

# THE DELICATE ART OF MED-ARB AND ITS FUTURE INSTITUTIONALISATION IN CHINA

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*Mediation is a participatory intervention process wherein disputing parties work with a third party, the mediator, to negotiate a resolution of their conflict. Arbitration is the most formal alternative to court adjudication wherein disputing parties present their case to one or more impartial third persons whom are empowered to render a binding decision. Med-arb refers to the hybrid process in which mediation is combined with arbitration. A narrower, more internationally recognized definition of this term refers to situations in which a party decides to employ the processes of both mediation and arbitration in a single case. The mediator(s) and arbitrator(s) are typically independent, and the mediation and arbitration proceedings operate independently.<sup>1</sup> However, a more Chinese oriented definition of med-arb refers to any hybrid process of mediation and arbitration. It does not matter if the arbitral tribunal or an arbitrator takes over the mediation itself, or if an arbitrator plays the dual (and often conflicting) role of mediator.<sup>2</sup> This relatively broad Chinese conception of med-arb concerns many in the Western world, who have reservations about allowing arbitrators to act simultaneously as mediators.*

*In Asia, med-arb is gaining popularity. Among other jurisdictions, Japan, Hong Kong, and Singapore have recently enacted particular*

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1. See, CARLOS DE VERA, "Arbitrating Harmony: 'Med Arb' and the Confluence of Culture and Rule of Law in the Resolution of International Commercial Disputes in China", 1 (2004) 18 *Columbia Journal of Asian Law*, pp. 155-157.

2. *Ibid.*

provisions requiring med-arb to employ proper procedural standards.<sup>3</sup> It is in this context that the delicate Chinese art of med-arb is being challenged. One major question that has been raised is whether the Chinese practice of med-arb is compatible with the rule of law. The usual med-arb proceedings in China often do not meet due process standards, prohibiting actual and apparent bias, as well as ensuring confidentiality. This paper reviews the regulatory landscape of med-arb in China in the context of the current Chinese practice (by China's flagship arbitration institution, China International Economic and Trade Arbitration Commission, CIETAC, and other local arbitration commissions). In light of the dominance of the med-arb process in commercial dispute resolution in China, and drawing on international experience, this paper proposes an improved institutionalisation of the system with proper procedural safeguards. This paper concludes that the institutionalisation of med-arb bears significant relevance to China's goal to establish rule-of-law because med-arb is a broadly-used system in a jurisdiction with a booming economy and burgeoning commercial disputes, yet, without established due process traditions. Accordingly, effective procedural safeguards for this system will eventually have a broad impact on Chinese dispute resolution as a whole.

## I. INTRODUCTION

In light of China's remarkable economic growth over the past few decades, there has been a dramatic, corresponding increase in the number of commercial disputes. A significant portion of these disputes are resolved through alternative dispute resolution. The leading arbitration institution in China, the China International Economic and Trade Arbitration Commission (CIETAC), reported that the total number of cases it accepted in 2013 was 1256, nearly twice the number of cases it accepted in 2000.<sup>4</sup> The emergent need to resolve disputes efficiently, coupled with China's long-standing tradition of mediation, created the opportunity for China's hybrid system of mediation and arbitration (med-arb) to thrive. Currently, CIETAC resolves approximately 20% to 30% of its caseload through med-arb.<sup>5</sup>

In an effort to promote the timely settlement of commercial disputes, China has attempted to reform its laws governing alternative dispute resolution. After the Arbitration Law came into effect in 1995, several big cities including Beijing, Shanghai, and Shenzhen were designated as pilot cities for the establishment of local arbitration commissions. Since 1995, more than 200 arbitration commissions have been established in China, including CIETAC and the various local arbitration

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3. Michael Pryles (ed), *Dispute Resolution in Asia* (3<sup>rd</sup> ed) (Kluwer Law International, 2006), pp. 15-17.

4. Statistics of CIETAC, available at <http://cn.cietac.org/AboutUS/AboutUS-4Read.asp>

5. Paul E. Mason, Follow-Up Note to 'The Arbitrator as Mediator, and Mediator as Arbitrator' (2011), *J. Int. Arb.* 6, 541.

commissions.<sup>6</sup> However, despite these attempts and the growth of arbitration institutions, there are still significant problems with the system. China's dispute resolution system is often criticized by both users of the system and observers of the system both at home and abroad, for its lack of concern for due process. The recent case of *Gao Haiyan v Keeneye Holdings Ltd*, in which the Hong Kong High Court challenged a med-arb award in enforcement proceedings, is a typical example of how the usual med-arb practice in China does not conform to procedural safeguards that protect against actual and apparent bias.

In the *Keeneye* case, the Hong Kong Court of Appeal reversed a Court of First Instance<sup>7</sup> decision, which refused to enforce an award rendered pursuant to med-arb proceedings in Xi'an, mainland China. The arbitration spanned two sessions, during which mediation took place as agreed by the parties upon the suggestion of the arbitration tribunal over a dinner at a Xi'an hotel.<sup>8</sup> During mediation, there was a private meeting between an arbitrator nominated by the applicants, the Secretary General of the Xi'an Arbitration Commission, and an affiliate of the respondents who was told to "work on" a RMB 250 million proposal with the respondents. Following an unsuccessful mediation, the tribunal resumed arbitration proceedings and rendered an arbitral award of RMB 50 million, an amount much lower than that proposed during the mediation. The Hong Kong Court of First Instance refused to enforce the award on the ground that the award was tainted by the appearance of bias.<sup>9</sup> It appeared to the court that the mediators first pushed for a favourable result for the applicants, and when the respondent refused to cooperate, the mediators-turned-arbitrators penalized the respondents with an adverse judgment in arbitration. The Court of Appeal reversed this decision, holding that apparent bias had not been sufficiently proven to warrant a refusal to enforce the award.<sup>10</sup> This case highlights the inherent difficulties in med-arb proceedings in China, especially with respect to more informal modes of mediation such as those ever popular "working on" parties taking place over dinners (做工作). This is crucial, as parties who opt for arbitration in China are often highly encouraged to adopt mediation within arbitration for amicable settlement. Yet, outcomes flowing

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6. In 2010, there were 209 arbitration commissions in China. See <http://www.cietac.org/index/news/4772c81b4d672a7f001.cms>.

7. The Court of First Instance of the High Court of the Hong Kong Special Administrative Region (referred to as the "Court of First Instance") is one of the two courts in Hong Kong's High Court, the other being Court of Appeal. The Court of First Instance, pursuant to the Hong Kong Arbitration Ordinance, receives application for enforcement of arbitration awards.

8. Paras 5, 17 of the judgment of the Court of First Instance (HCCT 41/2010). The two arbitration settings occurred on 21 December 2009 and 31 May 2010 respectively, whereas the unsuccessful mediation by the Arbitral Tribunal took place on 27 March 2010.

9. Paras 52-69, 100, 102 of the judgment of the Court of First Instance (HCCT 41/2010).

10. Paras 104-106 of the judgment of the Court of Appeal.

from the med-arb proceedings might run the risk of non-enforcement, thus rendering the arbitration award ineffective.

One of the defining characteristics of Chinese med-arb is the dual role of arbitrators and mediators. In order to enhance efficiency, mediation in China is often conducted by the arbitrator(s) of a case. The rationale for this approach is that the arbitrator who participated in the mediation becomes familiar with the case in the course of mediation. If mediation fails, the decision making process can be expedited and the dispute can be resolved sooner. In the absence of proper procedural safeguards, however, the impartiality of the arbitrator may be affected because he or she participated in the mediation process.

Due to the absence of legislative provisions governing med-arb, med-arb practices vary greatly. Med-arb procedures in China highly depend on the arbitrators and local customs of the governing arbitration commissions. While some institutional arbitration rules provide for procedural safeguards against actual or apparent bias, such safeguards still fall short of the internationally recognized standard of impartiality.<sup>11</sup> In view of the dominance of med-arb in commercial dispute resolution in China, and drawing on international experience, this paper proposes that adopting proper procedural safeguards can improve the med-arb system.

Part II reviews the regulatory landscape of med-arb in China and evaluates the current procedural safeguards against actual or apparent bias in med-arb. Having established that current procedural safeguards are insufficient to ensure due process, Part III reviews the med-arb practices of various jurisdictions, and, more importantly, the legislative efforts in these jurisdictions to prevent actual or apparent bias. Drawing on international experience, Part IV studies the institutionalisation of the med-arb process in China and proposes regulatory safeguards to preserve the arbitrator's impartiality. Part V discusses the significance of med-arb in China's rule-of-law progress. This paper concludes that the future institutionalisation of med-arb is particularly relevant to China's efforts to establish rule-of-law, as med-arb is a widely-used system in a jurisdiction with a booming economy and burgeoning commercial disputes, yet, without established due process traditions.

## II. THE PARADIGM OF MED-ARB IN CHINA

Although China has made great efforts to improve its dispute resolution system, the current legal framework remains problematic. Two major shortcomings of China's legal system are its lack of procedural safeguards and lack of respect for due process. The dispute resolution system in China is said to be result oriented;<sup>12</sup> judges and arbitrators are often

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11. See for example Part II.B.2 for the International Bar Association's definition of "partiality" and Part III for the sample safeguards in other jurisdictions.

12. See for example Hualing Fu and Richard Cullen, "From Mediator to Adjudicator: Justice: The Limits of Civil Justice Reform in China", in Margaret Y.W. Woo and Mary E. Gallagher, *Civil Dispute Resolution in Contemporary China* (Cambridge

more concerned with the outcome of a case and pay little attention to the process of making their decisions. In med-arb, the mediator-turned-arbitrator tends to impose his or her opinions on the parties. The result-oriented approach suggests that med-arb in China will be conducted in a manner that makes it likely for the parties to be forced to accept a settlement proposal. This can occur in a number of ways, including the mediator's exertion of undue influence over a party or holding a private caucus with a party. Furthermore, if a result-oriented arbitrator considers the outcome of the case more important than the process of reaching the decision, he or she may be preoccupied with what he or she thinks is the "right" outcome, even though procedural rules require the arbitrator not to take into account things said during the mediation process.

Another criticism of Chinese med-arb is its extreme emphasis on efficiency. Following the economic boom, the volume of international business transactions in China, as well as the volume of international commercial disputes, has experienced a dramatic rise. CIETAC's caseload has almost doubled in the past 10 years.<sup>13</sup> As a result, the legal profession requires more efficient settlement of disputes. Decision makers are under time-pressures and tend to resolve cases in a manner that resolves disputes quickly without paying much attention to due process requirements.

For these reasons, med-arb in China fails to grant sufficient due process protections. The *Keeneye* case reflects some of the most common problems with med-arb in China. In *Keeneye*, the mediator asked a third party to "work on" one of the parties to accept a settlement proposal.<sup>14</sup> The phrase "work on" is capable of encompassing many different meanings. In the Hong Kong Court of First Instance judgment, the court took the view that the phrase "work on" insinuated that the party might have been actively pushed to accept the settlement proposal. This case also illustrates how mediators tend to involve third parties who are not parties to the proceedings in hopes of influencing decisions.<sup>15</sup> Arguably, this results in undue influence if a party agrees to the settlement proposal under economic pressure or other forms of pressure. Such unscrupulous practices have an adverse impact on the integrity of China's rule of law.

Given the popularity of med-arb in China, substandard med-arb practices are likely to have a significant impact on the general dispute resolution system. The lack of procedural safeguards in Chinese med-arb suggests a high risk of due process failure. Domestic arbitration is not the

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University Press, 2011), pp. 25-57. Fu and Cullen state the importance of substantive justice over procedural justice in the Chinese judicial system, which focuses on attaining socially desirable results.

13. See n 4 above.

14. Para 22 of the judgment of the Court of First Instance (HCCT 41/2010).

15. Para 22(3) of the judgment of the Court of First Instance (HCCT 41/2010). The third party involved in this case was an individual named Zeng, who happened to be a witness for the Respondents in other litigation proceedings. Members of the arbitral tribunal regarded Zeng as "friendly with the Respondents," so they asked him "to work on" the Respondents to urge them to accept the Tribunal's settlement proposal.

only jurisdiction tainted by improper practices. The lack of concern for due process also has an impact internationally when parties seek to enforce Chinese med-arb awards overseas.<sup>16</sup> There is thus an emergent need to build a better institutionalised system of med-arb practice in China.

A. *There Is a Flawed Legislative Framework for Med-Arb in China*

The lack of concern for due process in med-arb in China is attributable to the absence of uniform legislative requirements and procedural safeguards. The Arbitration Law of China, which was passed in 1994 and came into effect in 1995, is the first legislation pertaining to arbitration in China and aims to ensure the fair and timely settlement of commercial disputes while safeguarding the development of China's economy. Although the Arbitration Law spells out basic procedural rules for arbitration and mediation, there is no specific provision regulating the substantive, detailed rules of the actualized med-arb process; at most, certain provisions encourage the adoption of mediation within arbitration proceedings.<sup>17</sup>

In line with an emphasis on social harmony in the Chinese legal tradition, the Arbitration Law strongly encourages the practice of mediation during arbitration proceedings. When parties submit their disputes to arbitration, the arbitral tribunal may take the initiative to conduct mediation, even without a request to do so from the parties.<sup>18</sup> If the parties indicate their willingness to attempt mediation, the arbitral tribunal is *obligated* to conduct mediation.<sup>19</sup> To reduce concerns over the enforceability of a settlement agreement reached by this mediation, the Arbitration Law provides that the tribunal may render an award in accordance with the terms of a settlement agreement and that such an award has the same legal effect as an arbitral award enforceable internationally under the New York Convention.<sup>20</sup> The strong emphasis on med-arb in legislation has contributed to the frequent incorporation of mediation into arbitration proceedings in practice. While the Arbitration Law successfully encouraged the rise of med-arb, it failed to bring Chinese med-arb into compliance with internationally recognized due process standards.

The Arbitration Law provides little guidance regarding how med-arb should be conducted. The administrative regulations issued by the

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16. With China as a contracting state under the New York Convention, arbitral awards made in China are recognized and enforceable in other Contracting States. See Article I(3) of the New York Convention.

17. Articles 49 to 52 of the Arbitration Law endorses med-arb but it does not provide further guidelines on how it is to be carried out.

18. Article 51 of the Arbitration Law of China.

19. *Ibid.*

20. Article 49 of the Arbitration Law of China. China became a member of the New York Convention in 1986, making Chinese arbitral awards enforceable overseas. New York Convention refers to the Convention on Recognition and Enforcement of Foreign Arbitral Awards. States which are members to the New York Convention can render arbitral awards rendered in that state recognized and enforced in other member states to the Convention.

State Council<sup>21</sup> and the judicial interpretations and notices issued by the Supreme People's Court of China likewise do not address the med-arb process. In fact, major questions regarding whether the parties' consent is required in order to conduct med-arb, and exactly who is eligible to act as a mediator remain unanswered as do questions about procedural safeguards against bias.

In light of the absence of detailed operational provisions regarding how med-arb should be conducted, med-arb practices in China are highly disparate. How a given med-arb proceeding will be conducted depends on the arbitrators and the local customs of the relevant arbitration commission. As a result, med-arb in China is often conducted in an informal manner, which casts doubt on the impartiality of the arbitrators as well as the integrity of the proceedings as a whole.

B. *Lack of Procedural Safeguards under the Arbitration Commission Rules*

While the general provisions governing arbitration proceedings are laid down in the Arbitration Law, the detailed operational provisions are usually found in the rules of the local arbitration commissions. Following the enactment of the Arbitration Law, more than 200 local arbitration commissions have been reorganized or established throughout China. In light of the legal vacuum in which med-arb operates, the arbitration rules of these commissions have a significant impact on the practice of med-arb. Unfortunately, most arbitration rules only contain operational provisions regarding arbitration proceedings with very little attention paid to med-arb. Recent attempts to reform arbitration rules to address issues arising out of med-arb have not included sufficient procedural safeguards against actual or apparent bias.

Certain procedural concerns are particularly important. Firstly, unlike in other jurisdictions, the mediation process in China is often conducted by the tribunal itself. Secondly, the arbitrators' impartiality may be affected or arbitrators may appear to give off the appearance of impropriety by reason of caucusing. Thirdly, there is no requirement of confidentiality in the med-arb process, meaning that sensitive and confidential information divulged in private meetings may be exposed in subsequent arbitral proceedings.

1. The dual capacity of arbitrator(s) and mediator(s)

A typical set of arbitration rules for a Chinese arbitration commission contain a general provision conferring power upon the arbitral tribunal to mediate the case. For instance, article 39(1) of the Beijing Arbitration Commission (BAC) Rules provides that "the arbitral tribunal may, at the request of both parties or upon obtaining the consent of

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21. According to Article 85 of the Chinese Constitution, the State Council is the highest organ of state administration, i.e. Central Government.

both parties, mediate the case in a manner it considers appropriate.”<sup>22</sup> The problem with such a general provision is that the wording appears to suggest that the mediation is to be conducted by the arbitral tribunal itself. In fact, it seems to be the default position that a mediation suggested by a tribunal after the commencement of arbitration will usually be conducted by members of the tribunal. While the provision does not expressly prohibit other alternatives such as having a neutral third party conduct the mediation, in practice it is unlikely that a tribunal will involve a third party mediator unless the parties request a third party mediator. Sally Harlope takes the view that the wording of the arbitration rules is a main reason why mediations in China are often conducted by the arbitrator in the same case.<sup>23</sup>

In practice, there are additional reasons explaining why med-arb in China is often conducted by the arbitrators of the case. It is convenient for parties to appoint the arbitrators of their case as mediators. The parties or their counsel have likely already gained some knowledge of the arbitrators’ backgrounds or professional qualifications. From the parties’ perspective, it is both convenient and comfortable to appoint someone with whom they are familiar. However, the parties might not be aware of the possible conflict that may arise from arbitrators’ dual capacity. Doubts as to the arbitrators’ impartiality most often arise only if mediation fails. The arbitrator(s) will become familiar with the case while acting as mediator(s). This will allow the dispute to be resolved in a quicker manner in case mediation fails and the tribunal needs to render an award. The problem with the med-arb process in China thus becomes quite apparent. The process will involve the same person acting both as a mediator in assisting parties in reaching a settlement, and, in the event mediation fails, as an arbitrator in determining the issues and rendering a binding arbitral award. The first instance decision of the *Keeneye* case commented that the Chinese-styled med-arb process runs into “self-evident difficulties” from an impartiality perspective.

At the core of the issue is the sharp difference between the two roles. The primary role of an arbitrator is to assess the merits of the parties’ claims and to make a decision, while a mediator mainly facilitates communication between the parties and assists them in reaching a settlement. In the course of acting as a mediator, the arbitrator will be exposed to confidential information that might not otherwise be available to him or her in arbitration proceedings.<sup>24</sup> If mediation fails and the mediator reverts back to the role of an arbitrator, there will always be a

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22. Article 39(1) of the BAC Rules.

23. Sally A Harlope, “The Combination of Conciliation with Arbitration in the People’s Republic of China” 24 *J. Int. Arb.* 6 (2007) 623.

24. Weixia Gu and Xianchu Zhang, “The Keeneye Case: Rethinking the Content of Public Policy in Cross-Border Arbitration Between Hong Kong and Mainland China” (2011) 42 *HKLJ* 1001, p 1015.

risk that he or she might lack impartiality due to previous exposure to confidential information.

Additionally, there are concerns that the arbitrator might, consciously or unconsciously, take into account information disclosed during mediation in rendering the award. There are situations in which mediation might involve the assessment of the strengths and weaknesses of each side's case (the so-called "evaluative mediation").<sup>25</sup> In the course of evaluative mediation, the mediator is likely to engage in substantive discussions regarding the merits of each party's position,<sup>26</sup> which is unlikely to happen in arbitration proceedings. There is a risk that the arbitrator, through in-depth discussion with the parties, would have formed his or her own view or preference before the arbitral proceeding. In such a context, a lack of procedural safeguards may result in actual or apparent bias on the part of the arbitrator(s).

In an effort to tackle the issue of bias, article 58(2) of the BAC Rules allows the parties to request the replacement of an arbitrator on the ground that the results of the award may be affected by his or her involvement in the mediation proceedings. Such a request is subject to the approval of the BAC Chairman and the additional costs of the replacement shall be borne by the parties. Under this rule, parties can replace the arbitrator if anything that happened in the course of mediation casts doubts over the arbitrator's impartiality. Regrettably, the BAC Rules are probably some of the very few arbitration rules, if not the only one in mainland China, that contain a provision to that effect.<sup>27</sup>

Another common safeguard under Chinese arbitration rules is that parties are restricted from invoking any of the statements or opinions expressed by the other party or the tribunal during the mediation as grounds for any claims in the arbitral proceedings if mediation fails.<sup>28</sup> However, there are no provisions, either in legislation or in the arbitration rules, which prohibit the arbitrators themselves from using the information obtained from mediation in adjudicating the case afterwards. As a result, many mainland Chinese arbitrators who were involved in the mediation process rely heavily on such information in making the award.<sup>29</sup> This is further complicated by the manner in which Chinese arbitrators draft awards. Unlike common law judges, Chinese arbitrators tend

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25. James T. Peter, "Med-Arb in International Arbitration" (1997) 8 *American Review of International Arbitration* 83. There are two types of mediation, "facilitative mediation" and "evaluative mediation." In "facilitative mediation," the mediator only facilitates communication between the parties and assist them in reaching a settlement; whilst in "evaluative mediation," the mediator may evaluate the case merits in giving opinions.

26. *Ibid.*

27. Although a new provision (article 45(8)) is included in the 2012 CIETAC Rules providing for a CIETAC-assisted mediation if parties do not want the mediation to be conducted by the arbitral tribunal, it is vaguely worded, permitting CIETAC to carry out mediation "in a manner and procedure it considers appropriate"

28. Article 39(4) of the BAC Rules; Article 45(9) of the CIETAC Rules.

29. *See* n 24 above, p 1021.

to state straightforward decisions without providing complete analysis and reasons to explain their decisions. It is sometimes difficult to tell from the contents of an award whether the decision is based on or influenced by information disclosed over the course of mediation.

## 2. Issues of caucusing and confidentiality

Of the many problems that arise out of Chinese style med-arb, the issue of caucusing is perhaps the most controversial. A caucus is a private meeting between the mediator and one of the parties that does not include the other party. Caucusing may have adverse effects on the arbitrators' impartiality.

The International Bar Association (IBA) Rules of Ethics for International Arbitrators provides that "partiality arises where an arbitrator favours one of the parties, or where he is prejudiced in relation to the subject matter of the dispute."<sup>30</sup> In other words, an arbitrator is considered to have lost impartiality if he or she develops any preference regarding either (a) the outcome, or (b) a party. Caucusing is particularly detrimental in the latter case. In caucuses the mediator may discuss a wide range of issues with the parties, including personal and emotional issues that might not be discussed in an arbitration proceeding. In the absence of an opponent, a party might be more inclined to disclose confidential information and compromise its positions. A mediator-turned-arbitrator may become more understanding, sympathetic and supportive of a particular party's position after learning this information during caucusing.<sup>31</sup> Additionally, a mediator-turned-arbitrator may be exposed to allegations made by one party in a private caucus that remain unknown to the other party.<sup>32</sup> The confidential nature of private caucuses would then deprive the other party of his or her right to be heard and of the opportunity to rebut all of the claims against him or her, including those not stated in the formal dispute resolution processes.<sup>33</sup> Arbitrators may end up relying on these unproven allegations and on other confidential information divulged in deciding the case.<sup>34</sup> As Michael Hwang puts it, an arbitrator will inevitably become biased as the result of private caucuses with the parties in which the arbitrator becomes privy to confidential information.<sup>35</sup>

Caucusing can potentially lead to actual or apparent bias if no appropriate procedural safeguards are adopted. The *Keeneye* case is a good

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30. Rule 3.1 of the IBA Rules of Ethics for International Arbitrators.

31. See n 25 above, p 93.

32. Gu Weixia, *Arbitration in China*, p 37.

33. Kaufmann-Kohler, "When Arbitrators Facilitate Settlement," p 198. See also Rosoff, Jacob, "Hybrid Efficiency in Arbitration: Waiving Potential Conflicts for Dual Role Arbitrators in Med-Arb and Arb-Med Proceedings" (2009) 26(1) *Journal of International Arbitration* 89, 93.

34. Michael Hwang, "The Role of Arbitrators as Settlement Facilitators: Commentary," A.J. Van Den Berg (ed.), *ICCA Congress Series no 12* (Kluwer Law International 2005), p 573.

35. Michael Hwang, "The Role of Arbitrators as Settlement Facilitators: Commentary," *ibid.* pp 556-564.

example of the problems that can arise out of caucusing. The alleged bias in the *Keeneye* case arises from a private meeting between an arbitrator, the Secretary General of the Xi'an Arbitration Commission, and an affiliate of the respondents. What further muddles the water is that the med-arb in issue was held at the Xi'an Shangri-la Hotel over a dinner and the Secretary General of the Xi'an Arbitration Commission told the affiliated party to "work on" the respondents. These were the main factors that the Hong Kong Court of First Instance concluded would "cause a fair-minded observer to apprehend a real risk of bias,"<sup>36</sup> leading the court to decline to enforce the award on the basis that enforcement would contradict Hong Kong's public policy, or "fundamental notion of justice and morality."<sup>37</sup>

In practice, caucusing with a party is a common technique employed in Chinese med-arb procedures. Despite the adverse implications on the arbitrators' impartiality, arbitration rules in China do not contain provisions governing how caucuses are to be conducted. As a result, there is a high risk of the arbitrators' impartiality being tainted. It must be noted that the test for impartiality is whether an objective, fair-minded, and informed observer, having considered the relevant facts, would conclude that there was a real possibility that the tribunal was biased.<sup>38</sup> If the other party has no knowledge about what was discussed between the arbitrators and the other party in a private meeting, there may be suspicion that what was said in the private meeting has unduly influenced the arbitrator. In order to address this issue, many common law jurisdictions require an arbitrator to make a disclosure to all parties of the confidential information obtained during the mediation which he or she considers to be "material to the arbitral proceedings" if mediation fails.<sup>39</sup> As will be discussed below, while the *Keeneye* case has promoted reform in the CIETAC Rules, the new rules continue to fail to address the issue of caucusing.

Another basis for due process concerns regarding med-arb arises from the confidential information obtained by the arbitrator(s) in the course of mediation. Currently, neither the China Arbitration Law nor the rules of the major Chinese arbitration commissions contain provisions addressing confidentiality in the med-arb process. While some arbitration commissions established ethical rules or codes of conduct requiring arbitrators to keep information obtained in the course of arbitration confidential, such rules, at least on their face, do not cover the med-arb

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36. See n 7 above, para 53.

37. Public policy in Hong Kong has been interpreted as the "fundamental notion of justice and morality in Hong Kong." See *Hebei Import & Export Corp v. Polytek Engineering Co Ltd* [1998] 1 HKLRD 287.

38. *Porter & Another v Magill* [2002] 2 WLR 37, per Lord Hope at pp 83-94; *Deacons v White & Case LLP & Others* (2003) 6 HKCFAR 322 at p 332.

39. See for example Section 33 of the Hong Kong Arbitration Ordinance, Cap 609.

process.<sup>40</sup> In the absence of confidentiality obligations, mediators may disclose information obtained from a party during caucuses to another party. Even if there is not an actual disclosure, studies reveal that judges are often unable to disregard inadmissible evidence when making decisions that are unlikely to be reviewed by higher courts.<sup>41</sup> Since arbitrators face scant risk of review, it would even be more unlikely for them to ignore information obtained from mediation when it comes time to render a judgment.<sup>42</sup>

The lack of a confidentiality requirement can be extremely detrimental to procedural fairness. Not only may a party, through the arbitrators, gain access to otherwise confidential information of the other party, but the arbitrators themselves may also use this confidential information as leverage to pressure a party to agree to a settlement proposal.

### 3. Reform of CIETAC Rules

Following the Hong Kong Court of First Instance judgment in the *Keeneye* case, the inadequacy of procedural safeguards against actual or apparent bias received public attention. As scholars and practitioners expressed concern over some common but arguably improper practices in Chinese med-arb, CIETAC reformed its rules to address the issue of the dual capacity of arbitrators and mediators.

Under the new CIETAC Rules, which came into effect in May 2012, the tribunal may only mediate the case with the consent of both parties.<sup>43</sup> Another significant reform can be found in article 45(8), which provides that where the parties wish to mediate their dispute but do not wish to have the mediation conducted by the arbitral tribunal, the CIETAC may, with the consent of both parties, assist the parties in mediating the dispute in a manner and procedure it considers appropriate.<sup>44</sup> Under this provision, CIETAC will only assist with the mediation. As a result, there will be no concern that the impartiality of the arbitrators has been affected in the mediation process. These changes are certainly a significant improvement to the existing med-arb framework. They remind parties that they do not necessarily have to designate the same arbitrator(s) to conduct the mediation. With this newly added provision, parties are likely to be more cautious in choosing the mediator(s).

Despite these advances, however, the overall framework remains deficient in preventing actual or apparent bias. The new CIETAC Rules

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40. See for example, article 12 of Beijing Arbitration Commission Ethical Standards for Arbitrators (effective from September 1, 2006).

41. Wistrich, Guthrie, and Rachlinski, (2005) 'Can Judges Ignore Inadmissible Information? The Difficulty of Deliberately Disregarding' 153 *University of Pennsylvania Law Review* 1251, at 1323-24. The authors state that 'Judges are indeed human; like juror, they are often unable to "close the [v]alves of [their] attention?'

42. Brian A. Pappas, 'Med-Arb: The Best of Both Worlds May Be Too Good To Be True' Spring 2013 *Dispute Resolution Magazine*, p 42.

43. Article 45(2) of the 2012 CIETAC Rules.

44. Article 45(8) of the 2012 CIETAC Rules.

merely provide an additional option to parties wishing to attempt mediation. In the event that parties still choose to have the same arbitrator conduct mediation, there are no further procedural safeguards to ensure the arbitrator's impartiality. In reality, parties may not be aware of potential conflicts at the time that they appoint a mediator. More importantly, parties may have concerns regarding the costs or the efficiency of the med-arb that may deter them from hiring extra mediators. As such, it will most likely remain a norm, rather than an exception, to have arbitrators function as mediators in China.

The lack of incentive to engage in more substantive reforms may be attributable to the Court of Appeal judgment in the *Keeneye* case. In the *Keeneye* case, the Court of Appeal held that the supervisory court<sup>45</sup> (the Xi'an Court) was in a better position to ascertain the facts and to decide whether those facts established a case of actual or apparent bias.<sup>46</sup> Having deferred to the views of the supervisory court, the Court of Appeal in Hong Kong, as the enforcement court,<sup>47</sup> held that there was no actual or apparent bias and upheld the award in question.<sup>48</sup> The approach adopted by the Court of Appeal in the *Keeneye* case is arguably inconsistent with the English position on public policy. The English position involves a balancing exercise between the enforcement court and supervisory court; the court will first look at the importance of preserving its public policy using its domestic standards, then balance that interest against the principle of pro-enforcement in international arbitration before deciding whether to defer its judgment to the opinion of the supervising court.<sup>49</sup>

Notwithstanding the reform efforts, the CIETAC rules are still deficient and fail to address concerns related to confidentiality and risks to impartiality. For instance, unlike the provisions in Hong Kong and Singapore, there are no procedural safeguards requiring the neutral arbitrator to divulge information obtained via private caucusing should the arbitration resume after mediation.<sup>50</sup> Without adequate procedural safeguards, the overlapping roles of the mediator and arbitrator may undesirably prolong the process of dispute resolution and even add to the cost of the med-arb process, thus detracting from the intended purpose of enhancing efficiency.

The *Keeneye* case may have left Chinese arbitration institutions with a false sense of security. Courts must recognize that the approach

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45. Supervisory court refers to the court at the place of arbitration, which exercises supervisory jurisdiction over the arbitration proceeding.

46. *Gao Haiyan v Keeneye Holdings Ltd* [2012] 1 HKLRD 627, para 68 (hereinafter referred to as "*Keeneye*")

47. Enforcement court refers to the court where the arbitral award is to be actually enforced, i.e. the court where the losing party or property against which enforcement is sought is located.

48. *Gao Haiyan v Keeneye Holdings Ltd* [2012] 1 HKLRD 627.

49. See n 24 above, p 1008.

50. See, for example, section 33(4) of Hong Kong Arbitration Ordinance (Cap 609).

adopted by the Court of Appeal is not entirely consistent with the English position<sup>51</sup> and the approach may be better understood as being confined to the facts of the particular case. The case can be more appropriately characterized as an ad hoc decision upholding the award in question rather than a blanket acceptance of the med-arb practices in China. More substantive reform in arbitration rules is needed to bring the med-arb practice in line with internationally recognized standards of impartiality and due process.

C. *Conclusion: The Need to Institutionalise The Med-Arb Process*

China has dedicated great efforts to promulgating legislation in the area of alternative dispute resolution. But legislators, as well as the drafters of local arbitration rules, seem to have overlooked many of the problems that arise from Chinese med-arb processes. The lack of mandatory procedural and confidentiality requirements for med-arb under the Arbitration Law is one of the factors contributing to the absence of an established due process tradition in Chinese arbitration. While there are certain existing safeguards and reforms under some arbitration commission rules attempting to address the issue of bias, these efforts are not satisfactory. As a result, the med-arb process in China is often tainted by procedural irregularities. It has been questioned whether the Chinese practice of med-arb is compatible with rule of law. Moreover, given the popularity of med-arb in China, the standard of due process in med-arb is likely to have a significant impact on the overall dispute resolution environment in China. All of this warrants institutional reforms that would bring Chinese med-arb in line with international standards. To clarify what reforms are needed, Part III reviews med-arb practices and relevant procedural safeguards in various jurisdictions in the East and West.

III. REVIEW OF MED-ARB PRACTICES AND RELEVANT PROCEDURAL SAFEGUARDS IN VARIOUS JURISDICTIONS

The problems of Chinese style med-arb have led scholars and drafters of arbitration rules to reassess procedural safeguards against bias. Regrettably, the recent reform of the CIETAC Rules has still failed to meet an internationally recognized due process standard. In order to explore how the current med-arb process can be improved, this section sets forth a review and comparison of med-arb and its degree of acceptance in various jurisdictions. More importantly, this section surveys these jurisdictions' legislative efforts to prevent actual or apparent bias.

The internationally recognized version of med-arb refers to the situation in which a party decides to combine the mediation process and

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51. The English case *Minmetals* has been cited in the Hong Kong Court of Appeal Judgment, *Minmetals Germany GmbH v Ferco Steel Ltd* [1999] CLC 647. (Queen's Bench Commercial Court, England and Wales), where Justice Coleman explained on English public policy of deference to the supervisory jurisdiction of arbitration. See *Minmetals*, per Justice Coleman, at para 661, cited in *Keeneye*, per Tang VP, at para 67.

arbitration process in a single case. The mediator(s) and arbitrator(s) are typically independent and, the mediation and arbitration proceedings operate independently.

#### A. *Asia*

In Asia, med-arb is gaining popularity. Amongst other jurisdictions, Hong Kong, Singapore, and Japan have all recently enacted provisions enhancing procedural safeguards in the med-arb process.

The Hong Kong Arbitration Ordinance (Cap 609, amended in 2011) and Singapore International Arbitration Act (Cap 143A, amended in 2012) are notable examples of legislative efforts to regulate med-arb, as the two jurisdictions are the two most frequently chosen jurisdictions for international arbitration in Asia. Unlike China, where med-arb is mostly regulated by the rules of arbitration institutions, in both Hong Kong and Singapore, legislation plays a crucial role in regulating med-arb.

Because of common law practitioners' concerns over the conflicting roles of arbitrator and mediator, under the Hong Kong Arbitration Ordinance, an arbitrator can only act as a mediator if all parties consent in writing, and only so long as no party withdraws its consent in writing.<sup>52</sup> Common law lawyers are particularly sensitive regarding the issue of caucusing. Some take the view that the meeting of the arbitrator with the parties separately is inconsistent with due process and inevitably leads to conflicts.<sup>53</sup> In order to reduce this concern, the Hong Kong Arbitration Ordinance imposes an obligation on the mediator-turned-arbitrator to disclose the confidential information obtained during mediation if mediation fails. If an arbitrator obtains information from a party during mediation proceedings and the proceedings terminate without reaching a settlement, the arbitrator is required to disclose to all other parties the information that he or she considers material to the arbitral proceedings before resuming them.<sup>54</sup>

One major caveat is worth mentioning, however: although both Hong Kong and Singapore are Asian jurisdictions with close ties to China, they are both common law jurisdictions. One must bear in mind the huge differences between the common law and civil law systems when considering the institutionalisation of med-arb in China.

It is thus helpful to look at civil law jurisdictions in Asia. The situation in Japan is particularly significant to analyze because it is a civil law jurisdiction in Asia whose dispute resolution tradition and culture bears a high resemblance to China's. Moreover, med-arb is developing quickly in Japan. An empirical study conducted by the Japan Commercial Arbitration Association (JCAA) in 2009 reveals the prevalence of

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52. Section 33(4) of Hong Kong Arbitration Ordinance (Cap 609). Section 17 of Singapore International Arbitration Act (Cap 143A) is in almost identical terms with section 31.

53. Mark Goodrich, "Arb-med: ideal solution or dangerous heresy?" (2012) 15(1) *International Arbitration Law Review* 12.

54. Section 33(4)(b) of Hong Kong Arbitration Ordinance (Cap 609).

med-arb.<sup>55</sup> In about 40% of cases heard by JCAA tribunals, the tribunal attempted mediation with the consent of the parties.<sup>56</sup> However, there are significant differences between the practice of arbitrators from common law backgrounds and those with civil law backgrounds. Where all three arbitrators were from the civil law backgrounds, the tribunal attempted to mediate in about 57% of the cases, but where at least one arbitrator was from a common law background, med-arb was not adopted in any of the cases.<sup>57</sup> It is also worth noting that med-arb was mostly employed by local Japanese arbitrators.<sup>58</sup>

Under the Japan Arbitration Law, an arbitrator may only act as a mediator in the course of arbitral proceedings with the agreement of the parties.<sup>59</sup> As with the Hong Kong Arbitration Ordinance, consent must be given in writing and can be withdrawn by the parties at any stage. To foreshadow what will be discussed in Part IV, most jurisdictions do not only require consent to be obtained in advance of conducting mediation, but separate consent is also required for the arbitrator(s) to act as mediator(s). This is an important procedural safeguard that is lacking in the Chinese legislation. There is, however, no disclosure requirement under the Japanese Arbitration Law. Arguably, because Japan is a civil law jurisdiction, it may not have as much concern over caucusing as a common law jurisdiction might. To a certain extent this might justify the absence of a disclosure requirement in the Chinese legal framework. As will be discussed below, disclosure requirements are absent in most civil law jurisdictions, not only in the East but also in the West.

## B. *Continental Europe*

Med-arb is relatively accepted in Germany,<sup>60</sup> but less popular in other countries in continental Europe such as Switzerland and France. It may be surprising to note that while civil law jurisdictions are generally more receptive to med-arb, few have passed national legislation to regulate the practice. The French arbitration legislation, which was codified in articles 1442 through 1527 of the French Code of Civil Procedure in 2011, makes no reference to mediation.<sup>61</sup> In a similar vein, the Swiss Federal

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55. Tatsuya Nakamura, "Brief Empirical Study on Arb-Med in the JCAA Arbitration," JCAA Newsletter, Number 22 (June 2009), pp10-12.

56. *Ibid.*

57. *Ibid.*

58. *Ibid.*

59. Article 38 of Japanese Arbitration Law (Law No.138 of 2003).

60. Renate Dendorfer, "Mediation in Germany: Structure, Status Quo and Special Issues," paper prepared for the Chartered Institute of Arbitrators European Branch Annual General Meeting and Conference, Paris 9, [http://www.ciarb-european-branch.com/Conference/Archive/Archive %20Paris%202011/Mediation%20in%20Germany%20by%20Renate%20Dendorfer.pdf](http://www.ciarb-european-branch.com/Conference/Archive/Archive%20Paris%202011/Mediation%20in%20Germany%20by%20Renate%20Dendorfer.pdf) (accessed 19 April 2013).

61. See articles 131-1 to 131-15 of French Code of Civil Procedure regulating the use of mediation in litigation.

Civil Procedure Code only regulates the combination of mediation with litigation but not arbitration.<sup>62</sup>

The German tradition allows for flexible practices of dispute resolution in order to increase efficiency. According to Section 1053(1) of the German Code of Civil Procedure, if parties settle their dispute in arbitral proceedings, the arbitral tribunal “shall record the settlement in the form of an arbitral award *on agreed terms* (emphasis added)” if requested by the parties, showing Germany’s accommodating attitude towards the development of med-arb. In addition, the acceptance of the arbitrator’s involvement in dispute resolution in Germany is reflected in a survey conducted by Christian Bühring-Uhle in 2004. The survey results show that German practitioners are much more supportive of arbitrators’ involvement in the mediation process.<sup>63</sup> And in practice, members of the arbitral tribunal (especially the chairman) attempt mediation in a significant proportion of German cases.<sup>64</sup> This practice accords with the common practice in German courts in which judges act as mediators. Thus, German lawyers who are familiar with this approach naturally have very few objections to the involvement of the arbitrator as a mediator.<sup>65</sup> Furthermore, it is not uncommon in Germany for the arbitral tribunal to express its preliminary views on the merits of the case during mediation.<sup>66</sup> In sharp contrast, nearly two thirds of the common law respondents thought of the proposal as “inappropriate.”<sup>67</sup>

The study of Germany’s med-arb practice is of some relevance to the situation in China. Med-arb’s degree of acceptance in a jurisdiction clearly has a strong link to how the judiciary in a particular jurisdiction functions. In Germany, the judiciary is more actively involved in mediating cases and part of the court’s mission is to settle the dispute at hand.<sup>68</sup> In other words, judges often assume the role of a mediator. This is also the case in China. This is perhaps the reason why practitioners in Germany do not find it problematic to have the arbitral decision maker act as a mediator.

However, other civil law countries in Europe seem to take the view that arbitration and mediation should be kept separate in order to

62. Article 214 of Swiss Civil Procedure Code.

63. Christian Bühring-Uhle, *Arbitration and Mediation in International Business* (Kluwer Law International 2006), p122.

64. *Ibid*, p125.

65. *Ibid*, at p122.

66. Paul E. Mason, “The Arbitrator as Mediator, and Mediator as Arbitrator” (2011) 28(6) *J. Int. Arb.* 541.

67. *See* n 53 above.

68. For instance, German courts will hold a pre-hearing settlement session when possible with the parties during which they make inquiries and assess the merits of the case. Such settlement sessions can be held after the proceedings have commenced and even at the appellate stage. The court may also refer the parties to another judge to conciliate or to out-of-court alternative dispute resolution. See Gabrielle Kaufmann-Kohler, “When Arbitrators Facilitate Settlement: Towards a Transnational Standard?” (2009) 25(2) *Arbitration International* 190.

maintain the neutrality of the proceedings. In France, arbitrators seldom act as mediators, despite the absence of statutory restrictions prohibiting the practice.<sup>69</sup> As in the case of Germany, the attitude towards med-arb may be influenced by the judiciary's practice. Although French courts have express power to conduct mediations,<sup>70</sup> French judges seldom take the initiative to mediate cases before them.<sup>71</sup>

In conclusion, while Germany is more receptive to the practice of arbitrator(s) acting as mediator(s), other European countries have concerns over actual or apparent bias that may arise from this practice. For these reasons, arbitrators in France are generally reluctant to act as the mediators of the same case. Despite the lack of procedural safeguards in the French legislation, the mediation process is often detached from the arbitration process and arbitrators are seldom involved in mediation. Thus, there is little chance that apparent bias will arise as a result of the mediation process.

### C. *Common Law Jurisdictions in the West*

According to the survey conducted by Christian Bühring-Uhle, arbitrators "practically never" participate in settlement negotiations in the United States.<sup>72</sup> Although it has been suggested that med-arb is gaining popularity in the United States, legislation seems to be lagging behind. For instance, there is no mention of mediation in the arbitration rules promulgated in the New York Civil Practice Law & Rules.<sup>73</sup> Precedent also suggests that legislation in the United States does not support med-arb. In *Advanced Bodycare Solutions v. Thione International*, the 11th Circuit held that a dispute resolution clause giving the parties an option to mediate or arbitrate was not "an agreement to settle by arbitration a controversy" and thus was not enforceable under the Federal Arbitration Act (FAA).<sup>74</sup> This illustrates that U.S. courts are slow to embrace med-arb. Given the courts' narrow construal of "arbitration" in the FAA, it is unlikely that existing U.S. arbitration laws will lend support to mediation attempts by the arbitrators.

In the United Kingdom, although no express provisions in the Arbitration Act of 1996 govern the use of med-arb, the courts have considered the implications of resuming arbitration or adjudication in the event of unsuccessful mediation by the same appointee. As a safeguard against the risk of prejudice on the part of the arbitrator, the High Court

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69. Kaufmann-Kohler, "When Arbitrators Facilitate Settlement", 190.

70. Article 1460 of French Code of Civil Procedure.

71. Kaufmann-Kohler, "When Arbitrators Facilitate Settlement", 190.

72. Christian Bühring-Uhle, *Arbitration and Mediation in International Business* (Kluwer Law International 2006), p 122.

73. Article 75 of New York Civil Practice Law & Rules.

74. *Advanced Bodycare Solutions v. Thione International*, No. 07-12309, 2008 U.S.App. Lexis 8584 (11<sup>th</sup> Cir. April 21, 2008). The FAA postulates that arbitration will produce a resolution "independent of the parties' acquiescence"; which differs from the voluntary agreement mediation aims to achieve. See p 1240 of the appeal.

case of *Glencot Development & Design v Ben Barrett & Son*<sup>75</sup> held that the objective test to apply is whether the “circumstances would lead a fair-minded and informed observer to conclude that there was a real possibility or a real danger . . . that the tribunal was biased.”<sup>76</sup> In that case, the arbitrator’s decision was held to be unenforceable. By merely conducting private discussions in the mediation phase, the adjudicator’s impartiality had been compromised and his decision was affected by apparent bias.<sup>77</sup>

The most comprehensive and detailed legislative provision governing the med-arb process can be found in the Commercial Arbitration Act (CAA) Model Bill of Australia. The CAA Model Bill is a model version of an arbitration act planned to be enacted in the Australian states. So far, the Model Bill has been adopted by several states including New South Wales, South Australia, Victoria, and Queensland.<sup>78</sup> Article 27D of the CAA Model Bill provides for several procedural safeguards in cases where an arbitrator acts as a mediator. Some of these safeguards resemble legislation in Hong Kong and Singapore. Firstly, arbitrators can only act as mediators if the arbitration agreement allows for such an arrangement, or if each party has consented to the arbitrator so acting.<sup>79</sup> Secondly, arbitrators may communicate with the parties collectively or separately only if parties consent. This refers to caucusing. Thirdly, under the CAA Model Bill, the arbitrator is required to treat information obtained from a party with whom he or she communicates separately in the mediation as confidential, unless that party otherwise agrees or unless the arbitration agreement provides otherwise.

In addition to these general safeguards, the CAA Model Bill also provides that an arbitrator who has acted as the mediator in the mediation proceedings may not conduct subsequent arbitration proceedings without the written consent of all the parties given upon or after the termination of the mediation proceedings.<sup>80</sup> In the event of subsequent arbitration proceedings following mediation, a substitute arbitrator will be appointed. Such a provision is a unique feature of the CAA Model Bill that does not have counterparts in the Hong Kong or Singaporean legislation. This mechanism would be helpful in safeguarding due process if it were adopted in China. This mechanism is helpful because the parties are given another opportunity after the termination of mediation to consider whether or not to retain the same arbitrator(s). If the conduct or attitude of the arbitrator(s) gives any party the impression that the arbitrator’s impartiality may be affected, one or both of the parties may choose to appoint a substitute arbitrator.

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75. *Glencot Development & Design v Ben Barrett & Son* [2001] B.L.R. 207.

76. *Ibid.*, para 21, *Glencot Development & Design v Ben Barrett & Son*.

77. *Ibid.*, paras 23-25, *Glencot Development & Design v Ben Barrett & Son*.

78. See for example, New South Wales Commercial Arbitration Act 2010, South Australia Commercial Arbitration Act 2011, Victoria Commercial Arbitration Act 2011 and Queensland Commercial Arbitration Act 2013.

79. Article 27D(1) of CAA Model Bill.

80. Article 27D(4) of CAA Model Bill.

#### IV. INSTITUTIONALISATION OF MED-ARB IN CHINA

A modern institutional framework should consist of both regulatory rules and facilitative rules. Regulatory rules refer to macro-level mandatory requirements while facilitative rules refer to those specific implementation details that facilitate the use of regulatory rules. Ideally, an institutionalised med-arb system should consist of mandatory requirements that create a minimum standard to ensure due process, but it should also leave arbitration institutions with a certain degree of flexibility in setting their own rules so that med-arb continues to thrive. China's current institutional framework consists only of facilitative rules that encourage the use of med-arb, but lacks regulatory rules that mandate procedural safeguards. As a result, the institutional framework for med-arb is incomplete and regulatory rules need to be developed and strengthened.

I suggest that legislators of arbitration law and drafters of arbitration rules should employ procedural safeguards to address the concerns over the impartiality of arbitrators in the process of med-arb. The safeguards should aim at (A) alerting parties to the potential risks of appointing the arbitrator(s) as mediator(s); (B) eliminating due process concerns over caucuses; and (C) maintaining the impartiality of arbitrators.

##### A. *Alerting Parties to the Potential Risks of Appointing the Arbitrator(s) as Mediator(s)*

As discussed above, the common practice in China is to have the arbitral tribunal or one of the arbitrators act as mediator. Due to the way arbitration rules are drafted, it has almost become a default position that arbitrators are responsible for mediating the case before them. When mediators are appointed, parties are often unaware of the potential adverse effect that mediating the case may have on the arbitrators' impartiality. The best way to alert parties to this risk is to require that informed consent be obtained from all parties before an arbitrator can be appointed to conduct the mediation.

Although many of the current Chinese arbitration rules, including the new CIETAC Rules and BAC Rules, stipulate that mediation will only be conducted with the parties' consent, this consent is only relevant as to whether mediation will occur, and does not apply to the mode in which it will be conducted. A specific requirement should be added to these rules to ensure that additional consent must be obtained from all parties before arbitrators can act as mediators. This will enable the parties to direct their minds to the problems that may arise from that form of mediation, seek legal advice, and make fully informed decisions. Legislation in many jurisdictions, including Hong Kong, Singapore, Japan, and Australia, require that parties' consent be obtained before an arbitrator can act as a mediator. It is desirable that China amend the Arbitration Law accordingly to match the international norm.

### B. *Eliminating Due Process Concerns over Caucuses*

The practice of caucusing has raised due process concerns, particularly among those with common law training. The arbitrator-turned-mediator is likely to engage in more substantive interactions with a party during caucuses. The arbitrator's impartiality may be affected, or may at least appear to be affected, by these caucuses.

Eliminating due process concerns over caucuses is a controversial issue for China. The common law method for dealing with caucuses has included the requirement that before resuming arbitration proceedings, arbitrators must disclose to all other parties any information divulged in a private caucus that they consider material to the arbitral proceedings.<sup>81</sup> Disclosure can put both parties on a level playing field by creating information symmetry with respect to the arbitrator. If such an arrangement can be implanted into the Chinese med-arb system, it would be a significant step towards adequate due process protections. Unfortunately, it is doubtful whether arbitration institutions will be willing to adopt these provisions because disclosure requirements may impede the rate at which mediations achieve settlements between parties. Parties may worry that what they say during caucuses will eventually be disclosed to the other party in case mediation fails. Hence, they may be less inclined to share their real concerns and expectations with the mediators.

On this issue, the BAC Ethical Standards for Arbitrators may provide some guidance on how to balance the success of mediation with due process concerns. These standards provide that the arbitral tribunal should be cautious in deciding to meet unilaterally with one of the parties or its representative. If such a decision is made, the meeting should be held in the presence of the secretary of the BAC and the other party should be informed of the meeting.<sup>82</sup> This provision therefore has the practical effect of limiting caucusing. Additionally, the BAC secretary serves as an independent supervisor and his or her presence discourages improper attempts by parties to influence the arbitrator's views.

Arbitration institutions may consider adopting a similar mechanism to supervise caucuses. Further provisions can also improve safeguards by regulating the manner in which a caucus can be held. For instance, arbitration institutions can enact a rule that a caucus can only be held at the hearing facilities of the arbitration institution or at a location agreed on by both parties. These rules can help better regulate caucusing and ease due process concerns.

### C. *Maintaining the Impartiality of Arbitrators*

The most fundamental objective of the institutionalisation of med-arb is to maintain the impartiality of the arbitrators. As discussed above,

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81. See section 33(4) of the Hong Kong Arbitration Ordinance (Cap 609); s17(3) of the Singapore International Arbitration Act.

82. Art 8 of Ethical Standards for Arbitrators of the Beijing Arbitration Commission (2006).

the problem with Chinese med-arb is the presence of dual capacity of arbitrators and mediators and the fear that an arbitrator may lose his or her impartiality by participating in the mediation process. The key to preventing actual or apparent bias is to ensure that an arbitrator, in rendering the award, does not take into account information obtained in the mediation process, which is not available in the arbitration process. Three safeguards are proposed which may prevent the misuse of such confidential information: (1) restricting the use of information obtained in the mediation process in subsequent arbitral proceedings; (2) giving parties an option to terminate the arbitrator(s) in case mediation fails; and (3) strengthening ethical rules for arbitrators.

1. Restricting the use of information obtained in the mediation process in subsequent arbitral proceedings

In order to facilitate communication during mediation, most arbitration rules provide that what is said by the parties in the course of mediation cannot be invoked by any other party in subsequent proceedings. However, such provisions only prohibit the use of information by the other party and do not restrict the arbitrator from relying on that information in making his or her decision. As a result, it is common for arbitrators who were involved in the mediation process to rely on information disclosed during mediation in determining the award.<sup>83</sup> The arbitrator's impartiality is thus compromised by his or her participation in the mediation process.

The underlying cause of this problem originates in the neglect of due process requirements. Chinese arbitrators tend to make decisions based on what they consider to be "right" without paying much attention to the process in which they reach this "right" determination.<sup>84</sup> Two proposals are put forward in regards to how this problem can be addressed: on the one hand, a mandatory requirement prohibiting the use of information obtained in the course of mediation in subsequent arbitral proceedings; and on the other hand, ethical rules requiring arbitrators not to take into account information that is made available to them in the course of mediation.

An arbitrator loses his impartiality if he develops preferences regarding the outcome of the case. First, there is the likelihood of the improper use of information obtained in mediation, where a mediator-turned-arbitrator may take into account confidential information made available to him during the mediation process but not available to him in an arbitral hearing with both parties present. If the mediator-turned-arbitrator does consider the confidential information in the subsequent arbitration and makes improper use of it in reaching his decision, his predisposition would be evidently to influence the ensuing arbitral outcome. It must

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83. See n 24 above, p 1021.

84. Chinese legal traditions place more emphasis on substantive (distributive) justice than procedural justice.

be borne in mind that such information may not have been available to the arbitrator in the arbitral proceedings and hence, under these circumstances, it would not have been possible at all for the arbitrator to be swayed by the additional information. The arbitrator's use of information obtained in mediation to render an arbitral decision must be strictly prohibited by legislation, as the impartiality of the decision-maker is fundamental to the procedural fairness of the system.

## 2. Giving parties an option to terminate the arbitrator(s) in case mediation fails

In general, parties are often not aware of the potential risks when they consent to using the same arbitrator(s) in mediation. In fact, actual or apparent bias most often takes place during or after the mediation process. Hence, obtaining the parties' consent prior to conducting mediation is not sufficient. Parties should be given a second opportunity to consider whether to allow the arbitrator who has been acting as a mediator to continue to conduct the arbitration proceedings. This "double consent mechanism" will allow parties to terminate the arbitrators (and hence eliminate the possibility of bias) if the arbitrators' attitude or conduct during mediation appears to be suspicious. Moreover, this reform allows the parties to retain the option to arbitrate their case with confidence in the new arbitrator's impartiality. This is a unique mechanism that is present in the Australian med-arb model but does not exist in the rules or statutes of other common law jurisdictions such as Hong Kong and Singapore.

The current BAC Rules contain a provision that has a similar effect. Parties are entitled to request the replacement of an arbitrator on the ground that the result of the award may be affected by his or her involvement in the mediation proceedings.<sup>85</sup> The BAC provision is slightly different from the Australian model in that the default position is to allow the arbitrator to continue to conduct the proceedings unless the parties make a specific request to replace him, but both provisions serve the purpose of preventing actual or apparent bias in the med-arb process. Because preventing actual or apparent bias is crucial to ensuring due process protections, this sort of provision should be included in all Chinese arbitration commission rules.

## 3. Strengthening ethical rules for arbitrators

While most reform proposals focus on arbitration rules, it must not be forgotten that ethical rules regulating the conduct of arbitrators in the med-arb process are equally important. Ultimately, the arbitrators are in a better position than the parties to evaluate their own inclinations. The onus is also on the arbitral tribunal to preserve the integrity of the arbitral proceedings.

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85. Article 58(2) of BAC Rules.

Currently, the codes of conduct for arbitrators issued by the Chinese arbitration institutions mostly focus on the conflict of interest that might exist at the time the arbitrator is appointed. There are very limited guidelines when it comes to conducting med-arb.

A comprehensive guideline can be found in the International Bar Association (IBA) Guidelines on Conflicts of Interest in International Arbitration. Under the IBA Guidelines, an arbitrator may assist the parties in reaching a settlement of the dispute at any stage of the proceedings provided that he or she has the consent of the parties to act in such manner.<sup>86</sup> However, “the arbitrator shall resign if, as a consequence of his or her involvement in the settlement process, he or she develops doubts as to his or her ability to remain impartial or independent in the future course of the arbitration proceedings.”<sup>87</sup>

This provision largely assimilates the legislations of various jurisdictions on this matter. What is significant is the last part of the provision, which requires the arbitrator to withdraw if he or she “develops doubts as to his or her ability to remain impartial or independent in the future course of the arbitration proceedings.” Unlike national legislation, which tends to place an emphasis on parties’ rights, the IBA Guidelines impose an obligation on arbitrators to consider their own impartiality after conducting mediation. The requirement that arbitrators should reassess their independence and impartiality after the termination of mediation places an important burden on arbitrators, and this type of safeguard should be adopted in Chinese med-arb.

## V. INSTITUTIONALISATION OF MED-ARB AND ITS SIGNIFICANCE ON THE RULE OF LAW IN CHINA

The state of the dispute resolution system of a society is a strong indication of the degree of rule of law in that country. The rule of law requires that no person is above the law and it is made possible if dispute resolution processes are carried out equitably, sufficiently, and efficiently within the legal framework. It determines how disputes will be resolved, whether every party will be treated equally before the law, whether redress can be obtained, and, if so, whether it can be obtained in a timely manner. These are all crucial elements of the rule of law. An institutionalised dispute resolution system will not only promote legal consciousness and acceptance of the law in the society, but also provide guidance to individuals’ behaviour. Disputants will therefore adapt their own behaviour to the set of institutionalised rules and thereby enhance any reforms to these rules at the macro level.

The key to developing a healthy dispute resolution system lies in its procedural rules. Procedural rules ensure that a fair and proper procedure is used when making a decision. They are therefore as important

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86. Article 4(d) of General Standard 4 of the IBA Guidelines on Conflicts of Interest in International Arbitration (2004).

87. *Ibid.*

as, if not more important than, the actual decision reached. The importance of due process in dispute resolution is well illustrated by Emeritus Professor of Comparative Law C.J. Hamson's comment: "it is in its legal institutions that the characteristics of a civilized society are most clearly reflected, not only, and not so much, in its substantive law as in the practice and procedure of its courts. Legal procedure is a . . . ritual of extreme social significance."<sup>88</sup> The purpose of an effective dispute resolution system is to provide an avenue whereby citizens can resolve disputes without resorting to self-help.<sup>89</sup> It follows that a civil justice system must use procedures, which are and are perceived to be fair to the disputants.

If legal procedure is considered to be of extreme social significance, then the procedural rules of the widely used med-arb approach to dispute resolution must bear significant relevance to the rule of law in China. This is not only because significant portions of disputes are currently being resolved by med-arb; it is also because under the harmonious-society-building tone set by the Chinese government officials, it is predicted that med-arb will be even more popular in the near future.<sup>90</sup> Currently, approximately 20% to 30% of the caseload of CIETAC is resolved by med-arb.<sup>91</sup>

The current popularity of med-arb is partly attributable to China's own tradition of dispute resolution and current social policy, which encourages the settlement of disputes through amicable negotiation. In practice, arbitrators systematically take the initiative in asking the parties if they wish the tribunal to assist them in reaching an amicable solution.<sup>92</sup> Chinese parties are familiar with this practice and are generally willing to cooperate in order to avoid leaving the tribunal with an impression that they are uncooperative.

Med-arb will likely continue to gain popularity. The advantage of med-arb lies not only in its efficiency, but also in the parties' awareness that a successful mediation will significantly reduce the cost of settling a dispute. If settlement is reached, the parties can avoid incurring further legal costs, which may be substantial in the context of complex commercial disputes. In addition, where a settlement agreement is reached, the parties may withdraw their claims, in which case the arbitration institution will normally refund part of the arbitration fees if the withdrawal occurs before the commencement of the hearing.

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88. C.J. Hamson, "In Court in Two Countries: Civil Procedure in England and France," *The Times*, November 15, 1949, p 5.

89. Sir Richard Scoot, "Legal System and Procedure" in David Hayton (ed.), *Law's Futures* (Hart Publishing 2000), p19.

90. It is pretty much because the harmonious-society-building tone in China by the Chinese leadership. See also subsequent discussions.

91. See Alison Ross, "An Interview with Yu Jianlong," *Global Arbitration Review*, Volume 6 Issue 5 (September 5, 2011).

92. See, generally, Gu Weixia, *Arbitration in China: The Regulation of Arbitration Agreements and Practical Issues* (Sweet & Maxwell 2012), paras 2.033 to 2.046.

More importantly, the rapid economic development of China has become a driving force of the development of med-arb. In the past few decades China has experienced an unrivalled growth in the volume of commercial transactions. An inevitable consequence of this development has been a dramatic increase in commercial disputes.<sup>93</sup> A large portion of the disputes are resolved through arbitration, which is often combined with mediation.<sup>94</sup> As such, the use of med-arb will inevitably become a norm (if it is not already) in China's dispute resolution system. Given the dominance of med-arb in Chinese commercial dispute resolution, the due process standard governing med-arb is likely to have significant impact on China's overall legal environment, particularly because this is an area that both Chinese companies and foreign companies investing in China favour for its overseas enforceability.<sup>95</sup> As med-arb continues to play a significant role in Chinese dispute resolution, its better institutionalisation will not only ease due process concerns regarding the dispute resolution system in China, but will also promote legal consciousness and acceptance of the law in Chinese society.

A system of rule of law must feature independent and impartial decision makers and a process that ensures the protection of fundamental rights and interests. It does so by subjecting individuals, as well as state authorities, to a uniform set of rules from both substantive and procedural perspectives. The last part of this Article will explore how an institutionalised system of med-arb will help promote China's rule of law process from the following three perspectives: (A) control of discretion; (B) equality before the law; and (C) certainty of the law.

#### A. *Control of Discretion*

The bedrock of the rule of law is that decisions must be made in accordance with legal rules as opposed to an individual person's discretion. The misuse or abuse of the state power is perhaps the greatest threat to the rule of law in a society.<sup>96</sup> Due to the element of personal choice inherent in discretion, laws conferring discretion are often met with criticism. A.V. Dicey, for example, equated discretion with arbitrariness.<sup>97</sup> Hence,

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93. Gu Weixia, *Arbitration in China: Regulation of Arbitration Agreements and Practical Issues* (Sweet & Maxwell, 2012), paras. 1.002-1.004.

94. About 20 to 30 percent of the cases are resolved through med-arb at CI-ETAC. See Paul E. Mason, Follow-Up Note to 'The Arbitrator as Mediator, and Mediator as Arbitrator' (2011), *J. Int. Arb.* 6, 541.

95. Unlike Chinese civil and commercial judgments which cannot be easily enforced across the border, because China is a member to the New York Convention, Chinese arbitral awards, including those made following the med-arb procedures, can be enforced overseas. This makes med-arb, which is a big portion of the arbitration practice in China, an appealing dispute resolution to domestic and foreign investors investing in China.

96. A.V. Dicey, *Introduction to the study of the law of the constitution* (Liberty Fund 1982).

97. *Ibid.*

restricting human discretion in the exercise of judicial power forms an important cornerstone of the rule of law.

An institutionalised system of med-arb contributes to China's development of rule of law because it helps control and restrict the exercise of discretion by arbitrators in the med-arb process. It is a well-known fact that arbitrators enjoy wide discretion in international arbitration, particularly over procedural matters. Due to the delocalized nature of arbitration, arbitral proceedings are not subject to the complex procedural rules that govern litigation before a local court. A typical set of arbitration rules will confer upon the tribunal the discretion to conduct the arbitration in any manner it sees appropriate, subject only to the basic procedural requirements in the mandatory arbitration law.<sup>98</sup> Indeed, the procedural flexibility of arbitration is one of the reasons for its popularity. But the exercise of discretion will become arbitrary if an arbitrator makes decisions based on irrelevant factors.<sup>99</sup> In the context of med-arb, because the information that an arbitrator gains by participating in mediation would not otherwise be made available to him or her in the course of arbitration, its use is plainly arbitrary and needs to be prohibited.

The problem with med-arb process lies in the inherent difficulty of disregarding one's knowledge and feelings. It is for this reason that procedural safeguards are needed to ensure that an arbitrator, in exercising his discretion, consciously disregards information that he receives by participating in mediation. The procedural safeguards proposed in Part IV above are designed to achieve this purpose by controlling the arbitrator's exercise of discretion through various requirements and mechanisms. The better improved a system is, the fewer chances that a decision will be made arbitrarily.

It needs also to be held in mind that arbitral awards have the same binding force as a court judgment. An arbitrator's decision has substantive influence over the rights and interests of the parties. The Chinese legal tradition, in terms of legal history, places more emphasis on outcome (substantive and distributive justice), rather than due process (procedural justice). Given that China is a jurisdiction without established due process traditions, where arbitrators are more likely to exercise their discretionary power arbitrarily in the absence of proper safeguards, the restriction of arbitrators' discretion in the med-arb process is of pivotal significance.

## B. *Equality before the Law*

Equality before the law is another fundamental principle of the rule of law and the Universal Declaration of Human Rights provides that "all... are entitled without any discrimination to equal protection

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98. See for example, Article 19 of the UNCITRAL Model Law, which provides that in the absence of express provision and parties' agreement, the tribunal has the power to "conduct the arbitration in such manner as it considers appropriate"

99. D.J. Galligan, 'Arbitrariness and Formal Justice in Discretionary Decisions', in: D.J. Galligan (ed.), *Essays in Legal Theory* (Melbourne University Press 1984).

of the law”<sup>100</sup> Under the principle of equality, each individual ought to be subject to a uniform set of rules and equal treatment. An unequal application of law will allow decision makers to act arbitrarily and abuse their power by subjecting different classes of similarly situated individuals to different standards.

Inequality before the law exists in the context of med-arb when an arbitrator favours one party over the other, perhaps by reason of having engaged in in-depth discussions with that party while in caucus. The arbitrator may, consciously or unconsciously, exercise his discretion in favour of that party to the prejudice of the other. An institutionalised system will help minimize the chances of parties receiving unequal treatment. For instance, if caucuses can only be held in the presence of arbitration commission staff (for example, as under the BAC rules), it is more likely that the two parties, even if they meet separately with the arbitrator, will be subject to equal treatment by the arbitrator because of the presence of an independent supervisor.

Equality before the law also requires that redress be made available to parties if unequal treatment occurs in the process of reaching a decision. In med-arb, redress is realized when parties are given an opportunity to dismiss the arbitrators if the arbitrators’ conduct or attitude in the course of mediation rises to the level of apparent bias. Without such a safeguard, parties are less likely to receive equal treatment.

### C. *Certainty of the Law*

As with control of discretion and equality before the law, certainty of the law is internationally recognized as a central requirement for the rule of law. Certainty of the law requires that laws be clear and precise, be made public, and that retrospective application of the law be prohibited. What lies at the heart of certainty of the law is consistency and predictability. In order for the law to be predictable, judges must interpret and apply the law in the same manner so that an individual will be able to predict the result of his or her case by looking at past decisions.

The current practice of med-arb in China is inconsistent due to a lack of uniform statutory requirements. The China Arbitration Law fails to give sufficient guidance for how med-arb should be conducted. As a result, med-arb practices in China are highly disparate. Arbitration rules are also insufficiently clear. Many arbitration rules fail to address the issue of caucuses and, moreover, fail to provide for procedural safeguards that would help promote a uniform practice of med-arb.

The facts in the *Keeneye* case are a good reflection of the uncertainty in current med-arb practice: while some mediations may be held at the hearing facilities of the arbitration center, some may be held over a dinner table at a hotel. While some arbitrators engage in substantive discussion with a party during caucuses or even give a hint of his or her views on the case (such as “working on” parties), others may refrain from

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100. Article 7 of the Universal Declaration of Human Rights.

doing so. These disparate practices lead to uncertainty of the law because the results of a med-arb may be different depending on how it is conducted in each individual case. The increasing institutionalisation of med-arb will help promote certainty of the law by implementing safeguards against issues that threaten the certainty of the law, such as the partiality of arbitrators.

D. *Conclusion: Contribution of Institutionalisation to Rule of Law Development*

The procedural rules of med-arb are highly pertinent to China's development of the rule of law. Under the current arbitral rules, arbitrators-turned-mediators, or mediators-turned-arbitrators have excessive discretion and flexibility.<sup>101</sup> This is incompatible with the due process requirements of modern dispute resolution systems and results in arbitrary "solutions" that do not accord with the rule of law. On careful inspection, the three crucial elements of the rule of law – control of discretion, equality before the law, and certainty of the law, are all intertwined with the institutionalisation of med-arb. In essence, all three principles require a well-functioning mechanism to regulate and control the "human" elements in the process of decision-making so as to establish a fair dispute resolution system. As such, the better institutionalisation of med-arb bears particular relevance to China in her progression towards establishing rule of law. Moreover, the significance of this institutionalization is particularly important, considering the wide reliance on med-arb in China, a reliance that looks likely to only increase with time.

## VI. CONCLUSION

When conducting med-arb in China, if mediation is successful and a settlement agreement is reached, the parties may request that the tribunal render an arbitral award as per the settlement agreement that enjoys the same international legal effect as any other arbitral award.<sup>102</sup> As China is a signatory state to the international arbitration enforcement standards governed under the New York Convention, the process through which med-arb is carried out in China inevitably has international legal ramifications. In its current state, the version of med-arb widely practised in China is highly controversial as it allows for the roles of mediator(s) and arbitrator(s) to be assumed by the same person(s), thus giving rise to significant due process concerns.

Despite having embarked on a series of legal reforms to promote the rule of law since 1978, China is often challenged for its underdeveloped dispute resolution system. When local Chinese custom clashes with

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101. See, for example, Article 45(2), 2012 CIETAC Rules, which permits an arbitral tribunal to mediate a case in a manner it considers appropriate with the consent of the parties.

102. Articles 45(4)-(5), 2012 CIETAC Rules. See also Article 49 of the Arbitration Law of the PRC.

international standards, a dilemma emerges. The huge commercial case-load in China and China's own tradition of harmonious dispute resolution explain why med-arb is prevalent in China. However, the Chinese med-arb process lacks international recognition. With arbitral tribunals given wide discretionary powers in conducting med-arb proceedings and a lack of procedural safeguards protecting parties, problems such as violations of due process are inevitable, and Chinese med-arb clearly fails to adhere to the rule of law. One of the most recent cases involving Chinese styled med-arb practice – the *Gao Haiyan v. Keeneye Holding Ltd.* case in 2011 – came under fire internationally for the ways that Chinese practice deviated from the rule of law and international standards.<sup>103</sup>

It is of paramount importance to overhaul the current med-arb mechanism in China to bring China closer to the rule of law and to cater to the rising numbers of foreign investors who distrust the Chinese courts and favour arbitration. This Article has reviewed the current regulatory landscape of med-arb in China and critically examined its norms and practices. Moreover, it identified gaps between the regulatory mechanisms in China and the international standards. Bearing in mind that it is in China's interests to make improvements, this Article has proposed a better institutionalisation of the med-arb process and shed light on its significance in regards to China's progress in establishing rule of law. As med-arb is heavily utilized, the institutionalisation of the mechanism and a refining of the rules will have a great impact on China's dispute resolution environment as a whole and the development of rule of law.

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103. See the Hong Kong Court of Appeal case of *Gao Haiyan v Keeneye Holdings Ltd* [2012] 1 HKLRD 627.