



# INTERNATIONAL ARBITRATION ALERT

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## THE SOUTH CHINA SEA ARBITRAL AWARD: DOES IT REFLECT CHINA'S ATTITUDE TOWARDS INTERNATIONAL ARBITRATION

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The PCA found that it had jurisdiction to entertain the dispute and on the merits held that China violated the UNCLOS by, among others things, infringing on the Philippines' exclusive economic zone. The PCA emphasised that it did not rule on any question of sovereignty over land territory and did not delimit any boundary between China and the Philippines. There are strong proponents stating that the PCA had the jurisdiction to entertain the dispute, as it was restricted to the interpretation of UNCLOS, despite China not actively participating in the arbitration proceedings. Other proponents state that the PCA should never have entertained the dispute, as it dealt with questions of sovereignty without China's expressed consent to the arbitration.

Without going into the legal basis of why the PCA concluded it had jurisdiction to entertain the dispute or the PCA's findings on the merits, does the refusal or failure by China to adhere to the South China Sea arbitral award (as it expressly indicated it would not) create the impression that China does not respect the outcome of any arbitration proceedings initiated against it? Further, has the arbitral award caused any reputational damage to China's initiatives to promote international commercial and investment arbitration, particularly with economic groupings such as BRICS? In answering these questions one must understand the following:

- The nature of the arbitration between China and the Philippines was a state-to-state arbitration (so-called "equal players") which is inherently politically charged, even though the legal conclusion reached by the PCA might be based on sound international law principles.



- China is not the first great power to ignore arbitration awards by the PCA. For that matter all five members of the UN Permanent Security Council (now also China) have ignored or refused to abide by arbitral awards by the PCA: the US for mining the harbours of Nicaragua, Russia in respect of a dispute with the Netherlands over a detained Dutch vessel, the UK in respect of its unilateral establishment of a Marine Protection Area in the Chagos Islands.
- From a trade and investment perspective, China has respected and complied with international tribunal decisions against it, specifically by the WTO Dispute Settlement Body on various trade related measures imposed by China.

Why should China's refusal to comply with the arbitral award of the PCA be treated any differently than other nations who have also failed to do so? Specifically, why should its failure to comply with this arbitral award be automatically construed as jeopardising international commercial arbitrations and international investment arbitrations in China? As a leading global economic player it is not in China's best interest to create the impression that it is anti-international arbitration or above the rule of law. In international commercial and investment arbitrations the political element is to some extent removed as one deals with either two private parties to a commercial dispute or a private foreign investor against the state.

China's outward direct investment now exceeds its inward direct investment making it very important for China to ensure that a robust and sound international arbitration system exists which protects its investors and traders in foreign jurisdictions. From China's conduct to date in promoting international commercial arbitrations and international investment arbitrations, one cannot logically conclude that its refusal to comply with the South China Sea arbitral award makes it anti-arbitration or selective on compliance with arbitral awards. From a BRICS perspective, China is the leading economy in the BRICS economic grouping, constituting more than approximately 70% of the GDP of the

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BRICS nations and approximately 50% of the population of three billion people. In the past few years China has been very active in promoting international arbitration for the settlement of both commercial and investment disputes, through the establishment of international arbitration centres such as China Africa Joint Arbitration Centre and concluding various bilateral investment treaties (BITs) in light of its new investment policies. In becoming a major outward direct investor, China had to conclude numerous BITs to ensure its investors are protected and specifically have recourse to investor-state arbitration.

Pursuant to the South China Sea arbitral award certain of the BRICS members have extended their support to China for a peaceful diplomatic resolution of the continued stand-off with the Philippines, while India was the only member to make an official public statement recording that:

India believes that States should resolve disputes through peaceful means without threat or use of force and exercise self-restraint in the conduct of activities that could complicate or escalate disputes affecting peace and stability. Sea lanes of communication passing through the South China Sea are critical for peace, stability, prosperity and development. As a State Party to the UNCLOS, India urges all parties to show utmost respect for the UNCLOS, which establishes the international legal order of the seas and oceans.

The statement is diplomatic, but essentially suggests that China must abide by the arbitral award of the PCA. For BRICS a robust system for the settlement of international commercial and investment disputes is important for further economic cooperation. Although the South China Sea arbitral award will continue to be a topic of debate, it should not hamper closer economic co-operation between the BRICS members.

China's position on the South China Sea arbitral award should be assessed independently from its position on international commercial and investment arbitrations, including how it has conducted itself with international trade disputes under the auspices of the WTO. China is well aware that it will be the biggest loser should it fail to comply with international commercial or international investment tribunal awards, as its own investors (such as major Chinese SOCs) and traders will ultimately be prejudiced by such an attitude.

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*Jackwell Feris*



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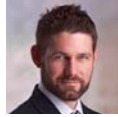
**Tim Fletcher**  
National Practice Head  
Director  
T +27 (0)11 562 1061  
E [tim.fletcher@cdhlegal.com](mailto:tim.fletcher@cdhlegal.com)



**Rishaban Moodley**  
Director  
T +27 (0)11 562 1666  
E [rishaban.moodley@cdhlegal.com](mailto:rishaban.moodley@cdhlegal.com)



**Jackwell Feris**  
Director  
T +27 (0)11 562 1825  
E [jackwell.feris@cdhlegal.com](mailto:jackwell.feris@cdhlegal.com)



**Jonathan Ripley-Evans**  
Director  
T +27 (0)11 562 1051  
E [jonathan.ripleyevans@cdhlegal.com](mailto:jonathan.ripleyevans@cdhlegal.com)



**Thabile Fuhrmann**  
Director  
T +27 (0)11 562 1331  
E [thabile.fuhrmann@cdhlegal.com](mailto:thabile.fuhrmann@cdhlegal.com)



**Jonathan Witts-Hewinson**  
Director  
T +27 (0)11 562 1146  
E [witts@cdhlegal.com](mailto:witts@cdhlegal.com)

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### JOHANNESBURG

1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa. Dx 154 Randburg and Dx 42 Johannesburg.  
T +27 (0)11 562 1000 F +27 (0)11 562 1111 E [jhb@cdhlegal.com](mailto:jhb@cdhlegal.com)

### CAPE TOWN

11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.  
T +27 (0)21 481 6300 F +27 (0)21 481 6388 E [ctn@cdhlegal.com](mailto:ctn@cdhlegal.com)

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