

## BETTER WAYS OF RESOLVING DISPUTES IN HONG KONG—SOME INSIGHTS FROM THE LEHMAN-BROTHERS RELATED INVESTMENT PRODUCT DISPUTE MEDIATION AND ARBITRATION SCHEME

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### I. INTRODUCTION

Following the collapse of Lehman Brothers in September, 2008 until December 23, 2009, the Hong Kong Monetary Authority (the “HKMA”) received 21,770 complaints from investors regarding the ways in which some banks were misselling Lehman Brothers-related investment products.<sup>1</sup> On October 31, 2008, the HKMA announced the Lehman Brothers-related Investment Products Dispute Mediation and Arbitration Scheme (the “Scheme”), and appointed the Hong Kong International Arbitration Centre (the “HKIAC”) as its service provider.<sup>2</sup> The purpose of the Scheme was to provide a dispute resolution platform for disputes between aggrieved investors that purchased Lehman Brothers-related investment products and the banks which sold it to them. The HKIAC provided such mediation and arbitration services to resolve those disputes. The introduction of the Scheme can be seen as a step taken by the Government of Hong Kong to promote the development of mediation as an alternative means of dispute resolution. This paper reviews the effectiveness of the Scheme since its implementation more than a year ago, in

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<sup>1</sup> H.K. MONETARY AUTH. (“HKMA”), COMPLAINTS STATISTICS CONCERNING LEHMAN-RELATED INVESTMENT PRODUCTS (2009), available at

<http://www.info.gov.hk/hkma/eng/new/lehman/lehman.htm> (last visited on Feb. 23, 2010). HKMA regularly updates the progress and statistics concerning Lehman-related investment products.

<sup>2</sup> Press Release, Hong Kong International Arbitration Centre (“HKIAC”), HKIAC to Provide Mediation and Arbitration Services for Lehman-Brothers Related Inv. Prods. Dispute (Oct. 31, 2008), available at [http://www.hkiac.org/documents/Mediation/News/081031\\_Lehman\\_E.pdf](http://www.hkiac.org/documents/Mediation/News/081031_Lehman_E.pdf).

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light of recent developments. Before introducing the Scheme, this paper first considers the use of mediation as an alternative dispute resolution compared to the traditional means of litigation. Following that, there is a brief outline of mediation in Hong Kong along with an introduction to the Scheme. Finally, this paper considers the latest empirical data published on the Scheme, before concluding with an evaluation of the Scheme.

## II. ALTERNATIVE DISPUTE RESOLUTION LANDSCAPE IN HONG KONG

### A. Litigation or Mediation?

Mediation is not a new phenomenon in Hong Kong. Prior to the enactment of the Scheme, mediation has been successfully used to resolve disputes relating to construction and building management. Despite the increase in popularity and usefulness of mediation, litigation is still likely to be the first choice of dispute resolution mechanism on which most people or commercial enterprises locked in disputes would rely on.

Litigation has not lost all of its attractiveness, and is likely preferable in the following circumstances.<sup>3</sup> First, litigation is most desired where courts are better equipped to understand the legal dispute at hand. For example, commercial courts have the specialization necessary to deal with financial products and will likely better understand the technical aspects of a transaction. Second, litigation is preferred where there is a desire for an authoritative and legal precedent, so that the judgment would be legally binding on similar cases.<sup>4</sup> Third, litigation can utilize the developed set of court procedures that allow quick judgments to be obtained and cut down legal costs, such as summary judgment. This is seen in some common law jurisdictions such as England & Wales, Singapore and Hong Kong.

Thus, despite its rise as an alternative means of dispute resolution, mediation will not replace litigation. Therefore, the types of cases suitable for mediation need to be identified prior to promoting its use.

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<sup>3</sup> James Kwan, *A New Solution*, ASIALAW, Dec. 2008, available at <http://www.asialaw.com/Article/2068790/Search/Results/A-new-solution.html?Keywords=%22a+new+solution%22>.

<sup>4</sup> Joseph Wong, *Repairing the Damage: The Government Can Do More for Lehman Minibond Investors, Including Helping to Expedite Legal Cases*, S. CHINA MORNING POST, Nov. 5, 2008, at 21.

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### B. Mediation as an ADR Process in General

Briefly, mediation is a form of voluntary dispute resolution for parties who are unable to reach a settlement on their own. Both sides of the dispute agree to appoint a neutral mediator, who will bring the two sides together to try to settle a claim in a speedy, confidential and amicable way.<sup>5</sup>

Generally, mediation has the following advantages over other forms of dispute resolution.<sup>6</sup> First, its costs are considerably lower. Second, it is quicker than litigation, which can drag on for many years. Third, the process is less adversarial than other methods of dispute resolution. Unlike litigation, mediation encourages the parties to negotiate and reach a settlement. This, in turn, creates a less pressurized setting as parties are not encouraged or 'forced' to compete by presenting their case or arguments according to the common law adversarial style of advocacy. Fourth, mediation is easy to follow and understand because it avoids or limits the use of legal jargon. Fifth, the mediation process is free from the restrictions of pre-trial procedures such as requests for particulars, specific discovery, security for costs and other interlocutory applications that can be quite onerous and not necessarily beneficial to the parties. Finally, the mediation process is private and confidential.

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<sup>5</sup> H.K.M.A., LEHMAN-BROTHERS-RELATED PRODUCTS DISPUTE MEDIATION AND ARBITRATION SCHEME: FREQUENTLY ASKED QUESTIONS (2008), *available at* [http://www.info.gov.hk/hkma/eng/new/lehman/lehman\\_dispute.htm](http://www.info.gov.hk/hkma/eng/new/lehman/lehman_dispute.htm) (follow "Frequently asked questions" hyperlink).

<sup>6</sup> For more discussion on the process of mediation and its benefits, *see* Julian Cohen, *Making Mediation Work for your Commercial Clients*, H.K. LAWYER, May 5, 2009, at 32-38, *available at* <http://law.lexisnexis.com/webcenters/hk/Hong-Kong-Lawyer-/Making-Mediation-Work-for-your-Commercial-Clients>; Louise Barrington, *Slowly but Surely... Mediation goes mainstream in Hong Kong*, H.K. LAWYER, March 2007, *available at* [http://www.hk-lawyer.com/InnerPages\\_features/0/2307/2007/3](http://www.hk-lawyer.com/InnerPages_features/0/2307/2007/3); Wong Yan Lung, H.K. Sec'y for Justice, Address at the EMBA Forum 2007-08: Mediation Helps Preserve Relationships (Feb. 25, 2008), *available at* <http://www3.news.gov.hk/isd/ebulletin/en/category/ontherecord/080226/html/080226en11001.htm>; CHAN BING WOON AND TAN KHAIN SEIN OSCAR, HOW MEDIATION CAN HELP CORPORATIONS SURVIVE THE RECESSION (Asian Mediation Conference, 2009), *available at* <http://www.asianmediationassociation.org/conference/pdf/AMA%20Conference%202009%20-%20How%20Mediation%20Can%20Help%20Corporations%20Survive%20Recession%20by%20Chan%20Bing%20Woon.pdf>; Bernard Chan, A Shifting Role from Facilitator to Mediator, S. CHINA MORNING POST, Dec. 5, 2008, at 18; Kwan *supra* note 3.

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**C. Mediation as an ADR Process in Hong Kong**

In Hong Kong, mediation is not a new vehicle for dispute resolution. In the 1980s, mediation was initially used in sectors like the construction industry as a standard dispute resolution clause within the multi-tiers dispute resolution process.<sup>7</sup> Mediation has also been used in the Hong Kong Family Court, and more recently, in the Lands Tribunal and the Companies Court in the format of pilot schemes.<sup>8</sup>

Since 1994, the Hong Kong Mediation Council (the “HKMC”), a division of the HKIAC, has been operating to promote and develop the use and education of mediation. At present, there are approximately three hundred “Accredited Mediators” on the list of general category kept and maintained by the HKIAC. Mediation schemes performed by the HKMC in sectors such as commercial, employees’ compensation and construction, have all been operating in full gears.

On April 2, 2009, the Civil Justice Reform (the “CJR”)<sup>9</sup> came into effect. Modeled on the approach taken in England and Wales, the CJR represents the most important change in the practice of civil litigation since the current rules were introduced.<sup>10</sup> A key feature of the CJR is the encouraged use of mediation, which is the main theme that permeates its underlying objectives. The CJR emphasizes cost effectiveness, the avoidance of delays, fairness, the facilitation of settlements and fair employment of the courts’ resources. Order 1A, rule 2(2) provides that in exercising its powers, the court shall recognize that the primary aim is to secure ‘the just resolution of disputes in accordance with the substantive rights of the parties.’<sup>11</sup>

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<sup>7</sup> The standard clause in construction contracts in Hong Kong commonly provide for the use of mediation and arbitration for the resolution of disputes, if they remain not settled after the decision by the Engineer/Architect. The contractual uses of adjudication or a dispute resolution adviser system have also been respectively seen in some standard contracts, such as the Airport Core projects in the 1990s and the refurbishment of hospitals.

<sup>8</sup> For more discussion on the use of mediation schemes in Hong Kong, *see* Barrington, *supra* note 6; Lung, *supra* note 6; Andrew Kwok Nang Li, Honorable Chief Justice, and Wong Yan Lung, Sec’y for Justice, Address at the Conference on Mediation in Hong Kong: Mediation in Hong Kong: The Way Forward, *available at* <http://law.lexisnexis.com/webcenters/hk/Mediation-in-Hong-Kong-The-Way-Forward>.

<sup>9</sup> Civil Justice Reform Homepage, <http://www.civiljustice.gov.hk>.

<sup>10</sup> David Ravenscroft, MEDIATION AND CIVIL JUSTICE REFORM, H.K. LAWYER, Oct. 2008, at 47-51, *available at* <http://law.lexisnexis.com/webcenters/hk/Hong-Kong-Lawyer-/Mediation-and-Civil-Justice-Reform>.

<sup>11</sup> Rules of the High Court, (2008) Cap. 4A, 1A, § 2(2). (H.K.), *available at* <http://www.legislation.gov.hk/eng/home.htm>. Rules of the District Court, (2008) Cap. 336H, 1A, § 2(2). (H.K.), *available at* <http://www.legislation.gov.hk/eng/home.htm>.

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Under the new CJR, courts are expected to take a more proactive approach in the management of their cases. Rule 4(2)(e) states that active case management includes “encouraging the parties to use an alternative dispute resolution procedure if the court considers that appropriate, and facilitating the use of such a procedure.”<sup>12</sup> Before the litigation commences, parties are expected to be ready, and come with their cases properly documented and prepared. The intention is to provide more initiatives for the parties and their legal representatives to know the facts, and realistically assess the merits of their cases at an earlier stage, with a view towards entering into direct negotiation for settlement.

In addition, the CJR obligates legal representatives to advise parties on mediation, and obligates parties to consider using it.<sup>13</sup> Courts are permitted to adversely take into account a party’s refusal to mediate without a reasonable explanation.<sup>14</sup> Likewise, a legal representative who fails to properly advise his or her client on the use of mediation can face a court order against himself or herself. Thus, in Hong Kong, litigants and their legal representatives need to seriously think before saying ‘no’ to mediation because of the risk of penalization by the Courts for legal costs. In addition, on January 1, 2010, a comprehensive set of Practice Directions<sup>15</sup> for the use of mediation following the CJR will take effect.

### D. Arbitration in Hong Kong

In addition to mediation, arbitration is another alternative to litigation. Although arbitration and mediation share many of the same advantages, arbitration may not necessarily be cheaper than litigation or quicker than mediation. In addition, arbitral awards are final and binding on both sides.

Because Hong Kong is now a common-law jurisdiction and part of the People’s Republic of China (“PRC”), it has a unique position on arbitration. As an arbitration venue, Hong Kong has benefited from the increasing number of Chinese-related disputes arising from the escalation of foreign investment and economic activities in Asia, particularly in China. It is believed that, because it

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<sup>12</sup> Cap. 4A, 1A, § (2)(e); Cap. 336H, 1A, 4(2)(e).

<sup>13</sup> This applies to the High Court and the District Court of Hong Kong. Other courts already have mediation schemes that encourage the use of mediation in similar settings, such as the Lands Tribunal for building management disputes, the Construction and Arbitration Court at the Court of First Instance, the Companies Court for shareholders disputes, and of course the Family Court.

<sup>14</sup> Cap. 4A, Order 62, § 5; Cap. 336H, Order 62, § 5

<sup>15</sup> Mediation Practice Direction, *Mediation* (2010) 31 (H.K.), available at [http://legalref.judiciary.gov.hk/doc/prac\\_dir/html/PD31.htm](http://legalref.judiciary.gov.hk/doc/prac_dir/html/PD31.htm).

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retained its English common law-based legal system, foreign parties regard Hong Kong as a fair, familiar and neutral forum for resolving commercial disputes. In addition, because of its proximity in location, Chinese parties regard Hong Kong as a culture-friendly venue.<sup>16</sup>

According to HKIAC's statistics, 602 arbitration cases have been recorded in 2008. Among them, the number of cases between two parties from Mainland China is increasing. For reference, the caseload figures for the last thirteen years are listed in the table below.<sup>17</sup>

<i>Year</i>	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
<i>Cases</i>	197	218	240	257	298	307	320	289	280	281	394	448	602

The existing Arbitration Ordinance (Cap. 341)<sup>18</sup> applies the UNCITRAL Model Law on International Commercial Arbitration ("UNCITRAL Model Law") as the statutory regime for international commercial arbitration. Hong Kong judges adhere not only to common law, but also to the New York Convention for enforcement of arbitral awards made overseas and in various arbitration commissions in Mainland China. In the High Court of Hong Kong, the Construction and Arbitration List operates to hear arbitration-related cases.

Currently, Hong Kong is in the process of reforming the existing Arbitration Ordinance in order to extend the UNCITRAL Model Law to its domestic regime and incorporate its framework, structure, and wordings to make it user-friendly for international users. Another one of its key features, apart from harmonizing the good aspects of laws and practices from the international arbitration world, is to give legal effect to the main amendments to the UNCITRAL Model Law in 2006 that deal with the definition of 'in writing' and the procedures for ordering and enforcing interim measures by the arbitral tribunal.<sup>19</sup>

With all these new and interesting developments in mind, it is now

<sup>16</sup> Lung, *supra* note 6.

<sup>17</sup> H.K.I.A.C. – About the HKIAC, *available at* [http://www.hkiac.org/show\\_content.php?article\\_id=9](http://www.hkiac.org/show_content.php?article_id=9).

<sup>18</sup> 'Cap.' is the standard abbreviation for 'Chapter.'

<sup>19</sup> UNCITRAL, MODEL LAW ON INT'L COMMERCIAL ARBITRATION (2006), *available at* [http://www.uncitral.org/uncitral/en/uncitral\\_texts/arbitration/1985Model\\_arbitration.html](http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/1985Model_arbitration.html).

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time for a closer examination of the use of mediation, particularly in conjunction with arbitration. To this end, an introduction of the Scheme may help cast some light on this specific issue.

### III. LEHMAN-BROTHERS RELATED INVESTMENT PRODUCT DISPUTE MEDIATION AND ARBITRATION SCHEME

#### A. Background of the Scheme

Founded in 1850, Lehman Brothers was the fourth largest investment bank in Wall Street and a leader in sales of various assets and equities. During the economic downturn in 2008, Lehman reported a loss of \$39 billion in the third quarter of 2008. On September 15, 2008, Lehman Brothers Holdings Inc., filed for bankruptcy protection under Chapter 11 of the US Bankruptcy Code. The collapse of Lehman Brothers caused serious repercussions on financial markets, and Hong Kong, an international financial center, was no exception. More than 48,000 Hong Kong investors invested in structured products, otherwise known as “minibonds,” that were related to Lehman Brothers. These investments derived part of its value from the performance of an underlying asset. The total invested in minibonds amounted to HK\$20 billion.<sup>20</sup> As a result of Lehman’s bankruptcy, these investments either lost the majority of its value or became entirely worthless.<sup>21</sup>

The HKMA is responsible for promoting the safety and soundness of Hong Kong’s banking system. The organization received 21,770 complaints regarding the sale of Lehman Brothers-related investment products, alleging fraud, misrepresentation and/or misconduct in the form of bad advice or the failure to disclose material information. As of December 23, 2009, only 246 of the 21,770 complaints filed with the HKMA have been referred to the Securities and Futures Commission (“SFC”) for further investigation.<sup>22</sup>

The complainants came from all walks of life. Some were still able to manage their lives despite dealing with the loss of value of their Lehman Brothers-related minibonds. Others, including many who were senior in age, invested all of their life-long savings in these products, and are thus, in very difficult situations. Not surprisingly, political parties got involved by assisting with the resolution of these disputes. There are also ongoing demonstrations by

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<sup>20</sup> See H. K.M.A., *supra* note 1.

<sup>21</sup> See Woon and Oscar, *supra* note 6.

<sup>22</sup> See H.K.M.A., *supra* note 1.

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investors in the Central Business District of Hong Kong.

Aiming to recover their investments, complainants were very proactive. Some commenced litigation against the banks in the High Court or the District Court, while others started legal proceedings in the Small Claims Tribunal. In addition, a number of complainants are in the process of pursuing a class action in the Courts of the United States.

Therefore, several measures were implemented to deal with the public outcry. On October 31, 2008, the HKMA introduced the Scheme to provide operative and administrative support to the mediation and arbitration services. In discussing the Scheme, Dr. Michael Moser, Chairman of the HKIAC commented:

[The Scheme] provides a mechanism for the resolution of the Lehman Brothers-related Investment Products disputes in a speedy, cost effective and efficient manner. The Scheme allows the Hong Kong Government, Hong Kong businesses and the entire community to address one of the consequences of the current financial crisis in a way which benefits all parties.<sup>23</sup>

Under the Scheme, the HKMA will pay half of the total costs to two groups of investors. The first group consists of the investors whose complaints to the HKMA resulted in a referral for investigation to the SFC (the “With-Referral Claims”).<sup>24</sup> The second group of investors consists of the investors whose complaints resulted in a finding against a relevant individual<sup>25</sup> or an executive officer, by either the HKMA or SFC (the Without-Referral Claims”). The Scheme is also available to claims other than the With-Referral Claims and Without-Referral Claims if the bank is willing to take part. As part of its commitment to assist the HKMA to launch the Scheme, the HKIAC has agreed to handle these claims according to the same procedures as under the Scheme. However in these circumstances, the costs of mediation are to be borne by the respective investors and the banks equally, unless otherwise agreed.<sup>26</sup>

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<sup>23</sup> See H.K.I.A.C., *supra* note 2.

<sup>24</sup> See H.K.M.A., *supra* note 5.

<sup>25</sup> The HKMA does not expressly define the term “a relevant individual,” but it should mean an individual relevant to the complaint in issue.

<sup>26</sup> See H.K.M.A., *supra* note 5.



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### B. Characteristics of the Scheme

Mediation is a voluntary, non-binding dispute resolution process in which a neutral mediator helps bring the parties together with the aim of settling the dispute in a speedy, confidential and amicable way. The mediator does not adjudicate on the dispute. Rather, the mediator either helps the parties narrow the issues in dispute or reach a negotiated settlement. In the former, an “Agreed Matters Form” is provided for the purpose of encouraging the parties to agree on certain issues, such as liabilities, facts, documents or method of calculating quantum, to name a few.<sup>27</sup> It should be noted that either party may terminate the process at any time.

As defined in the Rules, mediation proceedings are conducted in a private, confidential setting. Under the Scheme, parties may not appoint the mediator as an arbitrator, representative, counsel or expert witness of either party in any subsequent arbitration or judicial proceeding arising out of the mediation or connected to the dispute in question.<sup>28</sup> In addition, parties under the Scheme may not disclose, transmit, introduce or otherwise use any opinions, suggestions, proposals, offers or admissions obtained or disclosed during the mediation as evidence in any judicial proceedings, arbitration or other proceedings, unless the parties agree in writing or are compelled by law.<sup>29</sup>

Under the Scheme, the HKMA and the bank pay in equal shares the appointment fees<sup>30</sup> and mediator/arbitrator fees,<sup>31</sup> which are fixed amounts. As the Scheme is a means to resolve disputes by agreement, it expressly provides that parties may not be legally represented. If both parties agree to settle their dispute, a settlement agreement is negotiated, which is binding on both parties.<sup>32</sup>

### C. Operations of the Scheme

The Rules of the Scheme are quite simple: its four sections<sup>33</sup> and

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<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> H.K.I.A.C., *Lehman-Brothers-Related Investment Products Dispute Mediation and Arbitration Rules*, § 7 (Effective May 5, 2009) (H.K.), available at

[http://www.hkiac.org/documents/RICS/RICS\\_Procedure.pdf](http://www.hkiac.org/documents/RICS/RICS_Procedure.pdf) [hereinafter Scheme Rules].

<sup>30</sup> *See id.* at art. 4.; As per the Rules, the appointment fees for the appointment of a mediator and an arbitrator are the same, which is fixed at HK\$ 2,000 per case.

<sup>31</sup> *See id.* As per the Rules, the fees for the mediator and for the arbitrator are respectively fixed at HK \$15,000 and HK \$22,500 per case.

<sup>32</sup> *See* H.K.M.A., *supra* note 5.

<sup>33</sup> Namely, ‘Definitions,’ ‘Mediation,’ ‘Arbitration’ and ‘Fees and Costs.’

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twelve articles<sup>34</sup> aim to simplify the proceedings and languages to be as practicable as possible, while balancing the need for proper procedures. This is divided into three processes:

**i. Information gathering, pre-mediation briefings and preparatory meetings**

The HKMA supplies the Scheme with an office, staff and a venue (the “Scheme Office”), which is administratively supported by the HKIAC. The Scheme Office operates a special hotline that handles all inquiries relating to the Scheme,<sup>35</sup> and assists those who wish to initiate mediation. Furthermore, its staff, having been taught basic mediation knowledge, is able to answer and explain queries from investors regarding the Scheme, and help parties, including investors and banks, with the documentation required by the Scheme during the case intake process.

User-friendly forms and rules, including guidance notes and flowcharts, are tailor-made and prepared so that investors and bank personnel can easily understand the Scheme. Suitably qualified mediators and arbitrators draw up special lists that are used to provide services under the Scheme.

The Scheme Office is also used to hold mediation meetings. Parties interested in mediation are invited to attend pre-mediation briefing sessions at the Scheme Office. During these briefings, mediators discuss with banks and investors the suitability of mediating specific cases.<sup>36</sup> From these sessions, investors gain a basic understanding of mediation to make an informed decision as to whether or not to resolve their claims using mediation.

Investors having a complaint that was referred to the SFC or had resulted in a finding against a relevant individual or executive officer, receive information from the Scheme Office about the mediation service and the procedures for initiating it. Before mediation takes place, the parties attend preparatory meetings, which serve several purposes. Some investors come from low educational backgrounds. Most are unfamiliar with mediation. Thus, a mediator, other than the one in the actual mediation, acts as a mediation advocate by preparing the investor for negotiations, including familiarizing the

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<sup>34</sup> See Scheme Rules, *supra* note 29. Section 2 ‘Mediation’ contains articles titled ‘Appointment of Mediator,’ ‘Roles of Mediator and the Parties,’ ‘The Mediation Process,’ ‘Termination of the Mediation,’ ‘Confidentiality,’ ‘Language of the Mediation,’ ‘Mediator’s Role in Subsequent Proceedings’ and ‘Exclusion of Liability’. Section 3 ‘Arbitration’ contains articles titled ‘General,’ ‘Appointment of Arbitrator’ and ‘Procedures in General.’

<sup>35</sup> The hotline number is +852 8100 6448.

<sup>36</sup> All mediators are Accredited Mediators of the HKIAC, engaged or volunteering to provide assistance in the operation of the Scheme.

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investor with the mediation process. The mediation advocate also helps the investor explore settlement options using interest-based negotiation, in order to prevent the mediation from being dragged into hostile arguments that run counter to the amicable nature of mediation.

Additionally, the Scheme Office facilitates the exchange of information and documents between the parties. The mediator's task is to understand the interests and needs of the parties, to avoid legal arguments and to help explore settlement options, all while taking into account the parties' interests and needs. At this stage, parties are required to complete the consent to mediation form, the claim form and the response form. A 'Without Prejudice' offer may be made at this stage by the banks to settle a matter once and for all. Direct negotiations for an amicable settlement may happen before the completion of the forms, or shortly thereafter.

By the parties' choice, the substantive dispute resolution process under the Scheme can adopt a two-stage approach (mediation and arbitration), where a settlement does not need to be reached during the information gathering stage.

### **ii. Mediation**

Under the Scheme, mediation is designed to help the investor and the bank either settle the claim on terms agreed to by both parties or to narrow the issues in dispute. Where there is no direct negotiation, a mediator is appointed by agreement of the parties from a list of mediators provided by the HKIAC. The mediator must commence and finish the mediation within twenty-one days of the appointment, and unless otherwise agreed to by all involved, the mediation meetings should last no more than five hours. The mediator's task is to bring the two sides together to settle the case in an amicable, speedy and confidential way. Hence, a successful mediation concludes with a settlement agreement. In the event that no overall settlement agreement is reached, the process still encourages the parties and the mediator to endeavor to agree on the common facts, whether full or partial, that can be used in subsequent arbitration or litigation.<sup>37</sup>

### **iii. Arbitration**

The arbitration limb is not intended to be used in all types of disputes. In particular, under the Scheme, "documents-only" arbitration is not suitable for

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<sup>37</sup> Scheme Rules § 2.3.

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disputes involving complex issues or substantial examination of witnesses.<sup>38</sup> Parties electing to arbitrate under the Scheme are expressly required to thoroughly consider the circumstances before doing so. Relevant factors include the need for seeking, at the party's own cost, separate legal advice on whether to arbitrate on a "documents-only" basis, litigate or take other appropriate actions to resolve the dispute. The underlying rationale is to ensure that each party understands that he or she is at full liberty to decide whether to only use mediation or to use mediation in combination with "documents-only" arbitration, and to decide whether or not to agree to a settlement agreement in mediation.

When a dispute does not end in a settlement, the parties may agree to proceed with a "documents-only" arbitration. This commenced by a notice of arbitration. The arbitrator then has twenty-one days from its appointment to publish an award.<sup>39</sup>

Under "documents-only" arbitration, there should not be any in-person hearings (including hearings by teleconference, videoconference, and web conference), unless, under exceptional circumstances, the arbitrator determines, in his or her sole discretion, that such a hearing is necessary for deciding the claim and both parties have agreed to pay the related expenses and fees incurred. If needed, the arbitrator may conduct an informal hearing with the parties for the purpose of seeking any clarification. Awards under this kind of arbitration will be binding on the parties, and will not be subject to appeal.

### IV. EMPIRICAL STUDY OF THE SCHEME

#### A. Summary

The HKMA has received 21,770 complaints concerning Lehman Brothers-related investment products as of December 23, 2009. Of these complaints, the HKMA has completed the investigation process for 3,266 cases and is currently investigating an additional 5,108 cases. Among those investigated, 2,846 complaints have been closed, because of insufficient *prima facie* evidence. So far, disciplinary action has only been taken in one case, while 419 complaints cases are currently under disciplinary consideration or notice. The HKMA has also referred 246 cases, involving 16 banks, to the SFC for further action.<sup>40</sup>

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<sup>38</sup> See Woon and Oscar, *supra* note 6.

<sup>39</sup> *Id.*

<sup>40</sup> See H.K.M.A., *supra* note 1.

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As of November 2009, the HKIAC has recorded 334 requests for mediation. About thirty cases have been settled through direct negotiations between the banks and the investors. Of the investors who sought assistance from the Scheme Office, 78% of them have chosen mediation as the first method for resolving their disputes.<sup>41</sup> The first mediation was successfully concluded on December 10, 2008 and lasted for five hours. Mediation sessions were conducted in eighty-six other cases, all of which resulted in the conclusion of a settlement agreement. Thus, the Scheme has experienced an 88% success rate.

All of those mediation sessions took place within a week of having the mediators appointed and were concluded within five hours. In addition, some cases outside of the Scheme were mediated, of which the investors and the banks jointly agreed to use the Scheme to settle their disputes and pay the fees among themselves. In those cases, the amount in dispute ranged from approximately HK \$100,000 to approximately HK \$500,000. Post-mediation surveys revealed that parties were satisfied with the mediation process and the performance of their mediator.<sup>42</sup> So far, no case has reached the stage of 'documents-only' arbitration. As the matter presently stands, in view of the large number of pending cases, it is expected that the Scheme remain in operation for quite a while.

### B. Analysis of the Scheme

By obtaining full and final settlements, the Scheme helps to prevent disputes from escalating into full-blown litigation. For banks, mediation is attractive because settlement agreements do not have the binding effect of law. Thus, a bank can resume its normal operations and maintain amicable relationships with its customers. In addition, by avoiding long disputes, a bank can maintain long-term relationships the investors, which is in the best interest of its shareholders.<sup>43</sup>

The private and confidential nature of the Scheme also prevents the disclosure of private and sensitive information. This is an added incentive for banks because court hearings and decisions are assessable by the public and reported by the media. Thus, documents disclosed during the discovery process

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41 Press Release, H.K. Int'l Arbitration Ctr., Mediation 100% Success for Lehman Brothers-Related Investment Product Cases, (Feb. 19, 2009), *available at*

[http://www.hkiac.org/documents/Mediation/News/090219\\_LehmanUpdate\\_E.pdf](http://www.hkiac.org/documents/Mediation/News/090219_LehmanUpdate_E.pdf).

<sup>42</sup> *Id.*; Press Release, H.K. Int'l Arbitration Ctr., HKIAC Successfully Mediates First Lehman Brothers-Related Investment Products Case, (Dec. 22, 2008).

<sup>43</sup> See Woon and Oscar, *supra* note 6.

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would no longer remain confidential. As the Scheme is not subjected to the usual pre-trial discovery procedures, banks do not have to disclose confidential documents or information, including documents relating to internal operations and customers.<sup>44</sup>

Furthermore, mediation costs are low compared to other alternative means of dispute resolution. This is beneficial to investors who are unable to withstand a costly and time consuming litigation against financial institutions that are likely to have greater bargaining power due to advice from a team of legal counsel.<sup>45</sup>

As previously stated, the mediation process generally does not last longer than five hours. This benefits both parties since litigation is costly and can last for many years. For banks, on-going litigation is likely to affect its daily operations and damage its relationships with customers.<sup>46</sup>

Mediation can also be used under the Scheme as an attempt to narrow the issues in a dispute. In the event that no overall settlement agreement is reached, Article 2(3) of the Rules provides that the parties can agree on some, if not all, of the common facts. This will be helpful if the mediation fails to conclude in a settlement and the parties proceed to 'documents only' arbitration.

In general, the Scheme generated a lot of publicity among the various sectors of the communities. The intake of cases under the Scheme has been slower than expected, partly due to the limited understanding of mediation by its users and the limited number of complaints referred by the HKMA to the SFC. However, the HKIAC expects more cases to go through mediation as more inquiries regarding mediation are made, and investors and banks show eagerness to partake in a suitable, efficient and effective dispute resolution method for their disputes.<sup>47</sup> In any case, with its high rate of settling disputes, the Scheme has successfully delivered the message that "mediation is a flexible dispute resolution process and is more and more widely accepted as a practical and effective tool to settle disputes of various types and nature."<sup>48</sup>

### C. Challenges to the Scheme

Essentially, there are three key insights that can be drawn from the Scheme, in relation to the use of mediation as a dispute resolution process. First, the whole dispute resolution process should be and can be tailor-made to

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<sup>44</sup> *Id.*

<sup>45</sup> *Id.*

<sup>46</sup> *Id.*

<sup>47</sup> See H.K.I.A.C., *supra* note 42.

<sup>48</sup> See H.K.I.A.C., *supra* note 2.

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suit the users and the nature of their cases. One of the challenges under the Scheme is to control costs. Hence, the Scheme provides mediation and arbitration services at fixed fees.

Furthermore, the Scheme, in absence of an agreement otherwise, provides for “documents-only” arbitration. Since the allegations of disputes concern misselling of minibonds, there are different views on how “documents-only” arbitration might be helpful. It is believed that “documents-only” arbitration may still be used in suitable cases as an alternative to litigation where the issues involved are limited or have been narrowed down by mediation. The risks of a case not suitable for resolution by “documents-only” arbitration entering into the arbitration limb of the Scheme are safeguarded by the emphasis that the Scheme Office places on the types of cases that the process is designed for during the case intake process. The arbitration limb also helps parties stay more focused during the process of the mediation. Thus, instead of merely providing a one-size fits-all mediation or arbitration service to all users, consideration is given to the individual category of a case, to allow users to gain the most benefits of combining mediation and arbitration.

Second, to the users of mediation, the efficiency of the process is a significant indicator of whether mediation is helpful as a dispute resolution process. As such, it is important that the mediation process not be abused and seen as just another hurdle that the parties have to go through before beginning litigation or arbitration. Proper control of the timeline of the mediation needs to be maintained in order to build up public confidence in mediation. Speed is also an important matter that the parties appreciate. In some instances, investors held demonstrations in front of the banks on one day, and on the next day, their disputes were settled by mediation in hours.

Third, the Scheme Office and its special hotline have played a great role in contributing towards the success of the Scheme, from information gathering to the conduct of the mediation and arbitration. A team of HKIAC-led mediators and arbitrators perform the preliminary contacts and the arrangement of the logistics. Although mediation information and preliminary preparation are provided and done by the mediators under the Scheme, it is worthwhile to consider setting up a mediation helpline office.<sup>49</sup> Although many litigants are legally represented, the number of litigants appearing in person is increasing. The mediation helpline office, similar to the Scheme Office, would function as the one-stop contact point for the parties before entering into mediation. For other arbitration schemes that incorporate mediation, it may also be worthwhile to use a helpline in suitable cases and circumstances, which is essential to the success of the mediation.

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<sup>49</sup> See *supra* note 35.

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**D. The Future of Mediation**

With the CJR coming into force in Hong Kong, it is anticipated that the use and development of mediation as an amicable settlement process will be taken to new heights. The 100% success rate of the Scheme has not only increased the public's confidence in the use of mediation, but has also placed HKIAC in a positive light, as an institution to administer proceedings in an impartial and transparent manner. This opportunity encourages the HKIAC to promote its services in the financial sector and establish a panel of mediators and arbitrators with an expertise in financial transactions. As much as the Scheme is an indicator of the Hong Kong Government's efforts to promote mediation, the Scheme is now also an example of both the government's policy of promoting mediation and its goal of developing the city as an international mediation and arbitration center.<sup>50</sup>

**V. CONCLUSION**

Following the publicity and success of the Scheme, interest among the wider communities in the use of mediation in Hong Kong is growing. Experience garnered from the Scheme's operation has contributed new insights on how to better provide mediation services and how to integrate mediation with other dispute resolution processes, such as arbitration. The challenges of creating a tailored-made process, keeping the process of mediation efficient and establishing a helpline office for users should be considered, along with an aim to successfully use mediation, with or without arbitration, in the dispute settlement process for users. All in all, it is believed that the HKIAC's experience and observations over the Scheme's operation is valuable, in the sense that it helps identify ingredients for the successful use of mediation in the vast amount of cases to come under the CJR in Hong Kong.

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<sup>50</sup> For more discussion on the future of mediation, see Kwan *supra* note 3; Lung, *supra* note 6; Woon and Oscar, *supra* note 6; Li and Lung, *supra* note 8.