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Asymmetrical Arbitration Agreements Under PRC Law

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Introduction

This article explores the latest development of the People's Republic of China's jurisprudence regarding asymmetrical arbitration agreements. *(Cambodia) Fiber Optic Communication Network Co., Ltd. v. China Development Bank* (2022) Jing 74 Min Te No. 4 ("***Fiber Optic v. CDB***"), a recent case adjudicated by the Beijing Financial Court in October 2022 and made public in late 2023, marks the first instance where the court explicitly recognizes the validity of an asymmetrical arbitration agreement under the PRC law.

Asymmetrical arbitration agreements, which allow one contractual party to choose between arbitration or litigation for dispute resolution while restricting the other party in its options, have historically been deemed invalid under Article 7 of the PRC Supreme People's Court's *Judicial Interpretation on Certain Issues Concerning the Application of the Arbitration Law of the People's Republic of China* ("**Interpretation of Arbitration Law**"), which provides that arbitration agreements permitting parties to pursue either litigation or arbitration are null and void.

At first glance, *Fiber Optic v. CDB* appears to signal a departure from the established jurisprudence. However, upon closer examination, an argument can be made that the jurisprudence of Article 7 remains consistent. The key element that distinguishes *Fiber Optic v. CDB* from the previous cases lies in a nuanced distinction between two different sub-categories of asymmetrical arbitration agreements—one of which, according to the court, contains a clear agreement to arbitrate to the exclusion of litigation. The case underscores the importance for practitioners to meticulously draft asymmetrical arbitration agreements to ensure that they embody a clear and unambiguous consent to arbitrate to the exclusion of litigation.

What Are Asymmetrical Arbitration Agreements?

Under typical arbitration agreements, both parties to the contract are bound to resolve their disputes through arbitration. Such arbitration agreements are considered symmetrical, given that the obligations to refer to arbitration are equally vested in both parties.

Sometimes, however, the arbitration agreements introduce a disparity in the options available to the parties. They grant one party (hereinafter referred to as the "**Two-Options Party**") the flexibility to choose between arbitration and litigation, while the other party (referred to as the

"**One-Option Party**") is limited to a single dispute resolution method. This delineation creates a dynamic where the Two-Options Party possesses a strategic advantage to select the dispute resolution method that best suits its interests, while the One-Option Party must adhere to the single pre-determined route regardless of the circumstances. Such agreements are referred to as asymmetrical arbitration agreements.

Previous Jurisprudence Regarding Asymmetrical Arbitration Agreements

The enforceability of asymmetrical arbitration agreements under PRC laws has been on shaky grounds. Only a handful of precedents have tackled this issue and, in all of these cases, the courts have held that such agreements were invalid.

At the heart of this issue is Article 7 of the Interpretation of Arbitration Law, which states that an arbitration agreement must be invalid if it allows disputes to be resolved through either arbitration or litigation:

> *If the parties agree that their disputes could either be referred to an arbitration institution for arbitration or the people's court for litigation, then the arbitration agreement is null and void, unless one party submits the dispute to arbitration and the other party make no objections within the time period prescribed under Article 20(2) of the Arbitration Law.*

This provision's underlying legislative concern is to avoid chaos that would arise if one party pursues arbitration and the other party insists on litigation, in which case there would effectively be no agreement to arbitrate. Such conflict could potentially result in prolonged jurisdictional disputes and hence significantly increased costs.

Asymmetrical arbitration agreements, which typically allow the "Two-Options Party" the choice between arbitration and litigation, have been seen as falling into the category of such either-or agreements that are prohibited under Article 7 of the Interpretation of Arbitration Law.

For instance, in *Geox Trading (Shanghai) Limited v. Riqing Group-Ricco Rachel Trading Co., LTD.* (2015) Er Zhong Min Te Zi No. 12930 ("***Geox Trading v. Riqing Group***"), the arbitration agreement in dispute provides that both the seller and the buyer are entitled to refer their disputes to arbitration in China International Economic and Trade Arbitration Commission ("**CIETAC**"), whereas the seller is additionally entitled to submit disputes to litigation at the buyer's residence. The Second Intermediate Court of Beijing found this agreement to be in direct violation of Article 7 of the Interpretation of Arbitration Law, which therefore rendered the agreement void. Likewise, in both *Chen Youhua v. DBS Bank (China) Co., Ltd. Shanghai Branch* (2016) Jing 02 Min Te No. 93 ("***Chen v. DBS Bank***") and *Hainan Kangda Loan Co., Ltd. v. Hainan Xinyangguang Junan Real Estate Development Co., Ltd. et al* (2020) Qiong Min Xia No. 2 ("***Kangda v. Xinyangguang***"), the courts invalidated, on similar grounds, asymmetrical arbitration agreements permitting one party to choose between litigation and arbitration and constraining the other party to litigation.

Prior to *Fiber Optic v. CDB, t*he only exception we are aware of that explicitly recognized the

enforceability of an asymmetrical arbitration agreement was *Xiamen C&D Chemical Co., Ltd. v Switzerland Albert Trading Co., Ltd.* (2016) Hu 01 Min Zhong No. 3337. The judgment was rendered by the First Intermediate Court of Shanghai, however, applying Swiss law as the law applicable to the arbitration agreement.

Fiber Optic v. CDB

On 25 October 2023, the Beijing Financial Court released the White Paper on Judicial Review of Financial Arbitration Cases (the "**White Paper**"). The White Paper features *Fiber Optic v. CDB* as a guiding case for financial arbitration.

Fiber Optic v. CDB involved a dispute between Fiber Optic and CDB over an alleged breach of the pledge agreement between them. The asymmetrical arbitration clause of the pledge agreement provides:

> 23. DISPUTE RESOLUTION ***Unless* [CDB]*chooses otherwise***, *any dispute, difference or demand arising out of or in connection with this agreement, including issues regarding the existence, validity, interpretation and performance of the contract, shall be submitted to China International Economic and Trade Arbitration Commission for arbitration… 23.2* ***Notwithstanding Article 23.1, the parties shall be subject to the exclusive jurisdiction of Cambodian courts if* [CDB] *so elects.***

CDB submitted the dispute to CIETAC for arbitration, and Fiber Optic contested the validity of the arbitration agreement before the PRC courts relying on Article 7 of the Interpretation of the Arbitration Law.

Marking a departure from previous cases, the Beijing Financial Court did not invalidate the disputed asymmetrical arbitration agreement based on Article 7 of the Interpretation of Arbitration Law. Instead, highlighting that "*the nature of the agreement depended on* [CDB]*'s choice*", the court recognized the agreement's validity.

At first glance, *Fiber Optic v. CDB* marks a significant deviation from the established jurisprudence. However, a detailed examination of the arbitration agreement shows that the legal position of the One-Option Party in *Fiber Optic v. CDB* is markedly different from those under the previously invalidated agreements.

As is the case with all asymmetrical arbitration agreements, the One-Option Parties in both *Fiber Optic v. CDB* and the previous cases are limited to only one dispute resolution method. However, in *Fiber Optic v. CDB*, the One-Option Party's entitlement to its designated dispute resolution method, as set forth in the contract, is expressly conditional, whereas in previous cases, it is not. Specifically, Fiber Optic is entitled to seek arbitration *only if* the Two-Options Party, CDB, also chooses arbitration. As required by the clause "[u]*nless* [CDB] *chooses otherwise*" and by Article 23.2, if CDB elects litigation in Cambodian courts, Fiber Optic is bound to comply. In contrast, in *Geox Trading v. Riqing Group*, *Chen v. DBS Bank* and *Kangda v. Xinyangguang*, such express waiver of rights is missing and the One-Option Parties' rights to seek litigation/arbitration is unconditional. In other words, the asymmetrical arbitration agreements in those cases do not

expressly stipulate that the One-Option Parties must defer to the Two-Options Parties if the Two-Options Parties choose a different dispute resolution method.

Consequently, agreements such as the one in *Fiber Optic v. CDB* invariably lead to one exclusive and definitive dispute resolution process, where the outcome always depends on the Two-Options Parties' decision. In the event that arbitration is selected, such agreements guarantee a unanimous consent to arbitrate to the exclusion of litigation, as the One-Option Party's potential right to litigation would have been pre-emptively waived. In contrast, agreements like those in the earlier cases are readily susceptible to a deadlock scenario, where one party seeks litigation and the other party insists on arbitration, with no obligation for either party to defer to the other's choice.

While the Beijing Financial Court's reasoning does not explicitly capture this analysis, its focus on the unilateral element of the disputed asymmetrical arbitration agreements, highlighting that "*the nature of the agreement depended on the* [Two-Options Party's] *choice*", suggests that this is the underlying consideration leading to the recognition of the agreement's enforceability. As stated above, the main concern behind Article 7 of the Interpretation of Arbitration Law is to avoid enforcing arbitration in the absence of a clear consent to arbitrate and exclusion of litigation. The asymmetrical arbitration agreements in earlier cases, whose outcome does not depend on the Two-Options Party's choice, could well be invalidated following the same rationale.

Observations

It follows that, instead of interpreting *Fiber Optic v. CDB* as a shift towards a categorically more favorable treatment of asymmetrical arbitration agreements, an argument can be made that the jurisprudence of Article 7 of the Interpretation of Arbitration Law has remained consistent throughout the earlier cases and *Fiber Optic v. CDB*. That is, the real question is not whether asymmetrical arbitration agreements *per se* are valid, but whether a clear and unequivocal agreement to submit the dispute exclusively to arbitration is present in the asymmetrical arbitration agreement in question. In the earlier cases, it was not. In *Fiber Optic v. CDB*, it was.

In light of *Fiber Optic v. CDB*, practitioners are advised to exercise prudence when introducing asymmetrical arbitration agreements where the law applicable to the arbitration agreement could be PRC law. If an asymmetrical arbitration agreement is to be incorporated, it is suggested that drafters explicitly condition the One-Option Party's right to its designated dispute resolution method on the Two-Options Party's selection of the same method. On a broader scope, for any draft arbitration agreements, parties are advised to ensure that the clause is drafted in such a way that the court could readily identify a clear agreement to arbitrate to the exclusion of litigation.

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