THE LEGAL HURDLES PREVENTING A U.S.-CHINA BILATERAL INVESTMENT TREATY: PROBLEMS WITH NATIONAL SECURITY, ENVIRONMENTAL AND LABOR STANDARDS, AND INVESTOR-STATE DISPUTE SETTLEMENT MECHANISMS

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Abstract

This Article focuses on the legal obstacles, in particular national security concerns, environmental and labor regulation issues, and investor-state dispute resolution mechanisms, preventing a U.S.-China Bilateral Investment Treaty ("BIT"). It also discusses the extent to which such a BIT is necessary for the American or Chinese investors. The Article argues that a successful BIT between these two nations will not result from the fifth Strategic and Economic Dialogue ("S&ED") or in the immediate future. Instead, a U.S.-China BIT is more likely to result once the balance of China's outward foreign direct investments ("FDI") outweigh the inward FDI. Therefore, a U.S.-China BIT is more likely to result from a sixth S&ED.

TABLE OF CONTENTS

I. INTRODUCTION .........................................................304
II. LEGAL HURDLES TO A U.S.-CHINA BIT .........................309
   A. National Security .............................................309
   B. Environmental and Labor Standards ........................313
   C. Investor-State Dispute Mechanisms ..........................326
III. U.S.-CHINA BIT UNLIKELY IN THE IMMEDIATE FUTURE .........335
IV. CONCLUSION ............................................................342

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I. INTRODUCTION

After the Tiananmen Square incident in China in June 1989, discussions of a Bilateral Investment Treaty ("BIT") between China and the United States ceased. After the fourth Strategic and Economic Dialogue ("S&ED") meeting between the two nations, the increase in trade and investment flows between the two countries propelled them to resume negotiations in June 2008. Both nations have interests in negotiating a successful BIT. For the United States, "a BIT would help to increase the enforcement of intellectual property rights and investment protection in general, especially vis-à-vis state-owned companies" in China. For China, a BIT would help mitigate "protectionist sentiments against Chinese investments" that result from national security concerns in the United States. Those who support a U.S.-China BIT argue that the BIT will provide investors with more protection against expropriation, with fewer restrictions on corporate transfers of funds, and access to international arbitration when disputes arise between the investors and the government. Because the United States has the largest economy and China has the second largest economy in the world, and because the combined capital flows of these two countries eclipse those of most other countries combined, a U.S.-China BIT will likely have a great influence on future BIT negotiations of other countries.

2 Id. at 4.
4 Id.
5 Id.
6 The Economist Intelligence Unit, supra note 1, at 30.
The United States is seeking an agreement that would further the goals of the U.S. BIT program: protecting U.S. investment abroad; encouraging "the adoption of the market-oriented domestic policies that treat private investment in an open, transparent, and non-discriminatory way"; and supporting "the development of international law standards consistent with these objectives." The United States insists on signing BITs based on its 2012 Model BIT. The United States has a reputation for being inflexible during BIT negotiations, as it is typically unwilling to deviate from its Model BIT. Consequently, if a state is unwilling to accept a BIT predominately based on the U.S. Model BIT then no BIT would result. The 2012 U.S. Model BIT has thirty-seven articles and a few appendices, while the current Chinese Model BIT (Version III) has a preamble and thirteen articles. Based on some of the latest international investment agreements China has signed, it appears that the Chinese BIT approach is moving towards the American approach, especially in regard to the substantial and procedural investment protection. Nevertheless, for U.S. investors to determine whether or not a potential investment is permitted in China, they should refer to (1) the Investment Guidance 2002, and (2) the attached Guiding

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11 Id.


14 Berger, supra note 3, at 183.

Catalogue of Industries for Foreign Investment. The Investment Guidance and the Guiding Catalogue categorize all potential foreign investment projects into four subcategories: (1) encouraged, (2) restricted, (3) prohibited, and (4) permitted. The encouraged, restricted, and prohibited classifications are specifically defined, while all other investments are classified as permitted by default. If China were to accept a BIT based on the 2012 U.S. Model BIT, then it would indicate a further "revolution of its BIT practice and its national regulatory system," which would require some "behind-the-border regulatory changes." Past BIT negotiations between China and the United States have been unsuccessful for several reasons, such as differing views on pre-establishment phase protection, negative list approach, political issues, national security policies, environmental and labor standards, and investor-state dispute settlement provisions. Pre-establishment phase protection grants foreign investors the right to establish investments and guarantee them access to the host state's market. The divergent views China and the United States have on pre-establishment phase protection and China's desire to maintain a degree of discretion for the protection of its state-owned business sector have contributed to the unsuccessful BIT negotiations. Another area of disagreement between the two nations is that the United States uses the negative list approach and China uses the

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18 See id.
19 See Berger, *supra* note 3, at 182-83.
positive list approach. Under the negative list approach, the foreign investor is granted market access in all sectors except those that are explicitly prohibited in the agreement, whereas under the positive list approach, the foreign investor only has access to the sectors listed in the agreement and must seek approval for all other sectors.

However, during the meeting of the fifth U.S.-China S&ED in July 2013, China agreed to adopt the pre-establishment phase protection scheme and the negative list approach—both found in the 2012 U.S. Model BIT. Therefore, the pre-establishment phase model and the negative list approach are no longer legal hurdles to a successful U.S.-China BIT negotiation.

However, there are still several other factors that remain that may present problems during the U.S.-China BIT negotiations. For example, political tension between the United States and China presents an obstacle that may hinder a successful negotiation between the two countries. For instance, the Edward Snowden controversy has strained the relationship between the United States and China. The United States requested that China turn over Snowden, who was accused of leaking thousands of classified U.S. intelligence information, but Hong Kong permitted Snowden to leave the country. The U.S. Deputy Secretary of State, William Burns, expressed that the United States was “disappointed with how the authorities in Beijing and Hong Kong handled the Snowden case, which undermined our effort to build the trust needed to manage difficult issues . . . .” Consequently, the Snowden incident added tension to the already temperamental

23 Id. at 182.
24 Id.
26 Id.
28 See id.
29 Id.
30 Id.
31 Id.
relationship between the United States and China.\textsuperscript{32}

Even though China’s BIT policies are progressing toward emulating the U.S. Model BITs by including sections on most-favored nation ("MFN") treatment and national treatment of foreign investors,\textsuperscript{33} and agreeing to the pre-establishment phase model and negative list approach,\textsuperscript{34} it is unlikely that a successful BIT between the United States and China will result from the fifth U.S.-China S&ED meeting because of the national security concerns that each country possesses toward the other, the differing viewpoints on environmental and labor standards, and the differing viewpoints on investor-state dispute settlement (i.e., arbitration) mechanisms.\textsuperscript{35} Thus, the significant difference between the U.S. Model BIT and Chinese Model BIT, and the two countries’ conflicting interests and positions, will likely turn the U.S.-China BIT negotiations into a difficult and prolonged process.\textsuperscript{36} Although, if the trend in Chinese BIT policies continues to progress toward the American model, and if China’s outward foreign direct investments ("FDI") increases to surpass its inward FDI, the likelihood of a successful future U.S.-China BIT may occur at a sixth S&ED.\textsuperscript{37} Accordingly, Part II of this Article will discuss the legal hurdles (i.e., national security, environmental and labor, and arbitration) preventing a U.S.-China BIT in more detail, and Part III will explain why it is unlikely that a successful U.S.-China BIT will be achieved in the immediate future and that chances of success are more likely in the distant future. Part III will also address whether or not a U.S.-China BIT is necessary for American or Chinese investors. Although this Article focuses on BITs, some discussions will include Free Trade Agreements ("FTAs") because FTAs are broader in scope and contain investment chapters that resemble those found in BITs, which help

\textsuperscript{32} Id.
\textsuperscript{33} Berger, \emph{supra} note 3, at 183; The Economist Intelligence Unit, \emph{supra} note 1, at 13, 14.
\textsuperscript{34} Joint Statement, \emph{supra} note 25.
\textsuperscript{35} Id.; see The Economist Intelligence Unit, \emph{supra} note 1, at 9-10, 22-24.
\textsuperscript{36} Qiao Liu & Xiang Ren, \emph{Transfer of Funds in China-U.S. BIT Negotiations: Comparing the Articles of Agreement of the IMF}, 11 J. INT’L TRADE L. POL’Y 6, 6 (2012).
\textsuperscript{37} See id. at 6-7.
demonstrate the past practices in American and Chinese investment policies.\textsuperscript{38}

\section*{II. LEGAL HURDLES TO A U.S.-CHINA BIT}

\subsection*{A. National Security}

Because of the current political situation between the United States and China, an obstacle to a successful BIT negotiation is the national security concerns that arise from mergers and acquisitions.\textsuperscript{39} The U.S. government’s consistent rejection of state-controlled Chinese companies’ attempts to merge or acquire U.S. companies is raising concerns with the Chinese government.\textsuperscript{40} The Committee on Foreign Investment in the United States (“CFIUS”) reviews all potential foreign investments in the United States to assess the national security implications.\textsuperscript{41} The CFIUS generally “clears foreign investment proposals within 30 days,” but it can subject certain proposals to an additional forty-five-day scrutiny review.\textsuperscript{42} In 2005, the CFIUS blocked the $18.5 billion bid from the state-owned company China National Offshore Oil Corporation to acquire Unocal, the American oil company, due to national security concerns of allowing Chinese investors to take over a company that would affect the U.S. energy sector.\textsuperscript{43} Again, in 2008, the CFIUS blocked the $2.2 billion bid by the Chinese company Huawei Technologies for the U.S. company 3Com because of the Chinese company’s connection with China’s military and

\begin{thebibliography}{99}
\bibitem{Berger} Berger, \textit{supra} note 3, at 183.
\bibitem{Morrison} The Economist Intelligence Unit, \textit{supra} note 1, at 28.
\bibitem{Berger2} Berger, \textit{supra} note 3, at 183; The Economist Intelligence Unit, \textit{supra} note 1, at 28.
\end{thebibliography}
government.\textsuperscript{44}

The failure of the China National Offshore Oil Corporation’s and Huawei Technologies’ acquisitions reveal that the CFIUS views large national Chinese companies as being controlled by the Chinese government; therefore, the acquisitions may become potential tools the Chinese government uses to accomplish its strategic objectives.\textsuperscript{45} For the CFIUS, permitting the aforementioned acquisitions would be a national security risk to the United States because it would provide the Chinese government with a medium to gain access to sensitive information technology or critical energy sources.\textsuperscript{46}

On June 20, 2008, the U.S. Department of State released a fact sheet explaining that a U.S.-China BIT “would not interfere with the ability of the United States to take any action necessary to protect the national security.”\textsuperscript{47} It further states that the “essential security” exception in the U.S. BITs permits the CFIUS “to condition or block a Chinese acquisition of control over a U.S. company.”\textsuperscript{48} Thus, China is likely to demand the inclusion of “legal safeguards against political reviews” of Chinese investments by the CFIUS, which the United States would unlikely grant.\textsuperscript{49} However, in a joint statement from the fifth S&ED session, the United States agreed that CFIUS’ reviews will focus exclusively on national security and not on economic or other national policies.\textsuperscript{50} It further states that CFIUS would continue to review potential transactions as expeditiously as possible and aims for processes that would mitigate, rather than prohibit, a transaction when possible.\textsuperscript{51}

Like the United States, China also uses national security as a

\textsuperscript{44} The Economist Intelligence Unit, \textit{supra} note 1, at 28.
\textsuperscript{45} \textit{Id.}
\textsuperscript{46} \textit{Id.}
\textsuperscript{48} \textit{Id.}
\textsuperscript{49} Berger, \textit{supra} note 3, at 183-84.
\textsuperscript{50} Joint Statement, \textit{supra} note 25.
\textsuperscript{51} \textit{Id.}
justification for blocking mergers and acquisitions of Chinese companies by foreign investors and reserving certain industries that the government wants to maintain for state-owned enterprises.\(^52\) In China, national security review involves an interministerial joint committee established by the National Development and Reform Commission and the Ministry of Commerce under the guidance of the State Council and the other departments that oversee the industries and sectors in the proposed foreign acquisition.\(^53\) The national security review assesses the impact of the foreign investor’s proposed merger and acquisition on China’s national defense and security (which includes the domestic capability to provide services and produce products), on its national economy, on its public order, and on its research and development capabilities needed for national security.\(^54\) In February 2011, the Chinese government clarified that national security review is required if foreign investors are attempting to acquire “military-related enterprises such as: enterprises in the military industry and supporting firms; enterprises in the vicinity of strategic and sensitive military facilities; [or] other units that are related to national defence [sic] and security.”\(^55\) Foreign investors will also be subjected to national economic security review if the merger and acquisition involves “major agricultural products, major energy and resources; infrastructure; transport; key technologies; [and] manufacture of major equipment . . . .”\(^56\) Thus, the scope of review in China is broader than the scope in the United States.\(^57\)

\(^{52}\) Kong, supra note 20, at 186-87.


\(^{54}\) Id.

\(^{55}\) Id. at 26.

\(^{56}\) Id. at 26-27.

\(^{57}\) Compare Davies, supra note 53, at 27 (“The national security review examines the impact of the proposed M&A by foreign investors of a domestic enterprise on: national defence [sic] and security (including on the domestic capability to produce products or provide services, and on relevant facilities, needed for national defence [sic]); [and] stable running of the national economy . . . .”), with Joint Statement, supra note 25 (“The United States commits that all investment reviews by the Committee on Foreign Investment in the United States (CFIUS) focus exclusively on national security, not economic or other national policies.”).
CFIUS’ rejections of proposed transactions by Chinese investors may have induced the Joint Committee to take retaliatory measures against proposed transactions by U.S. investors in China.\textsuperscript{58} For instance, the Ministry of Commerce used its Anti-monopoly Law to block Coca-Cola, a U.S. company, from making a $2.4 billion bid to acquire China’s Huiyuan Juice Group ("Huiyuan")—the leading pure juice brand in China.\textsuperscript{59} Even if Coca-Cola had acquired Huiyuan, Coca-Cola would not have had a monopoly because Huiyuan’s sales and shares in the juice market had dropped.\textsuperscript{60} Arguably, China’s rejection of Coca-Cola’s merger can be viewed as retaliation to CFIUS’ rejections of several Chinese companies’ attempts to acquire U.S. companies, as it is evident that no monopoly would have arisen in Coca-Cola’s acquisition of Huiyuan.\textsuperscript{61}

Furthermore, for U.S. investors, access to some of China’s most profitable markets are often reserved or dominated by state-owned enterprises because China alleges national security issues, which have caused concern among U.S. investors in China.\textsuperscript{62} For instance, U.S. incorporated banks are not allowed “to trade bonds in the inter-bank market, both for their customers or their own accounts” in China in the same manner as Chinese investment banks.\textsuperscript{63} Additionally, U.S. investors are dissatisfied with longstanding barriers that limit their investment options, such as restrictions on foreign ownership of Chinese firms.\textsuperscript{64} Because the United States has “relatively few limitations on foreign investments,” a successful BIT would help “even the playing field for U.S. investors in China.”\textsuperscript{65} However, the distrust between the United States and China may make national security concerns an insurmountable legal hurdle that hinders the U.S.-China

\textsuperscript{59} See id.
\textsuperscript{60} See id.
\textsuperscript{61} See id.
\textsuperscript{62} See Kong, supra note 20, at 184.
\textsuperscript{63} See id. at 181, 184.
\textsuperscript{64} See id. at 184-85.
\textsuperscript{65} See id. at 186.
BIT negotiations.\textsuperscript{66}

\textbf{B. Environmental and Labor Standards}

Another legal hurdle that may be detrimental to the U.S.-China BIT negotiations is the differing viewpoints that the respective countries have on environmental and labor standards.\textsuperscript{67} Continuing from the 2004 U.S. Model BIT,\textsuperscript{68} the 2012 U.S. Model BIT\textsuperscript{69} maintains provisions pertaining to both environmental and labor concerns but with some modifications.\textsuperscript{70} According to the provisions, it is "inappropriate to encourage investment by weakening or reducing the protections afforded" to domestic environmental or labor laws.\textsuperscript{71} The latest Model BIT adds new responsibilities not to "waive or otherwise derogate" from or fail to "effectively enforce" domestic laws in order to attract investments and to reaffirm their commitments to the International Labor Organization Declaration on Fundamental Principles and Rights at Work and its Follow-Up.\textsuperscript{72} The 2012 U.S. Model BIT does not require environmental or labor restrictions beyond the existing national laws.\textsuperscript{73} Violations of the environmental or labor provisions in the 2012 U.S. Model BIT are not subject to any type of dispute resolution, but instead they are subject to a consultation procedure.\textsuperscript{74} The 2012 U.S. Model BIT also emphasizes the importance of multilateral environmental agreements and improves the consultation provisions.\textsuperscript{75}

\begin{itemize}
\item \textsuperscript{66} See id. at 188.
\item \textsuperscript{69} See U.S. Model BIT, supra note 67.
\item \textsuperscript{71} U.S. Model BIT, supra note 67, at arts. 12(2), 13(2).
\item \textsuperscript{72} Id.
\item \textsuperscript{73} See The Economist Intelligence Unit, supra note 1, at 9.
\item \textsuperscript{74} See U.S. Model BIT, supra note 67, at arts. 12(6), 13(4).
\item \textsuperscript{75} See id. at art. 12(1).
\end{itemize}
Nevertheless, these consultation procedures are a relatively weak mechanism that the United States is implementing in attempts to ensure that the other state enforces the environmental and labor provisions.

Unlike the 2012 U.S. Model BIT, the latest Chinese Model BIT (Version III) does not contain any provisions on environmental standards.76 China’s environmental problems are severe by almost any standard.77 According to the World Bank, China’s cities are some of the most polluted on earth, with sixteen out of the twenty most polluted cities in the world located in China.78 Some of the major environmental issues are “[a]ir and water pollution, water scarcity, desertification, land contamination and health problems among residents” in the heavily polluted areas.79 China’s water pollution problem is attributed to the fact that only approximately fifty percent of the urban sewage is treated, and nearly 278 out of China’s 661 cities had no sewage treatment plants in 2005,80 however, by 2012, 648 cities were establishing treatment plants.81 Even though the majority of the cities in China now possess sewage treatment plants, some of them operate at below capacity or do not function at all, so the water pollution problem persists.82

The environmental problems in China have been exacerbated because of the political culture and regulatory structures that place economic growth as a priority without considering the environmental ramifications.83 As China’s economy continues to grow and the per capita prosperity increases, the environmental problems will likely worsen without more efficient use of energy and water.84 Accordingly,

76 See GALLAGHER & SHAN, supra note 12, at Appendix IV: Chinese Model BIT Version III.
77 See The Economist Intelligence Unit, supra note 1, at 22.
78 See id. at 22.
79 See id.
80 See id.
83 See The Economist Intelligence Unit, supra note 1, at 22.
84 Id. at 23.
the Chinese government is paying more attention to environmental sustainability.\textsuperscript{85} For instance, because of the pollution crisis in China, the government has recently introduced regulations that permit the court to sentence serious polluters to death.\textsuperscript{86} China, however, has failed to meet its main targets for reducing pollution, and its structural constraints continue to be an obstacle to meeting its green initiative goals.\textsuperscript{87}

Another environmental issue that has been a focus for Washington during previous BIT discussions with China that will likely be a prominent issue during these BIT negotiations is the issue of global warming and climate change.\textsuperscript{88} Due to the growth in China’s economy, its large population, and its inefficient industrial sector, China is the “world’s largest emitter of carbon dioxide.”\textsuperscript{89} Therefore, China is now included in any global climate-change initiative.\textsuperscript{90} Because of China’s need to sustain its economic growth, it has been reluctant to accept any initiative that would mandate emissions targets on all countries.\textsuperscript{91}

However, China wants to shed its reputation as the world’s biggest polluter.\textsuperscript{92} Thus, it has launched a pilot project for a carbon emission-trading scheme in Shenzhen, with six additional cities to follow.\textsuperscript{93} Under the carbon-trading scheme, companies are given credits in which each credit is equivalent to one ton of carbon emissions.\textsuperscript{94} To ensure that companies limit their carbon emissions

\begin{thebibliography}{99}
\bibitem{85} Id.
\bibitem{86} Ben Blanchard & Andrew Roche, \textit{China Threatens Death Penalty for Serious Polluters}, \textit{REUTERS} (June 19, 2013), \url{http://in.reuters.com/article/2013/06/19/us-china-pollution-idINBRE95110D20130619}.
\bibitem{87} See The Economist Intelligence Unit, \textit{supra} note 1, at 23.
\bibitem{88} Id. at 26.
\bibitem{89} Id.
\bibitem{90} Id.
\bibitem{92} Puneet Pal Singh, \textit{Can China Achieve Success with Carbon Trading Scheme?}, \textit{BBC NEWS} (June 17, 2013), \url{http://www.bbc.co.uk/news/business-22932816}.
\bibitem{93} Id.
\bibitem{94} Id.
\end{thebibliography}
output, there is a cap on the number of credits issued to each company.95 Based on the pilot project, the companies must measure and report their carbon emissions and turn in one allowance credit for every ton of carbon they emit.96 If a company releases less carbon than it is allowed, then it may trade its excess credits.97 However, if a company releases more carbon than its allotted amount, it must purchase credits to cover the extra carbon emissions it releases, thereby placing a cost on pollution.98 The Chinese government will allow 635 companies in Shenzhen approximately 100 million tons of carbon emission for the next three years, representing a thirty percent reduction in carbon emission per unit of output.99 The exact amount of reduction in carbon emission per unit of output will need to be adjusted depending on the companies’ actual production of goods and services.100

However, analysts have suggested that the 100 million tons allocation is 10 million more than the companies would probably have emitted between 2013 and 2015, which may flood the market with excess permits.101 China’s pilot project is similar to Europe’s carbon emission trading scheme, but Europe’s program has been running for ten years and it is still ineffective because the program has been plagued with having excess permits on the market.102 Therefore, China must be cautious not to allocate too many permits that would flood the market with excess permits, which will cause the Chinese pilot project to experience the same problems the European program is experiencing.103 Whether China’s carbon trading scheme will be effective in ridding China of its title as the world’s largest polluter is yet to be determined

95 Id.
96 Id.
98 See Singh, supra note 92.
100 Id.
101 Id.
102 Id.
103 See id.
because industry leaders have warned of the potential difficulties in carbon financing, quota allocation and statistics collection, and the monitoring and use of the assessment systems for the project.\footnote{See J.P., \textit{supra} note 99.}

To China's credit, its focus on the environment is more pronounced, in comparison to previous years, as China included environmental goals in its high-level policy,\footnote{See The Economist Intelligence Unit, \textit{supra} note 1, at 23.} such as the Twelfth Five Year Plan (covering 2011 to 2015).\footnote{\textit{China's Twelfth Five Year Plan (2011-2015)—the Full English Version}, BRIT. CHAMBER OF COM. IN CHINA, \url{http://www.britishchamber.cn/content/chinas-twelfth-five-year-plan-2011-2015-full-english-version} (last visited May 25, 2015).} According to the Twelfth Five Year Plan, China is planning to invest ¥3.4 trillion into projects that focus on protecting the environment in the next five years.\footnote{China Briefing, \textit{China Unveils its 12th Five-Year Plan on Environmental Protection}, CHINA BRIEFING: MAG. & DAILY NEWS SERV. (Dec. 23, 2011), \url{http://www.china-briefing.com/news/2011/12/23/china-unveils-12th-five-year-plan-on-environmental-protection.html}.} The plan outlines specific environmental projects, such as major pollutants reduction through sewage treatment, environmental protection of rural areas through pollution control from agriculture, and environmental improvement of water, air, and soil.\footnote{Id.}

Even though the environment is set as a priority in the plan with targets that the government aims to meet at the end of the five-year period, critics note that China has set out similar plans before; however, the political will to achieve these goals has yet to appear.\footnote{Sarah Wang, \textit{What Does China's New Five-Year Plan Address?}, BBC NEWS (Mar. 3, 2011), \url{http://www.bbc.co.uk/news/world-asia-pacific-12639898}.} The green initiatives found in the Twelfth Five Year Plan, for example, are similar to those set out in previous Five Year Plans, but those targets were not accomplished.\footnote{Id.} Furthermore, the authors of the Twelfth Five Year Plan admitted that a more mature market economy is better qualified to meet the targets set out in the plan and that a "significantly reduced role of the state in the economy" would increase the odds of meeting the
targets in the plan. The overwhelming presence of the state in the economy, as seen in the state’s “monopoly on resources and the single-minded pursuit” of attaining high gross domestic product growth, some argue explains why China’s gross domestic product growth has been less green in past years. China may increase its odds of meeting its target by allowing its Ministry of Environmental Protection to determine the environmental impact of future development projects before carrying out the projects.

Many foreign-invested organizations complain that they face stricter enforcement of rules in comparison to domestic organizations. Some argue that the rationale behind the double standard from the Chinese government is because foreign corporations have more experience adhering to more rigorous environmental protection standards from their own countries; thus, they should meet stricter regulations in China. Although a state-owned organization typically poses a greater threat to the environment in China, the state-owned organization is “well connected with local authorities,” so it does not face the stricter environmental regulations that the foreign-invested organizations face in China. This discrepancy in treatment of foreign-invested organizations versus domestic organizations is likely to encourage U.S. investors to seek a U.S.-China BIT, but it will likely also be an obstacle for a U.S.-China BIT.

China includes environmental provisions in some of its investment treaties, but it has not included mandatory environmental provisions in its latest Model BIT, unlike the U.S. Model BIT. For example, as part of the China-New Zealand FTA, both countries signed

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111 Id.
112 Id.
113 Id.
114 The Economist Intelligence Unit, supra note 1, at 23.
115 Id.
116 Id.
118 Congyan, supra note 21, at 470-72; see also U.S. Model BIT, supra note 67, at art. 12.
an Environment Cooperation Agreement ("ECA"). Like the 2012 U.S. Model BIT, under the ECA, environmental disputes that arise between New Zealand and China will be resolved through a consultation meeting. However, unlike the 2012 U.S. Model BIT, the ECA does not mention that the parties should not waive or derogate environmental laws, but instead states that the parties "agree to cooperate on environmental matters of mutual interest and benefit." Moreover, the ECA details cooperative activities that China and New Zealand have agreed to work on together to benefit the environment. Thus, the ECA is structurally different from the environmental provisions in the 2012 U.S. Model BIT.

China also included some environmental provisions in its investment treaty with Canada, which is structurally more similar to the 2012 U.S. Model BIT. Like the 2012 U.S. Model BIT, the Canada-China Foreign Investment Promotion and Protection Agreement ("FIPA") states that "it is inappropriate to encourage investment by waiving...or otherwise derogating from...environmental measures" and that environmental disputes will be addressed in a consultation between the parties.

In contrast to China’s investment treaties with Canada and New Zealand, the only mention of the environment in the China-Colombia BIT is in relation to indirect expropriation. Thus, the inclusion of

121 Id. at arts. 2, 4.
122 Id.
123 Compare id. at art. 4, with U.S. Model BIT, supra note 67, at art. 12.
125 Compare id. at art. 18, with U.S. Model BIT, supra note 67, at art. 12.
126 China-Colombia Bilateral Investment Treaty, art. 4(2)(c) (2008), available at
environmental provisions in Chinese investment treaties is not guaranteed, which can pose a problem during the U.S.-China BIT negotiations.\textsuperscript{127}

Similar to China’s investment in improving its environment, China has also recognized the importance of improving its labor standards.\textsuperscript{128} Even though China has promulgated a number of legislations to protect workers’ rights in China, the relationship between corrupt local businessmen and local officials will hinder China’s progress on enforcing labor rights.\textsuperscript{129} China’s ability to consistently implement the labor legislations has been obstructed because breaches in labor regulations are often only investigated if senior officials make such an order.\textsuperscript{130} Moreover, the workings of China’s political system also compromise the efforts of the police and the agencies that are set up to detect the illegal activities.\textsuperscript{131}

However, China has introduced the Labor Contract Law ("LCL") that went into effect on January 1, 2008, that is intended to provide greater job security for employees.\textsuperscript{132} For instance, employees with ten years or more of employment will have open-ended contracts, and employers will have to inform the unions before firing any worker.\textsuperscript{133} Even though the LCL is intended to improve working conditions for workers, the LCL is criticized for not improving conditions for the “tens of millions of migrant workers from the countryside.”\textsuperscript{134} Because China currently lacks an official trade union for these migrant workers, these unskilled workers suffer from poor labor conditions.\textsuperscript{135}

In pursuit of improving labor conditions, China’s amended LCL

\textsuperscript{127} See Wang, supra note 109.
\textsuperscript{128} The Economist Intelligence Unit, supra note 1, at 24.
\textsuperscript{129} Id.
\textsuperscript{130} Id.
\textsuperscript{131} Id.
\textsuperscript{132} Davies, supra note 53, at 30.
\textsuperscript{133} The Economist Intelligence Unit, supra note 1, at 24.
\textsuperscript{134} Id.
\textsuperscript{135} Id.
went into effect on July 1, 2013.\textsuperscript{136} The amendment seeks to close the loopholes companies utilized to pay employees a lower wage when the workers are hired through labor dispatching agencies instead of the companies’ own human resources department.\textsuperscript{137} By hiring workers through labor dispatching agencies, the employees are deemed temporary, auxiliary, or substitute employees, and companies are not required to pay temporary employees the same wage as permanent employees.\textsuperscript{138}

However, under the amended LCL, regardless of how the employees are hired (directly or indirectly), companies are now required to pay employees the same wage for similar jobs.\textsuperscript{139} Foreign companies that currently rely on hiring workers through labor dispatching agencies to save on the costs of salary and benefits must adjust their hiring practices to ensure that they are complying with the new laws.\textsuperscript{140} If companies do not adjust accordingly to the new amendment they face tougher penalties, such as fines of ¥5,000 to ¥10,000 per dispatched employee.\textsuperscript{141} However, it remains to be seen how strictly China will enforce the amended LCL.\textsuperscript{142}

Like the environmental provisions, mandatory labor provisions are not found in the latest Chinese Model BIT.\textsuperscript{143} However, China has shown that it is willing to include labor provisions in its investment treaties, as it signed a Memorandum of Understanding ("MOU") on Labor Cooperation as part of the China-New Zealand FTA.\textsuperscript{144} Similar


\textsuperscript{137} \textit{Id.}

\textsuperscript{138} \textit{Id.}

\textsuperscript{139} \textit{Id.}


\textsuperscript{141} \textit{Id.}

\textsuperscript{142} \textit{Id.}

\textsuperscript{143} See GALLAGHER & SHAN, supra note 12, at Appendix IV: Chinese Model BIT Version III.

\textsuperscript{144} China-New Zealand FTA, supra note 118, at art. 177.
to the 2012 U.S. Model BIT, the MOU reaf{}rms the party’s commitment to International Labor Organization and states that labor disputes will be settled through a consultation procedure.\footnote{China-New Zealand Memorandum of Understanding, art. 1, 4 (2008) [hereinafter China-New Zealand MOU], available at http://www.chinafta.govt.nz/1-The-agreement/1-Key-outcomes/0-downloads/MOU-NZ.pdf; see also U.S. Model BIT, supra note 67, at art. 13.} Almost verbatim from a portion of the 2012 U.S. Model BIT, the MOU states that “it is inappropriate to encourage trade or investment by weakening or reducing the protections afforded in domestic labour laws, regulations, policies and practices.”\footnote{China-New Zealand MOU, supra note 145, at art. 1(4); see also U.S. Model BIT, supra note 67, at art. 13(2).} However, the remainder of the MOU is structurally different from the 2012 U.S. Model BIT because it lists cooperative activities that China and New Zealand agree to partner in together to enhance labor laws,\footnote{See China-New Zealand MOU, supra note 145, at art. 2(2).} while the 2012 U.S. Model BIT mentions activities that the parties to the investment treaties agree not to violate.\footnote{See U.S. Model BIT, supra note 67, at art. 13(3).} Arguably, the labor provision in the 2012 U.S. Model BIT is more difficult to abide by because it prohibits behavior from the states,\footnote{See id} whereas the MOU encourages particular activities from the states.\footnote{See Michael Snarr, Will Labor Rights Be Included In U.S.-China Bilateral Investment Treaty Negotiations?, BAKERHOSTETLER (Mar. 25, 2010), http://www.chinaustradelawblog.com/2010/03/articles/investment/will-labor-rights-be-included-in-u-s-china-bilateral-investment-treaty-negotiations%E4%B8%AD%E7%BE%AE%E5%8F%8C%E8%BE%B9%E6%8A%95%E8%B5%84%E5%8D%8F%E5%AE%9A%E8%B0%88%E5%88%A4%E5%B0%86%E5%8C%85/.} Because the 2012 U.S. Model BIT includes provisions pertaining to labor rights,\footnote{See China-New Zealand MOU, supra note 145, at art. 2(2).} the U.S. government is highly likely to insist that such a provision be included in the U.S.-China BIT.\footnote{See U.S. Model BIT, supra note 67, at art. 13.} In the 2012 U.S. Model BIT, host states have an obligation to recognize and enforce domestic labor laws and make a commitment not to derogate
them.\textsuperscript{153} If a violation of the labor laws occurs, then the latest U.S. Model BIT has outlined a dispute settlement procedure in which the parties may request a consultation to resolve the breaches.\textsuperscript{154} Violations of the labor provisions in the BIT are not subject to any kind of dispute resolution, other than the aforementioned consultation procedure, which arguably is a weaker form of dispute resolution because there is no organization like the International Centre for Settlement of Investor Disputes (“ICSID”) to support the results of the consultation.\textsuperscript{155} Although there does not appear to be a record of a case in which the United States has requested a consultation with a host state for violation of the labor provision in a BIT, the United States has requested a consultation based on similar labor provisions in its FTAs with Guatemala\textsuperscript{156} and Bahrain.\textsuperscript{157}

Under the Dominican Republic-Central American-United States FTA,\textsuperscript{158} the United States launched a formal complaint against Guatemala for labor rights violations.\textsuperscript{159} This was the first instance that the United States requested a consultation with a host state for its failure to adhere to the labor provision in the FTA.\textsuperscript{160} Specifically, the United States alleged that the Guatemalan government had failed to protect workers’ rights by not enforcing the Guatemalan laws, such as the right

\textsuperscript{153} See U.S. Model BIT, supra note 67, at arts. 12 (1)-(2), 13 (1)-(2).

\textsuperscript{154} See id. at art. 13(4).

\textsuperscript{155} See id. at art. 37.


\textsuperscript{160} Id.
to collective bargaining, the right to work in adequate conditions, and the right to freedom of association. Guatemalan's failure to enforce the laws harms U.S. workers because they are competing against substandard labor practices, which shifts the balance away from U.S. workers and businesses. After the consultation, the United States and Guatemala agreed to an eighteen-point plan to rectify the issues. According to the plan, Guatemala agrees

to strengthen labor inspections, expedite and streamline the process of sanctioning employers and ordering remediation of labor violations, increase labor law compliance by exporting companies, improve the monitoring and enforcement of labor court orders, publish labor law enforcement information, and establish mechanisms to ensure that workers are paid what they are owed when factories close.

For now, the United States appears satisfied with the commitment Guatemala has made in the enforcement plan, and the United States can use its experience with Guatemala in future consultations.

Similar to the Guatemalan case, the U.S. government requested

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161 Id.
162 Id.
a consultation with Bahrain for violations of labor provisions under the U.S.-Bahrain FTA. After a general strike in Bahrain in March 2011, there was widespread dismissal of trade unionists and leaders, some even faced criminal prosecution for their role in the strike, and political critics of the government and employees following the Shia religion faced discrimination. Although some of the employees who were fired were reinstated, the process for reinstating the workers raised concerns that the provision granting freedom of association were violated, demonstrating that labor rights in Bahrain were deteriorating. If both countries cannot come to terms in the consultation as the United States did with Guatemala, then Bahrain may be subject to a fine of up to $15 million if Bahrain is found guilty of violating labor rights. However, it is unclear whether a third-party organization will determine if Bahrain breached the labor provisions if the consultation is unsuccessful. If Bahrain fails to pay the fine, the United States may utilize trade sanctions, such as the suspension of the U.S.-Bahrain tariff benefits. Even though the consultation between the United States and Bahrain has not yet occurred, the United States will likely seek a resolution like the enforcement plan it established with Guatemala. Thus, it is likely that the United States will use similar consultation proceedings if environmental and labor breaches arise under U.S. BITs.

China appears willing to include environmental and labor

168 Id.
169 U.S.-Bahrain FTA, supra note 166, at art. 19.12(2).
170 See id. at art. 19.12(1).
171 Id. at art. 19.12(6).
173 See U.S. Model BIT, supra note 67, at art. 37.
provisions in its investment treaties.\textsuperscript{174} However, if China agrees to include the environmental and labor provisions found in the 2012 U.S. Model BIT in the U.S.-China BIT, it may be setting itself up for failure, as its ability to enforce its own regulations to improve China’s environmental and labor conditions is questionable.\textsuperscript{175} Therefore, it will likely be difficult for China to adhere to the environmental and labor standards set out in the 2012 U.S. Model BIT that the United States will likely insist on including in a U.S.-China BIT.\textsuperscript{176} Consequently, debate on including the 2012 U.S. Model BIT’s version of the environmental and labor provisions will likely be a legal hurdle in the U.S.-China BIT negotiations.\textsuperscript{177}

C. Investor-State Dispute Mechanisms

Investor-state dispute settlement provisions in BITs “are one of the most important rights granted in a treaty.”\textsuperscript{178} Most BITs include clauses that allow investors to submit “disputes with the host state to binding international arbitration under the UN Commission on International Trade Law (Uncitral) Arbitration Rules or the [ICSID].”\textsuperscript{179} Both the United States and China adhere to UNCITRAL Arbitration Rules and ICSID resolution; thus, these countries are unable to challenge the arbitral awards in their own courts and must enforce the arbitral awards in the same manner as they enforce awards from the highest court in their jurisdictions.\textsuperscript{180} Nevertheless, the arbitral award does not prevail over domestic law that pertains to sovereign immunity; hence, upon review, an arbitration decision or award can be annulled or revised.\textsuperscript{181} Because the arbitration process allows the parties to bypass

\textsuperscript{174} See, e.g., China-New Zealand FTA, supra note 119, at art. 177.
\textsuperscript{175} The Economist Intelligence Unit, supra note 1, at 23.
\textsuperscript{176} See id. (explaining that China has a serious environmental crisis and that the Chinese government faces a challenge in implementing corrective policies).
\textsuperscript{177} See id.
\textsuperscript{178} GALLAGHER & SHAN, supra note 12, at 8.175.
\textsuperscript{179} The Economist Intelligence Unit, supra note 1, at 35.
\textsuperscript{180} Id. at 36.
\textsuperscript{181} Id.; see also Wenhua Shan, From North-South Divide to Private-Public Debate: Revival of the Calvo Doctrine and the Changing Landscape in International Investment Law, 27 NW. J. INT’L L. & BUS. 631, 638 (2007).
the national courts it levels the playing field for foreign investors against the host state. However, the arbitration process also intrudes on the sovereignty of the signatory states to make any further changes to the regulatory environments, which reduces the flexibility of the states to pass regulations in response to certain situations and makes some countries more cautious about including arbitration in BITs.

China’s stance on including an investor-state dispute resolution in its BITs has changed throughout the years and has become more liberal. China’s first-generation BITs were produced around 1984 and typically limited arbitration to issues on the amount of compensation for expropriation and referred the cases to ad hoc tribunals while other disputes were referred to local courts. Additionally, China’s first-generation BITs required the application of the host country’s laws and the consent from both parties before the case could be submitted to an arbitral tribunal. As a result of these restrictions, the effectiveness of the investor-state dispute settlement provisions, included in the first-generation BITs, were reduced to a mere symbolic nature. China’s reluctance to include legalized investor-state dispute settlement provisions in its first-generation BITs can be attributed to its history as an FDI-importing country.

However, beginning in 1985, China began to concede on investor-state dispute resolution provisions in some of its BITs as it began to morph into an FDI-exporting country. For example, China has become a leading destination for FDI in the developing world because of its economic growth, its low labor costs, its efficient workforce, its improved infrastructure, and its entry into the World Trade Organization in 2001. Specifically, in 1982, FDI inflows into

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182 The Economist Intelligence Unit, supra note 1, at 35.
183 Id. at 35-36.
184 GALLAGHER & SHAN, supra note 12, at 1.81.
185 Id. at 1.71, Appendix II: Chinese Model BIT Version I.
186 Berger, supra note 3, at 174.
187 Id.
188 Id.
189 Id. at 173; see The Economist Intelligence Unit, supra note 1, at 17.
190 The Economist Intelligence Unit, supra note 1, at 16-17.
China were approximately $400 million, which increased to $11.2 billion in 1992, then rose to $44.2 billion in 2001, and then increased to $147.8 billion in 2008.191

As China’s economy grew, however, the country began to transition from an FDI-importing country, to an FDI-exporting country.192 For example, in 1982, China’s outward FDI totaled $44 million, then increased to $913 million in 1991, grew to $6.9 billion in 2001, rose to $17.8 billion in 2006, and increased to $53.4 billion in 2008.193 Even though global outward FDI was decreasing, China’s outward FDI reached $365 billion by the end of 2011, which made China one of the top ten exporters in the world for FDI.194 As a result, China began to turn away from its first-generation BIT approach of restricted investment dispute settlement provisions.195

China’s second-generation BIT appeared after China ratified the ICSID Convention in 1993, which made it possible for treaty negotiators to incorporate ICSID arbitration in BITs with China.196 The majority of China’s second-generation BITs that have the comprehensive investor-state arbitration procedures are signed between China and developing countries, while less than one-fourth of the second-generations BITs signed with developed countries include such a provision.197

China’s third-generation BIT was adopted in the late 1990s and permitted access to international arbitration, such as ICSID arbitration for all investor-state disputes.198 For instance, the 1998 China-Barbados BIT was the first treaty China signed that offered foreign investors

191 Id. at 16.
192 Berger, supra note 3, at 176.
193 The Economist Intelligence Unit, supra note 1, at 16.
195 Berger, supra note 3, at 176.
196 GALLAGHER & SHAN, supra note 12, at 1.75.
197 Berger, supra note 3, at 176.
198 GALLAGHER & SHAN, supra note 12, at 1.77.
unrestricted access to international arbitration. Continuing with this trend of including international arbitration in its treaties, China’s BIT with Mexico and its FTA with New Zealand both contain more detailed provisions on the arbitration proceedings. Even though most of the third-generation BITs China signs grant full access to ICSID jurisdiction, some BITs do not grant such access, like the China-Qatar BIT. In China’s current Model BIT, a foreign investor has two options for investor-state dispute resolution, either local court or ICSID arbitration. A foreign investor that chooses ICSID arbitration may be required to go through domestic administrative review procedures before submitting the case to ICSID. Under Chinese BITs, the default remedy for most investor-state disputes, with the exception of quantum, is the Chinese court system.

China’s change in perspective toward comprehensive investor-state arbitration is targeted at protecting Chinese outward FDI. It is becoming more and more common that a Chinese foreign investor will need to pursue investor-state dispute settlement through arbitration to protect its investments in the host state. As previously mentioned, the comprehensive investor-state dispute settlement procedures are more commonly found in China’s treaties with developing countries, which are the predominate destinations for Chinese outward FDI. Accordingly, China is engaging in behavior similar to FDI-exporting countries by attempting to increase the legal protection for its own investors in foreign countries.

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200 China-New Zealand FTA, supra note 119, at ch. 11 § 2; China-Mexico BIT, supra note 13, at ch. III.
201 GALLAGHER & SHAN, supra note 12, at 1.80.
202 Id. at 1.90.
203 Id.
204 Id. at 8.159.
205 See Berger, supra note 3, at 176.
206 See GALLAGHER & SHAN, supra note 12, at 8.112.
207 See Berger, supra note 3, at 176.
208 Id.
Even though many of China’s BITs give foreign investors the option of arbitration on issues beyond compensation for expropriation, many of the BITs also include the restrictive formulation.\(^{209}\) BITs with restrictive formulation limit the foreign investor’s ability to rely on the MFN clause to invoke broader provisions from other BITs.\(^{210}\) According to the ICSID, in cases in which both states have entered into restrictive and expansive dispute resolution clauses, “to invoke the MFN clause to embrace the method of dispute resolution is to subvert the intention of the parties to the basic treaty, who have made it clear that this is not what they wish.”\(^{211}\) Thus, with the restrictive formulation in the U.S. Model BITs and Chinese BITs, foreign investors should not rely on the MFN in an attempt to invoke broader provisions from other U.S. and Chinese BITs.\(^{212}\)

As of June 1, 2013, China has signed 128 BITs,\(^{213}\) but only one case has been submitted to the ICSID for arbitration by a foreign investor against China—**Ekran Berhad v. People’s Republic of China**.\(^{214}\) The low number of cases brought against China may be attributed to the fear that doing so would hurt the investor’s future business opportunities in China, that there may be a lack of awareness of this remedy, or that law firms are reluctant to recommend this option to clients because of the uncertainty in the process.\(^{215}\) However, on May 24, 2011, Ekran Berhad filed the first investment claim by a foreign investor against China under the China-Malaysia BIT.\(^{216}\)

\(^{209}\) See Gallagher & Shan, supra note 12, at 8.112.

\(^{210}\) Id.


\(^{212}\) See Gallagher & Shan, supra note 12, at 8.112.


\(^{215}\) See The Economist Intelligence Unit, supra note 1, at 36.

claimant asserted that "the revocation by the local authority of its interest in lands in Hainan for failure to develop it as required amounted to expropriation contrary to the BIT." It is unlikely that this case will proceed to arbitration as the parties have filed a request with the ICSID to discontinue the proceedings, suggesting that the parties may have reached a settlement.

Similarly, the number of cases brought by Chinese investors against host states for arbitration is low with three cases known to date: (1) Tza Yap Shum v. Republic of Peru in 2009—first public decision arising from claims brought under a Chinese BIT, (2) China Heilongjiang International Economic & Technical Cooperative Corp., et al. v. Mongolia in 2011, and (3) Ping An Insurance Co. of China, et al. v. Belgium in 2012. In Tza Yap Shum, Mr. Shum, a majority owner of a fish flour manufacturing and export company, brought claims against the Peruvian tax authority with the ICSID under the Peru-China BIT of 1995. The tribunal concluded that the claimant met the requirements to show a prima facie case for indirect

217 See Shan & Gallagher, supra note 17, at 174.
220 Tza Yap Shum v. Republic of Peru, ICSID Case No. ARB/07/6, Award, ¶ 1 (July 7, 2011).
expropriation and awarded Mr. Tza $786,306.24.\textsuperscript{224} The result of Tza Yap Shum produced two issues for China in future arbitral proceedings: (1) the extent of the consent clause in disputes over expropriation, and (2) the application of the MFN clause from older BITs when foreign investors are seeking to apply the broader and more favorable terms from the newer BITs.\textsuperscript{225} Thus, China will likely be more cautious during BIT negotiations with the United States to ensure that restrictive wording is used in the treaty to prevent the BIT from being interpreted in a broader manner.

The China Heilongjiang International Economic & Technical Cooperative Corp. case is the second case ever submitted to arbitration by a Chinese investor.\textsuperscript{226} This arbitration was conducted under the guidance of the Permanent Court of Arbitration, not the ICSID, and few details of this ongoing arbitration have been released.\textsuperscript{227} Another case submitted for ICSID arbitration is Ping An Insurance Co. of China in 2012.\textsuperscript{228} Ping An Insurance lost approximately $3 billion when its investment in the Belgo-Dutch bank Fortis was nationalized and sold off during the financial crisis in 2008.\textsuperscript{229} Ping An Insurance alleges that the Belgian government breached the China-Belgium BIT by expropriating Fortis, and the insurance company is seeking compensation for its loss.\textsuperscript{230} This case is still in the early stages of the arbitration process as the latest information released to the public shows that the tribunal just issued an order pertaining to the procedural matters.

\textsuperscript{224} See Shan & Gallagher, supra note 17, at 166.
\textsuperscript{227} Id.
\textsuperscript{229} Id.
If the Chinese investors are successful in the aforementioned cases, then other Chinese investors will become less leery of the arbitral process and become more comfortable invoking arbitration as its method of dispute resolution.

Unlike China, the U.S. government has been the respondent and the U.S. investors have been the claimants in a number of arbitration proceedings that have greatly influenced U.S. BIT policies and the current 2012 U.S. Model BIT. Even though the United States has typically sought to include investor-state dispute settlement mechanisms as an option for its overseas investors, for some time the United States differentiated treatment between developed and developing states. Generally, investor-state dispute settlement mechanisms are found in treaties between the United States and developing states, but not between the United States and developed states. The North American Free Trade Agreement ("NAFTA") is the first investment treaty with an investor-state dispute provision involving arbitration between the United States and developed states. NAFTA represents how the United States began treating developing states and developed states equally by including arbitration in investment treaties.

However, to reduce the risk of foreign investors abusing the arbitration provision, and as a result of the United States being the respondent state in a number of claims under NAFTA, the 2004 U.S. Model BIT provides for a dispute settlement process that is more detailed. The United States added appendices, which detail the scope of the application of some of the substantive provisions that restricted

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232 See GALLAGHER & SHAN, supra note 12, at 8.112 to .114.

233 See Congyan, supra note 21, at 490.

234 Also see Caplan & Sharpe, supra note 38, at 756.

235 Id. at 463-65.

236 Id. at 463.

237 Id. at 463.

238 See GALLAGHER & SHAN, supra note 12, at 8.176.
the application of the dispute provisions. These detailed provisions are "more transparent, more controllable, more consistent, and less costly" in comparison to its previous dispute settlement process. For the most part, the provisions pertaining to the dispute settlement process in the 2004 U.S. Model BIT remain the same in the 2012 U.S. Model BIT, except for the following changes: (1) adjustments made to mirror the 2010 revision in the UNCITRAL Arbitration Rules, (2) deletion of Annex D, (3) edits to Article 28(10), and (4) an increase in the number of days to interpret the annexes.

Because the Chinese government is well aware of the litigious nature of the American judicial system, it may be reluctant to open Chinese investors up to the possibility of facing an arbitral tribunal in a foreign territory. Typically, China includes the investor-state dispute settlement provisions to protect its own investors in countries where China is the FDI-exporting country. However, under a China-U.S.

239 Id.
241 See, e.g., id. at arts. 30(3), 31.
242 See, e.g., id. at art. 33.
243 See, e.g., id.
244 Congyan, supra note 21, at 480.
246 See U.S. Model BIT 2004, supra note 68, at art. 28(9)(b), Annex D; see also U.S. Model BIT, supra note 67, at art. 28(9)(b).
247 See U.S. Model BIT 2004, supra note 68, at art. 28(10); see also U.S. Model BIT, supra note 67, at art. 28(10).
248 See U.S. Model BIT 2004, supra note 68, at art. 31; see also U.S. Model BIT, supra note 67, at art. 31.
BIT, China will more often than not be the FDI-importing country.\textsuperscript{251} Therefore, China will likely be reluctant to include such a provision in its BIT with the United States.\textsuperscript{252} However, the United States is highly likely to insist on such a provision because it is included in its Model BIT and it protects U.S. investors abroad.\textsuperscript{253} Consequently, the investor-state dispute settlement provision will be another legal hurdle in the U.S.-China BIT negotiations.\textsuperscript{254}

\section*{III. U.S.-CHINA BIT UNLIKELY IN THE IMMEDIATE FUTURE}

In the current political climate, a U.S.-China BIT is unlikely to result from negotiations because of the national security concerns, the differing perspectives on environmental and labor provisions, and the differing viewpoints on investor-state dispute settlements.\textsuperscript{255} Because of the general distrust that the American and Chinese governments harbor toward one another, both governments have used national security concerns as justifications to block billion-dollar transactions from foreign investors from the other nation, depriving their own economies an opportunity to thrive.\textsuperscript{256} Some U.S. analysts have argued that more Chinese FDI in the United States, particularly in new ventures that manufacture products or provide services and create new jobs in the United States, could assist in improving the bilateral economic relations and might lessen perceptions that increasing U.S.-China trade

\begin{itemize}
\item \textsuperscript{253} See generally \textit{U.S. Model BIT}, supra note 67, at arts. 24-37 (illustrating the broad protections provided to investors under the U.S. Model BIT).
\item \textsuperscript{254} \textit{Id.}
\item \textsuperscript{255} See Berger, supra note 3, at 181-83.
\item \textsuperscript{256} See \textit{The Economist Intelligence Unit}, supra note 1, at 28.
\end{itemize}
undermines U.S. employment and damages U.S. economic interests.\textsuperscript{257}

Even though national security concerns are reserved in the Model BITs as reasons to reject foreign transactions, a U.S.-China BIT may make it more difficult for either government to raise such an excuse because the BIT will likely include provisions on MFN, national treatment,\textsuperscript{258} and minimum standard of treatment, which restrict the government's discriminatory capabilities.\textsuperscript{259} Therefore, the Chinese and American governments must decide if they are willing to grant Chinese and American investors such investment protections and consider the ramifications of raising national security concerns as a justification to block transactions in the future.\textsuperscript{260} Consequently, national security becomes a difficult legal hurdle to overcome in the BIT negotiations.\textsuperscript{261}

Along with national security, the different viewpoints that the United States and China have on environmental and labor regulations are another obstacle to a successful U.S.-China BIT.\textsuperscript{262} Environmental and labor regulations are mandatory provisions in the 2012 U.S. Model BIT, but not in the latest Chinese Model BIT.\textsuperscript{263} Although China is attempting to improve its environmental and labor regulations, it has difficulty enforcing its regulations and many of its regulations are fairly new, so it remains to be seen if China will actually improve its environmental and labor conditions.\textsuperscript{264} Even though the China-New Zealand MOU and ECA can be used as a guideline for the U.S.-China BIT negotiations, the environmental and labor provisions in the 2012 U.S. Model BIT are arguably stricter than those found in the MOU or ECA.\textsuperscript{265} Specifically, the U.S. model prohibits acts from the signatory

\begin{itemize}
\item \textsuperscript{257}See Liu & Ren, supra note 36, at 20.
\item \textsuperscript{258}See Berger, supra note 3, at 172-73.
\item \textsuperscript{259}Id.
\item \textsuperscript{260}See Kong, supra note 20, at 187.
\item \textsuperscript{261}Id.
\item \textsuperscript{263}See U.S. Model BIT, supra note 67; see also Gallagher & Shan, supra note 12, at Appendix IV: Chinese Model BIT Version III.
\item \textsuperscript{264}See The Economist Intelligence Unit, supra note 1, at 22-24.
\item \textsuperscript{265}Compare Memorandum of Understanding on Labour Cooperation, China-New
states, while the MOU and ECA encourage certain cooperative activities. With the difficulties that China currently has enforcing some of its domestic regulations, it is debatable whether China would be willing to include stricter environmental and labor provisions in a U.S.-China BIT. Therefore, environmental and labor standards are another legal hurdle to the BIT negotiations.

Like national security and environmental and labor standards, investor-state dispute settlement mechanisms are another issue that may hinder the U.S.-China BIT negotiations. Arguably, from the Chinese perspective, the U.S.-China BIT is not immediately necessary because the United States has a robust legal system that Chinese investors can access for dispute resolutions. However, not having a U.S.-China BIT limits the investor-dispute settlement mechanisms available to Chinese investors in the United States and vice versa, which for many foreign investors becomes a great disadvantage. Because the majority of U.S. BITs include an international arbitration provision, and because China is including a similar provision in some of its BITs, foreign investors from countries that do have BITs with China or the United States have the advantage of having international arbitration as an option for dispute resolution. Some advantages of investor-state arbitration over litigation are (1) neutrality because litigation occurs in


266 See sources cited supra note 265.
267 See The Economist Intelligence Unit, supra note 1, at 4, 22.
269 Id. at 214.
270 See Congyan, supra note 21, at 475-76, 490.
271 See The Economist Intelligence Unit, supra note 1, at 33.
However, some disadvantages of investor-state arbitration include the following: (1) arbitration can be more expensive than litigation, (2) negative impact on governmental relations, and (3) delays in the arbitral proceedings due to the time it takes to constitute the tribunal and the time for the tribunal to make an award. Consequently, not having international arbitration as an option for investor-state dispute resolution is not particularly detrimental to Chinese investors because of the strong U.S. legal system. For instance, the Chinese-owned company Ralls Corporation ("Ralls") is suing President Obama for blocking the company's attempt to acquire wind farm projects in Oregon on the grounds that the President's actions were unconstitutional. President Obama followed CFIUS' recommendation to block the acquisition on national security grounds. The court dismissed all of Ralls' allegations with the exception of count IV, which alleges the denial of the company's due process rights under the Fifth Amendment of the U.S. Constitution. Although Ralls' suit is still ongoing, having a U.S.-China BIT could help Chinese companies during the acquisition process because it provides companies with other dispute settlement options besides the U.S. court system.
In contrast, lacking international arbitration as an option for U.S. investors may be more of a detriment because of the reputation of corruption that engulfs the Chinese legal system. Thus, if the Ralls' situation is reversed it is unlikely that a U.S. investor would have progressed this far in the Chinese court system. Even though national security is a topic that both countries will likely agree to include in the BIT as a justification to block an investment, having arbitration as an option for dispute resolution provides investors with an alternative system to litigation to address their grievances.

Although some U.S. investors have complained that not having a U.S.-China BIT provides unfair advantages for Chinese companies and other foreign investors in China, some U.S. companies have continued to prosper without a BIT. For example, because of China's admittance into the WTO, China has improved some of its intellectual property regulations, which have become a catalyst for pharmaceutical companies to increase their research and development in China. Pfizer, the U.S. pharmaceutical company, is the largest foreign pharmaceutical company in China with investments worth over $500 million in China. Moreover, from January 2012 to March 2013, the U.S. ranked fifth in nations with the most FDI in China. Additionally, in 2012, Chinese FDI into the United States reached a

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282 See id.

283 See Kong, supra note 20, at 181, 188.

284 See The Economist Intelligence Unit, supra note 1, at 18.

285 Id.

286 Id.


record total of $6.5 billion, representing a twelve percent increase from its previous record in 2010 of $5.8 billion. Therefore, arguably, a U.S.-China BIT has low relevance to the capital inflow from the United States into China. Instead, foreign investors are drawn to investing in China because of its inexpensive labor force, growing large, national market, and low-cost export platform. Thus, the lack of BIT has not prevented significant amounts of Chinese investments into the United States and vice versa, which puts the necessity of a U.S.-China BIT into question.

However, foreign investors have noticed a trend of rising labor costs and a lack of skilled workforce in China, which reduces the incentive for foreign investors to invest in China. Consequently, China cannot continue to rely on low labor cost to attract FDI from U.S. investors and it should start considering other mechanisms to incentivize U.S. investors, such as a U.S.-China BIT. Investors from European and Asian countries that have BITs with China have received a competitive advantage investing in China over U.S. investors, thereby increasing the need for a U.S.-China BIT for U.S. investors.

Because the Canada-China FIPA includes provisions that are similar to NAFTA, of which the United States is a party, the successful negotiation of the Canada-China FIPA provides a helpful guideline for future U.S.-China BIT negotiations. In other words, China can

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290 See Congyan, supra note 21, at 473.
291 Id. at 476.
292 Kong, supra note 20, at 181, 183.
293 Id.
294 See Congyan, supra note 21, at 476.
295 See Davies, supra note 53, at 7.
296 See Kong, supra note 20, at 181, 184-85.
297 Id.
expect the United States to insist on similar provisions as Canada in an investment treaty because the United States and Canada have similar economic and social policies. 299 Although the environmental provision in the Canada-China FIPA resembles the provision in the 2012 U.S. Model BIT, the Canada-China FIPA does not mention labor regulations. 300 Therefore, unlike Canada, the United States will likely insist that labor provisions similar to the 2012 U.S. Model BIT be included in a U.S.-China BIT. 301

However, the definition of “investment” in the treaty that China signed with Japan and Korea in 2012 strays from the Chinese Model BIT (Version III) and instead mirrors the definition of investment in the 2012 U.S. Model BIT. 302 Additionally, in the China-Mexico BIT, the definition of “investment” resembles the NAFTA wording in Article 1139, demonstrating, again, that China is willing to deviate from its Model BIT. 303 Additionally, the latest U.S. and Chinese BIT models seem to be converging on key points, which should help ease future BIT negotiations between these two countries. 304

Nevertheless, in the past, China has been successful in attracting FDI; therefore, it may not be under great pressure to finish a treaty with the United States. 305 Although, with the successful negotiation of the

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300 See Canada-China FIPA, supra note 124, at arts. 18(3), 33(2); see also U.S. Model BIT, supra note 67.

301 See supra Part II.B.


304 See ALVAREZ, supra note 7, at 175.

305 See Shan & Gallagher, supra note 17, at 131, 181.
Canada-China FIPA and the Trilateral Investment Agreement with Korea and Japan, both of which share similarities with the 2012 U.S. Model BIT, this bodes well for future U.S.-China BIT negotiations. In other words, a U.S.-China BIT is unlikely to result in the immediate future but the trends in Chinese BIT policies is toward “Americanization.” The growth of Chinese outward FDI, the desire of U.S. investors to gain access to more markets in the Chinese economy, and the desire for protection of U.S. investments in China will increase the chances that these two countries will likely successfully negotiate a BIT in the distant future—like at a sixth S&ED.

IV. CONCLUSION

As China has developed over the years, its BIT policy has changed in focus and content. When China signed its first BIT in 1982 with Sweden, China aimed its investment policy toward promoting inward FDI rather than protecting outward FDI. As China has grown into the second largest economy in the world, its BIT policies have transformed into promoting and protecting both inward and outward FDI due to the increase in Chinese outward FDI. However, because the surge in China’s outward FDI can be considered rather novel for the country, China’s BIT policy is arguably slightly more geared towards benefiting inward FDI.

Throughout the years, the United States has generally negotiated BITs based on the latest versions of its model BIT. The United States

306 Id.
308 See Shan & Gallagher, supra note 17, at 131.
310 See Shan & Gallagher, supra note 17, at 131-32.
311 Id. at 131, 133.
312 Id. at 132.
is known for its unyielding reputation when it comes to negotiating BITs that deviate from its model BITs. However, it is not impossible to convince the United States to stray from its terms, as Australia was able to convince the United States not to include any investor-state dispute settlement mechanisms in the U.S.-Australia FTA.

Due to current contrasting styles that the United States and China typically use in BIT negotiations, with the United States traditionally adopting a more demanding, “liberalizing” approach and China adopting a more “protectionist” approach, the BIT negotiations will be difficult for both countries. In the current political environment, it will likely be difficult for the United States and China to overcome the legal hurdles of national security concerns, environmental and labor provisions, and investor-state dispute settlement mechanisms during BIT negotiations. Even if a successful U.S.-China BIT could be negotiated, the BIT would require ratification by the U.S. Senate, which may prove to be difficult because of the general distrust some U.S. senators feel towards the Chinese government. Furthermore, because China can take advantage of the sound economic, political, and legal systems in the United States, signing a BIT with the United States may not be necessary for China. Consequently, it is unlikely that a successful U.S.-China BIT will result from the fifth S&ED.

However, once the balance of China’s outward FDI outweighs the inward FDI, China will have more incentives to ensure that there is

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314 Id.
316 See GALLAGHER & SHAN, supra note 12, at 9.11.
317 See Kong, supra note 20, at 181, 187-89.
319 See Congyan, supra note 21, at 476.
a BIT between the two nations. Moreover, if the current trend in China’s BIT policy of liberalization or “Americanization” continues, then the probability of success for future U.S.-China BIT negotiations will increase. A U.S.-China BIT can act as a guideline to reduce the tension between the two nations and help liberalize the investment policies in both countries. Therefore, a successful U.S.-China BIT is unlikely to result from the fifth S&ED, but the current trends in American and Chinese BIT policies suggest that a successful U.S.-China BIT is more likely to result from future BIT negotiations, perhaps at a sixth S&ED.

321 See Liu & Ren, supra note 36, at 7.
322 See id.
323 See id.