



CISG and Hong Kong: its Implications on Hong Kong Arbitration

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Since the United Nations Convention on Contracts for the International Sale of Goods (“CISG”) became effective in 1988, 94 States have so far adopted it (as of December 2021). However, Hong Kong, being one of the international trade centres in the world, has only demonstrated intention to seek its application last year.

Recently in September 2021, the Legislative Council of the HKSAR has enacted the Sale of Goods (United Nations Convention) Ordinance (Cap 641), which will soon bring the CISG into place.

Before the handover, the CISG was not applicable to Hong Kong, against the background that the UK is not a party to it. After the handover, the status quo

on non-application of the CISG has been maintained. The reason for it may be similar to that of the UK, whose legal tradition has a great impact on Hong Kong’s legal system.

Historical Reasons why the CISG Has Not Been Applicable to Hong Kong

On this interesting question, it might be helpful to see why the UK refused to join

the CISG.

One major reason would be that the CISG is a mix of civil and common law, which involves compromises by countries of both legal traditions to agree to an internationally adopted convention. The hesitation of legal practitioners from the UK is based on their unfamiliarity with the civil law concepts involved in the CISG, including the fundamental breach, right to cure after the time fixed for performance and the self-help remedy of reducing the price where non-conforming goods are delivered.

The above appears to lead to the second reason why the UK is not eager to ratify CISG. It is because it sees the ratification as having the effect of diminishing the role of English law in settling international trade disputes, which would reduce the number of disputes to be solved in the UK (see "Convention on Contracts for the International Sale of Goods – Comments by the Council's Law Reform Committee," *Report of The Law Society of England & Wales*). This argument is mainly based on the self-perception of the UK legal practitioners that English Law is a world brand-name, and such prestigious position of the English Law might be jeopardized by ratifying the CISG (see Angele Forte, "The United Nations Convention on Contracts for the International Sale of Goods: Reason or Unreason in the United Kingdom", (1997) 26 *Baltimore Law Review* 51-66).

Concerns for uniformity is another issue. Lawyers in the UK have doubts on the uniformity in the application of the Convention, as it may be interpreted variously without any standard interpretation. This is particularly true when interpretation of law is usually with reference to case laws.¹ Some also see the flexibility offered by the Convention as diminishing its effectiveness because traders can simply opt out, and uniformity would be affected as well.

It seems that the above concerns similarly apply to some local legal practitioners after 1997, as Hong Kong's international sales law continues to be based on the relevant English law and legal principles.

Benefits for the Application of the CISG to Hong Kong

The HKSAR Government conducted a public consultation on the proposed application of the CISG to Hong Kong ("the Proposed Application") last year. The Proposed Application has received positive comments from different stakeholders. The following 6 main benefits were identified by major supporters.

First, the Proposed Application would help to facilitate Hong Kong's international trade development. As of December 2021, 94 states have adopted the CISG, including more than half of Hong Kong's top 20 trading partners by total trade value. With its great coverage, joining CISG will likely reduce the legal barriers, frictions and uncertainties regarding international trades, with the upshots of enhancing trades between Hong Kong and CISG party states, raising Hong Kong's reputation as an international leading centre of trade and commerce, and thus promoting Hong Kong's GDP and trade growth in the long run.

Second, the Proposed Application would strengthen Hong Kong's position as a leading centre for international legal and dispute resolution services in the Asia-Pacific Region, in terms of both arbitration and litigation. Hong Kong lawyers will become more equipped and better placed to advise on transactions from the CISG perspective. Hence, the Proposed Application will improve Hong Kong's competence in resolving disputes in relation to the CISG and may even promote Hong Kong's status as a dispute resolution hub for CISG disputes. Given the "neutral" nature of the CISG, it is usually welcomed by parties in dispute and their arbitrators. By applying the CISG to Hong Kong, Hong Kong's standing as an international trade and legal dispute resolution hub may be consolidated.

Third, in the context of the Belt and Road Initiative ("BRI"), the Proposed Application will also be beneficial. Currently, about 45% of the BRI countries are contracting parties to the CISG. The CISG will help to form an important basis for "bridging legal systems" among BRI

members, thus enhancing Hong Kong's status as a dispute resolution hub for CISG disputes, which would be favourable to sales of goods contracts between Hong Kong and other BRI countries governed by the CISG.

Fourth, following the Proposed Application, the current Hong Kong law on international sale of goods would be improved in three main areas, namely contract modification, effective acceptance and merchantable quality. This is likely to enhance the attractiveness of Hong Kong law to parties who are more familiar with the CISG, as they have greater confidence in the law.

Fifth, the CISG has a gap-filling function for small and medium enterprises (SMEs). It is common for SMEs to be involved with trades that are not properly protected by contracts drafted by lawyers. The CISG then serves the "gap-filling" function in helping these SMEs to save time and costs when conducting cross-border deals.

Lastly, the application of the CISG is flexible, as it allows flexibility and freedom for parties to choose. Parties may apply the CISG flexibly and exclude any articles (with the exception of Article 12, which concerns requirements as to form of contract²) that they do not wish to apply, thus bolstering commercial convenience.

Apart from the benefits raised during the consultation process, there are also other benefits worth noting. For example, the CISG provides a modern, uniform and fair regime for contracts for the international sale of goods, introducing certainties in commercial exchanges and reducing transaction costs. Also, by adopting a globally recognised set of rules, the CISG helps to prevent Hong Kong businesses from being subjected to unfamiliar foreign laws when entering into cross-boundary transactions.

CISG's Impact on Arbitration, in Particular in the Area of Trades and Shipping

CISG and Arbitration

The CISG was not designed to govern arbitration agreements, but international sales contracts. Nonetheless, the CISG governs basic contract law concepts including formation (Articles 14-24), interpretation (Article 8) and remedies for breach, which are relevant in determining the substantive validity of arbitration agreements. Thus, the CISG would be relevant to such determination when it governs a sales contract containing an arbitration clause itself.

When the CISG governs a sales contract containing an arbitration clause, some have argued that the CISG should be the law applicable at the seat of arbitration regardless of its “procedural” character (see Pilar Perales Viscasillas and David

Ramos Muñoz, “CISG and Arbitration in Andrea Büchler and Markus Müller-Chen,” (2011) *Private Law (national - global - comparative - Festschrift für Ingeborg Schwenzer zum 60. Geburtstag)*, Stämpfli Verlag AB 1355, 1366). On the other hand, others have argued that where the arbitral seat is located at a Contracting State to the CISG, the arbitrators would enjoy discretion in determining whether to apply the CISG as the law applicable at that seat (see Juan Pablo Hernández Páez, “Arbitration Agreements Under The CISG,” (2021) 1 *The Treaty Examiner* 24-30). Thus, to avoid problems of compatibility, if parties wish to apply the uniform CISG law, they should agree expressly in their arbitration agreement that disputes will be governed by the

CISG where applicable.

CISG in Hong Kong

More in line with international standards for dispute resolution, in particular arbitration

As of 2020, Hong Kong’s top 20 trading partners include Mainland China, Taiwan, USA, Singapore, Japan, Korea, Malaysia, Viet Nam, India, Thailand, The United Kingdom, Germany, The Philippines, Netherlands, France, The United Arab Emirates, Switzerland, Italy, Macao and Australia.

As shown in the table below, the CISG applies to 12 out of Hong Kong’s top 20 trading partners in 2020.

Rank	Total Trade			Does the CISG apply?
	Country/Territory	Value (HK\$, M)	Percentage Share (%)	✓ / ✗
1	Mainland China	4,248,047	51.8	✓
2	Taiwan	504,201	6.2	✗
3	USA	433,548	5.3	✓
4	Singapore	373,515	4.6	✓
5	Japan	349,311	4.3	✓
6	Korea	299,431	3.7	✓
7	Malaysia	196,348	2.4	✗
8	Vietnam	185,126	2.3	✓
9	India	154,778	1.9	✗
10	Thailand	135,220	1.6	✗
11	United Kingdom	109,497	1.3	✗
12	Germany	108,589	1.3	✓
13	Philippines	99,120	1.2	✗
14	Netherlands	80,439	1.0	✓
15	France	75,643	0.9	✓
16	United Arab Emirates	73,531	0.9	✗
17	Switzerland	67,183	0.8	✓
18	Italy	57,487	0.7	✓
19	Macao	48,750	0.6	✗
20	Australia	48,599	0.6	✓

Disputes in relation to trades and shipping are usually resolved through arbitration. According to the CISG, a contract for the sale of goods will come within its ambit if the places of business of the parties are in different states (Article 1, CISG) which are both contracting states to the CISG (Article 1(1)(a)). This is so unless the fact that the parties have their places of business in different states does not appear from the contract, or dealings between, or information disclosed by, the parties before or at the conclusion of the contract (Article 1(2)). With the CISG applied to Hong Kong, it is likely that more trade and shipping related arbitrations will be dealt with according to the CISG, particularly when such a great number of Hong Kong's trading partners are Contracting States to the CISG.

One may wonder whether the Proposed Application would actually attract more parties to contracts for international sale of goods to resolve disputes in Hong Kong, especially when a recent international arbitration survey already showed that Hong Kong is the third most preferred seat in the world. Though the CISG has never been applied to Hong Kong previously, such application may attract more parties to resolve disputes in Hong Kong in view of the option of applying the CISG through opting for Hong Kong law as the governing law of their contracts.

Moreover, the CISG is often welcomed by parties and the arbitrators due to its neutrality (that the law is not favouring parties from a particular state or region, but applicable to all Contracting States). The Proposed Application may result in Hong Kong starting to handle more international sale of goods cases with Hong Kong law (and hence the CISG) as the governing law.

This may help enhancing the competence of Hong Kong's arbitration community in dealing with CISG-related disputes, which will in turn boost the parties' confidence in Hong Kong's legal and arbitral system. With the alignment of Hong Kong's international sale of goods law with the CISG and hence the traders' greater confidence in it, not only Hong

Kong's international trade transactions may be promoted, but also parties are likely to be encouraged to resolve their disputes in Hong Kong. If this happens, more training opportunities might also be created for local lawyers and arbitrators.

Belt and Road Initiative Context

The above is particularly true when considering the role of Hong Kong in the BRI. Being a logistics and maritime services hub and a regional trading centre, Hong Kong acts as a trade and logistics integrator for cooperation in maritime and other types of transports among BRI countries, providing support services and other professional services given its strong base of professionals.

By applying the CISG, which is an international set of rules designed to provide clarity to most of the international sale of goods transactions, Hong Kong can further its capability in handling disputes arising from transactions facilitated by the BRI.

COVID-19

With Covid-19, popularity of online shopping has hit its historic high. This has resulted in great demand for shipping service, and hence, more disputes involving shipping. Indeed, the disruption of the supply chain caused by the pandemic has created a great number of disputes. With the application of the CISG to Hong Kong and its adoption in relevant international sales of goods contracts, the time cost for handling such disputes would be saved in light that the CISG is a standard law that parties from around the globe are more familiar with. It also allows greater capacity to handle more disputes caused by the pandemic.

Transactions with the Mainland China

As noted in the table above, Mainland



China is Hong Kong's top trading partner. Incidental to more trades between the two economies, more cross-boundary trade disputes may arise. However, being an international convention governing international sale of goods, the CISG does not apply to transactions within China, including those transactions between the Mainland enterprises and the HKSAR enterprises.

In the public consultation, there was general support to apply the CISG rules to Mainland-HKSAR transactions by way of a Mainland-HKSAR arrangement. According to Ms. Teresa Cheng, SC, the Secretary for Justice, the HKSAR Government is following up and working on reaching such arrangement through discussion with the Central People's Government, just as what has been done regarding the reciprocal enforcement of arbitral awards between the Mainland and the HKSAR through an arrangement modelled on the New York Convention. If such an arrangement is in place at the end, Hong Kong's ability to resolve cross-boundary sale of goods disputes smoothly through arbitration would likely be further enhanced. ■

¹ It may be noted, however, that uniform interpretation of the CISG has been assisted by the availability of opinions issued by the CISG Advisory Council (see <https://iic.law.pace.edu/cisg/page/cisg-advisory-council-opinions>), the CISG database of the United Nations Commission on International Trade Law as well as various leading commentaries on the Convention.

² Unless the CISG is excluded by the parties to the sales contract in its entirety.