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Chinese Law or No Law: The Lex Arbitri for Arbitrations Conducted by Overseas Arbitration Institutions in Mainland China

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***Longlide, Shenhua Coal* and the issue ahead**

In a case regarded by many as a "milestone" for arbitration in China, *Longlide Packing and Printing Co. Ltd. v. BP Agnati S.r.l* (hereinafter "Longlide") (Reply of the Supreme People's Court to the Request for Instructions on Application for Confirming the Validity of an Arbitration Agreement in the Case of *Anhui Longlide Packing and Printing Co., Ltd. v. BP Agnati Srl* ([2013] Min Si Ta Zi No. 13, 25 March 2013)), the Supreme People's Court of China (the "SPC") upheld the validity of an arbitration agreement providing for arbitrations seated in Shanghai, China, but administered by the ICC – opening the door for overseas institutions conducting arbitration in China. The SPC reasoned that the phrase "arbitration commission", an essential element for a valid arbitration agreement under Art. 16 of the Arbitration Law (1994), included foreign arbitral institutions such as the ICC, and rejected the request for invalidating the agreement.

However, in the earlier case of *Shenhua Coal Transportation & Trading Co., Ltd v. Marinic Shipping Company* (hereinafter "Shenhua Coal") (Reply of the Supreme People's Court to the Request for Instruction on the Validity Issue of Arbitration Agreement in the Case of *Shenhua Coal Trading Co., Ltd v. Marinic Shipping Company* ([2013] Min Si Ta Zi No. 4, 4 February 2013)), the SPC held that the "arbitration commission" under Art. 20 of the Arbitration Law referred only to Chinese arbitration institutions and **excluded "foreign arbitration institutions"**, and thus, there would be no judicial intervention by Chinese courts on the competence of the tribunal for proceedings administered by foreign institutions.

This divergence – *Longlide* adopted a different meaning for the same term "arbitration commission" even though it was interpreting a provision in the same chapter of the same statute as *Shenhua Coal* – raises several difficult issues. How could the phrase "arbitration commission" be construed so differently? Can the cases be reconciled?

Perhaps more importantly, *Longlide* and *Shenhua Coal* lead to the problematic situation whereby, if an arbitration is administered by a foreign institution and seated in China, it will be a valid arbitration under Chinese law (*Longlide*) but immune from judicial intervention and review by Chinese courts at the seat (*Shenhua Coal*). Can or should this be so? What is the *lex arbitri* for such an arbitration proceeding? What is the nationality of an award so rendered? Is it a "non-domestic award" under Art. 1(1) of the New York Convention (the "NYC")?

We will endeavour to navigate this modern Palace of Knossos, and to deliver our answers, or more accurately, our reasoned guesses, to these difficult questions.

Reconciling *Shenhua Coal* with *Longlide*

To reconcile the two decisions, readers should note that, the *Longlide* arbitration was seated in Shanghai, China, while the *Shenhua Coal* arbitration was seated in London.

According to generally accepted conflict of law rules as embodied in Art. V(1)(d) of the NYC, the *Longlide* arbitration was subject to Chinese law and the *Shenhua Coal* arbitration was subject to the laws of England and Wales. Thus, Art.20 was not applicable as the Chinese courts had no supervisory jurisdiction.

We may then find a reasonable explanation for the decision in *Shenhua Coal*: while *Shenhua Coal* said that Art. 20 was not applicable to an arbitration administered by a foreign institution, it was in fact referring to an arbitration seated abroad.

The "institution standard" in determining the nationality of arbitrations and awards

One may ask why the SPC based its conclusion in *Shenhua Coal* on the nationality of the administering institution instead of the seat of the arbitration.

In our opinion, this unfortunate choice was a result of the textual limitations of the Civil Procedure Law of 1991 (the "CPL"); the SPC was adopting the terminology used in legislation out of prudent judicial restraint, since the resolution of *Shenhua Coal* required only a literal interpretation.

In 1986, China ratified the NYC, Art. V(1)(d) of which provides that the law of the seat of arbitration ("the country where the arbitration [takes] place") will govern the procedure of arbitration.

Unfortunately, the first legislation dealing with foreign arbitration after China's accession to the NYC, the CPL 1991, did not embrace the concept, and its Art. 269 (now Art. 283) provides that if a party seeks the recognition and enforcement of an award rendered "by a foreign arbitral institution", it should apply to the Chinese courts "under international treaties to which China has entered into or joined, or in accordance with the principle of reciprocity", therefore characterizing awards rendered by foreign institutions as foreign irrespective of whether the award is rendered in China. This "institution standard" has remained for 24 years.

This is incompatible with the "seat standard" in the NYC. In a 2004 case, the SPC held that the nationality of the award depended on the location of the administering institution, and an ICC award rendered in Hong Kong should be regarded as a French award and be enforced under the NYC, rather than under the Arrangements on the Mutual Enforcement of Arbitral Awards between the Mainland and HKSAR.

Luckily, because of the broad reach of the NYC, the misidentification of nationality has not threatened the enforcement of foreign awards. Also, the NYC as an international convention is superior to the provisions of the CPL under Art. 260 of the CPL, and by virtue of Art. V(1)(d) the "seat standard" has been commonly adopted by the SPC in determining the applicable procedural law of a foreign arbitration proceeding in cases on recognition and enforcement of foreign awards.

Shifting to the "seat standard"

In 2006 and 2008, two lower courts, respectively in *Züblin II* and *Duferco*, characterized awards rendered by the ICC in China as "non-domestic awards" under Art. I(1) of the NYC, as no legislative basis could be found for a Chinese arbitration conducted by a foreign institution. Although these two decisions marked a shift towards the "seat standard", they were not endorsed by the SPC.

In 2010, in the Notice on Enforcement of Hong Kong Arbitral Awards in Mainland (Fa Fa [2009] No. 415), the SPC directed that arbitral awards rendered in Hong Kong, whether *ad hoc* or institutional, should be enforced under the Mainland-HK Arrangement. This implies that such awards are Hong Kong awards. However, this Notice is not an authority in the context of onshore arbitration or the enforcement of convention awards. The SPC possibly made this deviation because Hong Kong is technically not "foreign", and thus the hands of the court are not bound by Art.283 of the CPL.

Presentations made by judges from the SPC in recent seminars have also signaled that the prevailing view within the SPC supports the "seat standard", although there remains a technical difficulty to fully adopting this standard due to textual limitations of the legislation.

Chinese law as the *lex arbitri* and Chinese courts as supervisory courts

We believe that the exclusion of court intervention over foreign arbitrations described in *Shenhua Coal* should not be read literally. Chinese courts have sufficient legislative basis and judicial power to support and supervise arbitrations seated in China that are conducted by foreign institutions. We also suspect that when an appropriate case comes up, this power will be exercised.

The Chinese arbitration community has reached the consensus that the procedural law of an arbitration, the *lex arbitri*, is the law of the seat. However, when it comes to arbitrations conducted by foreign institutions in China, there is a profound disagreement over the *lex arbitri* and the nationality of such arbitration proceedings and consequent awards.

In our view, the silence or ambiguity in the Arbitration Law should not prevent Chinese courts from applying Chinese law to and exercising supervisory power over such arbitration proceedings.

Firstly, China's sovereignty and the inherent power enjoyed by a sovereign country over its territory, mandates that Chinese law is applicable to arbitration procedures conducted in the territory of China and that Chinese courts have in rem jurisdiction over such procedures.

Secondly, Art.V(1)(d) of the NYC, as an international convention and a reflection of customary international law, provides a solid foundation for applying Chinese law, as "the law of country where the arbitration [takes] place", to any arbitration seated in China.

Thirdly, under Chinese law there is sufficient basis for foreign arbitration institutions to conduct proceedings in China. The CPL authorizes parties in foreign-related contracts to refer their disputes to foreign-related or "other" arbitration institutions, without limiting the place of arbitration. *Longlide* was just entering an area, yet unexplored, but already provided for by the CPL framework.

Fourthly, regulating such arbitrations is in the public interest, as it provides confidence to domestic

and foreign users, promotes competition, enhances the quality of arbitration, alleviates the caseload of courts, and involves China more actively in the evolution of international commercial arbitration. Conversely, denying judicial review would leave parties arbitrating in China with a foreign institution in a legal vacuum, increase uncertainty in the enforcement of awards and may prejudice the final resolution of a dispute.

Finally, the lack of a specific set of rules does not render these arbitrations "non-domestic" under the NYC. The provisions applicable to foreign-related arbitrations, should generally be applicable to these arbitrations, *mutatis mutandis*; existing rules have provided solutions to many issues; the parties and the tribunal may also take measures to minimize legal uncertainty, such as designating a place of arbitration to provide clarity on judicial supervision; further, the SPC, as the supreme judicial authority, is empowered to make judicial interpretations, fill gaps, clarify rules and remedy incompatibilities.

Admittedly, a better solution is to amend the Arbitration Law and the CPL in line with international practice. However, the current legislation already provides sufficient grounds for the application of Chinese law and the exercise of its judicial power in a China-seated arbitration with a foreign institution.

Enforcement of awards

Once we agree that such proceedings are Chinese arbitrations, it is clear that such awards, as produced by arbitration procedures governed by Chinese law, should be enforced as Chinese foreign-related arbitral awards in Mainland China, instead of being treated as non-domestic awards.

The NYC leaves the definition of "non-domestic awards" to the discretion of national courts. According to Prof. van den Berg, one situation where an award is considered to be non-domestic is when the governing procedural law of the arbitration, as selected by the parties, and is different from the law of the seat of arbitration, which is not the case for a China-seated arbitration conducted by a foreign institution.

The term "non-domestic awards" should be construed in a pro-enforcement manner for the purposes of the NYC. The recommended approach provides greater certainty regarding the enforcement of arbitral awards domestically. It is undesirable that such awards be characterised as non-domestic awards, thereby reducing the likelihood of their recognition and enforcement in China. In order to facilitate the enforcement of such awards both internationally and domestically, it is necessary to recognize them as Chinese awards.

Conclusion

Longlide demonstrates the commitment of the Chinese legal system to a pro-arbitration policy and the development of arbitration in China. There are still uncertainties, due to the lack of legislation and judicial interpretation, about the *lex arbitri* of proceeding conducted by the ICC and other foreign institutions in China. We have strong reasons to believe that *Shenhua Coal* was not intended to exempt such proceedings from China's legal system. They ought to be governed by Chinese law and supervised by the judicial authorities in China. Awards rendered in such arbitrations should be enforced as onshore foreign-related awards in China.

However, when negotiating or re-negotiating an arbitration agreement in a China-related

international transaction, it would be advisable, while selecting an overseas institution such as ICC/SIAC/HKIAC, to designate the legal place of arbitration outside mainland China, to ensure that the arbitration can be conducted smoothly, and that enforcement can be sought with greater certainty.

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