Guarantee depends on whether LHK is liable to the plaintiffs under the BOT and the 2nd Supplemental. Since I am staying the action against LHK to arbitration, it will be a waste of costs and risking conflicting outcomes in the arbitration and in these proceedings, if I were to allow this action against X to proceed in tandem with the arbitration. For these reasons, I will exercise the court's discretion under its inherent jurisdiction, to stay the plaintiffs' claims against X in these proceedings until after the resolution of the arbitration between POL, PHIL, LHK and LG.

Orders

60. The application by LHK and X for stay of these proceedings is accordingly granted, in term of paragraph 1 of the Summons issued on 5 December 2016. I make an order nisi that the costs of the stay application are to be paid by the POL and PHIL to LHK and X, with certificate for 2 counsel.

61. By consent, leave is granted for the filing of the further affirmations, including those referred to in the summonses of 20 February 2017 and 27 February 2017, with costs in the cause of the Summons of 5 December 2016.

(Mimmie Chan)
Judge of the Court of First Instance
High Court

Mr Paul Lam SC and Mr Vincent Lung, instructed by ONC Lawyers,
for the 1st & 2nd plaintiffs

Mr Richard Khaw SC and Ms Bonnie Cheng, instructed by M/S Jones
Day, for the 1st & 3rd defendants