Does Supreme People's Court's Decision Open the Door for Foreign Arbitration Institutions to Explore the Chinese Market?

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Whether foreign arbitration institutions could conduct arbitration in the People's Republic of China ("PRC") is a question that many industry insiders are curious about. Back in 2006, when the Wuxi Intermediate People's Court ("Wuxi Court") refused to recognize and enforce an arbitral award issued by the ICC Court of Arbitration in Shanghai in the *Züblin* case,[fn]The ruling was given by Wuxi Intermediate People's Court on July 19, 2006. The Applicant: Züblin International GmbH□a German company; the Respondent: Wuxi Woke General Engineering Rubber Co. Ltd., a Chinese company. Wuxi is a city located in Jiangsu Province not far from Shanghai. [/fn] many practitioners deemed that Chinese courts would decline opportunities for foreign arbitration bodies to carry out arbitration in China. However, the recently published PRC Supreme People's Court ("SPC") instruction in *Longlide Packaging Co. Ltd. v. BP Agnati S.R.L.* may suggest otherwise.

Looking at PRC Court previous cases, in *Züblin*, the court denied enforcement of

the award based on the invalidity of the arbitration agreement; it did not comment on the legality of arbitration activities conducted by the ICC Court of Arbitration in Shanghai. The ruling categorized the arbitral award issued by the ICC Court of Arbitration seated in PRC as a "non-domestic award" and was therefore to be reviewed under the New York Convention. This view once caused heated debate among arbitration scholars, many of whom considered it a mistake to categorize such an award as "non-domestic."

In another controversial case, *Duferco S.A. v. Ningbo Art & Craft Import & Export Corp.*, Ningbo Intermediate People's Court enforced an arbitration award given by ICC with the arbitration seated in Beijing. *Duferco* was widely criticized by arbitration scholars and the media as a dangerous precedent because it classified the award as a "non-domestic award" and failed to take into account that Chinese law may not allow a foreign arbitration institution to arbitrate a case in China.

In *Longlide Packaging Co. Ltd. v. BP Agnati S.R.L.*, the SPC clarified the tests to be used in determining the validity of the arbitration agreement if the parties choose a foreign arbitration institution to arbitrate their dispute in China. Although such an arbitration agreement is supported by the SPC, the enforceability of the awards issued under such arbitration agreements remains uncertain. The authors believe that this instruction may trigger another round of heated discussions on the possibility of international arbitration organizations entering the Chinese market.

Facts of the Case:

In *Longlide* (SPC Docket Number: 2013-MinTa Zi No.13),[fn]This instruction was actually made by SPC on March 25, 2013, which was not published until April 2014. Please note that such instruction, acting as a guide for the lower court for individual cases, is handed out by the SPC to the lower court through an internal court system. Upon SPC publication, they become accessible to the public.[/fn] the SPC upheld the validity of an arbitration clause involving an ICC arbitration with the seat of arbitration in Shanghai.

Applicant Longlide Packaging is a Chinese company located in Anhui Province. On October 28, 2010, Longlide Packaging entered into a Sales Contract with respondent BP Agnati S.R.L, a company domiciled in Italy. The arbitration clause states that "any dispute arising from or in connection with this contract shall be submitted to arbitration by the International Chamber of Commerce ('ICC') Court of

Arbitration according to its arbitration rules, by one or more arbitrators. The place of jurisdiction shall be Shanghai, China. The arbitration shall be conducted in English."

The applicant argued that under PRC law, the arbitration agreement should be invalid based on three reasons. First, the ICC Court of Arbitration is not an arbitration institution recognized by the China Arbitration Act. Second, the seat of ICC arbitration in Shanghai would violate China's public policy because it could infringe China's judicial sovereignty. Third, even if the ICC Court of Arbitration in Shanghai issued an award, such award should be considered a domestic award, and thus the New York Convention is not applicable for its recognition and enforcement in China.

Review by the Intermediate Court of Hefei City ("Hefei Court")

First, the Hefei Court decided that Chinese law shall be the governing law in determining the validity of the arbitration agreement. According to the Hefei Court, the China Arbitration Act does not explicitly address the issue of whether a foreign arbitration institution is allowed to conduct arbitration in China. Since both parties selected Shanghai as the seat of arbitration, the arbitration shall be classified as a domestic arbitration, which is different from the "non-domestic" classification described in Article 1 of the New York Convention. Additionally, under Article 10 of the China Arbitration Act, "the establishment of an arbitration commission shall be registered with the administrative authority of justice of the relevant province, autonomous region or municipality directly under the central government." This regulation means that a foreign arbitration institution, acting as a service provider, can only conduct arbitration after obtaining the permission of and filing for registration in the appropriate administrative agency of justice. In fact, because the PRC has not opened its arbitration market to foreign arbitration institutions, a foreign arbitration institution cannot conduct arbitration proceedings in China. As a result, the court held that the arbitration agreement between the Chinese and the Italian company is invalid.

Review by the Higher People's Court of Anhui Province ("Anhui Court")

The Anhui Court agreed with the lower court's view that Chinese law should be the governing law for this issue. However, it disagrees with the substantive issues of the lower court's ruling. The Anhui Court explains that under Article 16 of the China

Arbitration Act, “an arbitration agreement shall contain three elements: 1) an expression of intention to apply for arbitration; 2) subject matters for arbitration; 3) a designated arbitration commission.” Here, the Sales Contract showcases the true intent of the parties, i.e. parties’ intent to apply for arbitration and the subject matter of the arbitration. Additionally, the parties have designated an arbitration institution, namely, the ICC Court of Arbitration. Therefore, the ruling of the lower court that the arbitration agreement is invalid because foreign arbitration institutions cannot conduct arbitration in China lacks merit.

However, the Anhui Court also included a minority view in their report to the SPC. Their view is that since the Chinese government has not opened up the market of arbitration service to foreign entities, foreign arbitration institutions cannot conduct arbitration in China. Here, since the parties agreed to arbitrate at the ICC Court of Arbitration, the arbitration agreement shall be invalid due to violation of the PRC’s arbitration law.

Final Review by the Supreme People’s Court of China

The SPC upheld the majority view of the Anhui Court. Since the three elements of a valid arbitration agreement had been satisfied, under Article 16 of the China Arbitration Act, the SPC determined that the arbitration clause is valid.

However, under its instruction, the SPC did not address the question of whether the law allows foreign arbitration institutions to hold arbitrations in China.

The Uncertainty of Enforcing an Award Issued by a Foreign Arbitration Institution with a Seat of Arbitration in PRC

China acceded to the New York Convention in 1987. Under Article 1, there are two kinds of arbitral awards for which recognition and enforcement shall be given based on the Convention:

> *“This convention shall apply to the recognition and enforcement of arbitral awards made in territory of a State other than the State where the recognition and enforcement of such award are sought, and arising out of differences between persons, whether physical or legal. It shall also apply to arbitral awards not considered as domestic awards in the State where their recognition and enforcement are sought.”*

Since the first criterion only applies to scenarios in which the seat of arbitration is outside China, an arbitration award issued by a foreign arbitration institution in China can either be enforced under the second criterion, i.e. a *non-domestic award*, or as a domestic Chinese arbitration award. Based on the intent of the New York Convention, an award could be accepted as a *'non-domestic award'* only if the governing law of arbitration for the award is different from the law of the country in which the award is to be made.[fn]Albert Jan van den Berg, The New York Convention of 1958, P23, Kluwer Law and Taxation Publishers (1981)[/fn] In reality, such scenario is rare in international arbitration practice.

In the *Züblin* and *Duferco* cases, whereas the court defined the ICC awards seated in China as "non-domestic" awards, the recognition and enforcement of the awards were subject to the New York Convention. Many scholars once criticized those decisions. Yet it is uncertain whether the courts had ever consulted with SPC before making such decisions.

In the *Longlide* case, the SPC declared the validity of the arbitration agreement, but failed to address how to classify such an award for enforcement purposes if the parties continue the arbitration proceedings under the said arbitration agreement. Nevertheless, if the winning party in *Longlide* seeks enforcement after issuance of the award, the Chinese court has to determine whether to treat the arbitration award as a domestic award or a "non-domestic" award under the New York Convention. If the award issued in *Longlide* is enforced by a Chinese court, it would be a big boost for foreign arbitration institutions to expand their presence in China because it would appear to give a green light for them to provide their services in the PRC.