

# Towards a comprehensive dispute settlement system in a China-EU bilateral investment treaty

Citation for published version (APA):

Zhao, C. (2020). *Towards a comprehensive dispute settlement system in a China-EU bilateral investment treaty*. [Doctoral Thesis, Maastricht University]. ProefschriftMaken. <https://doi.org/10.26481/dis.20201214cz>

## Document status and date:

Published: 01/01/2020

## DOI:

[10.26481/dis.20201214cz](https://doi.org/10.26481/dis.20201214cz)

## Document Version:

Publisher's PDF, also known as Version of record

## Please check the document version of this publication:

- A submitted manuscript is the version of the article upon submission and before peer-review. There can be important differences between the submitted version and the official published version of record. People interested in the research are advised to contact the author for the final version of the publication, or visit the DOI to the publisher's website.
- The final author version and the galley proof are versions of the publication after peer review.
- The final published version features the final layout of the paper including the volume, issue and page numbers.

[Link to publication](#)

## General rights

Copyright and moral rights for the publications made accessible in the public portal are retained by the authors and/or other copyright owners and it is a condition of accessing publications that users recognise and abide by the legal requirements associated with these rights.

- Users may download and print one copy of any publication from the public portal for the purpose of private study or research.
- You may not further distribute the material or use it for any profit-making activity or commercial gain
- You may freely distribute the URL identifying the publication in the public portal.

If the publication is distributed under the terms of Article 25fa of the Dutch Copyright Act, indicated by the "Taverne" license above, please follow below link for the End User Agreement:

[www.umlib.nl/taverne-license](http://www.umlib.nl/taverne-license)

## Take down policy

If you believe that this document breaches copyright please contact us at:

[repository@maastrichtuniversity.nl](mailto:repository@maastrichtuniversity.nl)

providing details and we will investigate your claim.

Download date: 20 Apr. 2024

## Summary

China and the EU are two of the biggest players in international investment. With the proliferation of international investment agreements throughout the world, China and the EU have also made concerted efforts to negotiate a China-EU Bilateral Investment Treaty. This prospective bilateral investment treaty (hereinafter “BIT”) will replace the 25 existing BITs between China and 27 EU Member States with one single comprehensive investment agreement. Since China and the EU have presented conflicting attitudes regarding various issues in investment dispute resolution, disagreements regarding what constitutes appropriate dispute settlement systems in the prospective China-EU BIT is expected to be one of the major stumbling blocks in the negotiations. Based on the exploration of the legal cultural characteristics in China’s and the EU’s dispute settlement mechanisms (hereinafter “DSMs”) and the influence thereof on their relevant internal and international practice, as well as their current investment legal relationship, the present thesis anticipates both parties’ possible proposals, discusses the potential thorny issues and recommends solutions that are worthy of consideration.

The legal cultural features influenced by the legal traditions of China and the EU and presented in their internal dispute settlement systems are discussed respectively in the first place. In China, traditional philosophies, especially Confucianism, constituted the ideological foundation of Chinese legal culture. Under Confucianism, harmony was particularly prioritized and took the central position. As a result, dispute settlement focused on restoring a harmonious relationship through amicable informal DSMs. The core values of traditional Chinese philosophies have been arguably inherited by contemporary Chinese ideology, and non-adjudicated solutions to disputes through amicable mechanisms are consistently preferred. Different from traditional philosophies, the socialist rule of law is established, but it is subject to the overall objective of socialist harmony. Concerning dispute settlement in the Chinese legal system, six DSMs act as the main avenues for disputes arising from foreign investment, including negotiation, mediation, arbitration, complaints coordination for foreign investment, administrative review, and litigation. Examining the procedural design of these DSMs and the general structure of China’s dispute settlement system from a legal cultural perspective, elements from Chinese ideologies can be identified: the promotion of amicable DSMs aims at restoring harmony between disputing parties as well as in the society; the extensive use of mediation is in line with the requirements of various legal cultural elements; and even the construction of the socialist rule of law is combined with the pursuit of harmony.

Regarding the traditional values preserved in European legal history, three constants—personalism, legalism and intellectualism—in particular formed the basis of the European legal culture of dispute settlement. Law is taken as the guarantor of justice, fairness and legal rights; the insistence on the rule of law ensures the supremacy of law; as a normal way of resolving disputes, litigation focuses on preserving substantive rights and procedural justice and, correspondingly, judges must make decisions according to law following due process. With regard to the commonly available DSMs for investment disputes in EU Member States, mediation, arbitration and litigation are identified. In addition to EU Member States’ relevant rules on these DSMs, the Union has also taken actions to regulate DSMs. The common

underlying motivation here is to preserve individuals' rights to access to justice, effective remedies and fair trial, which reflect the common values and principles arising from the constitutional tradition shared by the EU Member States. Taking a legal cultural perspective to analyse the DSMs in the EU Member States and the Union's relevant regulating measures, three points deserve attention: a consistent pursuit of the rule of law can be identified in dispute settlement; litigation has been commonly used, which focuses on realizing substantive and procedural justice, and; the increased attention on mediation is based on the recognition of its function in ensuring access to justice.

By comparison, the diverse features of dispute resolution employed by China and by the EU are typically reflected within legal culture, the perception of law, the role of law, and the objective of dispute settlement. The legal cultural characteristics of dispute settlement in China and those of the EU have further affected their legal systems, respectively. China's dispute settlement system shows a strong preference for amicable DSMs, while in the EU the focus is on the use of litigation. In addition, China arguably adopts a service-based doctrine of dispute settlement, but in the EU, DSMs are used to realize justice and to serve a justice-based doctrine. Furthermore, both China and the EU have made efforts to enhance the use of mediation in dispute settlement, but China's preference is based on the pursuit of social harmony, while the EU uses this DSM as an alternative way of realizing access to justice.

In terms of the approaches in international investment dispute settlement, two DSMs, state-state mechanisms for resolving disputes about treaty application and implementation as well as investor-state mechanisms for investors to bring cases against host states regarding complaints related to specific investments, are discussed. For state-state dispute settlement, a hybrid approach combining diplomatic consultations and ad hoc arbitration has been consistently adopted in China's Model BITs and most of its concluded International Investment Agreements (hereinafter "IIAs"). In addition, China's most recent treaty practice adjusts this hybrid approach to a quasi-WTO dispute settlement panel proceedings model, which in fact has been the practice of the state-state DSMs under its FTAs. Regarding investor-state dispute settlement, both the China Model BITs and its concluded IIAs witnessed the changes of China's attitude towards investor-state arbitration over time: from no acceptance of investor-state arbitration or acceptance of international arbitration only for disputes about the amount of compensation for expropriation, to an overall acceptance of investor-state arbitration, and now the acceptance of investor-state arbitration is being carefully revised. Until now, there have been eight investor-state dispute arbitration cases brought under the IIAs concluded by China. Possible underlying reasons for this relatively small number include the Chinese government's preference for the amicable settlement of investment disputes to preserve harmony and its political image as a friendly host state, together with foreign investors' worries about the Chinese government's retaliation and the lucrativeness of the Chinese market. In brief, China's practice resonates with some of its legal cultural characteristics in dispute settlement, such as the preference for amicable settlements and confidentiality in the dispute settlement process. At the same time, it is also clear that China has increasingly recognized the function of international adjudication in state-state and investor-state dispute settlement.

Similarly, the EU's approach to state-state trade and investment dispute settlement is mainly reflected in its FTAs and IIAs, and performance in the WTO Dispute Settlement System. The state-state DSMs laid out in the EU's FTAs and IIAs has chronologically shifted from a diplomatic approach to a quasi-WTO dispute settlement panel proceedings model. Along with its supportive attitude towards alternative DSMs, the EU has shown a preference for the judicial characteristics of the WTO Dispute Settlement System. Regarding investor-state dispute settlement, before 2009, EU Member States had the competence to conclude IIAs with third states, and they were quite active and productive in this regard. Most of these IIAs provide for amicable DSMs as well as arbitration, and many cases have been heard under the latter. The Lisbon Treaty brought about a shift in competence to conclude IIAs from the EU Member States to the Union. In the three IIAs that have been concluded by the Union since 2009, a ground-breaking approach to investor-state dispute settlement—the Investment Court System (ICS)—has been adopted consistently. In the ICS, amicable DSMs, including negotiation, mediation and consultations are provided and strengthened, acting as alternative ways to have access to justice. For adjudication, the ICS establishes a standing two-tiered court-like mechanism with typical judicial characteristics. The pool of arbitrators who may be appointed to adjudicate a particular dispute in a specific case is supposed to be pre-selected by treaty parties, and the dispute settlement proceedings are to be operated with great procedural transparency. At the same time, the joint committee and treaty parties are afforded significant roles and mechanisms for scrutinizing claims are created in particular. It can be said that from the proposal to reform the WTO Dispute Settlement System, the gradually improved state-state DSMs in its FTAs and IIAs, to the ICS, the EU's direction is clear: it calls for building a multilateral, judicialized and permanent system that respects the international rule of law to resolve international economic disputes.

Comparing China's and the EU's practice in international investment dispute settlement, both similarities and differences can be identified. For state-state dispute settlement, China's and the EU's most recent IIAs similarly adopt a quasi-WTO dispute settlement panel proceedings model, although there are differences in the details. Regarding investor-state dispute settlement, the two parties seem to have different perceptions on the objective of the whole system and the focus among the various DSMs. China puts its emphasis on settling disputes amicably and restoring harmonious relationships, while the EU cares more about realizing the international rule of law and developing jurisprudence through the system. Such differences correspondingly resonate with their internal practice and legal cultural characteristics, especially China's traditional preference for harmony and the EU's consistent pursuit of the rule of law.

Taking a particular look at the investment legal relationship between China and the EU, before 2009, the Union only concluded general economic cooperation agreements with China. While, at the same time, by exercising their treaty negotiating and concluding competence, China and EU Member States concluded 26 IIAs. Two categories of DSMs exist in these Agreements for investment dispute settlement: one for state-state and one for investor-state dispute settlement. The provisions on state-state DSMs are quite similar to each other: compulsory consultations through diplomatic channels is required as the first step; only if this fails, disputes can be submitted to ad hoc arbitration. In contrast, the situation of investor-

state DSMs is more complex. Before 1997, the IIAs are characterized by a limited acceptance of investor-state arbitration, while the IIAs signed thereafter reflect an overall acceptance of investor-state arbitration. There have only been two investor-state arbitration cases under these Agreements.

The dispute settlement system in the prospective China-EU BIT is expected to be composed of two sub-systems—one for state-state dispute settlement and one for investor-state dispute settlement. In terms of the former, it is appropriate to take the amicable resolution of disputes as the core objective. Disputes about the interpretation and application of treaty provisions should be allowed, based on which, treaty parties can raise diplomatic protection claims, interpretive claims and claims for declaratory relief. Specific DSMs within the state-state dispute settlement system can be divided into two categories—amicable and adjudicative ones. The former normally comes into play in the first place possibly through negotiation/consultations and/or mediation. A quasi-WTO dispute settlement panel proceedings mechanism serves as the general structure for the latter. In this regard, a problematic issue may be the composition of tribunals, for which China and the EU are likely to reach an agreement on pre-establishing a roster of adjudicators while leaving some room for party autonomy in specific cases. Another issue that deserves attention is procedural transparency. For a China-EU BIT, opening the whole process of adjudication to the public may be rejected by China, but third-party participation by submitting *amicus curiae* briefs is likely to be acceptable and even recommended. Regarding the effect of the decisions of tribunals, incorporating a provision similar to Article 3.2 of the DSU is anticipated to be the most acceptable option, which means the rulings would only have a precedential value instead of being binding on all following cases.

Regarding the investor-state dispute settlement system under the prospective China-EU BIT, amicable DSMs should focus on settling disputes amicably, while the aim of adjudication is supposed to be the development of jurisprudence and the realization of the international rule of law. Both amicable DSMs and the adjudication process cover disputes between an investor of one treaty party and the other treaty party concerning treatment alleged to breach a provision of investment protection and to cause damages. Specific DSMs within this system can be divided into three categories: amicable mechanisms, adjudication mechanisms and local remedies. Amicable DSMs are expected to include voluntary negotiation and mediation, as well as compulsory consultations as a precondition to adjudication. In particular, five issues regarding the procedural design of mediation deserve attention: first, the basic principle of voluntariness should be adhered to; second, the qualification of potential mediators should be based upon the agreement of disputing parties, and it is appropriate to establish various standards for mediators and adjudicators; third, interest-based mediation should be prescribed as the default type of mechanism, unless disputing parties agree otherwise; fourth, it is better to keep confidentiality as a fundamental feature, unless disputing parties reach a different agreement, and; finally, in order to trigger the enforcement system, the settlement agreements reached in mediation can be incorporated into the decision-making stage of adjudication. In international adjudication, China's attitude towards the EU's ICS is expected to be modestly positive. The adjudicatory nature of the ICS would be generally acceptable, but China may argue for eliminating the system's exclusive

jurisdiction to open the door for other arbitration institutions. A pre-established roster of adjudicators selected by treaty parties could be preferred by both parties, but this is suggested to come with the disputing parties' right to choose the adjudicators from the roster. In addition, a possible agreement is likely to be reached on the prospective binding force of the joint committee's treaty interpretations. Procedural transparency should be respected in general, but it is better to allow for a reasonable degree of party autonomy to prevent public disclosure. Furthermore, it does not seem to be necessary to have an appeal mechanism in a China-EU BIT. Regarding the relationship between local remedies and international DSMs, the prospective China-EU BIT may incorporate an article adopting the variant of the "fork-in-the-road" approach, and exhausting local remedies would not be required as a precondition to international adjudication.

Finally, the relationship between the state-state and investor-state dispute settlement systems in the prospective China-EU BIT are assessed. Diplomatic claims in state-state dispute settlement would be prohibited after investor-state dispute settlement has been resorted to by investors, while interpretive claims and declaratory relief claims should be generally allowed. At the same time, it is recommended to explicitly prohibit parallel proceedings concerning the same challenged measure. In order to preserve the system's consistency and predictability, for sequential relevant state-state dispute settlement and investor-state dispute settlement cases, it is necessary to incorporate a provision stressing the role of the dispute settlement system in providing security and predictability. Innovative combinations of state-state and investor-state dispute settlement are particularly suggested to be realized through three ways: establishing state-investor-state mediation, combining the rosters of adjudicators for state-state and investor-state dispute settlement and, granting relevant investors procedural rights in state-state dispute settlement proceedings.

It is believed that, with thoughtfully-designed procedural arrangements, the comprehensive dispute settlement system in the prospective China-EU BIT would be palatable to the treaty parties and attractive to potential users and, more importantly, may contribute to successful investment dispute settlement under, and sustainable development of, the prospective China-EU BIT.