

# Client Alert

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## Guangdong DOJ Wades Into the Fray by Demanding That CIETAC Cease “Illegal Arbitration Activities” in Guangdong

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### INTRODUCTION

On July 15, 2015, the PRC Supreme People’s Court (**SPC**) issued an interpretation clarifying various jurisdictional issues arising from the mid-2012 decision of the former South China and Shanghai Sub-Commissions of the China International Economic and Trade Arbitration Commission (**CIETAC**) to become independent arbitration commissions.<sup>1</sup> Commentators had hoped that the SPC’s interpretation had put to rest many of the thorny jurisdictional issues arising from the CIETAC split. In August 2015, however, the Guangdong Provincial Department of Justice (the “**Guangdong DOJ**”) issued a letter to CIETAC demanding that it immediately cease the “illegal arbitration activities” of its newly formed sub-commission in Guangdong under the names of “CIETAC South China Sub-Commission” and “CIETAC Shenzhen Branch.” CIETAC has denied that it is operating illegally in Guangdong and has asserted that its sub-commission is merely acting on its behalf. This development adds yet another twist to the long-running disputes and uncertainties flowing from the CIETAC split.

### BACKGROUND TO THE CIETAC SPLIT

Today, there are more than 200 arbitration commissions in China, which administer over one hundred thousand cases every year. PRC law requires that PRC-seated arbitrations be administered by registered PRC arbitration commissions and does not recognize *ad hoc* arbitration. Article 3 of the Interim Measures for Registration of Arbitration Commissions stipulates that the establishment of an arbitration commission must be registered with the government authority responsible for registration; if the establishment of an arbitration commission is not registered, any arbitral awards rendered by such commission shall not be legally binding. Article 10 of the PRC Arbitration Law provides that registration of arbitration institutions is the responsibility of judicial administration offices at the provincial, autonomous regional or directly administered municipal level.

CIETAC was one of the first arbitration commissions to be established in China in the late 1950s. Today, CIETAC is the most well-established and commonly used arbitration commission in the PRC. CIETAC is headquartered in Beijing. By 2012, CIETAC had established numerous sub-commissions throughout China, including the South China Sub-Commission in Shenzhen, the Shanghai Sub-Commission, the Tianjin Sub-Commission and the Southwest Sub-Commission in Chongqing.<sup>2</sup>

<sup>1</sup> Morrison & Foerster Client Alert, *SPC Issues Interpretation on Jurisdictional Issues Arising from CIETAC Split* (Aug. 4, 2015), <http://www.mofo.com/-/media/Files/ClientAlert/2015/08/150804CIETACSplitEnglish.pdf>.

<sup>2</sup> Review of company records shows that CIETAC registered its Tianjin Sub-Commission (also known as the Tianjin International Economic

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In mid-2012, however, the Shanghai and South China Sub-Commissions very publicly declared their independence from CIETAC and became independent arbitration commissions. In late 2012, the former South China Sub-Commission changed its name to the South China International Economic and Trade Arbitration Commission/Shenzhen Court of International Arbitration (**SCIA**). In April 2013, the former Shanghai Sub-Commission followed suit and changed its name to the Shanghai International Economic and Trade Arbitration Commission/Shanghai International Arbitration Center (**SHIAC**). In response to the secession of the former South China and Shanghai Sub-Commissions, CIETAC announced the establishment of new sub-commissions in both Shenzhen and Shanghai on December 31, 2014.<sup>3</sup>

The secession of the former South China and Shanghai Sub-Commissions and the establishment by CIETAC of new sub-commissions in Shenzhen and Shanghai raised difficult jurisdictional and procedural questions and resulted in significant uncertainty about the validity of arbitral awards issued by both the new and old sub-commissions in Shenzhen and Shanghai. On July 15, 2015, the SPC sought to resolve that uncertainty by issuing a judicial interpretation regarding arbitration agreements providing for submission of disputes to either the CIETAC South China Sub-Commission or the CIETAC Shanghai Sub-Commission (the “**Reply**”). In the Reply, the SPC confirmed that, if an arbitration agreement provides for reference of disputes to “CIETAC Shanghai Sub-Commission” or “CIETAC South China Sub-Commission,” parties should:

- Refer such disputes to SCIA or SHIAC if the arbitration agreement was concluded before the name change to SCIA or SHIAC (as appropriate); or
- Refer such disputes to the relevant new CIETAC Sub-Commission if the arbitration agreement was concluded after the name change to SCIA or SHIAC (as appropriate).<sup>4</sup>

The Reply, which came into effect on July 17, 2015, has *de facto* precedential effect and is binding upon courts of all levels throughout the PRC.

Many thought that the guidance provided by the Reply would put to rest the core jurisdictional uncertainty flowing from the CIETAC split. The conflict that has arisen between CIETAC and the Guangdong DOJ suggests that this may not quite be the case.

## CONFLICT BETWEEN CIETAC AND GUANGDONG DOJ

The Guangdong DOJ is the provincial governmental department responsible for judicial and administrative matters in Guangdong Province, including the registration of arbitration commissions. In August 2014, the Guangdong DOJ published a notice on its website stating that the PRC Arbitration Law and other regulations require that any arbitration commission must be registered with its local government department of judicial

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and Financial Arbitration Center of CIETAC) and its Southwest Sub-Commission as companies (rather than public sector organizations) in 2008 and 2009, respectively.

<sup>3</sup> See CIETAC Press Release, China International Economic and Trade Arbitration Commission Announcement On the Reorganization of CIETAC South China Sub-Commission and CIETAC Shanghai Sub-Commission (Dec. 31, 2014), <http://cn.cietac.org/notes/notes141.shtml>.

<sup>4</sup> If the administering arbitration commission is unclear or ill-defined, such as “the arbitration commission in Shenzhen,” PRC courts may find the arbitration agreement to be invalid, as no specific arbitration commission is identified.

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administration (the “**August 2014 Notice**”).<sup>5</sup> In its August 2014 Notice, the Guangdong DOJ asserted that, if an arbitration commission fails to register as required, any arbitral awards that it renders shall not be legally binding. The Guangdong DOJ appended to the August 2014 Notice a list of the 13 arbitration commissions (or their branches) that were registered to operate in Guangdong Province, including the SCIA.

It appears that—despite CIETAC’s announcement of its new sub-commission’s establishment in December 2014—CIETAC did not register its new sub-commission as an arbitration commission with the Guangdong DOJ. Likely due to strong local support for the SCIA, this failure to register the new sub-commission became a source of conflict between CIETAC and the Guangdong DOJ that became public in August 2015. On August 3, 2015, the Guangdong DOJ issued a letter to CIETAC, which was leaked to the media (the “**August 3, 2015 Letter**”). In the August 3, 2015 Letter, the Guangdong DOJ asserted that CIETAC had not registered its new South China Sub-Commission as an arbitration commission in Guangdong.<sup>6</sup> The August 3, 2015 Letter also stated that the Guangdong DOJ had received complaints that CIETAC has been conducting arbitrations in Guangdong under the names “CIETAC South China Sub-Commission” and “CIETAC Shenzhen Branch,” which remain registered names associated with the breakaway SCIA. The Guangdong DOJ demanded that CIETAC immediately cease its “illegal arbitration activities” in Guangdong.

In response, CIETAC issued a robust reply to the Guangdong DOJ on August 12, 2015, in which it denied violating any PRC laws and regulations, and demanded that the Guangdong DOJ withdraw its August 3, 2015 Letter. CIETAC asserted that its sub-commissions act on behalf of CIETAC, which is a registered arbitration commission approved by the PRC State Council. CIETAC further asserted that its sub-commissions function as branch offices that accept applications, and that arbitral awards are always issued in the name of CIETAC itself, not in the name of the new CIETAC South China Sub-Commission.<sup>7</sup> This characterization is in accordance with the practice of CIETAC’s headquarters, which is to affix its seal to all awards issued in PRC-seated arbitrations.

## IMPACT OF THE CONFLICT

Although commentators had hoped that the recent Reply issued by the SPC would eliminate jurisdictional uncertainties arising from the CIETAC split going forward, the Guangdong DOJ’s August 3, 2015 Letter has the potential to bring into question the validity of awards issued in respect of disputes referred to CIETAC’s new South China Sub-Commission. It is conceivable that losing parties in arbitration may seek to use the Guangdong DOJ’s declaration that CIETAC’s new South China Sub-Commission is improperly registered as a basis for seeking to set aside or challenging enforcement of arbitral awards in respect of disputes submitted to CIETAC’s new South China Sub-Commission. While no awards have yet been set aside or refused enforcement in Guangdong for this reason, the August 3, 2015 Letter may encourage losing parties to raise opportunistic challenges to awards on the jurisdictional basis of improper registration.

<sup>5</sup> See August 2014 Notice, Notice of the Guangdong Provincial Department of Justice Regarding Registration of Establishment of Arbitration Commissions (Aug. 2014), <http://www.sccietac.org/files/fckFile/file/notice.pdf>.

<sup>6</sup> For the Chinese version of the August 3, 2015 Letter and a relevant news report in Chinese language, see <http://news.163.com/15/0823/11/B1MV9KC200014AED.html>.

<sup>7</sup> Article 2(3) of CIETAC Rules 2015 provides that “CIETAC is based in Beijing. It has sub-commissions or arbitration centers (Appendix I). The sub-commissions/arbitration centers are CIETAC’s branches, which accept arbitration applications and administer arbitration cases with CIETAC’s authorization.”

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Given that awards are issued in the name of CIETAC's headquarters, which is indisputably a registered arbitration commission, the risk of successful applications for set aside or challenges to enforcement should be low. The threat of successful challenges is most likely where set aside is sought or enforcement is challenged in Guangdong Province, where the courts are particularly likely to pay heed to the pronouncements of the Guangdong DOJ. The risk of a successful challenge is particularly great for awards issued in domestic arbitrations. The SPC has implemented a safeguard in respect of awards issued in foreign or foreign-related arbitrations in the form of a pre-reporting system. Before a Chinese court may set aside a foreign-related award or deny enforcement of a foreign or foreign-related award, the SPC conducts a review to pre-approve the lower court's decision in all cases.<sup>8</sup> This safeguard does not, however, apply in respect of awards issued in domestic arbitrations.

Notably, this issue of improper registration of sub-commissions may potentially have implications for awards issued in arbitrations submitted not just to the new CIETAC South China Sub-Commission, but also to the new CIETAC Shanghai Sub-Commission. As Shanghai has not published a list of duly registered arbitration commissions, it is unclear whether CIETAC has registered its new Sub-Commission in Shanghai. The Justice Department of Shanghai has not taken an aggressive stance towards CIETAC's operations in Shanghai. However, if the new CIETAC Shanghai Sub-Commission is improperly registered or if it is not registered under the name "CIETAC Shanghai Sub-Commission," there is a risk that awards issued in arbitrations submitted to this Sub-Commission may face set aside and/or challenges to enforcement on the same ground of improper registration.

## CONCLUSION

In sum, the Guangdong DOJ's August 3, 2015 Letter may encourage losing parties to lodge opportunistic challenges to awards for improper registration. Users of CIETAC's new South China Sub-Commission (and, potentially, its new Shanghai Sub-Commission) should be aware of the potential for opportunistic litigation. While set aside or refusal of enforcement may be unlikely, parties to arbitration agreements providing for PRC-seated arbitration to take place in Shenzhen or Shanghai are advised to take steps to avoid jurisdictional issues.

Parties wishing to avoid the risk of jurisdictional issues arising from the split of the former Shanghai and South China Sub-Commissions from CIETAC should consider avoiding entering arbitration agreements referring disputes to CIETAC's new South China or Shanghai Sub-Commissions. Parties may eliminate the risk and achieve the same practical outcome by specifying in their arbitration agreements that disputes shall be submitted to CIETAC headquarters in Beijing for administration, with hearings to take place in Shenzhen or Shanghai (as appropriate). Alternatively, should administration in Shenzhen or Shanghai be favored, parties may agree that disputes shall be submitted to SCIA or SHIAC (as appropriate). Parties are advised to avoid using potentially problematic names such as "China International Economic and Trade Arbitration Commission South China Sub-Commission" or "China International Economic and Trade Arbitration Commission Shenzhen Sub-Commission."

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<sup>8</sup> See Article 2 of the SPC Notice on the Handling of Issues Concerning Foreign-Related Arbitration and Foreign Arbitration by People's Courts (in relation to refusal of enforcement of foreign or foreign-related awards) (as amended in 2008) and Articles 1 and 2 of the SPC Notice Regarding Matters Relating to People's Courts Setting Aside Foreign-Related Arbitral Awards (in relation to set aside of foreign-related awards).

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