The Aftermath of the CIETAC Split: Two years on, lower courts take clashing views on arbitration agreements and awards– but higher courts strive for consistency

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By Justin D'Agostino, Jessica Booth and Tracy Wu, Herbert Smith Freehills

Ever since the internal fight between CIETAC (Beijing) and its Shanghai and Shenzhen sub-commissions became public in May 2012, the internal jurisdictional dispute between Beijing and the two sub-commissions has loomed large, resulting in the latter two declaring independence, re-naming themselves and introducing new arbitration rules (see previous Kluwer blog entry dated 10 February 2014 for a discussion regarding recent developments in arbitration across the whole of Asia). This has caused concern among users of CIETAC arbitration as the validity of arbitration agreements specifying, and the enforceability of the arbitral awards rendered by, the breakaway sub-commissions has been called into question.

In particular, we have seen a number of local and intermediate court judgments taking inconsistent approaches towards the validity of arbitration agreements and the enforceability of awards involving these sub-commissions (now known as the Shenzhen Court of International Arbitration ("**SCIA**") and the Shanghai International Economic and Trade Arbitration Commission ("**SHIAC**")). This article takes a closer look at these court judgments, and examines the analysis and reasoning in detail.

Shenzhen Intermediate People's Court
([2012] Shen Zhong Fa She Wai Zhong Zi No.226) ((2012) 深中法涉外仲字第226号)

The Respondents applied to the Shenzhen Court to challenge the validity of a CIETAC Shenzhen arbitration agreement during the arbitration proceedings but the Shenzhen Court upheld the arbitration agreement.

The Claimant and the First Respondent entered into an Agency Agreement in February 2006. Following this, a Supplemental Agreement was signed which provided that the Second Respondent was entitled to replace the First Respondent.

The Agency Agreement provided for arbitration as follows:

"*for any disputes related to or occurring under this agreement, parties shall first settle through negotiation, if no settlement can be reached, any party can bring the dispute to CIETAC Shenzhen branch and arbitrate according to the rules of that institution.* "

On 25 September 2012, after the CIETAC Shenzhen sub-commission had declared its independence and changed its name to SCIA, the Notice of Arbitration was served on the Respondents by SCIA.

On 10 October 2012, the Second Respondent applied to the Shenzhen Court requesting it to confirm that there was no arbitration agreement between the parties and therefore CIETAC did not have jurisdiction over the dispute.

On 20 November 2012, the Shenzhen Court held that according to Article 16(2) of the PRC Arbitration Law, an arbitration agreement must contain the following elements: (i) an agreement to arbitrate by the parties; (ii) the matters which should be referred to arbitration; and (iii) a selected arbitration commission. Based on the facts of the case, the court stated that there was an explicit agreement between the parties to arbitrate, the matters to be arbitrated had been agreed and the name of the arbitration institution was correct and accurate. Therefore, the arbitration agreement was valid. Further, according to the Supplemental Agreement, the Second Respondent was entitled to replace the First Respondent and therefore the arbitration agreement was binding on the Second Respondent.

The court found that CIETAC Shenzhen Branch had jurisdiction over the case. The court specifically noted in the judgment that CIETAC Shenzhen Branch had changed its name to SCIA, which can only mean that SCIA similarly had jurisdiction. The court therefore held that the Second Respondent's application had no legal or factual basis.

It is worth noting that it is not clear from the judgment whether the Second Respondent was challenging the validity of the arbitration agreement on the basis that it was not covered by the Supplemental Agreement or on the basis that the CIETAC Shenzhen sub-commission no longer existed.

Suzhou Intermediate People's Court
([2013] Su Zhong Shang Zhong Shen Zi No.0004)((2013)苏中商仲审字第0004号)

The Suzhou Court initially refused to enforce an award issued by CIETAC Shanghai but it has been ordered by the Higher Court of Jiangsu Province to revoke its previous ruling and the case is being reviewed by the Higher Court.

In October 2007, the parties entered into a three-year supply agreement. It was agreed that "*if a dispute cannot be settled through negotiation, either party may submit the dispute to CIETAC Shanghai*". In June 2008, the parties also entered into two ten-year agreements which had a different arbitration clause providing that "*if the dispute cannot be settled through negotiation, both Parties may reach an agreement to submit the dispute to CIETAC (arbitration location: Shanghai, China)*".

In July 2010, the parties submitted their dispute to CIETAC Shanghai and on 7 December 2012, after its declaration of independence but prior to its change of name, CIETAC Shanghai issued its award. The Respondent challenged the enforcement of the award on the basis that (amongst other things) CIETAC Shanghai did not have jurisdiction.

On 7 May 2013, the Suzhou Court held that: (i) the effective arbitration clause was the one in the ten year agreements, in which the parties choose CIETAC with a place of arbitration in Shanghai; (ii) prior to its independence, CIETAC Shanghai and CIETAC were considered to be one entity but after its

declaration of independence CIETAC Shanghai was no longer part of CIETAC; and therefore (iii) CIETAC Shanghai was no longer the arbitration body chosen by the parties and so it had no jurisdiction over the case.

The Suzhou Court further held that CIETAC Shanghai should have: (i) informed both parties of the change in the nature of the arbitration body; and (ii) asked them to confirm their choice of institution. CIETAC Shanghai's failure to do this violated the parties' right to know and went against the parties' true intention.

It has been reported that the Higher Court of Jiangsu Province has asked the Suzhou Court to revoke its previous ruling and will review the case. Further, on 4 July 2013, the Higher Court reportedly released an internal notice requiring all of the Intermediate Courts in Jiangsu Province to ask for the advice of the Higher Court before making a decision on cases related to the CIETAC split. This notice has been superseded by a notice issued by the Supreme People's Court of China (the "**SPC**") in September 2013 (see below for discussion of the SPC Notice).

Ningbo Intermediate People's Court
([2013] Zhe Yong Zhi Cai Zi No.1] and [2013] Zhe Yong Jian Zi No.1) ((2013) 浙甬执裁字第1号及（2013）浙甬监字第1号)

The Ningbo Intermediate People's Court initially refused to enforce an award issued by CIETAC Shanghai but was ordered to amend its decision by the Higher Court of Zhejiang Province.

In August 2010, the parties entered into a sales contract, which stated that disputes should be resolved by CIETAC Shanghai. There was a dispute and CIETAC Shanghai accepted the case in August 2012, shortly after its declaration of independence from CIETAC Beijing.

The Respondent challenged the jurisdiction of CIETAC Shanghai but CIETAC Shanghai determined that it had jurisdiction over the case and issued an award in January 2013 (after its declaration of independence but prior to its change of name). The Respondent then challenged enforcement of the award on the basis that (amongst other matters) CIETAC Beijing no longer authorised CIETAC Shanghai to handle cases and therefore CIETAC Shanghai lacked jurisdiction to make the award.

On 22 May 2013, the Ningbo Intermediate People's Court issued a judgment agreeing with the Respondent on the grounds that (i) when CIETAC Shanghai accepted the case on 21 August 2012, it was no longer part of CIETAC and hence had no jurisdiction; and (ii) CIETAC Shanghai should have explained the change to the parties and asked them to confirm or reselect the arbitration institution. By rejecting the Respondent's challenge to jurisdiction, CIETAC Shanghai contravened the parties' intentions.

The Claimant appealed the lower court's decision to the Higher Court of Zhejiang Province. On 17 July 2013, the Higher Court ordered the Ningbo Court to amend its decision. On 25 July 2013, the Ningbo Court amended its judgment, accordingly, stating that the parties expressly selected CIETAC Shanghai, the award was made in the name of CIETAC Shanghai and therefore it should be upheld. Further, the Respondent participated in the proceedings after its challenge was rejected and therefore, through its acts, submitted to the jurisdiction of CIETAC Shanghai.

Taizhou Intermediate People's Court
([2013] Zhe Tai Zhi Cai Zi No.2) ((2013) 浙台执裁字第2号)

The Respondent challenged the enforcement of an award issued by CIETAC Shanghai but this was rejected by the Taizhou Intermediate People's Court.

On 18 January 2011, the parties entered into a sales contract. The arbitration clause provided that "*disputes shall be submitted to Shanghai branch of CIETAC for arbitration in accordance with law*."

On 26 December 2011, the Claimant submitted an application to CIETAC Shanghai for arbitration of disputes arising out of the sales contract. CIETAC Shanghai accepted the case and made an award on 5 November 2012 (after its declaration of independence but prior to its change of name). The Respondent refused to honour the award.

On 28 February 2013, the Claimant submitted an application for enforcement to Taizhou Intermediate People's Court. The Respondent advanced the following arguments (amongst others) objecting to enforcement of the award: (i) in the arbitration agreement, the parties chose the "Shanghai branch" of CIETAC. However, the nature of the CIETAC "Shanghai branch" had changed and so it did not have jurisdiction over the case; and (ii) the CIETAC Shanghai branch did not inform the parties of this change after accepting the notice of arbitration and so it infringed the Respondent's right to be informed of the change. In conclusion, the Respondent claimed that it was not the intention of the parties to choose the CIETAC Shanghai branch for its arbitration.

In its judgment dated 29 July 2013, the Taizhou Intermediate People's Court dismissed the Respondent's arguments and upheld the Claimant's application on the basis that (i) "CIETAC Shanghai branch" was the arbitration institution stipulated in the arbitration clause of the sales contract; (ii) the award was made in the name of "CIETAC Shanghai branch"; and (iii) the Respondent did not raise any objection to the jurisdiction of the CIETAC Shanghai branch during the arbitration itself.

Form over substance?

The Ningbo and Taizhou cases appear to place emphasis on the fact that the institution specified by the parties in the contract is the institution (in name at least) which issued the award. Even though a number of the parties have tried to stress that they chose CIETAC, that these sub-commissions are no longer part of CIETAC and so they have not been chosen by the parties, this does not appear to have been accepted by the higher courts. In the same way, the judgments do not currently focus on the possibility that the substance (i.e. personnel and administration) of the institutions may be the same as they were prior to their independence and so they may still be said to be the institution chosen by the parties (even though they are not formally part of CIETAC anymore). We note that in the Shenzhen case, CIETAC Shenzhen had already changed its name to "Shenzhen Court of International Arbitration" prior to issuing the award and, although this was noted, this discrepancy was not addressed by the Shenzhen Court. Now that CIETAC Shanghai has changed its name as well, it will be interesting to see how awards issued by SHIAC (relating to arbitration clauses specifying CIETAC Shanghai) will be dealt with by the higher provincial courts.

What does the SPC say?

In light of the inconsistent approaches adopted by lower courts, on 4 September 2013, the SPC issued the Notice on Certain Issues Relating to Correct Handling of Judicial Review of Arbitration Matters (the "**SPC Notice**"). Under the SPC Notice, any lower court that hears a case arising out of the CIETAC split must report the case to the SPC before making a decision.

This level-by-level reporting system is similar to the judicial review process that applies to enforcement of all foreign and foreign-related arbitral awards in China. However, it is more rigorous, in that it requires all cases that arise out of the CIETAC split to be reported to the SPC level-by-level (i.e. to every level of court in between the seised court and the SPC), not just those cases where the court is minded to nullify a CIETAC arbitration agreement or set aside / refuse to enforce an award made by CIETAC, SHIAC or SCIA.

Further clarity is required…

Although the different local courts across China initially adopted a different approach to these types of cases, they have been brought into line by their respective higher courts, which have taken a pro-enforcement approach. So far, all of the courts have (ultimately) upheld the validity of the arbitration agreements and the enforceability of awards issued by CIETAC's former sub-commissions, although the judgments do not offer detailed reasoning that can be applied in other cases.

The fact that China's highest court has acknowledged the potential problems caused by the division at CIETAC and has taken measures to address them is a very welcome development. However, the SPC Notice is brief and it does not offer any detailed guidance to lower courts on these issues. Hopefully, such guidance will be forthcoming in the future.