ARBITRATION OUTCOME-RELATED FEES: NO WIN, NO FEES, NO WORRIES?

Wing So
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The Arbitration and Legal Practitioners Legislation (Outcome Related Fee Structures for Arbitration) (Amendment) Bill 2022 (Arb ORFS Bill) was introduced to the Legislative Council on 30th March 2022 and is widely expected to be passed into law before the end of the term of the present government. Under the Arb ORFS Bill, lawyers will now be allowed to charge under "Outcome Related Fee Structures", with two principal structures.

A Conditional Fee Agreement (CFA) is an agreement whereby lawyers could charge an extra premium on top of their usual charges upon success, with a current cap set at 100%. For example, one can agree with a client for a 30% increase of one's hourly rate upon the success of the claim before an arbitral tribunal, but nothing if the claim fails.

Alternatively, a Damages-Based Agreement (DBA) is an agreement whereby lawyers could charge a percentile of the financial benefit obtained by the lay client, but nothing if the claim fails. For example, one can agree to represent a client for an arbitral claim, and charge 30% of the damages awarded by the arbitral tribunal, but nothing in the event that the claim is unsuccessful. The current cap of this percentile is set at 50%. There are also Hybrid Damages-Based Agreements which are DBAs, but even in a case fails, the lawyer will be entitled to some payment, typically the usual charges at a discounted rate.

But what of the practical applications of these new structures? Given the decision of the drafters of the Arb ORFS Bill to adopt unique directions and wordings not found in similar legislation in other common law jurisdictions, there will be a period of some legal uncertainties and potentially serious risks on this law's

operation. As the Arb ORFS Bill now stands, it is completely silent on the consequences when one accidentally steps on a compliance landmine in drafting the ORFS-based retainer. Would that mean that the lawyer will not receive anything at all at the end of the day?

In England & Wales, it had been held that no quantum meruit claims are allowed for void CFAs (Awwad v Geraghty – 2001), and one cannot argue that where a CFA failed a normal retainer could be read in to replace it (Radford v Frade – 2016). For DBAs, the English Ministry of Justice had made it clear in the Explanatory Memorandum to the Damages-Based Agreements Regulations 2013 –

"...the consequence of failing to comply with these Regulations is that the DBA will not be enforceable and, in those circumstances, the representative will receive no payment..."

In fact this is the very reason why DBAs have been "the singular unpopular choice of retainer" in England given the huge risk of not being paid for years of work (Friston on Costs [29.143]).

The Hong Kong legislation is even less clear than its English counterpart and, given how English lawyers remain hesitant to sign on DBAs given this risk, there is every reason to be cautious.

So, what kind of risks would practitioners face under the upcoming ORFS Regime in Hong Kong? The first type worth exploring is: what kind of cases can be subject to an ORFS? This issue may seem deceptively simple. ORFS arrangements are allowed for "arbitration", and "arbitration" is defined (under s98ZA) to cover not only arbitration proceedings, but "court proceedings arising under the Arbitration Ordinance" (AO). This definition can surprise the unwary practitioner, as many typical proceedings that one would reasonably consider as arbitration work may well fall out of the permissible scope of ORFS.

A good example would be arbitration cases interwined with elements of insolvency. Most applications seeking a stay in favour of arbitration will be done under AO s20, yet various exceptions exist. One notable example would be that in the context of a winding up where the substance of the dispute is subject to an arbitration clause, the basis of a stay application would be RHC O.18 r.19(1) instead (Re Quiksilver Glorious Sun JV – 2014). As such, in this not-uncommon scenario, an ORFS retainer funding the case may be void as it is clearly not a proceeding "under the AO".

Many other potential problems arise from this: where a party files any interlocutory application under the AO, yet later on amends the application such that it would be done under some alternative statute instead, would this case still be a court proceeding "under the AO"? Would any lawyer be allowed to use a ORFS retainer when defending such a case? No one can say for sure what is the answer to these questions until future case law eventually barnacle over the provision.

Insurance practitioners should also be on alert. The Arb ORFS Bill makes it (under s98ZK(1)) that any ORFS agreement would be "void and unenforceable to the extent that it relates to a personal injuries claim". The accompanying Law Reform Report (Report) further explicitly acknowledges that this would "adversely affect " insurance cases which "frequently require disputes to be resolved by arbitration": (Report [14.57]). Further combined with the Court of Final Appeal decision in Mariner International Hotels (2007) commenting that " in relation to" is one of the widest possible "words of association known to the English language", it would be prudent for one to be concerned that any ORFS retainer over a case that involves any element of

personal injury insurance may be void.

This may even affect other types of practitioners. Construction and shipping contracts readily include elements of insurance over the safety of construction workers and sailors. M&A deals for the purchase of factories or other similar businesses frequently has standard clauses for indemnification over workplace injuries of employees (e.g. a warranty by a vendor to the purchaser that none of its workers have any asbestos claims against the target company to be sold).

Legal representatives acting on insurance cases (or any cases with an element of insurance) subject to arbitration clauses ought to think twice before signing on any ORFS-based retainers.

Even attempts to use ORFS for garden-variety interim relief applications in support of arbitration may also encounter significant uncertainties. In practice, injunctions in support of an arbitration are often applied under both AO s45 and High Court Ordinance (HCO) s21M given their significant overlap (see Top Gains Minerals Macao Commercial Offshore – 2016). Another common example would be orders for sale of perishable goods which are often done both under AO s60(1) and RHC O.29 r4 (see Taxfield Shipping – 2006).

There are often tactical and practical considerations behind deciding whether to file an application under the AO or some other statute. For example, under Hong Kong law, it is not entirely clear whether the drafting of AO s60 allows one to apply for a search order (Anton Piller relief) or does one have to resort to HCO s21M. There is also no right to appeal for AO s45 applications yet there is one under HCO s21M.

In short, any attempts to use an ORFS retainer to cover interlocutory relief work in support of arbitration, even if the work is done in a fashion in accordance with the established practice in Hong Kong, may be at significant risk of being void if any part of the application is not strictly based on the AO. This is particularly dangerous if an ORFS arrangement is made at an early stage to cover "all interlocutory applications" (which is occasionally seen in jurisdictions such as the PRC), as no one has a crystal ball that can predict whether the case will develop in a way that would require an application under the AO or some other legislation instead.

The second type of major risk I see is: how does one calculate the "financial benefit" in DBAs?

Rewards for the lawyers under DBAs are calculated based on the "financial benefit" obtained in the case. The Arb ORFS Bill merely told us that "financial benefit" covers "money or money's worth", but the legislative intent is apparently that its calculation is not based on whether or when the client "actually receives money in hand": (Report [14.41]). To make matters worse, no guidance could be sought from foreign authorities as the concept of "financial benefit" is not even adopted as part of English costs law yet.

In the case of enforcement proceedings, the award exists already so there is no further "money or money's worth" in the enforcement process. The only real additional "financial benefit" that one would obtain is the theoretical difference of the value between the metaphorical bird in hand as compared to the metaphorical bird in the bush.

The same problem will arise in asset-freezing (Mareva) applications. How does one measure the "financial benefit" of successful Mareva applications, or a successful application to resist or discharge them? Is cash held in a bank account which belongs to a party worth the same "money or money's worth" if it is frozen or unfrozen?

It may be an unintended outcome of the Arb ORFS Bill that while it is possible to do CFAs for these applications (since one can define what is "success" with contractual terms under CFAs), it would be practically impossible (or at least economically unviable) to do DBAs on them.

In conclusion, and with jurisdictions such as England in mind, given these inherent risks of ORFS retainers, for cases involving larger sums (and thus higher risks) costs experts are often brought in for legal advice and to design retainers which are efficient and secure. The examples of the potential risks discussed above are but a tip of the iceberg. Hong Kong practitioners are warned to take extra care before signing ORFS retainers, unless one has the appetite for the risk of ending up as the namesake for the next reported judgment on arbitration costs.