CHINA DISPUTE RESOLUTION

NEWS LETTER



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NEWS ALERT

1. SPC Issues Opinions on the Lawful Adjudication of Cases Involving Artificial Intelligence

On 7 September 2026, the Supreme People's Court issued the *Opinions on the Lawful Adjudication of Cases Involving Artificial Intelligence*, addressing the use of AI in litigation. The Opinions provide that parties may be sanctioned where AI is used to fabricate facts or bring false claims, and that AI-generated evidence used to obstruct judicial proceedings may result in fines, detention or, where applicable, criminal liability. Parties are also required to verify the authenticity and accuracy of AI-generated litigation materials, including legal provisions, judicial interpretations and case law, before submitting them to the court, and must disclose the use of AI assistance when filing such materials. The SPC noted that courts have identified cases involving fabricated AI-generated authorities and stressed that parties and their representatives cannot rely on "AI hallucination" or technological neutrality to avoid legal responsibility. The Opinions provide an important reminder for parties and counsel using generative AI in litigation that AI-assisted legal research and drafting does not displace the practitioner's responsibility for the accuracy and authenticity of materials submitted to the court.

2. SPC Releases Bilingual Casebook on New York Convention Application

In late September, the SPC's Fourth Civil Trial Division and the SPC Collaborative Innovation Base for Foreign-Related Legal Talent Training (Tsinghua University) have published *Essentials of Typical Cases in Chinese Courts' Application of the New York Convention (Chinese-English Edition)*. The book contains 43 typical cases on key and difficult foreign-related judicial issues, including legality of arbitral procedure, cautious application of public policy, boundaries of excess of authority, commercial nature of sports arbitration, validity of arbitration agreements, identification of arbitral institution names, and limitation periods for recognizing and enforcing foreign arbitral awards. The decisions are clearly reasoned and provide strong rule guidance. For example, the included *Daniele Equipment Co.* case, prepared by the Wuxi International Commercial Court, held that the arbitral seat determines the law governing arbitral procedure and the competent court, and determines the award's nationality. The seat is a legal concept, not a physical location, and is not necessarily the institution's location, the hearing venue, or the place where the award is made. Parties may agree on the seat in writing; absent such agreement, it is determined under the arbitration rules or by the tribunal based on convenience. As the seat was Singapore, the court reviewed the case under the New York Convention and recognized and enforced the SCC award. The ruling reflects Chinese courts' commitment to multilateralism, alignment with high-standard international economic and trade rules, support for international commercial arbitration, and a pro-arbitration judicial environment.

3. Hong Kong Gazettes Rules for New Mainland Service Arrangement, in Force on 30 March 2027

On 16 October 2026, the Hong Kong Government gazetted three sets of court rules implementing the *Arrangement on Mutual Service of Judicial Documents in Civil and Commercial Proceedings between the Mainland and the Hong Kong Special Administrative Region*, signed by the Department of Justice and the Supreme People's Court on 20 April 2026. The Rules of the High Court (Amendment) (No. 2) Rules 2026, the Rules of the District Court (Amendment) (No. 2) Rules 2026 and the Matrimonial Causes (Amendment) Rules 2026 were made on 12 October 2026 under section 54 of the High Court Ordinance (Cap. 4), section 72 of the District Court Ordinance (Cap. 336) and section 54 of the Matrimonial Causes Ordinance (Cap. 179). The rules add new ways to serve court documents on people in the Mainland, including in matrimonial proceedings. By way of example, service by post , electronic service (email, fax, or mobile communication where the recipient expressly consents), service through law firms or relevant institutions, and service made by public announcement. They take effect on 30 March 2027, when the new Arrangement replaces the previous one, which has been in operation for more than 27 years. The Supreme People's Court will issue a judicial interpretation for the Mainland. Service—formally delivering court documents—often decides whether limitation periods are met, whether default judgment is available, and whether Hong Kong or Mainland judgments can later be recognized. The expanded methods should therefore be reviewed in live cross-boundary cases.

4. Revised Lawyers Law Takes Effect: Foreign-Related Legal Services and GBA Practice by Hong Kong and Macao Lawyers Now on a Statutory Footing

On 1 September 2026, the revised Lawyers Law of the People's Republic of China took effect, introducing new provisions concerning the development of foreign-related legal services and the cultivation of foreign-related legal talent, as well as the practice of Hong Kong and Macao lawyers in the Guangdong-Hong Kong-Macao Greater Bay Area (GBA). Article 62 provides that Hong Kong and Macao lawyers who pass the GBA lawyers' qualifying examination organized by the judicial administrative department of the State Council and obtain Mainland practice qualifications may practice, within the prescribed scope of business, in the nine Mainland GBA cities. On 19 September, the Ministry of Justice held the 2026 GBA lawyers' qualifying examination in Shenzhen and Zhuhai, the first examination since the GBA practice regime was placed on a statutory footing. Since the pilot scheme began in 2020, more than 700 Hong Kong and Macao lawyers have obtained GBA practice certificates covering all nine Mainland GBA cities. The amendments provide a statutory basis for the continued integration of legal services within the GBA and may further facilitate cross-border legal services and cooperation involving Hong Kong, Macao and Mainland China.

5. Hong Kong Court Recognizes Mainland Judgments as Final and Conclusive Despite Availability of Retrial

On 3 August 2026, the Hong Kong Court of First Instance in *Sanhe Hongxiang Concrete Co., Ltd v Zhang Yongtie [2026] HKCFI 4315* upheld the enforcement at common law of two Mainland judgments. The defendant resisted enforcement on the ground that the judgments were not "final and conclusive" because Mainland retrial procedures remained available. The Court rejected the argument, holding that the mere availability of trial supervision procedures does not, per se,

prevent a Mainland judgment from being final and conclusive. Instead, the relevant question is whether there is a real likelihood of a retrial, which the defendant had failed to establish. The Court also rejected late evidence concerning a newly filed retrial application. The decision reinforces that a party resisting enforcement of a Mainland judgment in Hong Kong on finality grounds must demonstrate more than the theoretical availability of retrial proceedings. It also highlights the importance of credible and independent expert evidence on Mainland law in cross-border enforcement proceedings.

6. Wingtech Obtains RMB 2.139 Billion Asset Preservation Order under China's Anti-Foreign Sanctions Law

On 1 September 2026, Chinese company Wingtech Technology Co., Ltd. announced that the Dongguan Intermediate People's Court had granted its application for property preservation in proceedings brought by Wingtech and its subsidiary Yucheng Holdings against Nexperia headquartered in Nihmegen, Netherlands, and other defendants. The Court ordered the seizure, attachment and freezing of assets worth approximately RMB 2.139 billion held by defendants, including their equity interests in several Chinese subsidiaries. The measures, which took effect between 20 and 25 August 2026, were based on Article 12 of the Anti-Foreign Sanctions Law, which permits Chinese citizens and organizations whose lawful rights and interests are infringed by conduct prohibited under that provision to bring proceedings before Chinese courts seeking cessation of the infringement and compensation for losses. The case is reported to be the highest-value judicial application of the Anti-Foreign Sanctions Law since its enactment in 2021. The proceedings illustrate the potential use of Chinese judicial remedies, including asset preservation, in disputes arising from foreign sanctions and related restrictive measures.

7. Singapore High Court Sets Aside Enforcement of CIETAC Emergency Arbitrator's Interim Award

On 11 September 2026, the Singapore High Court in *Zhejiang Crystal-Optech Co Ltd v Moveon Technologies Pte Ltd* [2026] SGHC 186 set aside an enforcement order concerning an interim award issued by a CIETAC emergency arbitrator in a China-seated arbitration. The Court held that the emergency arbitrator lacked the power to grant the relevant interim measures under Chinese law or the parties' agreement. The dispute arose from a failed joint venture between Zhejiang Crystal-Optech and Moveon Technologies, following which the emergency arbitrator issued an interim award restraining Moveon from receiving dividend payments from the joint venture's liquidators. The Singapore Court held that the "applicable law" under Article 23(2) of the CIETAC Rules referred to the *lex arbitri*, namely Chinese law, and that Chinese law reserved the power to grant the relevant interim measures to the courts. The Court further held that the parties' deemed agreement to the CIETAC Rules did not, without more, constitute a distinct agreement conferring such powers on the emergency arbitrator. The decision is significant for parties considering emergency arbitration in China-seated proceedings, as it underscores the importance of examining the legal basis for emergency arbitrator powers under the law of the seat rather than assuming that institutional rules alone confer such authority.

8. Hong Kong Court Restrains Mainland Litigation Brought to Evade HKIAC Arbitration

On 28 September 2026, the Hong Kong Court of First Instance in *A and Others v Z* [2026] HKCFI 5453 granted anti-suit injunctions requiring a Mainland company to discontinue proceedings brought before the Mainland courts, holding that they were commenced in order to evade arbitration clauses in two joint venture agreements. The applicants were a Singapore company in a United States-headquartered glass substrates group and three affiliates; the agreements were governed by Mainland law and provided for arbitration administered by the Hong Kong International Arbitration Centre. The Mainland company had commenced a shareholder derivative action, three claims of unfair competition and market monopoly, and actions challenging the validity of the arbitration agreements on grounds of duress and public policy. Madam Justice Mimmie Chan held that the threshold was a prima facie case, mirroring the standard for a stay under section 20 of the Arbitration Ordinance (Cap. 609), and that relief could extend to affiliates that were not parties to the agreements where the proceedings against them were vexatious, oppressive and an abuse of process. Challenges to validity, she held, fell to the tribunal in the first instance. The decision reinforces Hong Kong's pro-arbitration stance by confirming that parties cannot circumvent arbitration clauses simply by recasting contractual disputes as shareholder or competition claims, or by joining closely connected non-parties. It also clarifies that the court's role at the injunctive stage is protective rather than determinative of the arbitration agreement's validity—a question reserved for the tribunal, subject to the court's subsequent supervisory review.

9. Xiamen Maritime Court Grants Anti-Anti-Suit Injunction in Support of a XMAC Arbitration

On 19 October 2026, Fujian court authorities reported that the anti-suit injunction granted by Xiamen Maritime Court in *Smooth Ocean Pte Ltd v STS Seatoshore Group Pte Ltd*, dated 7 May 2026, had been selected for the *Chinese Maritime and Commercial Law Reports* 2026 (Volume 2). Both parties are Singapore companies. Disputes under finance leases of three vessels were referred to the Xiamen Arbitration Commission (XMAC), and during the arbitration the respondent commenced vessel arrest proceedings and criminal complaints in Guinea. The applicant applied, through the institution, for preservation restraining the respondent from pursuing those proceedings. The Court first issued a comprehensive disclosure order after finding the applicant's initial evidence selective, then applied Article 39 of the Arbitration Law, in force since 1 March 2026, and a three-tier test addressing impediment to enforcement, necessity and proportionality, and international comity. It ordered withdrawal of the specific Guinean arrest proceedings within 10 days, restrained collateral foreign applications against its own order, refused wider relief against all foreign proceedings, and set a daily penalty of RMB 1 million for non-compliance. The ruling is a landmarking maritime anti-anti-suit injunction under the revised law, and signals that Chinese courts will use preservation powers to hold the ring for an arbitration seated in China.

Remedies Following the Termination of Arbitration After an Unauthorised Settlement Agreement: Lessons from the Hong Kong Court's Decision in LT v RV for Cross-Border Settlement Arrangements

Ping Zhao, Stella Lu, Tianning Jiang

Abstract

On 3 March 2026, the Court of First Instance of the High Court of Hong Kong delivered its decision in LT v RV on the validity and effect of a settlement agreement entered into during arbitration. The Court held that neither the procedural order terminating the arbitration nor the Settlement Agreement was an arbitral award that could be set aside under section 81 of the Arbitration Ordinance. The Court nevertheless considered whether the Settlement Agreement was binding, relying on its supervisory jurisdiction as the court of the seat and on the exclusive-jurisdiction clause in the agreement. It concluded that the director had signed the agreement without actual or apparent authority because the required Creditor Directors' approval had not been obtained, and that the agreement was therefore not binding on LT. This article considers the practical implications for parties settling cross-border disputes, including the choice of procedural route for recording a settlement, the drafting of dispute resolution clauses and the verification of corporate authority.

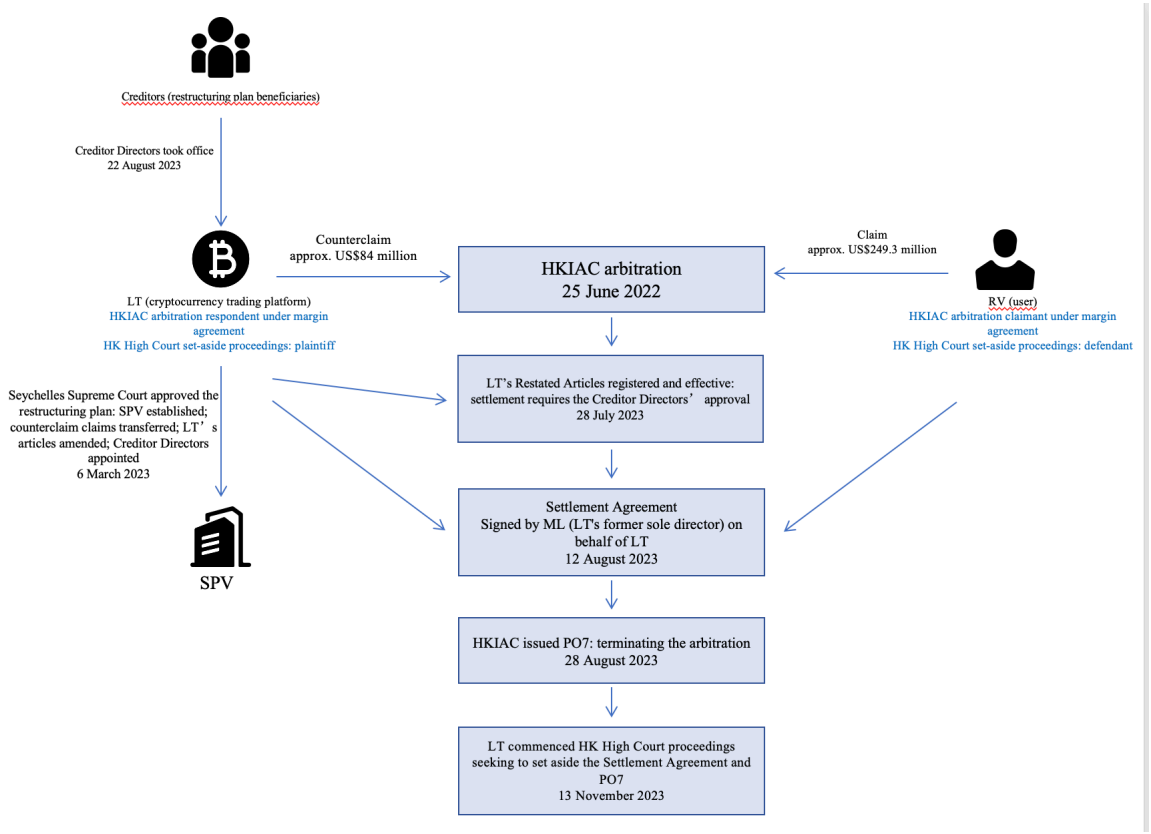
Main Text

In cross-border commercial disputes, settlement is often an effective way to resolve a dispute and reduce the costs of arbitration. But does signing a settlement agreement and terminating the arbitral proceedings necessarily mean that the dispute has been finally resolved? What happens if a party later argues that the person who signed the agreement lacked the necessary corporate authority?

The Hong Kong Court of First Instance's decision in LT v RV highlights these risks.[1] The parties settled a cross-border arbitration involving claims exceeding US$300 million, and the tribunal subsequently issued a procedural order terminating the proceedings. LT later challenged the settlement after alleging that its director had not obtained the internal approval required under a restructuring scheme sanctioned by the Supreme Court of Seychelles. LT sought relief in respect of both the Settlement Agreement and the procedural order.

LT v RV is a reminder that termination of arbitral proceedings does not necessarily resolve the underlying dispute on its merits. The legal character of the settlement, the procedural route chosen to give it effect and the signatory's authority each matter. Where a company is subject to a restructuring scheme or material governance restrictions, a settlement made without the required authority may not bind the company even after the arbitration has been terminated.

I. Case Overview



The case arose from a commercial dispute involving a cryptocurrency trading platform. LT, a company incorporated in Seychelles, had operated the platform; RV was a customer and Bitcoin investor. Following the collapse in cryptocurrency prices in 2022, LT encountered financial difficulties. RV then commenced arbitration against LT at the Hong Kong International Arbitration Centre (HKIAC), claiming approximately US$249.3 million in connection with alleged misrepresentations and breaches of a margin agreement. LT brought its counterclaim against RV for alleged breach of contract, seeking approximately US$84 million.

During the arbitration, LT underwent a restructuring. On 6 March 2023, the Supreme Court of Seychelles sanctioned a scheme of arrangement. Under the scheme, LT's claims against RV underlying its approximately US$84 million counterclaim were assigned to a special-purpose vehicle, with the creditors intended to benefit from any recoveries. The scheme also required the appointment of creditor representatives as directors of LT (the "Creditor Directors") and amendments to LT's constitutional documents. The Restated Articles, registered on 28 July 2023, required the Creditor Directors' approval for decisions concerning the prosecution, resolution and settlement of the "Assigned Claims" in the arbitration.[2] Those claims were the claims underlying LT's counterclaim against RV and were intended to benefit the creditors.

On 12 August 2023, ML, then LT's sole director, signed the Settlement Agreement with RV on LT's behalf. The parties agreed to settle on a "drop hands" basis: each would withdraw its claims and counterclaims and bear its own costs, subject to the agreement's terms. The parties jointly asked the tribunal to record the settlement in an award on agreed terms; instead, on 28 August 2023 the tribunal issued Procedural Order No. 7 ("PO7"), terminating the arbitration on the basis that there were no terms of settlement to record.

LT's creditors were not aware of the settlement when it was concluded and learned of it in October 2023. LT then commenced proceedings by originating summons in the Court of First Instance, seeking relief in respect of the Settlement Agreement and PO7 and a declaration that the Settlement Agreement was not binding. LT argued that the agreement was inconsistent with the Seychelles-sanctioned scheme and had been signed by ML without authority. It also challenged PO7 on the basis that it rested on the allegedly invalid agreement, was contrary to public policy, and impaired LT's ability to present its case in the arbitration.

On 3 March 2026, the Court held that neither PO7 nor the Settlement Agreement was an arbitral award capable of being set aside under section 81 of the Arbitration Ordinance. The Court nevertheless concluded that ML had signed the Settlement Agreement without actual or apparent authority and that it was not binding on LT.

II. Issues in Dispute

The principal issues were: (1) whether the Settlement Agreement and PO7 were arbitral awards capable of being set aside under section 81 of the Arbitration Ordinance; (2) if not, whether the Hong Kong court could nevertheless examine the validity and binding effect of the Settlement Agreement; and (3) whether ML had actual or apparent authority to sign it on LT's behalf, including whether RV could reasonably rely on any appearance of authority.

III. The Court's Analysis

(1) Whether the Settlement Agreement and PO7 Constituted Arbitral Awards Liable to Be Set Aside

The threshold issue was whether the Settlement Agreement or PO7 constituted an arbitral award that could be set aside under section 81 of the Arbitration Ordinance.[3] The Court considered the two separately.

Chan J explained that section 81 of the Arbitration Ordinance, which gives effect to Article 34 of the UNCITRAL Model Law, provides the exclusive recourse of setting aside an arbitral award; it does not apply to every decision or document connected with an arbitration.[4] "Award" is not defined in the Ordinance, nor in the Convention or the Model Law.[5] Referring to G v N [2024] 4 HKC 1, W v Contractor [2024] 3 HKLRD 179 and ZCCM Investments Holdings PLC v Kansanshi Holdings Plc [2020] 1 All ER (Comm) 132,[6] the Court emphasised that substance, rather than the label attached to a decision, is central. Relevant considerations include whether the decision finally determines substantive issues submitted to arbitration and whether it deals with substantive rights and liabilities rather than merely procedural matters.[7] In PO7, the tribunal expressly stated that it was terminating the proceedings "in the form of a procedural order and not in the form of an award, as requested by the Parties".[8] The tribunal did not determine the merits of the claims or counterclaims. PO7 terminated the proceedings and dealt with costs; it did not determine the claims, dismiss them on their merits or record their release. It was therefore not an award capable of being set aside under section 81. Because the claims had not been finally determined, fresh arbitration proceedings could potentially be commenced if the applicable limitation period had not expired.[9] The termination of the arbitration therefore did not, by itself, finally resolve the underlying dispute.

The Court separately considered the Settlement Agreement. The tribunal had not recorded the settlement in an award on agreed terms. Section 66(2) of the Arbitration Ordinance treats a written settlement agreement as an award only "for the purposes of its enforcement".[10] It does not extend section 81's setting-aside procedure to a private settlement agreement.[11] A party resisting enforcement must rely on the applicable statutory grounds for refusing enforcement, rather than seek to set aside the agreement as if it were an arbitral award. The Court therefore held that the Settlement Agreement was not an award that could be set aside under section 81.[12]

(2) Whether the Hong Kong Court Retained Jurisdiction to Review the Validity of the Settlement Agreement

The Court's conclusion that neither PO7 nor the Settlement Agreement could be set aside under section 81 did not mean that LT had no remedy.[13] Chan J considered that the Hong Kong court, as the court of the seat, had supervisory jurisdiction in relation to the arbitration. Further, clause 7.2 of the Settlement Agreement expressly submitted disputes arising out of or in connection with the agreement to the exclusive jurisdiction of the High Court of Hong Kong. That clause provided an independent contractual basis for the Court to determine whether the Settlement Agreement was valid and binding. The Court therefore had jurisdiction to examine the agreement's validity.

(3) Whether ML Had Authority to Sign the Settlement Agreement, and Whether RV Could Rely on Apparent Authority

Once jurisdiction was established, the central question was whether ML had authority to sign the Settlement Agreement on LT's behalf. If he did not, the Court also had to consider whether RV could nevertheless rely on apparent authority. The Court examined actual authority and apparent authority separately.

As to actual authority, Chan J considered LT's Restated Articles and the restructuring scheme. The Supreme Court of Seychelles had, in its judgment of 31 July 2025, found that ML lacked authority to sign the Settlement Agreement and that his failure to comply with the scheme constituted contempt of court.[14] Because LT was incorporated in Seychelles, its constitution and the authority of its directors were matters of Seychelles law.[15] The Hong Kong Court had to assess the evidence independently, but could consider the Seychelles judgment as evidence of that law.[16] Having considered that judgment and the evidence before it, Chan J reached the same conclusion: the scheme and Restated Articles required the board to include the Creditor Directors and required board approval for matters relating to the arbitration.[17] Given ML's knowledge of the scheme, the order of 6 March 2023 and the Restated Articles, he had no authority to enter into the Settlement Agreement without the creditors' knowledge and approval.[18]

As to apparent authority, Chan J held that the circumstances excluded reliance on that doctrine.[19] Applying the principles in Thanakharn Kasikorn Thai Chamkat (Mahachon) v Akai Holdings Ltd (No 2) (2010) 13 HKCFAR 479,[20] the Court considered, among other matters, whether LT had represented that ML had authority, whether any representation was made by someone with actual authority, whether RV relied on it, and whether LT had capacity under its constitutional documents to enter into the transaction or authorise ML to do so. The fourth requirement was not satisfied: under Article 14.9 of the Restated Articles, the Settlement Agreement required the prior approval of the Creditor Directors.[21] The Court also accepted that this was not an act in the ordinary course of LT's

business.[22] It was an "unusual and exceptional" agreement in the circumstances of LT's court-sanctioned restructuring. Further, even if LT had represented that ML was authorised, it was unreasonable for RV to rely on that representation without enquiring whether the creditors or Creditor Directors had approved the agreement.[23] RV knew of the scheme, had opposed it in the Seychelles proceedings and knew that it had been sanctioned. The settlement released LT's claims against RV that had been assigned for the creditors' benefit, yet there was no indication of creditor knowledge or approval. The Court also considered RV's own evidence that he did not trust ML. In those circumstances, accepting ML's authority without enquiry was unreasonable and amounted to turning a blind eye to suspicious circumstances.[24]

The Court concluded that ML had neither actual nor apparent authority to sign the Settlement Agreement and that the agreement was not binding on LT.[25]

IV. Practical Recommendations

(1) Parties Should Seek an Award on Agreed Terms After Reaching Settlement

The lessons of LT v RV are multi-faceted. For companies engaged in cross-border arbitration and settlement negotiations, at least three matters merit attention: how to choose the exit route, how to draft the dispute resolution clause, and how to verify the counterparty's authority.

The parties may choose to enter into a private settlement agreement without asking the tribunal to record it as an award. This can be flexible and economical, but the agreement remains a contract whose validity is governed by the applicable contract law. Section 66(2) of the Hong Kong Arbitration Ordinance treats a written settlement agreement as an award for enforcement purposes only. It does not make the agreement an arbitral award or subject it to the statutory setting-aside procedure. The agreement's validity and binding effect may therefore need to be determined through separate proceedings, as occurred in LT v RV.

Where appropriate, parties should consider asking the tribunal to record their settlement in an award on agreed terms. Article 30 of the UNCITRAL Model Law provides that, if the parties settle during the arbitral proceedings, the tribunal shall terminate the proceedings and, if requested by the parties and not objected to by the tribunal, record the settlement in an award on agreed terms. Such an award has the same status and effect as any other award on the merits.[26] An award on agreed terms may more readily be recognised and enforced under the New York Convention and provide greater finality than a private agreement alone. The parties should, however, confirm the requirements of the applicable arbitration law and rules, and ensure that the settlement is properly authorised and, where appropriate, recorded in an arbitral award.

(2) The Dispute Resolution Clause in a Settlement Agreement Should Be Carefully Drafted

In LT v RV, the Settlement Agreement conferred exclusive jurisdiction on the High Court of Hong Kong over disputes arising out of or in connection with the agreement. That clause gave the Court a contractual basis to determine whether the agreement was valid and binding, notwithstanding that it was not an arbitral award capable of being set aside. When drafting settlement agreements, parties should specify the governing law and dispute resolution mechanism clearly and consider how disputes about formation, authority, validity and performance will be resolved. A jurisdiction clause

does not itself cure a lack of corporate authority, but it can provide clarity about the forum in which such issues will be decided.

(3) Identify Authority Risks in Transactions with Unusual Backgrounds

LT v RV does not remove the protection that apparent authority may provide in an appropriate case. It illustrates, however, that a counterparty cannot safely infer authority from a person's title as director where the circumstances and information available point to material restrictions or a lack of authority. The nature of the transaction, the company's constitutional documents and any known restructuring arrangements may all be relevant.

For transactions involving restructuring, insolvency, debt adjustment or significant changes in corporate governance, parties should verify the applicable authorisation and approval requirements, including any approvals required from the board, Creditor Directors, shareholders or a court. This is particularly important where the settlement amount is substantial or the settlement involves the disposal of assets. Parties should obtain and retain the relevant resolutions, approvals and supporting communications before signing, rather than relying solely on the signatory's corporate title.

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1 LT v RV [2026] HKCFI 1280 (3 March 2026). https://legalref.judiciary.hk/lrs/common/ju/loadPdf.jsp?url=https://legalref.judiciary.hk/doc/judg/word/vetted/other/en/2023/HCCT000087B_2023.doc&mobile=N

2 *Supra* note 1, para 20.

3 Arbitration Ordinance (Cap 609), s 81 — Article 34 of the UNCITRAL Model Law, the text of which is set out below, has effect subject to section 13(5):

'Article 34. Application for setting aside as exclusive recourse against arbitral award

(1) Recourse to a court against an arbitral award may be made only by an application for setting aside in accordance with paragraphs (2) and (3) of this article.

(2) An arbitral award may be set aside by the court specified in article 6 only if:

(a) the party making the application furnishes proof that:

(i) a party to the arbitration agreement referred to in article 7 was under some incapacity; or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of this State; or

(ii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case; or

(iii) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the award which contains decisions on matters not submitted to arbitration may be set aside; or

(iv) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Law from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Law; or

(b) the court finds that:

(i) the subject-matter of the dispute is not capable of settlement by arbitration under the law of this State; or

(ii) the award is in conflict with the public policy of this State.

(3) An application for setting aside may not be made after three months have elapsed from the date on which the party making that application had received the award or, if a request had been made under article 33, from the date on which that request had been disposed of by the arbitral tribunal.

(4) The court, when asked to set aside an award, may, where appropriate and so requested by a party, suspend the setting aside proceedings for a period of time determined by it in order to give the arbitral tribunal an opportunity to resume the arbitral proceedings or to take such other action as in the arbitral tribunal's opinion will eliminate the grounds for setting aside.'

(2) Subsection (1) does not affect—

(a) the power of the Court to set aside an arbitral award under section 26(5);

(b) the right to challenge an arbitral award under section 4 of Schedule 2 (if applicable); or

(c) the right to appeal against an arbitral award on a question of law under section 5 of Schedule 2 (if applicable).

(3) Subject to subsection (2)(c), the Court does not have jurisdiction to set aside or remit an arbitral award on the ground of errors of fact or law on the face of the award.

(4) The leave of the Court is required for any appeal from a decision of the Court under article 34 of the UNCITRAL Model Law, given effect to by subsection (1).

4 *Supra* note 1, para 36.

5 *Supra* note 1, para 37.

6 G v N [2024] 4 HKC 1; W v Contractor [2024] 3 HKLRD 179; ZCCM Investments Holdings PLC v Kansanshi Holdings Plc [2020] 1 All ER (Comm) 132.

7 *Supra* note 1, paras 38–40.

8 *Supra* note 1, para 43.

9 *Supra* note 1, para 50.

10 Arbitration Ordinance (Cap 609), s 66(2) — If, in a case other than that referred to in article 30 of the UNCITRAL Model Law, given effect to by subsection (1), the parties to an arbitration agreement settle their dispute and enter into an agreement in writing containing the terms of settlement (settlement agreement), the settlement agreement is, for the purposes of its enforcement, to be treated as an arbitral award.

11 *Supra* note 1, para 57.

12 *Supra* note 1, para 60.

13 *Supra* note 1, para 65.

14 *Supra* note 1, para 70.

15 *Supra* note 1, paras 68, 74.

16 *Supra* note 1, para 73.

17 *Supra* note 1, para 75.

18 *Supra* note 1, para 80.

19 *Supra* note 1, para 83.

20 Thanakharn Kasikorn Thai Chamkat (Mahachon) v Akai Holdings Ltd (No 2) (2010) 13 HKCFAR 479.

21 *Supra* note 1, para 84.

22 *Supra* note 1, paras 85, 87.

23 *Supra* note 1, para 93.

24 *Supra* note 1, para 100.

25 *Supra* note 1, para 102.

26 UNCITRAL Model Law on International Commercial Arbitration (2006), art 30 — Settlement:

(1) If, during arbitral proceedings, the parties settle the dispute, the arbitral tribunal shall terminate the proceedings and, if requested by the parties and not objected to by the arbitral tribunal, record the settlement in the form of an arbitral award on agreed terms.

(2) An award on agreed terms shall be made in accordance with the provisions of article 31 and shall state that it is an award. Such an award has the same status and effect as any other award on the merits of the case.

Legal Principles of Permanent Termination of Independent Guarantees by Chinese Courts: A Review of Chinese Law and Supreme Court Cases (Part Two)

*Saibo Jin**

Abstract

The 2016 "Judicial Interpretation on Independent Guarantee" formulated and promulgated by the Supreme People's Court of China stipulates strict preconditions for a Permanent Injunction against an independent guarantee that is irrevocably payable upon presentation of documents. Examining how these conditions are actually applied, especially in the actual litigation cases handled by the Supreme People's Court itself, particularly exploring the analysis opinions and analytical thinking of judges in the judgments of real cases, and summarizing this promptly, is necessary for guiding international and domestic commercial and banking practices. It also provides extremely beneficial guidance for the handling of similar cases by courts and judges at all levels in China. This article is the part two of the series.

5. The Fifth Legal Principle: the Plaintiff Who Requests to Terminate the Payment of the Standby Letter of Credit (Independent Guarantee) Bears the Burden of Proof, and the Proof Should Meet the Standard of "beyond a reasonable doubt."

5.1 Provisions of Judicial Interpretation of Independent Guarantee

Article 20 of the judicial interpretation stipulates: "In the trial of an independent letter of guarantee fraud or dispute case, where a People's Court, upon eliminating reasonable doubts, rules that the case constitutes an independent letter of guarantee fraud and that the circumstances set out in the third paragraph of Article 14 of these Provisions do not exist, the People's Court shall order that the issuer should terminate payment of the amount demanded under the independent letter of guarantee."

5.2 Authoritative Jurisprudence of the Supreme Court

5.2.1 Supreme Court's Position in the Himalayan Bank Case

According to the "Himalaya Case" announced by the Supreme Court, in the "Australia and New Zealand Bank case", the applicant under the independent guarantee or standby letter of credit claims that the beneficiary has committed fraud under the guarantee, and the standard of proof should reach the level of "beyond a reasonable doubt".[1] The opinion of the judgment is quoted as follows:

Article 6 of the Provisions of Supreme People's Court on Several Issues Relating to the Hearing of Disputes over Independent Letter of Guarantee stipulates: "Where there is ostensible compliance between the documentation submitted by the beneficiary and the clauses of the independent letter of guarantee, or ostensible compliance between documentation, if the beneficiary claims that the issuer should undertake payment liability in accordance with the independent letter of guarantee, the People's Court shall uphold the claim." The people's court shall not support the issuer's defense

against the payment obligation based on the basic transaction relationship or the independent guarantee application relationship, except in the case of Article 12 of these Provisions.

This article embodies the system value of "demand payment" of independent guarantee, and maintains the commercial function of "first compensation, then dispute" of independent guarantee. The bank issuing the independent guarantee is only responsible for examining whether the documents submitted by the beneficiary conform with the terms of the guarantee and has the right to decide whether to pay or not. The payment obligation of the guaranteeing bank is not affected by the right of defense under the underlying transaction between the principal and the beneficiary. Therefore, the people's court should adhere to the principle of limitation and necessity in the examination of basic transactions.

According to the facts ascertained in the original examination, in the independent guarantees issued by Himalayan Bank and Bank of Kathmandu respectively, it is stated that "Himalayan Bank hereby irrevocably undertakes the following payments, after receiving the written request and written statement of Melamchi Board, reflecting that the contractor has violated its contractual obligations, without the need for Melamchi Board to certify the situation and the required amount. Himalayan Bank will pay ...","The Bank of Kathmandu hereby irrevocably undertakes that upon receipt of a written demand from the Melamchi Board and a written statement that the Contractor has breached its contractual obligations by using the advance payment for purposes other than project mobilization, the Bank of Kathmandu will pay."

Therefore, on the premise that both parties have disputes over the performance of the basic contract and that there is no arbitration award or effective judgment to clarify and identify the rights and obligations of both parties in the performance of the contract, the Melamchi Commission claims that the 15th Bureau of China Railway is in breach of the contract and sends it to Himalayan Bank and Kathmandu Bank in accordance with the advance payment guarantee and the performance guarantee. The amount claimed under the letter of guarantee conforms to the terms of the letter of guarantee, and the Melamchi Commission cannot be deemed to have abused the right "knowing that there is no right to claim for payment".

China Railway 15th Bureau failed to submit sufficient evidence to prove that Melamchi Board's claim for payment was subject to fraudulent claims as stipulated in Article 12 of the Provisions on Independent Guarantee, and the original judgment did not support China Railway 15th Bureau's claim that Melamchi Board constituted guarantee fraud. The determination of facts and applicable laws was correct. Therefore, the reasons for the retrial application of the 15th Bureau of China Railway are that the Melamchi Committee constitutes a guarantee fraud that cannot be established.

5.2.2 The Position of the Supreme Court in an Authoritative Case Involving the Standstill of Standby Letters of Credit

The first instance of the letter of credit fraud disputes between China National Electric Engineering Corporation (CNEEC) and Manila Branch of Australia and New Zealand Banking Group Co., Ltd. (ANZ Manila Branch) was heard in the first instance of the Commercial Division of the Supreme Court. It is even clearer that:

"After further hearing, the evidence submitted by CNEEC on the fraud of the ANZ Manila Branch

did not meet the standard of proof beyond a reasonable doubt stipulated in Article 20 of the Independent Guarantee Provisions."

In the latest and most authoritative standby letter of credit case of the Commercial Court of the Supreme Court, CNEEC v. ANZ Manila Branch and other letter of credit fraud disputes, [2]The Supreme People's Court and the People's Court have made the following detailed explanations on the standard of proof of "beyond reasonable doubt" stipulated in the judicial interpretation of independent guarantee:

" (2) Whether the ANZ Manila Branch has committed fraud as stipulated in Item 5 of Article 12 of the Provisions on Independent Guarantees."

The fifth clause of Article 12 of the Provisions on Independent Guarantee provides that "any other circumstances where the beneficiary is aware that it has no right to demand payment and yet still abuses such right". Under this provision, if a beneficiary requests payment with knowledge that no right to payment exists, the request constitutes an abuse of the right and amounts to fraud.

The Court holds that, although strictly speaking, in cases of fraud involving abuse of the right to claim for payment, the time for assessing the beneficiary's subjective malice should be limited to the moment the claim is made, in practice the beneficiary's subjective state may change. If the beneficiary believes in good faith that the right to claim for payment exists at the time of the claim but later learns that the right has been lost, and still refuses to withdraw the claim, this can be considered fraud, because at that point there is no legal interest that should be protected.

However, in this case, the Jiangsu Bank should have paid US $22,979,687.50 under the Counter Guarantee Standby Letter of Credit based on the ANZ Manila Branch's claim, but it paid only US $7,313,543.30. The right of the ANZ Manila Branch to claim payment from Jiangsu Bank has not been extinguished.

Kang Songji Company and the ANZ Manila Branch signed the Settlement Agreement on May 11, 2017. They issued the Letter of Abandonment/Certificate on September 13, 2017, promising to cancel the claim under the Standby Letter of Credit and acknowledging that the Standby Letter of Credit has expired and is no longer valid. The right of the ANZ Manila Branch to claim payment under the Counter Guarantee Standby Letter of Credit shall not be affected. Because the Settlement Agreement resolves the claim under the Standby Letter of Credit rather than the Counter-Guarantee Standby Letter of Credit, and because it stipulates that the ANZ Manila Branch should pay 6 million$ to Kang Songji Company, the claim letters under the Standby Letter of Credit involved in the case and the Standby Letter of Credit of China National Technical Import and Export Corporation (CNTIC) were returned to Kang Songji Company with the seal of "cancellation", and Kang Songji Company unconditionally and irrevocably released the claims, liabilities, and lawsuits against the ANZ Manila Branch under the two Standby Letters of Credit after receiving US $6 million. That is to say, Kang Songji's promise to waive the claim against the ANZ Manila Branch is based on the premise that the ANZ Manila Branch pays the consideration of US $6 million.

In essence, the claim amount is reduced to US $6 million, and the remaining unpaid part of the claim is withdrawn. The US $6 million actually paid by the ANZ Manila Branch does not fall within the scope of the withdrawal of the claim. As the Counter Guarantee Standby Letter of Credit is

independent of the Standby Letter of Credit, the payment obligation of Jiangsu Bank under the Counter Guarantee Standby Letter of Credit is not extinguished by the repayment arrangement of the Standby Letter of Credit.

CNEEC also contended that the lawyer's letter sent by ANZ Manila Branch to Jiangsu Bank on July 19, 2019, requesting payment of US $6 million, was a new claim made by ANZ Manila Branch in bad faith under the Counter Guarantee Standby Letter of Credit. It should be noted that there was only one claim and presentation under the Counter Guarantee Standby Letter of Credit in this case, namely the Compliant Claim filed by ANZ Manila Branch on November 27, 2015, which has not been fully satisfied and has not lapsed. The nature of the lawyer's letter is to urge Jiangsu Bank in writing to perform the payment obligations claimed under the Counter-Guarantee Standby Letter of Credit, which does not constitute a new claim. The lawyer's letter indicated that the claim amount was reduced from US $15,666,144.20 to US $6 million, which was a voluntary waiver of part of the claim amount and was not a new claim.

Jiangsu Bank also said that the Settlement Agreement signed by Kang Songji Company and ANZ Manila Branch included not only the Standby Letter of Credit involved in the case, but also the Standby Letter of Credit of CNTIC, but the Settlement Agreement was not a matter to be examined as stipulated in the Counter-Guarantee Standby Letter of Credit, which was based on the standby letter of credit transaction. Jiangsu Bank has no right to use the Settlement Agreement to defend its payment obligations under the Counter-Guarantee Standby Letter of Credit.

To sum up, CNEEC claims that ANZ Manila Branch is involved in the frauds specified in Item 4 and Item 5 of Article 12 of the Independent Guarantee Provisions, but the evidence provided by ANZ Manila Branch fails to meet the standard of proof beyond reasonable doubt specified in Article 20 of the Independent Guarantee Provisions, so CNEEC's claim cannot be established, and the Court does not support it. (Emphasis added by author.)

According to this authoritative case, to request termination of payment under standby letters of credit on the grounds of beneficiary fraud or abuse of rights exception, the plaintiff's proof must meet the standard of "beyond a reasonable doubt." However, the evidence of the appellee in this case is far from meeting this standard.

6. The Sixth Legal Principle: the "Limited Review" of the Underlying Contract by the Chinese Court Shall Not Exceed the Scope of "Limited and Necessary".

6.1 Provisions of Judicial Interpretation of Independent Guarantee

Article 18 of the judicial interpretation stipulates: "A People's Court trying an independent letter of guarantee fraud or dispute case or handling an application for suspension of payment may examine and verify the facts relevant to the underlying transaction, based on the specific circumstances set out in Article 12 of these Provisions as claimed by the party concerned."

The judicial interpretation of independent guarantee only provides for "limited review" of the underlying contract in Article 18. Still, this principle has been unexpectedly interpreted and developed into the principle of "limited and necessary review" in later cases. However, since then, the Supreme Court has not followed this "limited and necessary " principle in a large number of authoritative cases, but has supported the "limited review principle."[3] The jurisprudence of other

high courts has not followed this "development," which is not in line with the original drafting intention. In the case before the judicial interpretation came into effect, it was the second instance civil judgment (November 4, 2013) of Tianjin Higher People's Court "Appellant Gribwal Cement Co., Ltd. v. Appellee China Material Equipment Group Co., Ltd., Appellee Industrial and Commercial Bank of China Co., Ltd. Tianjin Branch Guarantee Fraud Dispute". The second instance judgment of the case was supported by the retrial review ruling of the Supreme Court.

6.2 Authoritative Jurisprudence of the Supreme Court

6.2.1 Position of the Supreme Court in the Reconsideration of the Russian CCB Case

The Supreme Court made it clear in the judgment that the ruling was brought up for retrial：[4]

"The Court holds that the independent guarantee and the underlying transaction, the guarantee and the counter-guarantee, are independent of each other, and the litigation under the underlying transaction and the underlying transaction should be examined only in a limited way." Shenyang Yuanda did not provide evidence to prove that the claim of CCB Esentepe Branch under the counter-guarantee letter constituted the situation stipulated in Article 12 of the Independent Guarantee Provisions, so it could not be concluded that the claim of CCB Esentepe Branch under the counter-guarantee letter constituted fraud.

6.2.2 Position of the Supreme Court in the Ruling of "Yiwu Industrial and Commercial Bank of China Retrial Case."

The Supreme Court explored into the issue of limited examination of the facts related to the underlying transaction in the Yiwu Industrial and Commercial Bank of China (Yiwu ICBC) retrial case.

Article 18 of the Judicial Interpretation of Independent Letter of Guarantee stipulates: "A People's Court trying an independent letter of guarantee fraud or dispute case or handling an application for suspension of payment may examine and verify the facts relevant to the underlying transaction, based on the specific circumstances set out in Article 12 of these Provisions as claimed by the party concerned."

This article sets out the principle of limited review in the case of independent guarantees. The word "may" in this provision indicates that the people's court may decide, based on the specific circumstances of the case, whether to examine the relevant facts of the underlying transaction, rather than being required to do so.

In this case, the second-instance court examined some facts of the underlying contract and transaction and also preliminarily examined Zhonggao Company's breach of contract, which was consistent with the above judicial interpretation. Yiwu ICBC claims that the second-instance judgment failed to conduct a limited review, which is inconsistent with the facts of the case and the above judicial interpretation.

7. The Seventh Legal Principle: the Subject Applying for an Injunction Should Be Qualified. Only the Issuing Applicant and the Issuer Itself Can Apply for a Stop Payment Order, and the Issuing Guarantor or Other Interested Parties Are Not Qualified to Apply for an Injunction.

7.1 Provisions of Judicial Interpretation of Independent Guarantee

According to the provisions of Article 13 of the judicial interpretation of the independent guarantee: "Upon becoming aware of the circumstances set out in Article 12 of these Provisions, the applicant, the issuer or the instructing party for an independent letter of guarantee may, prior to filing of lawsuit or applying for arbitration, apply to the People's Court at the place of residence of the issuer or a People's Court with jurisdiction for independent letter of guarantee fraud and dispute cases, to suspend payment of the amount under the independent letter of guarantee, or may make an application during the litigation or arbitration proceedings." An application may also be filed in the course of litigation or arbitration.

7.2 Supreme Court Jurisprudence

In 2022, the Supreme People's Court issued a civil retrial ruling (2021) Supreme Fa Min Shen No.5896 on the "Independent Guarantee Case of China Railway 15th Bureau", which held that only the performing party that bears the performance liability under the basic contract is a qualified plaintiff.[5]

8. The Eighth Legal Principle: The Payment of the Standby Letter of Credit (independent Guarantee) Can Not Provide Effective Judicial Relief: Two History Cases Involving the Bank of China

8.1 Case 1: Parallel Litigation Between Shandong Court and English Court on Independent Guarantee: "Rushan Shipyard Case."

According to the Shandong High People's Court (2015) LSCZ No. 71, "Bank of China Limited Shandong Branch v. China Electronics Import and Export Shandong Company, Rongcheng Xixiakou Shipping Co., Ltd. and Xixiakou Group Co., Ltd.," even if a Chinese court permanently suspends payment on a letter of guarantee or standby letter of credit, the British court does not recognize it. The British court can still enforce the Bank of China's assets in the UK. As Australia also belongs to the Commonwealth, the United Kingdom's case law is applicable.

Therefore, even if a standby letter of credit is involved in a permanent injunction case in a Chinese court, the Australian court can still enforce the Bank of China's assets in Australia to satisfy the judgment. The quotation is as follows:

"After the Qingdao Maritime Court made a ruling to suspend payment, the Shandong Branch of the Bank of China did not take the initiative to pay the guarantee. Because the Shandong Branch of the Bank of China refused to pay, the West Ford Company sued the head office of the Bank of China in the British court, which ruled that the head office of the Bank of China should pay the amount under the letter of guarantee. If the head office of the Bank of China did not perform the judgment, it would not only damage its financial reputation, but also the judgment would not be recognized and enforced in China. The West Ford Company can apply for the execution of the overseas assets of the head office of the Bank of China in the British courts. Therefore, the head office of the Bank of China

was forced to fulfill the judgment through the London branch. Payment by Bank of China Head Office through the London Branch is equivalent to the payment by Bank of China Shandong Branch under the Letter of Guarantee. It can be seen from the above facts that the payment of the amount under the letter of guarantee by the Shandong Branch of the Bank of China is not intended to violate the ruling of litigation preservation made by the Qingdao Maritime Court, but is caused by the performance of the judgment of the British court by the Shandong Branch of the Bank of China after the change of the objective situation. In this regard, the Shandong Branch of the Bank of China has no fault in paying the amount under the letter of guarantee. "

8.2 Case 2: Guangzhou Intermediate People's Court and Hong Kong Court Parallel Litigation Case: " Guangzhou Intermediate People's Court Case of BOC."

In its first-instance judgment in the "Thermal Power Company and Atalat Company Guarantee Fraud Case," the Guangzhou Intermediate People's Court held that the issuing bank's payment obligation under the guarantee is independent of any right of defense under the underlying contract, and that the issuing bank needs only to examine the documents under the guarantee agreement. As long as the documents are consistent, the issuing bank is obliged to pay the amount of the guarantee. Because the Hong Kong ICC has made a 28089/XZG ruling under the guarantee in this case, confirming the payment obligation of the Guangdong Branch of the Bank of China, the court rejected the thermal power company's request to terminate payment under the guarantee. The quotation is as follows:

"In the case of 28089/XZG applied for arbitration by Atalat Company, the Hong Kong ICC has made an arbitration award stating that the Guangdong Branch of the Bank of China has violated the independent guarantee and that the Guangdong Branch of the Bank of China shall pay the amount under the independent guarantee and interest to Atalat Company." Therefore, there is sufficient basis for Atalat Company to request payment from the Guangdong Branch of the Bank of China. The letter of guarantee is independent of the underlying transaction. As the issuer of the letter of guarantee, the Bank of China Guangdong Branch is responsible only for reviewing whether the documents submitted by Atalat Company conform to the provisions of the letter of guarantee. It has the right to decide whether to pay. The payment obligation of the Bank of China Guangdong Branch is not affected by any right of defense under the underlying transaction between Thermal Power Company and Atalat Company. Furthermore, even if the arbitration award between Thermal Power Company and Atalat Company on the underlying transaction finds that Atalat Company constitutes a breach of contract under the EPC Contract, a breach of contract does not necessarily constitute a sufficient and necessary condition for guarantee fraud."

9. Conclusions and Suggestions of This Paper

9.1 Conclusion

It can be concluded from the Chinese law listed in this article, especially the judicial interpretation of the independent guarantee of the Supreme Court of China and the past cases of the Supreme Court, that although it is relatively easy to obtain a temporary stop payment order in China, in terms of the conditions for obtaining a permanent stop payment order, the Chinese law is extremely strict. Judging from the Supreme Court's cases so far, only a few cases have succeeded in obtaining a permanent injunction of payments, and almost all other cases have been rejected by the Supreme Court.

The Supreme Court's problem with the Permanent Injunction appears to reflect the "layman's" understanding of the judge or collegial panel of independent guarantee cases towards the unique legal and banking practice rules governing the independent guarantee. This is mainly due to the Supreme Court's lack of experience in hearing disputes in this field and to a lack of understanding of the unique legal system of independent guarantee, which is still under development in international rules and the judicial practice of various countries.

9.2 Recommendations

The analysis of Chinese law and the Supreme Court in this paper shows that the Chinese court must be cautious in initiating the procedure of a permanent injunction, and must make special, solid preparations in sorting out the facts of the case and preparing evidence. Otherwise, it is better to settle than to start the proceedings easily.

Another important lesson and suggestion is that the judgment of the lawsuit case concerning the permanent injunction of the independent guarantee is a bit like "opening a blind box": the result of the case depends on whether the judge or collegial panel hearing the case is professional and reliable, even in the Supreme Court, which represents the highest level of international commercial trial in China. There are not a few cases of unreliable or clearly wrong judgments. This shows that there is a huge risk of uncertainty inherent in the outcome of litigation in courts at all levels in China. This represents a significant litigation risk that warrants close attention.

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He is a member of the Chinese delegation to Working Groups VI and V of the UNCITRAL Model Law on Secured Transactions in Movable Property and Model Law on Insolvency Law. Observer for the Working Group on the Drafting of a Model Law on Factoring (MLF), Rome Institute of Private International Law (UNIDROIT). Member of the Legal Committee (LC) of the International Factoring Association (FCI). Member of the Academic Committee of the Commercial Factoring Committee of the Academy of Trade in Services of the Ministry of Commerce. The English version of this article has been reviewed by Jin Dian (NYU intern), as well as Gu Haoran, a lawyer from the Jin Saibo's team.

1 On December 1, 2023, the Supreme People's Court, Case No.: (2023) Supreme Fa Min Shen No.1393, China Railway 15th Bureau Group Co., Ltd.) and China Construction Bank Corporation Henan Branch, Himalayan Bank Co., Ltd., Bank of Kathmandu Co., Ltd., Melamchi Water Supply Development Committee Independent Guarantee Fraud Dispute Retrial Civil Ruling, Collegial panel: Ma Dongxu, Chen Hongyu, Shen Jia.

2 Supreme People's Court "China Power Engineering Co., Ltd., Australia and New Zealand Banking Group Limited Manila Branch, etc. L/C Fraud Dispute Case" Civil Judgment of First Instance (August 24, 2023), (2020) Supreme Law No.2, Presiding Judge Shen Hongyu, Judge Xi Xiangyang, Judge Sun Xiangzhuang, Judge Yu Xiaohan, Judge Guo Zaiyu.

3 For example, the Civil Ruling of the Supreme People's Court on Retrial Review and Trial Supervision of the Dispute over Letter of Credit Fraud between Yiwu Branch of Industrial and Commercial Bank of China Limited and China National Technical Import and Export Corporation [Function of Independent Guarantee for Advance Payment and Beneficiary's Right to Claim] (December 28, 2017). Only Beijing is the first intermediate people to follow this standard in three cases of the same batch. See the Civil Judgment of the Second Instance of Beijing First Intermediate People's Court on the Dispute over the Guarantee Contract between Beijing Triumph Building Materials Engineering Co., Ltd. and Metallurgical Corporation of China Limited (December 15, 2021) (Judgment No.2425). Beijing First Intermediate People's Court "Beijing Triumph Building Materials Engineering Co., Ltd. and China Metallurgical Science and Technology Co., Ltd. Guarantee Contract Dispute Case" Civil Judgment of Second Instance (December 15, 2021) (Case No.2424). Beijing Triumph Building Materials Engineering Co., Ltd. and Ningbo Bank Co., Ltd. Beijing Branch and other guarantee contract disputes, the second instance civil judgment (December 15, 2021) (case No.2426).

4 On August 26, 2020, the Supreme People's Court issued the (2020) Supreme Fa Min Zai No.265 "Civil Judgment on Retrial of Letter of Credit Fraud Dispute between China Construction Credit Bank Co., Ltd. Esentepe Corporate Banking Center Branch and Shenyang yuanda Aluminum Engineering Co., Ltd.", collegial panel: Ma Dongxu, Li Guishun, Guo Zaiyu.

5 On December 12, 2022, the Supreme People's Law, Case No. (2021) No.5896, the contract disputes between Shenzhen Branch of China Construction Bank Co., Ltd., Sichuan Ganheng Construction Engineering Co., Ltd. and Shenzhen Branch of China Railway Fifteenth Bureau Group Co., Ltd., and the Third Party Chang'an Guarantee Co., Ltd. Members of the collegial panel: Ren Xuefeng, Ma Dongxu, Shen Jia.

Cost Management Tools in International Arbitration

Part One: Sealed Offer (Calderbank Offer)

Vera Zuo, Li Zhuangyi

Abstract

As Chinese enterprises expand overseas, cross-border disputes are becoming increasingly common, and international arbitration has become an increasingly important means of alternative dispute resolution (ADR). Compared with domestic litigation in China, international arbitration often involves higher amounts in dispute, more complex procedures, longer proceedings and greater legal costs. Managing costs risks throughout the proceedings has therefore become an important consideration for Chinese enterprises and their legal counsel.

International arbitration offers various procedural tools to help parties manage these risks. Drawing on international arbitration practice, this series of articles explores these tools and how they can be used effectively. As the first article in the series, this piece focuses on sealed offers, also known as Calderbank offers. It examines how they work and how parties can use them to influence costs allocation by combining settlement strategy with effective management of procedural costs.

I. What is Sealed Offer?

Influenced by the common law principle that "*costs follow the event*", international arbitral tribunals will generally order the unsuccessful party to bear the successful party's reasonable arbitration costs and legal costs. However, the outcome on the merits is not the sole determinant of costs allocation. Tribunals retain discretion to take into account other relevant factors, including the parties' procedural conduct, when determining costs. It is this discretion that provides the basis for the use of sealed offers, also known as Calderbank offers, in international arbitration.

The sealed offer/Calderbank offer originated from the English case of *Calderbank v Calderbank*[1] and was subsequently adopted in international arbitration. It allows a party to make a settlement offer during the proceedings without disclosing it to the tribunal until the merits have been determined. If the offer is rejected and the award on the merits is less favorable to the rejecting party than the terms of the offer, the offering party may rely on the rejected offer and argue that the rejecting party should bear some or all of the costs incurred after the offer was made, as those costs could have been avoided had the offer been accepted.

For example, suppose a claimant brings an arbitration claim for US$10 million and the tribunal ultimately awards it US$6 million. Although the claimant has succeeded on the merits, the respondent might ordinarily be expected to bear most or all of the arbitration costs and legal costs. If, however, the respondent made a sealed offer/Calderbank offer of US$7 million early in the proceedings and the claimant rejected it, the respondent may submit that offer to the tribunal at the costs stage and argue that, arbitration could have been concluded without further proceedings had the claimant accepted that offer. The claimant's refusal was therefore economically unreasonable. On that basis, the respondent may seek an order requiring the claimant to bear both parties'

arbitration costs and legal costs incurred from the date on which the sealed offer expired.

It should be emphasized that a sealed offer/Calderbank offer does not automatically result in a shift in costs liability. Rather, it is one of the factors informing the tribunal's exercise of its discretion on costs. Whether, and to what extent, the tribunal gives weight to the offer depends on an assessment of all the circumstances, including when the offer was made, whether its amount and terms were reasonable, and how the award on merit compares with the sealed offer/Calderbank offer. Therefore, the value of a sealed offer/Calderbank offer lies not only in its potential to facilitate settlement, but also in establishing a benchmark for the tribunal's costs decision, allowing the economic reasonableness of a party's decision to continue the arbitration to be taken into account in the final allocation of costs.

II. How to Design Sealed Offer?

In several international arbitration cases we have handled recently, we have advised on the use of the sealed offer/Calderbank offer and the sealed counteroffer/Calderbank counteroffer. Whether, and to what extent, the tribunal takes such offers into account when allocating costs depends heavily on the amount, timing and wording of the sealed offers/Calderbank offers. Their formulation therefore requires a careful assessment by counsel experienced in international arbitration, taking into account the merits of the dispute, the evidential position of each party, the stage of the proceedings and the client's commercial objectives.

First, the amount of a sealed offer/Calderbank offer should be determined following a careful assessment of the merits and the client's willingness to settle. It should not be set artificially high or low simply to secure a costs advantage.

For example, suppose the claimant claims US$10 million and the respondent assesses its likely exposure at approximately US$5 million. If the respondent makes a sealed offer/Calderbank offer of US$8 million, this may help mitigate future costs and increase the likelihood of acceptance. However, if the claimant accepts the offer, the respondent would have to settle the dispute for an amount exceeding its own assessment of its likely exposure.

Conversely, if the amount of the sealed offer/Calderbank offer is too low (e.g. US$2 million), it may lack commercial appeal to the claimant. Moreover, if the tribunal ultimately awards around US$5 million, the amount of the award would substantially exceed the amount of the sealed offer/Calderbank offer, limiting its effectiveness in shifting costs.

Therefore, a sealed offer/Calderbank offer should be a genuine settlement offer first and foremost, rather than merely a procedural device designed to secure a favorable costs order. In determining the amount, the offering party must strike a careful balance among the merits of the dispute, the client's settlement willingness and the potential costs implications.

Second, the timing of a sealed offer/Calderbank offer should be aligned with the progress of the arbitral proceedings. If a sealed offer/Calderbank offer is made too early in an attempt to maximize the costs that could be shifted, the parties may not yet have a sufficient understanding of the evidence, liability and quantum, making it difficult for the offeror to assess a reasonable settlement range. If the sealed offer/Calderbank offer is made too late, most arbitration costs and legal costs will already have been incurred, leaving fewer future costs that may be shifted through the sealed

offer/Calderbank offer and diminishing its value as a costs management tool.

Therefore, there is no single, universally appropriate point in the arbitral proceedings at which to make a sealed offer/Calderbank offer. The conclusion of pleadings, document disclosure or the exchange of expert reports, as well as the period before the hearing, may each present a suitable opportunity. The key is whether the offeror has sufficient information to assess the risks and likely course of the case, while the remaining proceedings are still expected to generate substantial additional costs.

Third, the terms of a sealed offer/Calderbank offer should be clear and enforceable, avoiding any ambiguity that could undermine its intended effect on costs allocation. Generally, the offer should be expressly marked "*without prejudice save as to costs*". It should also specify the acceptance deadline, settlement amount, payment terms, treatment of costs and interest, and any arrangements concerning disclosure to the tribunal and confidentiality, etc.

Fourth, a party receiving a sealed offer/Calderbank offer is not limited to accepting or rejecting it; it may instead manage its costs exposure by making a sealed counteroffer/Calderbank counteroffer. If the receiving party considers the sealed offer/Calderbank offer lower than a reasonable valuation of the claim but wishes to preserve the potential for costs shifting, it may consider making a sealed counteroffer/Calderbank counteroffer. This allows the party to maintain its position on the merits while establishing a further benchmark for the allocation of arbitration costs and legal costs.

III. Insights

We have observed that Chinese enterprises expanding overseas often approach international arbitration primarily in terms of winning or losing on the merits, paying relatively little attention to costs management. Complex international arbitrations can last several years and incur substantial legal and expert fees. Parties should therefore consider not only the merits of their claims and defences, but also how to mitigate their financial exposure if the proceedings do not unfold as expected.

For enterprises involved in international arbitration, strategy should extend beyond predicting the outcome on the merits to encompass ongoing risk management throughout the proceedings. An initial assessment of the merits and key risks should be undertaken early in the case. As pleadings are exchanged, documents are disclosed and expert evidence is submitted, assessments of liability and quantum should be updated promptly. At appropriate stages of the proceedings, enterprises should consider using available procedural tools to adjust and manage their risk exposure.

Against the backdrop of rising international arbitration costs, sealed offers/Calderbank offers serve not only as a means of facilitating settlement but also as a tool for managing costs risks throughout the proceedings. Used effectively, they can help enterprises pursue commercially sensible resolutions to their disputes and manage their costs exposure at an early stage, providing greater protection against financial uncertainty while the outcome of the case remains uncertain.

1 *Calderbank v Calderbank* [1975] 3 All ER 333

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