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Explaining China's approach to investor-state dispute settlement reform: A contextual perspective

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Abstract

China's approach to ISDS reform is widely perceived as undecided and ambiguous. This paper provides the first detailed analysis of China's submission to the UNITRAL Working Group III and situates China's approach in the context of global dialogue of ISDS reform and competing reform proposals. The paper shows that China's open, flexible, and evolving approach to ISDS reform could be better understood by a contextual evaluation of the pertinent factors which have contributed to its formation. Moreover, this paper explains why China did not sign up to the EU's investment court system (ICS) proposal in the EU-China Comprehensive Agreement on Investment (CAI). Lastly, the paper argues that China should reconsider its attitude towards the ICS in the CAI context and that the EU's recent suggestion that the envisaged multilateral investment court may adopt an 'open architecture' is likely to enhance its appeal to China.

1 | INTRODUCTION

International investment law scholarship has shifted the discourse from the legitimacy crisis of, and the resulting backlash against, the investor-state dispute settlement (ISDS) system to its possible reforms.[1] The United Nations Commission on International Trade Law (UNCITRAL) Working Group III (WGIII) has been mandated to deliberate possible structural and procedural reform of the ISDS system since 2017. The reform proposals cover a wide set of issues, ranging from incremental improvement of the current ISDS system to more ambitious, systemic reforms such as a wholesale replacement of *ad hoc* investor-state arbitration with a two-tiered permanent multilateral investment court (MIC).[2] In July 2021, UNCITRAL approved a workplan to move forward on ISDS reform with the ultimate

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[1]Sergio Puig and Gregory Shaffer, 'Imperfect Alternatives: Institutional Choice and the Reform of Investment Law' (2018) 112 American Journal of International Law 361, 366.

[2]Report of Working Group III on the Work of its Thirty-ninth Session (10 November 2020), A/CN.9/1044.

objective of formulating a multilateral instrument that allows each state the choice of whether and to what extent it wished to adopt the relevant reforms in 2026.[3]

Since its first bilateral investment treaty (BIT) with Sweden in 1982, China has entered into an extensive network of international investment treaties (IIAs) over the past four decades. According to the United Nations Conference on Trade and Investment (UNCTAD), China has signed 145 BITs (107 in force) and 24 treaties with investment provisions (19 in force) by June 2023, second only to Germany in terms of the number of IIAs concluded.[4] China was the second largest recipient of foreign direct investment (FDI) inflows (USD 181 billion) and the fourth largest source of outward FDI in 2021 (USD 145 billion).[5] China's presence in ISDS proceedings has also been fast rising in recent years. At least thirteen investment arbitration cases have been filed by Chinese investors against host states and six cases filed by foreign investors against the Government of China from January 2018 to June 2023 (see Appendix Tables 1 and 2), more than what China had experienced for more than 30 years since the conclusion of its first BIT.[6]

Then, what approach does China take to ISDS reform? For some time, China's approach to ISDS reform was viewed as undecided and ambiguous.[7] On 19 July 2019, the Government of China submitted the first proposal on ISDS reform to UNCITRAL WGIII. In the proposal, China reaffirms its commitment to ISDS as an important mechanism for resolving investor-state disputes, outlines its concerns about the current ISDS regime, and suggests several priority areas for reform.[8] The issues covered in China's proposal include, *inter alia*, an appellate mechanism, code of conduct for arbitrators, alternative means of investment dispute settlement and third-party funding. However, the content of China' proposal on ISDS reform has received only scant analysis in the existing literature.[9]

The ensuing development after China's UNCITRAL submission provide more clues to what China wants from ISDS reform. To start with, the landmark EU-China Comprehensive Agreement on Investment (CAI) concluded in December 2020 does not contain any ISDS clauses. Given the EU's unambiguous position that 'there can be no return to the old-style ISDS',[10] it is reasonable to assume that the EU tabled with China its proposal on the two-tier International Investment Court System (ICS) during the CAI negotiations. After all, the EU has successfully negotiated this reformed ISDS mechanism in its free trade agreements (FTAs) with Canada, Singapore, Vietnam, and Mexico. The fact that there is no ISDS provision in the current version of the CAI is an unmistakable signal that differences remain in China and the EU's respective positions regarding the appropriate mechanism for the resolution of investment protection disputes. To say the least, China is not yet ready to endorse the EU's ICS proposal in either bilateral or multilateral negotiations.[11] This makes a deep understanding of the Chinese position on ISDS reform even more necessary from an EU perspective.

Furthermore, China formally submitted a request to accede to the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in September 2021.[12] China's accession request is a clear indication that China is comfortable with the incremental changes of ISDS embodied in the CPTPP. Nevertheless, as a senior Chinese official made it clear, China's ambition for a 'comprehensive approach' to ISDS reform exceeds what the CPTPP promises.[13] For instance, China has called for institutional reforms of ISDS such as the establishment of an appellate

[3]Report of the Working Group III on the Work of its Resumed Fortieth Session (27 May 2021), A/CN.9/1054.

[4]UNCTAD Investment Policy Hub <https://investmentpolicy.unctad.org/international-investment-agreements/countries/42/china>.

[5]UNCTAD, *World Investment Report 2022: International Tax Reform and Sustainable Development* (9 June 2022) 9, 21.

[6]See Appendix Table 1 and 2.

[7]Yuwen Li & Bian Cheng, 'China's Stance on Investor-State Dispute Settlement: Evolution, Challenges, and Reform Options' (2020) 67 Netherlands International Law Review 503, 530–531; Mark McLaughlin, 'Global Reform of Investor-State Arbitration: A Tentative Roadmap of China's Emergent Equilibrium' (2018) 6 Chinese Journal of Comparative Law 73, 97; Huiping Chen, 'Reforming ISDS: A Chinese Perspective' in Yuwen Li et al (eds), *China, the EU, and International Investment Law: Reforming Investor-State Dispute Settlement* (Routledge 2020) 100–111.

[8]Note by the Secretariat, 'Possible Reform of Investor-State Dispute Settlement: Submission from the Government of China' (8 July 2019), A/CN.9/WG. III/WP.177.

[9]For an exception, see Anthea Roberts and Taylor St. John, 'UNCITRAL and ISDS Reform: China's Proposal' (5 August 2019) <https://www.ejiltalk.org/uncitral-and-isds-reform-chinas-proposal/>.

[10]European Commission, 'Key Elements of the EU-Japan Economic partnership Agreement' (Brussels, 12 December 2018).

[11]On possible reasons why the current CAI does not include ISDS provisions, see Katia Fach Gómez, 'EU- China Negotiations on Investor State Dispute Settlement within the CAI Framework: Are We on the Right Track' (2021) 55 Revista General de Derecho Europeo 48, 54–61.

[12]Eleanor Olcott, 'China Seeks to Join Transpacific Trade Pact', Financial Times (16 September 2021).

[13]Jiang Chenghua, Remarks at UNCTAD High Level IIA Conference (Geneva, 13 November 2019).

mechanism modelled on the WTO dispute settlement system.[14] In comparison, largely operating under the traditional ISDS framework, the CPTPP does not even pursue the creation of an appeal facility and only contains an 'opening clause' that requires the contracting parties to consider opting into a future appellate mechanism.[15]

This article seeks to push forward the debate on China's approach to ISDS reform in three moves. Firstly, this article provides the first in-depth analysis of China's UNITRAL WGIII submission. It shows that China is a strong proponent of ISDS reform and that China's approach to ISDS reform converges considerably with key ISDS reform-minded states. However, it is challenging to put China in the camp of either the incrementalists or the systemic reformers in the UNCITRAL process.[16] Secondly, to better understand China's position on ISDS reform, this article provides a contextual evaluation of the pertinent factors which have contributed to China's open, flexible, and evolving approach to ISDS reform. These factors include China's status as both a capital-importing and capital-exporting power, China's immensely ambitious Belt and Road Initiative (BRI), the ISDS clauses in China's evolving IIA practices, China's limited experience with the ISDS system, and China's changing attitude towards international adjudication. Finally, this article explores the future of ISDS in the CAI. It concludes that it is unlikely for China to accept the ICS system in the CAI in the short term because China favours a multilateral approach to ISDS reform and it is not yet convinced that the EU's MIC proposal is the best path to reform ISDS. Nevertheless, this article argues that China should reconsider its position on the EU's ICS proposal and that the EU's suggestion that the envisaged MIC may adopt an 'open architecture' could potentially enhance its appeal to China.[17]

China's contribution to global ISDS reform dialogue should not be viewed as an isolated event. It is part of a bigger trend of China's active participation in global economic governance.[18] Chinese President Xi Jinping has called for China to 'lead the reform of the global governance system', transforming institutions and norms in ways that will reflect Beijing's values and priorities.[19] Therefore, a sophisticated understanding of China's position on ISDS reform provides a new angle to appreciate its approach to shaping global economic norms. The rest of the article proceeds as follows. Part 2 provides the first detailed analysis of China's UNITRAL submission, situating China's approach to ISDS reform in the context of global dialogue of the ISDS regime and competing reform proposals. Part 3 analyses a range of contextual factors which have contributed to shape China's approach to ISDS reform. Part 4 explores China's attitude towards the EU's ICS proposal in the CAI negotiations. Part 5 concludes the article.

2 | UNDERSTANDING CHINA'S APPROACH TO ISDS REFORM

2.1 | China's UNITRAL WGIII submission

In its UNCITRAL submission, China begins by making it clear that it supports the maintenance and reform of the ISDS system. In recent years, the ISDS system has been frequently criticised as suffering a 'legitimacy crisis'.[20] China concurs with many criticisms levelled at the current *ad hoc* ISDS system: lack of an appropriate error-correcting mechanism; lack of stability and predictability in arbitral awards; arbitrators' professionalism and independence have been put into question; a small club of lawyers and arbitrators that lack gender and geographical diversity; the risks

[14]Submission from China (n 8) 4.
[15]Article 9.23 (11) of the CPTPP.
[16]Anthea Roberts, 'Incremental, Systemic, and Paradigmatic Reform of Investor-State Arbitration' (2018) 112(3) American JIL 410, 410.
[17]Submission from the European Union and its Member States, 'Possible Reform of Investor-State Dispute Settlement (ISDS)', A/CN.9/WG.III/WP.159/Add.1. (24 January 2019) para 3.16.
[18]Shahar Hameiri & Lee Jones, 'China Challenges Global Governance? Chinese International Development Finance and the AIIB' (2018) 94 (3) International Affairs 573, 573–574. For example, China has been playing an active role at the World Trade Organization (WTO) and Hague Conventions. See Communication from China, 'China's Proposal on WTO Reform', WT/GC/W/773 (13 May 2019); China International Commercial Court, 'The 2019 HCCH Convention on the Recognition and Enforcement of Foreign Judgements in Civil or Commercial Matters has been Adopted' (3 July 2019) <http://cicc.court.gov.cn/html/1/219/208/209/1303.html>.
[19]Council on Foreign Relations, 'China's Approach to Global Governance' <https://www.cfr.org/china-global-governance/>.
[20]Malcolm Langford and Daniel Behn, 'Managing Backlash: The Evolving Investment Treaty Arbitrator?' (2018) 29 (2) European Journal of International Law 551, 554–558.

that third-party funding in ISDS poses to the public and to the investment regime itself; and lengthy and costly ISDS proceedings.[21] China's criticism of the current ISDS system is partly based on China's own experience. For example, arbitral tribunals have given different interpretations to identical ISDS provisions in China's first-generation BITs.[22] The lack of an appellate mechanism in the current ISDS system renders it impossible for such inconsistent awards to be reconciled. Despite its drawbacks, China views the present ISDS system as playing an important role in protecting the rights and interests of foreign investors and promoting cross-border investment. In addition, China stresses the role of ISDS in promoting the rule of law in international investment governance and avoiding politicisation of investment disputes between foreign investors and host states.[23] China's overall positive attitude towards ISDS distances it from the other emerging powers such as Brazil and South Africa, which advocate paradigm shifting reforms to replace ISDS with the return to either state-to-state arbitration or local remedies.[24]

Based on its concerns about the current ISDS system, China supports a *multilateral and comprehensive* approach to reforming ISDS, arguing that some of the institutional issues of ISDS tend not to lend themselves to resolution through BITs and regional trade agreements.[25] A multilateral solution to ISDS reform is clearly optimal because global investment is regulated by a 'spaghetti bowl' of over 3000 IIAs. If each country engages in its own piece-meal reforms, the ISDS system will end up even more variegated and fragmented.[26] China's preference for a multilateral approach to ISDS reform echoes Chinese President Xi Jinping' call for multilateralism in global governance in many international fora.[27]

More specifically, China has made five recommendations, stressing that they are non-exhaustive since the proposals that are currently considered at UNICTRAL WGIII cover a much wider range of issues that China's submission does not address.[28] First, China supports the establishment of a permanent multilateral appellate mechanism, modelled on the WTO dispute settlement system, with fixed procedures, institutions, and staff. China views the creation of an ISDS appellate mechanism key to improving consistency, correctness, coherence, and predictability of ISDS decisions.[29] China's proposal is not surprising as it has long held a favorable view and made active use of the WTO dispute settlement system.[30] An ISDS appeal mechanism was envisaged in the China-Australia FTA in 2015, even though no substantial outcome emerged from the negotiations.[31] However, China does not explain *how* a permanent appellate mechanism could be implemented.[32] For example, it is not clear whether China supports an appeal facility in lieu of ICSID annulment under the ICSID framework, a permanent standalone appellate body that will hear all ISDS cases, or an appellate mechanism as the second tier in a MIC.

The creation of an appellate mechanism for ISDS is not uncontroversial. The ICSID considered the possibility of introducing an appeals facility in 2004 but finally concluded that its proposal was 'premature' in view of the concerns voiced by many governments during informal debates.[33] The ICSID has recently completed a five-year consultative process on updating the ICSID rules. However, the proposed reforms of the ICSID rules do not mention the introduction of an appeal facility.[34] At UNCITRAL WGIII, critics questioned whether an appeal mechanism would

[21]Puig and Shaffer (n 1) 366.
[22]See part 3.2 below.
[23]Submission from China (n 8) 2.
[24]Stephen W. Schill and Geraldo Vidigal, 'Cutting the Gordian Knot: Investment Dispute Settlement a la carte', International Centre for Trade and Sustainable Development (ICTSD) and the Inter-American Development Bank (IDB) (November 2018) 15–17.
[25]Submission from China (n 8) 4.
[26]Colin M. Brown, 'The Contribution of the European Union to the Rule of Law in the Field of International Investment Law through the Creation of a Multilateral Investment Court'' (2021) 27 European Law Journal 96, 106–107.
[27]Xi Jinping, 'Let the Torch of Multilateralism Light up Humanity's Way Forward', Special Address at the World Economic Forum (25 January 2021).
[28]Submission from China (n 8) 4.
[29]Ibid.
[30]Gregory Shaffer and Henry Gao, 'China's Rise: How It Took on the U.S. at the WTO' (2018) Illinois Law Review 115, 134–137.
[31]Article 9.23 of the China- Australia Free Trade Agreement.
[32]Jose E. Alvarez, 'ISDS Reform: The Long View' (2021) 36 (2) ICSID Review 253, 267.
[33]ICSID Secretariat Discussion Paper, 'Possible Improvements of the Framework for ICSID Arbitration' (22 October 2004) 14–16.
[34]ICSID, *Proposals for Amendment of the ICSID Rules* (November 2021). The establishment of an appellate mechanism at ICSID is challenging as it will involve an amendment of the ICSID Convention. See Albert Jan van Den Berg, 'Appeal Mechanism for ISDS Awards: Interaction with the New York and ICSID Convention' (2019) 34 (1) ICSID Review 156, 188.

necessarily increase coherence and consistency of arbitral awards since substantive investment protection standards are found in different sources of law, such as IIAs and domestic laws. Given the variations of language in these texts, it is quite likely that even an appellate body may not prevent different outcomes arising from the same factual circumstances and legal issues.[35] On the other hand, views were reiterated that there are common standards in different sources of law that could be interpreted in a more consistent and predictable manner than currently done by *ad hoc* arbitral tribunals.[36] Some states also expressed concerns that an appellate mechanism could cause significant increases in costs and duration of arbitral proceedings. Other states dismissed such concerns and argued that an appellate mechanism would actually lead to a decrease in costs and duration of ISDS in the long run as certainty and predictability are increased.[37] Even among the states which support the establishment of an appellate facility of some kind, there is as yet no consensus on its scope, effect, enforcement, or the method for its establishment.[38]

Second, China favors the option of retaining the right of the parties to appoint arbitrators at the first-instance stage of arbitral proceedings in any reform proposals. China views the right of the parties to appoint arbitrators not only a widely accepted institutional arrangement in settling international disputes, but also the 'core and most attractive feature of international arbitration'.[39] China further justifies its preference for party-appointed arbitrators on three grounds. The first reason is that a wide pool of arbitrators provides the advantage of a broad expertise. Because investment disputes often involve complex factual and legal issues in different sectors and industries at the first-instance stage of legal proceedings, the parties value the ability to vet an arbitrator in determining the composition of the arbitral tribunal for a particular case.[40] By contrast, the appointment of arbitrators from a limited and closed list could compromise this valued aspect of investor-state arbitration. Furthermore, the right of parties to choose their trusted experts to hear cases is a widely accepted institutional arrangement not only in most BITs and all of the major international arbitration rules, but also in most other dispute settlement mechanisms in the fields of public international law.[41] Finally, China stressed that the protection of investments was the original motivation for setting up international investment arbitration mechanisms. The right of parties to appoint arbitrators at the first-instance stage of investment arbitration is an important aid to enhancing the confidence of parties to disputes, especially investors.[42] China's argument echoes the popular perception that disputing parties will tend to have greater faith in an arbitral process and be less likely to challenge the legitimacy of the tribunal's decision-making process if they played an intimate role in constituting the tribunal.[43]

China's insistence on maintaining the practice of party-appointed arbitrators is in stark contrast to the EU's MIC proposal at UNCITRAL WG III. According to the EU, since the choice of arbitrators is made after a dispute has arisen, investors and state respondents tend to appoint arbitrators who are considered as having a predisposition towards one side (investor or state-friendly). However, the long-term interests of the ISDS system lie in providing for adjudicative bodies that faithfully interpret and apply the underlying substantive provisions.[44] Therefore, the EU advocates moving away from appointment of arbitrators by the disputing parties to a two-tier investment court system of full-time adjudicators on long, non-renewable terms.[45]

Third, while retaining the right of parties to appoint arbitrators, China submits that it is necessary to improve the rules governing arbitrators' qualifications, conflicts of interest, selection and disqualification procedures. Specifically,

[35]Julian Arato et al, 'Parsing and Managing Inconsistency in Investor-State Dispute Settlement' (2020) 21 Journal of World Investment and Trade 336, 338.
[36]UNCITRAL, Report of Working Group III on the work of its resumed thirty-eighth session, A/CN.9/1004/Add.1 (28 January 2020) 5–6.
[37]Ibid, 6. See also Margie-Lys Jaime, 'Could an Appellate Review Mechanism Fix the ISDS System?' Kluwer Arbitration Blog (11 February 2021).
[38]UNCITRAL, 'Possible Reform of investor–State dispute settlement, Appellate mechanism and enforcement issues', UN Doc A/CN.9/WG.III/WP.202 (12 November 2020).
[39]Submission from China (n 8) 4.
[40]Ibid.
[41]Ibid.
[42]Ibid.
[43]Charles N. Brower, 'The (Abbreviated) Case for Party Appointments in International Arbitration' (2013) 1 American Bar Association Section of International Law International Arbitration Committee 1, 11.
[44]Submission from the EU, 'Possible Reform of Investor-State Dispute Settlement (ISDS)' (December 12, 2017), A/CN.9/WG.III/WP.145, 10.
[45]Submission from the EU (n 17) 10.

China notes that, given the public international law foundation of investment arbitration, arbitrators should have professional knowledge in the fields of public international law and international economic law.[46] Requiring expertise in public international law will remedy a concern that a significant number of adjudicators in the current system have limited expertise in public international law. In addition, China wants to develop a code of conduct for arbitrators in investment arbitration that will avoid potential conflicts of interest and prevent inequities that may be caused by arbitrators improperly practicing as legal counsel in other arbitral proceedings.[47] The so-called 'double-hatting' problem may give arbitrators improper incentives to decide cases in a manner that favors the party that appointed them so as to assure a flow of future client instructions, calling into question their independence and impartiality.[48] On the other hand, China highlights that countries with differing cultural backgrounds often have different understandings of arbitrators' conflicts of interest issues, so it is necessary to further clarify the specific connotation of such conflicts.[49] Last but not least, China calls for greater participation of experts from developing countries as investment arbitration lawyers and arbitrators comprise only a very small pool of experts.[50]

However, China was not specific about the reform proposals it is prepared to support. For instance, at UNCITRAL WGIII, general support was expressed for developing a code of conduct for ISDS tribunal members. For this purpose, the ICSID and UNCITRAL have prepared jointly a draft code of conduct.[51] On how to address the question of 'double hatting', three options were proposed: an absolute ex-ante prohibition, putting certain limitations on double hatting based on specific criteria, and extensive disclosure of the concurrent roles combined with the possibility of challenge.[52] It is not clear which option China prefers, other than stating that something should be done to regulate double hatting.

Fourth, China reaffirms its commitment to alternative means of dispute settlement, including a mandatory three to six month pre-arbitration consultation procedure. In China's view, alternative procedures can help the parties to achieve mutually beneficial results as well as avoid lengthy arbitration proceedings and high litigation costs.[53] Chinese culture plays an important role in shaping China's preference for consultation and mediation mechanisms in ISDS.[54] China's deeply rooted Confucian philosophy emphasises harmony and conflict avoidance and sees that the optimal resolution of disputes should be achieved not by the exercise of legal power but by moral persuasion.[55] As a cultural predisposition, Chinese investors usually prefer non-adversarial methods to resolve their disputes with host states. This cultural preference partially explains why Chinese investors have initiated only a small number of investment arbitration cases despite the fact that Chinese overseas investment often encounters legal, political and economic difficulties in host states.[56]

At UNCITRAL WGIII, Submissions from states underline the need to further explore mediation, conciliation and other alternative dispute resolution methods to prevent and reduce the occurrence of investor-state disputes. Nearly all submissions referring to alternative dispute resolution methods highlight that their use is less time and cost intensive than arbitration. They are considered as offering a high degree of flexibility and autonomy to host states and investors, allowing the parties to adopt creative and forward-looking methods to promote the settlement of

[46]Submission from China (n 8) 5.
[47]Ibid.
[48]Malcolm Langford, Daniel Behn & Runar Hilleren Lie, 'The Revolving Door in International Investment Arbitration' (2017) 20 Journal of International Economic Law 301, 328.
[49]Submission from China (n 8) 5.
[50]Ibid, at 3.
[51]Note by the Secretariat, 'Possible Reform of ISDS: Draft Code of Conduct', A/CN.9/WG.III/WP.209 (15 September 2021) 2.
[52]Ibid, at 7–8.
[53]Submission from China (n 8) 5. This stands in contrast to the Government of Indonesia's proposal for mandatory mediation to prevent a dispute from escalating into a legal dispute. See Note by the Secretariat, 'Possible Reform of ISDS: Comments by the Government of Indonesia', A/CN.9/WG.III/WP.156 (9 November 2018) paras. 19–20.
[54]Danny McFadden, 'The Growing Importance of Regional Mediation Centers in Asia' in Catharina Titi and Katia Fach Gómez (eds), *Mediation in International Commercial and Investment Disputes* (OUP 2019) 160–181.
[55]Xue Hanqin, 'Cultural Element in International Law', Melland Schill Lecture at University of Manchester (5 May 2016) 12–13.
[56]Guiguuo Wang, 'Chinese Mechanisms for Resolving Investor-State Disputes' (2011) 1 (1) Jindal Journal of International Affairs 204, 222–223.

investment disputes while maintaining long-term cooperative relationships.[57] The integration of mediation or conciliation into the ISDS system has become more frequent in IIAs. For example, out of 2572 BITs, 624 provide for mediation or conciliation procedures, accounting for twenty-four percent of all BITs.[58] The rules on mediation and other alternative dispute resolution methods that could be applied in ISDS have been developed in ICSID, UNCITRAL, ICC and SCC. Still, alternative dispute resolution methods were rarely used in practice.[59]

Fifth, China supports the regulation of third-party funding. Recent years have seen significant increases in the number of third-party funded ISDS cases. In such cases, investors turned to third-party funders who would pay the expenses incurred in pursuing the claim and enforcing the arbitral award in exchange for a share of the eventual financial award and influence over case management.[60] There are serious concerns about the impact of third-party funding on the arbitral proceedings, on investors' incentives, on respondent states' exposure, liability, and responses to ISDS claims, and on the investment law system itself.[61] However, in many cases third-party funding remains largely unregulated both in the IIAs and under applicable arbitration rules.[62]

Though China views third-party funding as problematic, China is not in favor of an outright prohibition as proposed by South Africa and Morocco.[63] Instead, it supports the regulation of third-party funding in ISDS by imposing transparency obligations on the parties. Specifically, China suggests that the parties disclose related funding on a continuous basis, including the content of the funding contract or arrangement, and avoid direct or indirect conflicts of interests between arbitrators and third-party funders. The legal consequences of the relevant parties for failure to fulfil their disclosure obligations should also be clarified.[64]

2.2 | Locating China's position in competing ISDS reform proposals

To better understand China's position on ISDS reform, it is useful to provide a brief overview of competing ISDS reform proposals made by other states and situate the Chinese submission in this broader context. Roberts has identified three main camps that have emerged with distinct proposals at UNCITRAL WGIII: incrementalists, systemic reformers and paradigm shifters.[65] The main supporters of an incremental reform of the current ISDS system are Japan and to some extent the United States.[66] This camp favours the retention of the ISDS system and downplays the criticisms levelled at it as perceptions rather than reality.[67] Even though they recognise that there are some outstanding problems to be addressed, incrementalists prefer to adopt small to moderate adjustments and more targeted reforms as opposed to systematic reforms. For example, incrementalists view the problem of inconsistent awards from *ad hoc* tribunals either as a natural and positive consequence of the bilateral nature of BITs or something that can be rectified by adopting more precise and detailed treaty language or authoritative interpretations.[68] The typical example of an incremental approach to ISDS reform is the CPTPP.

The CPTPP allows investors to resort to ISDS without prior recourse to domestic courts.[69] However, the CPTPP defines more precisely the contours of contracting parties' obligations, such as fair and equitable treatment and

[57]Note by the Secretariat, 'Possible reform of ISDS Dispute prevention and mitigation - Means of alternative dispute resolution', A/CN.9/WG.III/WP.190 (15 January 2020) 9. For a comprehensive analysis of mediation in international commercial and investment disputes, see Titi and Gómez (eds) (n 54).
[58]Kun Fan, 'Mediation of Investor-State Disputes: A Treaty Survey' (2020) Journal of Dispute Resolution 327, 331.
[59]Note by the Secretariat (n 57) 10–11.
[60]ICCA-Queen Mary Task Force, 'Third Party Funding in Investor-State Dispute Settlement Draft Report' (17 October 2017) 2.
[61]Brooke Guven and Lise Johnson, 'The Policy Implications of Third-Party Funding in Investor-State Dispute Settlement' (Columbia Centre on Sustainable Investment Working Paper 2019) 1.
[62]Eric De Brabandere, 'Mercantile Adventurers? The Disclosure of Third-Party Funding in Investment Treaty Arbitration' in Willem H. van Boom (ed), *Litigation, Costs, Funding and Behavior: Implications for the Law* (Routledge 2017) 127–128.
[63]Note by the Secretariat, 'Possible reform of ISDS: Third-party Funding: Possible Solutions', A/CN.9/WG.III/WP.172 (2 August 2019) 5–6.
[64]Submission from China (n 8) 5.
[65]Roberts (n 16) 410.
[66]Yuka Fukunaga, 'ISDS under the CPTPP and Beyond: Japanese Perspectives', Kluwer Arbitration Blog (30 May 2018).
[67]Anthea Roberts & Zeineb Bouraoui, 'UNCTIRAL and ISDS Reform: What are States' concerns?' EJIL:TALK! (5 June 2018) <https://www.ejiltalk.org/uncitral-and-isds-reforms-what-are-states-concerns/>.
[68]Ibid.
[69]Article 9.19 (1) of the CPTPP.

indirect expropriation, in an attempt to eliminate the likelihood of successful challenges to non-discriminatory public welfare measures.[70] The CPTPP also put restrictions on the types of claims that can be submitted to ISDS. These exceptions cover important policy areas such as tobacco control measures and authorisation of foreign investment to ensure that these sensitive issues are not subject to review by arbitral tribunals. Moreover, the CPTPP addresses perceived legitimacy concerns that arise from the double hatting problem of arbitrators. On 19 January 2019, the Commission of the CPTPP endorsed a decision on the Code of Conduct for Investor–State Dispute Settlement Proceedings, requiring *inter alia* that an arbitrator, upon selection, shall refrain for the duration of the proceedings from acting as counsel or party-appointed expert or witness in any pending or new investment dispute under the CPTPP Investment Chapter or any other international agreement.[71] Finally, largely operating under the traditional ISDS framework, the CPTPP does not even pursue the creation of an appeals facility.[72] Thus the CPTPP has addressed current concerns about the ISDS in an 'evolutionary' rather than a 'revolutionary' manner.[73]

Systemic reformers move further compared to incrementalists. They see merit in retaining the ISDS based on its oft-repeated advantages. However, systemic reformers view the current ISDS as seriously flawed and push for systematic and structural reforms.[74] The most vocal advocate for this camp is the EU. In 2015, the European Commission proposed the establishment of an ICS to replace the traditional ISDS system within the context of the negotiation of an FTA with the United States. The novel ICS retains the standing of private investors to file claims directly against states, but it effectively creates a permanent tribunal of first instance and an appellate tribunal with full-time adjudicators having fixed terms, paid a regular salary, and appointed to hear the case on a random basis.[75] The new model was designed to respond to the criticisms that party-appointed, *ad hoc* arbitrators make investment arbitration insufficiently accountable to democratic institutions by moving away from appointment by the disputing parties to ensure independence and impartiality of arbitrators. Viewing a standing two-tier court mechanism as the only available option that effectively responds to all the concerns about the traditional ISDS model, the EU later incorporated the ICS in some recent FTAs and described it as an important first step towards the EU's ultimate goal of establishing a MIC.[76]

Paradigm shifters hold the most critical view of the ISDS system, dismissing the current system as irrevocably flawed and arguing for a fundamental overhaul. In practice, they advocate going back to the past before the existence of ISDS. For example, Brazil championed in a series of Cooperation and Investment Facilitation Agreements the establishment of one 'Focal Point' or 'ombudsman' for each party and one Joint Committee composed of both parties to the IIA. Focal Points are domestic governmental institutions that are mandated to hear foreign investors' complaints, with the aim of preventing the emergence of formal disputes between investors and host states. When Focal Points are unsuccessful, the disputes will be referred to the Joint Committee, who shall examine the dispute and issue a public report with its recommendations. If the dispute persists, the aggrieved party may initiate a state-to-state arbitration.[77] South Africa terminated most of its BITs and adopted domestic legislation permitting foreign investors to sue in domestic courts or bringing mediation claims against the host government. If a dispute cannot be resolved, the government may later consent to state-to-state arbitration.[78]

[70]Article 9.6 and Annex 9-B of the CPTPP; Caroline Henckels, 'Protecting Regulatory Autonomy through Greater Precision in Investment Treaties: The TPP, CETA and TTIP' (2016) 19 Journal of International Economic Law 27, 33–43.

[71]Article 3 (d), Code of Conduct for Investor-State Dispute Settlement under Chapter 9 Section B of the CPTPP.

[72]Article 9.23 (11) of the CPTPP.

[73]Lars Markert et al, 'The Investment Treaty Arbitration Review: The Comprehensive and Progressive Agreement for Trans-Pacific Partnership' (25 June 2020) <https://thelawreviews.co.uk/title/the-investment-treaty-arbitration-review/the-comprehensive-and-progressive-agreement-for-trans-pacific-partnership>.

[74]Submission from the EU (n 17) para 2.4.

[75]Catharina Titi, 'The European Union's Proposal for an International Investment Court: Significance, Innovations and Challenges Ahead' (2017) TDM 1, 9–16; Marc Bungenberg and August Reinisch, *From Bilateral arbitral Tribunals and Investment Courts to a Multilateral Investment Court* (Springer 2020) 29–115.

[76]European Commission, 'European Commission Proposes Signature and Conclusion of EU-Canada Trade Deal' Press Release (Brussels, 5 July 2016).

[77]Geraldo Vidigal and Beatriz Stevens, 'Brazil's New Model of Dispute Settlement for Investment: Return to the Past or Alternative for the Future?' (2018) 19 Journal of World Investment and Trade 475, 487–489.

[78]Roberts (n 16) 417.

2.3 | China's open, flexible and evolving approach

Where does China stand on ISDS reform? By recognising the important value of ISDS, China distances itself from countries such as Brazil and South Africa that call for a paradigm shift in ISDS reform. However, it is challenging to put China in the camp of either incrementalist or systemic reformers. On the one hand, China has pointed out structural problems of the *ad hoc* ISDS system and prefers a comprehensive reform, including the establishment of an appellate mechanism. On the other hand, China does not go so far as to endorsing the EU's two-tier permanent MIC proposal and prefers to retain the investors' right to appoint arbitrators. It is probably fair to describe China's position on ISDS reform as a 'middle-of-the-road' approach. China adopts a reformist approach to ISDS, takes into account the positions taken by other parties, and refrains from advocating radical changes to existing ISDS institutions. China's approach to ISDS reform is likely to represent the majority states' views at UNCITRAL WGIII. For example, the establishment of an appeal mechanism advocated by China is more likely to be accepted by the international community than the EU's proposal of creating a MIC. This is in part because the proposal for a MIC presently envisages giving little role to investors in appointing a first instance tribunal. In comparison, an appeal mechanism supported by China would allow the parties to continue selecting their trusted arbitrators for the tribunal of first instance, while ensuring consistency and predictability of the ISDS system.[79]

It is important to stress that China has to date only outlined a few broad guidelines on ISDS reform. China has *not* expressed clear views on specific reform options that have emerged from the UNCITRAL WGIII deliberations.[80] China's reticence about *how* to establish an appeal facility and whether China wants ex-ante prohibition or regulation of the 'double hatting' question, as discussed in section 2.1 above, are just some examples. Moreover, ISDS reform proposals keep evolving. For instance, the EU has recently suggested an 'open architecture', i.e., building a certain level of flexibility into its MIC proposal.[81] It is therefore better to view China's approach to ISDS reform not as static, but as an open, flexible, and evolving process. Indeed, in its UNCITRL submission, China explicitly states that it is 'open to possible proposals for improving the ISDS mechanism'.[82]

China's flexible approach to ISDS reform is also reflected in its treaty-making practices after the UNCITRAL submission in 2019. To start with, in the Regional Comprehensive Economic Partnership (RCEP) that China concluded with 14 member countries in November 2020, an all-purpose state to state dispute settlement mechanism is provided. If a party to the RCEP breaches any of its obligations under the RCEP, the investor would need to request its home state to bring a claim against the host state.[83] The conclusion of the RCEP clearly shows that, even if China prefers the inclusion of ISDS provisions in FTAs, China might not insist on it. Furthermore, China's CPTPP application announced in September 2021 shows that China can accept an ISDS without an appellate mechanism. It should also be highlighted that China is not alone in adopting such an open and flexible approach to ISDS reform. Similar positions are taken by other countries such as Canada, Mexico, and Singapore.[84] That China's approach to ISDS is highly flexible is an important point, as it opens space to discuss the probability of China supporting certain ISDS reform proposals, such as the EU's MIC proposal, in the future. The question will be further explored in Part 4 below. Before that, it is useful to highlight that China's approach to ISDS reform is profoundly shaped by a range of contextual factors.

[79]Margie-Lys Jaime, 'A New Legal Framework for Improving Investor-State Dispute Settlement (ISDS)' in Loic Cadiet et al (eds), *Privatizing Dispute Resolution: Trends and Limits* 483 (Nomos 2019) 531–532.
[80]Gómez (n 11) 60.
[81]Submission from the EU (n 17) para 3.16.
[82]Submission from China (n 8) 6.
[83]Chapter 19 of the RCEP.
[84]For example, these three countries have signed with the EU FTAs which provide two-tier ICS but are also members of CPTPP with traditional ISDS clauses.

3 | A CONTEXTUAL ANALYSIS OF CHINA'S APPROACH TOWARDS ISDS REFORM

3.1 | ISDS clauses in three generations of Chinese BITs

Based on the scope of consent to ISDS provisions, Chinese BITs may be categorised into three generations. Signed from the early 1980s to the late 1990s, China's first- generation BITs provide either no ISDS provisions at all or a narrowly constructed ISDS clause that only admits 'the amount of compensation for expropriation' to arbitration. Two factors may explain China's conservative attitude towards ISDS during the period. First, skeptical of international dispute resolution mechanisms as Western biased after a long isolation from the international community, China perceived the acceptance of the jurisdiction of international arbitral tribunals as inconsistent with the sacred notion of sovereign independence.[85] Second, being a capital-importing country with scarce overseas foreign investment at the time, it would be in China's interest to retain the adjudicative prerogatives within Chinese domestic courts in settling disputes with foreign investors.[86]

China deposited its instruments of ratification of the Convention for the Settlement of Investment Disputes Between States and Nationals of Other States (ICSID Convention) on 7 January 1993. The accession to the ICSID Convention was hailed as one of the milestones in China' engagement with mechanisms of international adjudication as China for the first time accepted the possibility of submitting disputes over its sovereign actions to the jurisdiction of a third-party arbitration system.[87] Nevertheless, as a reflection of China's wary approach to ISDS, China limited the scope of its consent to ICSID's jurisdiction with a declaration under Article 25 (4) of the ICSID Convention that 'the Chinese Government would only consider submitting to the jurisdiction of the ICSID disputes over compensation resulting from expropriation and nationalisation.'[88]

The second generation of Chinese BITs since 1998 to 2011 were characterised by unobstructed access to ISDS clauses.[89] In contrast to the narrowly constructed ISDS clauses in the first generation BITs, ISDS provisions in the second generation Chinese BITs feature the adoption of an extended and liberal access to international arbitration, which usually stipulate that '*any dispute* concerning an investment between an investor of one Contracting Party and the other Contracting Party can be submitted unconditionally at the request of the investor concerned either to the ICISD or an ad hoc arbitral tribunal.'[90] This drastic policy shift towards liberal ISDS provisions is explained by China's changed status to become a capital-exporting country, particularly in developing countries.[91] Deeply integrated into the global economy, China was no longer a mere capital-importing country and the protection of its overseas investment against risks through BITs has become an important policy prerogative. It is no coincidence that out of the 46 second generation Chinese BITs, 37 signatory states are developing countries located in Africa, South East Asia and Latin America, which are commonly considered as capital importing countries.[92]

The emergence of China's second generation BITs with liberal ISDS clauses raise the question of the legal effects of China's declaration concerning classes of disputes when acceding to the ICSID in 1993. Would China's declaration mean that the unconditional consent given in the second generation BITs is only valid to the extent that it does not conflict with the declaration? Some commentators believe so, arguing that China's declaration constitutes a

[85]Kong Qingjiang, 'Bilateral Investment Treaties: The Chinese Approach and Practice', 8 Asian Yearbook of International Law (1998/1999) 105.
[86]Chi Manjiao and Wang Xi, 'The Evolution of ISA Clauses in Chinese IIAs and its Practical Implications: The Admissibility of Disputes for Investor-State Arbitration' (2015) 16 The Journal of World Investment and Trade 869, 874.
[87]Julian G. Ku, 'Enforcement of ICSID Awards in the People's Republic of China' (2013) 6 Contemporary Asia Arbitration Journal 31, 34.
[88]Notifications Concerning Classes of Disputes Considered Suitable or Unsuitable for Submission to the Centre (7 January 1993) <https://icsid.worldbank.org/sites/default/files/2020_July_ICSID_8_ENG.pdf>.
[89]Norah Gallagher and Wenhua Shan, *Chinese Investment Treaties: Policies and Practice* (OUP 2009) 41–42.
[90]For example, Article 10(3) of China-Germany BIT (2003) and Article 10(3) of China-Netherlands BIT (2001).
[91]Ka Zeng, 'Understanding the Institutional Variation in China's Bilateral Investment Treaties (BITs): the Complex Interplay of Domestic and International influences' (2016) 25 Journal of Contemporary China 97, 112; Cai Congyan, 'Outward Foreign Direct Investment Protection and the Effectiveness of Chinese BIT Practice' (2006) 7 The Journal of World Investment and Trade 621, 646.
[92]Li and Bian (n 7) 516.

reservation and that China's acceptance of the ICSID jurisdiction is limited to investment disputes over compensation resulting from expropriation and nationalisation.[93] The prevailing view, however, is that the legal nature of China's ICSID declaration is not a reservation but for information purposes only. Article 25(4) of the ICSID Convention allows that 'any Contracting State may, at the time of ratification, acceptance of 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.' At the same time, Article 25 (4) makes it clear that 'such notification shall not constitute the consent required by Article 25 (1)'. Since a state's consent to jurisdiction in accordance with Article 25 (1) of the ICSID Convention, in addition to the ratification of the ICSID Convention, is a condition for an ISCID arbitral tribunal to have personal jurisdiction over the state, any declaration the state makes under Article 25(4) has no direct legal consequences. An ISCID contracting state is therefore free at any moment to accept the jurisdiction of the ICSID for all investment disputes.[94] This is exactly what China has done in its second and third generations of BITs.

As part of a move in the international investment regime to reformulate IIAs aiming to recalibrate the relationship between the level of protection for foreign investors and the policy space of host states, China has begun to conclude the third generation BITs since the China-Canada BIT in 2012.[95] In comparison with the unobstructed access to ISDS in the second-generation BITs, the third generation Chinese BITs have adopted a more balanced approach. To begin with, procedural pre-requisites are added that aim to discourage abuse of rights by foreign investors. In addition, exceptions and a variety of exclusions are stipulated to constrain the arbitral tribunal's jurisdictional outreach and to ensure that it is not unlimited or overly expansive.[96] For instance, in the China-Canada BIT, only breaches of specific provisions which cause a loss or damage to investors are admissible to arbitration.[97] At the same time, specific provisions in the BIT such as prudential measures in the financial sector, initial approval of an investment that is subject to review, investment permit that is subject to national security review, and taxation measures are explicitly excluded from the application of ISDS clauses.[98]

The developmental trajectory of China's approach to the ISDS system makes it plain that allowing foreign investors access to ISDS has been a standard feature of Chinese BITs for two decades. China is now deeply engaged and intertwined with ICSID and other mechanisms of investment protection and investor-state arbitration. China views ISDS as an important mechanism to promote cross-border investment flows and the rule of law in international investment governance.[99]

3.2 | China's limited experience with ISDS

For some time, international investment lawyers have been debating the puzzle of the so-called 'China disequilibrium' in international investment arbitration. Despite the fact that China is a signatory of almost 150 IIAs in which comprehensive ISDS procedures are a common feature, there are only a few investor-state investment disputes involving the Chinese government, Chinese investors or Chinese BITs.[100] But the "China disequilibrium" is fast disappearing. According to public records, the Chinese government is at present the respondent in four pending

[93]Mark A. Cymrot, 'Investment Disputes with China' (2006) 61 Dispute Resolution Journal 80, 82.
[94]Monika C.E.Heymann, 'International Law and the Settlement of Investment Disputes Relating to China' (2008) 11 (3) Journal of International Economic Law 507, 517–518.
[95]Axel Berger, 'Hesitant Embrace: China's Recent Approach to International Investment Rule-making' (2015) 16 The Journal of International Investment and Trade 843, 850.
[96]Sonia E. Rolland and David M. Trubek, *Emerging Powers in the International Economic Order* (CUP, 2019) 104–107.
[97]Article 20.1 of the China- Canada BIT.
[98]Articles 14, 33 and Annex D.34 of the China- Canada BIT.
[99]Qingjiang Kong and Kaiyuan Chen, 'ISDS Reform in the Context of China's IIAs' (2021) 36 (3) ICSID Review 617, 627–629; Guiguo Wang, 'China's Practice in International Investment Law: From Participation to Leadership in the World Economy' (2009) 34 Yale Journal of International Law 575, 584.
[100]Wei Shen, 'Guarding the Great Wall? Jurisprudential Review of Treaty Interpretative Tools in Chinese BIT-Based Arbitration Cases' (2021) 37 (1) Arbitration International 239, 240.

investor-state disputes. In total, there are nine reported cases against the Chinese government by June 2023 among which eight are concerned with China's first-generation BITs (See Appendix Table 1). Concurrently, Chinese investors have become increasingly active in using ISDS to protect their overseas investment. They are at present claimants in ten pending investor-state disputes. In total, Chinese investors have launched 22 cases before the ICSID and other international arbitration forums by June 2023 (See Appendix Table 2).

Several reasons were offered to explain the Chinese Government's absence from investment arbitration.[101] One explanation is that the Chinese government has always appreciated the important role of foreign investment in Chinese economic development and offered sufficient investment protection to foreign investors.[102] For example, China used to accord foreign investors superior national treatment in the sense that they enjoyed even more favorable treatment when compared with Chinese domestic enterprises in terms of tax rate and other conditions of competition.[103] Therefore, the risk of the Chinese government violating BIT obligations is very low. Opposite to this optimistic explanation, a competing argument holds essentially that a dearth of ISDS claims against China is precisely due to the lack of the rule of law in China. Foreign investors may fear that their ISDS claim could jeopardise their relationship with the Chinese government and in turn put their business dealings in China at risk. By contrast, foreign investors may gain more from non-adversarial means such as negotiation and mediation to resolve their disputes with the Chinese government in view of its preference to settle disputes informally. Initiating arbitration against the Chinese government is therefore only the last resort.[104] Yet another school of thought attributes the low utility rate of Chinese BITs to the fact that early Chinese BITs often incorporate restrictive terms of investor, investment, and fork-in-the road, mandatory administrative review procedures, temporary jurisdictional limitations among others with the practical effect of discouraging foreign investors from initiating ISDS against China.[105]

A careful analysis of China-related ISDS arbitral awards up to date, including both Chinese investors as claimants against foreign states and cases by foreign investors against the Chinese government, shows that most of the arbitral awards were ruled in China's favor. First, it was confirmed that Chinese state-owned enterprises (SOEs) are qualifying 'investors' capable of initiating ISDS proceedings against a host state under Chinese BITs.[106] In *BUCG v. Republic of Yemen*, one of the jurisdictional objections raised by Yemen was that BUCG, being an Chinese SOE, should not be regarded as a 'national of another Contracting State' as required by Article 25(1) of the ICSID Convention because 'it was under the direction and control of the Chinese government in carrying out its activities, and that it was empowered to exercise elements of governmental authority in China.'[107] The tribunal held that, notwithstanding the fact that BUCG was an SOE, the evidence demonstrated that the claimant was acting as a commercial contractor in carrying out the work and was neither an agent of the Chinese government nor fulfilling governmental functions.[108] The tribunal further found the assertion that the Chinese State is the ultimate decision maker for BUCG 'too remote to be relevant'.[109] Given that Chinese SOEs have played a significant role in China's overseas FDI,[110] the Chinese government welcomes this decision as it would afford Chinese SOEs direct access to ISDS to protect their interests

[101]Dae Un Hong & Ju Yoen Lee, 'Why Are There So Few Investor-State Arbitrations in China? A Comparison with Other East Asian Economies' (2018) China & WTO Review 35, 47–51.

[102]Yuqing Zhang, 'The Case of China' in Michael Moser (ed), *Investor-State Arbitration – Lessons for Asia* (Juris Publishing 2008) 159.

[103]Wenhua Shan, Norah Gallagher and Sheng Zhang, 'National Treatment for Foreign Investment in China: A Changing Landscape' (2012) 27 ICSID Review 120, 125–130.

[104]Leon E. Trakman, 'Geopolitics, China, and Investor-State Arbitration', in Lisa Toohey, Colin B. Picker and Jonathan Greenacre, *China in the International Economic Order* 268 (CUP 2015) 279.

[105]Fredrik Lindmark, Daniel Behn and Ole Kristian Fauchald, 'Explaining China's Relative Absence from Investment Treaty Arbitration' in Daniel Behn, Ole Kristian Fauchald and Malcolm Langford (eds), *The Legitimacy of Investment Arbitration: Empirical Perspectives* (CUP, 2022) 437–455.

[106]Ming Du, 'The Status of Chinese State-owned Enterprises in International Investment Arbitration: Much Ado about Nothing' (2021) 20 (4) Chinese Journal of International Law 785, 801–809.

[107]*Beijing Urban Construction Group Co., Ltd. (BUCG) v. Republic of Yemen*, ICSID Case NO. ARB/14/3, Decision on Jurisdiction (31 May 2017) para 29.

[108]Ibid, para 39.

[109]Ibid, para 43.

[110]Daniel Michaels, 'Behind China's Decade of European Deals, State Investors Evade Notice', Wall Street Journal (30 May 2020).

rather than recourse to traditional diplomatic protection. In fact, a growing number of Chinese SOEs have launched ISDS proceedings to protect their overseas investment.[111]

Second, the arbitral tribunals in disputes related to Chinese BITs have ruled consistently against the extension of the most-favoured nation (MFN) clause to procedural rights in ISDS. In *Ansung Housing Co., Ltd. v. China*, the Korean Ansung sought to invoke the MFN clause to save its claim from being time-barred as other Chinese BITs do not prescribe a three-year limitation period within which an investor is required to initiate an arbitration claim against the host state. Relying upon a plain reading of the MFN clause, the tribunal held that Ansung's claim was time-barred because the MFN clause did not extend to a state's consent to arbitrate with investors nor to the temporal limitation period for investor-state arbitration.[112] More recently, in *AsiaPhos Limited and Norwest Chemicals Pte Limited v. China*, the tribunal held that the expansion of an arbitration clause by virtue of an MFN clause requires the clear and unambiguous intention of both parties for the MFN clause to have this effect.[113] Again, these rulings are consistent with China's preference. Recent Chinese BITs have eliminated potential controversies over the scope of the MFN clause by making clear that the MFN treatment does not cover the procedural rights to dispute settlement.[114]

Granted, China has not always been content with investment arbitral tribunals' awards. One recurrent issue in China-related investment disputes is whether individuals or companies from Hong Kong and Macau may qualify as 'Chinese investor' protected by Chinese BITs under the 'one country, two systems' policy. The issue is further complicated by the fact that Hong Kong and Macau have their own independent IIAs with other countries. Two arbitral tribunals of *Tza Yap Shum v. Peru* and *Sanum v. Lao Republic* answered this question in the affirmative. The UNCITRAL award of *Sanum v. Lao Republic* was later annulled by the Singapore High Court, holding that Macau investors could not avail themselves of the China- Lao BIT because the BIT does not apply to Macau. Sanum later prevailed in its appeal against the Singapore High Court's decision before the Court of Appeal of Singapore (SGCA), Singapore's highest court.[115] Notably, even though the Lao Government produced formal diplomatic correspondence between itself and China in 2014 and 2015 expressing both governments' view that the China-Laos BIT is not applicable to Macau, the SGCA declined to place any weight on such evidence as it was adduced only after Sanum's commencement of the arbitration proceedings. The Chinese Ministry of Foreign Affairs reacted to the SGCA ruling by issuing a statement criticising the judgment and reiterating its position that only mainland Chinese investors are entitled to protection of Chinese BITs and that Hong Kong and Macau investors should not be allowed to take advantage of their Chinese nationality for such purposes.[116] Sanum and the Laos Government signed a binding settlement agreement in 2014. In 2017, Sanum reinstituted arbitration proceedings against the Laos government before ICSID, alleging that the respondent had breached the terms of the settlement.[117] More recently, two Hong Kong investors have launched ISDS proceedings against host states based on Chinese BITs.[118] It remains to be seen how the ICSID tribunals will respond to the issue.

The more problematic issue concerns China's first-generation BITs which limit international arbitration to disputes 'involving the amount of compensation for expropriation'.[119] The tribunals in *China Heilongjiang International Economic & Technical Cooperative Corp. et al., v. Mongolia*, *Beijing Everyway Traffic & Lightning Tech. Co., Ltd v. Ghana* and *AsiaPhos Limited v. China* adopted an extremely narrow construction of the provision. In the tribunal's view, the only arbitrable matter under the provision was the amount of compensation for an expropriation. The tribunal therefore lacked

[111] *China Machinery Engineering Corporation v. Republic of Trinidad and Tobago*, ICSID Case No. ARB/23/8 (April 6, 2023); *PowerChina Huadong Engineering Corporation and China Railway 18th Bureau Group Company Ltd. v. Socialist Republic of Vietnam*, ICSID Case No. ARB (AF)/22/7 (November 29, 2022).
[112] *Ansung Housing Co., Ltd. v. People's Republic of China*, ICSID Case No. ARB/14/25, Award (9 March 2017) para 115.
[113] *AsiaPhos Limited and Norwest Chemicals Pte Limited v. People's Republic of China*, ICSID Case No. ADM/21/1, Award (16 February 2023) paras 207–219.
[114] For example, Art. 139 (2) of the New Zealand–China Free Trade Agreement (2008).
[115] *Laos v Sanum* [2016] SGCA 100–121.
[116] Huawei Sun, 'Emerging Investment Treaty Arbitration Practice in China' (2018) 112 Proceedings of ASIL Annual Meeting 103, 104.
[117] *Sanum Investments Limited v. Lao People's Democratic Republic*, ICSID Case no. AHDOC/17/1 (April 14, 2017)
[118] *PCCW Cascade (Middle East) Ltd. v. Kingdom of Saudi Arabia*, ICSID Case No. ARB/22/20 (July 26, 2022); *Alpene Ltd v. Republic of Malta*, ICSID Case No. ARB/21/36 (July 2, 2021).
[119] For example, Art 13.3 of the China-Singapore BIT (1985) and Art 11.2 of the China-Japan BIT (1988).

jurisdiction with regard to other legal issues such as whether an expropriation had actually occurred.[120] By contrast, the tribunals in *Tza Yap Shum v. Peru*, *Sanum v. Laos* and *BUCG v. Yemen* adopted a diametrically opposite interpretation when faced with the same question. They found that a limitation of the ISDS clause solely over the amount of compensation for expropriation would deprive the clause of its *effect utile* because a host state could effectively avoid arbitration by simply denying that they had engaged in expropriation. Moreover, an investor who would have recourse to a competent national court to determine whether an expropriation had occurred would be precluded from submitting the dispute on the amount of compensation to international arbitration pursuant to the fork-in-the-road provision in relevant BITs, as a national court would have already determined the compensation.[121] A narrow interpretation of the restrictive ISDS clauses in Chinese BITs is a double-edged sword for China. Whilst it has shielded the Chinese government from scrutiny of the merits of foreign investors' claims in some disputes,[122] it has denied Chinese investors' access to ISDS on other occasions.[123]

On balance, different from other developing countries which are more likely to suffer net losses when getting involved in ISDS proceedings,[124] China has up to date rarely been a respondent in ISDS proceedings and never experienced firsthand the pains of 'losing face', i.e., being found to breach its international legal obligations to foreign investors and being ordered to divert public funds to compensate foreign investors' financial loss by an arbitral tribunal. China's limited but triumphant exposure to ISDS partially explains China's overall positive attitude towards ISDS. With China's position as the largest FDI destination in the world, there is little doubt that the number of investment disputes involving China will rise in the future. One may wonder how China will respond to an investment arbitral award if it finds itself on the losing end. After all, China traditionally took an extremely cautious attitude towards binding third-party international dispute settlement.[125] China also officially dismissed the rulings of the Permanent Court of International Arbitration in the South China Sea dispute as 'waste paper' and the arbitration a 'farce'.[126] Moreover, recent empirical studies demonstrate that whereas the majority of states have promptly complied with adverse investment arbitral awards, the instances of non-compliance and significantly delayed compliance have been rising since the 2000s.[127]

It is highly unlikely that China would completely turn its back on ISDS simply because it lost one or two cases before investment arbitral tribunals. It is increasingly clear that China has adopted a bifurcated approach to international dispute settlement. On the one hand, China is hostile to international adjudication and prefers political or diplomatic approaches when 'core interests', such as issues of sovereignty and territorial integrity, are at stake. On the other hand, China has embraced international adjudication to settle trade and investment disputes.[128] China has incorporated liberal ISDS clauses in its new generation of BITs and participated in a number of ICSID proceedings. The reputational cost and the negative signaling effects on FDI would be too high for China to openly renege on international commitments to foreign investors. Empirical studies have shown that the failure to comply with BIT obligations conveys negative information about a host country's behavior to the broader investment community, which could result in a sizable loss of future FDI into that country.[129] Given the important role of foreign investment to China's economic development and export success and growing consensus for 'de-risking' from China in Europe

[120]*China Heilongjiang International Economic and Technical Cooperative Corp. et al, v. Mongolia*, PCA Case No 2010–20, Award (30 June 2017) paras 435–454; *Beijing Everyway Traffic & Lighting Tech. Co., Ltd v. The Government of the Republic of Ghana*, PCA Case No 2021–15, Final Award on Jurisdiction (30 January 2023) paras 135–259.

[121]*Tza Yap Shum v. The Republic of Peru*, ICSID Case No ARB/07/6, Award (7 July 2011) para. 148; *Sanum Investments Limited v. Lao People's Democratic Republic*, PCA Case No 2013–13, Award on Jurisdiction (13 December 2013) paras 239–242; *BUCG v. Yemen* (n 112) paras 70–87.

[122]For example, *see AsiaPhos Limited v. China* (n 113) para 221. The arbitral tribunal found that it does not have jurisdiction over any of the claimant's claims.

[123]For example, *Beijing Everyway Traffic & Lighting Tech. Co., Ltd v. The Government of the Republic of Ghana* (n 120).

[124]Tim R. Samples, 'Winning and Losing in Investor-State Dispute Settlement' (2019) 56 (1) American Business Law Review 115, 163.

[125]Julian Ku, 'China and the Future of International Adjudication' (2012) 27 Maryland JIL (2012) 154, 158–160.

[126]Simon Denyer & Emily Rauhala, 'Beijing' Claims to South China Sea Rejected by International Tribunal', Washington Post (12 July 2016).

[127]Emmanuel Gaillard and Ilija Mitrev Penusliski, 'State Compliance with Investment Awards' (2020) 35 (3) ICSID Review 540, 593.

[128]Yayezi Hao and Ignacio de la Rasill, 'China and International Adjudication – Picking up Steam?' (2021) 12 Journal of International Dispute Settlement 637, 639–658.

[129]Todd Allee and Clint Peinhardt, 'Contingent Credibility: The Impact of Investment Treaty Violations on Foreign Direct Investment' (2011) 65 International Organization 401, 402.

and elsewhere,[130] China may find it more advantageous to comply with an adverse arbitral award or seek to settle with the aggrieved foreign investor.

Although China may initially choose to comply with a small number of adverse ISDS awards, it is almost certain that repeated loss in ISDS proceedings would have a serious impact on China's attitude toward ISDS as well as the design and content of China's juggernaut BIT regime, as was the case in other developing countries such as Brazil and India. The first adverse arbitral award against the government of India in the case of *White Industries* in 2011 prompted public outcry and led to a complete review of the country's BITs. India adopted a new model BIT that, while it incorporates ISDS, conditions its use on the initial pursuit of remedies before domestic courts for at least five years.[131] Likewise, due to various arbitral proceedings initiated against it, the Republic of South Africa expressly stated that it needed to do damage control and excluded ISDS from BITs.[132]

3.3 | China's 'Go Global' strategy and the Belt & Road Initiative

As an essential part of its government-directed development model, China has adopted a government-mandated 'Go Global' policy since 2000. The essence of the 'Go Global' policy is to promote the international operations of capable Chinese firms through outbound direct investment (ODI) with a view to enhancing their international competitiveness.[133] This policy has been very successful, with the world witnessing a dramatic increase in Chinese ODI and an even larger potential for growth. In 2022, China's ODI posted a year-on-year increase of 5.2 percent, reaching US $145 billion.[134]

With the introduction of China's ambitious Belt and Road Initiative (BRI), Chinese ODI has reached a new level. As one of the most ambitious infrastructure projects ever conceived, the BRI includes a vast network of railways, energy pipelines, highways and streamlined border crossings both westward and southward, as well as invests in port development along the Indian Ocean, from Southeast Asia all the way to East Africa.[135] In 2022, despite the impact of covid-19 pandemic, Chinese ODI in BRI countries stood at US$67.8 billion, compared to USD 68.7 billion in 2021. The BRI has resulted in US$962 billion worth of ODI in total from its inception in 2013 to 2022.[136]

Despite all the rhetoric, China's BRI represents an inherently risky endeavor given the severe political instability and the lack of rule of law in many countries expected to participate in the BRI.[137] Many BRI countries perform poorly in the World Bank's Doing Business and Rule of Law rankings.[138] Some of them, such as Czechia, Poland, Egypt, and Russia, are among the most frequent respondents in ISDS proceedings.[139] Consequently, the protection of China's ODI from investment risks in BRI countries figures prominently in the Chinese government's approach to BIT negotiations. In particular, Chinese investors may increasingly fall back on ISDS mechanisms in Chinese BITs, which promise to provide them with an enforceable procedural remedy against infringing host states.[140] Public records show that at least seven mainland Chinese investors have brought ISDS claims against host states since 2020.[141] The advantages of ISDS in 'delocalising' investment disputes by affording foreign investors an alternative

[130]Speech by President von der Leyen at the European Parliament Plenary on the Need for a Coherent Strategy for EU-China Relations (18 April 2023) <https://ec.europa.eu/commission/presscorner/detail/en/speech_23_2333>; G7 Hiroshima Leaders' Communiqué (May 20, 2023) para. 51 <https://www.whitehouse.gov/briefing-room/statements-releases/2023/05/20/g7-hiroshima-leaders-communique/>.

[131]Grant Hanessian & Kabir Duggal, 'The 2015 India Model BIT: Is This the Change the World Wishes to See?' (2017) 32(1) ICSID Review 216, 221–225.

[132]Engela C. Schlemmer, 'An Overview of South Africa's Bilateral Investment Treaties and Investment Policy' (2016) 31(1) ICSID Review 167, 185–188.

[133]Wayne M. Morrison, 'China's Economic Rise', Congressional Research Service (25 June 2019) 17–18.

[134]The State Council of the PRC, 'China's Outbound Direct Investment Rises 5.2% to $145b', <https://english.www.gov.cn/archive/statistics/202302/10/content_WS63e5fdd8c6d0a757729e69d3.html>.

[135]Andrew Chatzky and James McBride, 'China's Massive Belt and Road Initiative Backgrounder', Council on Foreign Relations Report (2 February 2023).

[136]Christoph Nedopil, *China Belt and Road Initiative (BRI) Investment Report 2022*, Green Finance & Development Centre, Fudan University (January 2023).

[137]Matthew Erie, 'Chinese Law and Development' (2021) 62 (1) Harvard International Law Journal 51, 78–84.

[138]On critique of the use of such rankings, see Kevin Davis et al (eds), *Governance by Indicators: Global Power through Quantification and Rankings* (OUP, 2012).

[139]UNCTAD Investment Policy Hub <https://investmentpolicy.unctad.org/investment-dispute-settlement>.

[140]Dilini Pathirana, 'Making an Arbitration Claim under Chinese BITs: Some Inferences from Recent ISDS Cases' (2017) 5(2) The Chinese Journal of Comparative Law 420, 422.

[141]See Appendix Table 2.

to domestic courts, and in 'depoliticising' investment disputes by removing them from the realm of diplomatic protection, have long been acknowledged.[142] For decades, ISDS has been the preferred means for capital exporting countries to protect the interests of their investors and to enforce the terms of investment agreements. Likewise, strong ISDS clauses have been found to have positive effects on capital importing countries to attract inbound FDI flows.[143] Therefore, a fair, efficient and transparent ISDS mechanism at either global, regional or bilateral level is in China's interest as both a major capital exporting and capital importing country.

In an effort to support the BRI, China has reformed domestic arbitral institutions, such as the Shenzhen Court of International Arbitration (SCIA) and the China International Economic Trade Arbitration Commission (CIETAC), by extending their competence from commercial disputes to include investor-state investment disputes. In addition, China is building joint arbitration centres to resolve investor-state and commercial disputes with other regions, such as the China-Africa Joint Arbitration Center (CAJAC).[144] China's new arbitral mechanisms for investor-state disputes may be a response to the perceived deficiencies of existing ISDS mechanisms. They could operate as trial runs for China's preferred ISDS reforms, such as a bigger role for mediation and reducing time and costs of ISDS proceedings. More important, China's reforms are an attempt to break the monopoly of existing Western-dominated investment arbitral institutions.[145]

Although China's ambitions are legitimate, one may wonder if the development of China-led arbitration mechanisms will not conflict with China's asserted preference for a multilateral approach to ISDS reform. One way to understand China's move is that China prefers a multilateral approach to reform ISDS procedures, but not necessarily the dominance of Western arbitral institutions. Why, for example, a BRI dispute between a Chinese investor and another Asian or African state should be arbitrated in Washington D.C. or the Hague rather than Beijing? Alternatively, China's development of new arbitral mechanisms may be understood as a pragmatic move because, as a practical matter, no single model of ISDS will wholly replace all other alternatives at UNCITRAL WGIII negotiations.[146] This is simply another example of how China oscillates between the idealistic vision that all differences between countries could be settled by consultation and negotiation and the realistic vision that it should act proactively, sometimes even unilaterally, to shape global norms.[147] It remains to be seen how these new arbitral institutions will play out as no investor-state dispute has been submitted to them to date.

4 | THE FUTURE OF ISDS IN THE CAI

On 30 December 2020, the EU and China reached an agreement in principle on CAI, after thirty-five rounds of intense negotiations which lasted seven years. The EU's general objective for the CAI was to use the exclusive competence for foreign direct investment it gained after the Lisbon Treaty to modernise and replace the BITs all EU Member States except Ireland concluded with China with a single EU-China CAI.[148] The EU's specific objectives, among others, were to provide for new opportunities and improved conditions for access to the Chinese markets for

[142]Gabrielle Kaufmann- Kohler and Michele Potesta, *Investor-State Dispute Settlement and National Courts: Current Framework and Reform Options* (Springer 2020) 17–21.

[143]Asian Development Bank, 'ASEAN Economic Integration Report 2016: What Drives Foreign Direct Investment in Asia and the Pacific' (2016) 163. On contrary findings, see Jason Yackee, 'Bilateral Investment Treaties, Credible Commitment, and the Rule of (International) Law: Do BITs Promote Foreign Direct Investment' (2008) 42 Law & Society Review 805, 827–828.

[144]Huiping Chen, 'China's Innovative ISDS Mechanisms and Their Implications' (2018) 112 AJIL Unbound 207, 207–208. Different from arbitral institutions, the newly created China International Commercial Courts (CICC) in Shenzhen and Xi'an have no jurisdiction on investor-state disputes. See Weixia Gu and Jacky Tam, 'The Global Rise of International Commercial Courts: Typology and Power Dynamics' (2021) 22 (2) Chicago JIL 443, 479–482.

[145]Chen, Ibid, 210–211.

[146]Alvarez (n 32) 254.

[147]On China's romantic and realist perceptions of international law, see M Sornarajah and Jiangyu Wang, 'China, India, and International Law: A Justice Based Vision Between the Romantic and Realist Perceptions' (2019) 9 Asian Journal of International Law 217, 249.

[148]Although the EU has exclusive competence to conclude investment agreements, ISDS provisions fall within the shared competence between the EU and the Member States. See European Court of Justice, Opinion 2/15 of the Court (16 May 2017).

EU investors; establish guarantees regarding the treatment of EU investors in China; support sustainable development initiatives by encouraging responsible investment and promoting core environmental and labour standards, and allow for the effective enforcement of commitments through investment dispute settlement mechanisms. To what extent the CAI serves the EU's economic and strategic interests in view of the alleged recycled market access commitments, China's human rights policy and the implications for the transatlantic relationship was fiercely debated.[149] Shortly after the agreement in principle, the trajectory of the CAI was pivotally reshaped by China-EU tit-for-tat sanctions over alleged human rights violations in Xinjiang. Members of the European Parliament voted overwhelmingly on 20 May 2021 in support of freezing the legislative process for ratifying the CAI until Beijing lifts the sanctions against members of the European Parliament.[150] Despite Beijing's efforts to revive the CAI, including extending an olive branch by suggesting China and the EU simultaneously removing sanctions and following through on its promise in the CAI to ratify ILO conventions on forced labour, a steep rise in strategic mistrust in the EU concerning China's human rights violations, coercive trade practices, the China-Russia relationship, among other things, have cast a long shadow on the future of the CAI.[151]

The originally envisaged 'comprehensive' China-EU BIT has not been fully completed since the CAI does not cover substantive standards of investment protection, nor does it include any ISDS clauses. In the final text, China and the EU only agreed to a detailed state to state dispute settlement system, coupled with a monitoring mechanism at pre-litigation phase established at political level to ensure effective monitoring of the implementation of the CAI. Nevertheless, both sides were committed to pursue the negotiations on investment protection and investment dispute settlement within two years of the signature of the Agreement. The common objective was to work towards modernised investment protection standards and a dispute settlement that takes into account the work undertaken in the context of the UNCITRAL WGIII deliberations on the EU's MIC proposal.[152] Given the present stalemate over the CAI, it is not clear whether the CAI will be revived. There is also considerable uncertainty as to how the final ISDS mechanism would look like in the CAI in the future, should the negotiations restart. In the same vein, China has so far *not* commented on the EU's MIC proposal.

Then, is there any likelihood that China may sign up to the EU's ICS proposal in future CAI negotiations and ultimately be a supporter of the EU's MIC proposal? Both Chinese and Western commentators are pessimistic about this prospect with little analysis.[153] This article does not intend to challenge this conclusion. Nevertheless, I would argue that the analysis leading to this conclusion should be more sophisticated and nuanced than what the existing literature suggests. To begin with, China has made it clear in its UNCITRAL submission that China favors a *multilateral* approach to ISDS reform since it is more efficient than doing so through BITs, and it can minimise institutional costs.[154] Thus China may argue that both parties should wait and see what consensus may emerge from the UNCITRAL WGIII negotiations and avoid making drastic ISDS innovations through bilateral means. This is reflected in the commitment expressed in the CAI that both sides should continue to pursue the negotiations on investment dispute settlement, taking into account the work undertaken in the context of the UNCITRAL WGIII deliberations on the EU's MIC proposal.

Second, the EU's MIC proposal itself is highly controversial. Critics argued that the clamour for radical ISDS reform is a populist trend inspired by irrational fear, by some countries and their citizens' objections to a rule of law

[149]Lily McElwee, 'The Rise and Demise of the EU – China Investment Agreement: Takeaways for the Future of German Debate on China', CSIS Brief (March 2023), at 3–7; Arlo Polettia et al., 'Time for a New Atlanticism: The EU-China Comprehensive Agreement on Investment and the International Order' (2023) 58 (1) The International Spectator 23, 24.

[150]Jack Ewing, 'European Lawmakers Block a Pact with China, Citing Human Rights Violations', New York Times (20 May 2021).

[151]Stuart Lau, 'EU's von der Leyen Calls for Tougher Policy on China Ahead of Beijing Visit (30 March 2023) <https://www.politico.eu/article/eus-ursula-von-der-leyen-xi-jinping-calls-for-tougher-policy-on-china-ahead-of-beijing-visit/>; Lily McElwee, 'Despite Beijing's Charm Offensive, the EU-China Investment Agreement Is Not Coming Back', CSIS Commentary (23 February 2023) <https://www.csis.org/analysis/despite-beijings-charm-offensive-eu-china-investment-agreement-not-coming-back>.

[152]European Commission, 'EU-China Comprehensive Agreement on Investment: The Agreement in Principle' (30 December 2020).

[153]Gómez (n 11) 54–61; Julien Chaisse and Xueliang Ji, 'Stress Test for EU's Investment Court System: How Will Investments Be Protected in the Comprehensive Agreement on Investment?' (2022) 49 (1) Legal Issues of Economic Integration 101, 123–124; Li Jia and Wu Siliu, 'From Bilateral to Multilateral: EU's Reform of Investment Dispute Settlement Mechanism and China's Choice' (2020) 9 International Trade 46, 52–53.

[154]Submission from China (n 8) 4.

that is not 'home-grown', and determinedly by left-wing intellectuals and allied non-governmental organisations long on inflammatory rhetoric and emotion and very short on established facts and substance.[155] Questions were also raised on whether judges appointed only by states would not be biased in favour of states; the impact of an international investment court on the well-functioning ICSID, and substantial problems of coherence, rationalisation, negotiation, ratification, establishment, functioning, staffing and financing that the new international investment court would face.[156] At UNICITRAL WGIII, some of the EU's major trading partners, including the USA and Japan, strongly question the need for reforming the ISDS in such a radical manner and many other states are lukewarm about the idea of moving forward a MIC.[157] With only limited support at the multilateral level, it is not clear how the MIC idea could be implemented. Therefore, it makes sense for China to wait to see if some level of multilevel consensus may emerge on the EU's MIC proposal. Before that happens, China prefers to keep its options open. This open attitude may be reinforced by China's recent bid to join the CPTPP, which features an incremental change over the traditional ISDS.

Finally, China has reservations about the EU's MIC reform proposal from its own perspective. For example, when it comes to the appointment of the arbitral tribunal, the EU advocates for a standing mechanism with the same body of adjudicators appointed for long and staggered terms who will form panels for individual cases on a randomised basis. China, by contrast, emphasises party autonomy in selecting and nominating arbitrators, at least at the first instance level.[158] It is quite clear that China attaches high importance to this point when it stresses that the right of parties to appoint arbitrators is not only a widely accepted institutional arrangement in settling international disputes, but also helpful to solve complex and legal issues in different sectors and to enhance the confidence of investors in ISDS. To conclude, it is unlikely for China to accept ICS in the CAI in principle in the near future because, first, China favors a multilateral approach to ISDS reform and second, China is not yet convinced that the EU's MIC proposal is the best path to reform ISDS.

Given the rapidly deteriorating EU-China relationship against the background of the Ukraine war, ratification of the CAI is unlikely to occur anytime soon. Nevertheless, the hope to revive it has never vanished in both the EU and China.[159] China's EU ambassador has recently reiterated Beijing's commitment to resuscitate the CAI, noting that Beijing is 'open to proposals from the EU' that would permit movement toward ratification.[160] To provide a diagnosis and prognosis of how to revive the CAI is clearly beyond the scope of this paper. To break the stalemate over the CAI, one modest proposal put forward in this paper is for China to reconsider its position on the EU's ICS proposal in the CAI. Specifically, it is submitted that China's approach to ISDS reform and the EU's ICS proposal are not inherently incompatible. While China is ambivalent about the EU's ICS proposal, on close examination, there are really no strong reasons for China to oppose it. Indeed, there are some good reasons for China to consider agreeing to a two-tier ICS in the CAI as well as support the EU's MIC proposal at UNCITRAL WGIII.

To begin with, it is clear from China's UNCITRAL submission that China shares with the EU many concerns about the traditional ISDS model, in particular the lack of error-correcting mechanism and the lack of consistency and predictability of investment arbitral awards. Therefore, China supports the idea of an appeal body within the wider ISDS mechanism. It is true that China's support for an appellate mechanism does not necessarily lead to its support for the EU's idea of a two-tier ICS. For example, when it comes to the appointment of the investment tribunal, the EU advocates a standing mechanism with the same body of adjudicators appointed for long and staggered terms who will form panels for individual cases on a randomised basis. China, by contrast, emphasises party

[155]Judge Charles N. Brower and Jawad Ahmad, 'Why the "Demolition Derby" That Seeks to Destroy Investor-State Arbitration?' (2018) 91 Southern California Law Review 1139, 1157.

[156]van den Berg (n 34) 169–174.

[157]Brower and Ahmad (n 155) 1155.

[158]Submission from China (n 8) 4.

[159]Jamil Anderlini, 'Europe's Disunity over China Deepens' (24 April 2023) <https://www.politico.eu/article/europe-germany-france-olaf-scholz-disunity-over-china-deepens/>; Chen Weihua, 'Sweden Keen to Push for Progress on CAI' (11 January 2023) <https://www.chinadaily.com.cn/a/202301/11/WS63bded50a31057c47eba8d3f.html>.

[160]Transcript of Ambassador Fu Cong's Interview with the South China Morning Post (23 December 2022) <http://eu.china-mission.gov.cn/eng/mh/202212/t20221224_10994641.htm>.

autonomy in selecting and nominating arbitrators, at least at the first instance level. But even though this argument may be relevant to explaining China's reticence about the EU's MIC proposal, it is less relevant to a BIT such as the CAI. This is because China's preference for party autonomy in appointing adjudicators in the first instance could largely be accommodated by the EU's two-tier ICS in the CAI. This can be illustrated by the ISDS clauses in the EU-Canada Comprehensive Economic and Trade Agreement (CETA). Among fifteen members of the tribunal, five of the members shall be nationals of a member state of the EU, five shall be nationals of China, and the remaining five are nationals of third countries. The tribunal shall hear investment disputes in divisions consisting of three members of the tribunal, of whom one shall be a national of a member state of the EU, one a national of China and one a national of a third country. The division shall be chaired by the member of the tribunal who is a national of a third country.[161] Therefore, China retains at least some autonomy in appointing arbitrators at the first-instance stage of arbitration proceeding, albeit from a much smaller pool of experts.

Furthermore, while the ICS differs from traditional ISDS in some respects, notably regarding the existence of a permanent adjudicatory body and an appeal mechanism, in many other respects the ICS merely accommodates to trends already developed under IIAs and case law.[162] Both China and the EU have already expressed support for these trends, including strengthening ethical rules to avoid conflicts of interest for arbitrators and inclusion of alternative dispute resolution provisions in ISDS clauses.

Next, China's preference for multilateralism does not necessarily prevent China from agreeing to the ICS in the CAI. Given the diversified preferences to ISDS reform, it is highly unlikely for states to agree on a uniform multilateral agreement on investment dispute settlement. At UNCITRAL WGIII, the work plan proceeds on the assumption that these reforms will be brought together in a multilateral instrument that gives states the choice of which reforms to accept and with respect to which treaties, modelled on the Mauritius Convention.[163] It is entirely possible for China to embrace both incremental reforms embodied in the CPTPP and the ICS in the CAI.

Finally, China has so far not commented on the MIC proposal, for several reasons. For one thing, different from a BIT like the CAI, China's preference to retain the right to appoint arbitrators at the first-instance stage of arbitration proceeding cannot be accommodated in a multilateral treaty establishing the MIC. However, China's concerns may be mitigated now because the EU has recently suggested an 'open architecture', i.e., building a certain level of flexibility into its MIC proposal. For example, some countries may like to stick to *ad hoc* arbitral tribunals and utilise only the appeal mechanism of the two-tier MIC; or some countries might want to use the standing mechanism for state-to-state dispute settlement, but do not use ISDS in their agreements.[164] This flexibility is likely to enhance the appeal of the MIC to China. In addition, the EU's proposal to establish a standing MIC is institutionally modelled on the WTO dispute settlement system.[165] As a staunch defender of the WTO dispute settlement system, China may find the EU's MIC proposal familiar and is more willing to support it when it adopts an 'open architecture'. This is particularly true if other initiatives such as an appeal facility in lieu of ICSID annulment under the ICSID framework does not gain much traction.

5 | CONCLUSION

The EU has been very proactive in shaping the agenda regarding the reform of the ISDS. Given China's economic clout, some commentators predicted that China would soon become 'a global ISDS power'.[166] Moreover, in contrast

[161]CETA Art. 8.27 (3) and (6).

[162]Hannes Lenk, 'The EU Investment Court System and Its Resemblance to the WTO Appellate Body', in Szilard Gaspar-Szilagyi et al., *Adjudicating Trade and Investment Disputes: Convergence or Divergence* (CUP, 2020) 62, 70–75.

[163]Note by the Secretariat, 'Possible Reforms of ISDS: Multilateral Instrument on ISDS Reform', A/CN.9/WG.III/WP.194 (16 January 2020).

[164]Submission from the EU (n 17) para 3.16.

[165]European Commission, 'Commission Proposes New Investment Court System for TTIP and Other EU Trade and Investment Negotiations' (16 September 2015) <https://ec.europa.eu/commission/presscorner/detail/en/IP_15_5651>.

[166]Diane A. Desierto, 'China as a Global ISDS Power' (24 August 2018) <https://oxia.ouplaw.com/page/715>.

to other rising powers such as India and Brazil, China supports the ISDS system and keeps an open attitude to possible reform options. This makes China a key contender and potential partner for the EU in the ongoing global negotiations on ISDS reform. This paper provides the first detailed analysis of China's UNITRAL WGIII submission and explains how China's approach to ISDS reform is shaped by the underlying political, economic, and cultural forces in China. It shows that China's switch from conservative to proactive engagement with the ISDS system goes hand in hand with China's shifting role from a major capital importing country to a hybrid of capital importing and capital exporting country with active ODI. As the second largest economy in the world, it would be only a matter of time before China gets involved in more and more investment disputes. This switching position also reflects China's ambition to be part of the global economic governance reform. The ISDS reform provides a good opportunity for China to voice its ideals in the international investment sphere.

Given the competing preferences to how ISDS should be reformed, current efforts are likely to produce an ever more complex ISDS regime, governed by more diverse substantive rules and methods for interpreting ever more diverse IIAs.[167] It remains to be seen how China will choose from the menu of reform options for ISDS. For the time being, it seems unlikely for China to accept the ICS in the CAI negotiations. Nevertheless, this paper urges the Chinese government to reconsider its position. At the same time, there is a strong possibility that China may support an 'open architecture' MIC, and only make use of its appellate facility.

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[167] Alvarez (n 32) 254.

APPENDIX A

TABLE 1. Government of China as Respondent in ISDS (By 31 May 2023).

	Case Name	Applicable Rules	Case Registration Date	Instruments Invoked	Economic Sector	Status of Proceeding
1	Eugenio Montenero v. China	UNCITRAL Ad Hoc Arbitration	2021	China-Switzerland BIT 2009	Creative, Arts and Entertainment	Pending
2	Goh Chin Soon v. China	UNCITRAL Ad Hoc Arbitration administered by the PCA, PCA Case No 2021–30	2021	China-Singapore BIT 1985	Construction	Pending
3	Asia Phos Limited v. China	UNCITRAL Arbitration administered by ICSID	2020	China-Singapore BIT 1985	Mining and Quarrying	Decided in favour of China
4	Goh Chin Soon v. China	ICSID Case No. ARB/20/34	2020	China-Singapore BIT 1985	Construction	Discontinued pursuant to ICSID Arbitration Rule 43(1)
5	Marco Trading Co. Ltd v. China	ICSID Case No. ARB/20/22	2020	China-Japan BIT 1988	Construction	Discontinued pursuant to ICSID Administrative and Financial Regulation 14(3)(d).
6	Jason Yu Song v. China	UNCITRAL Ad Hoc Arbitration administered by the PCA, PCA Case No 2019–39	2019	China-United Kingdom BIT 1986	Unknown	Pending
7	Hela Schwarz GmbH v. People's Republic of China	ICSID Case No ARB/17/19	2017	China-Germany BIT 2003	Spice Products	Pending
8	Ansung Housing Co., Ltd. v. People's Republic of China	ICSID Case No. ARB/14/25	2014	China-Korea BIT 2007	Construction	Decided in favour of China
9	Ekran Berhad v. People's Republic of China	ICSID Case No ARB/11/15	2011	China-Israel BIT 1995 & Malaysia-China BIT 1998	Real Estate	Discontinued pursuant to ICSID Arbitration Rule 43(1)

TABLE 2. Chinese Investors as Claimant in ISDS (By 31 May 2023).

	Case Name	Applicable Rules	Case Registration Date	Instruments Invoked	Economic Sector	Status of Proceeding
1	China Machinery Engineering Corporation v. Republic of Trinidad and Tobago	ICSID Case No. ARB/23/8	2023	China-Trinidad and Tobago BIT 2002	Manufacturing	Pending
2	PowerChina Huadong Engineering Corporation and China Railway 18th Bureau Group Company Ltd. V. Socialist Republic of Vietnam	ICSID Case No. ARB (AF)/22/7	2023	ASEAN-China Investment Agreement 2009	Construction	Pending
3	Junefield Gold Investment Limited (Hong Kong) v. Ecuador	UNCITRAL Ad Hoc Arbitration	2022	China-Ecuador BIT 1994	Mining	Pending
4	PCCW Cascade (Middle East) Ltd (Hong Kong) v. Kingdom of Saudi Arabia	ICSID Case No. ARB/22/20	2022	China–Saudi Arabia BIT 1996	Information and Communication	Pending
5	Huawei Technologies Co., Ltd. v. Kingdom of Sweden	ICSID Case No. ARB/22/2	2022	Sweden-China BIT 1982	Telecommunications	Pending
6	Qiong Ye and Jianping Yang v. Kingdom of Cambodia	ICSID Case No ARB/21/42	2021	ASEAN-China Investment Agreement 2009	Information & Communication	Pending
7	Alpene Ltd (Hong Kong) v. Republic of Malta	ICSID Case No ARB/21/36	2021	Malta-China BIT 2009	Finance	Pending
8	Beijing Everyway Traffic and Lighting Tech Co. Ltd v. Ghana	UNCITRAL Ad Hoc Arbitration administered by the LCIA	2021	China-Ghana BIT 1989	Construction	Decided in favour of Ghana
9	Shift Energy (Hong Kong) v. Japan	UNCITRAL Arbitration	2020	Hong Kong-Japan BIT 1997	Electricity Supply	Decided in favour of Japan
10	Wang Jing, Li Fengju, Ren Jinglin and Others v. Republic of Ukraine	UNCITRAL Arbitration	2020	China-Ukraine BIT 1992	Manufacturing	Pending
11	Fengzhen Min v. Republic of Korea	ICSID Case No. ARB/20/26	2020	China-Korea BIT 2007	Real Estate	Pending
12	Jetion Solar Co. Ltd and Wuxi T-Hertz Co. Ltd. v. Hellenic Republic	UNCITRAL Ad Hoc Arbitration	2019	China-Greece BIT 1992	Electricity Supply	Withdrawn

(Continued)

	Case Name	Applicable Rules	Case Registration Date	Instruments Invoked	Economic Sector	Status of Proceeding
13	Zhongshan Fucheng Industrial Investment Co. Ltd. v Federal Republic of Nigeria	UNCITRAL Ad Hoc Arbitration	2018	China-Nigeria BIT 2001	Construction	Decided in favour of the Chinese Investor
14	Sanum Investments Ltd. (Macao) v. Lao People's Democratic Republic (II)	ICSID Case No. ADHOC/17/1	2017	China-Lao BIT 1993	Gaming	Pending
15	Standard Chartered Bank (Hong Kong) Limited v. The United Republic of Tanzania	ICSID Case No. ARB/15/41	2015	Contract	Financial Services	Decided in favour of Investor
16	Beijing Urban Construction Group Co. Ltd. v. Republic of Yemen	ICSID Case No. ARB/14/30	2014	China-Yemen BIT 1998	Construction	Discontinued pursuant to ICSID Arbitration Rule 43(1).
17	Sanum Investments Limited (Macao) v. Lao People's Democratic Republic (I)	UNCITRAL Arbitration administered by the PCA: PCA Case No 2013–13	2013	China-Lao BIT 1993	Gaming	Decided in favour of Lao
18	Ping An Life Insurance Company, Limited v. Government of Belgium	ICSID Case No ARB/12/29	2012	China-Belgium BIT 1984 & 2005	Banking and Financial Services	Decided in favour of Belgium
19	Philip Morris Asia Limited (Hong Kong) v. The Commonwealth of Australia	UNCITRAL Arbitration administered by the PCA: PCA Case No. 2012–12	2011	Australia-Hong Kong BIT 1993	Tobacco	Decided in favour of Australia
20	Standard Chartered Bank (Hong Kong) Limited v. Tanzania Electric Supply Company Limited	ICSID Case No. ARB/10/20	2010	Contract	Financial Services	Decided in favour of Investor
21	China Heilongjiang International Economic and Technical Cooperative Corp. et al. v. Mongolia	UNCITRAL Arbitration administered by the PCA: PCA Case No 2010–20	2010	China-Mongolia BIT 1991	Mining	Decided in favour of Mongolia
22	Tza Yap Shum (Hong Kong) v. The Republic of Peru	ICSID Case No ARB/07/6	2007	Peru-China BIT 1994	Fishing	Decided in favour of Investor