

A Long March towards Compatibility, Coherence and Consistency: the Future of China's Investment Agreements

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A. Introduction

Up to the present, the People's Republic of China (China/P.R.C.) has concluded a large number of international investment agreements (IIAs). China's IIAs roughly include three different types, namely, bilateral investment treaties (BITs),¹ trilateral investment treaty (TIT)² and investment chapters of regional free trade agreements

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1 According to the official website of the Department of Treaty and Law, Ministry of Commerce of the P.R.C. (MOFCOM), up to August 2015, China has concluded over 130 BITs, 102 are currently in force, <http://tfs.mofcom.gov.cn/article/Nocategory/201111/20111107819474.shtml> (9/9/2015). Unless otherwise indicated, all Chinese BITs cited in this article can be found on this website.

2 China has one TIT, namely the Agreement among the Government of the People's Republic of China, the Government of Japan and the Government of the Republic of Korea for the Promotion, Facilitation and Protection of Investment (China-Japan-Korea TIT), <http://tfs.mofcom.gov.cn/article/Nocategory/201405/20140500584797.shtml> (9/9/2015).

(FTAs).³ According to the United Nations Conference for Trade and Development (UNCTAD), China now hosts the second largest number of BITs in the world, next only to Germany.⁴

China remains quite active in IIA-making, which actually forms an important part of its global strategy of participating in global economic governance and rule-making. The ongoing negotiations of the China-US BIT and the China-EU BIT have attracted worldwide attention given the economic size of the contracting parties and the potential profound impacts of the BITs.⁵ It seems unlikely to be disputed that the China-US BIT will be an unprecedentedly high-level BIT for China; it has also been suggested that the China-EU BIT, if successfully concluded, is “likely to become a symbol for the emerging ‘global BIT 2.0’”.⁶

Besides, China has also sped up its FTA-making efforts in recent years. It has just concluded several FTAs with major trade partners, such as the China-Switzerland FTA,⁷ the China-Korea FTA⁸ and the China-Australia FTA.⁹

China’s active engagement in IIA-making and international investment rule-making may have impacts at both national and international levels. There have been ample discussions of China’s existing IIAs, especially BITs. In general, these discussions appear more empirical than prospective, mainly focusing on certain important IIA provisions, such as clauses of most favored nation treatment (MFN), expropriation and compensation (E&C) and investor-state dispute settlement (ISDS). Despite the merits of the existing literatures, scant attention has been paid to China’s IIA-making strategy and its “hidden” interrelation between China’s national economic policy and its potential impacts on international investment rule-making. This paper aims at presenting a brief review of China’s IIA-making program, exploring the correlation between China’s economic policy and IIA-making strategy. Further, as the deepening globalization raises unprecedented challenges to China’s future IIA-making, this paper will also highlight some of the major challenges and raise proposals to help confront them.

This paper has three parts in addition to the introduction (A.) and the conclusion (E.). Part B reviews China’s IIA-making during the 1980s and 1990s, focusing on the correlation between China’s “opening up” policy and the “host state centralism”

3 A list of Chinese FTAs can be found in the website of MOFCOM, <http://fta.mofcom.gov.cn/> (9/9/2015). Unless otherwise indicated, all Chinese FTAs cited in this article can be found on this website.

4 UNCTAD IIA Database, <http://investmentpolicyhub.unctad.org/IIA/IiasByCountry#iiaInnerMenu> (9/9/2015).

5 See *Bungenberg/Chi*, Chinese Investment Law, in: *Bungenberg/Griebel/Hobe/Reinisch* (eds.), *International Investment Law: A Handbook*, 2015, p. 234 et seqq.

6 *Shan/Wang*, The China-EU BIT and the Emerging “Global BIT 2.0”, *ICSID Rev.* 30 (2015), p. 260.

7 This FTA came into force as of 1/7/2014, http://fta.mofcom.gov.cn/article/chinaswitz/chinaswitznews/201404/15576_1.html (9/9/2015).

8 This FTA was signed on 1/6/2015, http://fta.mofcom.gov.cn/article/chinakorea/koreanews/201506/21837_1.html (9/9/2015).

9 This FTA was signed on 17/6/2015, http://fta.mofcom.gov.cn/article/chinaaustralia/chinaaustralianews/201506/22203_1.html (9/9/2015).

mentality in IIA-making and investment governance. Part C discusses China's IIA-making since the new Millennium, highlighting the "Going abroad" policy and the Americanization of Chinese IIAs. Part D discusses the future of China's IIA-making, pointing out China's major challenges and raises suggestions to help confront these challenges. Overall, this article not only reviews China's progress and achievements in its IIA-making history, but also reveals the challenges and risks China will face in the future. If China really wants to play a leading role in international investment rule-making and global investment governance in the future, it should update its perception of IIA and make concerted efforts at national and international levels.

B. The "Opening up" Policy and the "Host State Centered" IIA-making

Different from some Western countries, China has no history of concluding treaties on friendship, commerce and navigation (FCN), which is deemed as the predecessor of modern BITs.¹⁰ China's IIA-making program started in early 1980s, shortly after it started the economic reform and adopted the "Open Door" policy. The major aim of this program is to help China establish a safe and sound legal environment to attract foreign investment, especially foreign direct investment (FDI) to boost its national economy that was at the edge of bankruptcy as a result of years of internal revolution and external isolation.¹¹ China's early IIA-making practice may clearly convey such purpose. Out of the total of 17 BITs of China concluded between 1982 and 1989, almost all were concluded with European and Asian countries, many of which were major FDI exporting countries to China.

During the 1980s and the 1990s, attracting FDI was on the top list of China economic development agenda. China was also a major investment destination country in the world. Thus in IIA-making the central question to China was "how to efficiently and effectively utilize foreign investment to develop its national economy". Gradually, China has cultivated a "host state centralism" mentality in IIA-making, highlighting "preserving power in the hands of host state". To put it plainly, while China is obligated to protect foreign investment as required by its IIAs, it tries to fulfill such obligation without unnecessarily refraining its power in guiding, utilizing, controlling and supervising foreign investment in its territory.

The "host state centralism" mentality in China's IIA-making has two distinct features. First, it is highly economy-oriented. Economic calculations are conducted with great care when negotiating IIAs, while non-economic factors, such as environment and labor rights protection, are not likely to be seriously considered. Second, it stresses "state control" in almost all phases of investment activities, including the entry, using, regulating and even nationalizing of foreign investment.¹² Although foreign investors

10 Berger, China's New Bilateral Investment Treaty Programme: Substance, Rational and Implications for International Investment Law Making, www.die-gdi.de/uploads/media/Berger_ChineseBITs.pdf (9/9/2015), p. 3.

11 See Gallagher/Shan, Chinese Investment Treaties: Policies and Practices, 2009, p. 5 et seq.

12 See e.g. Kong, Bilateral Investment Treaties: The Chinese Approach and Practice, Asian Y.B. Int'l L. 8 (1998-1999), p. 109.

may be granted certain preferential treatment, they are not fully respected as market players. The E&C and ISDS clauses of early Chinese BITs can help demonstrate how China apply such mentality to its IIA-making practice.

China has a notorious history of expropriating private properties. Shortly after its establishment, China launched the “socialist reform” policy in early 1950s, aiming at realizing “socialist industrialization”. The essence of this policy, at least from the perspective of its implementation, is large-scale nationalization/expropriation of private properties of the so-called “capitalist industrialists” (including individuals and enterprises of various forms) with minimum or even no compensation.¹³ Although the 1954 Constitution of the P.R.C. clearly obligates the state to protect the various types of private properties, it also authorizes the state to nationalize and expropriate private properties for “public interest” need.¹⁴ Such situation has not been fundamentally changed even up to the present day, although it is undeniable that China has made great progress in protecting private properties. It is not until the new Millennium that China has adopted its first specialized national law on property protection, the Property Law of the P.R.C.¹⁵

With regard to protection of foreign investments, since the launch of the economic reform by the end of the 1970s, China has gradually become aware and accepted that compensation for expropriation is obligated under international law. It is particularly important for China to enhance its legal protection of foreign investment since it was eager to attract foreign investment to boost its economy. However, with regard to the issue of the standard of compensation for expropriation, China still appeared reluctant to pay “full” compensation for expropriation of private properties, including foreign investment. Such reluctance is clearly reflected in the E&C clause of many Chinese BITs, especially the early ones. According to these BITs, China is only obligated to pay “appropriate” compensation in case of expropriation, while “full” or “adequate” compensation is often resisted, not to mention the “Hull Formula” that requires “prompt, adequate and effective” compensation.¹⁶

Similarly, China’s attitude towards ISDS was also quite “host state-centred” for various reasons. First, due to the private nature of arbitration, investor-state arbitration (ISA) is more often deemed by China as erosion of sovereign judicial power rather than an international dispute settlement mechanism. Second, in general, China has formed a cultural tradition of non-confrontational dispute settlement. Conciliation and mediation are more often preferred to litigation and arbitration as they appear less confrontational. Third, China also has a tradition of prioritizing state interests over private interests. Because ISA enables foreign private parties to directly challenge state measures and legislations, it is deemed as a potential threat to the dignity of state.

13 See *Gallagher/Shan*, (fn. 11), p. 4 et seq.

14 Article 13, Constitution of the People’s Republic of China, adopted at the 1st Meeting of the 1st National People’s Congress of the People’s Republic of China on 20/9/1954.

15 See Property Law of the People’s Republic of China, adopted at the 5th Meeting of the 10th National People’s Congress of the People’s Republic of China on 16/3/2007.

16 See *Ji*, Voluntary “Westernization” of the Expropriation Rules in Chinese BITs and Its Implication: An Empirical Study, *J. World Inv. & Trade* 12 (2011), p. 84.

Fourth, as mentioned, there exists sharp difference with regard to private property protection in Chinese national laws and IIAs. As international arbitrators would review China's measures and legislations according to the standards laid down in the IIAs without necessarily applying Chinese national laws, China had grave concerns that ISDS would incur excessive pressure on its administration, law-making and enforcement. Last but not least, China was a bit uncomfortable with international adjudication due to its distrust of international courts and tribunals that are often predominantly composed of citizens from Western countries. For these reasons, China was reluctant to allow foreign investors to submit disputes to ISA, but tried to keep them within its domestic jurisdiction.

China's unfriendly attitudes towards ISA may be clearly sensed from the ISDS clause of many of its early BITs. These BITs often provide high threshold requirements on the admissibility of disputes for ISA, only allowing "disputes concerning the amount of compensation for expropriation" to be submitted to ISA.¹⁷ In general, a narrow ISA clause is intended to limit the jurisdiction of an arbitral tribunal only to disputes concerning the amount and the procedure of compensation, while excluding disputes concerning the occurrence and legality of an expropriation from the realm of ISA.¹⁸ The latter types of disputes are expected to be decided by national courts and in accordance with the national law of China.

However, it should be noted that ISA case law suggests that narrow ISDS clause may be expansively interpreted in practice. A typical case in this regard is *Tza Yap Shum v. Peru*, the first ISA case relying on a Chinese BIT.¹⁹ The underlying BIT, the China-Peru BIT of 1994, contains a narrow ISDS clause.²⁰ The investor requested the ICSID tribunal to rule, among other things, that Peru's measures constituted expropriation and that he should be compensated.²¹ The tribunal needed to rule on the occurrence of the alleged expropriation and the amount of compensation. While following the international law rules of treaty interpretation laid down in the Vienna Convention on the Law of Treaties of 1969 (VCLT),²² the Tribunal ruled that the narrow ISA clause can be interpreted to cover both the claim of amount of compensation and the claim of occurrence of expropriation.²³ Although, strictly speaking, arbitral awards are not necessary binding on future tribunals, they may have profound

17 See *Chi/Wang*, The Evolution of ISA Clauses in Chinese IIAs and Its Implications: The Admissibility of Disputes for Investor-State Arbitration, *J. World Inv. & Trade* 16 (2015), pp. 862-891.

18 *Reinisch*, How Narrow Are Narrow Dispute Settlement Clauses in Investment Treaties, *J. Int'l Disp. Settlement* 2 (2011), p. 118 et seq.

19 *Tza Yap Shum v. the Republic of Peru*, ICSID Case No. ARB/07/6, www.italaw.com/cases/1126# (9/9/2015).

20 Article 8(3), the China-Peru BIT 1994, <http://tfs.mofcom.gov.cn/aarticle/h/bk/201002/20100206785109.html> (9/9/2015).

21 Decision on Jurisdiction and Competence (19/6/2009), "Jurisdictional Award", www.italaw.com/sites/default/files/case-documents/ita0880.pdf (9/9/2015).

22 Articles 31 and 32, the VCLT.

23 Jurisdictional Award, (fn. 21), para. 192.

influence. Given that many Chinese BITs contain similar narrow ISDS clauses, the potential impacts of *Tza Yap Shum v. Peru* should not be neglected.

C. The “Going abroad” Policy and the “Americanization” of IIAs

The “Going abroad” policy was adopted by the end of the 1990s, mainly aiming at encouraging capable Chinese enterprises to invest abroad.²⁴ There are profound economic and political considerations behind this policy. First, during the first two decades of Opening up, China’s national economy has gradually become export-oriented and import-substitutive. By the end of the 1990s, China faced serious internal economic deflation. To export redundant productivity, especially in the iron and steel industry, it is necessary for China to encourage outbound investment. Second, some Chinese enterprises, although limited in number, were eager to seek chances to invest overseas for better development opportunities. The “Going abroad” policy could help them access the international market and benefit from overseas resources. As many Chinese enterprises that were able to invest abroad are state-owned enterprises (SOEs), the protection of such investment has also become “politicized” to some extent. Third, China may also use this policy as a strategy for distributing foreign aids and exporting service personnel, especially in some African, Southeast Asian and Latin American countries. In the context of “the rise of China”, this policy may also form a part of the overall strategy of raising China’s “soft” power at global level.

The “Going abroad” policy also raises challenges to China’s IIA-making. With the implementing of this policy, an increasing number of Chinese enterprises, many SOEs in particular, have invested abroad heavily, and part of the investments have been channeled to environmentally vulnerable, politically unstable and economically underdeveloped regions, such as African, Southeast Asian and Latin American countries.²⁵ In these regions, Chinese enterprises may face a high risk of expropriation and other unfair treatment. Naturally, they show increasing concerns and aspirations for strong international treaties to better protect their overseas investment.²⁶

Although, in the dictionary of international investment law, it is difficult to find such term as “strong IIAs”, in the Chinese context as mentioned, “strong IIAs” would refer to IIAs that can provide a higher level of investment protection than the protection granted under the national laws of the host states and existing Chinese IIAs. To successfully negotiate “strong IIAs” would require China, inter alia, to allow broader access to ISA and higher standard of compensation for expropriation in its

24 A typical and authoritative expression of the “Going Abroad” strategy can be found in the Tenth Five-Year Plan for National Economic and Social Development, adopted by the 4th Meeting of the 9th National People’s Congress of the People’s Republic of China on 15/3/2001, www.people.com.cn/GB/shizheng/16/20010318/419582.html (9/9/2015), original in Chinese.

25 See China Council for the Promotion of International Trade (CCPIT), Survey on Chinese Enterprises’ Outbound Investment and Operation, www.ccpit.org/docs/2012-08-03/2012_haiwaitouzi_diaochabaogao.pdf (9/9/2015), p. 70.

26 Ibid., p. 103.

IAs. However, this would go against China's traditional "host state mentality". The questions naturally follow: Should China abandon the old mentality and shift to the "home state mentality"? If such a mentality shift is necessary, how should China negotiate and draft IAs in the future? There is no fixed answer to these questions. However, from empirical perspective, China's IIA-making practice in the recent few years seems to show a trend of Americanization, which helped China in answering these questions.

Although no precise definition of the term "Americanization" has been produced in international investment law, this term may be understood as a tendency of making "American style" IAs, modelled after US and Canadian IAs, such as the 2012 US Model BIT and the 2004 Canadian Model BIT. In legal literatures, the term "Americanization" is also used interchangeably with some alternative terms, such as "NAFTA-zation"²⁷ or "westernization".²⁸ Compared with China's existing IAs which are of "European style",²⁹ "American style" IAs in general appear comprehensive and complicated, often with detailed provisions, broader coverage, more self-contained structure and higher level of enforceability. In addition to the major clauses of investment treatment and protection, a typical "American style" IIA would also cover, among others, general exceptions, pre-establishment protection of investment and a standalone ISDS section.

Methodologically, Americanization is not unique to China; it can also be sensed from EU's recent IIA-making. The investment chapter of the EU-Canada Comprehensive Economic and Trade Agreement (CETA) can be seen as a sign of Americanization.³⁰ The negotiation of this chapter, especially its ISDS clause, has aroused heated debate in Europe and across the Atlantic.³¹ If one carefully compares this Chapter with an "American style" IIA and a typical BIT of a European country, one may find that it actually appears more "American" than "European". This chapter is comprehensive and complicated and incorporates a separate ISDS section similar to that of the US and Canadian model BITs. According to the European Commission, the investment chapter of CETA will profoundly influence the negotiations of the investment chapter of the US-EU Transatlantic Trade and Investment Partnership (TTIP), although CETA is not necessarily as the blueprint of TTIP.³²

27 See e.g. *Berger*, Investment Rules in Chinese PTIAs: A Partial "NAFTA-ization" Reintegration, in: Hofmann/Schill/Tams (eds.), *Preferential Trade and Investment Agreements: From Recalibration to Reintegration*, 2013, pp. 297-333.

28 See e.g. *Ji*, (fn. 16), p. 84.

29 *Li*, Factors to Be Considered for China's Future Investment Treaties, in: Shan (ed.), *China and International Investment Law: Twenty Years of ICSID Membership*, 2014, p. 174.

30 Chapter 10 of CETA, http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc_152806.pdf (9/9/2015).

31 See e.g. *McKeagney*, Investor State Dispute Settlement Dominates CETA Debate in Strasbourg, <http://ttip2015.eu/blog-detail/blog/CETA%20Plenary%20September.html> (9/9/2015); GUE/NEL, EU-Canada Trade Deal Not in Tune with Public Opinion, www.guengl.eu/news/article/eu-canada-trade-deal-not-in-tune-with-public-opinion (9/9/2015).

32 Available at <http://ec.europa.eu/trade/policy/in-focus/ceta/questions-and-answers/> (9/9/2015).

With special regard to Chinese IIAs, one is to find that several recent IIAs appear Americanized, although they do not necessarily contain all features of “American style” IIAs. The China-Canada BIT is a convincing example. Different from almost all existing BITs of China, it contains not only standalone ISDS section, covering a wide range of issues from initiating arbitration to award enforcement,³³ but also a clause of general exceptions,³⁴ modeled after the exception clause of the General Agreement on Trade and Tariffs (GATT).³⁵ Both are deemed as symbolic features of “American style” IIA. Besides, although the China-Japan-Korea TIT does not contain a separate ISDS section, its ISDS clause is quite comprehensive and appears much closer to that of an “American style” IIA.³⁶ This is quite indicative given the fact that this TIT is concluded exclusively among Non-American (or Asian) countries.

The Americanization of Chinese IIAs can be sensed from the evolution of the E&C and ISDS clauses of Chinese BITs. The E&C clauses of China’s different generations of BITs have experienced a “Westernization” process.³⁷ With regard to both the conditions for expropriation and standard of compensation, Chinese BITs have become increasingly similar to “American style” BITs. Consequently, although none of Chinese BITs expressly inserts the “Hull Formula”, all of the key elements of this Formula have been absorbed in some recent Chinese BITs.³⁸ Thus these clauses could be interpreted to have the same effect as the “Hull Formula” in arbitral practice. The development of Chinese BITs also shows a clear tendency of broadening the scope of disputes for ISA. As the author has discussed elsewhere, China’s second generation BITs have generally abandoned the narrow ISDS clause used in the first generation BITs to generally allow “investment disputes” to be submitted to ISA.³⁹

Practically speaking, “American style” IIAs provide a convenient model for China’s BIT-making in the new era, because it presupposes China as an investment exporting country vis-à-vis its partner countries. This presupposition seems well founded given the fact that China is now in such a position as one of the leading FDI exporting countries. However, to China, Americanization as an IIA-making strategy may carry not only methodological implications, but more importantly, it may have potential sociopolitical and ideological ramifications. This raises the question whether and to what extent Americanization is truly suitable for China. After all, “American style” IIAs are designed to meet the needs of North American countries. As these countries and China have remarkably different social, political and economic situations, it is doubtful whether “American style” IIAs are truly desirable and feasible for China. For instance, “American style” IIAs sometimes incorporate provisions concerning

33 Section C, the China-Canada BIT.

34 Article 33, the China-Canada BIT.

35 Article 20, the GATT.

36 Article 15, the China-Japan-Korea TIT.

37 *Ji*, (fn. 16), p. 91.

38 See *Chi*, From Ownership-Oriented to Governance-Oriented: An International Economic Law Perspective of China’s Shifting Attitudes towards Resource Sovereignty, in: Bungenberg/Hobe (eds.), *Permanent Sovereignty over Natural Resources*, 2015, p. 109.

39 *Chi/Wang*, (fn. 17), p. 891.

human rights protection.⁴⁰ Yet, since China is quite reluctant to deal with human rights issues in investment and trade agreements, and no Chinese IIAs contain express human rights clauses, it seems quite difficult for China to be truly willing to consider including such issues in IIA-making.⁴¹

Aside from the debate over the suitability of Americanization of IIAs to China, a more pertinent question should be considered, i.e., will Americanized IIAs become “stronger” in protecting Chinese investors and their overseas investment? Indeed, it is difficult to answer this question because it is almost impossible to assess the actual effectiveness and impacts of these IIAs on the protection of Chinese investors and their investments for practical reasons. First, China has not institutionalized an effective communication mechanism between the government (IIA-maker) and the individuals/enterprises (Chinese investor), although informal communication channels do exist at different levels. Besides, many Chinese investors do not have sufficient knowledge of the roles, advantages and defects of IIAs and lack ability in properly using IIAs when making investment decisions. It is difficult for IIA-makers to be accurately and completely informed of the concerns of the investors. Second, Americanization is a just recent trend in China's IIA-making and the number of Americanized IIAs is quite limited. As none of these IIAs has been applied in ISA practice up to the present, it is unclear what practical consequence they will have with regard to investment protection. These have made the economic calculations of the IIA-making extremely difficult for Chinese IIA negotiators. This situation cannot be changed fundamentally unless economic governance reforms are carried out in China.

D. The Challenges to China's Future IIA-making and the Proposed Solutions

More recently, especially since the past few years, China has already grown up to a leading country in both FDI importing and exporting. With its economic rise, China has determined to play an active role in international investment governance and transform itself from a rule-taker to a rule-maker in global investment rule-making.⁴² There are also calls that China should take a leading part in the negotiation of a multilateral investment convention (MIC).⁴³ Although the Chinese government has not formally issued a policy titled “enhancing governance”, it is apparent that active participation in international investment governance, especially global rule-making, is among the top items of China's development agenda. As will be discussed infra, the recent adoption of the “One Belt, One Road” (OBOR) strategy demon-

40 See e.g. Article 13 (Investment and Labor), the 2012 US Model BIT.

41 See *Hang*, Investing in Human Rights: Using Bilateral Investment Treaties to Hold Multinational Corporations Liable for Labor for Labor Rights Violations, *Fordham Int'l L. J.* 37 (2014), p. 1262 et seq.

42 See e.g. *People's Daily*, Making Efforts to Gain Its Say in International Investment Rule-Making, <http://theory.people.com.cn/n/2014/0402/c40531-24801269.html> (9/9/2015), original in Chinese.

43 See e.g. *Shan*, 15 Years in WTO: Changing China, Reforming the World, <http://fxy.xjtu.edu.cn/Newsshow.aspx?Id=1802&ClassId=300&ParentId=297> (9/9/2015).

strates China's ambition and determination to play a leading role in global economic governance. The implementation of the policy will inevitably influence China's future IIA-making.

Nowadays, as China has acquired a blended status (a leading investment importing and exporting country), the "host state centralism" and the "home state centralism" has become one-sided for China. It is necessary for China to negotiate more inclusive IIAs which can better accommodate the seemingly conflicting needs of host state and home state. This not only implies that China should carefully strike a balance between the preservation of state regulatory power and foreign investment protection, but also requires China to become more accommodating to certain public interest values in its IIA-making.

China's IIA negotiators, policy makers and scholars are aware of the need of more inclusive IIAs.⁴⁴ For example, *Yongjie Li*, a highly experienced IIA negotiator of China, has mentioned that "Lessons learned from investor-state arbitration also make states realize the importance of striking a balance between the protection of foreign investment and the regulation for public interests".⁴⁵

The point raised by *Li* is not unique to China; it also applies to other countries, but *Li* has put forward an insightful suggestion for China's future IIA-making. Although there is no fixed model for negotiating inclusive IIAs, it is advised that the following factors should be taken into consideration in China's future IIA-making.

I. Making IIAs More Compatible with Public Interest Goals

One has to admit that IIAs are not and should not be the primary discourse for public interest protection. But this does not necessarily mean IIAs are completely isolated from and have no constructive role to play in protecting public interest. While IIAs impose international obligations on states to protect foreign investment in their territories, they may potentially limit the regulatory power of states that is necessary to protect public interests. In recent years, it is frequently seen that foreign investors invoke IIA provisions, especially indirect expropriation and fair and equitable (FET) treatment clauses, to claim compensation consequential to host states' adoption of measures for public interest protection, such as environmental protection measures.⁴⁶

The high-profile case of *Methanex v. U.S.A.*⁴⁷ is a typical example to show the tension between environmental protection and investment protection in the discourses of IIA. In this case, the Mexican investor claimed that, among other things, the environmental measures taken by the US (State of California) government con-

44 See e.g. *Zeng*, Balance, Sustainable Development and Integration: Innovative Path for BIT Practice, *J. Int'l Econ. L.* 17 (2014), p. 299.

45 See e.g. *Li*, (fn. 29), p. 175.

46 See e.g. Bernasconi-Osterwalder/Johnson (eds.), *International Investment Law and Sustainable Development: Key Cases from 2000 to 2010*, 2010, www.iisd.org/publications/international-investment-law-and-sustainable-development-key-cases-2000-2010 (9/9/2015).

47 *Methanex Corporation v. the U.S.A.*, <http://italaw.com/cases/683>, (9/9/2015).

stituted expropriation and that it should be compensated for the incurred loss of such measures. Although the NAFTA tribunal did not rule in favor of the investor,⁴⁸ this case has put the international community on high alert that IIAs should be made more compatible for public interest purposes.

To ensure that states would not be deprived of their necessary regulatory power and that the exercises of such power would not be improperly hindered, it is necessary for IIA negotiators to take public interest into account in IIA-making. IIAs should be carefully drafted in order not to deprive contracting states of their regulatory power in taking necessary measures for public interest purposes or to inappropriately limit such power, without necessarily or excessively derogating from their role and purpose of investment protection. In this connection, however, the reality allows little optimism. There are various reasons to explain why IIAs are unable to play a constructive role in environmental protection. Investment protection is deemed as the primary purpose of BITs,⁴⁹ while environmental protection is often addressed by specialized multilateral treaties.⁵⁰ At international level, according to an OECD report, few BITs incorporate environmental provisions tailored for environmental protection.⁵¹ In addition, international arbitrators often tend to prioritize investment protection over public interest protection in ISA practice.⁵²

With regard to Chinese IIAs, a similarly pessimistic picture is to be found. As this author has mentioned elsewhere, despite China's large number of BITs, only a fraction of these BITs contain environmental provisions and many of these provisions lack practical effectiveness in ISA practice, which makes Chinese IIAs in general insufficiently capable in addressing environmental concerns.⁵³ This is particularly worrying because China is facing mounting environmental pressure nowadays. To substantially change such situation, China must "greenize" its future IIAs, which would necessitate an incorporation of larger numbers and more effective environmental provisions in its IIAs and harmonizing its IIAs and national law.⁵⁴

China has been and still is reluctant to make IIAs a forum that could accommodate public interest concerns, as these concerns are often deemed as non-investment issues.

48 See Final Award of the Tribunal on Jurisdiction and Merits (3/8/2005), *Methanex Corporation v. the U.S.*, <http://italaw.com/sites/default/files/case-documents/ita0529.pdf> (9/9/2015), part IV, chapter F.

49 See, e.g. *Sornarajah*, *The International Law on Foreign Investment*, 3rd ed. 2010, p. 79; *Salacus*, *The Emerging Global Regime for Investment*, *Harv. J. Int'l L.* 51 (2010), p. 427 et seq.; *Romesh Weeramantry*, *Treaty Interpretation in Investment Interpretation*, 2012, p. 10 et seq.

50 *Walde*, *International Disciplines on National Environmental Regulation: With Particular Focus on Multilateral Investment Treaties*, in: *the International Bureau of the Permanent Court of Arbitration (ed.), International Investments and Protection of the Environment: The Role of Dispute Resolution Mechanisms*, 2000, p. 40.

51 See OECD, *International Investment Law: Understanding Concepts and Taking Innovations*, 2008, www.oecd.org/daf/inv/investment-policy/40471550.pdf (9/9/2015), p. 138.

52 *Kulick*, *Global Public Interest in International Investment Law*, 2012, p. 51.

53 See generally *Chi*, *The "Greenization" of Chinese BITs: An Empirical Study of the Environmental Provisions of Chinese BITs and Its Implications for China's Future BIT-making*, *J. Int'l Econ. L.* 18 (2015), pp. 511-542.

54 *Ibid.*, pp. 536-540.

Some issues could be acceptable to varying extents, such as environmental protection and transparency of ISDS procedures; others appear too provocative to be accepted, such as human rights protection and anti-corruption. Thus, the key step for China to make its future IIAs more inclusive is to change its evasive attitudes towards these “sensitive” issues in IIA-making. Ultimately, China needs to be aware and accept that IIAs should not be deemed only as forum for the exchange of economic interests between states, but should also be seen as helpful discourse to address certain non-investment concerns.⁵⁵ This will take some time and inevitably necessitate a different set of calculation of gains and losses in IIA-making.

II. Developing a Coherent IIA-Making Strategy

Although BITs remain the major component of IIAs, countries around the world are engaged in intense FTA negotiations, including some megaregional FTAs, such as TPP and TTIP.⁵⁶ Many FTAs contain an investment chapter, but BIT and FTA are different in many ways. Essentially, while BIT is designed mainly for investment protection and promotion, FTA often appear more liberal, covering not only investment, but also a broad range of other topics, such as market access, competition, trade and intellectual property.

Recently, while China remains actively engaged in BIT negotiations, it has sped up its FTA-making efforts. Comparing China’s BITs with the investment chapters of its FTAs, one is to find that they are quite similar in both format and contents. This seems to imply that, in China’s IIA-making, no distinction between BIT and FTA investment chapter has been drawn and no distinct strategy for FTA-making has been developed. Although in the strict sense such IIA-making strategy cannot be said wrong, it can be misleading given the difference between FTA and BIT and the potential impacts of FTA on regional economic integration. In its future IIA-making, China needs to make smart choice between standalone BIT and FTA investment chapter. This should be decided on a case-by-case basis with all social, economic and political factors taken into consideration.

In this connection, the implementation of the “One Belt, One Road” strategy calls for innovation in China’s future IIA-making. This strategy was first officially proposed by the Chinese President in 2013.⁵⁷ Despite the active promotion of China, the positive responses of the involved countries and the conclusion of a few cooperation memoranda, no comprehensive agreement has been concluded among all involved countries and the legal institution for this strategy has not been put in place up to the

55 Ibid., p. 540.

56 UNCTAD, World Investment Report 2015 – Reforming International Investment Governance, <http://unctad.org/en/pages/PublicationWebflyer.aspx?publicationid=1245> (9/9/2015), p. 107.

57 The State Council Information Office, The Background and Roadmap of the “One Belt One Road” Strategy, www.scio.gov.cn/ztk/wh/slxxy/31200/Document/1415297/1415297.htm (9/9/2015), original in Chinese.

present.⁵⁸ While the scope of this strategy is far broader than mere regional trade cooperation, one may expect that a new round of IIA-making efforts would be needed among the involved countries. It is imperative for China to carefully assess the existing trade agreements concluded with these countries, including BITs and FTAs, to prepare for future IIA-making.

In addition, in recent years, China seems to show an increasing amount of interest in concluding a multilateral investment convention (MIC).⁵⁹ There are various reasons for a MIC. First, the fragmentation of international investment law, especially the proliferation of BITs has made global investment governance increasingly difficult.⁶⁰ Second, the international community has drawn lessons from the failed negotiations of the Multilateral Agreement of Investment (MAI) initiated by the Organization for Economic Co-operation and Development (OECD).⁶¹ Third, under the framework of the World Trade Organization (WTO), negotiations of investment issues appear unsuccessful,⁶² and there emerged a need for a new forum for international investment rule-making. Fourth, as China is determined to be a rule-maker in global economic governance, the making of a MIC would provide an excellent opportunity for it to “realize this dream”. Although it seems too early for the international community to formally kick off the negotiation of a MIC, it is important for China to get prepared for it as social sentiments and political willingness keep accumulating.

It can be imagined that in the future China will face much more complicated situations in IIA-making. It may need to negotiate or renew BITs, FTAs and MIC concurrently. It is necessary for China to carefully assess which form of IIA is most suitable and can best meet its need for sustainable development. China should also harmonize its positions in these different negotiating fronts to form a coherent strategy. It is worth studying whether a MIC is truly needed by the international community, and if so, what role China can play in the negotiation.

III. Enhancing the Consistency of IIA, National Law and Soft Law Rules

IAs are an important pillar of international investment law. But national laws, regulations and policies (collectively referred to as “national laws”) and certain soft law

58 The National Development and Reform Commission of the P.R.C., the Ministry of Foreign Affairs of the P.R.C. and the Ministry of Commerce of the P.R.C., Vision and Proposed Actions for Jointly Building the Silk Road Economic Belt and the 21st-Century Maritime Silk Road, www.gov.cn/xinwen/2015-03/28/content_2839723.htm (9/9/2015), original in Chinese.

59 See e.g. The Chinese Academy of Social Science, Trying to Seize the Power of Discourse in International Investment Rule-Making, <http://theory.people.com.cn/n/2014/0402/c40531-24801269.html> (9/9/2015), original in Chinese.

60 See e.g. *Schill*, *W(h)ither Fragmentation? On the Literature and Sociology of International Investment Law*, *European J. Int'l L.* 22 (2011), p. 875.

61 See e.g. *Chen*, *OECD's Multilateral Agreement on Investment: A Chinese Perspective*, 2002.

62 See *Kennedy*, *A WTO Agreement on Investment: A Solution in Search of a Problem*, *U. Pa. J. Int'l L.* 24 (2014), p. 77.

rules are also indispensable for the construction and perfection of this legal framework. The rules of international, national and soft law are not necessarily consistent. Even within a certain branch of law, inconsistency may still exist. It is thus important for China to enhance the consistency of the relevant rules scattered in the different branches of laws to create a coherent and sensible legal framework for its investment governance.

On one hand, “inter-branch” consistency needs to be enhanced. Many investment rules contained in China’s IIAs, national laws are inconsistent. This is not only caused by China’s poorly coordinated law-making practice, but is also a reflection of China’s splitting attitudes towards these different branches of laws. In general, China is quite friendly towards IIAs and active in IIA-making; although Chinese national law is not sufficiently effective in supporting China’s investment governance, China is making gradual improvements in recent years.⁶³ In contrast, China is somehow hostile towards soft law instruments, which can be shown by its conservative attitudes towards incorporation of certain non-binding rules in IIAs, such as those concerning human rights and corporate social responsibility.⁶⁴

Partly due to the splitting attitudes, China’s IIAs, national laws and soft law often contain inconsistent rules with regard to the same subject matter. For instance, regarding the standard of compensation for expropriation, there is sharp difference between Chinese IIAs and national laws. As mentioned, while some recent Chinese IIAs have actually adopted the key elements of the “Hull Formula”, the compensation standard in Chinese national law remains quite low and vague. Such difference leads to the gap in investment protection in the two legal systems. To seek sufficient and effective investment protection, foreign investors would prefer protection under IIAs in case of expropriation, because domestic remedies in China would only provide lower level of protection according to Chinese national law. In turn, this would necessitate forum shopping in settling investment disputes with China (since many Chinese IIAs contain fork-in-the-road clause or wavier clause), meaning that foreign investors will choose ISA, while administrative litigation available under Chinese law will be “abandoned”.

On the other, from practical perspective, “inter-IIA” inconsistency is probably a more ostensible problem. Such inconsistency typically appears where the IIAs have been renewed or updated and may take different forms.

63 For instance, China has launched its reform of its foreign investment laws a few years ago and has issued the Draft Foreign Investment Law of the P.R.C. in January 2015. China has also promulgated its first comprehensive rules of overseas investment regulation, Regulation Rules of Overseas Investment (Order No. 2014-3 of the Ministry of Commerce), effective as of 6/10/2014.

64 See *Hang*, (fn. 41), p. 1222 et seq.

- First, at general level, “inter-IIA” inconsistency may exist in the different generations of Chinese BITs.⁶⁵ As mentioned, different generations of BITs have sharp differences with regard to E&C and ISDS clauses.
- Second, “inter-IIA” inconsistency may exist in different types of IIAs with a specific country. There are some countries that have concluded different IIAs with China (such as a BIT and an FTA), such as Switzerland and Australia. Although Chinese BITs and FTA investment chapters are similar, their provisions are not necessarily identical. Unless these IIAs contain express provisions dealing with the intra-IIA relationship, it is unpredictable how the inconsistency will be solved.
- Third, “inter-IIA” inconsistency may also exist in successive IIAs with a specific country. Since the new millennium, China has gradually renewed its BITs with several countries, especially European countries. Besides, as the duration of effect of Chinese BITs is often set for ten years, some other BITs may also need to be renewed. As renewed BITs may contain rules different from their predecessors, it is almost inevitable that inconsistency problems will arise.

Up to the present, China has not produced an ideal method to deal with such inconsistency, but China’s current IIA-making practices reveal two major approaches. One way is to provide a “transition” or “replacement” clause in successive IIAs to avoid possible overlap in application. For instance, the renewed China-Belgium BIT (effective as of 2009) contains a clause titled “Transition” to deal with its relation with the old BIT (effective as of 1986), according to which the new BIT “replaces and substitutes” the old one.⁶⁶ Similarly, to deal with its relation with the China-Germany BIT (effective as of 1985), the renewed BIT (effective as of 2005) also contains a clause, providing that upon entry into force of the new BIT, the old one shall terminate.⁶⁷ The other way is to allow parallel application of the successive IIAs. For instance, the China-Japan-Korea TIT contains a clause titled “Relation to Other Agreements”, clearing recognizing that the TIT shall not affect the effect of the existing BITs concluded among the contracting states.⁶⁸

Despite the existence of the transition clause, the actual effects of such a clause is not always predictable. In the recent case of *Ping An v. Belgium*,⁶⁹ two successive BITs are involved, i.e. the 1986 and 2009 China-Belgium BITs. The tribunal held that it lacks jurisdiction to hear the dispute between the Chinese investor and Belgium and

65 Although without precise and official classification, China’s BITs can be roughly divided into three generations: BITs concluded before late 1990s are the first generation; BITs concluded after the 2010s are the third generation; BITs concluded between these two points of time are the second generation. On this issue, see e.g. *Dulac*, *The Emerging Third Generation of Chinese Investment Treaties*, *Transnat’l Disp. Management* 7 (2007), p. 1; *Gallagher/Shan*, (fn. 11), pp. 34-43.

66 Article 10(1), the 2009 China-Belgium BIT.

67 Article 16(1), the 2005 China-Germany BIT.

68 Article 25, the China-Japan-Korea TIT.

69 *Ping An Life Insurance Company of China, Limited and Ping An Insurance (Group) Company of China, Limited v Kingdom of Belgium* (“*Ping An v. Belgium*”), ICSID Case No. ARB/12/29, <https://icsid.worldbank.org/apps/icsidweb/cases/Pages/casedetail.aspx?caseno=ARB/12/29> (9/9/2015).

dismissed the investor's claims.⁷⁰ The tribunal noted the successive BITs between China and Belgium and treated this issue essentially as a treaty interpretation issue.⁷¹ Although the case of *Ping An v. Belgium* does not directly and necessarily involve the issue of "inter-IIA" inconsistency, its profound relevance with the issue of successive IIAs of China should have sent an alarming message to China's IIA-makers in future IIA-making.

As discussed, inconsistency of Chinese IIAs, national laws and soft law rules may have profound impacts on investment governance. Aside from treaty shopping, there may incur other unexpected problems, such as forum shopping when settling investment disputes. Such difficulty could be amplified given China's large number of IIAs. It would be quite difficult, if possible, to produce an ideal method to solve the inconsistency problem once and for all. While acknowledging these problems, China should make concerted efforts at international, transnational and national levels to harmonize its IIAs, national laws and certain soft law rules. The key to such harmonization is to align China's national laws with the higher standards laid down in its IIAs and certain soft laws. This could be done through IIA-making and law-making; it could also be done through ISA practice, which would actually require arbitrators to carefully interpret relevant IIA clauses to help achieve "inter-branch" and "intra-branch" consistency.

E. Conclusion

Notwithstanding China's large number of IIAs, BITs in particular, its IIA-making strategy and the formation and function thereof have seldom been studied. This article demonstrates that China's IIA-making strategy and its shifts is mainly prompted by and serves China's changing economic development policies. To a large extent, IIA-making has been instrumentalized by China as a policy tool to achieve its national economic development goals.

Along with China's economic rise in recent years, its IIA-making has also entered into a new era. China faces unprecedented challenges in IIA-making as a result of its changed economic, political and social situations. Economically, China has acquired a blended status as a leading country in investment importing and exporting; politically, China is determined to become an active participant in global investment governance and a leader in international investment rule-making. Socially, Chinese enterprises have gradually realized of their roles in participating in global investment governance as a key stakeholder. They have become aware of the function and importance of IIAs and begun to urge the government to negotiate "strong IIAs" to offer higher level of protection for their overseas investment.

70 Award (30/4/2015), *Ping An v. Belgium*, [71 See *ibid.*, paras. 192-233.](https://icsid.worldbank.org/ICSID/FrontServlet?requestType=CasesRH&actionVal=showDoc&docId=DC5912_En&caseId=C2463(9/9/2015), para. 240.</p>
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In light of China's new situation, neither the "host state centered" strategy nor the "home state centered" strategy can truly meet China's future need for IIA-making. It is advisable for China to make its IIAs more compatible with public interest purposes, develop a coherent IIA-making strategy and enhance the consistency of the relevant IIA, national law and relevant soft law rules. None of these is an easy task that can be solved overnight. In this sense, China has just embarked on a long march of IIA-making. As the situations of China and the world keep changing, it remains to be seen how China will adjust its IIA-making strategy to serve its future development goals in the era of deepening globalization.

