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Guiding Cases 196 – 198 Issued by the PRC Supreme People’s Court – Further Steps Toward a Pro-Arbitration Regime

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In 2010, the Supreme People’s Court of the People’s Republic of China (the “SPC”) issued the Provisions of the Supreme People’s Court on Case Guidance (the “Provisions”). The Provisions are widely considered to establish a unique case guidance system in China, under which courts at all levels should refer to the selected guiding cases when adjudicating similar issues.

On the last working day of 2022, and “on the eve” of a revised Chinese Arbitration Law, the SPC released its 36th batch of six guiding cases. Unprecedentedly, all of the six guiding cases are related to the judicial review of arbitration cases. This article highlights the backgrounds and key holdings of Guiding Cases 196, 197 and 198 (the first three of the six guiding cases, which focus on several pivotal issues related to the arbitration agreement) and seeks to explain the significance behind these court decisions.

Guiding Case 196: The Doctrine of Separability of the Arbitration Agreement

In Guiding Case 196 (*Yunyu Co. Ltd. v Shenzhen Zhongyuancheng Commercial Investment Holdings Co. Ltd.*), the First International Commercial Court of the Supreme People’s Court (the “FICC”) was faced with an arbitration respondent’s application to confirm the non-existence of an arbitration agreement on the ground that the whole contract that contained the arbitration agreement had been in the process of negotiation and was never signed between the Plaintiff and the Defendant.

The FICC first affirmed its jurisdiction to review this issue. It confirmed that the issue of determining the *existence* of an arbitration agreement falls within the scope of assessing the *validity* of an arbitration agreement, which is a cause of action pursuant to Article 20 of the Arbitration Law of the People’s Republic of China.

The FICC then carefully examined the parties’ negotiation history, particularly as it relates to the arbitration clause. The judges noted that in the first draft contract (“Draft Contract I”) sent by the Plaintiff, the arbitration clause listed the Beijing Arbitration Commission (“BAC”) as the arbitration institution. However, after receiving Draft Contract I from the Plaintiff, the Defendant replied to the Plaintiff and suggested changing the arbitration institution from BAC to the Shenzhen Court of International Arbitration (“SCIA”). Afterwards, the Plaintiff adopted SCIA as

the arbitration institution in the revised draft contract (“Draft Contract II”) and sent the copy back to Defendant. Subsequently, the Defendant had Draft Contract II sealed and delivered back to the Plaintiff. The parties then engaged in further negotiations regarding other clauses in the contract, but the arbitration clause remained unchanged.

Based on the above conduct surrounding the negotiation of the arbitration clause, the judges held that, as far as the arbitration clause was concerned, the Plaintiff’s sending of Draft Contract II should be regarded as an offer made by the Plaintiff in accordance with [the PRC Contract Law](#) and that the Defendant’s subsequent sealing of Draft Contract II should be regarded as an acceptance of the arbitration clause. As a result, the judges ruled that the arbitration clause had already been concluded at the time the sealed Draft Contract II was delivered to the Plaintiff even though other clauses in the contract did not come into effect because the contract had not been signed.

In sum, Guiding Case 196, which was heard by a panel of five SPC judges, presents an opportunity for the court to meticulously apply the doctrine of separability in determining the status of the arbitration clause where the main contract has arguably not yet been concluded.

It is noteworthy that in *DHL Project & Chartering Ltd v Gemini Ocean Shipping Co Ltd* [2022] EWCA Civ 1555, the High Court of Justice of England and Wales reached a different conclusion facing a similar issue. The different conclusions reached by the courts likely primarily stem from the factual differences between the English case and Guiding Case 196. In the English case, it is difficult to trace any substantial negotiations or discussions regarding the arbitration clause that were separate from negotiations of the main contract. In contrast, in Guiding Case 196, because such negotiations were quite distinct, the FICC engaged in a fact-intensive inquiry into whether the parties had a meeting of minds with respect to the arbitration clause. Therefore, it is understandable that the two cases reached opposite conclusions about the existence of the arbitration clause.

Guiding Case 197: Challenging the Arbitration Agreement in “the First Hearing at the Arbitration Tribunal”

The issue in Guiding Case 197 (*Shenzhen Shizhenggongying Investment Holdings Co. Ltd v Shenzhen Municipal Transport Bureau*) relates to [Article 20\(2\) of the Arbitration Law of the PRC](#), which provides that “[a] *doubt as to the effectiveness of the arbitration agreement, should be raised before the first hearing at the arbitration tribunal.*”

In Guiding Case 197, the arbitration claimant did not raise any jurisdictional challenge—either before the arbitration tribunal or in the court—before the first hearing in the arbitration proceeding. After the arbitral award was issued, Claimant resisted enforcement in the Shenzhen Intermediate People’s Court (“Shenzhen Intermediate Court”). The Shenzhen Intermediate Court neither refused to enforce the award nor dismissed Claimant’s application; instead, the court found it appropriate for the arbitration tribunal to make a new award and remanded the award in whole for re-arbitration according to [Article 61 of the Arbitration Law of the PRC](#).

In the re-arbitration, the Claimant, for the first time, raised a new challenge over the validity of the arbitration agreement in the Shenzhen Intermediate Court. The challenge was dismissed by the Shenzhen Intermediate Court, whose dismissal was affirmed by the Shenzhen High Court. The Shenzhen High Court held that even though the underlying case went to re-arbitration, insofar as the two arbitrations relate to the same dispute, the Claimant remained bound by its conduct during

the first arbitration. The Claimant's failure to challenge jurisdiction in the first arbitration thus constitutes a waiver of its right to challenge under Article 20(2) of the Arbitration Law; and the Claimant cannot have a second bite at the cherry in the re-arbitration process. The Shenzhen High Court opinion was selected as Guiding Case 197.

The Shenzhen High Court's opinion was also in line with ensuring the efficiency of the arbitration process. If parties facing the same dispute, without newly discovered material evidence or facts, were to be entitled to challenge the validity of the arbitration agreement, it may cause undue delay in the arbitration process, and may also run afoul of the principle of *res judicata*. This case serves as a reminder for the parties to proactively exercise their legal rights as failure to do so may constitute a waiver even in a re-arbitration proceeding.

Guiding Case 198: Privity of the Arbitration Agreement in Construction Arbitration

Guiding Case 198 (*Industrial and Commercial Bank of China Limited, Yueyang Branch v Liu Youliang*) concerns the privity of the arbitration agreement in the context of the arbitration of construction work disputes. Relevant parties involved in a construction arbitration generally include the employer, the contractor, and the subcontractor(s) (or actual constructor(s)). The contractor typically signs contracts with the employer and the subcontractor(s) respectively. As such, there is generally no contractual privity between the employer and the sub-contractor(s).

In 2004, in order to protect the legitimate interests of the subcontractors (mostly migrant workers), specifically with regard to their wages, the SPC issued "The Interpretation of the Supreme People's Court on Issues Concerning the Application of Law for the Trial of Cases of Dispute over Contracts on Undertaking Construction Projects" (the "2004 Interpretation"). Article 26 of the 2004 Interpretation grants the subcontractor the right to break the contract privity and to directly file a lawsuit against the employer when the employer failed to make payment of construction project costs owed to the contractor. Though controversial, this particular provision was never abrogated and remains included in the latest SPC Interpretation issued in 2020 as Article 43.

A thorny issue raised by this provision is whether the employer may rightfully contend—as many do—that the subcontractor is subject to any arbitration clause established between the employer and the contractor, as the subcontractor has in effect, substituted the contractor's rights. Prior to the issuance of Guiding Case 198, Chinese courts were divided on this issue. In *Zhongjiao Second Highway Engineering Co. Ltd v. Fu Yang* and *Qinghai Senkeyanhua Industry Co. Ltd v Xiong Daohan, Chongqing Jianan Construction Co. Ltd*, the SPC opined that the right granted to a subcontractor under Article 26 of the 2004 Interpretation should be defined as a subrogation right under civil law; and that a subcontractor is accordingly bound by any arbitration clause that was originally agreed upon between the contractor and the employer. However in *RongSheng (BengBu) Properties Co. Ltd v HeFei Huaxing Construction Installation Co. Ltd* and *Cheng Jingnan v Nantonghaizhou Construction, Nantong Branch Co. Ltd*, the SPC and the Anhui High Court held that, insofar as Article 26 of the 2004 Interpretation is a special arrangement designed to address the issue of outstanding wages for migrant workers in a particular era and social context, the assertion of rights by the subcontractor against the employer should not be interpreted as a succession of the contractor's rights and that, accordingly, the subcontractor should not be bound by the arbitration clause between the contractor and the employer.

Guiding Case 198 adopts the latter view. Yueyang Intermediate People’s Court, in the opinion that was selected as Guiding Case 198, expressly held that there was no “succession” of the contractual arbitration clause from the contractor to the subcontractor. Article 26 of the 2004 Interpretation only grants the subcontractor a *sui generis* right to initiate a lawsuit against the employer but does not serve as a legal basis to extend the scope or effect of the arbitration clause between the employer and the contractor to the subcontractor.

This author is of the view that Guiding Case 198 does not firmly shut the door to a contention that the subcontractor could, in certain circumstances, be bound by an arbitration agreement between the employer and the contractor. For example, in circumstances where the subcontractor has taken on the *de facto* role of the contractor and has performed the contractor’s duties and obligations during the construction process, or where the contractor-subcontractor contract clearly stipulates that its performance shall be subject to the employer-contractor contract, and the subcontractor is aware of the existence of the arbitration clause in the employer-contractor contract, then the subcontractor may arguably rely on or be bound by the arbitration clause. Such circumstances should still be diligently examined on a case-by-case basis.

These three guiding cases shed light on Chinese courts’ stance on three significant while controversial issues related to arbitration agreement. Meanwhile, with the substantial revision of the Chinese Arbitration Law, the future arbitration practice in this regime is worth expecting.

Note: The views expressed in the article are the authors’ own and do not represent the views of others.

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This entry was posted on Friday, September 29th, 2023 at 8:01 am and is filed under [Arbitration Agreement, China, Separability](#)

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