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THE RELATIONSHIP BETWEEN CHEQUES (AND OTHER BILLS OF EXCHANGE) AND ARBITRATION CLAUSES

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SUMMARY

In T v W (HCA 366/2020, [2020] HKCFI 2918), the Hong Kong Court of First Instance considered the interesting question of whether a claim made on a dishonoured cheque was caught by and fell within the application of an arbitration clause in the underlying loan agreement in respect of which the cheque was issued.

The Loan Agreement and the Cheque

On 22 March 2019, the Plaintiff (as the lender) and the Defendant (as the borrower) entered into an agreement for a loan of HK$5 million with monthly interest of 2.5% (the "**Loan Agreement**").

The Loan Agreement provided that the governing law of the agreement was Hong Kong law, and that any dispute should be arbitrated in Hong Kong. (Unfortunately, the judgment does not quote the actual wording of the arbitration clause. The judgment says simply that the underlying Loan Agreement provided that "any dispute should be arbitrated in Hong Kong": para 4 of the judgment.)

On 16 May 2019, the Defendant drew a cheque payable to the Plaintiff for repayment of the loan (the "**Cheque**"). The Cheque was postdated 21 September 2019, which was the agreed repayment date of the loan. The Loan Agreement referred to the Cheque as being "*evidence*" of the loan.

It would seem that the Cheque was dishonoured when presented by the Plaintiff to the bank for payment. On 19 March 2020, the Plaintiff initiated a court action to claim the sum of HK$5 million and interest, as due and payable under the Cheque. The court action was a simple court action, claiming just in respect of the dishonoured Cheque, rather than purporting to be a claim in respect of the underlying loan.

On 6 May 2020, the Defendant applied to stay the Plaintiff's action in favour of arbitration. The Defendant relied on article 8 of the UNCITRAL Model Law (as adopted by section 20(1) of the Arbitration Ordinance (Cap. 609)):-

> *"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 first statement on 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".*

The obvious question that arose was: whether the Plaintiff's claim on the Cheque falls within the ambit of the arbitration clause of the Loan Agreement, and hence whether the Plaintiff's action should be stayed in favour of arbitration.

The Hong Kong Court of First Instance (the "**Court**") held that the arbitration clause in the Loan Agreement could not be construed to extend to the claims made under the Cheque. We will look at the Court's analysis below.

Presumption against the inclusion of bills of exchanges without "*plain manifestation*"

It is trite that a bill of exchange creates a separate cause of action, and therefore is a separate contract to the underlying contract.

The Hong Kong Court of Appeal in *CA Pacific Forex Ltd v Lei Kuan Ieong* [1999] 1 HKLRD 462 held that an arbitration clause must contain a "*plain manifestation*" that it is applicable to a bill of exchange before the presumption against taking a bill of exchange into arbitration is to be rebutted.

In the absence of such "*plain manifestation*", an arbitration clause would not extend to claim under a bill of exchange, unless there is some special reason arising from the intention of the parties, or the circumstances of the case.

Pro-arbitration trend and one-stop dispute resolution presumption

The well-known arbitration case of *Fiona Trust & Holding Corporation v Privalov* [2007] 4 All ER 951 is often cited for the proposition that the modern pro-arbitration trend favours the one-stop dispute resolution presumption. *Fiona Trust* advocated that the presumption should be that the parties intended that all disputes arising out of the same relationship should be determined by the same tribunal, unless there is clear language to exclude any particular dispute.

Language of the arbitration clause in this case

The Court held that deciding whether to apply *CA Pacific* on the one hand or *Fiona Trust* on the other hand, will depend on the language used in the arbitration clause. In the exercise of construing the arbitration clause, if there is any conflict as to the significance to be placed upon any presumption, the Court is bound by the decision of the Hong Kong Court of Appeal in *CA Pacific*.

In this case, the arbitration clause in the Loan Agreement provided that "*any disputes*" should be submitted to arbitration. The Court held that "*disputes*" should be construed to cover only disputes relating to the Loan Agreement and the parties' claims and liabilities under the Loan Agreement.

The phrase "*any disputes*" in the arbitration clause did not establish a "*plain manifestation*" of the parties' intention for the arbitration clause to be extended to claims and disputes as to the parties' rights and liabilities under the Cheque.

Reference of the Cheque in the Loan Agreement

In this case, the Cheque was referred to in the Loan Agreement as "*evidence*" of the loan and the agreement to repay the loan.

However, by reading the Loan Agreement as a whole, the Court's view was that it was the intention of the parties for the Cheque to be offered and retained as security for the Defendant's repayment of the loan on the due date. The fact that the Cheque and the Loan Agreement were separate contracts at law should not per se be treated as being negated by the reference to the Cheque in the Loan Agreement.

How is a bill of exchange (including a cheque) considered by reasonable and rational business people?

Generally, a bill of exchange is regarded as the equivalent of cash because of its high degree of convertibility and the limited grounds for resisting enforcement. Reasonable and rational business people are entitled to have high regard for the importance and value of a bill of exchange being issued and held as security, so as to ensure due payment and to facilitate easy and speedy enforcement of the security.

In this case, the Court held, the issue of the Cheque implied the parties' acceptance of the Plaintiff's entitlement to a quicker and easier recovery procedure for the sum due under the Cheque through legal action. Any attempt to hold an arbitration clause of an underlying contract as applicable to a bill of exchange would make "*a substantial inroad upon the commercial principle on which bills of exchange have always rested*".

Comment

An important point to note is that this case involved a claim that was framed purely and simply as a claim upon one dishonoured cheque. It was not framed by the claimant in any way by reference to the underlying transaction that contained the arbitration clause.

It will be interesting to see how this interplay, between the dishonoured cheque and the underlying transaction pursuant to which the cheque is issued, is viewed when the facts become more complicated. For example, where the cheque issuer raises cross-claims under the underlying transaction by way of a legal or equitable set-off against the debt covered by the dishonoured cheque. Or where the arbitration clause is a more complex or bespoke clause than the very simple clause that seemed to apply in this case.

The case does serve as a reminder to drafters of arbitration clauses to be careful to ensure that the clause is drafted so as to fit specifically with the transaction involved.

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MEET THE TEAM

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