

Opinio Juris in Comparatione

Op. J. Vol. 2/2011, Paper n. 6

Studies in Comparative and National Law
Études de droit comparé et national
Estudios de derecho comparado y nacional



INVESTMENT ARBITRATION AND CHINA: INVESTOR OR HOST STATE?

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Yang Shu-dong

Suggested citation: Yang Shu-dong, *Investment Arbitration and China: Investor or Host State?*, *Op. J.*, Vol. 2/2011, Paper n. 6, pp. 1 - 19, <http://lider-lab.sssup.it/opinio>, online publication December 2011.

INVESTMENT ARBITRATION AND CHINA: INVESTOR OR HOST STATE?

by

Yang Shu-dong[♦]

Abstract:

China's international investment arbitration practices are currently not plentiful, but its domestic legal and BITs-concluding practices allow the use of international arbitration to resolve China-related international investment disputes to a varying degree at different times. For the disputes between the host government and foreign investors, China's early BITs often adhere to the principle of exhaustion of local remedies and foreign investors only can restrictedly use a third-party international arbitration, such as ICSID under the Convention on the Settlement of Investment Disputes between States and National of Other States; the later BITs broadly allow to use a third-party international arbitration. However, China should continue to maintain the early cautious BITs-concluding position and make a prudent use of the ICSID arbitration mechanism, taking partial acceptance as the principle and full acceptance case by case where appropriate as an exception. For the disputes between private investors, investors always agree to a third-party international commercial arbitration. China should actively improve the environment of domestic arbitration to attract investors to willingly choose China as the arbitration place and make a greater use of China's international commercial arbitration. Only by doing so, can the interests of all the investors be better protected and the healthy development of the national economy can be better promoted.

Keywords: international investment arbitration; China's arbitration practices; ICSID international arbitration; international commercial arbitration.

[♦] Law Faculty of Chongqing University, Chongqing, P.R., China

I. INTRODUCTION¹

International investment is a kind of cross-border capital flow. With the development of economic globalization, the cross-border investment is more and more becoming one of the pillars of the international economy like the cross-border trade.² Especially in the last two decades the global FDI³ have been expanding under the incentives of the investment liberalization policy. Just as other states/regions do, China is actively integrating into the wave of international investment liberalization and has become one of the most states/regions that have attracted foreign direct investment and is expanding its overseas direct investment. The rapid development of international investment is bound to bring the stakeholders a variety of frictions and lots of disputes, but how to properly address these investment disputes is a matter relating to the national sovereignty and economic security and also relating to the rights and interests of all the investors. In recent years the international arbitration mechanism, including the common international commercial arbitration and the dedicated international investment arbitration by ICSID⁴ under Washington Convention⁵, is increasingly becoming the most powerful way to deal with international investment disputes. In this context, how does China treat international arbitration? Does China employ the international arbitration of the investor (capital-exporting) state or that of the host (capital-importing) state or a third-party international arbitration, such as ICSID, to resolve international investment disputes? How does China make better use of the international arbitration mechanism to resolve the disputes concerning international investment to promote the healthy development of its national economy? To these issues, a detailed analysis and discussion is made in this paper.

II. METHODOLOGY

Through the combined techniques of a qualitative analysis, a quantitative analysis, an illustration with selected examples and a comparative study, the paper makes a systematic analysis and an empirical study on the international investment arbitration practices in China.

III. FINDINGS AND DISCUSSIONS

A. The Significance of International Investment Arbitration to China

The international arbitration mechanism, including the common international commercial arbitration and the dedicated international investment arbitration by ICSID under Washington

¹ In this paper, China refers only to the Mainland of People's Republic of China, excluding Hong Kong, Macao and Taiwan of P.R., China and Hong Kong, Macao and Taiwan are specially treated.

² Chen An, *New Developments in International Investment Law and China's New Practice of Bilateral Investment Treaties*, 11 (Shanghai, Fudan University Press, 2007).

³ It is a short form for "foreign direct investments".

⁴ It is a short form for "the International Centre for Settlement of Investment Disputes".

⁵ It is a short form for "the Convention on the Settlement of Investment Disputes between States and National of Other States".

Convention, is of great significance to the international investment dispute settlement in China and the healthy development of its international investment.

1. China's stock of international investment is huge and the arising of international investment disputes is inevitable.

Since 1979, China has begun the reform and opening-up policy and actively absorbed foreign investments and encouraged foreign investors to set up investment enterprises in China, for which a series of laws and regulations were promulgated, such as *On the Provisions to Encourage Foreign Investments*, *The Foreign Investment Industrial Guidance Catalogues*, *Sino-foreign Cooperative Ventures Law*, *Sino-foreign Joint Ventures Law* and *Foreign-owned Enterprises Law*. China is committed to create a good investment climate for foreign investors and strives to achieve a win-win state of affairs, having resulted in remarkable achievements. Over the past decade, China has also started the "going out" strategy and increased its overseas direct investment.

According to the statistics of the PRC⁶ Ministry of Commerce, as of the end of March 2011, China has attracted more than 710,000 foreign-funded enterprises and the actual amount of foreign capital utilization has reached nearly \$1.1 trillion.⁷ The latest *Global Investment Trends Monitoring Report* by UNCTAD⁸ issued on January 17, 2011 shows that China's foreign capital utilization amount is increasing year by year. The attracting amount in 2010 was more than one hundred billion U.S. dollars for the first time and arrived at \$101 billion and the actual foreign capital inflow accounted for 9% of the total global FDI (see Table 1), ranking second in the world just after the United States and ranking first in developing states. China's top ten investment source states/regions were all developed states and regions, the investment amount from which accounted for 90% in its total foreign capital utilization amount (see Table 2). The actual foreign capital utilization amount by manufacturing industries accounted for almost half of the total foreign investment and the manufacturing industries were still the main areas to attract foreign investment.⁹

⁶ It is a short form for "People's Republic of China".

⁷ PRC Ministry of Commerce website <http://www.mofcom.gov.cn/aarticle/tongjiziliao>

⁸ It is a short form for "United Nations Trade and Development Board".

⁹ PRC Ministry of Commerce website <http://www.mofcom.gov.cn/aarticle/tongjiziliao>

Table 1: the percentage of China's actual foreign capital utilization in the total global FDI inflows in recent years (Unit: billion U.S. dollars)¹⁰

year	Global FDI inflows	China`s amount	Percentage□ %□
2000	1387.953	40.715	2.93
2001	817.574	46.846	5.73
2002	678.751	52.734	7.77
2003	559.576	53.505	9.56
2004	648.146	60.63	9.35
2005	958.694	60.325	6.29
2006	1411.018	63.021	4.47
2007	1833.324	82.658	4.51
2008	1697.353	92.395	5.44
2009	1114.185	90.033	8.69
2010	1122.257	101.035	9.07

Table 2: the 2010' top ten states/regions of the investment in China¹¹
(Unit: billion U.S. dollars)

States/regions	The amount	Percentage□ %□
Hong Kong SAR	67.474	63.83
The Region of Taiwan	6.701	6.33
Singapore	5.657	5.35
Japan	4.242	4.01
USA	4.052	3.83
South Korea	2.693	2.55
the UK	1.642	1.55
France	1.239	1.17
Netherlands	0.952	0.91
Germany	0.933	0.89

Note: The investment data of above states/regions include the investment in China of these states/regions through Virgin, Cayman Islands, Samoa, Mauritius and Barbados and other free ports.

¹⁰ The United Nations Commission on Trade Development http://www.unctad.org/en/docs/webdiaeia20111_en.pdf

¹¹ PRC Ministry of Commerce website <http://www.mofcom.gov.cn/aarticle/tongjiziliao/v/201101/20110107370784.html>

According to the statistics of the PRC Ministry of Commerce, as of the end of March 2011, more than 12,000 Chinese investors have established over 17000 overseas direct investment enterprises, distributing in 177 states/regions and the net cumulative overseas direct investment amount (hereinafter referred to as the stock) is more than \$320 billion.¹² *The UNCTAD 2010 World Investment Report* shows that: China's overseas direct investment flow ranked fifth among all the states/regions and ranked first among developing states/regions; Asia and Latin America are the highly concentrated areas of China's overseas direct investment stock and the total stock accounts for 87% (see Figure 1); China's stock of direct investment in developed states/regions is \$18.17 billion, just accounting for only 7.4% (see Figure 2); The direct investment from the state-owned enterprises and limited liability companies account for 90% (see Figure 3).¹³

Figure 1: the regional distribution of China's overseas direct investment flows

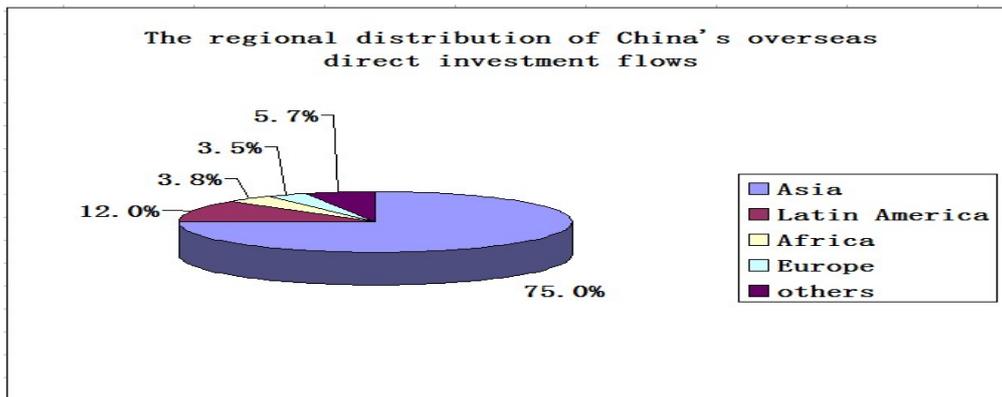
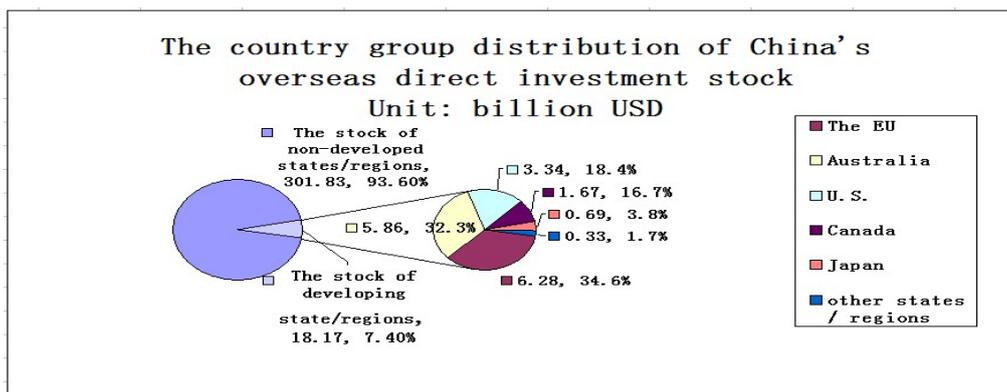


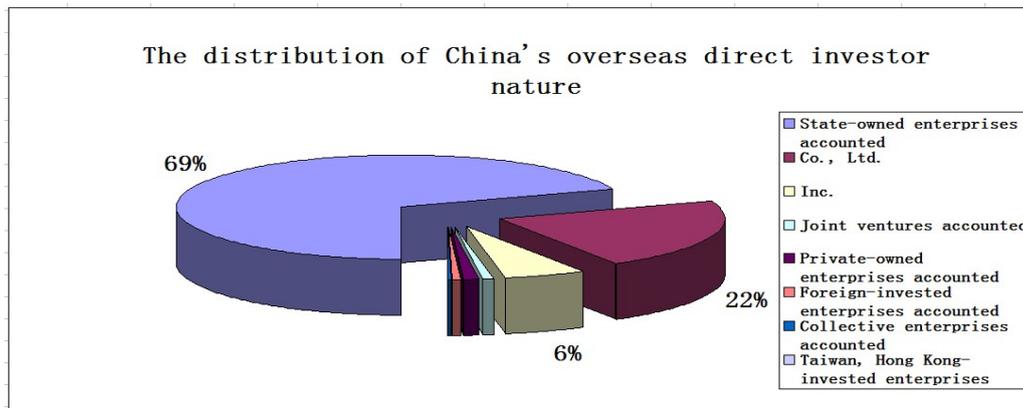
Figure 2: the country group distribution of China's overseas direct investment stock



¹² PRC Ministry of Commerce website <http://www.mofcom.gov.cn/aarticle/tongjiziliao>

¹³ See 2010' *Bulletin of China's Foreign Investment*.

Figure 3: the distribution of China's overseas direct investor nature



From the situations of the foreign investment and overseas investment mentioned above, it can be seen that developing trend of international investment in China is very strong and the international investment has become an important part of China's rapid economic development. China's rapid development of international investment is bound to bring the stakeholders a variety of frictions and the occurrence of disputes is inevitable.

2. The international arbitration mechanism is increasingly becoming a most powerful way to address global international investment disputes.

The resolving of international investment disputes unexceptionally relate to the tripartite of investors, the host state, the investor state, involving the relations of the subjects in private law and public law, of foreign interests and the interests within the state, of international law and domestic law and etc. The multiple interests cannot be balanced if just simply applying the principle of private law or public law. Given that the scale of international investment continues to expand and the increasing of investment disputes is inevitable, all states arrange their own investment dispute resolution methods to promptly and effectively resolve their own investment disputes in their bilateral, multilateral, or regional trade agreements and investment agreements so as to strengthen their own ability of attracting foreign investment and stabilize their own domestic investment environment. Some international organizations have also established the corresponding mechanisms.

Generally, a variety of methods can be employed in the international investment dispute settlement: negotiation and mediation, local relief in the host state (including judicial, administrative and arbitration ones), foreign court litigation, international arbitration (including the common international commercial arbitration), and so on.

Specifically, there exist different types of dispute resolution methods to the different types of international investment disputes:

- For the interstate disputes arising from international investment, a political solution is often involved. The agreements between states usually make some brief provisions and require the disputes to be resolved through friendly consultation or diplomatic channels. To such disputes, WTO dispute settlement mechanism also has a detailed solution.
- For disputes between private investors, which are mainly disputes arising out of the investment contracts and the distribution of the interests between the host state's private investors and foreign private investors in the cooperative or joint ventures. At present, the host state's local relief and the international commercial arbitration mechanisms are always applied to such disputes. As a private dispute resolution method, the international commercial arbitration is highly sought after by private investors and is getting a universal attention in domestic legislation and international investment treaties. "The Principle of Autonomy", a generally accepted principle of law in many states, has been fully embodied in international commercial arbitration process. In the international commercial arbitration, the parties have rights to choose the arbitration institution, the organization form of arbitration, the arbitrator, the applicable substantive law and procedural law and the arbitration rule, and it also has the merits of low cost, confidentiality, and a high degree of professionalism and the strong enforceability safeguarded by *the Convention on Recognition and Enforcement of Foreign Arbitral Awards* and other international conventions. Therefore, all states have adopted policies conducive to the international commercial arbitration.¹⁴
- For the disputes between the host government and foreign investors, because of a particular subject feature, one being private investors and the other being a sovereign state, "they are the most complex disputes, which are most difficult to resolve, and thus the studies on international investment dispute resolution methods are mainly for this type of disputes."¹⁵ Under the auspices of the World Bank, in 1965 quite many states signed *the Convention on the Settlement of Investment Disputes between States and National of Other States* and set up an "International Centre for Settlement of Investment Disputes" according to the Convention. Currently, ICSID international arbitration is a special dispute settlement mechanism for these disputes and provides a convenient solution for the investment disputes between investors and the host states. From the new century, more and more cases are submitted to ICSID for arbitration. The statistics released by United Nations Trade and Development Board in March 2011 show that: As of the end of 2010, they have accumulated to 390. Of these cases, there are 51 developing states and 17 states being sued and the vast majority of the applicants

¹⁴ See Xu Hanming and Jiang Jianwei, "China international commercial arbitration in the context of economic globalization", 2 CHINESE PROSECUTORS 23-24(2005).

¹⁵ Cao Jianming and Chen Zhidong, *On International Economic Law*, 207 (Beijing, Law Press, 2000).

are investors from developed states, the highest number of cases of which are against Argentina, amounting to 51 and followed up by Mexico, amounting to 19 cases.¹⁶

B. China's International Investment Arbitration Practices

This paper divides the international investment disputes into the investment disputes between host government and foreign investors and the investment disputes among Sino-foreign investors to examine China's international investment arbitration practices and its domestic legal and BITs¹⁷-concluding practices. For disputes between the states on international investment, they are often categorized as political disputes and the states concerned now rarely use the international arbitration to resolve them, so they are not to be discussed in this paper.

1. The investment dispute arbitration between the host government and foreign investors.

a. China's ICSID international arbitration practices.

So far, in the ICSID international investment arbitration practices, China has never been filed as a respondent and Chinese investors also have never filed an arbitration case as an applicant. The main reason relates to China's attitudes on the ICSID jurisdiction and the range of dispute issues which can be submitted to ICSID. China made the reservations when acceding to Washington Convention: according to Article 24, paragraph 4, China only agrees to submit the compensation disputes arising from expropriation and nationalization to ICSID jurisdiction.¹⁸ In its early BITs China keeps a conservative approach and the majority of BITs only agree to submit "the disputes about expropriation compensation" to ICSID arbitration. The other treaties also adhere to the principle of "case-by-case approval". Despite China's early BITs-concluding position has undergone a marked change, the effect and impact brought about by this change has not yet emerged. In 1998 the BIT concluded between China and Barbados for the first time accepted uncritically the ICSID jurisdiction.¹⁹ Since then, China has fully accepted the ICSID jurisdiction in nearly 30 BITs. The range of dispute issues to which China accepts the jurisdiction of international investment arbitration is also growing and the range of matters which can be submitted to international arbitration are gradually relaxed. Additionally, since the reform and opening up, China has not yet taken any nationalization measure against any foreign investment, so there exists no investment arbitration basis in reality.

b. China's BITs practices.

Since the first BIT between China and Sweden signed in 1982, China has outside concluded more than 110 BITs, ranking first in developing states. From nearly three decades' BITs signed by China, it can be found that the phase characteristic of the BITs-concluding position is very clear about the

¹⁶ The United Nations Commission on Trade Development http://www.unctad.org/en/docs/webdiaeia20113_en.pdf

¹⁷ It is a short form for "bilateral investment treaties".

¹⁸ See Yu Jinsong and Wu Zhipan, *International Economic Law*, 598 (Beijing, Higher Education Press and Beijing University Press, 2008).

¹⁹ See Article 9 of China-Barbados BIT.

jurisdiction of international arbitration on the disputes between the host government and private investors:

- The period of "partial consent" to international arbitration (the BITs of the first generation).

In March of 1982, China signed its first BIT with Sweden, but the treaty only provides a dispute resolution method to the interpretation or implementation of the agreement and does not provide a dispute resolution method in the event of the dispute occurrence between private investors and the host government. The BIT signed by China and Germany in 1983 "for the first time uses international arbitration as a solution way to the 'investor-host' disputes",²⁰ but it makes a strict restriction to the range of dispute issues which may be submitted to the international arbitration, only allowing investors to submit the matter of compensation amount out of expropriation to an international arbitration tribunal. To other investment issues, out of the respect for the basic legal principles of the state sovereignty, of the closest connection, of the state territorial jurisdiction and etc, China adheres to the Calvo doctrine and advocates the principle of exhaustion of local remedies, which means that the host state enjoys the unalienable jurisdiction over the investment disputes within its territory and has the right to require the parties to seek solutions through local relief to their disputes. Under normal circumstances, unless otherwise provided by law or expressly agreed by the host government, private investors cannot submit the disputes with the host government directly to the international settlement.

²¹ Only in exceptional circumstances, the two sides can establish a temporary tribunal to resolve their disputes. For example, Article 9 of *The Encouragement and Reciprocal Protection of Investments between PRC government and the Government of the Republic of Kazakhstan* signed in August 1992 states that: " any dispute about the compensation amount for expropriation between Contracting Party and any other`s investors can be submitted to an arbitral tribunal and the tribunal shall be established in each case in accordance of the following ways:" In short, based on national sovereignty, China essentially claimed the jurisdiction over the investment disputes between the host government and private investors before China acceded to Washington Convention and took a very cautious position of "partial consent" to international arbitration.

On February 6, 1993, China officially joined Washington Convention, but after 5 or 6 years of the formal accession, China remained cautious about an international arbitration to the investment disputes, especially about ICSID international arbitration jurisdiction, and thus still adhered to a "partial consent" position. In this time China imposed a strict restriction on ICSID arbitration to the disputes between investors and the host government in its BITs and most treaties followed the same common conditions: "If the investment-related disputes between the host government and investors cannot be

²⁰ Li Bei, "On the perfection of the international arbitration mechanism to 'investor host' disputes of Sino- foreign BITs", (Master Degree thesis, East China University of Politics and Science, 2008).

²¹ See Liu Shen, *On Some Important International Legal Issues of International Investment Protection*, 221-222 (Beijing, Law Press, 2002).

resolved through friendly consultations within six months from the date on which a party requests a solution in writing, at investors' choice, they shall be submitted to the competent court in the host state, or the ICSID under Washington Convention, ...".²² In the BITs, China advocates the host state's "right of case-by-case approval or consent", "priority of local remedies" and "right of applying the host law" empowered by Washington Convention.

It can be seen that during the period of "partial consent" to international arbitration in the BITs of the first generation, China's BITs-concluding practices very restrictedly allow to choose a third-party international arbitration, such as ICSID, and more frequently advocates the principle of exhaustion of local relief. So foreign investors can only seek local relief from the host state and since China does not accept the common international commercial arbitration to settle the 'investor-host' disputes, they can mainly resort to the judicial or administrative remedies. Even they are occasionally allowed to employ another kind of international arbitration, for example, a dedicated temporary arbitral tribunal belonging to neither the host nor investor state, they are also required to take the host state for the arbitration place and use the host law as the applicable law.

- The period of "comprehensive consent" to international arbitration (the BITs of the second generation).

China and Barbados in 1998 concluded a BIT, in which China for the first time agreed that investors might submit all the investment disputes with the host state to international arbitration. Until January 2007, China has signed about 36 new BITs, most of which have accepted uncritically the ICSID jurisdiction ²³(See Figure 4). For example, Article 10 of 2001' BIT between China and the Netherlands provides a dispute settlement method as follows: "... if the dispute fails to be resolved within six months since the date being submitted to an amicable settlement, the parties shall unconditionally agree that the dispute is submitted to ICSID or an ad hoc arbitral tribunal established following UNCITRAL²⁴ Arbitration Rules upon the demanding of the investors concerned." The new investment agreement between China and Finland in April 2005 provides that: "any dispute arising out of investments between the Contracting Party and the other's investors fails to be resolved within three months from the date of requesting in writing, at investors' choice, the dispute may be submitted to: i. the competent court of Contracting Party where to be invested; ii. ICSID established by *The Convention on the Settlement of Investment Disputes between States and National of Other States* signed in Washington on March 18, 1965; iii. The ad hoc arbitral tribunal set up according to the UNCITRAL Arbitration Rules, unless the parties to the dispute otherwise agree." The bilateral investment agreements of China with

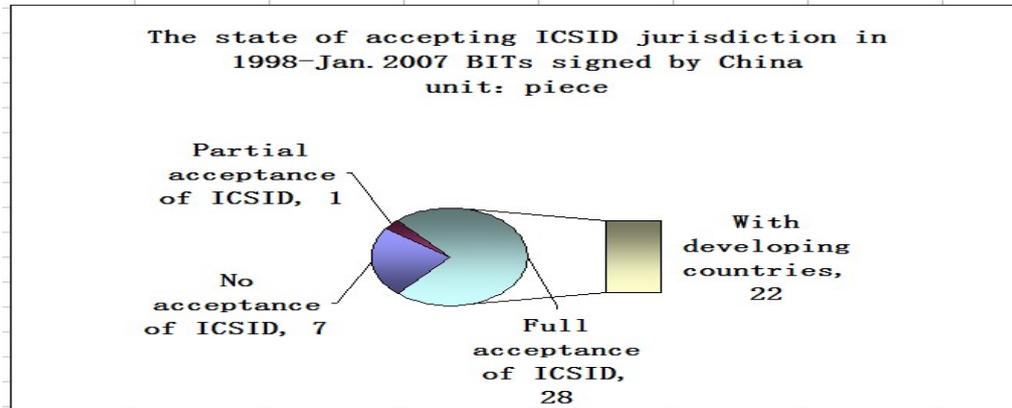
²² Chen An, "Distinguishing between two categories of states and implementing the differential treatments and reciprocal benefits: again on the issue that the four big 'safety valves' given to China by the ICSID system should not rush to be fully removed", 3 JOURNAL OF INTERNATIONAL ECONOMIC LAW 61 (2007).

²³ See Li Xiaoxia, "On the new development trends of bilateral investment treaties and China's Countermeasures", 3 ECONOMIC PROBLEMS 53-56 (2010).

²⁴ It is a short form for "United Nations Commission on International Trade Law".

the governments of Germany, Bosnia and Herzegovina signed in 2004 also have similar provisions respectively. These BITs-concluding practices of China still have a trend to continue.

Figure 4: the state of accepting ICSID jurisdiction in 1998-Jan.2007 BITs signed by China



From these BITs of the second-generation, it can be found that most of the BITs signed by China and other states give full acceptance to the ICSID jurisdiction and abandon "the right of case-by-case approval or consent" and "the priority of local remedies", "the right of significant security exception" and other relevant rights, and that they doesn't exclude the disputes involving public safety, national economy and other important matters from the international arbitration jurisdiction. As a result, China's BITs of the second generation have entered into a period of "comprehensive consent" to the international arbitration, broadly allowing a choice of a third-party international arbitration, such as ICSID, or an ad hoc international tribunal which belongs to neither the host nor investor state, and have no restriction of the arbitration place and applicable law.

- The causes and effects of the change in China's BITs-concluding positions on international arbitration.

"To what extent to accept ICSID jurisdiction is dependent on the accounting and weighing of gains and losses among the three factors of the demand for foreign capital attraction, the protection to overseas investment and the impact on national economic sovereignty."²⁵ Some scholars believe that China's current BITs-concluding position of full acceptance to ICSID arbitration relates to the implementation of the 'going out' strategy beginning in China around 1998.²⁶ The purpose of keeping such a position is to satisfy the needs of creating a favorable investment environment to attract foreign investment, and more importantly, to satisfy the needs of protecting China's overseas investment and perfecting China's overseas investment service. Throughout the world, even some Latin American

²⁵ Chen An, *The New Development of International Investment Law and China's New Practice of Bilateral Investment Treaties*, 411 (Shanghai, Fudan University Press, 2007).

²⁶ See *Id.* at 409.

states, having strictly implemented the Calvo doctrine before, e.g. Argentina, no longer adhere to the original position and empower investors the right to resort to international arbitration. So many scholars have argued that China should follow this trend to better attract investment from foreign states and make its own overseas investment.

Another very important reason is that China does not accept the common international commercial arbitration to settle 'investor-host' disputes and the international commercial arbitration institutions in China cannot do the investment dispute arbitration between the host government and foreign investors well. Although the China's foreign-related arbitration has made considerable progress in the past 40 years and there are more than 180 arbitration institutions nowadays, there still exist many problems in the arbitration, which cause foreign investors in international investment disputes unwilling to arbitrate in China. The arbitration institutions should be non-government organizations to ensure its independence, impartiality and neutrality, but the China's arbitration institutions are still prepared to apply the administrative regime and the arbitration committee directors are part of the executive leaders. Moreover, the local arbitration committees are set up by the local governments and there are a lot of contacts with them in staffing, finances, and etc. Thus, foreign investors will inevitably wonder whether the arbitrator can make a fair and equitable award of no favoritism. As a leader in the commercial arbitration, the China International Economic and Trade Arbitration Commission ranks in the forefront of the world's arbitral bodies by the number of cases, but it also has many problems. For example, professional umpire is not trustable, confidentiality of arbitration proceedings is not strong, and the staff functions as an arbitrator,²⁷ and so on.

The effect and impact on China brought about by the position change in BITs-concluding practices has not yet appeared, but the potential risk it may cause should be of great concern. To foreign investors, especially the investors in developed states, they often hope to be able to resolve the investment disputes in a third-party international arbitration and do not want their disputes subject to the host state jurisdiction (e.g. China). Therefore, China's position of "comprehensive consent" to international arbitration in the BITs of the second generation will inevitably result in the situation that the majority of investment disputes between foreign investors and China will be under the ICSID jurisdiction and ICSID will become a most influential permanent international arbitral institution to solve the 'investor-host' disputes arising out of the Sino-foreign BITs.²⁸

2. The investment dispute arbitration among Sino-foreign private investors.

The investment disputes among Sino-foreign private investors are mainly from joint ventures and cooperative ventures. Sino-foreign joint ventures, referred to as joint ventures, are a kind of partnership relations between foreign investors and Chinese economic entities. They are companies or other

²⁷ See Jerome Cohen and Xiao Kai (tr.), "China's international commercial arbitration: some thoughts from the personal experience", 7 THE SCIENCE OF LAW 44 (2005).

²⁸ See Li Bei, *supra* note 20.

economic organizations established upon the government's approval based on China's relevant laws. They are equity-based businesses and the joint venture parties share the risk, total profits and losses. Sino-foreign cooperative ventures, referred to as cooperative ventures, are similar to joint ventures, but this type of business enterprises connect both domestic and foreign investors in the form of contracts and all the obligations, rights and responsibilities are stipulated by the contracts. Unlike joint ventures, the profit distributions in cooperative ventures are not based on contribution shares but rather on the contract provisions.

In 1954 China set up the Foreign Trade Arbitration Commission (now the China International Economic and Trade Arbitration Commission), which supplies its professional solutions to contractual and non-contractual international economic and trade disputes, including international investment disputes. China International Economic and Trade Arbitration Commission is now the most important international commercial arbitration in China. Since *Arbitration Act* was enacted in 1994, some Chinese cities have created more than 170 arbitration committees, which gradually begin to accept foreign-related arbitration cases.

Article 25 of *PRC Sino-foreign Cooperative Ventures Law* provides: "When Chinese and foreign joint venture partners dispute with one another in fulfilling the contract and the articles of association, the disputes should be resolved through negotiation or mediation. If they do not want to resolve them through consultations and mediation, or the negotiation and mediation fail, the disputes may be submitted to China's arbitration institutions or other arbitration bodies for arbitration in accordance with the arbitration clause in the contract or a written arbitration agreement reached afterwards;". Article 15 of *PRC Sino-foreign Joint Ventures Law* also has similar provisions.

Thus, in view of the nature of disputes among private rights and obligations, China's legislation ensures the parties' autonomy and let them have the freedom to choose arbitration institution and the arbitration place, but because of the special features in Sino- foreign joint ventures or cooperative ventures-the joint or cooperative ventures contracts are signed and implemented in China and their closest points of contact are within China, Article 12 of *PRC Sino-foreign Joint Ventures Law Implementing Regulations* provides: " The laws of China shall govern the formation, validity, interpretation, and implementation of a joint venture contract and its dispute resolution." The similar provisions are also for the cooperative ventures. However, "due to foreign investors' lack of trust in the current legal environment of arbitration in China, the bottom line of foreign investors often is that: it will be good if the dispute is able to be resolved not in China".²⁹ The arbitration mechanisms and legal measures mentioned above have not reversed the trend of foreign investors' choosing a foreign arbitration. In fact, the international commercial arbitration cases which the arbitration institutions around China have

²⁹ Kou Li, "On the law application of China's international commercial arbitration", 4 POLITICAL AND LEGAL FORUM - CHINA UNIVERSITY OF POLITICS AND SCIENCE 90-100 (2004).

accepted are almost of foreign-related “non-investment” commercial arbitration nature, the net international investment dispute cases which the China International Economic and Trade Arbitration Commission have accepted are also very limited. For this type of investment disputes, China now relies more on judicial or administrative relief and even if the parties have agreed to resolve them through an international commercial arbitration, they are always ready to choose a third-party international commercial arbitration, rather than the international commercial arbitration in the host or investor state.

C. China and Its Future in International Investment Arbitration

In order to make better use of international arbitration mechanism to deal with China-related international investment disputes, China should focus on the following aspects:

1. China should coordinate the relations between its own sovereign interests and the investors.

In recent years, most of the investment dispute settlement mechanisms provided in international investment agreements or free trade agreements are for the emphasis on international arbitration, which essentially internationalizes the investment dispute settlement mechanism between investors and the host state. To investors, this kind of dispute settlement mechanism will undoubtedly help strengthen the protection to them; to the host states, it can create a climate conducive to attracting foreign investment and thereby promoting their economic development. As a developing state, it is necessary for China to take into account both the protection to investors and the safeguard to the host state's sovereignty and interests and it is also necessary for her to take into account both the substantive rights and the procedural issues so as to perfect its investment dispute settlement mechanism.

2. China should reduce the acceptance range of international arbitration jurisdiction.

China is now in the stage of economic restructuring, the state should have an appropriate management and adjustment capacity to the domestic investment market and environment. For foreign investors, compared with the preferential investment commitments that China has made to the foreign capital, China's huge market potential is the real attracting factor to the investment, so a full acceptance of ICSID arbitration jurisdiction makes no real sense to attracting foreign investment. As mentioned earlier, China's full acceptance to ICSID arbitration of the investment disputes between the host state and foreign investors is out of the dual needs of attracting foreign capital and protecting overseas investment, but factually this wish has not gotten the expected effects. *Global Economic Prospects 2003* of World Bank points out: "It seems that even relatively strong BITs protection measures have not increased the investment flows to the developing states that signed the agreements"; "Many bilateral investment agreements are concluded between unequal partners These agreements do not set clear requirements that the capital-exporting state ensure the capital flow into the other, but the party hoping to get foreign investment surrenders its sovereignty in the trust of foreign capital inflows. Because the foreign investment under the agreement can obtain foreign protection from the international dispute

settlement mechanism, the local law of the host state is largely beyond the reach and has no jurisdiction, and thus its sovereignty is handed over".³⁰ To China's overseas investment, the investors choosing to invest in a state have not primarily considered whether the state signed a BIT with China and whether the BIT fully accepted ICSID jurisdiction. Moreover, China's current "introducing amount" is far more than "that of going out", and close to the end of March 2011, China has actually used nearly \$ 1.1 trillion foreign capitals while the total non-financial overseas direct investments are \$ 320 billion. So, it is obviously not worth the candle to risk being sued ten international investments to protect a foreign investment.

The range of the dispute issues which can be submitted to ICSID has all the times been closely watched and prudently decided by the contracting states. Argentina are facing waves of lawsuits and has been filed in 51 cases, ranking number one as respondents in ICSID, which has a lot with its overall acceptance of ICSID jurisdiction when signing the BITs. In fact, the United States, Canada and other developed states are adopting the principle of significant security exception to sign the BITs and the United States straightly abandons "investors vs. state" dispute settlement procedures in its recent investment treaties.³¹ China's foreign investment legislation and administrative regime are still in the stage of reform and improvement, so now it not a safe move for China to rush to accept the ICSID jurisdiction in a wide range of dispute issues.³²

Therefore, in terms of the arbitration mechanism to investment disputes between the host government and foreign investors, China should change the existing position of "comprehensive consent" to the international arbitration jurisdiction, reiterate the principle of exhaustion of local remedies, make a strict limitation to the range of dispute issues which foreign investors can directly file to international arbitration and readjust the position of full acceptance. China should adopt a position of partial acceptance as the principle and full acceptance case-by-case where appropriate as an exception when newly signing, resigning, or amending the BITs in the future. For the range of dispute issues which may be submitted to international arbitration, it is improper to have all investment disputes submitted to international arbitration based on prior unilateral consent in the agreement, except for the disputes about expropriation, compensation, transfer and other relevant matters. The issues of foreign access, transparency and other relevant matters are not suitable for opening-up, because the consent shall be liable not to take back once made according to Washington Convention.³³

³⁰ M Sornarajah, *The International Law on Foreign Investment*, 207-208 (Cambridge, Cambridge University Press, 2004).

³¹ See Liu Shen, "On the challenges of international dispute arbitration to national sovereignty - Comments on the U.S. policy response and its Implications", 3 *LAW AND BUSINESS RESEARCH* 3-13 (2008).

³² See Chen An, *On International Economic Law*, 388 (Beijing, Higher Education Press, 2002).

³³ See Yu Jinsong and Zhan Xiaoning, "On the settlement mechanism of disputes between investors and the host state and its impact", 5 *CHINA LEGAL SCIENCE* 175-184 (2005).

3. China should improve its internal dispute settlement mechanism.

As far as the arbitration of investment disputes between Chinese investors and foreign investors from Sino-foreign joint ventures and cooperative ventures is concerned, because all the closest points of contact of such contract disputes are within China and the laws of China shall govern the formation, validity, interpretation and execution of the joint venture or cooperative contract and its dispute settlement in accordance with Chinese laws, the arbitration place of such disputes should be better in China and the jurisdiction should also belong to China following the principles of territorial jurisdiction and of the closest connection. For the settlement of investment disputes between foreign investors and the host government, it is also necessary for China to take a two-pronged strategy. China should make good use of ICSID international arbitration mechanism and also make full use of the effective domestic dispute settlement mechanisms, including the domestic international commercial arbitration. However, in reality, foreign investors try to avoid arbitration in China through the investment arbitration clause of the contract, for foreign investors do not trust Chinese arbitration and there really exist some problems in its arbitration environment.

Therefore, China should endeavor to improve and perfect the local dispute resolution mechanisms and make them trustable from foreign investors and build up an increasingly sound legal environment. For example, the domestic courts can more directly and frequently apply BITs so that foreign investors can have a direct access to international protection in the host state, which will not only provide the interests of foreign investors more effective protection, but also maintain the jurisdiction of sovereign states and other major public interests. The need to resort to international dispute settlement mechanism will be reduced only at the existence of transparent, reliable and objective local dispute resolution mechanisms. In the long run it is a fundamental solution most favorable to China to improve the domestic dispute settlement mechanism, encourage local solutions to investment disputes as possible so as to avoid abuse of the right to appeal by the investors and to save or reduce the costs, In order to fundamentally solve this problem, China needs to improve the status quo of China's arbitration mechanism and strengthen the independence of local arbitration committee from the regime and organizing mechanism to set it free from the local government's control and let it be the return of their own folk. To China International Economic and Trade Arbitration Commission, so a deeply influenced permanent arbitration institution in China, it should play a leading role in strengthening the arbitrator's neutrality and impartiality and appoint some legal experts of international trade law, investment law, financial law and other relevant areas as the presiding arbitrators and should also strengthen the confidentiality of the arbitration proceedings so that the legitimate interests of foreign investors can get full protection. Only in this way, it can help to improve the environment for arbitration and make foreign investors believe that the results of the investment

arbitration in China are fair and impartial so that they can rush to choose China as a place of arbitration just as treating England and Hong Kong.

IV. CONCLUSIONS

The stock of China's international investment is very huge and the arising of international investment disputes is inevitable, so China should make a rational use of the international investment dispute settlement mechanisms, especially international arbitration, including the common international commercial arbitration and the ICSID international investment arbitration under Washington Convention, to protect the interests of all investors, safeguard the national economic security and economic sovereignty and promote the healthy development of the national economy. In fact, despite China's own international investment arbitration practices are now rare, China's domestic legal and BITs practices allow the use of international arbitration to resolve China-related international investment disputes to a varying degree at different times.

In terms of international arbitration to the disputes between the host government and foreign investors, so far, in the ICSID international investment arbitration practices, China has never been filed as a respondent and Chinese investors also have never filed against other states as an applicant. This greatly relates to China's attitudes towards the ICSID jurisdiction, the range of dispute issues which may be submitted to ICSID and the other relevant issues in its earlier BITs practices. Additionally, China has not so far imposed any nationalization measure on any foreign investment, so ICSID has no jurisdiction basis in reality. Although China's BITs-concluding positions have undergone a significant change, the effect and impact the change brings about has not yet emerged. From the recent three decades' BITs-concluding practices of China, it can be easily found that a phrase characteristic in the attitudes towards the international arbitration jurisdiction concerning the disputes between the host government and foreign investors is obvious:

In the BITs of the first generation before 1998, China adopts a prudent position of "partial consent" to international arbitration. During this period, China very restrictedly allows the use of a third-party international arbitration, such as ICSID, and very broadly advocates the principle of exhaustion of local remedies, so foreign investors can only seek local relief from the host state. Because China doesn't allow the common international commercial arbitration to address the 'investor-host' disputes, foreign investors mainly seek for the judicial or administrative remedies from the host state; even another kind of international arbitration is occasionally allowed, for example, a temporary tribunal specially organized, belonging to neither the investor nor host state, it is still required to use the host state as the place of arbitration and the law of the host state as the applicable law.

From the BIT concluded in 1998 between China and Barbados, an opening-up position of "comprehensive consent" to international arbitration is taken in nearly 30 BITs of the second generation. During this period, China broadly allows using ICSID –a third-party international

arbitration or an ad hoc international tribunal belonging to neither the investor nor host state and also has no longer the restrictive requirements of the arbitration place and the applicable law. This BITs-concluding position change still has a continuing trend. The reasons for them may be as follows: China began implementing the 'going out' strategy around 1998 and China's international commercial arbitration institutions are not allowed to do the investment dispute arbitration between the host government and foreign investors. However, the potential risk in the change of China's BITs-concluding positions should be of great concern. Considering the painful lessons of other states, China's own economic development level and China's scale ratio of attracting foreign investment to its overseas direct investment, China should amend the current opening-up position of "comprehensive consent" to international arbitration of the investment disputes between the host government and foreign investors and keep the early cautious position and make a prudent use of ICSID arbitration mechanism, taking a partial acceptance as the principle and a full acceptance case-by-case where appropriate as an exception, to reestablish the state's control to the international investment dispute settlements.

For international arbitration on the disputes among Sino-foreign private investors, since foreign investors lack a trust in China's current legal environment of arbitration, China are making more use of the judicial or administrative relief. Even if the parties have agreed to the international commercial arbitration, they often make a choice of a third-party international commercial arbitration, rather than international commercial arbitration from the investor or host state. China should actively improve the environment of domestic arbitration to attract investors to willingly choose China as the arbitration place and make a greater use of China's international commercial arbitration mechanism to resolve their disputes based on the autonomy and closest connection principles.

V. CLOSING REMARK

How to resolve the international investment disputes is one of the most complex issues in the international investment law. In recent years, the investment dispute settlement mechanism in international investment agreements is becoming mature and international arbitration is increasingly becoming the most powerful way to deal with global international investment disputes, which helps to strengthen the protection to investors and improve the investment climate in developing states. In the incentives of the global investment liberalization policy, with the deepening of China's reform and opening-up process and accession to the WTO, China's favorable investment environment and huge market potential for foreign investors are more and more popular to the foreign investors and the attracting amount of foreign investment is rising every year. As a host state, how China meets the challenges, including how to resolve the frictions and disputes among the stakeholders, has become the hot issues which must be taken seriously to China. Meanwhile, with China's rapid economic development and economic capacity enhancement, the stock of China's overseas investment is also

increasing, how to better protect the interests of overseas investors also deserves a more attention. China should adopt the "two-hand" policy and design and make good use of international arbitration mechanism. China should strengthen the protection of investors` rights and interests under the premise of safeguarding national sovereignty and should both maintain the power of the government management of public interests and safeguard the right of investors to obtain the legitimate interests to further optimize the investment environment and promote the steady and fast national economic development in China.