

Dispute Resolution in the People's Republic of China ("China" or "PRC").

In this Newsletter, we will attempt to address, in a nutshell, several aspects of dispute resolution – with regard to the PRC-related transactions, bearing in mind recent developments in the Chinese laws and regulations.

Choice of Law

Foreign (i.e. non-Chinese) persons and legal entities are often concerned with the law which shall apply to their dealings with PRC persons and legal entities. Review of the (quite recent – 2011) PRC Law on the Application of Laws to Foreign-Related Civil Relations (the "Law")¹ may alleviate some of these concerns, especially given the recent (December 2012) opinion of the PRC Supreme People's Court ("SPC") in this regard.

The Law provides that parties to an agreement may expressly select the law governing their foreign-related relationship – if the (PRC) laws applicable to such relationship explicitly allow them to do so. Since the PRC Contract Law, PRC Maritime Law, PRC Civil Aviation Law explicitly allow such selection (where a foreign party is involved), this issue seems to be settled. Moreover, the Law itself includes specific provisions which allow parties to a foreign related civil relationship to elect the applicable law with regard to many aspects of international trade and business. The Law (as interpreted by the SPC) further allows the parties to elect an "applicable law" which has no linkage to the parties and/or to the transaction in question.

Having said that – one should bear in mind several caveats and exceptions: the Law further provides that where the PRC laws contain mandatory provisions which

apply to foreign-related civil relations, these mandatory provisions shall directly apply irrespective of the choice of law. Moreover, the Law further provides that if the application of foreign laws will damage the social public interests of the PRC, the laws of the PRC shall apply.

In the absence of an explicit election of the applicable law, the provisions of the Law shall apply. The Law, as construed by the SPC provides that the following circumstances may be considered as establishing a foreign-related civil relationship:

- Where either party is or both parties are foreign citizens, foreign legal persons or other organizations or stateless persons;
- Where the subject matter is located outside the territory of the PRC;
- Where the legal facts which establish, modify or terminate the civil relationship take place outside the territory of the PRC;
- Where the habitual residence ("Domicile") of either party or both parties is located outside the territory of the PRC;
- Other circumstances that may be deemed foreign-related civil relationships.

The SPC further ruled that attempts to evade the applicability of PRC laws (e.g. by adding to an agreement a party, such as a foreign parent company of a Foreign Investment Enterprise, where the latter is the actual party to the agreement) shall be disregarded, and the PRC courts shall not respect the parties' choice of law in such circumstances.

Arbitration Proceedings in the PRC

Many foreign entities include a foreign (usually Hong-Kong or Singapore – both have Common Law-based legal system) arbitration clause in their agreements with Chinese counterparts. Since China is a part of the New York Convention, foreign arbitral awards are generally enforced in the PRC (having said that – a court of first instance may decline to enforce a foreign arbitral award,

but its decision requires the approval of the SPC.

However, since many PRC entities are adamant in having a PRC law – PRC arbitration clauses in their agreements. It may be advisable to introduce, in a nutshell, the PRC arbitration law, institutions and practice.

In general, arbitration in China may not be conducted under the ICC rules of international arbitration (or any other non-PRC arbitration rules – for that matter) or by an ad-hoc arbitration. PRC arbitration procedures are actively and intrusively supervised by PRC courts. For example, under Chinese law, applications for interim relief are ultimately dealt with by the Chinese courts, rather than by the arbitrators themselves. Moreover, such interim measures are limited in their scope to only two categories: the preservation of property and evidence.

The arbitration process itself is more inquisitorial than adversary: Chinese arbitrators tend to be proactive and closely control the arbitration proceedings. Witnesses and documentary evidence may play a more limited role in such process. Moreover, in many cases, the arbitrator may play a dual role of both an arbitrator and a mediator. Thus arbitration proceedings may be shorter and cheaper (legal fees-wise) than the "Western"/Israeli proceedings. Having said that, quite a few non-PRC entities involved in such proceedings have voiced their discomfort with what may appear as informal/hybrid proceeding. Therefore, it is advisable (to the extent legally possible) to include in PRC arbitration clauses explicit provisions regarding the administration of the arbitration process, in line with the common practice in Israel, the US or Europe.

PRC's most prominent arbitral institution, the China International Economic and Trade Arbitration Commission ("CIETAC"), is the world's largest international

arbitration institution. It may be noted that in 2012, in response to concerns voiced by foreign entities, the CIETAC has issued its new arbitration rules², which among other things:

- Allow the CIETAC (where the parties have failed to address this issue) to conduct the arbitration proceedings either in Chinese or in English – depending on the circumstances of the dispute (previously the default language of the arbitration was Chinese).
- Grant the arbitrators more flexibility with regard to interim measures.
- Allow the CIETAC to conduct arbitration proceedings in locations other than mainland China.
- Allow the CIETAC to conduct arbitration proceedings according to the arbitration rules of other arbitration institutions.

We believe that we did not see the last of such developments and reforms. We therefore advise all concerned parties to keep a close watch on the legal development in this field.

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² <http://cn.cietac.org/rules/rules.pdf>