LATEST DEVELOPMENTS IN INVESTMENT TREATY-MAKING: CASES OF CHINA AND THE UNITED STATES

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Najnovšie trendy v uzatváraní medzinárodných investičných zmlúv: Čína a Spojené Štáty Americké

Abstract: *Are the nation states losing their position as the main actors in the global arena? Are they being supplanted by international institutions, regimes and transnational corporations? This article focuses on these questions within the specific framework of international investment regimes. The goal of this article is to identify the most recent trends in investment treaty-making of China and the US in relation to the conflict between investment protection and state sovereignty. The article compares a sample of treaties from both countries from two different eras and identifies the main changes that have a bearing on the influence of states, investors and international tribunals in the area of foreign investment. The conclusion of the analyses consists of demonstrating conflicting tendencies, where since 1990s, the US has moved slightly towards protection of state sovereignty, while China has moved away from its position of strict sovereignty protection towards a more standard investment protection based on the international consensus.*

Keywords: *sovereignty, investment protection, state, investment regimes, investment arbitration, USA, China*

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1 Introduction

In the past ten years, investment treaty making has been a subject of significant change, with increased complexity and diversity of the new investment treaties being the main features of this change, mainly in the areas of market access and investment arbitration. We are in fact now talking about a new generation of investment treaties. This article focuses on the latest trends in investment treaty making of arguably the two most important countries with respect to investment – the USA and China. My aim is to focus my analysis on the way that the new trends in investment treaty-making of China and the USA affect the national sovereignty of the parties on the level of investment treaties. This will not only show the developing view of these countries towards the conflict between investment protection and national sovereignty, but also have wider implications for the theory of international relations, and the ongoing debate between neoliberal and neorealist approaches.

The approach of this paper towards the latest trends of the USA and China's investment treaty-making is based on the theory of international relation. The theoretical framework of this paper is built on the conflict between the two predominant approaches to international relations: neorealism and neoliberalism. There is no space here, nor necessity to go into details of the two theories, since I will only be focusing on one aspect of the conflict, namely the role that the sovereign states have in the global political system. While we have seen some significant convergence between the two theories in the last three decades, significant differences remain in the positions of the two approaches on the relative relevance of nation states, international organizations, international regimes and transnational corporations in the global arena (Krasner, 1983; Strange, 1996). While accepting the crucial importance of states as the main actors of international relations, neoliberalism emphasizes globalization as the most important global process, highlighting the growing importance of international organizations and transnational corporations in global economic and political relations (Krasner, 1983). Neorealism, on the other hand, stresses the importance of anarchic character of international relations, therefore highlighting the dominance of state sovereignty (Strange, 1996).

On the level of investment regimes, which is what this article is interested in, this conflict can be translated into the conflict between the concepts of investment protection and national sovereignty. Investment protection is a concept that comes straight out the neoliberal view of development, which

stresses the importance of foreign direct investment. In order to ensure sufficient levels of investment throughout the world, the international community needed to create an international regime of investment protection based on a network of bilateral and multilateral investment treaties, regulated by transnational arbitral institutions. As we will see, this system limits to a certain degree the sovereign space for the nation states to regulate their investment environment, therefore coming into conflict with the theory of sovereignty, which is integral for neorealist worldview.

The issue of the conflict between investment protection and national sovereignty has attracted significant interest in the scholarly research, which is mostly related to the concept of the right to regulate. One of the leading scholars, Dolzer (2005) has for example analyzed the impact of investment regimes on domestic sovereignty in the area of administrative law (Bird-Pollan, 2018). Other scholars that have studied the issue of sovereignty on the level of investment regimes include Bjorklund (2005),Thaliath (2016), Bird-Pollan (2018) and others.

The goal of this paper is to analyze the latest trends in investment treaty-making of China and the USA as two of the most important capital exporters in the global measure. This will enable us to make comparison between the current positions of the two countries on the investment protection and state sovereignty, as well as make inferences relevant for the theoretical conflict between neorealism and neoliberalism.

2 Methodology

The question posed by this article can be formulated in the following way: How has the nature of investment treaties of the USA and China changed since the 1990s in relation to the competing concepts of investment protection and state sovereignty? The relevance of this question rests on the fact that China and the USA are among the most important actors in global investment regimes and consequently, the analysis of their position on the issue of sovereignty of nations states in these regimes will give a strong indication of the direction that these regimes will take in the close future. In order to answer this question, I will conduct a simple content analysis (Shannon and Hsieh, 2005; Kohlbacher, 2006) of a convenience sample of 18 investment treaties. The aim will be to compare treaties signed between 1991 ─ 1994 with treaties

signed recently for each country in terms of the way that these treaties reference investment protection and state sovereignty. While the presented sample is relatively small, it is sufficient in the view of the fact the two analyzed countries are among the most powerful in the international arena, and it can therefore be assumed that the treaties that they sign with relatively smaller countries represent faithfully their position on the matters that the treaty deals with[2]. If I find that the treaties from the same era differ significantly so that it renders the results of the analysis irrelevant, it will be necessary to enlarge the sample.

The logic of the research is deductive in the sense that I will be taking concepts of state sovereignty and investment protection, which are well established within the theory of international relations, and I will be applying these concepts to the analyzed investment treaties. In practice, this means that the coding process for the content analysis (Shannon and Hsieh, 2005; Kohlbacher, 2006) will consist of identifying these existing concepts among the provisions of the investment treaties, and comparing the prevalence of either of the concepts in treaties from 1990s with their prevalence in the most recent treaties. The coding process is facilitated by the structured and consistent form of investment treaties, which establishes codes to be identified such as the fair and equitable treatment or expropriation provision. This process ought to enable us to see 1) how has the view of the conflict between state sovereignty and investment protection developed in time in the cases of the USA and China, as well as 2) any existing differences between the positions of the two countries.

3 Theoretical Framework

The theoretical framework that was used for the content analysis of the relevant investment treaties consists of the competing concepts of national sovereignty and investment protection, as defined within the neoliberal and neorealist conceptions of international relations. I will be using the most parsimonious definition of sovereignty, which is particularly suited to this article, since it makes obvious its conflict with investment protection, Sovereignty will be understood here as *"a distinct lack of other authority over the state than the domestic authority"* (Krasner, 2001). This means that when it comes

[2] This is confirmed by even a cursory glance at the treaties. The practice for countries with large outgoing investment is to have "model BITs". However, as explained later, the position of the USA is not as clear, since the last BIT was signed in 2008, and the most recent investment treaties are multilateral.

to investment treaties, I will be looking for provisions, which either protect the right of the state to regulate its investment environment, or provisions, which limit the involvement of transnational actors (such as investment arbitration tribunals).

When it comes to investment protection, I first need to point out that I am always talking about foreign investment protection (as opposed to domestic investment), since I am working within the theory of international relations. Investment protection can therefore be defined as the set of provisions commonly found in investment treaties, whose purpose is to stimulate investment between countries by providing foreign investors with rights and limiting government interference. This means that when it comes to investment treaties, I will be looking for provisions, which grant foreign investors rights, or which limit the ability of the host state to interfere with the investment activity of the investor. These provisions are well established, and generally include the following provisions: fair and equitable treatment (FET), full protection and security, most favored nation treatment (MFN), national treatment (NT), provisions against discriminatory and arbitrary treatment, provisions against unlawful expropriation, free transfers, subrogation, right to international arbitration of investment disputes, and other (Dolzer and Schreuer, 2012). It is easy to see, that the concepts of state sovereignty and investment protection as defined here are in conflict, since investment protection provisions of investment treaties define specifically conditions, where the domestic authority is not exclusive. It sets clear limits on what the states can do in relation to foreign investments, and it creates legal mechanisms, which enable foreign investors to appeal to transnational arbitration tribunals in order to solve any disputes arising out of a perceived breach of an investment treaty. If we apply this framework to the research question formulated previously, we are essentially asking whether the investment treaties of China and the USA have moved towards protecting state sovereignty, or towards protecting investment since the 1990s.

4 Analysis of Investment Treaties – USA

In this part of the paper, I will present the results of the content analysis of US investment treaties from two different time frames. The treaties from 1991 – 1994 include bilateral investment treaties with Argentina (1991), Estonia

(1994), Georgia (1994), Mongolia (1994), and Trinidad and Tobago (1994). The content analysis of the treaties reveals that these treaties are remarkably consistent with only minor differences when it comes to provisions related to the concepts of investment protection and state sovereignty. The provisions that all of these treaties contain that provide rights to foreign investors (therefore contributing to investment protection) include: FET, MFN, NT, full protection and security, expropriation provision, free transfers, subrogation, provisions against arbitrary and discriminatory measures. Moreover, the treaties also include provisions that are not as common for this generation of investment treaties, namely the provision that forbid the host state to *"impose performance requirements as a condition of establishment, expansion or maintenance of investments"* (1994). These provisions are mostly interesting because of the fact that they establish a limited version of pre-establishment market access for foreign investors, which has only recently become more common in investment treaties, but has always been part of the US model.

As far as protection of state sovereignty is concerned, all these treaties *"shall not preclude the application by either Party of measures necessary for the maintenance of public order, the fulfillment of its obligations with respect to the maintenance or restoration of international peace or security, or the Protection of its own essential security interests"* (1994). This is a standard provision for an investment treaty and only offers a very limited space for the state to regulate its investment environment. However, two of the treaties also include several exceptions to the NT provision. These exceptions are specific to the two countries. The provisions state that USA/Argentina, Estonia *"reserves the right to make or maintain limited exceptions to national treatment in the following sectors"* (1991, 1994). While the number of sectors in favor of the USA, the size of its economy means that the provision is not necessarily disproportionate in its protections.

We can therefore conclude that while the US treaties from 1991 ─ 1994 offer all common investment protection provisions, the protections of state's sovereign regulatory space is limited.

When it comes to US treaties signed recently, the issue that arises is the relative inactivity of the USA in terms of treaty-making. Since the US has the most developed network of existing BITs, this (not signing new treaties) suggests that their position on investment treaties, including the conflict between the state sovereignty and investment protection remains the same. I will proceed

with my analysis taking into account these facts and focusing on the three treaties that have been signed in the last decade. Analyzed US investment treaties signed most recently (2008 ─ 2016) include BIT with Rwanda (1994), the Agreement between the United States of America, the United Mexican States, and Canada (USMCA) (2018) and the Transpacific Partnership (TPP) (2016). The treaties are very similar to the treaties from the 1991 – 1994 in terms of investment protection, containing all the usual provisions (see above).

As far as protection of the regulatory space of the sovereign state, there are two main changes compared to treaties from 1991 – 1994. First, all three treaties contain a special paragraph, which explicitly states that: *"Nothing in this Chapter shall be construed to prevent a Party from adopting, maintaining, or enforcing any measure ... appropriate to ensure that investment activity in its territory is undertaken in a manner sensitive to environmental, health, safety, or other regulatory objectives"* (2016). Second, the definition of indirect expropriation in all three treaties explicitly excludes measures *"designed and applied to protect legitimate public welfare objectives, such as health, safety and the environment"* except in "rare circumstances" (1994, annex B, p39.). These changes increase the potential for sovereign regulation in public interest without the necessity to compensate relevant foreign investors. Finally, the investment arbitration option is not available in relationship between the USA and Canada (as per USMCA) (2018), mainly thanks to a long history of consistent rulings of domestic courts on investment disputes, which makes investment arbitration unnecessary.

All these changes increase to a certain degree the sovereignty of the nation states. However, this analysis would benefit from a larger sample of BITs in the future, since the multipolar treaties, such as TPP and USMCA might not necessarily express the position of the USA on the issue of the conflict between investment protection and state sovereignty, but rather an acceptable compromise.

Overall, we can conclude that while investment protection provisions of investment treaties remained the same for the USA, and the provision protecting sovereignty are more numerous. This leads me to infer that in terms of investment treaty-making, the USA has moved slightly towards states sovereignty away from investment protection, with qualifications made in the previous paragraph.

5 Analysis of Investment Treaties – China

In this part of the paper, I will present the results of the content analysis of China's investment treaties from two different time frames. The treaties from 1991-1994 include BITs with Argentina (1992), Czech Republic (1991), Estonia (1994), Jamaica (1994) and Hungary (1991). Treaties signed by China in this period contain most of the common investment protection provisions, such as FET, MFN, full protection and security, expropriation, free transfers, subrogation, non-discrimination. However, compared with the same treaties signed by the US in the same period, these treaties contain the NT provision less frequently, with only the China – Czech Republic BIT containing this provision. The treaties also do not contain the provision against performance requirements that we could see in the case of the US treaties, thus increasing the sovereign space of the state, especially in terms of measures in the pre-establishment phase of the investment activity.

When it comes to protecting the sovereignty of the state, we can see no provisions, which would protect the regulatory space of the state explicitly. However, the absence of the transnational investment arbitration mechanism, except for disputes regarding the amount of compensation due for expropriation represents a strong provision, which severely limits the ability of the foreign investor to submit disputes outside the framework of the domestic legal system. We can see this in all the analyzed treaties. This provision offers a very strong protection of state sovereignty, as it severely limits the access of foreign investors to investment arbitration. The investors can naturally submit their disputes to domestic courts, but this leaves the power to determine potential treaty breaches to the state power.

We can therefore conclude that the Chinese treaties signed between 1991–1994 provide stronger protections to sovereignty of the state, especially in terms of the legal sovereignty, and less protection to the investors.

Analyzed Chinese investment treaties signed most recently (2009 – 2015) include BITs with Malta (2009), Tanzania (2013), Switzerland (2009), Uzbekistan (2011), and the China-Australia Free Trade Agreement (CHAFTA) (2015). When it comes to investment protection, the treaties are similar to those signed between 1991 – 1994. The only important difference is that China has since become more willing to make the NT provision a part of their investment treaties, with all the analyzed treaties from 2019 ─ 2013 containing the NT

provision. Other than that, the treaties contain all the usual provisions, with the exception of provision against performance requirements.

As far as protecting the sovereignty of the state is concerned, the more recent treaties no longer limit the access to disputes on the amount of compensation for expropriation. This new position is more in line with the global practice and represents a move away from protecting the sovereignty of state towards investment protection, therefore corresponding with the "opening up" of China.

The two treaties signed in 2009 do not contain any new provisions for national sovereignty. However, the three other treaties contain both the provision, which states that *"nothing in this Agreement shall be construed to prevent a Contracting Party from adopting or maintaining environmental measures necessary to protect human, animal or plant life or health"* (2015), and the definition of indirect expropriation, which excludes *"...legitimate regulatory measures adopted by one Contracting Party for the purpose of protecting public health, safety and the environment, and that are for the public welfare and are non-discriminatory..."* (2015). This hints at a change in the position of China towards investment protection and national sovereignty after 2009, but could also be the result of a more general change in the global practice of investment treat-making.

Overall, we can conclude that the treaties signed between 2009 – 2013 provide greater investment protection and a different, but more limited protection to state sovereignty than the treaties signed between 1991 – 1994.

6 Conclusion

This article focused on the latest trends in investment treaty-making of two of the most important economies in the global investment system: the USA and China. The goal of the article was to compare investment treaties signed in the 1990s with the most recently signed treaties for both countries, in order to see whether the positions of the two countries on investment protection and state sovereignty have changed in the last three decades. The analysis of the selected treaties shows that the position of the US towards the conflict between investment protection and state sovereignty has shifted slightly towards protection of state sovereignty, although the reluctance to negotiate new

BITs suggests that the old treaties work just fine for the US. On the other hand, Chinese treaties have moved away from their strict protection of domestic legal sovereignty, and now allow for international investment arbitration in the full scope, while they have at the same time expanded the investment protection to what amounts to international standard under the current investment regime. Overall, we can conclude that both countries have moved at different pace in opposite directions, and have now met somewhere in the middle, as their treaties are now substantially similar in terms of investment protection and state sovereignty.

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