Supreme People's Court
Reply Regarding First Investment Corp (Marshall Island)'s Application for Recognition and Enforcement of an Arbitral Award Made in London by an ad hoc Arbitral Tribunal

27 February 2008

Higher People's Court of Fujian Province:

We acknowledge receipt of your Report Regarding First Investment Corp (Marshall Island)'s Application for Recognition and Enforcement of an Arbitral Award Made in London by an ad hoc Arbitral Tribunal, with the reference of (2007) Min Min Ta No 27. Having considered the issues, we agree with the conclusion of the opinion of the Judicial Committee of your court regarding the handling of the case.

This is a case brought up by First Investment Corp (Marshall Island) for recognition and enforcement of an arbitral award made in London by an ad hoc arbitral tribunal. China is a contracting state to the 1958 Convention for the Recognition and Enforcement of Foreign Arbitral Awards ("the New York Convention"), recognition and enforcement of this arbitral award should be considered in accordance with the New York Convention.

Although the arbitral tribunal in the present case was composed of three arbitrators, Arbitrator Wang Shengchang did not participate in the whole process of the arbitral proceedings, he did not participated in the full deliberation of the final arbitral award Therefore, the composition of the arbitral tribunal or the arbitral procedure is not in accordance with the provisions of the agreement between the parties, and in violation of the law of England as the place of arbitration. According to provisions of Article 5-I-(d) of the New York Convention, the arbitral award shall not be recognized or enforced.

Appendix:

Higher People's Court of Fujia Province
Report Regarding First Investment Corp (Marshall Island)'s Application for Recognition and Enforcement of an Arbitral Award Made in London by an ad hoc Arbitral Tribunal

12 October 2007

Supreme People's Court:

Regarding First Investment Corp (Marshall Island)'s ("FIC") Application for Recognition and Enforcement of an Arbitral Award Made in London by an ad hoc Arbitral Tribunal, Xiamen Maritime Court I to refuse recognition and enforcement of the arbitral award. In accordance with the requirement contained in your court's (1995) No. 18 Notice For The Handling of Relevant Issues Concerning Matters In Relation to Foreign Arbitration and Foreign Related Arbitration, Xiamen Maritime Court reported the case to this court. Having considered the issues, the Judicial Committee of this Court agreed with the opinion of the Xiamen Maritime Court. Now the opinion of this Court is reported below:

I The composition of the tribunal is not in accordance with the agreement of the parties, and also not in accordance with the law of the place of arbitration, according to Article V-I-(d) of the New York Convention recognition and enforcement shall be refused

A. The arbitral award has not been deliberated on by all members of the tribunal, the composition of the arbitral tribunal is in violation of provisions of the arbitration clause in respect of composition of the tribunal.

1. The provisions in the arbitration clause in respect of composition of the arbitral tribunal

The arbitrate clause is contained in the Option Agreement concluded between claimant and respondent on 15 September 2003. Providing for "matters in disputes shall be resolved by an arbitral tribunal composed of 3 arbitrators", the clause required that any disputes arising out of or in relation to the contract must be arbitrated before an arbitral tribunal composed of 3 arbitrators, and also that the 3 arbitrators should participate in the whole process of the following proceedings, including: hearing of all the evidence presented by the parties; hearing of the arguments presented by the parties; deliberation on the award among the arbitrators.

2. Arbitrator Wang Shengchang has not participated in the deliberation of Procedural Order No. 8

The Order comprised of 3 parts, namely, introduction, notice of the arbitral award and draft dissenting opinion, and the request by the respondent dated 2 March 2006. On 2 March 2006, the respondent requested the tribunal to return to the proceedings. The majority of the tribunal, without the participation of Wang Shengchang, rejected the respondent's request of 2 March 2006 on the grounds that "the factual background relied upon by respondent for this request is irrelevant to the liability issue or the quantum issue in the present case" and that "even if Wang Shengchang had participated in the making of this decision, it would be impossible for him to persuade the majority to change their determinations." It was stated in the Order that "for some time, we have lost contact with Dr. Wang Shengchang". Obviously, Wang Shengchang

has not participated in the deliberation of the Procedural Order No. 8.

3. Arbitrator Wang Shengchang has not participated in the whole process of deliberation on the final arbitral award

(i) Completion of deliberation on the first draft of the award did not end the process of deliberation.

Prior to the rendition of the arbitral award, the arbitral tribunal had deliberated the issues under the award by various means and under various occasions. According to the facts described in Procedural Order No. 8, there had been 3 drafts of the final award, dated 21 January 2006, 25 March 2006 and 31 March 2006 respectively. Completion of deliberation on the first draft did not mean completion of the whole process of deliberation, because: first, after the second draft was prepared, Martin Hunter, as chairman of the chairman of the tribunal, sent the second draft to the other two arbitrators, Wang Shengchang and Harris Bruce, for their reviewing, indicating that the process of deliberation was continuing; second, in the tribunal's letter of 3 May 2006, Martin Hunter expressly stated that the tribunal had substantially finished its deliberation, but had not yet finished the whole deliberation; third, Wang Shengchang used the word "draft" on his comments, an indication that his comments on the first draft of the award was not final, and also that the process of deliberation had not come to an end. Therefore, completion of deliberation of the first draft of the award did not end the process of deliberation.

(ii) According to the facts described in Procedural Order No. 8, Wang Shengchang had only presented his draft dissenting opinion on the first draft, bud had not participated in the whole process of deliberation on the final award.

On 21 January 2006, Martin Hunter finished the first draft of the final award, which was distributed to Wang Shengchang and Harris Bruce. On 16 February 2006, Wang Shengchang presented his draft dissenting opinion, and in early March, Harris Bruce presented his comments on the draft. On 25 March 2006, Martin Hunter distributed the second draft of the award marked "Draft 2 (final) -23-3-06". On 31 March 2006, having incorporated some clerical comments from Harris Bruce, Martin Hunger finalized the arbitral award, and sent it to Wang Shengchang and Harris Bruce for their signature. The Order clearly stated that Wang Shengchang's participation in the deliberation of the final award was limited to the first draft.

(iii) According to the facts described in the tribunal's letters of 3 May 2006 and 28 July 2006, Wang Shengchang had not participated in the arbitral proceedings after February 2006, and had not participated in the whole process of deliberation on the final award.

In his letter of 3 May 2006, the chairman of the tribunal, Martin Hunter, informed the

parties: that the tribunal has substantially completed the deliberation, and two of the arbitrators had already signed the award, the other arbitrator, Dr. Wang Shengchang, had lost contact for a period of time; that Dr. Wang Shengchang had previously expressed his intention to sign the award as suggested by the majority of the tribunal with his reservations; that Dr. Wang Shengchang had sent his draft dissenting opinion to the other two members of the tribunal. In his letter of 28 July 2006 to counsel of the parties, Martin Hunter explained that the last time Harris Bruce and Martin Hunter was in contact with Wang Shengchang was in February 2006, since then they had not heard anything from him. The above facts demonstrated that Wang Shengchang had not participated in the arbitral proceedings after February 2006.

(iv) From the factual circumstances of Wang Shengchang being subjected to coercive measures, he could not have participated in the whole process of deliberation in this arbitration

Wang Shengchang was subjected to custody on criminal charges on 20 March 2006. From this it is obvious that he had not read the second draft of the arbitral award which was sent to him by Martin Hunter on 25 March 2006, nor had he read the final draft dated 31 March and other documents thereafter, he could not have participated in the whole process of deliberation in this arbitration.

The above evidence shows that after Wang Shengchang lost contact in late February 2006, the arbitration proceedings were attended to by only two arbitrators, Martin Hunter and Harris Bruce. It is a violation of the provision that "matters in dispute shall be resolved by an arbitral tribunal composted of 3 arbitrators" as contained in the arbitration clause that the remaining 2 arbitrators continued the arbitral proceedings.

B. Composition of the tribunal is in violation of the law at the place of arbitration regarding composition of arbitral tribunal

The English Arbitration Act 1996 contains provisions to deal with the situation where an arbitrator refuses or is unable to hold office as an arbitrator, the legal remedy for a truncated tribunal includes (1) revocation of the authority of the arbitrator; (2) removal of the arbitrator by the court; (3) filling of vacancy by appointment of another arbitrator.

In the present case, when Wang Shengchang was under coercive measures, he was unable to continue the arbitral proceedings, and unable to hold office as an arbitrator. Under the English Arbitration Act 1996, when an arbitrator is unable to hold office, the parties have the statutory right to agree on whether a replacement arbitrator is to be appointed. The parties can either, by agreement or by joint action, revoke the authority of Wang Shengchang as an arbitrator in accordance with Article 23 of the English Arbitration Act 1996 regarding "revocation of arbitrator's authority", and let Martin Hunter and Harris Bruce to constitute a 2 member tribunal to continue the

arbitral proceedings; or the parties can apply to the court to remove Wang Shengchang as an arbitrator in accordance with Article 24 of the Act regarding "power of court to remove arbitrator" due to his inability to discharge his duty; or according to Paragraph (1) of Article 27 of the Act under the heading "filling of vacancy", where an arbitrator ceases to hold office, the parties are free to agree: (a) whether and if so how the vacancy is to be filled, (b) whether and if so to what extent the previous proceedings should stand, and (c) what effect (if any) his ceasing to hold office has on any appointment made by him (alone or jointly). The above three measures are the parties' statutory rights, which can not be deprived of.

Paragraphs (2) and (3) of Article 27 of the Act further provide that if or to the extent that there is no such agreement, the provisions of sections 16 (procedure for appointment of arbitrators) and 18 (failure of appointment procedure) apply in relation to the filling of the vacancy as in relation to an original appointment.

Therefore, in the present case, when the circumstance arose where Wang Shengchang became unable to hold office, before the parties have taken actions according to the law, Martin Hunter and Harris Bruce could not validly constitute an arbitral tribunal and continue the proceedings.

C. Majority opinion is not a remedy for the defect in the composition of the tribunal

According to the opinion of Martin Hunter and Harris Bruce, the arbitral award was made according to majority opinion of the tribunal, even if Wang Shengchang had participated in the whole process from the end of March 2006 to the end of the arbitral proceedings, the arbitral award would not have been changed at all. Procedural Order No. 8 stated in paragraph 5 that most of the modern arbitration rules have authorized a truncated tribunal to continue the arbitral proceedings under certain circumstances, and the LMAA Terms 2002, which was the applicable rules in the present arbitration, provide under Article 8(c) that "after appointment of the third arbitrator decisions, orders or the award shall be made by all or a majority of the arbitrators."

However, a majority opinion is not a remedy for the defect in the composition of the tribunal.

First, the presumption that an award by majority opinion is a valid award is applicable in and only in circumstances where all the arbitrators have participated in the whole process of the arbitral proceedings. A majority opinion is meaningless where only some of the arbitrators have participated in the arbitral proceedings. Where a member of the tribunal was unable and in fact did not participate in the arbitral proceedings, the question is not about a majority or minority opinion, but rather a question about

whether the remaining arbitrators can still continue the arbitral proceedings.

Second, if a majority opinion alone can bind the parties, then after the appointment of Wang Shengchang and Harris Bruce by the parties respectively, as long as they were in agreement they would not have to appoint Martin Hunger as the third arbitrator, for whatever Martin Hunter's opinion might be, a majority opinion agreed upon by Wang Shengchang and Harris Bruce would stand unchanged. In fact, even Martin Hunter and Harris Bruce themselves were not in agreement with this suggestion. As mentioned above, in his fax dated 28 July 2006, Martin Hunter clearly said that he and Harris Bruce could not make a decision on the costs of the tribunal unless the parties' consent was obtained. If the suggestion that an award by majority opinion is valid applies, then as long as Martin Hunter and Harris Bruce were in agreement, they would have been able to issue a valid decision on the costs of the tribunal even without the participation of Wang Shengchang. As a matter of fact, they did not do so, this is just an indication that without the participation of Wang Shengchang, the suggestion that an award by majority opinion is valid is unsustainable.

D. When qn arbitrator was unable to hold office, the arbitral tribunal failed to inform the parties accordingly, causing a defect in the composition of the tribunal, and the arbitration proceedings in violation of the law at the place of arbitration

As explained above, the English Arbitration Act 1996 contains provisions to deal with the situation where an arbitrator refuses or is unable to hold office and has provided legal remedies for defects in the composition of an arbitral tribunal. In the present case, the tribunal in its letter of 3 May 2006 stated that deliberation had been substantially concluded, and an arbitral award by majority opinion was forthcoming. This is the most severe mistake by the tribunal, which deprived the parties of their statutory rights, and the remedies that they might have chosen to resort to.

II. The arbitral award dealt with disputes not covered by the arbitration agreement, exceeded the jurisdiction of arbitration, for which recognition and enforcement should be refused under Article V-I-(c) of the New York Convention.

The parties' agreement to arbitrate in London was contained in the Option Agreement. Therefore, any disputes that may be subjected to arbitration in accordance with this arbitration clause must be within the scope of coverage of the Option Agreement. Under the Option Agreement, claimant FIC had appointed 8 single vehicle companies incorporated in Marshall Island as parties to sign an optional shipbuilding contract with respondent, namely Magna Maritime SA, Magnifico Maritime SA, Magnolia Maritime SA, Magnum Maritime SA, Maistrali Maritime SA, Margarita Maritime SA, Mimosa Maritime SA, Myrtia Maritime SA ("the 8 appointed companies", the second to ninth claimants in the arbitration). As a consequence of this act, claimant FIC was not a buyer under the optional shipbuilding contract. When the claimant had

appointed the 8 appointed companies as buyers of the optional shipbuilding contract, the claimant stepped out of the transaction of optional shipbuilding, there was no longer a contractual relationship for optional shipbuilding between claimant FIC and the respondent. Since no optional shipbuilding contract had been signed in the event, the arbitration clause contained in the contract had not come into force, there was not an agreement to arbitrate between the respondent and the 8 appointed companies. However, the tribunal accepted and dealt with the contractual claims including those of the 8 appointed companies. Though the final award declared that the 8 appointed companies were not appropriate parties in the arbitration, the tribunal embraced the alleged losses of the 8 appointed companies within the scope of the arbitration. In the final award, the tribunal reasoned that claimant FIC, after having made the appointment, was free to withdraw the appointment, and claim for the losses in its own name. But the key issue here is that as a matter of fact claimant FIC had never withdrawn its appointment after the appointment was made. According to the original Option Agreement, it is the 8 appointed companies that was to signe the optional shipbuilding contract with the respondent. If the respondent was in breach of contract, it is the 8 appointed companies that would have suffered losses, not the claimant FIC. While the tribunal declared that the 8 appointed companies were not appropriate parties in the arbitration, the tribunal nevertheless embraced the disputes between the 8 appointed companies and the respondent and their alleged losses in the scope of this arbitration, and finally awarded the losses of the 8 appointed companies in favor of the claimant FIC. The content and effect of the award obviously went beyond the obligations of the respondent agreed under the Option Agreement. In essence, the subject matter of this arbitration should have been the disputes between claimant FIC and respondent under the Option Agreement, the tribunal nevertheless embraced the disputes between the 8 appointed companies and the respondent under the optional shipbuilding contract in the scope of the arbitration. Therefore, the arbitral award falls under the circumstances of Article V-I-(c), which states that “the award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, … ”, exceeded the jurisdiction of the tribunal, and should be refused recognition and enforcement.

III. Misconduct of the arbitral proceedings deprived the respondent of its opportunity and right of defense

At the initial stage of the arbitration, respondent raised objections to the standing of 8 appointed companies as claimants in the arbitration, claimant FIC and the 8 appointed companies insisted on the 8 appointed companies being named as claimants. In the process of the arbitral proceedings, the tribunal failed to clarify on the relationship between the standing of the 8 appointed companies and possible outcome of the arbitration and its impact thereon, and in its Procedural Order No. 1 rejected respondent’s request for a decision on this issue as a preliminary issue. Such a

procedural misconduct had the effect of misleading the respondent, and had serious impact on the procedure and outcome of the arbitration. The respondent was misled to pursue this issue, and focused its submissions and arguments on the defense of the 4 grounds raised by claimant FIC for purpose of this issue under various theories of "agency, promise in trust, assignment, and the Contracts (Rights of Third Parties) Act 1999", to the point that both parties regarded this issue as so essential as a key issue in the whole proceedings. Only in the final stage, the tribunal decided that the 8 appointed companies lacked the standing to be named as claimants in the arbitration, and ruled that "under the English law, to the extent that the 8 appointed companies can prove their respective losses, FIC is entitled to compensation for such losses." Prior to this moment, the tribunal failed to direct the parties to include in the issues in dispute such important questions as whether the losses of the 8 appointed companies could be deemed as FIC's losses, and whether FIC could and in fact did withdraw its appointment of the 8 appointed companies, and failed to direct the parties to present their submissions on the factual and legal issues as just mentioned. Therefore, the outcome of the tribunal's award was based on arbitrary conclusions such as that FIC was free to withdraw its appointment, etc., which conclusions were reached by the tribunal without investigation and examination on the factual issues and full argumentation on the legal issues. This obviously deprived the respondent of its opportunity and right to present its case on this issue. Therefore the arbitral procedure is defective, falls under the circumstances described in Article V-I-(b) of the New York Convention which states "the party against whom the award is invoked was not give proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case", therefore, the arbitral award should be refused recognition and enforcement.

IV. The tribunal's treatment of the "without prejudice documents" in the arbitral proceedings is procedurally defective, and in violation of English law, and falls within the coverage of Article V-I-(d) of the New York Convention on arbitral procedure not in accordance with the law at the place of arbitration

Under English law, "without prejudice documents" refer to part or all of the contents of negotiations originally aimed at a settlement of the disputes. Under English law, "without prejudice documents" should not be relied by an arbitral tribunal, otherwise the tribunal is suspicious of procedural misconduct, which may lead to denial of enforcement of its award. In this arbitration, the claimant presented without prejudice documents signed by the parties in negotiations aimed at a settlement of the disputes, including "without prejudice" negotiations between the parties conducted orally or in writing and meetings in Fuzhou, Shanghai and other places from September 2003 and onwards. During this period, the respondent asked to increase the price due to the fact that they would suffer a loss of USD2,000,000 for each ship they built as a result of the rise of steal price. In the arbitral proceedings, FIC disclosed in its Statement of Claims the details that the respondent revealed in

those “without prejudice” negotiations as evidence of respondent’s breach of contract. These documents were assessed by an independent appraiser appointed by the tribunal, and were confirmed as containing without prejudice documents which should not be disclosed. These documents left the tribunal an impression that the respondent did not sign the optional shipbuilding contract because they wanted a price increase. This is serious violation of procedural justice. Paragraph 182 of Part 7 of the arbitral award directly quoted respondent’s position put forward in a “without prejudice” negotiation that building a ship at the contract price would produce huge deficits as a result of steel price rise, and the tribunal thus found that the respondent failed to perform its contract because of financial difficulties. Under the English law, this will render the arbitration invalid. On this particular point, the tribunal admitted flaw in procedure, but failed to make any effort for a remedy, except declaring those ‘without prejudice documents” irrelevant, and to be disregarded.

Based on the foregoing, taking into account the serious defects in the arbitral procedure, and in accordance with Article V-I-(b), (c) and(d) of the New York Convention, it is the unanimous opinion of the judicial committee of this court that the arbitral award should be refused recognition and enforcement.

Submitted for your review.