# The Developing Trend of the World ISDS Mechanism: Echoes from China and the Approaches to Be Adopted

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**Abstract** *Due to the fact that the International Centre for Settlement of Investment Disputes ["**ICSID**"] has been sharply criticized by its member countries in recent years, the ICSID rules were amended through a process of several rounds. Conventionally, the US has always been the global leader in using the Investor-state dispute settlement ["**ISDS**"] mechanism since its establishment. Meanwhile, the other two economic giants of the world, China and the European Union ["**the EU**"], have their own plans. While the EU has advocated establishing an International Investment Court during the negotiation of the Transatlantic Trade and Investment Partnership ["**the TTIP**"] with the US, China is in the process of constructing the Belt & Road Dispute Settlement Mechanism. If the EU and China succeed, it will lead to a triple-pillared world ISDS in the future. In order to make its ISDS mechanism more competitive, China has taken several substantial steps, including amending its domestic laws and regulations, modernizing its Bilateral Investment Treaties ["**BITs**"], promulgating new arbitration rules, etc. This article will provide a systemic introduction and analysis of these approaches adopted by China and comment on the way forward.*

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## INTRODUCTION

Investor-State Dispute Settlement ("**ISDS**") mechanism is usually defined as a mechanism that allows private investors to take legal actions against a foreign government if the investors believe that the foreign government's behaviors have infringed their rights within that country.

In an investor-State dispute settlement, the two parties involved are quite imbalanced: the claimant is a private investor and the respondent is a sovereign State. In the relationship between investors and States, the private investors are subordinate to the powers of government, and are deemed to be more vulnerable. As a result, the traditional ISDS mechanism was designed with a bias towards protection of investors. In recent years, however, the International Centre for Settlement of Investment Disputes ["**ICSID**"] has been criticized by its member States as an "investor- friendly" and "State-hostile" mechanism, and several member States even denounced the ICSID Convention. Against this background, The United Nations Conference on Trade and Development ["**UNCTAD**"] launched several rounds of amendments of the ICSID Arbitration Rules. The US, the European Union ["**EU**"], and China all participated in the amendment process very actively, forwarding their own opinions.

In this article, the author explains the position of China, illustrates the developing trend of the world ISDS mechanism, and introduces the measures China has taken and the ones that are to be taken in the near future:

Part I provides a brief introduction of the world ISDS mechanism from the perspective of history, notably, the history of ICSID. Based on the analysis of the relationship between investors and States, the author analyzes the underlying reasons for the deficiencies in the ICSID mechanism, and the legitimacy crisis of the ICSID.

Part II focuses on the dramatic changes of ISDS clauses in several newly signed investment treaties. The author highlights the divergence between the main countries reflected in different investment treaties, such as TTIP, CPTPP, and USMCA.

Part III first analyzes Chinese traditional attitudes towards the ICSID, then summarizes its experiences from its ratification of ICSID Convention. After providing a general overview of the cases that China has been involved in, the author focuses on a typical case registered recently against China, and comments on the existing problems as reflected in this case.

Part IV focuses on the approaches that China has adopted and will adopt, including the approval of 2019 PRC Foreign Investment Law, promulgation of China International Economic and Trade Arbitration Commission Arbitration Rules ["CIETAC Arbitration Rules"], and the future amendment of Chinese Bilateral Investment Treaty ["**BITs**"] regime.

## I. Brief Background of the World ISDS Mechanism and its development prospects

### A. World ISDS Mechanism in the Pre-ICSID Era

At the very beginning of the proliferation of cross-border capital flow, there did not exist a legal mechanism specifically designed for the Investor-State Dispute Settlement. As a result, investor-claimants had to resort to the only mechanism available under the international law system at that time, i.e., "State-State" dispute resolution mechanism. "State-State" dispute resolution mechanism came into being in the late 18th century, and originates from "Jay Treaty" concluded in 1794 by the UK and the United States.[1] However, "State-State" dispute resolution mechanism proved unfit to be employed in settling the "investor-State" disputes due to several reasons. *First*, under such a mechanism, investors who deemed themselves infringed by the host states had no independent rights to claim for damages; instead, they had to resort to their home country, and only upon the consent of their home country, the dispute could be brought to international tribunals, most notably, International Court of Justice ("**ICJ**"). *Secondly*, this highly political means proved to be inefficient, slow and cumbersome in settling the "investor-State" disputes, due to the strict procedural and substantial restrictions, such as "exhaustion of local remedies" and "inherently closely-tied-nationalities". As a result, a new and efficient ISDS mechanism was urgently needed.

### B. Modern ISDS Mechanism symbolized by the ICSID Convention

After World War II, the western developed countries kept seeking to establish a set of better protection standards for their overseas investments in developing countries. To achieve this goal, the Organization for Economic Co-operation and Development (OECD) countries carried out several

[1] "Jay Treaty" was concluded by the US and Great Britain on November 19, 1794. The full name of the treaty is "Treaty of Amity, Commerce, and Navigation of 1794 between Great Britain and the United States". Pursuant to the treaty, mixed commission was created to settle the disputes between two disputing countries.

negotiations on investment protection standards, however, they all ended in failure. Later, World Bank Director General Aron Broches suggested that the issues of protection standards should be set aside, and a set of worldwide uniform "investor-State" dispute settlement procedural rules be established in its lieu. This suggestion was adopted, and the most influential "investor-State" dispute settlement organ, ICSID was subsequently established in 1966 by ICSID Convention[2], which symbolized the birth of the new ISDS mechanism.

Under the ICSID rules, investors could bring their investment disputes to ICSID for arbitration upon their own decisions. ICSID's unblocking availability to investors contributes to remove obstacles of investor-State disputes settlement and helps to promote international investment by providing legal predictability in the investor-state dispute resolution. ICSID is appraised as an independent, depoliticized, and effective arbitration institution. It is also available for State-State disputes under investment treaties and free trade agreements. In addition, it also administers arbitration cases under other rules, such as the UNCITRAL Arbitration Rules and *ad hoc* investor-State and State-State cases.[3]

The great achievement of ICSID could be seen from the number of the cases that have been registered and have successfully concluded since its establishment. As of December 31, 2018, ICSID had registered 706 cases under the ICSID Convention and Additional Facility Rules,[4] and 463 cases were concluded.[5]

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[2] The full name of the ICSID is "International Centre for Settlement of Investment Disputes"; and the full name of the ICSID Convention is "Convention on the Settlement of Investment Disputes between States and Nationals of other States", which was signed in 1965. According to the newest update, ICSID counted 154 contracting States to the ICSID Convention. Website of International Center for Settlement of Disputes, Database of ICSID Member States, <https://icsid.worldbank.org/en/Pages/about/Database-of-Member-States.aspx> (accessed March 22, 2019).

[3] Website of International Center for Settlement of Disputes, Non-ICSID Arbitration, <https://icsid.worldbank.org/en/Pages/process/Non-ICSID-Arbitration.aspx> (accessed January 18, 2019).

[4] Website of International Center for Settlement of Disputes, The ICSID Caseload – Statistics (Issue 2019-1), <https://icsid.worldbank.org/en/Documents/resources/ICSID%20Web%20Stats%202019-1 (English).pdf> (accessed March 22, 2019), at 7.

[5] Website of International Center for Settlement of Disputes, concluded cases, <https://icsid.worldbank.org/en/Pages/cases/ConcludedCases.aspx?status=c> (accessed March 25, 2019).

## C. The Legitimacy Crisis of ICSID and the Trend of the Future Development

### 1. Criticisms targeting the ICSID Mechanism

Although the ICSID has been playing exclusively important role in investor-State dispute settlement since its establishment, recent years saw severe criticisms targeting the ICSID mechanism despite of its great achievements.

*First*, ICSID mechanism was criticized to be an "investor-friendly" and "State-hostile" mechanism with a tendency of over-protecting the investors' interests. It is not strange that such criticism was raised, as in fact, from its birth, ICSID was designed to provide a quick pass for investors into the ISDS procedures and to better protect the capital-exporting-country investors' property rights. This could be verified from the fact that the awards upholding the investors' claims in part or in full amounted to 30.6% among all the cases concluded by ICSID.[6]

*Secondly*, the procedural deficiencies of ICSID were also criticized. The most frequently criticisms are that arbitration procedures include are lack of transparency; the independence and impartiality of the arbitrators cannot be guaranteed; and non-availablity availability of an appellate review.

*Thirdly*, ICSID was criticized for being overly commercial and infringing the sovereign States' regulatory power and not adequately considering public interests. As indicated by the statistics published by ICSID, by the end of 2018, nearly 60% of the cases administered by ICSID concentrated on several important industrial sectors of a country's national economy, such as gas, oil, and electricity.[7] Since these fields are traditionally subject to a State's exclusive regulatory power, it is not strange that host states felt its sovereign powers severely challenged.

### 2. Regulatory Chill and Legitimacy Crisis of ICISD

Latin American countries were the first victims who suffered greatly from investors' suits in ICSID. Among these Latin American countries, Argentina is an extreme example of this wave of investment litigations. After CMS,

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[6] Website of International Center for Settlement of Disputes, The ICSID Caseload – Statistics (Issue 2019-1), <https://icsid.worldbank.org/en/Documents/resources/ICSID%20Web%20Stats%202019-1 (English).pdf> (accessed March 22, 2019), at 14.

[7] According to The ICSID Caseload – Statistics (Issue 2019-1), cases in the sector of Oil, Gas, & Mining amount to 24%, cases in the sector of electric power & other energy amount to 17%, cases in the sector of construction amount to 8%, cases in the sector of transportation amount to 9%. <https://icsid.worldbank.org/en/Documents/resources/ICSID%20Web%20Stats%202019-1 (English).pdf> (accessed March 22, 2019), at 12.

an American investor, filed the ICSID suit against Argentina in 2001[8], 24 suits were registered against Argentina by the foreign investors to ICSID for Arbitration in the following 3 years from 2001 to 2003.[9] Till date, 54 suits have been registered against Argentina.[10] As *Randal C. Archibold* pointed out in his article "*First the Gold Rush, Then the Lawyers*"- in the ICSID, "Latin American governments make up 9 percent of the court's 155 members but about 55 percent of the cases."[11] Additionally, the compensation amount claimed by the investors is usually excessive. Take the CMS case for example, CMS claimed for 2611 million dollars and was awarded the compensation of 1332 million dollars.[12]

Several years later, even developed countries became vulnerable to large claims. Some developed countries, including the US, Canada, Germany have also suffered large claims brought by the foreign investors.[13] For example, there are two typical ICSID cases - *Vattenfall* v. *Germany (I)*[14] and *Eli Lilly* v. *Canada*[15].

In 2009, Vattenfall, a Swedish energy company engaging in the construction of a coal fired power plant in Hamburg, brought a suit against Germany in 2009. Vattenfall alleged that the quality controls on the waste waters imposed by the Hamburg environmental authority made its investment project unviable, and claimed EUR 1.4 billion. The case was eventually settled when the City of Hamburg agreed to lower the environmental requirements previously set. The other example is *Eli Lilly* v. *Canada*. In this case, Claimant asserts claims arising from the invalidation of its Canadian patents protecting the drugs marketed in Canada as "Strattera" and "Zyprexa". The Canadian courts invalidated these two patents in 2010 and 2011 under

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8 *CMS Gas Transmission Co.* v. *Argentine Republic*, (ICSID Case No. ARB/01/8).

9 Searched by respondent nationalities on the website of International Centre for Investment Dispute Settlement, <https://icsid.worldbank.org/en/Pages/cases/AdvancedSearch.aspx> (accessed January 19, 2019).

10 Searched by respondent nationalities on the website of International Centre for Investment Dispute Settlement, <https://icsid.worldbank.org/en/Pages/cases/AdvancedSearch.aspx> (accessed March 25, 2019).

11 Julia G. Brown, "International Investment Agreements: Regulatory Chill in the Face of Litigious" Heat, 3 W. J. Legal Stud. 1, 17 (2013).

12 Website of International Center for Settlement of Disputes, Award of the *CMS Gas Transmission Co.* v. *Argentine Republic*, (ICSID Case No. ARB/01/8), <http://icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C4/DC504_En.pdf> (accessed January 19, 2019), at 27, 139.

13 There were 9 cases brought against Canada from 2002, 2 cases brought against Germany in 2009 and 2012, and 6 cases brought against the US from 1998. Searched by respondent nationalities on the website of International Centre for Investment Dispute Settlement, <https://icsid.worldbank.org/en/Pages/cases/AdvancedSearch.aspx> (accessed March 25, 2019).

14 ICSID Case No. ARB/09/6.

15 ICSID Case No. UNCT/14/2.

Canadian patent law, and claimant claimed for an amount of CDN $500 million, plus any payment arising out of its loss of patents and inability to enforce the patents.[16] Although the claimant's claim was dismissed in entirety, this is an example of challenge of the Canada's regulatory power in the field of drug patents.

Not only developing countries, but also developed countries deemed that ICSID has infringed upon their regulatory powers, and began to challenge the legitimacy of the ICISD tribunal, criticize the procedural deficiencies, and question the impartiality of the arbitrators.

## 3. Amendments of ICSID Rules Launched in Recent Years

Due to the fierce criticisms and legitimacy crisis,[17] ICSID launched 5 rounds of amendments of arbitration rules from both procedural and substantial perspectives, in order to make a better balance between the rights and obligations of the investors and States, and to keep the coherence and consistency of the arbitral awards.[18]

The most recent amendment was launched by ICSID in October 2016, focusing on these aspects: *first*, the changes are intended to modernize the rules based on case experience; *secondly*, the amendments will make the process increasingly time-and-cost-effective while maintaining due process and a balance between investors and States.[19]

In this round of amendment, ICSID advocated that member states submit amendment proposals, so as to modify and reconstruct a set of rules more acceptable by both investors and member States. 41 countries submitted their written comments and proposals for the ICSID rules amendment, including

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[16] ICSID Case No. UNCT/14/2, Final Award, <http://icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C3544/DC10133_En.pdf> (accessed March 25, 2019), at 1, at 25.

[17] Even several contracting parties denounced the ICSID Convention, including Ecuador, Bolivia. From the list of ICSID contracting Member States, the two countries cannot be found. Website of International Center for Settlement of Disputes, <https://icsid.worldbank.org/en/Pages/about/Database-of-Member-States.aspx> (accessed January 19, 2019).

[18] The procedural issues of the ISDS are mainly provided in ICSID Convention Rules of Arbitration and Additional Facility Rules. There have been four rounds of rule changes following the adoption of the rules, the last of which entered into force in April 2006. The ICSID Convention Rules and Regulations were adopted in 1967, and the Additional Facility Rules in 1978. Website of International Center for Settlement of Disputes, <https://icsid.worldbank.org/en/amendments/Pages/About/about.aspx> (accessed January 23, 2019).

[19] Website of International Center for Settlement of Disputes, About ICSID Amendments, <https://icsid.worldbank.org/en/amendments/Pages/About/about.aspx> (accessed January 23, 2019).

Australia, Canada, China, European Union and its member States, etc. Not only the member States, but also some important international organizations have contributed to the ICSID rule amendment. Notably, the ICJ has established a practice of avoiding conflict of interests of the international Judges, which will contribute to the perfection of the ICSID Rules. Mr. Abdulqawi A. Yusuf, President of ICJ, on the 73rd session of the UN General Assembly, announced that the ICJ judges will not ordinarily participate in international arbitration. In particular, they will not participate in investor-State arbitration or in commercial arbitration.[20] This is a very critical step for ICJ to limit the extrajudicial activities of ICJ Judges, which is being undertaken to guarantee the impartiality and independence of the ICJ Judges. Several ICSID member States have been calling for establishing a "Conduct Code" for the ICSID arbitrators.

## II. TRENDS IN THE ISDS MECHANISM

### A. Divergence between US and EU in the Negotiation of TTIP

The EU and US have long been important trade partners. The EU and the United States (US) economies account together for about half the entire world GDP and for nearly a third of world trade flows, and they also have the largest bilateral trade and investment relationship. They enjoy the most integrated economic relationship in the world. For the purpose of further strengthening the EU-US economic ties, the two blocks decided to initiate a free-trade agreement called Transatlantic Trade and Investment Partnership ("**TTIP**"), entered into at the EU-US Summit in Lisbon in November 2010.[21]

However, the US and EU had a big divergence of opinion on the role of the ISDS during the TTIP negotiation. While the US advocated establishment of a traditional ISDS mechanism, the EU advocated that an Investment Court should be established. On 12 November 2015, EU formally presented to the US its proposal for the establishment of the Investment Court System.[22] The

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[20] Speech by H.E. Abdulqawi A. Yusuf, President of the International Court of Justice, on the occasion of the seventy-third session of the United Nations General Assembly, see: <https://www.icj-cij.org/files/press-releases/0/000-20181025-PRE-02-00-EN.pdf> (accessed January 23, 2018), at 11,12.

[21] EU and US boost economic partnership (November 29, 2011), <http://trade.ec.europa.eu/doclib/press/index.cfm?id=757>.

[22] European Commission — Press release, EU Finalizes Proposals for Investment Protection and Court System for TTIP (November 12, 2015), <http://europa.eu/rapid/press-release_IP-15-6059_en.htm>.

final text of the TTIP[23] aims at safeguarding the right to regulate and create a court-like system with an appeal mechanism based on clearly defined rules, with qualified judges and transparent proceedings.[24] The new system would replace the existing investor-state dispute settlement (ISDS) mechanism in TTIP and in all ongoing and future EU trade and investment negotiations.[25] The idea was to establish a permanent body to decide investment disputes, moving away from the ad hoc system of investor-State dispute settlement (ISDS).[26]

## B. Dramatic Changes of ISDS Mechanism From NAFTA to USMCA

"Should ISDS exist? Is it a good thing or bad thing?" Although such questions have been frequently asked in recent years, no substantial steps were taken to remove it or impose severe limitations on it. However, the newly signed USMCA (The United States-Mexico-Canada Agreement)[27] made a dramatic change and removed the existing ISDS between member States. The North American Free Trade Agreement (NAFTA) ISDS mechanism was provided in Chapter 11 and has played very important role since NAFTA came into effect. However, it was removed between the United States and Canada, and was only maintained for certain instances between the United States and Mexico.[28] It is believed that this removal is for the benefit of Canada.[29]

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[23] Transatlantic Trade and Investment Partnership, <http://trade.ec.europa.eu/doclib/docs/2015/november/tradoc_153955.pdf> (accessed January 23, 2019).

[24] European Commission — Press release, EU Finalizes Proposals for Investment Protection and Court System for TTIP (November 12, 2015), <http://europa.eu/rapid/press-release_IP-15-6059_en.htm>.

[25] European Commission — Press release, EU Finalizes Proposals for Investment Protection and Court System for TTIP (November 12, 2015), <http://europa.eu/rapid/press-release_IP-15-6059_en.htm>.

[26] European Commission – Fact Sheet, A Future Investment Court, Brussels (December 13, 2016), <http://europa.eu/rapid/press-release_MEMO-16-4350_en.htm>.

[27] USMCA was signed on November 30, 2018. While the United States, Mexico, and Canada have concluded a new, rebalanced agreement, NAFTA currently remains in effect. The USMCA can come into effect following the completion of TPA procedures, including a Congressional vote on an implementing bill. United States-Mexico-Canada Agreement, <https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement> (accessed January 14, 2019).

[28] Art. 14.2(4) of USMCA provides: "For greater certainty, an investor may only submit a claim to arbitration under this Chapter as provided under Annex 14-C (Legacy Investment Claims and Pending Claims), Annex 14-D (Mexico-United States Investment Disputes), or Annex 14-E (Mexico-United States Investment Disputes Related to Covered Government Contracts)." <https://ustr.gov/sites/default/files/files/agreements/FTA/USMCA/Text/14_Investment.pdf> (accessed January 14, 2019), Ch. 14.

[29] See From NAFTA to USMCA Free Trade in North America, Today & Tomorrow, Understanding the Renegotiation of North American Free Trade Agreement, <https://www.livingstonintl.com/NAFTA/> (accessed January 14, 2019): "The removal of ISDS is considered more of a win for Canada than the United States as the United States

## C. Limitations imposed on ISDS Mechanism from TPP to CPTPP

CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership) is another example of dramatically changing the current ISDS mechanism. CPTPP is the successor of TPP (Trans-pacific Partnership Agreement). Despite the withdrawal of the US, CPTPP came into effect on December 30th 2018, including 11 countries.[30]

Compared with TPP, 22 provisions were suspended or otherwise changed, and one of the most important revisions was in the investment chapter. In the CPTPP investment chapter, investors' ability to litigate disputes under 'investment agreements' and 'investment authorizations'—which are used mostly for mining and oil investments—will be more limited relative to that under TPP."[31] That is to say, investors cannot bring the disputes arising from "investment agreements" and "authorizations" to arbitration, and cannot claim damages either. Like a toothless tiger, the ISDS mechanism will only function in a limited manner. During the original negotiation of TPP, the US insisted to incorporate ISDS provisions into the text of the TPP; however, this did not enjoy similar support from the other countries. After the withdrawal of US, other countries suspended the most important part of investment chapter, greatly reducing the application scope of the ISDS mechanism.

## D. The Triple-Pillared ISDS Mechanism

### 1. US-oriented ICSID

The US-oriented ICSID came into being in 1960s, and has been the leading choice for investor-State dispute resolution from its establishment. *First*, ICSID Convention covers 154 States. Thus, there is no doubt that ICSID

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Government has never had to pay damages to a foreign corporation throughout NAFTA's history. Conversely, Canada has been forced to pay damages of more than $300 million to US corporations through ISDS resolutions."

[30] CPTPP is one of the largest free trade agreements in the world, representing nearly 13.5 per cent of global GDP Matthew P. Goodman, "From TPP to CPTPP" (March 8, 2018), <https://www.csis.org/analysis/tpp-cptpp>.

CPTPP negotiations concluded on January 23, 2018. Eleven States signed the Agreement on 8 March in Santiago: Australia, Brunei Darussalam, Canada, Chile, Japan, Mexico, Malaysia, New Zealand, Peru, Singapore and Vietnam. Australia, Canada, Japan, Mexico, New Zealand, Singapore, and Vietnam have all ratified the CPTPP triggering its entry into force from December 30, 2018.

Comprehensive and Progressive Agreement for Trans-Pacific Partnership, <https://www.mfat.govt.nz/en/about-us/who-we-are/treaties/cptpp/> (accessed January 14, 2019).

[31] Matthew P. Goodman, "From TPP to CPTPP" (March 8, 2018), Centre for Strategic and International Studies <https://www.csis.org/analysis/tpp-cptpp> ((accessed July 31, 2019).)

is the most influential investor-State investment dispute resolution mechanism as indicated by its wide range of member States. *Secondly*, its leading place could also be illustrated by the number of cases administered under its regime, which totally amounted up to 706 by the end of 2018. Although other arbitration institutions, like the ICC (International Chamber of Commerce), the SCC (Arbitration Institute of Stockholm Chamber of Commerce), the LCIA (London Court of International Arbitration) also deal with arbitration cases, the amount of cases are few when compared with ICSID. In the short run, ICSID cannot be replaced or competed by other investor-State disputes resolution mechanism.

## 2. EU-oriented Investment Court

During the TTIP negotiation, EU advocated that an Investment Court should be established, and the ISDS provisions in the original TTIP text be abandoned. If successfully established, this multilateral investment court would cover 26 countries (25 EU member countries, and the United States) and play an important role in settling investment disputes arising among EU members.

As an important step, the newly signed EU-Canada Trade Agreement (CETA) and the EU-Vietnam Trade Agreement both contained a reference to the establishment of a permanent multilateral investment court, and similar references were included in all of its ongoing negotiations involving investment.[32] Take the CETA for example, the Joint Interpretative Instrument for the EU-Canada Trade Agreement (CETA) states: "The EU and Canada will work expeditiously towards the creation of the Multilateral Investment Court. It should be set up once a minimum critical mass of participants is established, and immediately replace bilateral systems such as the one in CETA, and be fully open to accession by any country that subscribes to the principles underlying the Court."[33]

## 3. China- oriented "B&R" ISDS Mechanism

2018 marks the 5th anniversary of Chinese Belt & Road Initiative. During these 5 years, China has achieved great progress in carrying out economic cooperation with the B&R partners. However, trade and investment disputes arose inevitably between China and B&R countries, and it is necessary to establish a B&R Dispute Settlement Mechanism. In January 2018, President

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[32] European Commission — Fact Sheet, A Future Investment Court, Brussels (December 13, 2016), <http://europa.eu/rapid/press-release_MEMO-16-4350_en.htm>.

[33] Website of European Commission, A Future Investment Court (December 13, 2016), <http://europa.eu/rapid/press-release_MEMO-16-4350_en.htm>.

Xi Jin-Ping presided over the second meeting of the Central Leading Group for comprehensively deepening the reform, and the "opinion on the establishment of Belt & Road dispute settlement mechanism and institution" was adopted.

By the end of 2018, China has signed Co-constructing B&R Cooperative Documents with 122 sovereign states and 29 international organizations, including cooperative agreements, understanding memorandums, strategic partnerships, etc.[34] However, the provisions of these "agreements" are of general nature, and the duties and obligations of the investors and countries, the investment disputes resolution are still to be further clarified. Even if it is established in the near future, B&R investment dispute resolution system is still an immature mechanism to be testified and perfected by the practice with time. However, it will undoubtedly contribute to the world investor-State dispute resolution.

## III. THE STATUS QUO OF CHINA PARTICIPATING ICSID ARBITRATION AND THE UNDERLYING REASONS

### A. Chinese Historical Attitudes towards ICSID Convention and Underlying Reasons

Since the establishment of People's Republic of China ("PRC") in 1949, China adhered to the principle of "Absolute State Immunity", according to which China, in any event, will not be subject to the jurisdiction of any foreign countries' courts or any international tribunals. As one PRC publicist argued in 1958, "*Since the subjects of international treaties are sovereign states, there cannot be a supra-national organ in international affairs to interpret international treaties and compel the contracting parties to accept its interpretation. Consequently, the interpreters of international treaties can only be the contracting States themselves, and the best method of settling this problem is through diplomatic negotiations.*"[35]

In such a background, China was also reluctant to be subject to the ICSID jurisdiction, as China does not accept intervention in its sovereign issues by international tribunals. Once China accepts jurisdiction of ICSID, the conduct of Chinese governments and their employees, and even the conduct of the courts will be subject to review of international tribunals according

[34] Website of Belt and Road, The List of Countries that have signed cooperative documents with China (January 14, 2019), <https://www.yidaiyilu.gov.cn/xwzx/roll/77298.htm>.

[35] Julian Ku, "China and the Future of International Adjudication", 27 Md. J. Int'l L. 154, 156 (2012).

to the rules of international law, which runs contrary to Chinese law and policies.

## B. Chinese Ratification of ICSID Convention and Notice of Jurisdiction

China signed ICISD Convention in 1990 and entered into force from 6th February 1993.[36] When submitting ratification letter to ICSID Secretariat on 7 January 1993, China sent a notification pursuant to Article 25(4) of ICISD Convention[37], intending to impose some restrictions on ICSID jurisdiction over the China-related cases. The notification reads: "*Pursuant to Article 25(4) of the Convention, the Chinese Government would only consider submitting to the jurisdiction of the ICSID disputes over compensation resulting from expropriation and nationalization.*"[38]

However, there has been a controversy over the nature of this "notice", focusing on whether it is a "reservation" of the ICSID Convention Jurisdiction Clause, or it is only a non-binding claim made by China expressing its intention to limit ICSID jurisdiction to some extent. Chinese international law Professor Chen' An held the view that "the notice was neither a binding promise to other contracting states accepting the ICSID jurisdiction, nor a reservation excluding the ICSID jurisdiction, it was just a unilateral intentional claim."[39] In my opinion, this notice is just indicative of a possibility that China would accept jurisdiction over several types of disputes mentioned in the notice. Given that, the phrase used was "consider submitting", which means China could make a decision not to accept jurisdiction, and thus it is not binding for China.

In fact, the Chinese government never invoked this "notice" to challenge the ICSID jurisdiction in the 3 ICSID cases brought against China; and this "notice" never excluded ICSID jurisdiction, even though the claim went far beyond "expropriation or nationalization compensation amount" as stated

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[36] Website of International Center for Investment Dispute Settlement, Database of ICSID contracting Members, <https://icsid.worldbank.org/en/Pages/about/Database-of-Member-States.aspx> (accessed January 18, 2019).

[37] ICSID Art. 25(4): Any Contracting State may, at the time of ratification, acceptance or approval of this Convention or at any time thereafter, notify the centre of the class or classes of disputes which it would or would not consider submitting to the jurisdiction of the centre. The Secretary General shall forthwith transmit such notification to all contracting States. Such notification shall not constitute the consent required by para (1).

[38] Website of International Center for Investment Dispute Settlement Search ICSID Member State, <https://icsid.worldbank.org/en/Pages/about/MembershipStateDetails.aspx?state=ST30> (accessed January 18, 2019).

[39] Chen'An, International Investment Arbitration- A Study of ICSID Mechanism 83 (1st edn. 2001).

in the notice. For example, in the first case against China brought by a Malaysian company, *Ekran Berhad* v. *People's Republic of China*[40], ICSID established jurisdiction over this case pursuant to Malaysia- China BIT 1988. Article 7 of the BIT provided: "the disputes over expropriation compensation amount, or other types of disputes upon mutual consent, could be submitted to ICSID Center for Arbitration".[41] And in the second case that China acted as respondent, *Ansung Housing Co, Ltd*. v. *People's Republic of China* ARB/14/25, ICSID dismissed all the claims made by the claimant pursuant to Article 9(7) of the China-Korea BIT[42], deciding that the Center "manifest lack of legal merit due to a lack of temporal jurisdiction".[43]

## C. Chinese ICSID Investor-State Dispute Settlement Practice in Recent Years

### 1. An Overview of the ICSID Cases that China was involved

Although China ratified the ICSID Convention in 1993, there was not a single case brought to ICSID relating to China until as late as 2007. The year 2007 is a benchmark for China, which while participating in the World ISDS, which saw a citizen of Hong Kong, XieYe-Shen, bring a case against Peru.[44] And till now, ICSID Cases in which China acted as Claimants amounted to 6, among which 2 cases were pending, with the residuary 4 cases being successfully concluded.[45] And on the other hand, cases in which China was sued as Respondents amounted to 3, among which 1 case is still pending,

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[40] ICSID Case No. ARB/11/15. .

[41] Mutual Encouragement and Protection Agreement between PRC Government and Malaysia Government (1988), Ministry of Commerce of the People's Republic of China Department of Treaty and Law, <http://tfs.mofcom.gov.cn/aarticle/h/at/200212/20021200058404.html> (accessed January 23, 2019).

[42] Art. 9(7) China-Korea BIT provides: [A]n investor may not make a claim pursuant to para 3 of this article if more than 3 years have elapsed from the date on which the investor first acquired, or should have first acquired, knowledge that the investor had incurred loss or damage.

[43] *Ansung Housing Co. Ltd*. v. *People's Republic of China*, ICSID Case No. ARB/14/25, Award, <http://172.28.1.2/files/30600000004D9169/icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C3885/DC10053_En.pdf> (accessed January 24, 2019), at 20.

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

[45] Concluded Cases, International Center for Investment Disputes Settlement, <https://icsid.worldbank.org/en/Pages/cases/searchcases.aspx> (accessed January 26, 2019). The four concluded cases are as following: *Tza Yap Shum* v. *Republic of Peru*, (ARB/07/6); *Standard Chartered Bank (Hong Kong) Ltd*. v. *Tanzania Electric Supply Co. Ltd*., (ARB/10/20); *Ping An Insurance (Group) Co. of China Ltd*., (ARB/12/29); *Beijing Urban Construction Group Co. Ltd*. v. *Republic of Yemen*,(ARB/14/30). The two pending cases are as following: *Standard Chartered Bank (Hong Kong) Ltd*. v. *United Republic of Tanzania*, (ARB/15/41); *Sanum Investments Ltd*. v. *Lao People's Democratic Republic*, (ADHOC/17/1).

with the other 2 cases reaching conclusion.[46] The three cases brought against China all disputed over the land use rights, which went far beyond the matters of expropriation and nationalization compensation. These cases covered a wider range of legal matters, including expropriation, arbitrary conducts of the government, breach of investment contract by the government, due process, denial of justice, etc.

## 2. A Typical ICSID Case that China acted as Respondent

*Hela Schwarz GmbH* v. *People's Republic of China* is the most recently registered ICSID case brought against China, which is also the 3rd Case in which China acted as respondent. This is a very typical case, reflecting several negative aspects in Chinese foreign investment practice that require urgent correction and improvement. This case is still in arbitration procedure, and is currently pending.

The Claimant established a wholly owned subsidiary in 1996 in China, Jinan Hela Schwarz Food Co., Ltd. ("JHSF"). In 2001, JHSF was granted the legal right to use a parcel of state-owned industrial land in Shandong Province for 50 years, i.e., until 29 July 2051. After receiving this right, JHSF built a series of buildings on the Land. However, on 11 September 2014, the Jinan Municipal Government issued a Housing Expropriation Decision to expropriate the land and the buildings. According to the Respondent, this expropriation measure was implemented as part of the Huashan area renovation project, a program aimed at improving environmental and living conditions along the river Xiaoqing.[47]

The claimant JHSF first sought a local remedy, challenging the expropriation decision through an administrative review procedure in November 2014, however rejected by Shandong Provincial Government. Afterward, the claimant brought an administrative lawsuit against the Jinan Municipal Government at the Intermediate People's Court, which issued a procedural ruling dismissing JHSF's complaint. Later this procedural ruling was upheld by the Shandong High Court in December 2016.[48]

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[46] Website of International Center for Investment Disputes Settlement, Concluded Cases, <https://icsid.worldbank.org/en/Pages/cases/searchcases.aspx> (accessed January 26, 2019). The two cases concluded including: *Ekran Berhad* v. *People's Republic of China*, (ARB/11/15); *Ansung Housing Co. Ltd.* v. *People's Republic of China*, (ARB/14/25); The one pending case was *Hela Schwarz GmbH* v. *People's Republic of China*, (ARB/17/19).

[47] *Hela Schwarz GmbH* v. *People's Republic of China*, (ICSID Case No. ARB/17/19), Procedural Order No. 2, <http://172.28.1.2/files/21650000004D7569/icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C6447/DS11402_En.pdf> (accessed January 26, 2019).

[48] *Hela Schwarz GmbH* v. *People's Republic of China*, (ICSID Case No. ARB/17/19), Procedural Order No. 2, <http://172.28.1.2/files/21650000004D7569/icsidfiles.

This case reflected some negative aspects of Chinese administrative management and judicial system. The most egregious problem in this case is the failure to comply with the due process in dealing with the disputes between foreign investors and the Chinese local government. According to the claimant, the Court did not hold a hearing or issue a substantive judgment. Rather, it issued a procedural ruling dismissing JHSF's complaint without rationale reasons.[49] This was challenged by the investor as "denial of justice".

## IV. CHINESE APPROACHES ADOPTED & TO BE ADOPTED

### A. Active Participation in the ICSID Rules Amendment

In recent years, China has demonstrated a willingness to participate in international law rule-making, which could be attributed to globalization. Cognizant of the importance of international law rules, China has changed its traditional avoidant attitude and has begun to participate in the international law rule-making much more actively, trying to shift its role from "rule-taker" to "rule-maker". In this round of ICSID rules amendment, China took an active part and fed back its comments and proposals, emphasizing on the following aspects:[50]

*First*, China proposed that in order to avoid inappropriate interpretation, Article 31 and Article 32 of the Vienna Convention on the Law of Treaties (VCLT) shall be added to the ICSID Arbitration Rule.[51] This is because China believes that once an investor-State dispute arises, legal rights and obligations of the two parties are to be established pursuant to investment treaties. Some of the investment treaty clauses are vague in expression, and are

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worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C6447/DS11402_En.pdf> (accessed January 26, 2019), at 9.

[49] *Hela Schwarz GmbH* v. *People's Republic of China*, (ICSID Case No. ARB/17/19), Procedural Order No. 2, <http://172.28.1.2/files/21650000004D7569/icsidfiles.worldbank.org/icsid/ICSIDBLOBS/OnlineAwards/C6447/DS11402_En.pdf> (accessed January 26, 2019), at 9.

[50] As an active response to the ICSID calling for State opinions, PRC Ministry of Commerce issued the draft of ICSID Rules Amendment on its website for public opinions. In view of the professional characteristic in this field, Chinese proposals and comments of the ICSID Rules amendment were mainly based on some academic institutions' and scholars' opinions. The most contributive organ is "Institute of International Law" subordinate to "Chinese Academy of Social Science". On December 28, 2018, China fed back its comments and proposals on the amendment of ICSID Rules.

[51] Website of International Center for Investment Disputes Settlement, Comments on the Proposed Amendments to the ICSID Rules Submitted by China, <https://icsid.worldbank.org/en/amendments/Documents/China_Comments_12.28.18.pdf> (accessed January 30, 2019).

vulnerable to the interpretation of the arbitrators. Only under a set of rationale interpretation rules that the consistency of awards shall be guaranteed.

*Secondly*, China proposed that any arbitrator who has made manifestly inappropriate interpretation of the legal issues or claims in an investment dispute shall not be appointed as arbitrator in any other investment dispute against the same respondent where legal issues or claims are the same as in the previous dispute.[52] This is because China believes that in order to guarantee the impartiality and fairness of the arbitration, it is necessary to establish a set of conduct rules for the ICSID arbitrators, among which avoiding the conflict of interest is the most important. Working on reciprocity, if China is sued sometime in the ICSID, it does not wish that any arbitrator who has demonstrated prejudice against China in a previous arbitration participates in the arbitration process.

*Thirdly*, China proposed that all claims must be submitted by the claimant in the request for arbitration once for all, and any new claims not raised in the Request, shall not be allowed in the Memorial and the Reply, and the Tribunal shall not have jurisdiction over such claims.[53] This is because China believes that according to the due process principle in the litigation law, the investors who brought a suit must give the defendant plenty of time for preparation to respond, and a sudden attack by a new claim should not be permitted, as the same is not fair to the defendant.

*Fourthly*, China proposed that a new definition of third-party-funding should be formed, and consequences for failure of disclosure of third party information shall be clarified as well.[54] In ICSID arbitration, third-party funding agreements are usually signed between investors and professional funding organs, who normally gain very high return if the investor wins the case. Chinese scholars suggested that the contents of such agreements be disclosed in detail, including the return rate of the funding party. If the agreement is kept secret, the investors' interests are likely to be undermined.

*Lastly*, China proposed to add a rule stating that the respondent shall not be required to disclose information involving national secrets, the disclosure of which the respondent considers contrary to its essential security.[55] This is because China believes that each state as a sovereign country, shall have the rights to refuse to disclose those national secrets that it deemed to be

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[52] *Ibid.*
[53] *Ibid.*
[54] *Ibid.*
[55] *Ibid.*

important for national security, although the information is relevant with the arbitration and requested by the investors.

## B. Endeavor to Form a Uniform Foreign Investment Law

### 1. The Old Three Main Foreign Investment Laws to be Replaced

Traditionally, Chinese foreign investment law regime was consisted of three laws, i.e., the Law of the PRC on Sino-foreign Equity Joint Ventures[56], the Law of the PRC on Wholly Foreign-owned Enterprises[57], and the Law of the PRC on Sino-foreign Cooperative Joint Ventures[58]. The three laws were issued to implement "the reform and opening-up" policy adopted in 1978, which was the benchmark for China starting to allow foreign investors to run business within the statutory limits. Afterwards, some supplementary regulations were issued, which functioned together with the three main laws.[59]

However, China has been dramatically changed during these 40 years, and the three laws cannot satisfy the rapid development of Chinese economy and must be replaced. For example, the entry approval of foreign invested enterprises (FIEs) is on "case-by-case" basis, which is low-efficient and cumbersome; the investment promotion measures are not attractive enough; the protection of intellectual property rights is not perfect; and the protection of the investors' legitimate rights is vague in provisions; and some important issues, such as national security issue was not provided in the old foreign investment law regime.

From 2015, China started to draft on the new investment law, and based on the two Drafts issued in 2015 and 2018[60], the "PRC Foreign Investment

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[56] The Law of PRC on Equity Joint Ventures was adopted by the 3rd Session of the 7th National People's Congress on July 1, 1979, and came into force on July 8, 1979.

[57] The Law of PRC on Wholly Foreign-Owned Joint Ventures was adopted by the 4th Session of the 6th National People's Congress on April 12, 1986.

[58] The Law of PRC on Cooperative Joint Ventures was adopted by the 1st Session of the 7th National People's Congress on April 13, 1988.

[59] Including Regulations for the Implementation of the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures enacted by PRC State Council on September 20, 1983; Regulations for the Implementation of the Law of the People's Republic of China on Chinese-Foreign Cooperative Joint Ventures, ratified by PRC State Council on August 7, 1995, and issued by MOFTEC (Ministry of Foreign Trade and Economic Cooperation) on September 4, 1995; Regulations for the Implementation of the Law of the People's Republic of China on wholly foreign-owned enterprises, ratified by PRC State Council on October 28, 1990 and issued by MOFTEC (Ministry of Foreign Trade and Economic Cooperation) on December 12, 1990.

[60] The first Draft of "Foreign Investment Law of PRC" was issued by the Ministry of Commerce of PRC on January 19, 2015; Based on this Draft and the comments fed back,

Law" (FIL) was approved by NPC (National People's Congress) on 15th March, 2019 and will come into force on 1st January, 2020.[61] And upon taking effect, the new law will take place of the old three main foreign investment laws.

## 2. Highlights of the 2019 New Foreign Investment Law

### *a. More Convenient and Efficient Market Access*

As an important investment promotion measure, the FIL adopts "pre-establishment national treatment" plus "negative list" rule for the investors' market access, in order to further accelerate investment liberalization and convenience. Under the old foreign investment law regime, the establishment of the foreign investment enterprises is subject to the "case-by-case" approval system, i.e., the establishment of a foreign invested enterprise must be approved by the Ministry of Commerce (MOFCOM) and its competent local branches. In view of the low-efficiency of the system in practice, China began to explore a more efficient system and adopted "negative list" rule in a limited number of areas in 2016, which released several types of FIEs from case-by-case approval, and only subject to record-filing.[62] By the end of 2018, the official text of "negative list" which is to be applied nationwide, was issued by National Development and Revolution Commission (NDRC) and Ministry of Commerce (MOFCOM).[63] In 2019, FIL added "pre-establishment national treatment" and formed the new rule of entry. This is a very substantive and creative step that China has taken since its opening up in 1980s.

Under this new entry rule, on one hand, those FIEs whose industrial sectors that are not on the negative list are to be granted treatments no less favourable than domestic investors in the period of entry; on the other hand, the FIEs whose industrial sectors fall under the scope of the negative list are to be prohibited from establishment, or to be established subject to the

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NPC (National People's Congress) issued the second draft on December 26, 2018, named as "Foreign Merchants Investment Law of PRC (Draft for Comments)".

61 Website of China Daily, <http://cn.chinadaily.com.cn/a/201903/15/WS5c8b8280a31010568bdcfd53.html>, March 15, 2019. As of the geographical application scope, the NPC spokesman made a comment on the law application of investments from Hong Kong, Macau, and Taiwan. He said that Hong Kong, Macau, and Taiwan are separate customs territories, and the investments from these regions are different from both foreign investment and domestic investment, and will be managed with a reference to 2019 Foreign Investment Law. Furthermore, the relating rules are to be further perfected.

62 In March 2016, the "Draft of the Negative List (Trial)" was issued and implemented first in four regions i.e. Tianjin, Shanghai, Fujian, and Guangdong.

63 <http://www.xinhuanet.com//2018-12/25/c_1123900483.htm>.

restrictions provided in the negative list. The negative list will be issued or to be approved for issuance by the State Council.[64]

### *b. Better Protection of Intellectual Property Rights*

The new law strengthened that the foreign investors' intellectual property rights shall be better protected. The new law states that: *firstly*, any infringement upon the foreign investors' intellectual property rights will be subject to strict liabilities; *secondly*, cooperation on the basis of mutual consents in the field of intellectual property is to be encouraged; thirdly, the government is strictly prohibited from forcing the foreign investors to transfer technology under the coercion of its administrative powers.[65] This is the first time that foreign investors' IP rights are expressly stipulated in Chinese foreign investment law legislation.

### *c. Better Protection of the Investors' Legitimate Rights*

In the 2019 Foreign Investment Law, the Government is imposed greater compulsory duties than ever seen before, and breach of which will incur legal liabilities. The new law states that: *firstly*, only under exceptional circumstances provided by law, the foreign investors' investments shall be expropriated through due process with fair and prompt compensation; *secondly*, administrative organs and their staff are obliged to keep the commercial secrets of the foreign investors acquired in the process of performing their duties;[66] *thirdly*, unless expressly stipulated, the lawful rights and interests of foreign investors shall not be derogated, no extra obligations shall be imposed, and no extra conditions for market entry is to be affiliated, and the management and operation of the FIEs are not subject to intervention;[67] *fourthly*, the governments are required to strictly implement policy commitments made to foreign investors and keep promise in the performance of investment contracts; once the contract clauses are to be changed, the investors must be compensated reasonably and fairly.[68]

### *d. A Complaining mechanism is Established*

Pursuant to the new investment law, when foreign investors consider that the administrative agencies or their employees have infringed upon their lawful rights and interests, they might resort to this mechanism to seek a

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[64] Art. 4 of the 2019 Foreign Investment Law (FIL).
[65] Art. 22 of the 2019 Foreign Investment Law (FIL).
[66] Art. 23 of the 2019 Foreign Investment Law (FIL).
[67] Art. 24 of the 2019 Foreign Investment Law (FIL).
[68] Art. 25 of the 2019 Foreign Investment Law (FIL).

conciliation, and in addition, the investors could also seek administrative review in the higher level administrative agency and judicial trial in local courts.[69]

## C. Endeavour to Construct B&R ISDS Mechanism

### 1. The Motive to Construct B&R ISDS Mechanism

Since the early stage of cross-border investment, arbitration has been the main method of solving the disputes between foreign investors and sovereign States. However, China has never had a set of arbitration rules and its own institutions devoted to solving the disputes between foreign investors and sovereign States. The underlying reasons are multi-folded: *first*, China was traditionally a capital-importing country since the "reform and opening up" policy was adopted in 1978, and in a rather long period of time, policy of attracting foreign investment overrides rules of law and supra-national treatments were accorded to foreign investors; *secondly*, Chinese overseas FDI has been in a low level due to Chinese economic capacity and policy barriers before the year of 2000; *thirdly*, most of the disputes arising between foreign investors and Chinese local authorities were solved through diplomatic negotiations and conciliations, there was not an urgent need for arbitration rules and professional institutions settling the disputes between investors and States.

However, in recent years, circumstances have been dramatically changed. On one hand, with the deepening of Chinese opening up in foreign investment field, the legal problems and disputes are becoming more sophisticated; and on the other hand, Chinese outbound investment has been greatly increased,[70] notably in the area of the B&R overseas investment. 2018 is the BRI 5th anniversary, and during these five years, China's outbound investment to the B&R countries has been greatly increased during the recent years.[71] Chinese overseas investors are faced with uncertain political risks and suffer

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[69] Art. 26 of the 2019 Foreign Investment Law (FIL).

[70] In 2017, Chinese FDI outflow amounted up to 125 billions of dollars, ranking the 2nd in the world; in 2016, Chinese FDI outflow amounted up to 196 billions of dollars, ranking the 2nd in the world. Statistics from: World Investment Report 2018, at 4, 5.

[71] Take 2017 and 2018 as examples, from January to November 2017, Chinese enterprises' FDI outflow to 59 countries of B&R countries amounted to 12.37 billion dollars, counting 11.5% of the Chinese FDI outflow worldwide; the price of newly signed project construction contracts with 61 B&R countries amounted to 113.52 billion dollars, counting 54.1% of the whole contract price of Chinese enterprises worldwide; from January to November 2018, Chinese enterprises' outflow FDI to 56 countries of B&R countries amounted to 12.96 billion dollars, counting 12.4% of the Chinese FDI outflow worldwide; the price of newly signed project construction contracts amounted to 90.43 billion dollars, counting 48.8% of the whole contract price of Chinese enterprises worldwide.

unfair treatment from time to time. China has never been in such an urgent need for a set of its own arbitration rules and professional institutions.

## 2. Substantial Steps Taken to construct B&R ISDS Mechanism

### *a. Shenzhen International Arbitration Institute*[72] *expanding its Jurisdiction*

In order to better serve the B&R implementation, Shenzhen International Arbitration Institute issued a set of new arbitration rules at the end of 2016, which extended its jurisdiction over investor-State disputes. Article 2(2) provides: "Shenzhen International Arbitration Institute shall accept the investment disputes arbitration cases brought by investors against sovereign State Governments."[73]

According to the new arbitration rule, foreign investors in China may bring their investment disputes to Shenzhen International Arbitration Institute. Theoretically, Chinese overseas investors could also bring the cases against other sovereign States to this Arbitration Institute, upon the consent of the respondent sovereign State. This expansion of arbitration jurisdiction will immediately contribute to the investment disputes settlement in the area of Province of Guang Dong, Hong Kong, and Macao. Additionally, this Institute also has the possibility to serve the Belt & Road countries in the future.

### *b. CIETAC ISDS Mechanism Established With Its Own Arbitration Rules*

As the most spectacular step, China adopted its first investor-State arbitration rules named as Arbitration Rules of International Investment Disputes for China International Economic and Trade Arbitration Commission (CIETAC) (Trial), which came into force on 1st October 2017.[74] CIETAC has always been in the leading place in foreign trade and investment arbitration

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[72] An alternative name of Shenzhen International arbitration Institute is South China International Economic and Trade Commission, and the ever-used names include South-China Branch of CIETAC, Shenzhen Branch of CIETAC. Art. 1 of the Arbitration Rules of Shenzhen International Arbitration Institute.

[73] Arbitration Rules of Shenzhen International Court of Arbitration, website of Shenzhen Court of International Arbitration, <http://www.sccietac.org/web/doc/view_rules/856.html> (accessed January 31, 2019).

[74] Website of China Council for the Promotion of International Trade, Arbitration Rules of International Investment Disputes for CIETAC, <http://www.ccpit.org/Contents/Channel_4132/2017/0926/883777/content_883777.htm> (accessed January 30, 2019).

since its establishment in China, and it's also one of the institutions collaborating with ICSID on the list of cooperation agreements.[75]

The promulgation of CIETAC Arbitration Rules was based on the full consideration of Chinese foreign investment practice, and meanwhile on the basis of learning from the mature experience of the investment arbitration institutions (such as ICSID, ICC, and SCC) and the worldwide famous arbitration rules (such as ICSID Arbitration Rules and UNCTAL Arbitration Rules). Consequently, the CIETAC Arbitration Rules are characterized with the features of high efficiency, impartiality, as well as transparency. Its most important aspects are as follows:

*First*, as of the jurisdiction scope, the CIETAC Rules cover wide range of international investment disputes. Article 2 of the CIETAC Rules provided that the CIETAC shall accept international investment disputes arising from BITs, investment contracts, as well as domestic laws and regulations, filed by the investors against a state or its governments, based on the arbitration agreement between the parties.

*Secondly*, as of the distribution of jurisdictions between the two branches, Article 4 clarified the two arbitration institutions available for the investors, namely, Beijing Arbitration Center of the CIETAC and Hong Kong Arbitration Center of the CIETAC. Except otherwise agreed upon, the Beijing Center will accept the arbitration application and administer the case; if the parties have decided to arbitrate in Hong Kong or agreed to submit the case to the Hong Kong Center in their arbitration agreement, the Hong Kong Center will accept and administer the case.

*Thirdly*, as of other issues, the CIETAC Arbitration Rules also include the rules of arbitration tribunal composition, challenge of jurisdiction, disclosure of third-party funding, provisional measures, coordination between arbitration and conciliation, award, etc.

### *c. Establishment of the International Commercial Court*

In order to better settle the B&R commercial disputes, The International Commercial Court was established in July 2018, which is a standing trial institution of the PRC Supreme Court.[76] Two branching Commercial Courts will be established in Xi'an and Shenzhen. Xi'an Branching Court is designed

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[75] ICSID 2017 Annual Report, at 44.

[76] Website of The Supreme People's Court of the People's Republic of China, Art.1 of "Provisions of the Supreme People's Court on Several Issues Concerning the Establishment of an International Commercial Court", <http://www.court.gov.cn/fabu-xiangqing-104602.html> (June 29, 2018).

to settle the commercial disputes from the B&R land countries adjacent and near to the North of China; and Shenzhen Branching Court is designed to settle the commercial disputes from the B&R Sea Countries that are near to the south of China. Although this international commercial court mainly deals with commercial disputes such as contracts, it will be in a supplementary status in settling investor-State disputes by settling the commercial disputes involved or related to the investor-State disputes.

## D. Endeavour to Modernize Chinese BITs System Aligned with the IIA Reform[77]

### 1. An overview of Chinese BITs System

China signed its first BIT with Sweden in 1982, and it has so far signed 130 BITs in total, of which 104 are effective.[78] In 1980s and 1990s, the main aim of China was to attract foreign investments from developed countries. On one hand, China provided supra-national treatments to foreign investors and their investments, and on the other hand, China was very cautious in imposing any restrictions on its regulatory powers. As a result, Chinese BITs at that time had several characteristics, including: *first*, the standards of investment protection were incomplete, for example lack of an accurate definition of FET; *secondly*, the standards of investment protection were obscure, for example, indirect expropriation was not clarified in detail; *thirdly*, lack of international dispute settlement mechanism, limiting the settlement of investment disputes to "local remedies" and diplomatic negotiations.

### 2. Motive for China to Modernize its BITs System

The year 2010 marked the 10th Anniversary of Chinese 'Going Abroad" strategy, and was seen as a beginning of Chinese overseas FDI booming. By 2010, Chinese overseas FDI flow ranked the 5th highest in the world.[79]

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[77] BITs are very important sources of international investment law, which contain the legal rights and obligations of investors and States and are binding for both of them. Most of the ISDS cases were brought on the basis of BITs, namely, 60% among all the cases registered. However, in recent years, most of the BITs were criticized as unbalanced, imposing restrictions on regulatory powers, inadequacies in arbitration. And in 2016, UNCTAD launched the IIA Reform, in order to better balance the rights and obligations of the investors and States, as well as to better settle the disputes between investors and States. Website of UNCTAD, Investment Policy, <https://investmentpolicyhub.unctad.org/IIA/KeyIssueDetails/553>.

[78] Ministry of Commerce of People's Republic of China Department of Treaty and Law, List of Chinese BITs, <http://tfs.mofcom.gov.cn/article/h/> (accessed January 31, 2019).

[79] In 2001, the very beginning of 21 Century, "Chinese Enterprises Going Abroad" strategy was put forward, and subsequently established as an important State strategy in 16 Session Communist Party Conference held in 2002. After that, Chinese enterprises began to invest

Accordingly, the rapid development and prosperity of Chinese overseas FDI also prompted China to review its traditional BITs system and to consider making necessary changes. It is argued that instead of only underscoring the host State's regulatory powers, the future BITs must spend some efforts to provide better treatments and protections for the foreign investors. Consequently, on a reciprocal basis, Chinese overseas investors will enjoy better investment treatments and protection standards. Furthermore, some efforts must also be taken to make a better balance between the rights and obligations of investors and host States.

As an important move, China signed Sino-Canada BIT (2012) and Sino-Australia FTA (2015). Sino-US BIT, Sino-EU BIT are under negotiations. In these newly signed BITs and BITs under negotiations, there appeared some new changes.

## 3. The changes that have been made in the new-generation-BITs[80]

### *a. Pre-Establishment Treatment is to Be Incorporated*

In the negotiation of China-US BIT, for the first time, China promised to accord foreign investors "pre-establishment treatment" in market access. Although pre-establishment treatment was not incorporated in any BITs, it is sure to be accorded to all foreign investors from the countries that have signed BITs with China. On 15th March, 2019, PRC National People's Congress has ratified the "PRC Foreign Investment Law" which will be effective from January 1st, 2020. In this law, "pre-establishment treatment" plus "negative list" rule was established for the market access of foreign investors.[81]

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overseas, at first mainly in developing countries in Asia, Latin America, and Africa, in 2003, Chinese overseas FDI in Asia, Latin America and African countries amounted together up to 51.4%. With the further implementation of the strategy of "Going Abroad", Chinese FDI began to increase in those main economic bodies, including EU, ASEAN, US, Russia, and Japan. This could be seen a beginning of Chinese investment globalization. Website of Ministry of Commerce of People's Republic of China Department of Treaty and Law, Statistics Bulletin of Chinese Outward Foreign Direct Investment (2003, 2010).

[80] New-generation BITs refer to those BITs signed before 2010, namely, the pre-2010 BITs. In recent few years, the IIA (international investment treaty) reform was launched by UNCTAD, and in order to distinguish, the UNCTAD named the pre-2010 BITs as old-generation BITs, and accordingly, named the post-2010 BITs as new-generation BITs. The old-generation BITs amounted up to 95% of the current IIAs, and played major roles in international investment dispute settlement, and all of the ISDS cases were based on the pre-2010 IIAs by the end of 2016 (Website of UNCTAD, Investment Policy, <https://investmentpolicyhub.unctad.org/IIA/KeyIssueDetails/553>).

[81] Art. 4 of the "Foreign Merchants Investment Law" (to be effective from January 1, 2020).

### *b. Scope of MFN Became More Specified*

The scope of the most-favoured-nation treatment ("**MFN**") was more specified and became clearer. Take the Sino-Australia FTA and Sino-Canada BIT for example: in the Sino-Australia FTA, the most-favoured nation treatment will be accorded to foreign investors and the covered investments with respect to the "expansion, management, conduct, operation and sale or other disposition of investments" in China territory.[82] And in Sino-Canada BIT, MFN will be accorded to investors and the covered investments with respect to the "establishment, purchase, expansion, management, conduct, operation and sale or other disposition of investments" in Chinese territory.[83]

### *c. FET is Incorporated and Defined More Elaborately*

From the newly signed BITs, it is apparent that China is much more cautious to incorporate and define Fair and Equitable Treatment (FET). Take the Sino-Canada BIT for example, Article 4 named "minimum standard of treatment" provided that: first of all, FET and full protection and security shall be accorded to foreign investors; *secondly*, the standard of FET shall not exceed the MST (Minimum Standard of Treatment)required by the customary international law established by the state practice recognized as law; *thirdly*, any violation of other clauses in this BIT or other international treaties will not be deemed to have violated FET.

### *d. ISDS Mechanism is to be Diversified and Flexible*

In its first stage of opening up, China used to settle the investor-state disputes by diplomatic negotiations between the States, or by conciliations between investors and local authorities. China was very apprehensive of incorporating investor-State dispute settlement clauses in its BITs, trying to reduce the host state risks of being sued while not including ICSID arbitration clauses in most of its BITs. According to the statistics available to the author, till the end of 2018, only 12.5% of BITs (13 out of 104 BITs) contain ICSID arbitration clauses, most of which were newly signed BITs, or the newly revised old BITs after the year of 2000.[84]

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[82] Sino-Australia FTA, Art. 9.3: National Treatment. Website Services of PRC Free Trade Area, <http://fta.mofcom.gov.cn/Australia/annex/xdwb_09_en.pdf>.

[83] Sino-Canada BIT, Art. 5. Website of Ministry of Commerce of PRC Department of Treaty and Law, <http://tfs.mofcom.gov.cn/article/Nocategory/201111/20111107819474.shtml>.

[84] Website of Ministry of Commerce of PRC, Department of Outward Investment and Cooperation, List of Bilateral Investment Treaties, <http://tfs.mofcom.gov.cn/article/Nocategory/201111/20111107819474.shtml>.

However, the circumstances changed since Belt & Road Initiative was put forward in 2015, i.e., in order to push forward the implementation of BRI, a more flexible and multiple-ways dispute settlement mechanism is urgently needed. In order to form a rationale investor-State dispute settlement mechanism, China must coordinate the local ISDS mechanism and international ISDS mechanism well, and further to perfect the two mechanisms from perspectives of Chinese domestic rules of law and its BITs system. At the domestic level, China should perfect the local rules of law, especially guaranteeing due process, transparency, avoiding arbitrariness and denial of justice on the part of the judges and the administrative officials. At the international level, China should incorporate flexible ISDS clauses, such as ICSID jurisdiction clause, *ad hoc* arbitration clause, or other international jurisdiction clause into more BITs. Further, in the BITs signed with those B&R partners, CIETAC jurisdiction clause, together with its Arbitration Rules must also be incorporated as a choice for the investors.

In fact, in the newly signed Sino-Canada BIT and Sino-Australia FTA, an international arbitration mechanism was clearly established, i.e., the investors could bring the claim to an *ad hoc* arbitration tribunal, which will be constituted under the rules of ICSID with the administrative assistance of the ICSID Secretariat, including the appointment of arbitrators, conduct of arbitrations, etc. Compared with the previous BITs, the arbitration rules in these two investment treaties are more detailed and more open to international settlement. We can expect that in the near future, a unified BITs system will be formed gradually with a better ISDS mechanism based on the newly-passed Foreign Investment Law.

## Conclusion

Since more than half a century, ICSID has been in the leading place in investor-State disputes settlement. In recent years, due to the fierce criticisms from its member States, ICSID began to amend its rules. The aims of this amendment are multi-folded: better balancing the investors' interests and host States' regulatory powers; keeping coherence and consistency of the awards; and improving legal predictability and certainty on the part of investors.

Meanwhile, other two influential ISDS mechanisms are on their way of construction: the EU advocated establishment of an Investment Court, and China is taking steps to construct B&R ISDS mechanism, which is designed to solve the disputes between China and its B&R trade partners. If successfully established, these two ISDS mechanisms will be very competitive. In

such a triple-pillared ISDS mechanisms regime, China must make its ISDS mechanism more attractive for the foreign investors and other trade partners.

On one hand, China must take all efforts to form a legal environment by effectively binding the conducts of the government officials and the judges of courts, eliminating the arbitrariness in the law execution; and on the other hand, China must properly settle the disputes between foreign investors and Chinese government once controversies arise. In view of the problems encountered in the Chinese ISDS practice, the author strongly suggested that the following aspects shall be improved:

*First*, the conducts of the judges and administrative officials must be made subject to "due process". Usually, when an investor-State dispute arises, the investor first seeks administrative review or resorts to the court for judicial trial. In practice, "denial of justice" is the most frequently alleged procedural deficiency, for example, dismissing the investors' claims arbitrarily, confirming the government's decisions without rationale reasons, etc.

*Secondly*, Chinese BITs system must be reformed aligned with the IIA reform launched by UNCTAD. BITs are main legal sources of investment law and the basis of ISDS jurisdiction, which play a very critical role in constructing the B&R ISDS mechanism. China should reform the existing BITs in several aspects, such as amending the old BITs provisions, terminating the old existing BITs, replacing the outdated BITs, abandoning unratified old BITs, in order to form a unified BITs system.

*Thirdly*, China must construct CIETAC into a highly international ISDS mechanism. In order to achieve this goal, the CIETAC should borrow arbitration experience from the world-influential investment arbitration institutions such as ICSID, ICC, SCC, and establish effective communication with them.