Foreign Administered Arbitration in China: The Emergence of a Framework Plan for the Shanghai Pilot Free Trade Zone

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On 6 August 2019, the State Council of the People's Republic of China (PRC) (the "**State Council**") published the "Framework Plan for the New Lingang Area of the China (Shanghai) Pilot Free Trade Zone" (the "**2019 Framework Plan**").

Under Article 4 of the 2019 Framework Plan, reputable foreign arbitration and dispute resolution institutions may register with the Shanghai Municipal Bureau of Justice and the judicial administrative authority of the State Council, and set up operations in the New Lingang Area of the Shanghai Pilot Free Trade Zone ("**Shanghai FTZ**").

Registered institutions can conduct arbitrations involving civil and commercial disputes arising from areas including international commerce, maritime affairs and investment. This appears to allow foreign arbitration institutions to handle investor-state disputes seated in China, though in reality this will largely depend on whether the state involved will agree to such an arrangement.

Also, according to Article 4, registered arbitration institutions will be permitted to

enact rules to allow interim measures in favour of both the PRC and foreign parties to support the conduct of dispute resolution processes, including through preservation of assets and evidence. (The relevant parts of Article 4 as summarised above shall be referred to as the "**Statement**" in this blogpost.)

The Statement is in line with the "Plan for Further Deepening the Reform and Opening-up of China (Shanghai) Pilot Free Trade Zone" issued by the State Council in 2015 (the "**2015 Plan**"). The Statement represents an important step towards developing Shanghai into an international arbitration hub with a leading role in the Asia-Pacific region. In contrast, equivalent framework plans in relation to other free trade zones in the PRC have not placed as strong an emphasis on arbitration.

Status of Arbitrations Seated in mainland China but Administered by Foreign Arbitration Institutions

Prior to the publication of the 2019 Framework Plan, there were no express provisions allowing foreign arbitration institutions to administer cases with a seat in mainland China.

In 2013, in a reply to a request for instructions from a lower court, the Supreme People's Court ("**SPC**") acknowledged the validity of an arbitration clause providing for an arbitration seated in mainland China but administered by a foreign arbitration institution. (See an earlier blogpost on this here.) However, as the SPC's reply is not technically binding on Chinese courts, and the nationality of such an arbitration award is unclear (as discussed in the succeeding section), the prevailing view among legal practitioners remained that parties should avoid foreign-administered arbitrations seated in mainland China in light of the uncertainty.

Since 2015, foreign arbitration institutions have been allowed to set up representative offices in the Shanghai FTZ. Currently, representative offices have been set up by the Hong Kong International Arbitration Centre ("**HKIAC**"), the Court of Arbitration of the International Chamber of Commerce ("**ICC**"), the Singapore International Arbitration Centre ("**SIAC**"), and the Korean Commercial Arbitration Board ("**KCAB**"). Thus far, perhaps because of the uncertainty, these representative offices appear to have focused on promotional efforts and logistical support in arranging for arbitration hearings, rather than administering cases

seated in mainland China.

The Statement is therefore a significant step towards certainty as it suggests that, subject to successful registration, foreign arbitration institutions are permitted to administer cases seated in mainland China.

Status of Awards

Whilst this is clearly a positive development, uncertainty remains as to the status of awards: domestic or non-domestic? As discussed in a previous blogpost, the SPC has been shifting its approach in determining the nationality of an arbitral award, which in turn affects whether an award is "domestic" or "non-domestic". Under PRC law, there are procedural differences in relation to the annulment and enforcement of domestic as opposed to non-domestic awards. Hence, it would be very helpful if future guidance or regulations issued by Shanghai governmental bodies could clearly delineate whether awards made in foreign-administered arbitrations seated in mainland China would be considered domestic awards or non-domestic awards.

Alignment of Arbitration Rules

In the 2015 Plan, the State Council stated its goal to align with international dispute resolution rules, improve the arbitration rules of the Shanghai FTZ, and strengthen the internationalisation of commercial arbitration in mainland China.

With respect to various important aspects (such as the appointment of arbitrators, hearings, memorials, procedural orders, discovery, documentary evidence, witness evidence, expert evidence, confidentiality, joinder and consolidation, etc.), CIETAC arbitration rules and guidelines on evidence are, on paper, broadly in line with usual international practices. Nevertheless, the general perception is that the application of Chinese arbitration procedural laws involves, and results in, significant procedural uncertainty.

In our view, such perception is less about what is on paper (the law and rules) and more about what happens in practice. Notwithstanding the similarities in the rules

(which are stated in general terms to allow for flexibility), there is quite often a significant difference in the way arbitrations, particularly domestic ones, are handled in mainland China, and the way international arbitrations are handled outside mainland China. For example, the use of witness testimony and cross-examination is not common in arbitrations in mainland China, and practitioners are generally unfamiliar with the relevant procedures and requirements. What remains to be seen is how these China-seated foreign-administered arbitrations will be conducted. There may well be no consistency in approach as it ultimately comes down to how individual arbitrators manage a specific arbitration.

In any event, as foreign arbitration institutions start to administer cases seated in China, there will be a "cultural exchange" at a deeper level as more PRC lawyers get involved in foreign-administered cases, and more foreign parties get involved in China-seated cases. This will certainly be a welcomed development towards the improvement of the PRC arbitration rules and practice, as well as towards the internationalisation of commercial arbitration in mainland China.

Impact on Hong Kong

When the Statement has been fully implemented, and foreign arbitration institutions begin to operate directly in mainland China, Shanghai will likely become a much more important arbitration hub than it is currently. Foreign commercial parties, who previously preferred arbitrations seated in Hong Kong, may be increasingly willing to have arbitrations seated in mainland China if they are administered by a reputable foreign arbitration institution. This is particularly the case with respect to the Belt and Road Initiative, where Chinese parties have strong bargaining power and would most likely prefer to have arbitrations seated in mainland China.

As Shanghai becomes a more important arbitration centre, there is some prospect of Hong Kong gradually losings its competitive advantage as the leading disputes resolution hub in Asia.

Nevertheless, an important factor in selecting an arbitration seat is court supervision. Hong Kong is still perceived to have a very strong rule of law. For example, the World Bank Group, as part of its World Governance Indicators project,

ranked Hong Kong as second in Asia and fourteenth globally for the rule of law for the year of 2017. The World Economic Forum's Global Competitiveness Report 2018 has ranked Hong Kong's judiciary as the number one most independent in Asia and eighth globally. Mainland Chinese courts still do not reach the perceived standards of independence and reliability of the Hong Kong courts. The Hong Kong common law system is perceived as very stable and predictable, with its system of precedent and *stare decisis*.

Moreover, there are well established frameworks for Chinese courts to grant interim measures in connection with arbitrations seated in mainland China and Hong Kong. (See this previous blogpost with respect to the arrangement with Hong Kong.) To date, the PRC has not established any similar arrangements with other jurisdictions. In other words, Hong Kong will remain an attractive option for PRC-related international arbitration disputes: for court supervision by an independent and reliable judiciary system and procedural convenience in connection with interim measures in mainland China.

Concluding Remarks

It goes without saying that China's economic development has been, and still is, at high speed, with six new free trade zones announced just days ago in six provinces (including border regions) across China. The Shanghai FTZ (whose size doubled recently following the inclusion of the New Lingang Area) takes the lead in all this. The Statement comes as a bold step to bolster international confidence in Shanghai's disputes resolution system – a crucial element to establish Shanghai's status as a "world city"— and a demonstration of China's commitment to deepen its reform as laid out in the 2015 Plan. This is certainly a positive initiative, both for Shanghai and for foreign parties with commercial interests in China. As for Hong Kong – it retains its unique edge but tough competition is waiting ahead.