The Developments of ISDS Mechanism Initiated by the EU Investment Court System and China's Choice

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Abstract *The European Union has initiated fundamental transformations to the existing investor-state dispute settlement ("ISDS") mechanism by introducing the investment court system ("ICS") in recently concluded the 2016 EU-Canada FTA and the 2016 EU-Vietnam FTA, as well as the 2015 TTIP Proposal. Furthermore, the EU also proposed a more comprehensive proposal for a multilateral investment court ("MIC"), which may lead to significant impacts on the ISDS reform. China has become one of the world's biggest recipients and sources of foreign direct investment, and has more concerns regarding ISDS reform than before. By now, China has not clarified its proposal on ISDS reform. Given the "American First" policy and the intense relationship between U.S. and China in trade and investment, both the EU and China consider the BIT negotiations as the breakthrough point. Recently, in light of the EU's ambition for a 2020 deadline for an EU-China BIT negotiation, the Foreign Investment Law of China was passed by the National People's Congress on 15 March 2019 which provides higher standards investment protection for foreign investors, as well as the Premier Minister of China, Keqiang Li's proposed visit to the Summit with EU leader on 9 April 2019 are signals to accelerate EU-China BIT negotiations ahead of expected passage. Whether China will adopt the ICS mechanism in the EU-China BIT, and whether China will expand the ICS mechanism in the ongoing China-Japan-Korea FTA and*

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Regional Comprehensive Economic Partnership ("RCEP") are important not only for these BITs/FTAs, but also for the future of the ICS mechanism or even MIC.

The article can be divided into five chapters. The first chapter introduces the drawbacks of the current ISDS mechanism and EU's standpoint for ISDS reform; the second chapter discusses the main contents and features of ICS; the third chapter focuses on potential challenges against ICS from the perspectives of inside and outside the EU; the fourth chapter analyzes interests and benefits of the two-way investment of China and China's adoption of ISDS in BITs/FTAs and in practice; and the fifth chapter attempts to explore China's choice in ISDS reform. The suggestions include but are not limited to the abolition of some content of the ICS, the combination of the ISDS mechanism and state-state dispute settlement mechanisms, the establishment of arbitration rules of China's "one-stop" dispute settlement mechanism, and improving substantive provisions in China-foreign BITs to balance the interests in capital-importing and capital-exporting.

Key Words: Investment Court System; Investor-State Dispute Settlement; ISDS Reform; China's Choice

Ever since 1992, China has been the developing country that absorbs the most foreign direct investment ("FDI"). With the continuous climb of China's outbound foreign direct investment ("OFDI") in recent years, China officially became a net capital exporter in 2015.[1] In 2016, the amount of China's OFDI grew up to 196.15 billion US dollars, ranking the 2nd largest source in the world.[2] As China has indeed become a big player in two-way investment, both Chinese investors and the Chinese government will likely face more investment disputes than ever before. Whether those disputes can be solved properly concerns the effective protection of the legitimate interests of Chinese investors and the Chinese government in the field of investment, and therefore deserves attention.

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1 In 2015, the amount of China's FDI outflows was 145.67 billion US dollars. The amount of FDI inflows of that year was 135.6 billion dollars. The amount of net capital inflows was 10.07 billion US dollars.

2 Though China's OFDI dropped to 158.3 billion US dollars, decreasing 19.3% compared to the OFDI volume of 2016, since 2015, China has been net capital exporter for 3 years. See Ministry of Commerce, National Bureau of Statistics and State Administration of Foreign Exchange of the People's Republic of China, *2017 Statistical Bulletin of China's Outward Foreign Direct Investment*, Beijing: China Statistics Press, 2018, at 83-84.

I. DEFECTS OF THE CURRENT ISDS MECHANISM AND EU'S TRANSFORMATIVE APPROACH

The settlement of disputes between foreign investors and host countries has always been the most complicated issue in the field of international investment dispute settlement. International investment agreements ("IIAs") mainly entail provisions for the protection of foreign investments in the host country and provide for a dispute settlement mechanism to enforce these investors' rights. Traditionally, IIAs have used the following instruments for solving disputes with investors: foreign investor access to domestic courts; state-to-state dispute settlement ("SSDS") via diplomatic protection, and investor-state dispute settlement ("ISDS") via international arbitral proceedings. The ISDS mechanism founded upon the *1965 Convention on the Settlement of Investment Disputes between States and Nationals of Other States* (hereinafter "*Washington Convention*")[3] provided foreign investors with the likeliness to resort to international investment arbitration for disputes arising from the host country's legislative, administrative or judicial conduct. Compared to the judicial settlement (via domestic courts of host states) and political settlement (via diplomatic protection or SSDS), the ISDS has conspicuous advantages. Nonetheless, there's no denying that it also has noticeable drawbacks.

A. Main Defects of the ISDS Mechanism

1. Undue Emphasis on the Protection of Investors' Interests

There has been criticism all along in the international community that the ISDS mechanism puts undue emphasis on the protection of investors' interests and neglects the public interests of host countries.[4] Some critics even contended that the current ISDS mechanism was an unbalanced legal mechanism detrimental to a country's sovereignty[5] and negatively impacts on public

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[3] The International Center for the Settlement of Investment Disputes (hereinafter "ICSID") founded upon *1965 Washington Convention* is the constitution that deals with the most ISDS cases. Apart from ICSID, the Permanent Court of Arbitration (PCA), the Arbitration Institute of the Stockholm Chamber of Commerce (SCC) etc. also deal with some ISDS cases. These arbitration institutes usually apply *United Nations Commission on International Trade Law Arbitration Rules* (hereinafter "*UNCITRAL Arbitration Rules*") in their awards.

[4] See Kaitlin Y. Cordes, Lise J. Johnson and Sam Szoke-Burke, Grievances, Human Rights and Investor Protections, Columbia Center on Sustainable Investment, March 2016, at 7. Also see Jesse Coleman, Lise J. Johnson, Lisa E. Sachs and Nathan Lobel, "International Investment Agreement, 2017: A Review of Trends and New Approaches", in Lise E. Sachs, Lise J. Johnson and Jesse Coleman (eds.), *Yearbook on International Investment Law & Policy 2017*, Oxford: Oxford University, 2019, at 116-127.

[5] See Guo-Yu Jun, "Lack of Legitimacy in International Investment Treaty Arbitration and Its Rectification", Jurists Review, 2011(3), at 143-147.

concerns. Such opinion was held mainly by developing countries. However, in recent years, some developed countries are starting to side with it. Take Germany as an example -the German government has been twice brought before the ICSID by Vattenfall, a Swedish power company.[6] Although the first Vattenfall case was terminated after Vattenfall received favorable judgment in the District Court of Hamburg and thus withdrew its allegations, the German public widely believed that the District Court of Hamburg unduly protected the interests of Vattenfall under the serious pressure of being sued before the ICSID.

2. Discrepancy Between Different Cases Due to the Lack of An Appellate Mechanism and Error-correction Mechanism

Due to the different constitution of tribunals and the fact that arbitration awards are final and binding upon parties, there exist obvious and sometimes even fundamental discrepancies among different tribunals with regard to basic questions such as whether issues like investment, investors, umbrella clauses, most-favored nation treatment as well as security clauses shall apply to the dispute settlement clauses. Five cases arising from Argentina's financial crises, which have similar factual backgrounds, were submitted to the ICSID between 2001 and 2003.[7] The common legal issue in these five cases was the application of Article XI of Argentina-US BIT of 1991 ("Emergency

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[6] By 30 April 2019, Germany had been sued for three times. Two of them were brought by Vattenfall. The case *Vattenfall AB* v. *Federal Republic of Germany (1)* (ICSID Case No. ARB/09/6) has been settled. The other case *Vattenfall AB* v. *Federal Republic of Germany (2)* (ICSID Case No. ARB/12/12) is still pending before the tribunal. The former one concerns a thermal power plant invested and established by Vattenfall in Germany. The local government restricts the water supply to the plant for the purpose of preserving some animal species. Vattenfall not only filed a lawsuit in the District Court of Hamburg but also brought the German government before the ICSID. Vattenfall withdrew its application to the ICSID after winning the case in the domestic court. In the latter case, the German government announced to shut down all nuclear power plants within its border before 2022 under the influence of the 2011 nuclear accident in Fukushima, Japan. This measure affected two nuclear power plants Vattenfall invested in Germany. Vattenfall brought the German government before the ICSID in 2012, claiming damages which amounted to 470 million euros, i.e. 514 million US dollars. UNCTAD, available at <http://investmentpolicyhub.unctad.org/ISDS/Details/467> (accessed 30 April 2019).

[7] The five cases refer to *CMS* v. *Argentina*, ICSID Case ARB/01/08, Award, 12 May 2005; *Sempra* v. *Argentina*, ICSID Case ARB/02/16, Award, 28 September 2007; *Enron* v. *Argentina*, ICSID Case No. ARB/01/03, Award, 22 May 2007; *LG&E* v. *Argentina*, ICSID Case ARB/02/1, Award, 3 October 2006; Continental *Casualty Co*. v. Argentine *Republic*, ICSID Case No. ARB/03/9, Award, 5 September 2008. In the first three cases, the ICSID found that Argentina had no right to invoke Article XI of the Argentina-US BIT and therefore cannot be justified for its suspected conducts. However, the ICSID recognized the invocation of that provision and exempted Argentina from paying huge damages in the last two cases.

Clause"). The accused Argentine government invoked the emergency clause as a justification for its temporary violation of its obligations under the BIT. However, the ICSID made totally different awards in these five cases. Furthermore, under the current ISDS mechanism, in principle either party to the disputes can resort to the ICSID's annulment procedure or the domestic courts at the place of arbitration under ad hoc arbitrations in order to annual the awards. However, the annulment mechanism can only allow the Committee to either uphold or annual the awards but not modify them. To some extent, it can be determined that the annulment mechanism for ISDS cases is not for error-correction but for the substantial violation of fundamental procedural requirements.[8]

3. Procedural Defects in the ISDS Mechanism

The ISDS mechanism was born out of commercial arbitration and thus has irrevocably inherited the features of the latter, including the privacy of arbitration and the freedom of the disputing parties to choose arbitrators. In practice, the ISDS also has such problems such as the lack of transparency, lack of public regulation, procedural delays and high costs.[9]

The internal defects of the ISDS mechanism which are amplified and diffused in practice, have induced a legitimacy crisis of the ISDS mechanism[10] and even led to the debate for abolishing the ISDS mechanism.[11] There exists an urgent need to reform and improve the current mechanism.

B. EU's Transformative Approach

Seeking to address the thorny problems of the current ISDS mechanism, the United Nations Commission on International Trade Law ("UNCITRAL"), the ICSID and other relevant international organizations are making their efforts, however, up to now, there are extremely limited efforts that will lead to any kind of meaningful reform because they only address procedural issues and ignore the substantive problems with the current system.[12] Moreover,

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[8] See Christopher Schreuer, *The ICSID Convention: A Commentary*, Cambridge: Cambridge University Press, 2009, at 901.

[9] In FY 2017, the ICSID is committed to adopting relative measures to reduce the time period and costs of case processing. *See* ICSID: *ICSID Annual Report* 2017, at 47.

[10] See Huang-Shi Xi, "The Innovation of the International Investment Dispute Settlement Mechanism from the Perspective of Sustainable Development", Contemporary Law Review, 2016(2), at 30.

[11] See Rudolf Dolzer, "Perspectives for Investment Arbitration: Consistency as a Policy Goal?" in Roberto Echandi and Pierre Sauvé (eds.), *Prospects in International Investment Law and Policy*, Cambridge: Cambridge University Press, 2013, at 406-409.

[12] A typical example is the United Nations Convention on Transparency in Treaty-based Investor-State Arbitration. The treaty entered into force as from 27 October 2017.

it is noteworthy that some representative countries and organizations have already come up with some approaches to the problems. Those countries can be divided into four groups: (1) reformists (the representative countries include the US, Japan and Chile); (2) transformists (the representative countries/regions include the EU and Canada); (3) abolitionists (the representative countries include Brazil[13], South Africa, Indonesia and some Latin American countries[14]); (4) fence-sitters (the representative countries include Australia). The reformists group proposes adopting progressive reforms and improving the current system by perfecting the procedural rules, taking measures such as establishing an appellate system, appointing *amicus curiae* and improving transparency. Relevant reforms were embodied in the 2004 U.S. Model BIT and the 2012 U.S. Model BIT. The US-Mexico-Canada Agreement concluded on 1 October 2018 still mainly focuses on procedural issues in ISDS including more transparency, coherence and efficiency.[15] On the flip side, Brazil, India, Indonesia, South Africa and other countries are making radically diversified movements.[16] They demanded the abolition of the ISDS system and even asked for the reversion to the Calvo doctrine. More specifically, they either abolished or terminated BITs with ISDS provisions that have been signed, denounced the *Washington Convention*,[17] or announced that

[13] Brazil is a special country in international investment treaties. By now, Brazil has no effective BIT. However, in recent years, Brazil concluded BITs with Angola, Mozambique and Malawi in Africa and Mexico, Chile, Colombia and Peru in Latin America. Unlike the treaties concluded with African States, which refer only to the possibility of future development of State-to-State dispute settlement ("SSDS"), which constitutes a political compromise that seek to maintain coherence with the traditional policy discourse of Brazil against ISDS, the treaties concluded with the Latin American States contain consent by the parties to SSDS. See Murilo Otávio Lubamdo de Melo, "*Host States and State-State Investment Arbitration: Strategies and Challenges*", Brazilian Journal of International Law, 14(2), 2017.

[14] Latin America countries diversified in the issue. For example, Bolivia, Ecuador and Venezuela denounced the Washington Convention. Ecuador has just recently accorded protection via legislation to foreign investors, while Argentina still signs BITs with ISDS provision and accepts the ISDS jurisdiction but Argentina nearly submits an annulment application in any case when it is a respondent State.

[15] According to the information revealed by the USTR, the US made several requests regarding dispute settlement in the renegotiation of the NAFTA. Those requests included the encouragement of early identification and settlement of disputes through consultation and other mechanism, the effectiveness and efficiency of the dispute settlement mechanism, publicity of information, participation of non-governmental entities etc. See Office of the United States Trade Representative: *Summary of Objectives for the NAFTA Renegotiation*, November 2017, at 18, available at <https://ustr.gov/sites/default/files/files/Press/Releases/Nov%20Objectives%20Update.pdf>, (accessed 21 December 2017). Also see USMCA Agreement, Annex 14-B.

[16] Brazil is signing investment agreements, but limited to State-State. Indonesia has a new model. India's model has ISDS in it and it is signing treaties. South Africa put into place a domestic law for investment protection.

[17] Article 71 of Washington Convention states "Any Contracting State may denounce this Convention by written notice to the depositary of this Convention. The denunciation shall take effect six months after receipt of such notice."

they would adopt SSDS or other alternative resolutions after effective BITs expired. Australia, however, seesaws in its attitude towards the ISDS mechanism. Australia excluded the ISDS mechanism in the Investment Chapter of the 2005 Australia-US FTA and the 2011 Australia-New Zealand FTA. However, in the 2014 Australia-Korea FTA and the 2015 Australia-China FTA, the ISDS mechanism was preserved in the Investment Chapter.

The transformists group, the representatives being the EU and Canada, followed by Vietnam and Singapore is somewhere in between the reformists and the abolitionists. They ask for the substantive transformation of the current ISDS system and request the establishment of an ICS composed by a Tribunal of First Instance and an Appeal Tribunal, which is similar to that of the WTO dispute settlement mechanism.[18] Compared with the reformists who adopt progressive and pragmatic methods, the EU, despite being a latecomer, goes a step further and brings more remarkable changes to the procedural issues of the current ISDS mechanism.

II. MAIN CONTENT AND FEATURES OF THE EU ICS

A. Main Content and Developments of the EU ICS

The *Investment Protection and Investor-to-State Dispute Settlement in EU Agreements* passed by the European Commission in November 2013 emphasized the important role ISDS plays in the promotion and protection of investment. It also pointed out that EU should draw lessons from its previous agreements and avoid imposing inappropriate restrictions on host states' right to regulate. Furthermore, it provided that EU should clarify the provisions regarding substantive rights and make transformations to the ISDS mechanism. The development of the EU ICS mechanism has gone through four phases.

In the first phase, EU adopted an "improved version of the ISDS mechanism", which was mainly embodied in Chapter 10 of the *EU-Canada Comprehensive and Economic Trade Agreement* (hereinafter "CETA") signed on 26 September 2014. It kept most features of an arbitration mechanism and did not include a court mechanism with an appellate system.

[18] The expressions regarding the Investment Tribunal System in various FTAs made by EU in recent years are not consistent. For example, in the texts of TTIP, the expression was "Investment Court System" (*see* S. 4 of the TTIP) and the two-tier mechanism was called "Tribunal of First Instance" and "Appeal Tribunal". Nevertheless, in the 2016 EU-Vietnam FTA and the 2016 EU-Canada CETA, the expression was "Investment Tribunal System", while the two-tier mechanism was called "tribunal" and "appeal tribunal (or appellate tribunal)". The expression adopted in the CETA was "appellate court". This article uses ICS in order to keep coherence of expression.

On 5 May 2015, when Cecilia Malström presented a concept paper titled "*Investment in TTIP and Beyond—The Path for Reform*" to the European Parliament and to the Council.[19] This concept paper was aimed at addressing the longstanding controversy surrounding the criticism of ISDS and considered that the ISDS was mounted on the perceived need to reclaim "fairness and independency".[20]

The second phase saw a "forward version of the ICS mechanism", which was embodied in the *Trans-Atlantic Trade and Investment Partnership* (hereinafter "TTIP") officially issued by EU on 12 November 2015. In the TTIP, EU suggested establishing an ICS mechanism composed of an Investment Tribunal and an Appeal Tribunal to substitute for the current ISDS mechanism.

In the third phase appeared a "mixed version of the ICS mechanism", mainly reflected in Article 8.18-8.45 of the 2016 CETA.[21] Compared with the strong judicial features in the Investment Chapter of TTIP, the 2016 CETA ebbed away and put forward a mixed version. It was neither an improved version of the ISDS nor a forward version of the ICS containing strong judicial elements, but a version in between. This feature was well shown in Chapter 8, Section 3 of the EU-Vietnam FTA published on 1 February 2016. The EU-Vietnam FTA also signaled that the ideas of EU's ICS mechanism had been put into practice.

In the fourth phase, EU proposed to set up a multilateral investment court ("MIC") to set up a more transparent, coherent and fair system to deal with investment disputes under IIAs.[22] In the EU's ambitious proposal, the MIC would be an international court empowered to hear investments disputes arising from investors and host states that will have accepted its jurisdiction over their BITs. The EU states that the MIC favors multilateral solutions and adds an imperative much needed piece to the multilateral system. In 2017, the UNCITRAL also agreed to discuss possible multilateral approaches to address the ISDS reform.

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[19] Press Release, EU Commission Press Release database, A future multilateral investment court, MEMO/16/4350, 13 December 2016, available at <http://europa.eu/rapid/press-release_MEMO-16-4350_en.htm> (accessed 25 December 2018).

[20] See Stephan Wilske, Raeesa Rawal and Geetanjali Sharma, "The Emperor's New Clothes: Should India Marvel at the EU's New Proposed Investment Court System", Indian Journal of Arbitration Law, 6(2), 2018, at 86-87.

[21] CETA entered into force provisionally as from 21 September 2017, available at <http://ec.europa.eu/trade/policy/in-focus/ceta/> (accessed 30 April 2019).

[22] EU: State of the Union 2017: A Multilateral Investment Court, at 1, available at <http://trade.ec.europa.eu/doclib/docs/2017/september/tradoc_156042.pdf> (accessed 8 December 2018).

1. Improvement of the ISDS mechanism in the 2014 CETA

The EU-Canada CETA of 2014, in its preface as well as Chapter 23 (*Trade and Labour*), Chapter 24 (*Trade and Environment*) and some other chapters, noted that states should take measures to protect public interests in a manner consistent with their international commitments. However, there was no such provision in Chapter 10 (*Investment*). In that chapter, the 2014 CETA still adopted expressions like "arbitral tribunal" and "arbitrator" which carried strong characteristics of an arbitration. Furthermore, the 2014 CETA allowed the disputing parties to choose arbitrators and it had not established an appellate system yet. Therefore, the 2014 CETA was still an improved version of the original ISDS mechanism.

2. Design of the ICS mechanism in Investment Chapter of the TTIP

Compared with the 2014 CETA, the TTIP put more emphasis on host states' right to regulate. Section 2 Article 2 of the TTIP provided that "*the provisions of this section shall not affect the right of the Parties to regulate within their territories through measures necessary to achieve legitimate policy objectives*." This was the first time that EU put the host states' right to regulate in the text of a treaty. Meanwhile, Article 2 also provided that the provisions of investment protection shall not be interpreted as a commitment from a Party that it will not change the legal and regulatory framework. It also recognized the competence of the host states' authorities to freely make decisions on subsidies, and did not prohibit EU from implementing state aid law. Moreover, with regard to the issues of indirect expropriation, EU was trying to restrict the scope of indirect expropriation in order to reduce potential suits brought by investors.

The Chapter II *(Investment)* of the TTIP Draft aims to construct a set of quasi-judicial dispute settlement mechanisms which refers to that of the WTO.[23] First, the ICS includes a two-tier system composed of a Tribunal of First Instance and an Appeal Tribunal. It also specifies the authority of review of the Appeal Tribunal. Second, the ICS improves the mechanism of judge appointment. The Investment Chapter of the TTIP Draft nails down issues including but not limited to the roster of permanent judges, terms of office, non-competition agreement and qualifications of judges.[24] The Tribunal of First Instance is composed of fifteen judges -- five of them shall be nationals of a member state of EU, five shall be nationals of the United

[23] There are fundamental differences in ICS and the WTO system. For one, WTO is only State-State so you avoid the asymmetrical nature of investment law. Second, and less relevant to the structure but notable, WTO only has forward looking remedies.

[24] TTIP Chapter II, Arts. 9-11

States and the other five shall be nationals of third countries. The judges shall be appointed for a six-year term, renewable once. The three judges composing the division of the Tribunal who hear the cases shall be appointed on a rotation basis. Third, although the ICS is hitherto a bilateral tribunal mechanism, it is aimed to develop into a multilateral investment tribunal and/or a multilateral appellate mechanism in future.[25]

3. Improvement of the ICS in 2016 CETA

Compared with the ICS mechanism in the TTIP, the 2016 CETA[26] has the following features. First, it involves compulsory proceedings of consultation (Article 8.19 of the CETA) and mediation (Article 8.20 of the CETA) and made specific stipulations on the time period and the maximum period of the consultation.[27] Second, depending on who conducted the measures identified in the claimant's notice, EU determines whether EU or a member state shall be the respondent.[28] Third, the CETA clarifies the structure of the Investment Tribunal, especially the competence of the Appellate Tribunal. It stipulates that the Appellate Tribunal can uphold, modify or reverse a Tribunal's award.[29] Fourth, it combines the characteristics of both an arbitration and a litigation. The CETA did not adopt terms and phrases like "court" or "judge" which have strong judicial characteristics in its text. It didn't use the terms and phrases commonly used in traditional investment treaties such as "arbitral tribunal", "arbitrator" or "award". Instead it employed neutral terms like "tribunal", "member", "decision" etc. Fifth, the members of the Tribunal shall be independent. They shall not be affiliated with any government and shall not take instructions from any organization or government with regard to matters related to the dispute.[30] The members of the division of the Tribunal shall be appointed by the chair of the CETA. Therefore, both parties of the disputes are deprived of the right to appoint the judges. Sixth, the CETA learned from the 2006 *ICSID Arbitration Rules* and introduced a set of rules regarding two procedures of fast-track rejection, provisional and precautionary measures, participation of third parties, etc.

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[25] TTIP Chapter II, Arts. 9-12

[26] "CETA" refers to the 2016 CETA hereinafter, unless otherwise specified.

[27] Pursuant to Art. 8.19(6)(a), a request for consultations must be submitted within three years after the date on which the investor or the locally established enterprise first acquired or should have first acquired knowledge of the alleged breach and knowledge that the investor or the locally established enterprise, has incurred loss or damage thereby. CETA also imposed a time limit of 18 months. Once the investor submits the request for consultations, the investor shall settle disputes through consultation with the host State or submit a claim to the Tribunal within 18 months. Otherwise, the investor would have no access to remedies.

[28] CETA, Art. 8.21

[29] CETA, Art. 8.28.

[30] CETA, Art. 8.30.

4. Latest Changes of the ICS Mechanism by the 2018 EU-Singapore FTA

In April 2018, the EU Commission presented the outcome of negotiations for the trade and investment agreements with Singapore to the Council. The provisions in Chapter 3 (Dispute Settlement) are similar to those in 2016 CETA but there are great changes on the composition of the Tribunal of First Instance[31] and the term of appointment,[32] which may lead to more coherence and consistency in results due to fewer but more highly qualified, and more independent long-term members.

B. Features of the EU ICS Mechanism

1. More Concerns on Public Interests

In response to the criticism that the current ISDS mechanism poses a threat to the host states' right to regulate, the EU ICS mechanism seeks to rebalance the interests of investors and host states. In Chapter 9, Article 9.16 of the *Trans-Pacific Partnership* ("TPP")[33] provided that the provisions shall not be construed to prevent a party from adopting, maintaining or enforcing any measure otherwise consistent with the Chapter for the purpose of ensuring that investment activity in its territory is undertaken in a manner sensitive to environmental, health or other regulatory objectives. In comparison, the TTIP Draft has further enriched the scope of legitimate public welfare objectives, which include but is not limited to public health, safety, environment or public morals, social or consumer protection or promotion, and protection of cultural diversity.

2. Avoidance of Potential Double Remedies

Under the current ISDS mechanism, investors might delay undertaking their obligation owed to the host states by using judicial settlement --including the hearings made by the courts at the place of arbitration-- and arbitral settlement simultaneously. Pursuant to Article 9.20 of the TPP, such parallel proceedings were precluded by the TPP. However, the TPP does not

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[31] EU-Singapore FTA, Art. 3.9.2. The Committee shall appoint six members to the tribunals. The EU party and Singapore shall appoint two members and the both parties shall jointly nominate two members who shall not be nationals of any member State of the EU and of Singapore.

[32] EU-Singapore FTA, Art. 3.9.5. The Members shall be appointed for an eight-year term. However, the inaugural terms of three of the six persons appointed immediately after the entry into force of this Agreement, to be determined by lot, shall extend to twelve years.

[33] The Comprehensive and Progressive Trans-Pacific Partnership ("CPTPP") concluded on 8 March 2018 has adopted all of provisions in Investment Chapter (Chapter 9) of the TPP.

prohibit investors from seeking domestic judicial proceedings before they initiate arbitral proceedings. That is to say, investors can still initiate the ISDS mechanism when they didn't get favorable resolutions in the domestic courts of the host states, thereby having a two-tier system to seek remedies while the host states can only seek remedies of one form. In contrast, under the EU ICS mechanism, investors have been excluded from double remedies, which is not only consistent with the principle of equality and justice, but also instrumental in balancing the interests of investors and host states.

3. Promotion of the Tribunal's Justice and the Coherence of Its Decisions

Despite great endeavors made by the UNCITRAL, the ICSID and some countries to reform the current system, the ISDS, a mechanism born out of commercial arbitration, still preserves many characteristics of a commercial arbitration. Worse still, the limited effects of the reforms were pared down because of the fragmentation of International Investment Agreements (hereinafter "IIAs").[34] The report of the Investor-State Dispute Settlement (ISDS) Provisions in the EU's International Investment Agreements submitted by the EU International Trade Commission to the European Parliament, mentioned that one of the ideal ways to resolve the drawbacks of the current system was to exhaust local remedies of host states if their domestic courts are sufficient to ensure due process.[35]

The EU ICS mechanism, by contrast, contributes to the coherence and predictability of investment arbitration by constructing an Appeal Tribunal. On the one hand, since the Appeal Tribunal is competent to rectify the decisions made by the Tribunal of First Instance, the latter will be more prudent when making decisions. On the other hand, the Appeal Tribunal has the competence to review both factual and legal issues. Moreover, due to the limited number of its members, the constitution of the Appeal Tribunal is relatively stable. However, due to fragmented IIAs and different composition of tribunals, to what extent coherence and stability shall be followed is still doubtful.

4. Enhancement of Procedural Justice

Apart from the changes mentioned above, the EU ICS mechanism also endeavors to make up for other procedural defects. For example, pursuant

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[34] *See* Wang-Yan, "*Controversies between the US and the EU over Reforms of Arbitration Mechanism of International Investment*", Global Law Review, 2017(2), at 183.

[35] European Parliament's Committee on International Trade, Investor-State Dispute Settlement (ISDS) Provisions in the EU's International Investment Agreements, available at <http://www.europarl.eu/RegData/etudes/STUD/2014/534979/EXPO_STU(2014)534979_EN.pdf> (accessed 1 January 2019).

to the CETA, the arbitration tribunal may receive unsolicited submissions of briefs from *amicus curiae* under some specific circumstances.[36] Article 23 of the Investment Chapter of the TTIP provided that any natural or legal person which can establish a direct and present interest in the result of the dispute can be permitted to intervene as a third party. The intervener shall receive a copy of every procedural document served on the disputing parties, save the confidential documents. The intervener may also submit a statement within a time period set by the Tribunal and shall be permitted to make an oral statement in hearings. Nonetheless, the intervention is limited to supporting, in whole or in part, the award sought by one of the disputing parties and that's why the TTIP uses the expression of "right of intervention" instead of "right of standing" in its text. Furthermore, the TTIP laid down specific rules concerning the obligation of notification imposed on the disputing party benefiting from it,[37] which to some extent, helps reduce frivolous claims made by investors. To restrain investors from making frivolous claims, the Investment Chapter of the TTIP also laid down provisions regarding the security for costs.[38]

5. Appropriate Response to the Doubts About the Impartiality of ISDS

The ICSID, the most representative institution of the ISDS mechanism, was headquartered in Washington D.C., US. By far, the US has never failed in any ISDS case in which it acted as the respondent state, inducing the doubts of many countries and organizations, including EU, regarding the impartiality of the ISDS mechanism. In response, the EU ICS mechanism is seeking to shift most of the ISDS cases from the ICSID to the ICS in order to relieve such doubts. Meanwhile, this move also epitomizes the efforts that EU has made to vie with the US for the dominance over international investment agreements.

6. Improved Efficiency of Dispute Resolutions

Under the current ISDS mechanism, the ICSID being the representative, it takes 3-4 years on average to process an ISDS case. Pursuant to the provisions of the Investment Chapter of the TTIP concerning the ICS mechanism, the Tribunal of First Instance shall issue a provisional award within 18 months of the date of submission of the claim. In the event that neither disputing party has appealed to the Appeal Tribunal, a provisional award shall become final if 90 days have elapsed after being issued.[39] Generally,

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[36] CETA, Annex 39-A (Rules of Procedure for Arbitration), Arts. 43-46.
[37] TTIP Chapter II, Art. 8.
[38] TTIP Chapter II, Art. 21.
[39] TTIP Chapter II, Art. 28(5).

the appeal proceedings shall not exceed 180 days, from the date a party to the dispute formally notifies its decision to appeal, to the date the Appeal Tribunal issues its decision. In certain circumstances, the period can be extended but shall never exceed 270 days.[40]

III. Potential Challenges the EU ICS Mechanism Might Face

Compared with the current ISDS mechanism, the EU ICS mechanism made significant endeavors in the promotion of the right to regulate of host states, the avoidance of double remedies and the improvement of the coherence of decisions. That being said, given its internal drawbacks and the oppositions that come from both inside and outside the EU, the ICS mechanism might not be fully realized.

A. Internal Defects of the ICS Mechanism

1. The establishment of the Investment Tribunal is ultra vires.

Setting up the Investment Tribunal, EU has in fact exceeded the limit of its own legislative and judicial authority. EU has the exclusive competence to regulate direct investment. However, the ICS mechanism encompasses regulations on indirect investment, and thus deviates from the legislative foundation of EU laws. Furthermore, the novel Investment Tribunal puts EU and its member states under its jurisdiction, which means that EU and its member states are required to transform their current domestic judicial systems. However, on 16 May 2017, the Court of Justice of the EU ("ECJ") clarified that in relation to indirect investment and ISDS, the EU does, in fact, share competence with its member states, since such a mechanism "removes disputes from the jurisdiction of the courts of member states".[41] Now that approval by member states and regional parliaments is required, the EU Commission's strategy appears to be to split such future agreements into two groups: one which does not require member states' ratification, and the other pertaining to the investment portions that require approval from all member states and regional parliaments. In any event, obtaining approvals from member states and regional parliament will be a cumbersome process.[42]

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[40] TTIP Chapter II, Art. 29(3).

[41] Opinion 2/15 (EU-Singapore FTA) of 16 May 2017.

[42] See Stephan Wilske, Raeesa Rawal and Geetanjali Sharma, "*The Emperor's New Clothes: Should India Marvel at the EU's New Proposed Investment Court System*", Indian Journal of Arbitration Law, 6(2), 2018, at 88.

2. The scope of host governments' right to regulate is still indefinite.

Though the TTIP Draft, the 2016 CETA, and the 2016 EU-Vietnam FTA intend to safeguard host governments' right to regulate and what they have done theoretically may contribute, there are no specific criteria that can oblige or lead the Investment Tribunal to interpret the host governments' right to regulate. In fact, the key issue, i.e. the issue of how to balance the promotion and protection of investment and host governments' right to regulate, was merely shifted from arbitral tribunals to the Investment Tribunal. Before these treaties came into existence, regulatory measures taken by the host states were considered legitimate if they were proportionate to the objectives of public policies and if there were no other methods that could impose fewer restrictions on investment. However, if the Investment Tribunal still employs such methods in practice when making decisions and repeats the practice just like that of the current ISDS mechanism, then the EU ICS mechanism will be of little help to define the scope of the host governments' right to regulate. More importantly, the EU ICS mechanism should be more prudent when taking into consideration issues such as environment and human rights. Excessive transition from private law into public law might impair the inherent value of the ICS and even poses a threat to the value of existence of the whole EU ICS mechanism.

3. The professionalism of Tribunal members cannot be guaranteed.

In response to doubts over the qualification of arbitrators, impartiality and conflicts of interests in the current ISDS mechanism, the ICS substantially reduces the number of the members of tribunals. For example, the 2016 EU-Vietnam FTA provided that the list of arbitrators in the Tribunal of First Instance shall be composed of three sub-lists: (a) one sub-list for Vietnam; (b) one-sub list for the EU; (c) one sub-list of individuals who are not nationals of either Party and do not have permanent residence in either Party.[43] As for the arbitration panel established to hear a specific case, two of the three arbitrators shall be appointed by each party from the sub-list of that party, while the other arbitrator is selected from the third-party sub-list and he or she shall act as the chairperson to the arbitration panel.[44] The random selection of the chairperson is to guarantee that every member has an even chance to be selected. The Investment Chapter of the TTIP stipulated that a judge shall be paid a monthly retainer fee. The retainer fee of a judge of the Tribunal

[43] 2016 EU-Vietnam FTA Chapter 13 (Dispute Settlement), S. 4, Art. 23(1).
[44] 2016 EU-Vietnam FTA, Chapter 13 (Dispute Settlement), S. 4, Art. 7.

of First Instance suggested by the EU would be around EUR 2,000 (€2,000) per month, i.e. one third of the retainer fee for a WTO Appellate Body member,[45] while that of a judge of the Appeal Tribunal would be around EUR 7,000(€7,000) per month, which is the same as for a WTO appellate body member.[46] Apart from that, fees for dealing cases are not be included in the retainer fee and shall be counted separately.[47] The Judges shall be available at all times and on short notice, and shall stay abreast of dispute settlement activities.[48] Although the current standard of the retainer fee is quite considerable, the requirement of serving on a full-time basis may still deter the most experienced lawyers from participating in it. Both the investors and host states are deprived of their right to choose arbitrators since the composition of the Tribunal of First Instance and the Appeal Tribunal is prescribed to be selected randomly and that the chairperson shall only be selected from a third-party list. It is questionable whether members of the ICS Tribunal appointed through a non-transparent and non-consultative process will be free from real and perceived bias.[49] If the appointment process is lacking in transparency or fairness, it shall be a great concern to impair the ICS values. Although the existence of an appellate system might be conducive to the coherence of the decisions made in different cases, it might also lead to a quagmire if most of the cases would be appealed, and thus results in the further increase in time and expenses of dispute settlement. A typical and instructive example is the dispute settlement mechanism of the WTO. According to relevant statistics, from 1996-2016, 222 cases passed panel reports and 151 of them were appealed, which means that the rate of appeals was up to 68%.[50] If the existence of the Appeal Tribunal brings about significantly more appeals of cases, the increment in time and cost hereby induced would delay the compensation to the investors, or lead to more costs and expenses to both parties.

4. The determination of the respondent is complicated.

EU's *Regulation No. 912/2014Establishing a Framework for Managing Financial Responsibility Linked to Investor-to-state Dispute Settlement Tribunals Established by International Agreements to Which the European*

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[45] TTIP Chapter II, Art. 9.12

[46] TTIP Chapter II, Art. 10.12

[47] CETA explicitly stated that members of the Investment Tribunal shall be paid a monthly retainer fee but did not specify the exact numbers. *See* CETA Chapter VIII (Trade in Services, Investment and E-Commerce), Arts. 14, 15 and 17.

[48] TTIP Chapter II, Art. 9.11

[49] See Stephan Wilske, Raeesa Rawal and Geetanjali Sharma, "*The Emperor's New Clothes: Should India Marvel at the EU's New Proposed Investment Court System*", Indian Journal of Arbitration Law, 6(2), 2018, at 89-90.

[50] WTO: Annual Report for 2016, Appellate Body, at 136.

Union is Party issued on 23 July 2014 set up the principle that one shall bear responsibility for its own conducts. Article 5.5 of the Investment Chapter of the TTIP also recognizes this principle and goes a step further, specifying that EU has the competence to determine whether EU or a certain member state shall be the respondent. Once it makes such determination, neither EU nor the member state concerned can assert the inadmissibility of the claim, lack of jurisdiction of the Tribunal or otherwise assert that the claim or award is unfounded or invalid. The vulnerability of this mechanism, however, is whether in practice EU will dodge its own responsibility and scapegoat a certain member state, especially one with limited capacities. It also casts doubt over whether EU shall bear joint responsibility or partial responsibility if the interests of investors cannot be satisfied. Furthermore, since EU is neither a party of the *Washington Convention*, nor a party of the *Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 1958* (hereinafter "*New York Convention*"), if EU does not voluntarily perform its obligations under an award, how can the winning party seek remedies in such event?

5. The ICS mechanism obviously carries some overly ambitious elements.

The ICS mechanism fundamentally transformed the current ISDS mechanism but in the meanwhile it was inevitably influenced by the ISDS mechanism as well as by the court system. This explains why the expression of "greater certainty" appeared 25 times in the text of Chapter II of the TTIP Draft (22 times in the text, 3 times in the footnote), 5 times in the 2016 CETA (4 times in the text, 1 in the footnote), and 14 times in the EU-Vietnam FTA of 2016 (9 times in the text, 5 times in the footnote). Different from the current ISDS mechanism which only allows for the procedure of annulment, Chapter 13 (*Trade in Services, Investment and E-Commerce*), Section 2, Article 28 of the EU-Vietnam FTA and Article 29 of the EU's TTIP Draft substantially expanded the authority of the Appeal Tribunal. Accordingly, the Appeal Tribunal not only can reject the provisional award of the Tribunal of First Instance, but also can modify or reverse the legal findings and conclusions in the provisional award in whole or part while the annulment procedure of the ISDS mechanism can only affirm or reserve an award in whole. Therefore, it's obvious that the Appeal Tribunal has greater discretion than the annulment procedure of the existing ISDS mechanism. However, greater discretion may inevitably lead to "greater certainty". We can even say that "greater certainty" makes the mechanism impractical and even unrealistic. Whether the Appeal Tribunal can lead to greater certainty as what has been expected by drafters of the ICS mechanism shall depend on many factors including but not limited to: (a) there are a certain amount of decisions that can provide a

reference for the expected results of future disputes while the ICS mechanism has not been put into practice; (b) different Appeal Tribunals organized on a rotation basis can make decisions based on the relative consistency and coherence (i.e. there is no important value for information if the decisions are very diversified on similar disputes); (c) different Appeal Tribunals can interpret the disputed treaty or the disputed contract in good faith, particularly paying more attention to the original purposes of the disputed treaty or contract and never abusing their power in treaty or contractual interpretation; (d) the whole process of the ICS mechanism can be seriously limited to the certain period of time limit set in BITs/FTAs in order to prevent impact from potential external noises. In addition, it must be emphasized that "greater certainty" in the ICS mechanism improves the expectation to a higher standard for the legitimacy and fairness and may result in the whole mechanism going bankrupt if it does not work smoothly in practice.

6. The EU ICS has not been put into practice and there will be some obstacles in the multilateralised the EU ICS.

According to the text, the EU ICS mechanism has some significant advantages. For example, it includes an Appeal Tribunal and promotes transparency, clearly establishes and maintains the right to regulate of host states, sets high standards for selection and code of conduct for members, strengthens the independence and impartiality of the dispute settlement mechanism as well as avoids double remedies.[51] However, it just stays at the theoretical and ideal level, and has not been put into practice. No one can predict whether it will really work in practice. If the Tribunal of First Instance and the Appeal Tribunal, especially the chairman whose nationality is of the third party abuses his power in a similar way in the current ISDS mechanism, the advantages of an Appeal tribunal for consistency or coherence with preceding cases may lead to disasters of repeating faults in the following cases. Furthermore, the EU ICS has only been adopted in bilateral treaties and has not been adopted in multilateral agreements though EU initiated to establish a MIC, and there may be a very long and different way to put it into reality.

B. Oppositions to the ICS Mechanism inside the EU

Different from the US BITs, the traditional BITs initiated by EU member states[52] are not so detailed and specific and there has not been an independent

[51] Jian Zhang, *Research on Jurisdiction in International Investment Arbitration*, Doctoral Degree Thesis of China University of Political Science and Law, 2018, at 244.

[52] Among EU member States, Germany, France, Netherlands, Belgium as well as the United Kingdoms have concluded a number of BITs and established the broad BIT framework.

chapter for dispute settlement.[53] Issues like the transparency, procedure publication, selection of arbitrators and the code of conduct of the arbitrators are left out, let alone the acceptance of an appellate mechanism. However, in recent years, almost all the BITs conducted by the EU member states have adopted the ISDS mechanism and therefore, the member states might not endorse the substantive transformation initiated by the ICS mechanism. In practice, 28 EU member states can be divided into four groups according to their participation in ISDS and the roles they have played.

Table A: The participation of the EU member states in the ISDS mechanism and the main roles they have played[54]

	Types of Group[55]	***Countries***	***Number of Countries***
1	A frequent claimant and unusual respondent under the ISDS mechanism	Austria, Belgium, Cyprus, France, Germany, Greece, Luxembourg, the Netherlands, U.K.	9
2	A frequent respondent and unusual claimant under the ISDS mechanism	Bulgaria, Croatia, Czech, Hungary, Latvia, Poland, Romania, Slovakia	8
3	An unusual claimant and unusual respondent under the ISDS mechanism	Denmark, Estonia, Finland, Ireland, Lithuania, Malta, Portugal, Slovenia, Sweden	9
4	A frequent claimant and frequent respondent under the ISDS mechanism	Spain, Italy	2

As demonstrated in the table above, large power blocks like Germany, France and U.K., with great clout belong to the first group. Generally

[53] The 2006 Model BIT of France (*Draft Agreement between the Government of the Republic of France and the Government of ... on the Reciprocal Promotion and Protection of Investments*), Art. 7 provided that if a dispute has not been settled amicably within a period of six months, it shall be submitted at the request of either party to the arbitration of the ICSID. In the case where the dispute may involve the responsibility for actions or omissions of sub-sovereign entities of the Contracting Parties, the sub-sovereign entity must give their unconditional consent to the use of arbitration of the ICSID. The 2008 Model BIT of Germany (*Treaty between the Federal Republic of Germany and ... Concerning the Encouragement and Reciprocal Protection of Investments*), Art. 10 prescribed that if the dispute cannot be settled amicably within six months, it shall, at the request of the investor of the other Contracting State, be submitted to arbitration.

[54] See Investment Policy Hub, UNCTAD, available at <http://investmentpolicyhub.unctad.org/ISDS/FilterByCountry> (accessed 24 May 2019).

[55] Any EU member State which has claimed more than 10 ISDS cases and has been challenged in less than 10 ISDS cases is classified into the first group of "A frequent claimant and unusual respondent"; any EU member State which has been challenged in 10 ISDS cases and has claimed no more than 10 ISDS cases is classified into the second group of "A frequent respondent and unusual claimant"; any EU member State which has been challenged in 10 ISDS cases and has claimed no more than 10 ISDS cases is classified into the third group of "A frequent respondent and unusual claimant"; Any EU member State which has claimed no more than 10 ISDS cases and has been challenged in no more than 10 ISDS cases is classified into the fourth group of "An unusual claimant and unusual respondent".

speaking, those states are the real beneficiaries of the current ISDS mechanism though there have been some negative impacts in recent years. Take Germany as an example, it is the country that has concluded the largest network of BITs in the world,[56] and overall those BITs with ISDS provisions have provided better protection for OFDI of German investors until Germany was brought before the ICSID twice by Vattenfall. A large number of those BITs encompass the current ISDS mechanism and the German Association of Judges have clearly raised their objections towards the ICS mechanism.[57]

The Netherlands Draft Model BIT in 2018, still adopts the arbitration-style terms and phrases such as "tribunal", "arbitrators" and "award", but it pays more attention to multilateral investment court (Art.15), transparency (Art.20) and efficiency (award to be ruled within 24 months, Art.22). It can be inferred that the Netherlands does not support the EU ICS without any reservations.

C. Oppositions to the ICS Mechanism from Other Countries

Owing to the economic crises, the refugee crises, the Brexit and other setbacks, EU's influence in the world has been weakened. EU, therefore, is seeking to vie with the US in the field of investment regulation and restore its clout by transforming the ISDS mechanism and cooperating with Canada and other countries. Ostensibly, EU's OFDI is neck and neck with that of the US and Japan. However, EU's OFDI is mainly comprised of two parts: the cross-border capital flows within EU and EU's investment in the US. Therefore, EU is far less competent than the US in its negotiation with other countries when persuading them to accept the ICS mechanism. For instance, the Japanese Association of Judges has clearly stated their opposition to the ICS mechanism. Although the US and China haven't shown their stance yet, it is impossible for US to abandon the current ISDS system that US has been acquainted with and has never failed as a respondent state, and the ISDS

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[56] The Germany-Pakistan BIT was concluded on 25 November 1959 was the first BIT in the world. By the end of October, 2017, Germany has signed 155 BITs with other countries. 15 countries have signed BITs twice with Germany, including China, Congo, Egypt, Ethiopia, Gabon, Guinea, Iran, Jordan, Morocco, Oman, Pakistan, Romania, Sri Lanka, Thailand and Yemen. 20 of those BITs have been terminated, including the Germany-India BIT, the Germany-Indonesia BIT and the Germany-Bolivia BIT. *See* UNCTAD, available at <http://investmentpolicyhub.unctad.org/IIA/CountryBits/78#iiaInnerMenu> (accessed 14 May 2019).

[57] See The Oppositions of the German Association of Judges to the European Commission's Proposal for the Investment Tribunal System, the Ministry of Commerce of People's Republic of China, available at <http://www.mofcom.gov.cn/article/i/jyjl/m/201603/20160301282656.shtml> (accessed 15 December 2018).

system is retained in the recently concluded USMCA. Considering more interests abroad than before and the status of capital-exporting, China may resort to accept a more powerful, more convenient and well-balanced dispute settlement mechanism. It's obvious that the EU ICS shall not be the only choice for China. Is it possible for China to adopt the EU ICS at the first priority, the second priority or just reference? What kinds of changes shall China make for the EU ICS? Due to the internal defects of the ICS mechanism and the dissenting voices from both inside and outside of the EU, the prospect of the ICS mechanism is still in a haze. As China is now actively negotiating with EU about the BIT, we should make detailed consideration of potential problems and seek feasible solutions.

IV. CHINA'S INTERESTS AND PRACTICES UNDER THE ISDS MECHANISM

A. China's Special Interests in the Investment Law

Ever since 1992, China has been the developing country that absorbs the most foreign direct investment. In recent years, with the transformation and upgrade of the domestic economy, there have been significantly more claims against the Chinese government for some of its regulatory measures under the ISDS mechanism. On the flip side, with the rapid increment of China's outbound foreign direct investment, the potential risks of investment disputes between Chinese investors and foreign governments have increased substantially. Therefore, China is no longer a bystander or a passive accepter, but rather should be an active participant and even a rule-maker in the ISDS mechanism. In particular, China should make better preparations for potential investment disputes by striking a balance between its interests in FDI and those in the OFDI. Before the 1998 China-Barbados BIT, all the BITs China had signed merely allowed for the submission to international arbitration of compensation disputes arising from expropriation or nationalization.[58] From the standpoint of a host state, such a strict restriction on the scope of arbitrated disputes is far from ominous. However, from the perspective of a home state, such a choice might be detrimental to the protection of China's interest in the OFDI. Therefore, we should take an appropriate stance on the ISDS mechanism in the light of China's development and future. Due to more concerns on public interests and the right to regulate of host states, China adjusted its attitude towards the ISDS mechanism in

[58] The only exceptions are the 1994 China-Romania BIT and the 1997 China-South Africa BIT, based on which all investment disputes can be submitted to the ISDS mechanism.

the 2012 China-Canada BIT, and the decisions made by either contracting state with respect to whether or not to initially approve an investment that is subject to review or permit an investment that is subject to national security review is excluded from the coverage of ISDS mechanism.[59]

In this way, theoretically, China BITs can be roughly divided into three phases, starting from the 1998 China-Barbados BIT and ended with the 2012 China-Canada BIT.[60] In the first phase (1982-1998), the scope of the application of the ISDS mechanism was limited to compensation disputes arising from expropriation and nationalization. In the second phase (1998-2012), China substantially expanded the coverage of ISDS mechanism and allowed all investments disputes to be arbitrated.[61] In the third phase (2012-present), China imposed some restrictions on arbitrated issues in the ISDS mechanism. It is also reflected in China's BITs concluded with EU member states. By now, China has concluded 26 BITs with EU member states.[62] Among of which, 10 BITs[63] belonged to the second phase, and other 16 BITs belong to the first phases. However, China-EU BIT negotiations on ISDS provisions shall lead to fundamental changes in dispute settlement.

B. China's Acceptance of the Current ISDS Mechanism and Its Practice

According to the statistics of the UNCTAD, by 31 December 2018, China had been involved in 8 ISDS cases.[64] Among these, China appeared in 5 cases as claimants, and in 3 cases as respondent state. The details are as follows:

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[59] 2012 China-Canada BIT, Article 34.

[60] To be brief, the 1998 China-Barbados BIT and 2012 China-Canada BIT hereinafter will be referred to as "1998" and "2012" respectively.

[61] In the second phase, only the China-Qatar BIT of 1999 and the China-Bahrain BIT of 1999 still limited the application of the ISDS mechanism to the disputes arising from expropriation and nationalization.

[62] Among EU member States, Ireland has not concluded a BIT with China, and Belgium and Luxembourg concluded a BIT with China as the Belgium-Luxembourg Economic Union in 1984 and in 2005 respectively, and the 2005 BIT has come into effect as from 1 December 2009.

[63] According to the time sequence of conclusion, the contracting States are Serbia (2001), Netherlands (2001), Germany (2003), Latvia (2004), Finland (2004), Belgium-Luxembourg Economic Union (2005), Spain (2005), Portugal (2005), France (2007) and Malta (2009).

[64] It is reported by IA Reporter that China Railway Construction Corporation brought the disputes against Mexico on 4 December 2018, but there is no detailed disclosed information. And the UNCTAD has not counted it in, available at <http://www.sohu.com/a/208771739_652123> (accessed 8 December 2018).

Table b: List of the ISDS cases involving China as the home state[65]

	Short Case Name	***Legal Basis***	***Status***	***Outcome of Proceedings***	***Arbitration Institution***
1	Sanum Investments v. Laos (2) (2017)[66]	China-Lao People's Democratic Republic BIT (1993)	Pending	Procedural Order No.3 made on 14 November 2017.	ICSID (Arbitration Rules: ICSID Additional Facility)
2	Beijing Urban Construction Corpn. (BUCG) v. Yemen (2014)[67]	China-Yemen BIT (1998)	Settled[68]	On 31 May 2017, the Tribunal made the decision on its jurisdiction. It declined the jurisdiction to hear the claims.	ICSID
3	Ping An v. Belgium (2012)[69]	China-BLEU BIT (1984/2005)	Decided	On 30 April 2015, the Tribunal decided to dismiss Ping An' claims for lack of jurisdiction.	ICSID
4	Beijing Shougang v. Mongolia (2010)[70]	China-Mongolia BIT (1991)[71]	Pending	One 30 June 2017, the Tribunal decided that it did not have the jurisdiction to hear the claims.	PCA
5	Tza Yap Shum v. Peru (2007)[72]	China-Peru BIT (1994)	Decided	On 7 July 2011, the Tribunal decided that the conduct of the Peruvian government constituted an indirect expropriation of Tza's investment. Tza was awarded around $786,000 in compensation.	ICSID

[65] *See* UNCTAD available at <http://investmentpolicyhub.unctad.org/ISDS/CountryCases/42?partyRole=1> (accessed 15 November 2018).

[66] *Sanum Investments Ltd.* v. *Lao People's Democratic Republic*, ICSID Case No. ADHOC/17/1, available at <http://investmentpolicyhub.unctad.org/ISDS/Details/797> (accessed 17 May 2018).

[67] *Beijing Urban Construction Group Co. Ltd.* v. *Yemen*, ICSID Case No. ARB/14/30.

[68] *Beijing Urban Construction Group Co. Ltd.* v. *Yemen* case has been settled, but there is no detailed disclosed information, available at <https://investmentpolicyhub.unctad.org/ISDS/CountryCases/42?partyRole=1> (accessed 8 December 2018).

[69] *Ping An Life Insurance Co. of China Ltd.* v. *Kingdom of Belgium*, ICSID Case No. ARB/12/29.

[70] *China Heilongjiang International Economic & Technical Cooperative Corpn.* v. *Mongolia*, PCA Case No. 2010-20, available at <http://www.pcacases.com/web/view/48> (accessed 31 October 2018).

[71] The award of the Tribunal has not been made public. Sources from the official account of the Wanbanglaw. According to the website of PCA, the Tribunal made its award on the jurisdiction on 30 June 2017, but the result was not available to public. According to the website of UNCTAD, this case concerned indirect expropriation, available at <http://investmentpolicyhub.unctad.org/ISDS/Details/367> (accessed 31 July 2018).

[72] *Tza Yap Shum* v. *Republic of Peru*, ICSID Case No. ARB/07/6.

Table c: List of the ISDS cases involving China as the host state[73]

	Short Case Name	***Investor's Nationality***	***Legal Basis***	***Status***	***Outcome of Proceedings***	***Institution of Arbitration***
1	Hela Schwarz v. China (2017)[74]	German	China-Germany BIT (2003)	Pending	On 10 August 2018, the tribunal made No.2 Procedural Order of Decision on the Claimant's Request for Provisional Measures.	ICSID
2	Ansung Housing v. China (2014)[75]	Korean	China-Korea BIT (2007)	Decided	On 9 March 2017, the Tribunal made the award of dismissing Ansung's claims and terminating all the proceedings.	ICSID
3	Ekran v. China (2011)[76]	Malaysian	China-Israel BIT (1995) and China-Malaysia BIT (1998)	Settled	All of the proceedings were terminated on 22 July 2011.	ICSID

Among the aforementioned 8 cases involving Chinese parties, the *Ekran* case and the *BUCG* case were settled while the *Hela Schwarz* case is still in process. Furthermore, the Tza Yap Shum case of 2007 and the Sanum Investments v. Laos (2) case of 2017 mainly concerned whether investors from Hong Kong and Macao could invoke the BITs signed by China — in other words, they concerned the interpretation of the "investors" under the BITs. Therefore, our analysis of China's participation and practices under the ISDS mechanism should be primarily based on the two decided cases (*Ping An* v. *Belgium* case[77] and *Ansung* v. *China* case) and one settled case (*BUCG* v. *Yemen* case).

In the *Ping An* case, the Tribunal held that Article 10(2) of the 2005 China-BLEU BIT made clear stipulations on the application of the old and

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[73] *See* UNCTAD, available at <http://investmentpolicyhub.unctad.org/ISDS/CountryCases/42?partyRole=2> (accessed 15 December 2018).

[74] *Hela Schwartz GmbH* v. *People's Republic of China*, ICSID Case No. ARB/17/19, available at <https://www.italaw.com/cases/5973> (accessed 8 December 2018).

[75] *Ansung Housing Co. Ltd.* v. *People's Republic of China*, ICSID Case No. ARB/14/25.

[76] *Ekran Berhad* v. *People's Republic of China*, ICSID Case No. ARB/11/15.

[77] On 19 September 2012, Ping An Insurance (Group) Company of China, Limited (hereinafter "Ping An") brought the Belgian government before the ICSID for its compulsory split of Fortis Group (hereinafter "Fortis"). It was the first time that Chinese investors had used the ICSID mechanism to protest their interests in investment. On 30 April 2015, ICSID made an award against Ping An.

new BIT.[78] The Tribunal decided, "*there is nothing in the wording of the 2005 BIT to justify on the basis of its express language, or on the basis of an implication or inferences, that the more extensive remedies under the 2005 BIT would be available to pre-existing disputes that had been notified under the 1984 BIT but not yet subject to arbitral or judicial process*,"[79] thereby dismissing the claimant's claims. Ping An could only invoke the 1984 BIT and the 2005 BIT was not applicable to this dispute.[80] The decision of the Tribunal made no reference to the merits of the dispute, i.e. whether the Belgian government's compulsory split and resale of an institution in which the claimant had invested in constituted indirect expropriation. In the *Ansung Housing* case, the Tribunal dismissed all claims made by Ansung Housing Co., Ltd. on the ground that it was time-barred,[81] pursuant to ICSID Arbitration Rule 41(5).[82] The award, therefore, did not touch upon the merits either. The *Ansung Housing* case reminded China that the arbitration rules and arbitration procedures were of crucial importance to the settlement of disputes.

In the *BUCG* case, the Tribunal affirmed its decision on the jurisdictional issue in May 2017. The Tribunal held that it had the jurisdiction over this case but also pointed out that it could only hear those claims related to the claimant's allegations of expropriation.[83] Thus far the Tribunal has not proceeded to hear the legal merits, i.e. whether the control of the Yemeni local military force over the BUCG's assets and construction site constituted

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[78] China signed two BITs with the Belgium-Luxembourg Economic Union (hereinafter "BLEU") in 1984 and 2005 respectively. The 2005 BIT came into effect as from 1 December 2009. Article 10(2) of the 2005 China-BLEU BIT provided that "The present Agreement shall apply to all investments made by investors of either Contracting Party in the territory of the other Contracting Party, whether made before or after the entry of this Agreement, but shall not apply to any dispute or any claim concerning an investment which was already under judicial or arbitral process before its entry into force."

[79] *Ping An Life Insurance Co. of China Ltd.* v. *Kingdom of Belgium*, Award, 30 April 2015, para 231.

[80] Pursuant to Art. 10 of the *1984 China-BLEU* BIT, if the dispute between the investor and the host State cannot be settled amicably through consultation, it shall be subject to the jurisdiction of the host State. As an exception, a dispute which arises from an amount of compensation for expropriation, nationalization or other similar measures and has not been settled within 6 months, can be submitted to an international arbitration without resort to any other means. In contrast, Article 8 of the 2005 BIT provided that if the investor-State dispute cannot be solved amicably through consultation, the investor may choose to submit the dispute to the ICSID. The *2015 China-BLEU BIT* did not make restrictions on the scope of arbitrated disputes.

[81] *Ansung Housing Co. Ltd.* v. *People's Republic of China*, Award, 9 March 2017, Section X.

[82] R. 41(5) of the ICSID Arbitration Rules provided that "if the Tribunal decides that the dispute is not within the jurisdiction of the Center or not within its own competence, it shall render an award to that effect."

[83] *Beijing Urban Construction Group Co. Ltd.* v. *Yemen*, Decision on Jurisdiction, 31 May 2017, paras 146-147.

de facto expropriation. However, the BUCG case has been settled with no released information. In summary, both Chinese investors and the Chinese government have begun to be involved in the ISDS mechanism in recent years. Nonetheless, due to very limited experience in practice and, they are thus unacquainted with the opportunities as well as the potential risks raised by the ISDS mechanism.

V. China's Choice and Future Contributions

During a long certain period, China has remained skeptical and even averse to an international dispute settlement mechanism. China's acceptance of the WTO dispute settlement mechanism and the ISDS mechanism may be the only two deviations from China's tradition. With China's transition from a large FDI recipient[84] to a big player in the two-way investment, China is likely to make its own choice of the development of the ISDS mechanism.

Due to the significant interests in two-way investment, in recent years, China has concentrated on negotiating China-U.S. BIT,[85] China-EU BIT, China-Japan-Korea FTA and other new BITs and other treaties with investment provisions ("TIPs"). Among the aforementioned BITs and TIPs, China intends to establish a more balanced international investment rules system to protect two-way investment and even to make more voices of China in the future international investment law to strengthen the "presence" and even the leadership of China in the future international community.

However, the China-U.S. BIT negotiations have been suspended after the Trump Administration took the position and interpreted the "American-First" policy as "zero-sum game" in many circumstances. It is almost impossible for China and U.S. to recommence the BIT negotiations under the serious trade tensions between the two giants in the short term. Due to the meager chance to partner with U.S., China shall focus more than ever on enhancing the cooperation with EU. In addition to this, it is particularly worth emphasizing that the two-way investment between China and EU needs to be improved. According to the EU statistics, the level of EU FDI

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[84] China continued to be the largest FDI recipient among developing countries and send largest in the world, only behind US. See UNCTAD, *World Investment Report 2018*, New York and Geneva: United Nations, 2018, at 4.

[85] From 31 October 2016 to 16 November 2016, the US and China negotiated the China-US BIT for the 31st round. By then, the parties had exchanged the Negative List for three times. See the Ministry of Commerce of People's Republic of China, available at <http://www.mofcom.gov.cn/article/ae/ai/201611/20161101678030.shtml>(accessed 20 December 2017). By far the two parties haven't entered into the 32nd round of negotiation yet.

in China has hovered around EUR 10 billion per year in the past five years before 2015 and has further declined in 2016 and 2017 to EUR 8 billion per year.[86] While in the same period, China was the largest partner for EU imports of goods and the second largest partner of EU exports of goods, with the trade export volume (from EU to China) of EUR 198.2 billion and the trade import volume (from China to EU) of EUR 374.6 billion.[87] While China's OFDI volume in EU reached USD 10.27 billion in 2017 and accumulated China's OFDI volume in EU reached USD 86.015 billion, they only occupying 6.49% of the China's OFDI volume in 2017 and 4.75% of the China's accumulated OFDI volume by 2017.[88] China-EU BIT shall be a good platform to enhance the cooperation between EU and China. The EU-China BIT negotiation was commenced in November 2013, and after meeting to consent on comprehensive scope, the EU and China have moved on to specific text-based BIT negotiations since January 2016.[89] During the 12th-16th rounds, the EU and China primarily focused on the basics of definitions, performance requirements, national treatment, fair and equitable treatment as well as dispute settlement. More topics were covered in the 17th-18th rounds, including expropriation, transparency, and sustainable development.[90] At the 20th EU-China Summit on 16 July 2018, both parties exchanged market access offers, whose feedback was then discussed in the 19th round held on 29-30 October 2018. The exchange of offers marks the milestone of BIT negotiations' progress, but to achieve the ultimate desired outcome for both sides, stress is needed on some main concerns, among which, the ICS is also counted in. In early March 2019, given the EU's ambition for a 2020 deadline for an EU-China BIT,[91] the *Foreign Investment Law of China* was passed by

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[86] Thilo Hanemann and Mikko Huotari, "EU-China FDI: Working towards Reciprocity in Investment Relations", available at <http://www.merics.org/en/papers-on-china/reciprocity> (accessed 14 January 2019.)

[87] China-EU-International Trade in Good Statistics, available at <http://ec.europa.eu/eurostat/statistics-explained/index.php/China-EU_-_international_trade_in_goods_statistics> (accessed 14 January 2019).

[88] Ministry of Commerce, National Bureau of Statistics and State Administration of Foreign Exchange of the People's Republic of China, 2017 Statistical Bulletin of China's Outward Foreign Direct Investment, Beijing: China Statistics Press, 2018, at 6, 14, 20.

[89] See European Parliament, Resolution of 9 October 2013 on the EU-China Negotiations for a Bilateral Investment Agreement, 2013/2674(RSP), available at <http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+TA+P7-TA-2013-0411+0+DOC+XML+V0//EN> (accessed 24 May 2019).

[90] See EU-China Comprehensive Agreement on Investment (EU-China CAI), available at <http://www.europarl.europa.eu/legislative-train/theme-a-balanced-and-progressive-trade-policy-to-harness-globalisation/file-eu-china-investment-agreement> (accessed 20 January 2019).

[91] Michael Peel, James Kynge and Lucy Hornby, "EU Seeks to Hasten China in Investment Deal to Curb Divisions", available at <https://www.ft.com/content/e8677c3c-4026-11e9-b896-fe36ec32aece> (accessed 15 March 2019).

the National People's Congress on 15 March 2019[92] which provides higher standards investment promotion and protection for foreign investors. In particular, after meetings between senior EU officials and Keqiang Li, the Premier of China in Brussels on 9 April 2019, a joint statement signaled China's willingness to discuss EU concerns about state support for its companies and forced technology transfer which are some of the major concerns in EU-China BIT negotiations, and China and the EU also set a 2020 target date to conclude the long-planned EU-China BIT.[93] All of them are signals to accelerate the EU-China BIT negotiations ahead of schedule.

It's determinable that the EU insists on incorporating ICS in the conclusion of TIPs with other contracting states including Canada, Vietnam, Singapore and Japan. It can be expected that EU will actively promote the ICS in the future BITs and TIPs without any reservations. The China-EU BIT will not be an exception. What is China's attitude to ICS in China-EU BIT negotiation? Will it be complete copy, conversion application or just for reference? If China decides to adopt the ICS wholly or incorporate some features of the ICS, what kinds of considerations will be asked by China and what kinds of key elements must be secured.

A. Partial Acceptance of the ICS mechanism in the China-EU BIT Negotiation

Although China hasn't taken a clear stand on the acceptance of the EU ICS mechanism yet, China's Ministry of Commerce has already considered and discussed the ICS mechanism. At present China is not only actively promoting the negotiations of the China-US BIT, the China-EU BIT and the China-Japan-Korea FTA, but also endeavoring to advance the signing or amendment of the international economic and trade agreements with countries along the "One Belt One Road". Thus, compared with other contracting parties who vary in their opinions on the ISDS mechanism, China seems to be faced with a dilemma of choosing among a reformed version of ISDS mechanism, the ICS mechanism, the rejection of the ICS mechanism, etc. Different from the role of a passive accepter and bystander that China used to play, the role China is now playing in the ongoing negotiations is a participant and even

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[92] The *Foreign Investment Law of China* will come into effect as from 1 January 2020, see Summary of China's New Foreign Investment Law, available at <https://npcobserver.com/2019/03/15/summary-of-chinas-new-foreign-investment-law> (accessed 24 May 2019).

[93] Jim Brunsden and Alan Beattie, "*Beijing and EU Agree Target of Next Year for Investment Access Deal*: *Premier Li Keqiang Signals Willingness to Discuss Concerns on State Support and Technology Transfer*", available at <https://www.ft.com/content/4a37a40c-5add-11e9-9dde-7aedca0a081a> (accessed 28 April 2019).

a future leader. To some extent, by bargaining with different contracting parties, China can even make appropriate modifications to the current ISDS mechanism and insert some Chinese elements, by which it can eventually establish a "China Model" led by China. As originally expected, the "China Model" may be developed from the current ISDS mechanism and adopted some EU ICS features. Factually, the Ministry of Commerce of China has discussed whether China may adopt the EU ICJ since mid-2016 and has focused on the MIC proposal.

In this way, if China can advance BIT negotiations with U.S. and EU at the same time, it may be favorable for China to optimize final results. Compared with the current ISDS mechanism, the China Model is closer to the EU's ICS, and therefore can better get the EU on the same page. Meanwhile, compared with the ICS mechanism, the China Model is closer to the American ISDS mechanism and thus can more easily land the US on the same page. From this perspective, the Chinese government can achieve favorable outcomes on both sides by using the China Model. Overall, it is less likely that China will adopt the EU ICJ and the discussion over the investor-state dispute settlement mechanism is sure to be the top priority of the negotiation. With the enormous investment of EU member states within China's border as well as China's increasing investment in those states, China should pay more attention to its interests as a big player of the two-way investment[94] and strike a balance between China's interests arising from the absorption of EU's investment and those arising from its investment in the EU. In this sense, China would be better off to consider adopting or perfecting the effective part of the transformation of the EU ICS. However, due to the suspension of China-US

[94] For a long time, the member States of the EU have made vast investment in China. According to the statistics from 2013-2016 (only those of the ten countries or regions that China absorbs the most investment from), in 2013, China absorbed capital inflows of 5.18 billion US dollars from 4 EU member States — 2.10 billion from Germany, 1.28 billion from the Netherlands, 1.40 billion from the UK and 762 million from France. In 2014, China absorbed capital inflows of 3.86 billion US dollars from 4 EU member States — 2.07 billion from Germany, 1.35 billion from the UK, 710 million from France and 640 million from the Netherlands. In 2015, China absorbed capital inflows of 3.86 billion US dollars from 3 EU member States — 1.56 billion from Germany, 1.22 billion from France, and 1.08 billion from the UK. In 2016, China absorbed capital inflows of 6.31 billion US dollars from 3 EU member States — 2.71 billion from Germany, 2.21 billion from the UK, and 1.39 billion from Luxembourg. *See* Commercial Data Center, available at <http://data.mofcom.gov.cn/lymz/topten.shtml> (accessed 19 December 2017). If other EU members were taken into account, the amount of the investment from EU member States would be considerably more. In recent years China has made rapidly increasing outbound investment in EU. In 2016 the amount of the investment in 28 EU member States grew up to 9.99 billion US dollars, rising by 82.4% on the corresponding period of 2015. In spite of this, by the end of 2016, the amount of China's stock of FDI amounted to 69.84 billion US dollars, which was only 5.14% of China's overall stock of FDI in that period. For more details, see *2016 Statistical Bulletin of China's Outward Foreign Direct Investment*, China Statistics Press, at 4-20.

BIT negotiations, both EU and China are eager to reach mutual consent in BIT negotiations. In this way, China may incorporate more features of EU ICS in the dispute settlement clause, but in any event, China must secure its key interests. In addition to China-EU BIT negotiations, China also needs to develop the "China Model".

1. Improvement of the Mechanism of Selecting the Third-party Members of the Tribunal of First Instance

Under the EU ICS mechanism, one third of the members of both the Tribunal of First Instance and the Appeal Tribunal shall not be nationals of either disputing party. The chairman of the division of the Tribunal shall be selected from the third-party member list. Although the current EU ICS mechanism made no specific stipulation as to whether the opinion of the chairman or the majority opinion shall prevail, the selection of the third-party members undoubtedly has a bearing on the result of a case. When selecting the third-party members, we should first preclude those who hold dual nationalities both of an EU member state and a non-EU state. Moreover, China should not be constrained by the traditional North-South division and should stop the practice of selecting members mostly from developing countries. As China has its special interests as a big bloc engaging in two-way investment, experts selected from developing countries as third-party members do not necessarily represent China's interests. In fact, geographic factors may yield better representative effects in practice than factors of whether the third-party members come from a developing or a developed country. That is to say, China may be better off selecting the third-party members from diverse areas like Africa, Oceania and South America.

2. Determination of the Respondent and Guaranteeing its Solvency

Under the EU ICS mechanism, EU shall determine whether EU or a specific member state will become the respondent in the dispute settlement, primarily depending on who conducted the measures identified in the claimant's notice. However, in the event that EU loses a case in which EU acts as the respondent, it would give rise to the problem of recognition and enforcement of the arbitration award since EU is neither a contracting party of *the Washington Convention* nor that of the *New York Convention*. Amending the two conventions and extending their application to non-sovereign entities like EU wouldn't be practical. A feasible method is to establish a mutual recognition and enforcement mechanism, thereby requiring EU to assume its obligations. Meanwhile, EU shall undertake joint or at least partial

responsibilities in cases where a certain member state is the respondent and could not afford the compensation.

3. Preclusion and Preservation of the Application of the EU ICS

The U.S. BITs and 2012 China-Canada BIT are precedents of explicitly excluding finance, tax and sensitive issues from the application of the EU ICS. At this point, China shall refer to the provisions in the TPP (then concluded as CPTPP), which excludes explicitly some aspects including: (i) "an act or fact that took place or a situation that ceased to exist before the date of entry into force"(Article 9.2.3); (ii) public debt (Annex 9-G); (iii) pre-establishment investment review of results of host states (Annex 9-H); (iv) Malaysian reservation for breaching a government procurement contract with a covered investment, below the specified contract value, for a period of three years after the date of entry into force of this Agreement for Malaysia (Annex 9-K); (v) the most-favored-nation provision shall not be extended to dispute settlement (Article 9.5); and (vi) no claim shall be submitted to arbitration if more than three years and six months have elapsed from the date on which the claimant first acquired (Article 9.21). The reservations from the application of the ISDS mechanism are systematic and definite for adopting in "China Model".

B. The In-between "China Mode" that China May Lead

In the light of the multiple defects of the ISDS mechanism and China's key interests both in absorbing FDI and protecting OFDI, China shall add some Chinese elements into the development of the current ISDS mechanism, thereby better protecting the interests of Chinese investors and Chinese government. More specifically, China may take measures as follows:

1. Change from hinging on the ISDS mechanism to properly combining the ISDS and the SSDS mechanism

Though many previous BITs included both the ISDS and the SSDS mechanism[95] simultaneously, there exists a lacuna in international investment

[95] The SSDS mechanism is primarily aimed at the application and interpretation of the treaty. For example, Art. 14 of China-Singapore BIT states "Any dispute between the Contracting Parties concerning the interpretation or application of this Agreement shall, as far as possible, be settled through diplomatic channels." And Art. 15 of 2012 China-Canada BIT has the same provision as that of 1985 China-Singapore BIT and states "1. Any dispute between the Contracting Parties concerning the interpretation or application of this Agreement shall, as far as possible, be settled by consultation through diplomatic channels".

law as to whether their relationship is primary-subsidiary, parallel, mutually exclusive, or complementary. In fact, the burden of harmonizing the two mechanisms fell on the interpreters of the treaties.[96] China's BITs have the similar features. In practice, compared to the rapid developments of the ISDS mechanism and heated debate on the legitimacy crisis or the future of the ISDS, by far the SSDS mechanism has merely been employed in three cases arising from BITs including *Peru* v. *Chile*, *Italy* v. *Cuba* and *Ecuador* v. *United States*,[97] which leads to the SSDS mechanism being nearly shelved and put away. The three cases basically interpret the reasons for SSDS proceedings as follows: (i) declaratory relief leads to SSDS, in *Peru* v. *Chile*, the Peruvian government invoked the SSDS mechanism as the legal resort to block a proceeding ISDS case brought by a Chilean investor. After the SSDS tribunal denied the claim for declaratory relief, the Peruvian government terminated all of proceedings soon; (ii) The host state exercised the power of diplomatic protection, which triggered the SSDS mechanism. In *Italy* v. *Cuba*, the Italian government invoked Article 10 of Italy-Cuba BIT to submit the claim to ad hoc arbitration to support Italian investors' allegations and to exercise diplomatic protection.[98] Finally, neither the claims brought by Italy nor the counter-claim brought by Cuba was denied; (iii) the SSDS mechanism arising from the interpretation for abstract and obscure provisions. In *Ecuador* v. *United States* case, the Ecuadorian government was dissatisfied with the ISDS tribunal's interpretation concerning Article 2.7 of Ecuador-U.S. BIT. The few SSDS cases may owe to the dilemma that states are not willing to bear the risk of submitting important disputes to the SSDS mechanism or are willing to go through the complicated process of submitting disputes that are irrelevant to the SSDS mechanism. Due to more criticism on the current ISDS mechanism, some states such as Bolivia, Venezuela and Ecuador denounced the *Washington Convention*, which increases the possibility to turn to the SSDS mechanism. Furthermore, the adoption of the SSDS may lead to benefits in some aspects, including but may be not limited to, better enforcement of the ISDS; including the investment disputes excluded from the ISDS; securing host states' right to commence the dispute settlement mechanism against foreign investors; providing other forms of remedies besides the money compensation under the ISDS mechanism; and intervening those disputes not suitable for the ISDS mechanism.

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[96] *See* Zhu-Ming Xin, "A Mechanism in Oblivion: Study on the Procedure of the State-State Investment Dispute Settlement", Chinese Review of International Law, 2016(5), at 121.

[97] *See* Jarrod Wong, "The Subversion of State-to-State Investment Treaty Arbitration", Columbia Journal of International Law, 53(1), 2014, at 21-22.

[98] *Italian Republic* v. *Republic of* Cuba, Ad Hoc Arbitral Tribunal, Interim Award, 15 March 2005, para 30.

In the process of the China-EU BIT negotiation, the Chinese government may consider defining the relationship between the ISDS and the SSDS as mutually exclusive or complementary and broadening the scope of the SSDS mechanism to include issues like environment, labor, taxation, public health, and financial prudence, thereby protecting the right to regulate of the Chinese government.

2. Appropriately narrow the scope of the application of the ISDS mechanism

Just as the introduction in Section IV (A), the whole process of China's attitude to the ISDS mechanism can be summarized as "overall restricted—overall openness—overall openness with partial restraints". Taking the China-Canada BIT as the example, the decisions made by a contracting state with respect to whether or not to initially approve an investment that is subject to review or permit an investment that is subject to national security review is excluded from the coverage of ISDS mechanism.[99] In this respect, China should learn from the texts of the 2004 US Model BIT, the 2012 US Model BIT as well as the TPP, and exclude disputes arising from environment, labor, taxation, public health, financial prudence and national security review from the application of the ISDS mechanism. Furthermore, China should also make clear in future agreements that the dispute settlement clauses shall not apply to the most-favored nation treatment.[100]

3. Establish an ISDS mechanism led by China

China's outbound foreign investment has been soaring, especially the investment made in the countries along the "One Belt One Road Initiative" , although the stability of the investment environment of many of those countries is still far from satisfactory. In this context, China is actively seeking an effective ISDS mechanism and has already put it into practice. First of all, on 26 November 2016, the Shenzhen Court of International Arbitration (hereinafter "SCIA") published its *2016 SCIA Arbitration Rules*. Pursuant to Article 2(2) of the *2016 SCIA Arbitration Rules*, the SCIA can accept the ISDS arbitration cases. In order to avoid direct conflicts with the current

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[99] 2012 China-Canada BIT, Art. 34.

[100] In BITs signed recently such as the 2008 China-Colombia BIT, the 2011 China-Uzbekistan BIT and the 2012 China-Canada BIT, it has been made clear that the dispute settlement clauses do not apply to the most-favoured nation treatment. However, almost all the BITs signed by China in earlier phase didn't explicitly excluded the most-favoured nation treatment from the scope of the application of dispute settlement.

1994 Arbitration Rules of the People's Republic of China,[101] its supplementary rules, i.e., *the Guidelines for the Administration of Arbitration under the UNCITRAL Arbitration Rules*, explicitly stated in Article 3 that where the parties have agreed on the place of arbitration, the parties' agreement shall prevail; where the parties have not agreed on the place of arbitration, unless otherwise determined by the arbitral tribunal, the place of arbitration shall be Hong Kong.[102] Second, on 21 September 2017, China International Economic and Trade Arbitration Commission released its *Arbitration Rules for International Investment Disputes* (hereinafter "*CIETAC Arbitration Rules*").[103] Pursuant to Article 2 of the *CIETAC Arbitration Rules*, the CIETAC has jurisdiction over investor-state disputes based on a contract, treaty, applicable law or regulation, or other type of documents. To avoid unnecessary conflicts, Article 3(5) of the *CIETAC Arbitration Rules* expressly stated that its application did not preclude the application of mandatory legal norms. Moreover, it also put emphasis on the combination of mediation and arbitration and borrowed some advanced ideas and practices at the international level in respect of the name list of arbitrators,[104] public hearings,[105] publicity of information,[106] place of arbitration, jurisdiction of the tribunal, consolidation of arbitration, third-party funding as well as the transparency of the arbitration procedures. Furthermore, it specified that the tribunal shall issue the final award within 6 months from the conclusion of the hearing, which is markedly shorter than the period of the ISDS cases.

Objectively speaking, however, the endeavors made by the SCIA and the CIETAC are more like declarations than practices of real value. Even if we put aside the conflicts between the two mechanisms and the current *1994*

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[101] Art. 2 of the *1994 Arbitration Rule of the People's Republic of China* provided that "Disputes over contracts and disputes over property rights and interests between citizens, legal persons and other organizations as equal subjects of law may be submitted to arbitration."

[102] Pursuant to Art. 3(5) of the *SCIA Arbitration Rules*, where the parties submit their dispute referred to under Art. 2, Paragraph 2 of the Rules to the SCIA for arbitration, the SCIA shall administer the case in accordance with the *UNCITRAL Arbitration Rules* and the *SCIA Guidelines for the Administration of Arbitration under the UNCITRAL Arbitration Rules*.

[103] The *CIETAC Arbitration Rules* entered into effect as from 1 October 2017.

[104] The establishment of name list of professional arbitrators conforms to the Chinese arbitration system which has the tradition of setting up name lists of arbitrators, which made the *CIETAC Arbitration Rules* more inclusive. It reflected the features of internationalization and meanwhile fulfilled the realistic needs of China's investment arbitration.

[105] Pursuant to Art. 32 of the *CIETAC Arbitration Rules*, all hearings are to be open to the public unless the parties agree or the tribunal decides otherwise. If a party uses confidential or other protected information, the party shall give notice to the tribunal in advance. The tribunal shall take appropriate measures to protect the information from being released.

[106] Pursuant to Art. 55 of the *CIETAC Arbitration Rules*, information relating to the arbitration shall be publicly disclosed by the CIETAC unless the parties agree otherwise, except the confidential and other protected information.

Arbitration Rules, the submission of the ISDS cases to the SCIA and the CIETAC has no obvious advantage other than the low cost of arbitration.[107] Worse still, it remains unsettled whether the SCIA or the CIETAC can hear cases brought by foreign investors against the Chinese government. Suppose that such a case was heard and decided by the SCIA or the CIETA, what if the Chinese government did not voluntarily fulfill its obligations under the awards? In such event, the award could not be defined as a "foreign arbitration award" under the *New York Convention* since it was merely a domestic award, not to mention that pursuant to the judicial interpretation of the Supreme People's Court, China expressly excluded the investor-state investment arbitration from the scope of recognition and enforcement of arbitration awards when it joined the *New York Convention*.[108] In fact, even the SCC has never accepted any ISDS case brought against the Swedish government, which may be attributed to the limitation of an arbitration institution set up within the border of a country. Suppose that a foreign investor or a Chinese investor brings before the SCIA or CIETAC a case against the government of a third country, if the host government, i.e. the respondent invokes China's judicial interpretation in the *Democratic Republic of the Congo and Ors* v. *FG Hemisphere Associates LLC* (citation: Reported at (2011) 14 HKCFAR 395) in which China adopted the principle of absolute immunity, it would pose a direct challenge to the jurisdiction of the tribunal. Moreover, the acceptance of the ISDS cases by the SCIA and the CIETAC have already exceeded the scope of arbitrated disputes under the *1994 Arbitration Rules*. Therefore, the SCIA or the CIETAC might encounter various problems when putting the rules and ideas into practice.

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[107] Pursuant to Appendix (Schedule of Arbitration Fees and Costs) of the *Guidelines for the Administration of Arbitration under the UNCITRAL Arbitration Rules*, the registration fee shall be RMB 5,000 Yuan. The fee of appointing 3 arbitrators shall be no more than RMB 18,000 Yuan. The amount of each decision on the challenge of arbitrator(s) shall be RMB 2,000 Yuan. The SCIA shall charge a financial management fee, being 0.1% of the total amount of fees in custody of the SCIA. The minimum financial management fee chargeable shall be RMB 1,000 Yuan, and shall be capped at a maximum of RMB 100,000 Yuan. According to the 2017 *CIETAC International Investment Dispute Arbitration Fees Schedule*, the arbitration fees include the registration fee (RMB 25,000 Yuan), institution management fee (the excessive part shall be multiplied by a diminishing percentage, at the minimum of RMB 24,000 Yuan and maximum of RMB 420,900 Yuan), and remuneration and fees of arbitrators (the excessive part shall be multiplied by a diminishing percentage, at the minimum of RMB 6,000 Yuan and maximum of RMB 10 million Yuan).

[108] Pursuant to Art. 2 of the *Notice about the Implementation of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards China Joined* [Law (Economic) Issued (1987) No. 5] which was issued by the Supreme People's Court on 10 April 1987, the Convention merely applies to the disputes arising from contractual or non-contractual relationship within Chinese legal system and expressly excluded the disputes between investors and host governments.

4. Integration of other alternatives into the "one-stop" dispute settlement

Although it has been proved that the ISDS mechanism is effective in protecting the interests of investors, China should seek an ISDS mechanism that meets its special needs in future when concluding international economic and trade agreements. Meanwhile, China should also pay attention to the application of other methods of dispute settlement such as consultation and negotiation, thus avoiding the huge risks that the ISDS mechanism might pose to a host government's right to regulate or even the sovereignty of the country.

On 5 December 2018, the Supreme People's Court of China issued three documents including *Notice on Determining the First International Commercial Arbitration and Mediation Agencies Incorporated into the "One-Stop" International Commercial Disputes Diversification Mechanism* (henceforth "Notice"), *Procedural Rules of the International Commercial Court of the Supreme People's Court (Provisional)*(henceforth "Procedural Rules') *and Working Rules of the International Commercial Expert Committee of the Supreme People's Court (Provisional)* (henceforth "Working Rules"), which highlighted that the "one-stop" international commercial dispute settlement diversification mechanism for litigation, arbitration and mediation has been officially completed and entered the operational phase. According to the Notice, the five international commercial arbitration and two mediation agencies, including CIETAC, SCIA, Shanghai International Economic and Trade Arbitration Commission, Beijing Arbitration Commission, China Maritime Arbitration Commission, as well as China International Trade Promotion Council Mediation Center and Shanghai Economic and Trade Commercial Mediation Center are firstly incorporated into the "one-stop" international commercial dispute settlement diversification mechanism. In addition, Procedural Rules and Working Rules stipulate the acceptance, delivery, pre-trial mediation, case hearing, executing, and supporting to resolve disputes by arbitration, etc. and refine the functions and compositions of International Commercial Experts Committee, the qualifications, responsibilities and duties of experts, as well as mediation and consultation mechanism of experts. Integration of mediation, conciliation, consultation and other alternative resolution may lead to significant contributions to the ISDS reform.

C. Improvements in Substantive Rules

Many states currently feel that the ISDS mechanism is fundamentally incompatible with inclusive economic growth and sustainable development. To some extent, the problems in the current ISDS mechanism are profound and the ISDS mechanism is itself contributing to inequality, and to undermining the rule of law. It is clear that the ICS has come about due to the criticism levelled at the investment arbitration in recent years. However, the ICS proposal is an ambitious project just like a rabbit eager to win the race, with little regard for thoroughly going through all the necessary steps in sequence.[109] In our opinion, all of the proposals by now have no great contributions to the ISDS reform is owed to the fact that the ISDS mechanism is based on the current investment law system. The current ISDS reform cannot be contributable because IIAs protect the interests of foreign investors rather than establish a good balance between foreign investors and host government and the framework of international investment law is highly fragmented. By the end of 2017, there were 3,322 IIAs (2,946 BITs and 376 TIPs), of which 2,638 IIAs were in force at the year end.[110] In addition, in the past 50 years, the legal basis to submit a dispute to the ISDS mechanism has been fundamentally changed. When the founders of the *Washington Convention* drafted the ISDS mechanism in 1960s, investment contracts were the primary sources of "consent" required in Article 25 of the *Washington Convention*,[111] which was equivalent to host states exercisinge the review power on "case-by-case" basis. The first BIT with the ISDS provision was concluded between Netherlands and Indonesia in 1968, and even after then, there still had no ISDS cases arising from a BIT until *Asian Agricultural Products Ltd.* v. *Republic of Sri Lanka*[112] case (U.K.-Sri Lanka BIT) which followed the rapid development of ISDS cases based on BITs. Compared to the consent under investment contracts, all of investors with the nationality of the other contracting state in the BIT can invoke the BIT to invoke the ISDS mechanism against the host state, which exceeded the reasonable expectations of the drafters of the *Washington Convention*. Therefore the ISDS reform shall not be limited to

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[109] Stephan Wilske, Raeesa Rawal and Geetanjali Sharma, "The Emperor's New Clothes: Should India Marvel at the EU's New Proposed Investment Court System", Indian Journal of Arbitration Law, 6(2), 2018, at 95.

[110] UNCTAD, World Investment Report 2018, New York and Geneva: United Nations, 2018, at 88.

[111] Art. 25 of the Washington Convention states "1. The jurisdiction of the Centre shall extend to any legal dispute arising directly out of an investment, between a Contracting State (or any constituent subdivision or agency of a Contracting State designated to the Centre by that State) and a national of another Contracting State, which the parties to the dispute consent in writing to submit to the Centre. When the parties have given their consent, no party may withdraw its consent unilaterally."

[112] *Asian Agricultural Products Ltd.* v. *Republic of Sri Lanka*, ICSID Case No. ARB/87/3.

procedural issues but must extend to the substantive issues, including but not limited to adopting sustainable development, public interests concerns, essential security interests and etc. into the new generation IIAs.

VI. Conclusion

Ernest-Ulrich Petersmann, the renowned scholar in international and European law, once said, "*A characteristic feature of all civilized societies is the need for rules and procedures for the peaceful settlement of disputes over the interpretation and application of rules*."[113] If the law fails to address the new issues arising from social and economic development, people will no longer rely on the law or employ it in social organization.[114] While it is important to apply the laws and rules rightfully when conducting procedural regulation or making substantive awards, it is also of crucial importance to balance the interests of different parties within the laws and rules. There is no doubt that the architects of the ISDS mechanism made some efforts pursuing such an aim, and in practice, the current ISDS mechanism has provided a comparatively efficient way to resolve investment disputes. However, as time elapses, the purpose and the aim of the international investment law have gone through substantial changes. As noted by the *International Investment Guidelines* issued at the 2016 Group of 20 (G-20) Hangzhou Summit, the international investment policies should promote inclusive economic growth as well as sustainable development. Some measures that could fairly and appropriately address the disputes in the past now seem to fall short of the needs if we are to achieve the sustainable development of the international investment agreements. Nevertheless, it would be impractical and disproportionate to give up the whole ISDS mechanism because of the several problems that have emerged. Both the EU ICS mechanism and the ISDS mechanism to be reformed by China should take full advantage of the current situations as two late-movers and create a dispute settlement mechanism that can more fairly and appropriately address investment disputes and better guarantee the sustainable development of investment.

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[113] *See* Ernst-Ulrich Petersmann, "The Dispute Settlement System of the World Trade Organization and the Evolution of the GATT Dispute Settlement System since 1948", Common Market Law Review, 31(6), 1984, at 1157. Cited from Zhao-Wei Tian, Study on GATT/WTO Dispute Settlement Mechanism, Chinese Journal of Law, 1997(3), at 53.

[114] *See* Michael Faure and Song Ying, *China and International Environmental Liability: Legal Remedies for Transboundary Pollution*, Cheltenham and Northampton: Edward Elgar, 2008, at 300.