CHAPTER 2 HISTORY OF ARBITRATION IN CHINA

By Damien McDonald

INTRODUCTION

China's unique path to arbitration

2.1 A discussion of the history of Chinese arbitration is important to understanding many of the other chapters and concepts in this text. This is because it engages with the question of how and why Chinese arbitration has developed into its existing model.

2.2 In this respect, Chinese arbitration is a unique model of arbitration. It is not the western model of arbitration transplanted into China without change. Instead it has developed according to its own cultural, political, legal and economic environment. Within each of these aspects is embedded a specific policy perspective and set of values from a particular stage of China's history. In this respect, it is submitted that the PRC government policies, perspectives and values from the early 1990s and earlier, effectively underpin the structure of the present Arbitration Law.

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Scope of this chapter

2.3 The discussion in this chapter focuses on PRC commercial arbitration and the development of both domestic and foreign-related arbitration systems. The term 'commercial arbitration' is used in the sense that both these systems engage with contracts, investment (and in particular foreign investment) and trade.

2.4 This chapter briefly introduces the early models of arbitration in the late-Qing Dynasty and the Republican period of China, but focuses mainly on the People's Republic of China era from 1949 until the early part of this century. While this last era has seen the most significant developments, especially since the mid-1990s, it is also important to consider the development of arbitration throughout the entire period of the PRC.

2.5 In doing so, it observes that while both domestic and foreign-related arbitration did not develop in any meaningful sense from 1949 until the early 1990s, the developments in the early part of this period and, in particular, the establishment of the Foreign Trade Arbitration Commission ('FTAC') in 1956 (later the FETAC and then CIETAC) was crucial in the development of foreign-related arbitration in the period post-1978. The establishment of domestic arbitration commissions in the early 1980s was equally important in terms of framing the structure and values underpinning the future Arbitration Law.

Development and change

2.6 The reasons arbitration did not develop in the early period (1949–1978) can to some extent be explained by China's Socialist political, legal and (planned) economic model that was in many respects (and for many reasons) an isolationist one that did not require a full domestic arbitration system and had no reason to fully develop a foreign-related or international arbitration system. The existing domestic and foreign-related arbitration systems have grown since the early 1990s and developed at an astonishing pace, not only in terms of caseload but also the increased sophistication of the People's Courts, and in particular the SPC, which interpret and set the judicial policy on those laws, and the Chinese arbitration commissions that apply them.

2.7 The reason that it has developed so rapidly is almost the inverse of the reasons for the stalled development, namely sufficient reforms within the Chinese Socialist legal and economic models and engagement with the international business and legal communities through trade and foreign direct investment.

2.8 There are many limitations in trying to deal with all of these issues in one short chapter,[1] but the next section will frame some of the discussion into themes that will be developed throughout the chapter below.

The History of Commercial Arbitration in China

2.9 The history of Chinese arbitration is not simply about the chronological development of the relevant laws and their content, it is also about asking how and why these laws were introduced and the extent to which they have impacted on the practice of arbitration in China. The laws are connected to the broader developments in Chinese history over the past century and are interesting because they reflect changes in China itself. This approach brings out some of the themes below, such as the importance of the legal framework, the role of the State and economic development.

1 For further reading see K Fan, *Arbitration in China. A Legal and Cultural Analysis* (Hart Publishing, 2013), J Tao, *Arbitration Law and Practice in China* (3rd edn, Kluwer Law International, 2012) and S Lubman, *Bird in a Cage: Legal Reform in China After Mao* (Stanford University Press, 1999). S Lubman is not particularly focused on arbitration but is an important piece of scholarship on the development of law in China. There are many other contributions in this area, such as W Wang, 'Distinct Features of Arbitration in China: A Historical Perspective' [2006] 23(1) Journal of International Arbitration 49, which explain in detail the different systems pre- and post- the Arbitration Law. The further articles cited below in this chapter also contribute to the discussion on the history of arbitration.

Legal frameworks

2.10 The first theme for this chapter is that the development of commercial arbitration in China first required the development of a legal framework and a legal system that would support it. The absence of a developed framework or legal system, including not only laws, but also lawyers to practise the law and judges and courts to enforce them, meant that China would not have a fully functioning arbitration system until at least the early 1990s (although elements of it did exist, including a framework for the conduct of foreign-related arbitrations conducted by CIETAC and CMAC before then).

2.11 The slow development of the PRC court system and its lack of sophistication in terms of arbitration post-1978 has required the SPC itself to take more of a leadership role in educating, supervising and assisting lower People's Courts in the implementation of the law. This is discussed further in paragraphs 2.106–2.111.

2.12 The development of the legal framework in the China context encompasses more than the particular framework for arbitration itself (which is discussed in Chapter 3). It includes the separate reforms to contract and civil law in China, which in the early 1990s began to separate the State as an interested party in the contract into something that was about rights and obligations between the two contracting parties, without (or with less) interference or involvement from the State. This change was also an integral part the broader economic reforms, which is another of the themes set out below.

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The State

2.13 The State is central to any discussion on dispute resolution in China. In China, the State has historically had a role in all forms of dispute resolution, whether as a party, administrator, mediator, arbitration commission or legislator. This position still exists to an extent today in terms of the People's Court structure and administration and separation from the government.

2.14 Arbitration is however an exercise of quasi-judicial power authorised by the parties to the arbitration agreement. The exercise of this power is problematic in that this area falls within the scope of roles formally undertaken directly by the State itself until the mid-1990s in the domestic arbitration context. In this respect, the State has remained involved indirectly through the introduction of Chinese arbitration commissions as part of the legal framework (discussed below and in more details in Chapters 3 and 8).

2.15 In the period post the introduction of the Arbitration Law, the PRC government also remained directly involved via the *de novo* judicial review of domestic awards until the revised Civil Procedure Law on 1 January 2013 removed these grounds of review.[2] This *de novo* review was available in the domestic

2 The Civil Procedure Law (1991), Article 217(4) states that 'the main evidence for ascertaining the facts is insufficient' (认定事实的主要证据不足的) and 217 (5) states that 'there is definite error in the application of the law' (适用法律确有错误的).

arbitration system existing immediately prior to the introduction of the Arbitration Law in 1995, both as an internal supervisory (adjudicatory) function within the hierarchy of domestic commissions and also via the option to commence a separate legal proceeding in the People's Courts if a party did not agree with the award.[3] While it is possible to overstate the significance of the overlap between the scope of review of administrative arbitration and domestic arbitration systems, it is a reflection of the parallel review function of the State within the two systems.[4] There was, in essence, no difference between the scope of review between the two systems.

Economic development and changes in policy

2.16 There was minimal arbitration in the period 1949–1978 during which China was largely isolated with little international trade and was operating under a strict centrally planned economy.[5] The FTAC was operating during this period, but the level of cases it managed was so statistically insignificant that it is not meaningful in any sense of Chinese arbitration practice. The mere fact that the FTAC and its successors existed as an institution is important for other reasons, referred to in paragraph **2.86**.

2.17 The opening up to foreign investment and development of the economy which started in 1978 required law reform of the commercial law and in particular the law of contract (starting with the Economic Contract Law in 1982). These reforms were required in order to facilitate foreign investment into China and was an explicit policy goal of the Chinese government. This in time led to the development of a far more detailed and comprehensive Chinese Arbitration Law in 1995, which is the focus of every chapter in this book.

Before the Late Qing Reforms—Merchant Guilds

2.18 A full discussion on the Chinese legal system of the pre-Qing Dynasty is beyond the scope of this short chapter.[6]

3 Economic Contract Arbitration Commission Working Rules (Promulgated by SAIC and effective on 20 August 1985) (经济合同仲裁委员会办案规则) Articles 37 and 38 and the Technology Contract Arbitration Institution Rules (for Trial Implementation) (技术合同仲裁机构仲裁规则（试行）) (Promulgated by the State Technology Commission on 26 June 1991 and effective on 1 November 1991), Articles 46 and 47.

4 This point is discussed further in paragraphs **2.76–2.83** below in terms of the legacy of the old administrative domestic system.

5 This is not to concede that no arbitration occurred, but only that it was largely irrelevant internally and had a limited role in terms of international trade.

6 There are a number of very good introductions to the history and development of Chinese law. For example, J Chen, *Chinese Law: Towards an Understanding of Chinese Law, Its Nature and Development* (Kluwer Law International, 1999).

Self-regulation

2.19 The Chinese governments for most of the Qing Dynasty were content for China to be an agrarian economy with strict divisions within society and separation between classes. The merchants were a separate class from other classes in this period (for example, peasants, landlords and craftsmen). The merchants (including their disputes) were not regulated apart from the imposition of taxes. Instead, the merchants formed 'Guilds' (会馆), which were largely self-regulated in terms of their internal dealings.[7]

Internal justice

2.20 The guilds instead developed a system of internal dispute resolution for disputes between their members in which disputes were referred to internal arbitration for dispute resolution. The right to complain to the authorities or bring a legal proceeding was preserved, but the members were obliged to resort to the internal dispute resolution system first. This system could also be seen as a way in which the merchants themselves filled the gap in the law on matters dealing with commercial law (an observation which is made below on the late-Qing period, but is equally applicable here as well).

2.21 Professor Fan explains that in this system the dispute resolver shifted between arbitrator to mediator, but does not conclude that the system was arbitration because it was not a 'semi-formal neutral institution which resolved disputes on the principles of free will and private justice'.[8] It is, however, evidence of merchants, seeking to create a separate system of dispute resolution as an alternative to civil justice in the courts.[9] This of course continues to be a reason for parties wanting to adopt arbitration today.

Arbitration and trade

2.22 The more important observation is that there was an alternative system of commercial dispute resolution which had developed because of the need to resolve disputes, which the then Magistrates system was not capable of (or indeed interested in) resolving in the same way.[10] In this respect, it does have something in common with the way in which arbitration in other countries developed outside the court system, but ultimately required the assistance of the government or the

7 Fan (n 1) 204–207.

8 K Fan, 'Glocalization of Arbitration: Transnational Standards Struggling with Local Norms Through the Lens of Arbitration Transplantation in China' [2013] 18 Harvard Negotiation Law Review 175, 208.

9 The system was not arbitration, but it was perhaps closer than many forms of arbitrations claimed as early models of arbitration: F D Emerson, 'History of Arbitration Practice and Law' [1970] 19(1) Cleveland State Law Review 155, refers to King Solomon (1 Kings 3:16–28).

10 Fan (n 8) 205.

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courts to develop the actual framework.[11] The next step in development depended on the involvement of the Chinese government.

2.23 This was also, in many respects, the reason that it did not develop because it was not something successive governments of the time had any interest in developing. It is interesting to contrast this with the further discussion below (the late-Qing in paragraphs **2.24–2.29** and the PRC (1978–1995) in paragraphs **2.62–2.104**), in which the role of the government is key in terms of allowing arbitration systems to develop.

Late-Qing Dynasty: 1860–1911

2.24 The late-Qing government's reforms were designed to make China's legal, administrative and commercial organs more self-reliant.[12] The law reform was focused on revising the old Qing Code, but also the drafting of new civil and criminal codes. The revision of the Qing Code was completed in 1910, but the two new codes were not completed before the Republic in 1912.[13] There was also a very extensive set of new regulations and laws that were promulgated for the first time, including China's first Company Law and the Bankruptcy Code promulgated in 1904.[14]

2.25 This rush of legislation is not dissimilar in terms of policy to the PRC's extensive reforms post-1978, which are discussed in more detail below. There is, however, an important distinction between those two reforms in that the late-Qing reformers tended to adopt foreign laws with little change. The early PRC Reformers in the 1980s *adopted and adapted* foreign laws that the Chinese system needed.[15] The Arbitration Law was no exception.

2.26 It is against this backdrop of reform that the guilds were organised into chambers of commerce and put under the control of the newly formed Ministry of Commerce with the first chamber of commerce being created in 1904 by the

11 See e.g. Lord Mustill, 'Arbitration: History and Background' [1989] 6(2), Journal of International Arbitration 43, who outlines the path of development of arbitration in England and the relationship of reforms in the courts to support arbitration. The point here is not a comparative one, but rather a self-evident one in that in order for arbitration to develop beyond a purely consensual and internal model it needs the support of the government and the courts.

12 For a fuller discussion on the origin of the late-Qing reforms, the key reformers and their relative success, see C Shi 'Commercial Development and Regulation in Late Imperial China' [2005] 35(1) Hong Kong Law Journal 481, 495 and J Zhang, *The Tradition and Modern Transition of Chinese Law* (Springer-Verlag, Berlin Heidelberg, 2014), Ch 18.

13 P Huang, *Code, Custom and Legal Practice in China—The Qing and the Republic Compared* (Stanford University Press, 2001) 21.

14 Y Zhu, 'On Late Qing Economic Laws and Regulations' [1995] Chinese Studies History 101, 116. In this article, Zhu cites a very wide range of laws and regulations that were introduced to China for the first time, ranging from banking laws to railway regulations. There were also reforms in the areas of courts with the Law for the Organisation for the Supreme Court (大理院审判编制法) being issued in 1906 as well as The Imperial Outline of the Constitution in 1908 (钦定宪法大纲).

15 Chen (n 6) 18–21 and 48.

Qing government with the 'Concise Regulations of the Chamber of Commerce' (商会简明章程) promulgated to officially recognise the legal status of arbitration institutions set up by various local chambers of commerce.

The first arbitration commissions

2.27 Professor Fan refers to the 'Western model of arbitration' as being introduced into China in 1906 and the introduction of arbitration institutions within the chambers of commerce, which adopted the term 'commercial arbitral bodies' (商事公断处).[16] These bodies were however restricted by the Ministry of Justice to conducting arbitration and mediating disputes and their arbitration awards were only binding if both parties accepted the result. If there was no agreement then the matter could be brought before the courts. This is a significant limitation, but it is not fundamentally different from the position for domestic awards until 2013 in that there was in substance no difference between a *de novo* review and starting again in the Chinese courts. This change is discussed in paragraphs **2.128–2.129** below.

2.28 The chambers' commercial arbitral bodies were functioning, and based on the (albeit) reportedly incomplete records, relatively busy institutions. These bodies were established by various chambers of commerce throughout China, from Tianjin to Shanghai to Chongqing and Baoding. The caseloads reflect the requirement for an alternate method for the resolution of commercial disputes and the commercial law in the late-Qing.[17]

Government and frameworks

2.29 The most important observation on this initial period is that arbitration was recognised by the late-Qing government as a method of commercial dispute resolution that the merchants (chambers of commerce—formerly the guilds) wanted and needed to conduct their business. The non-binding nature of the award is however an area that will continue to be a theme, at least in the domestic sense, in the next and later periods set out below.

16 Fan (n 1) 207, footnote 121 Zhizun Yang, 'Explanation of Commercial Bodies', 25 Official Journal of Commerce (1906) (6). The 'Western' model is however not exhaustively defined, but in broad terms contemplates the importance of arbitrators having the relevant business expertise. E.g., businessmen in Belgium can be appointed as arbitrators provided that they (1) have paid a certain amount of business tax; (2) have the right level of experience; and (3) are entitled to be elected as a city councilor. This is an economic qualification rather than a legal one.

17 Ren Yunlan, 'Chambers of Commerce's Function of Commercial Arbitration in Modern China' [1995] 4 Chinese Economy History Research (任云兰《论近代中国商会的商事仲裁功能》中国经济史研究1995年第4 期). From the archive records, the effectiveness of commercial arbitration institutions was remarkable. According to the statistics, from the period between 1903 and 1917, a total of 5157 commercial disputes were settled by the Tianjin Chamber of Commerce (从档案记载来看，商事仲裁机构成效卓著。据统计，从1903年至1917年间，天津商会理结的商事纠纷共5157起).

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REPUBLICAN PERIOD: 1912–1949

2.30 The chambers of commerce continued their push for the introduction of a commercial code and, in the absence of that law, they wanted to be able to resolve commercial disputes outside of the court system.[18] The result appears to be that on 28 January 1913, the Beiyang Government (北洋政府)[19] established the Constitution of the Arbitration Court of Commerce and the Regulations of the Arbitration Court of the Chinese Republic (商事公断处章程) in the same year.[20] These Rules provided for disputes to be referred to the Business Arbitration Office for arbitration, but the awards were not binding and if a party did not agree with the result they could bring a lawsuit in the courts.[21] This limitation is no different to that set out above.

The chambers of commerce

2.31 The chambers embraced the new rules with the chambers of commerce in Guangzhou and Shanghai setting up arbitration offices in 1914. By the end of 1915, there were a total of 57 offices set up throughout China. The chambers of commerce continued to take cases and operate throughout this entire period (though the extent of caseload is not clear).[22] This is also subject to the vicissitudes of this period up to the founding of the People's Republic, namely an extended civil war and the war with the Japanese and the extensive economic turmoil that these conflicts caused.[23]

2.32 The chambers were important in terms of the development of arbitration because they were effectively the impetus for its continued development in China (rather than the government). The chambers were very much focused on the development of a workable arbitration system that would meet the significant gaps in the law and the courts at the time.[24] The government was however concerned to ensure that the chambers were not effectively usurping the judicial power of the State. This will be a theme for the periods discussed below, but in particular the

18 Ibid.

19 The Republican Government in Beijing (1912–1928).

20 Official Translation of The Regulations of the Arbitration Court of the Chinese Republic (promulgated by the Ministry of Justice and the Ministry of Agriculture and Commerce on 28 January 1913) (商事公断处章程) Chapter II (a copy on file with the author).

21 L Song, J Zhao and H Li 'Approaches to the Revision of 1994 Arbitration Act of the People's Republic of China' [2003] 20(2) Journal of International Arbitration 169.

22 Ibid.

23 It is important to note that in the Warlord Era (1916–1928), China was divided into fragmented spheres of power during which the Republican Government exercised very little control. As James Sheridan notes, '[in this period, t]here were literally hundreds of armed conflicts, short and long, on local, regional and national scales.' J Sheridan, 'The Warlord Era: Politics and Militarism under the Peking Government' in J Fairbank (ed) *The Cambridge History of China* (Vol 11, Cambridge University Press, 1983), 296, and for an illustration of the fragmented nature of power in China at the time, see the maps at 298–301.

24 Lubman (n 1) 31–32.

tension within some of the early reforms in arbitration post-1978 and, to an extent, the Arbitration Law itself.

Other reforms

2.33 There is nothing to indicate that there were significant developments in the area of arbitration that require separate mention, beyond the formalisation of arbitration and the role of the chambers as just described.[25]

THE PRC: 1949–1978

Overview

2.34 The founding of the People's Republic of China on 1 October 1949 represents a fundamental break with China's past, including the former legal systems of the Republic or Guomindang.[26] In terms of the history of arbitration, it is no less significant. The most fundamental point to appreciate is that the newly formed PRC with its Socialist economic, political and legal model was wholly inconsistent with established western forms of dispute resolution, including arbitration.

2.35 Arbitration was not high on the political or legislative agenda. China was dealing with various challenges in the period from 1949. The PRC was attempting in very practical and real terms to rebuild an economy and infrastructure that had been completely devastated by nearly 20 years of civil war and the war with the Japanese.

2.36 In the West, Europe had the Marshall Plan to assist with reconstruction.[27] In the East, China had to deal with reconstruction largely with the assistance of the Soviet Union. The link with the Soviet Union was deliberate (Chairman Mao's 'leaning to one side') and away from the United States.[28] This reliance continued to be the model for the next eight years. China was also dealing with the conflict in

25 Tao (n 1) 1. For completeness, Tao mentions the law for settling disputes between labour and management (1930) and the separate promulgation of the Tianjin Municipality Interim Rules of Organization for Mediation and Arbitration Commission (1949). These are unlikely to be the only legal rules issued throughout this period, although no exhaustive survey of all the rules appears to have been undertaken to date.

26 In February 1949, the Chinese Communist Party ('CCP') had issued an edict that abolished the Guomindang ('KMT') six codes, namely the Constitution, the Commercial Law, the Civil Law, the Law of Civil Procedure and the Criminal Code. The Common Program of the Chinese People's Consultative Conference issued then effectively became the basic law of China until 1954. Also see Chen (n 6) 34–36 on the ideological nature and administrative instruments for implementing the rejection of the Guomindang laws.

27 China was of course not as developed economically as Western Europe in 1949, even taking into account the devastation of the Second World War on Europe.

28 People's Daily (人民日报) dated 1 July 1949, available at <http://cpc.people.com.cn/GB/4162/64165/67447/67448/4554761.html>, accessed 5 September 2015, reporting Chairman Mao's speech in which he declared China would lean to one side on all things domestic and foreign.

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3.198 Items (1) and (2) are broad enough to include discussion of foreign arbitration in China. This is though largely speculative until the NPC replies with their study. Items (3), (4) and (5) identify the scope of the discussion in broad terms, but it is difficult to say with any precision what the scope of that discussion is. The time period for setting aside an arbitral award under the Arbitration Law is six months.

Development via the arbitration commissions

3.199 The main areas of development are being led by the Chinese arbitration commissions. This is discussed in more detail in Chapter 5, particularly in terms of interim remedies, and Chapter 8 but for the purposes of the present discussion it is important to observe that none of the areas referred to in this chapter and generally considered requiring reform, can be dealt with by the arbitration commissions.

3.200 These issues are entirely separate from adopting international practice and go to the legislative framework and ideological underpinnings of the Chinese arbitration system in the early 1990s, namely an arbitration system in which the government had a continued role and the Chinese arbitration commissions had a monopoly. These points are discussed in more detail in Chapter 2. It is submitted that these underlying policies would need to be abandoned or significantly modified before the arbitration market was opened up to foreign institution.

Shanghai FTZ

3.201 On 8 April 2015, the State Council published a circular to further accelerate the opening up of the Shanghai FTZ.[173] This circular states that the renowned international arbitration institutions are supported to enter and stay. There are no specific further measures mentioned, at the date of publication, but common sense dictates that any measures introduced to support foreign institutions entering China, would need to tackle the structural issues highlighted in paragraphs **3.153** to **3.163** above. It is not possible to say anything more meaningful at this stage, than to observe that this may be a potentially important area for development in terms of foreign arbitration institutions.

173 Scheme to Deepen the Opening Up and Reform with China (Shanghai) Pilot Free Trade Zone published on 8 April 2015 by the State Council to support the international noted dispute resolution institutions to enter (the China (Shanghai) Pilot Free Trade Zone). (进一步深化中国（上海）自由贸易试验区改革开放方案).

Chapter 4 The Arbitration Agreement

By Peter Yuen

Introduction

4.1 In PRC arbitration law (and in other jurisdictions around the world), the arbitration agreement forms the fundamental basis for a valid arbitration. It records the parties' agreement to arbitrate, how the parties will arbitrate, and is the fundamental source of the tribunal's jurisdiction to determine the dispute submitted to it.

4.2 China is unique among other jurisdictions in that its laws impose several requirements on the creation of a valid arbitration agreement that are not found in other jurisdictions, chief among these is the requirement in Article 16 of the Arbitration Law[1] to 'designate an arbitration commission' in the arbitration agreement. This requirement is in practice the subject of many challenges to arbitration agreements before the PRC courts. The PRC legal framework for arbitration is also unique in that it places limitations on party autonomy in respect of the right to choose '*ad hoc*' arbitration, the choice of seat, the choice of foreign arbitration institution and the choice of appointing authority for the chairman of the tribunal.

4.3 The focus of this chapter is primarily on the substantive Chinese law requirements for a valid arbitration agreement and sets out the circumstances in which it may be held to be invalid (for example, failure to comply with the requirement to designate the arbitration commission, lack of capacity to conclude the arbitration agreement and issues of arbitrability).

4.4 The aim of this chapter is to set out the requirements for not only a valid arbitration agreement, but also an effective arbitration agreement. This means an arbitration agreement that, irrespective of what may reasonably be argued as areas of uncertainty in academic and legal circles, is not at risk of challenge in the PRC courts for being invalid or open to challenge in the enforcement of award stage, and which actually delivers an effective and efficient arbitration.

4.5 Other than avoiding challenges, when drafting an arbitration agreement, parties will do well to think more practically about issues such as bilingual arbitration and whether they genuinely assist or hinder the arbitration process.

1 Arbitration Law of the People's Republic of China, 中华人民共和国仲裁法, adopted at the Ninth Meeting of the Standing Committee of the Eighth National People's Congress on 31 August 1994, promulgated by Order No 31 of the President of the People's Republic of China on 31 August 1994, and effective as of 1 September 1995, Article 16.

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The Legal Framework for Arbitration Agreements

4.6 The Arbitration Law is the main legislative text establishing the legal framework for arbitrations in China. Article 16 sets out the fundamental requirements for an arbitration agreement to be recognised as valid under Chinese law.

4.7 The Arbitration Law stipulates that where a valid arbitration agreement exists in relation to a dispute, parties are precluded from resorting to the courts for the determination of that same dispute.[2] Moreover, an arbitration agreement is also a prerequisite for an arbitration commission in China to accept a case.[3]

4.8 The Arbitration Law is not the only law that parties arbitrating in China need to be aware of. Various other laws impact the validity of the arbitration agreement concluded between the parties, for example the Civil Procedure Law, the Law on Foreign-Related Civil Relations (2011), the Contract Law, as well as SPC interpretations on various laws. To the extent that these laws affect the arbitration agreement, they will be discussed throughout this chapter. The legal framework itself is discussed in more detail in Chapter 3.

Who determines the validity and existence of an arbitration agreement?

4.9 In China, the arbitration commission and the PRC courts have jurisdiction to determine the validity and existence of the agreement,[4] whereas the tribunal is only entitled to rule on the issue if permitted to do so by the arbitration commission.[5]

2 Ibid Article 5 provides that the PRC courts must refuse to accept the case where a party institutes an action when a valid arbitration agreement exists.

3 Ibid Article 4 provides that if a party applies for arbitration where there is no agreement for arbitration, the arbitration commission or institution cannot accept the case.

4 Ibid Article 20. This is in contrast with the near universal position in the rest of the world, where national and institutional rules enshrine the principle that the tribunal is entitled to rule on the question of the validity of the arbitration agreement and therefore its own jurisdiction to hear the dispute pursuant to the arbitration agreement.

Note that the PRC courts have previously made a distinction between the determination of the validity and the determination of the existence of the arbitration agreement. However, this distinction is no longer made pursuant to the SPC Interpretation on Certain Issues Concerning the Application of the Arbitration Law, Fa Shi [2006] No 7 (最高人民法院关于适用《中华人民共和国仲裁法》若干问题的解释, 法释[2006]7号), Article 18: if an arbitration agreement is found to be invalid, then it is deemed not to exist. See J Tao, *Arbitration Law and Practice in China* (3rd edn, Kluwer, 2012) for a discussion at paras 196–199.

5 China International Economic and Trade Arbitration Commission (CIETAC) Arbitration Rules, 中国国际经济贸易仲裁委员会仲裁规则, revised and adopted on 4 November 2014 and effective as of 1 January 2015, Article6(1); Beijing Arbitration Commission ('BAC') Arbitration Rules, 北京仲裁委员会仲裁规则, revised and adopted at the Fourth Meeting of the Sixth Session of the Beijing Arbitration Commission on 9 July 2014, and effective as of 1 April 2015, Article 6(4).

4.10 If applying to the courts for a determination, parties may do so at the initial stages of the arbitration or during the arbitration proceedings. Parties may also challenge the validity and existence of the arbitration agreement after the award has been rendered in an application to set aside the award on the basis that 'there is no arbitration agreement'[6] or in an application for non-enforcement of the award,[7] provided however that such party first raised an objection as to its validity during the arbitration proceedings.[8]

4.11 The procedure for challenge at the court and with the arbitral commissions, including the timing of such challenges, is discussed in detail in Chapters 7 and 13.

Requirement to state an arbitration commission (Article 16)

4.12 The formal requirements for arbitration agreements are discussed below at paragraphs **4.19–4.34**. A particular issue which is unique to PRC law is the requirement that the arbitration agreement states the arbitration commission (仲裁委员会) selected by the parties.[9] Thus, the model clauses for the Chinese institutions such as CIETAC, the SHIAC and the BAC specifically refer to the arbitration commission in line with this requirement.[10]

4.13 Article 4 of the SPC Interpretation on Arbitration (2006) has helped to clarify how this requirement should be applied. While it confirms that an arbitration agreement that merely refers to the applicable arbitration rules (but not the arbitration institution) is invalid, it does provide an exception: where the arbitration institution can be determined from the reference to the relevant arbitration rules.

Applicable / governing law of the arbitration agreement

4.14 The law applicable to the arbitration agreement is discussed in Chapter 3 and also paragraphs **4.58–4.61** below.

6 Arbitration Law, Article 58(1). Note that the SPC Interpretation on Arbitration (2006), Article 18 clarifies that 'no arbitration agreement' means that 'the interested parties did not reach an arbitration agreement.' Article 18 also states that if the arbitration agreement is affirmed as invalid or is revoked, it shall be regarded that there is no arbitration agreement.

7 Civil Procedure Law of the PRC (Revised in 2012), Order No 59 of the PRC (中华人民共和国民事诉讼法（2012年修订）, 中华人民共和国主席令第59号), Article 274.

8 SPC Interpretation on Arbitration (2006), Article 27.

9 Arbitration Law, Article 16.

10 The CIETAC Model Clause provides that: 'Any dispute arising from or in connection with this Contract shall be submitted to China International Economic and Trade Arbitration Commission (CIETAC) for arbitration which shall be conducted in accordance with the CIETAC's arbitration rules in effect at the time of applying for arbitration. The arbitral award is final and binding upon both parties.' 'Model Arbitration Clause' (CIETAC), available at http://www.cietac.org/index/applicationForArbitration/47601fd59fcac97f001.cms, accessed 5 September 2015; The SHIAC Model Clause provides that: 'Any dispute arising from or in connection with this Contract shall be submitted to Shanghai International Economic and Trade Arbitration Commission/ Shanghai International Arbitration Centre for arbitration.' 'Model Arbitration Clauses' (SHIAC), available at <http://www.cietac-sh.org/English/Guide.aspx?tid=13>, accessed 5 September 2015.

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4.15 It is, however, important to briefly note here that parties to a foreign-related arbitration may choose the law applicable to their arbitration agreement. Failing such designation, the law of the place of arbitration or of the domicile of the arbitration institution will apply.[11] Where the parties have not stated the arbitration institution or the seat of arbitration or where these designations are not clear, the PRC courts will apply PRC law to the arbitration agreement.[12] Importantly, purely domestic arbitration agreements will always be governed by PRC law.

4.16 Parties to a foreign-related contract are advised to specify the law applicable to their arbitration agreement if they wish to avoid the courts or tribunal finding that PRC laws govern the validity of their arbitration agreement, particularly in light of the additional requirements that PRC law imposes for its validity. Such additional requirements are discussed below.

Types of Arbitration Agreements

4.17 Article 16 of the Arbitration Law states that arbitration agreements can include a clause in a contract or a separate independent arbitration 'submission' agreement concluded before or after a dispute arises.[13] In the first case, the clause will provide for future disputes between the parties to be arbitrated during the contract and possibly after the contract has been terminated. In the case of submission agreements, these tend to be concluded by parties after a particular dispute has arisen. The arbitration proceedings resulting from the submission agreement will cover that specific dispute only.

4.18 An arbitration agreement can also be incorporated into an agreement by referring to an arbitration agreement in another document.[14]

11 Law of the People's Republic of China on Application of Laws to Foreign-Related Civil Relations, [2011], Order No 36 of the President of the PRC (中华人民共和国涉外民事关系法律适用法, [2011] 中华人民共和国主席令第36号), Article 18 states: 'Parties concerned may agree upon the laws applicable to an arbitration agreement. Where the parties have made no such choice, laws of the domicile of the arbitration institution, or laws of the place of arbitration shall apply.' See para **4.36** below in respect of the concept of the 'seat' or place of arbitration in China.

12 Interpretation of the Supreme People's Court on Several Issues Concerning the Application of the Law of the People's Republic of China on Foreign-Related Civil Relations (I) Fa Shi [2012] No 24, (promulgated on 28 December 2012, Effective 7 January 2013) (最高人民法院关于适用《中华人民共和国涉外民事关系法律适用法》若干问题的解释（一）法释[2012]24号), Article 18 is supplemented by Article 14: 'Where the parties make no choice of law applicable to the foreign-related arbitration agreement, nor agreement on the arbitration institute or place of arbitration, or they make no explicit agreement thereon, the people's court may apply the laws of the People's Republic of China to determine the validity of such arbitration agreement.'

13 See Redfern and Hunter et al, *Redfern and Hunter on International Arbitration* (5th edn, Oxford University Press, 2009), paras 2.03 and 2.106–2.111 for further guidance on submission agreements (including the drafting of such agreements), subject however to the specific PRC requirements set out in this chapter.

14 SPC Interpretation on Arbitration (2006), Article 11.

The formal requirements of an arbitration agreement under the Arbitration Law

Requirements

4.19 In order to be enforceable under PRC laws, an arbitration agreement must comply with the requirements of Article 16 of the Arbitration Law, which provides that:

(1) the arbitration agreement must be in writing; and

(2) it must contain an expression of intention to apply for arbitration; and

(3) it must state the matters for arbitration; and

(4) it must designate an arbitration commission.

Must be in writing

4.20 Although the wording of Article 16 of the Arbitration law has been criticised for being too vague and ambiguous (for example, it does not take into account the possibility of electronic commerce),[15] the established position is that whatever form the arbitration agreement takes, it must be in writing, and this requirement applies to the contract that contains it.[16]

4.21 'Written form' is not defined in the Arbitration Law. The PRC courts have previously relied on Article 11 of the Contract Law[17] for a definition of what constitutes 'written form', which includes written documents, letters and electronic documents sent by email, fax, etc. In this way, the courts have extended Article 16 to electronic commerce.

4.22 In the SPC Interpretation on Arbitration (2006), the SPC provided a substantially similar definition of 'written form' at Article 1:

> Arbitration agreements in other written forms as stipulated in Article 16 of the Arbitration law shall comprise of the agreements on requesting for arbitration by means of contracts, letter or data message (including telegraph, telefax, fax, electronic data interchange and e-mail), etc.

15 C Manjiao, 'Is it Time for Change? A comparative Study of Chinese Arbitration Law and the 2006 Revision of the UNCITRAL Model Law on International Commercial Arbitration' (2009) 5(2) Asian International Arbitration Journal 142, 149.

16 See Tao (n 4), for a discussion at para 108. The abolished Economic Contract Law and Foreign Economic Contract Law, which preceded the Arbitration Law, previously expressly required commercial contracts to be in writing.

17 Contract Law of the People's Republic of China (1999) Order No 15 of the President of the PRC (中华人民共和国合同法主席令[1999]第15号), Article 11, which provides that 'written form' 'means any form which renders the information contained in a contract capable of being reproduced in tangible form such as a written agreement, a letter, or electronic text (including telegram, telex, facsimile, electronic data interchange and e-mail).'

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4.23 With the SPC Interpretation on Arbitration (2006), Chinese law is now consistent with international practice, and in particular the requirements of the New York Convention Article II (2)[18] and the 2006 Model Law Article 7 Option 1.[19]

4.24 In line with this Interpretation, the CIETAC Arbitration Rules, Article 5(2) provides that 'an arbitration agreement is in writing if it is contained in the tangible form of a document such as a contract, letter, telegram, telex, fax, electronic data interchange, or email.' The SHIAC Arbitration Rules, Article 5(3) and BAC Arbitration Rules, Article 4(2) have similar provisions, but the SCIA Arbitration Rules do not clarify what is considered to be in written form.

4.25 There is no specific requirement in Chinese law that the arbitration agreement needs to be separately signed.

Must contain an expression of intention to apply for arbitration

4.26 Article 16(1) of the Arbitration Law requires the parties to have jointly and freely elected arbitration and that such election be unambiguous.

4.27 A clause will therefore fail this requirement if:

(1) the arbitration agreement was procured by duress or coercion (this is supported by Article 17(3) which provides that duress is a ground for finding the arbitration agreement void);[20] or

18 The Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958) ('New York Convention'), Article II(2) states that the term 'agreement in writing' 'shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.' UNCITRAL later issued a Recommendation dated 7 July 2006 recommending that states should not consider the circumstances listed in Article II(2) to be exhaustive. See the Recommendation regarding the interpretation of Article II, para 2, and Article VII, para 1, of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards done in New York, 10 June 1958, adopted by the United Nations Commission on International Trade Law on 7 July 2006 at its thirty-ninth session' United Nations, *Treaty Series*, vol 330, No 4739, available at <https://www.uncitral.org/pdf/english/texts/arbitration/NY-conv/A2E.pdf >. This was in recognition of the development of modern communications, which are changing the way that contracts are executed, and the fact that many jurisdictions have adopted more liberal approaches to the writing requirement, including for example, recognising that an arbitration agreement contained in an exchange of letters, emails etc. will meet the writing requirement. See K Fan, *Arbitration in China. A Legal and Cultural Analysis* (Hart Publishing, 2013) 36.

19 The UNCITRAL Model Law on International Commercial Arbitration (2006), Chapter II, Option 1 Article 7 reflects the latest standard for the written requirement: the arbitration agreement is in writing if its content is recorded in any form, whether or not the arbitration agreement or contract has been concluded orally, by conduct, or by other means. Option II Article 7 is more progressive in that it envisages the written form requirement to be removed. See also Manjiao (n 15) 148.

20 According to Article 69 of the Opinions of the Supreme People's Court on Several Issues concerning the Implementation of the General Principles of the Civil Law of the People's Republic of China (Trial Implementation) Fa Ban Fa [1988] No 6 (最高人民法院关于贯彻执行《中华人民共和国民法通则》若干问题的意见（试行）(法(办)发[1988]6号)), it is deemed an act of duress if a party forces another party to make an expression of intention contrary to his true will by threatening harm to *inter alia* the life, health, honour, reputation, or

(2) the intention is unclear and ambiguous. For example, a split clause providing both for arbitration and litigation in the courts will fail this requirement.[21]

Must contain the matters to be referred to arbitration

4.28 Article 16 of the Arbitration Law further requires the arbitration agreement to state the matters to be referred to arbitration. It is of course common for parties to adopt broad wording in their arbitration agreements, which is intended to ensure that a wide range of future disputes will be captured within the agreement to arbitrate. Thus, wording such as 'any disputes arising out of or in connection with the contract', 'any dispute, controversy, difference or claim arising out of or relating to this contract, including the existence, validity, interpretation, performance, breach or termination thereof or any dispute regarding non-contractual obligations arising out of or relating to it', are often found in the model clauses of various arbitration institutions.[22]

4.29 Article 2 of the SPC Interpretation on Arbitration (2006) provides that:

> Where the parties concerned agree that matters to be arbitrated are contractual disputes, the disputes arising out of the formation, effectiveness, modification, assignment, performance, liabilities for breach, interpretation, rescission and etc. of the contract may all be ascertained as matters to be arbitrated.

4.30 This means that if the parties agree in the arbitration agreement that contractual disputes are to be referred to arbitration, it is presumed that this will include any disputes as to the formation, validity, modification, transfer, performance, liabilities for breach, interpretation, and rescission of the contract.[23]

4.31 Notwithstanding Article 2, it is recommended that parties expressly adopt broad wording as suggested above rather than merely stating that 'contractual disputes' will be referred to arbitration and relying on the courts applying Article 2.

4.32 However, even if the dispute that eventually arises is captured by the arbitration agreement, whether the dispute can in fact be arbitrated is a question of arbitrability.[24] Paragraphs **4.108–4.143** below deal with what matters can be referred to arbitration under PRC law. An arbitration agreement which provides for arbitration in relation to matters that are not arbitrable under PRC law is invalid in mainland China.[25]

Must designate a (Chinese) arbitration commission

4.33 Article 16 is reinforced by Article 18 of the Arbitration Law, which provides that an arbitration agreement is void if it contains no or unclear provisions

property of a citizen or his relatives, or threatening harm to the honour, reputation, or property of a legal person.

21 SPC Interpretation on Arbitration (2006), Article 7 and paras **4.87–4.89** below.

22 See the model clauses of CIETAC, ICC and HKIAC.

23 A Ma, B Miao, H Shi, 'Chapter 3: The Law and Practice of International Arbitration in the People's Republic of China', in M Moser and J Choong (eds.), *Asia Arbitration Handbook* (Oxford, 2011) 197, para 3.86.

24 Arbitration Law, Article 17(1).

25 Ibid Article 3 and Article 17(1).

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regarding the arbitration commission, unless the parties can reach a supplementary agreement. The requirement that the arbitration agreement designates an arbitration commission is, as a consequence of these provisions, interpreted as a compulsory requirement that is in practice strictly enforced by the PRC courts and the frequent subject of dispute between the parties. Issues that may arise in relation to this requirement are discussed below at paragraphs **4.64–4.91**, in particular, Article 16 has traditionally been interpreted to mean that a Chinese (not foreign) arbitration commission must be designated by the parties.[26]

4.34 Notably, these provisions are relevant to whether arbitration agreements designating foreign arbitration institutions or specifying *ad hoc* arbitration are valid in light of the requirement to designate an arbitration commission. These issues are also discussed in Chapter 3 and paragraphs **4.78–4.84** below.

Other key elements of the arbitration agreement

4.35 In addition to the formal requirements under the Arbitration Law set out above, parties will generally be advised to consider specifying the following key elements in their arbitration agreements.

Seat or place of arbitration

4.36 Before discussing the law limiting parties' ability to select the seat of arbitration, it is worth mentioning that PRC courts are not always consistent in their understanding of the concept of the 'seat of arbitration'. This is in part due to the classifications in the Arbitration Law and the Civil Procedure Law, which distinguish between domestic and foreign-related arbitrations,[27] and do not take into account the concept of the 'seat'.[28]

4.37 Chinese arbitration institutions will often use the term 'place of arbitration' instead of the 'seat of arbitration' to designate the jurisdiction whose laws will govern the arbitration proceedings.[29] In 2005, the CIETAC Rules became the first

26 See Fan (n 18) 38 for a discussion.
27 The distinction between 'domestic' and 'foreign-related' arbitration is discussed in Chapter 3.
28 See, for e.g., the Civil Procedure Law, Article 283 which provides that 'if an award rendered by foreign arbitration institutions needs the recognition and enforcement of a People's Court of the PRC, the party shall directly apply to the Intermediate People's Court located in the place where the party subject to the enforcement has its domicile or where its property is located. The Peoples' Court shall deal with the matter according to the relevant provisions of the international treaties concluded or acceded to by the PRC or on the principle of reciprocity.' This provision therefore appears to require awards rendered under the auspices of a foreign arbitration institution, regardless of where the arbitration is seated (for example, an ICC award rendered in China), to be enforced in accordance with international treaties, rather than in accordance with the Arbitration Law and the Civil Procedure Law if the seat is China. This contradicts the terms under which China has acceded to the New York Convention. China, through its 'reciprocity' reservation, has only agreed that the Convention is applicable to awards made 'within the territory of another contracting state'. (See also Fan (n 18) 50. This has led to some problems in the enforcement of Chinese awards rendered under the auspices of a foreign arbitration institution, discussed below at paras **4.81–4.84**).
29 For example the CIETAC Arbitration Rules, Article 7.

Chinese rules to recognise the concept of the seat of arbitration as distinct from the place where the proceedings are held, when the rules provided that parties may choose the place of arbitration, and that the 'award shall be deemed as being made at the place of arbitration.'[30] This was seen as a positive step forward for Chinese arbitration, not least because it explicitly allows CIETAC to administer arbitrations seated outside China.[31]

4.38 Since then, the SCIA, SHIAC and BAC Arbitration Rules have adopted the same or similar provisions, with the BAC Arbitration Rules taking the most progressive approach out of the Chinese arbitration rules with its use of the term 'seat' of arbitration at Article 26.[32] However, it appears that for the moment, the explicit recognition of the concept of the seat of arbitration in the Chinese institutional rules has not yet led to any corresponding changes in the legislation or in the courts' decisions.

4.39 It is important to understand that currently Chinese law imposes a significant limitation on parties' right to choose the place/seat of arbitration.[33] Article 128 of the Contract Law provides that parties can only choose a foreign arbitration institution (and by implication, a foreign seat) if their dispute is 'foreign-related'.[34] Parties to a domestic dispute must choose a Chinese arbitration commission in China (and by implication, a Chinese seat).

4.40 Parties from other jurisdictions will need to appreciate that this rule may in practice be problematic for them due to the strict definition of what constitutes a 'foreign-related' arbitration. As mentioned in Chapter 3, 'foreign-related' arbitrations generally only include arbitrations that involve a non-PRC citizen or a non-PRC company. A PRC company that is wholly or partly owned by foreign companies (known as a foreign invested enterprise or FIE) is considered to be a PRC company.[35] Disputes between foreign invested enterprises and a PRC party will be considered domestic disputes.[36]

4.41 If, contrary to Article 128 of the Contract Law, parties to a purely 'domestic dispute' choose a foreign arbitration institution or a foreign seat, they will not be able to enforce the resultant award in mainland China.

30 See Tao (n 4) para 229 and K Fan, 'Prospects of Foreign Arbitration Institutions Administering Arbitration in China', Journal of International Arbitration 350.
31 Ibid.
32 Compare to the SCIA Arbitration Rules, Article 4 and the SHIAC Arbitration Rules, Article 7.
33 G Johnston, 'Party Autonomy in Mainland Chinese Commercial Arbitration', (2008) 25(5) *Journal of International Arbitration* 537.
34 '... The parties to a foreign-related contract may, according to the arbitration agreement, apply to a Chinese arbitration institution or *any other arbitration institution for arbitration* ...' (emphasis added).
35 See Chapter 3 for what constitutes 'foreign-related arbitration'. See Johnston (n 33) 539 for recommendations for reform or liberalisation.
36 For an explanation on how domestic disputes and foreign-related disputes are treated, see Chapter 3.

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CHAPTER 11 CHINA-RELATED INVESTMENT ARBITRATION

By Professor FAN Kun

INTRODUCTION

11.1 There has been a burgeoning number of Bilateral Investment Treaties ('BITs') and investment chapters incorporated into bilateral and regional Free Trade Agreements ('FTAs') in China. This chapter explains the policy and practice of China-related investment arbitration. On the basis of an overview of the general trend and patterns of legal framework for investment arbitration and the Washington Convention, this chapter critically assesses the investment policy and practice in China and its track record in investment treaty claims. It analyses the investment policy in its historical timelines, in order to identify the evolution of the policy and investment treaty practices over time. It also addresses the controversial issue on the application of the China BITs to the Hong Kong SAR and the Macau SAR.

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THE INTERNATIONAL LEGAL FRAMEWORK FOR INVESTMENT ARBITRATION

Overview

11.2 In light of the shortcomings of the recourse by national court[1] and diplomatic protection,[2] international arbitration provides an attractive alternative to the settlement of investment disputes. It provides a framework within which foreign investors could refer a dispute with a state party directly to a neutral arbitral tribunal. However, due to the divided opinions between the capital exporting and importing states, many attempts to establish a multilateral legal framework for

1 The courts of the host state are often not seen as sufficiently impartial in this type of situation. In addition, domestic courts are bound to apply domestic law even if that law should fail to protect the investor's rights under international law. Domestic courts of other states are usually not a realistic alternative. In most cases, they will lack territorial jurisdiction over investment operations taking place in another country. Even if a host State were to agree to a choice of forum clause pointing to the courts of the investor's home state or of a third state, sovereign immunity or other judicial doctrines will usually make such proceedings impossible.

2 The availability of diplomatic protection depends on the nationality of the investor, whether the local remedies are exhausted and the discretion of the espousing state.

investment treatment initiated by states and non-governmental organisations all ended up in failures.[3]

11.3 The result is that the current international legal framework governing foreign investment consists of a vast network of national and international rules and principles, of diverse form and origin. The entire structure rests on the twin foundations of customary international law and national laws and regulations. For its concrete substantive content, it relies primarily on a multitude of international agreements addressing investment issues—interntional investment agreements ('IIAs') for short.[4] This fragmentation of IIAs is sometimes described as a 'spaghetti bowl'.[5]

11.4 Countries' efforts to attract FDI and benefit from it increasingly take place in an environment characterised by a proliferation of investment rules at the bilateral, regional and multilateral levels. They are said to be 'the most effective means for developing and applying international norms, with respect to FDI as in other areas'.[6]

Multilateral agreements

11.5 Multilateral agreements, especially those of worldwide scope, are the closest equivalent to 'legislation' that exists in international law. Some multilateral agreements deal with broad issues that are important for FDI, as in the case of the Articles of Agreement of the International Monetary Fund, the GATT, or the international conventions concerning intellectual property, within the framework of the WIPO or the WTO. Other multilateral agreements, although not dealing with the FDI process in its entirety, address important aspects of it. For instance, the 1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States ('Washington Convention') provides a comprehensive framework for the settlement of disputes. It is complemented by other institutions dealing in particular with international commercial arbitration.[7]

11.6 Regional agreements are agreements in which only a limited number of countries participate and which are often not open to the participation of all countries.[8] These include The North American Free Trade Agreement ('NAFTA'), the Energy Charter Treaty ('ECT') and the ASEAN Agreement for the Promotion

3 A Newcombe and L Paradell, *Law and Practice of Investment Treaties: Standards of Treatment*, (Kluwer Law International, Hague, 2009), paras 1.9–1.16.
4 UNCTAD, 'Trends in International Investment Agreements: An Overview' (1999) UNCTAD/ITE/IIT/13.
5 J Karl, 'The "Spaghetti Bowl" of IIAs: The End of History?', Columbia FDI Perspectives, Perspectives on Topical Foreign Direct Investment Issues by the Vale Columbia Center on Sustainable International Investment, No 115, 17 February 2014.
6 UNCTAD (n 4) 40.
7 Ibid 40–42.
8 Ibid 42–44.

and Protection of Investments. In 2014, the ECT surpassed the NAFTA as the most frequently invoked IIA.[9]

Bilateral Investment Treaties

11.7 Bilateral Investment Treaties ('BITs') are a principal element of the current framework of FDI. It is estimated that over 2900 such BITs have been concluded worldwide.[10] Their principal focus has been 'from the very start on investment protection, in the wider context of policies that favour and promote FDI: the protection of investments against nationalization or expropriation and assurances on the free transfer of funds and provision for dispute-settlement mechanisms between investors and host States'.[11]

11.8 The resulting BITs, numerous FTAs with investment components and multilateral investment agreements are multi-layered and multi-faceted, with obligations differing in geographical scope and coverage. They constitute an intricate web of commitments that partly overlap and partly supplement one another.[12]

11.9 According to the United Nations Conference on Trade and Development ('UNCTAD'), 'the year 2014 saw the conclusion of 27 IIAs, that is one every other week'.[13] This brings the total number of IIAs to 3,268. The UNCTAD report further reveals that 'investors continue to use the investor–state dispute settlement ('ISDS') mechanism. In 2014, claimants initiated 42 known treaty-based ISDS cases. With 40 per cent of new cases initiated against developed countries, the relative share of cases against developed countries has been on the rise (compared to the historical average of 28 per cent)'.[14] Fifty-seven new cases were initiated in 2013, just below the record number of new claims recorded in 2012. The total number of known treaty-based cases reached 568.[15]

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9 UNCTAD, 'Recent Trends in IIAs and ISDS' (Expert Meeting on The Transformation of the International Investment Agreement Regime) (2015) , available at <http://unctad.org/en/PublicationsLibrary/webdiaepcb2015d1_en.pdf>, accessed 27 May 2015.
10 The data is based on the information provided on International Investment Agreements Navigators, UNCTAD, 'International Investment Agreements Navigators', available at <http://investmentpolicyhub.unctad.org/IIA>, accessed 27 May 2015.
11 UNCTAD (n 4) 44.
12 UNCTAD 'International Investment Agreements: Key Issues' (2004) UNCTAD/ITE/IIT/2004/10 (Vol I).
13 UNCTAD 'Recent Trends in IIAs and ISDS' (2015) UNCTAD/WEB/DIAE/PCB/2015/1 (n 9).
14 Ibid.
15 UNCTAD, 'Recent Developments in ISDS' (2014), available at <http://unctad.org/en/PublicationsLibrary/webdiaepcb2014d3_en.pdf>, accessed 27 May 2015.

ICSID and the Washington Convention

Framework and requirements

11.10 The Washington Convention is designed to facilitate private international investment through the creation of a favourable investment climate.[16] By virtue of the Washington Convention, international law could now be applied diretly to the relationship between the investor and the host state. The Washington Convention entered into force on 14 October 1966, after ratification by the first 20 states. Of the early participating states, most were developing countries notably in Africa. As of 31 December 2014, ICSID had 159 signatory states, and 150 contracting states had ratified the Convention.[17] China is a member of the Washington Convention. The Standing Committee of the National People's Congress issued a decision to ratify the Washington Convention on 1 July 1992, which became effective in China as of 6 February 1993.

11.11 The ICSID was established under the Washington Convention in 1966. It is now the world's leading institution devoted to international investment dispute settlement. The ICSID process is designed to take account of the special characteristics of international investment disputes and the parties involved, maintaining a careful balance between the interests of investors and host states.[18] The first ICSID case was not decided until 1974. This situation has since changed, especially in the 1990s, when there was a dramatic increase in the number of registered cases.[19] As of 31 December 2014, ICSID had registered 497 cases under the Washington Convention and Additional Facility Rules.[20]

Limitations on jurisdiction

11.12 Article 25(1) of the Washington Convention provides the conditions for the ICSID's jurisdiction:[21]

> The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that

16 The Preamble to the Convention provides that 'considering the need for international cooperation for economic development, and the role of private international investment therein […]'.

17 ICSID Convention (entered into force 14 October 1966), available at <https://icsid.worldbank.org/apps/ICSIDWEB/icsiddocs/Pages/ICSID-Convention.aspx>. For background information about the ICSID, see <https://icsid.worldbank.org/apps/ICSIDWEB/about/Documents/ICSID%20Fact%20Sheet%20-%20ENGLISH.pdf>, accessed 6 May 2015.

18 ICSID, 'About ICSID', available at https://icsid.worldbank.org/apps/ICSIDWEB/about/Pages/default.aspx, accessed 6 May 2015.

19 See UNCTAD, 'Course on Dispute Settlement: 2.1 Overview' (2003) UNCTAD/EDM/Misc.232, available at <http://unctad.org/en/Docs/edmmisc232overview_en.pdf>, accessed 6 May 2015).

20 ICSID, 'The ICSID Caseload – Statistics (Issue 2015-1)', available at <https://icsid.worldbank.org/apps/ICSIDWEB/resources/Documents/ICSID%20Web%20Stats%202015-1%20(English)%20(2)_Redacted.pdf>, accessed 6 May 2015.

21 ICSID Convention, Article 25(1).

> State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre.

11.13 Accordingly, to establish jurisdiction before the ICSID, the following three conditions discussed below must be met.

Jurisdiction *ratione materiae* or subject-matter jurisdiction

11.14 This condition has three components:

(1) the requirement of a legal dispute;
(2) the requirement that the legal dispute arise directly out of the underlying transaction; and
(3) that such underlying transaction qualifies as an investment.

11.15 The Washington Convention does not provide a *priori* definition of 'investment', which is left open for countries to work out and thereby preserve the integrity and flexibility in the progressive development of the term.[22]

Jurisdiction *ratione personae* or personal jurisdiction

11.16 The dispute must be between a contracting state (or any constituent subdivision or agency of a contracting state designated to the centre by that state) and a national of another contracting state.

Consent

11.17 Arbitration is always based on an agreement between the parties. In the case of the ICSID, there must be an agreement to arbitrate between the host state and the foreign investor. The accession to the Washinton Convention is not of itself consent to the jurisdiction of the ICSID.[23] Rather, the host state may make a general offer to foreign investors or to certain categories of foreign investors to submit to arbitration. This offer may be contained in legislation or in a treaty to which the host state is a party. To perfect a consent agreement, the investor has to accept this offer in writing or through the act of instituting proceedings.[24]

11.18 When China ratified the ICSID Convention on 7 January 1993, it made the reservation under Article 25(4) of the ICSID Convention that '[t]he Chinese government would only consider submitting to the jurisdiction of the [ICSID] disputes over compensation resulting from expropriation and nationalization.'[25]

22 *Mihaly International Corporation v The Democratic Socialist Republic of Sri Lanka* (2002) 41 ILM 867, para 33 (ICSID).

23 Author's Preface, in C H Schreuer, *The ICSID Convention: A Commentary XVII* (Cambridge University Press, 2001), paras 25–244 at 192.

24 See, for instance, C Schreuer, 'Jurisdiciton and Applicable Law in Investment Treaty Arbitration', (2014) 1(1) McGill Journal of Dispute Resolution, 2.

25 China's statement under Article 25(4) of the ICSID Convention is available on the ICSID's website, <https://icsid.worldbank.org/ICSID/FrontServlet>, accessed 21 May 2013.

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China's Engagement with the Framework and the Rise of its Investment Related Arbitration

Overview

11.19 China has entered into three types of treaties for the promotion and protection of foreign investment: bilateral investment treaties (BITs), multilateral treaties and Free Trade Agreements (FTAs). China negotiated its first BIT with Sweden in 1982 and since then has concluded a total of 130 BITs by May 2015 (with 108 BITs in force).[26] With a notable exception of the United States,[27] China has BITs with almost all of its important economic partners, including with capital-exporting countries such as Germany, France, the United Kingdom, Japan, and more recently with Canada,[28] as well as with a large number of developing economies in Asia, Africa, Eastern Europe and Latin America. It is still very active in entering into new treaties and renegotiating existing ones. The tendency of Chinese IIAs has evolved significantly over time.[29] The growing number of BITs and the policy shift from a restrictive to a liberal approach is consistent with

26 The data is based on the information provided on International Investment Agreements Navigators, UNCTAD, available at <http://investmentpolicyhub.unctad.org/IIA>, accessed 28 May 2015. For a list of these BITs, see <http://investmentpolicyhub.unctad.org/IIA/CountryBits/42>, accessed 28 May 2015.

27 China and the United States declared the launch of BIT negotiations at the conclusion of the fourth China–US Strategic Economic Dialogue on 18 June 2008. During the Obama administration, the US-China BIT talks were put on hold while the United States revised the terms of the US model BIT. US-China BIT negotiations resumed in 2013; the 17th round of negotiations was held in December 2014. For a discussion, see generally, Peterson Institute for International Economics, 'Towards a US-China Investment Treaty', February 2015; Gongyan Cai, 'China–US BIT Negotiations and the Future of Investment Treaty Regime: A Grand Bilateral Bargain with Multilateral Implications' (2009) 12 Journal of International Economic Law; Qingjiang Kong, 'U.S.-China Bilateral Investment Treaty Negotiations: Context, Focus, and Implications' (2012) 7 Asian Journal of WTO & International Health Law and Policy; Karl Sauvant and Huiping Chen, 'A China–US bilateral investment treaty: A template for a multilateral framework for investment?' (2012) Columbia FDI Perspectives, No 85.

28 On 9 September 2012, Canada and China signed a BIT known in Canada as a Foreign Investment Promotion and Protection Agreement ('FIPA'). For a discussion, see J Saulino, 'The Canada-China Investment Treaty—Lessons for a U.S.–China BIT?' (2012) 9 Transnational Dispute Management.

29 For a discussion on the different generations of Chinese IIAs, see E Dulac, 'The Emerging Third Generation of Chinese Investment Treaties' (2010) 7(4) Transnational Dispute Management; G Kong, 'Bilateral Investment Treaties: the Chinese approach and Practice' (2003) 8 Asian Yearbook of International Law; K Rooney, 'ICSID and BIT Arbitrations and China' (2007) 24 Journal of International Arbitration 689; S Schill, 'Tearing down the Great Wall: the New Generation Investment Treaties of the People's Republic of China' (2007) 15 Cardozo Journal of International and Comparative Law 73; A Berger, 'China and the Global Governance of Foreign Direct Investment: The Emerging Liberal Bilateral Investment Treaty Approach' (2008) German Development Institute Discussion Paper 10/2008, available at <http://www.die-gdi.de/uploads/media/DP_10.2008.pdf>, accessed 27 May 2015.

China's recent development from a capital-importing country to an increasingly important exporter of FDI, notably to developing countries in Asia and Africa.[30]

11.20 With the significant increase of both FDI inflow and outflow in the past few years, China's investment policy today has characteristics of both a capital-importing and capital-exporting country. By and large, we can divide the Chinese IIAs into the following three stages of development discussed below.

Chinese policy 1978–1998: first generation of Chinese IIAs

11.21 China's law reform program began in late 1978 when the third Plenum of the 11th Central Committee of the Chinese Communist Party was convened. The Plenum reflected a tentative policy consensus about the need to reform the state-planned economy and build a legal system that would support economic growth. The new leadership took a pragmatic view and decided to implement a 'socialist system with Chinese characteristics' in China. In line with the 'reform and opening-up' policy, China's attitude towards foreign investments began to change, with a view to attract foreign investment.

11.22 As China was predominately a capital-importer at the time, its earlier BITs mainly targeted capital exporting states. In 1982, China signed its first BIT with Sweden; in 1983, China signed a BIT with Germany; in 1984, with France, with Belgium and Luxemburg, with Finland, with Norway. From 1985, however, Chinese BITs became diversified. China continued to enter into BITs with other developed states (in 1985 China signed BITs with Italy, with Denmark, with the Netherlands, with Austria; in 1986, with the United Kingdom and Switzerland), and started to sign BITs with developing countries (China's first BIT with a developing country was entered into with Thailand in 1985, followed by Kuwait in the same year, Sri Lanka in 1986, Malaysia in 1988 and Pakistan in 1989). Approximately 71 BITs were concluded during this period.[31]

11.23 However, in the first generation of IIAs, China opted for limited investment protection and narrowly defined investor-state arbitration clauses. This conservative approach in the first generation IIAs was reflected in the first and the second Chinese Model BITs. China's first Model BIT was formulated in around 1984, after the China-France BIT was signed.[32] It incorporated the basic provisions contained in BITs, such as definitions of investment and investors, FET, MFN, expropriation and compensation, compensation for damages and

30 For a discussion of China's emerging role as a capital exporter, see generally K Cai, 'Outward Foreign Investment: A Novel Dimension of China's Integration into the Regional and Global Economy' (1999) 160 China Quarterly 856; C Cai, 'Outward Foreign Direct Investment Protection and the Effectiveness of Chinese BIT Practice' (2006) 7 Journal of World Investment & Trade 621.

31 UNCTAD (n 26).

32 Directorate-General of Treaty and Law Ministry of Commerce of PRC, 'Bilateral Investment Treaty', available at http://tfs.mofcom.gov.cn/article/Nocategory/201111/20111107819474.shtml, accessed 29 May 2015; N Gallagher and W Shan, *Chinese Investment Treaties: Policies and Practice* (Oxford University Press, Oxford, 2009) 421–25.

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losses, etc. However, it did not include a National Treatment ('NT') provision, even though NT is 'one of the core guarantees regularly endorsed in international BIT practice'.[33]

11.24 In terms of dispute resolution, the First Model BIT stipulated that a dispute involving the amount of compensation for expropriation, if it cannot be settled within six months after resort to negotiations, can be submitted to an ad hoc arbitral tribunal; and for other disputes, if it cannot be settled within six months after resort to negotiations, shall be submitted to the competent court of the contracting party.[34] Since around 1989, the Second Model BIT was adopted by the State Council.[35] It retained the main framework of the First Model BIT, but included a qualified NT provisionand an umbrella clause.[36] In terms of the compensation for expropriation, it also included the concept of 'market value' and elements of evaluation.

11.25 In line with the principles in the first two Chinese Model BITs, the vast majority of the first generation Chinese IIAs did not include NT. In the few first generation BITs that contain a NT provision, it is often limited. For instance, the China–UK BIT (1986) provides that:

> ... either Contracting Party shall *to the extent possible*, accord *treatment in accordance with the stipulations of its laws and regulations* to the investment of nationals or companies of other Contracting Party the same treatment that accorded to its own nationals or companies.[37] (emphasis added)

11.26 The limitation of the obligation to accord NT 'to the extent possible' and the reference to domestic law has significantly undermined the effectiveness of the NT guarantee.[38] In the China–Japan BIT (1988), limitation was imposed on the scope of the NT provision by the treaty's Additional Protocol. Article 3 of the Protocol provides that with respect to NT:

> ... it shall not be deemed treatment less favourable for either Contracting Party to accord discriminatory treatment, *in accordance with its laws and regulations*, to national and companies of the other Contracting Party, *in case it is really necessary for the reason of public order, national security or sound development of national economy*.[39] (emphasis added)

33 Schill (n 29) 94.
34 Article 9 of the Chinese Model BIT Version I.
35 Directorate-General of Treaty and Law (n 32); Gallagher and Shan (n 32).
36 An umbrella clause seeks to ensure that each party to the treaty will respect undertakings towards nationals of the other party. Recent jurisprudence has given greater weight to the view that the umbrella clauses can elevate breaches of contract into breaches of international law.
37 Agreement Between the Government of the People's Republic of China and the Government of the United Kingdom of Great Britain and Northern Ireland Concerning the Promotion and Reciprocal Protection of Investments (signed 15 May 1986, entered into force 15 May 1986), Article 3(3).
38 Schill (n 29) 95.
39 Agreement Between the People's Republic of China and Japan Concerning the Encouragement And Reciprocal Protection of Investment (signed 27 August 1988, entered into force 14 May 1989), Article 3.

11.27 The reference to domestic law and exceptions for 'public order, national security or sound development of national economy' allows the host state to differentiate in its laws between domestic and foreign investors.[40] Scholars argued that China's reluctance to provide for NT derive from 'China's desire to protect the privileges of its state-owned enterprises',[41] and 'the need to create a system that allows for foreign investment while at the same time upholding structures of a socialist planning economy'.[42]

11.28 In terms of dispute resolution, the first generation Chinese BITs either did not contain investor-state arbitration clauses at all,[43] or contained a narrowly defined arbitration clause—limited to 'disputes concerning the amount of compensation for expropriation'.[44] For instance, the China–UK BIT (1986) provides that:

> ... a dispute between a national or company of one Contracting Party and the other Contracting Party *concerning an amount of compensation* which has not been amicably settled after a period of 6 months from written notification of that dispute shall be submitted to international arbitration ... .[45] (emphasis added)

11.29 The China–Japan BIT concluded in 1988 also provides for arbitration with a narrow scope, limited to the dispute concerning the amount of compensation, and only allows other matters to be submitted for arbitration if the parties to the disputes so agree.[46] In reality, however, after a dispute arises, it will be very difficult to obtain the consent from the host state to submit the matter to arbitration.

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40 Schill (n 29) 96; Dulac (n 29) 16.
41 Dulac (n 29) 16.
42 Schill (n 29) 96.
43 Agreement Between The Government Of The People's Republic Of China and the Government Of the Kingdom Of Thailand For the Promotion and Protection Of Investments (signed 12 March 1985, entered into force 13 December 1985).
44 See e.g. China–UK (n 37); China-Japan (n 39); Agreement Between The People's Republic of China and the Republic of Turkey Concerning the Reciprocal Promotion and Protection of Investments (signed 13 November 1990, entered into force 19 August 1994); Agreement Between the Government of the People's Republic of China and the Government of the Socialist Republic of Vietnam Concerning the Encouragement and Reciprocal Protection of Investments (signed 2 December 1992, entered into force 1 September 1993); Agreement Between the Government of the People's Republic of China and the Government of the Argentine Republic on the Promotion and Reciprocal Protection of Investments (signed 5 November 1992, entered into force 1 August 1994).
45 China–UK (n 37), Article 1.
46 China-Japan (n 39), Article 11, which provides:
(1) Any dispute between an a national or company of either Contracting Party and the other Contracting Party with respect to investment within the territory of the latter Contracting Party shall, as far as possible, be settled amicably through consultation between the parties to the dispute.
(2) If the dispute *concerning the amount of compensation referred to in para 3 of Article 5 [protection of investments and returns]* between a national or company and the other Contracting Party, charged with the obligation for making compensation under its laws and regulations, cannot be settled through negotiations within six months from the date either party requested consultation for the settlement, such dispute *shall*, at the request of such national or company, be submitted to a conciliation board or an arbitration, to be established reference to the Washington Convention. *Any dispute concerning other matters* between a national or company of either Contracting Party and the other Contracting Party *may* be submitted by mutual agreement to the Centre *if the parties to the disputes so agree*, to a conciliation board or an arbitration board as stated above. In the event that such national or company has resorted