The New Generation of Chinese BITs and Investment Arbitration

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Key Question:

The new generation of Chinese BITs:

Why?

What?

So?
I. Background: The Changing Role of China in International Investment Relations

From a major FDI recipient to a major recipient, as well as an investors of growing importance.
1. China as a Major FDI Recipient

i. No. 1 among developing states since 1992; consistently top 5 FDI recipient worldwide.

ii. 709.18 billion US$ (600161 FDI projects) by end February 2007.

iii. Great contribution in China’s development and growth (GDP, Forex reserve, trade, tax, trade,)

iv. Two jumps: a bit of history
Major Investors in China

Major Investors in China as of 2005

- Asia 10: 68%
- EU: 7%
- North America: 9%
- Free Ports: 10%
- Others: 6%

BIICL Investment Treaty
Forum Seminar: "China and International"
16:18:00 PM, 2 April 2007, DLA Pipper London
Tope 15 Investors in China

Top 15 Investors in China

- 42% in USA
- 9% in UK
- 8% in Hong Kong
- 7% in Japan
- 7% in Germany
- 5% in Singapore
- 4% in Cayman Islands
- 2% in France
- Others

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Industrial Structure by 2005

Industrial Structure of FDI in China as of 2005

Primary Industry: 29%
Secondary Industry: 2%
Tertiary Industry: 69%
Industrial Structure in 2005

Industrial Structure of FDI in China in 2005

- Primary Industry: 62%
- Secondary Industry: 37%
- Tertiary Industry: 1%

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Industrial Distribution as of 2005

Industrial Distribution of FDI in China as of 2005

- 65% Manufacturing
- 17% Real Estate
- 4% Lease and Business Service
- 3% Wholesale, Retailing
- 2% Transport, Warehousing, Post & Telecommunication
- 2% Construction
- 2% Agriculture, Forestry, Animal Husbandry and Fishing
- 1% Resident Service and Other Services
- 1% Production and Supply of Power, Gas, and Water
- 3% Others
2. China as a Foreign Investor

i. Policy: from ‘control’ to ‘promotion’:
   i. 1998: “going abroad” strategy
   ii. 2001: “going abroad” in 10th Five-Year Plan

ii. Measures:
   i. Simplified approval process: SDRC
   ii. Financial support: credit support, special funds
   iii. SAFE: Forex regulation relaxed
   iv. China Export & Credit Insurance Co (Sinosure): investment insurance

iii. Result:
Top 15 Destinations as of 2005

Top 15 Destinations for Chinese FDI as of 2005 (Unit: US$ 100 Million)

- Hong Kong
- Cayman Islands
- Virgin Islands
- RO Korea
- USA
- Malaysia
- Abu Dhabi
- Shanghai
- Bermuda Islands
- Singapore
- Germany
- Kazakhstan
- Vietnam
- Macau
- Australia
- Russia
- Sudan
- Bermuda

16:18:00 PM, 2 April 2007, DLA Pipper London
Further Increase?

- The establishment of the Forex Investment Company (1.07 trillion forex reserve)

Responses: e.g., UK:

- Investment Promotion MOU, and
- ‘Touchdown London’
3. Changed Role: Implications for BITs?

- Changed role has led to the changed policy and law:
    - 1998 Sino-Barbados BIT and the launch of the ‘Going Abroad’ strategy
    - Same Pattern: post-2000 BITs: essentially the same
    - All developing partners (1997-2002)
Demands from Developed States

- Renegotiation and negotiation of BITs with developed states:
  - Negotiations: Canada, Mexico (Indian, Russia completed)
  - Renegotiations: Netherlands, Germany, Sweden, Finland, Belgium & Luxemburg, Spain, Portugal.

- a policy dilemma
  - To resist (a fragmented approach?)
  - To literalize (ready to bear the consequences?)
II. The New Generation of Chinese BITs

The Sino-Germany BIT: The State-of-Art Chinese BIT:

1. Definition:

‘investment’: ‘every kind of asset invested directly or indirectly by investors’.

"Invested indirectly" means invested by an investor of one Contracting Party through a company which is fully or partially owned by the investor and having its seat in the territory of the other Contracting Party.
Sino-Germany BIT

2. Treatment:

- National Treatment: common limitations (such as ‘subject to its laws’ and ‘sound development of national economy’) lifted but a ‘grandfather clause’ for China---China clause No.1 provided:
  - Existing inconsistent measures fine, but not more
  - Measures may be amended if no to increase the degree of incompatibility
  - Phase out promise

- Same on non-discrimination treatment
3. Transfer:

- ‘China clause’ modified:
  - Previous condition ‘subject to Chinese laws’, but requires:
    - Transfer of proceeds subject to relevant ‘formalities stipulated by the present Chinese laws and regulations”, and
    - A loan-agreement has been registered with the relevant authority for the loan to be paid freely.
Sino-Germany BIT (cont.)

- Dispute Settlement: full access
  - From ‘only amount of compensation’ disputes to ‘any dispute concerning investments’, to be submitted to:
    - ICSID or UNCITRAL based arbitration
    - Exhaustion of 3 months domestic administrative review
    - Weak ‘fork in the road’
III. Implications on Investment Arbitration

1. Investment treaty arbitration cases?
   Highly likely:
   • Opened access: No more ‘AOA only’ limitation:
     • *Changchun Huijing v Changchun City Government* case
   • Large FDI stock
   • Frequent change of laws and policies:
     • *Fujian Xinyuan v Fuzhou City Government* case
   • Local v central interests
III. Implications on Investment Arbitration (cont.)

2. A flood of investment treaty arbitration cases?
   Unlikely:
   - Legal: limited BITs with open access (one/two of the top 15 investors)
     + Uncertainty with the effect of MFN
   - Economic: the economy is sound
   - Politically: generally stable
   - FDI structure: Hong Kong and other investors
   - Efforts by Chinese government: *Huajie* and the so-called ‘*regulatory retaliation*’ culture
     • the *McDonald’s v Beijing City Government* case
## Chinese BITs: Full Access to International Arbitration

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III. Implications on Investment Arbitration (cont.)

3. The other side: Chinese investors suing foreign governments? Likely:

- Dramatic increase
- High risk destinations
  - Sinosure Country Risk: of the 67 states encouraged to invest, 70% with high or very high risk (34 Grade D (very high), 11 (high))
- Tza Yap Shum v. Republic of Peru (Case No. ARB/07/6)
Conclusions

- New Role---new thinking and new policy toward BITs
- New generation of BITs with higher standards (definition, treatment, transfer and dispute settlement)
- Implications: investment treaty arbitration cases against Chinese government highly possible, but a dramatic surge unlikely in near future.
- Meanwhile more and more Chinese investors may start making use of these BIT DS mechanisms.
Thank you very much!