

Beijing

27/F, North Tower
Beijing Kerry Centre
1 Guanghua Road
Chaoyang District
Beijing 100020, P.R.C.

Tel: +86 10 5769 5600
Fax: +86 10 5769 5788

Guangzhou

1701, International Finance
Place, 8 Huaxia Road,
Zhujiang New Town
Guangzhou 510623, P.R.C

Tel: +86 20 3225 3888
Fax: +86 20 3225 3899

Hong Kong

26/F One Exchange Square
8 Connaught Place Central
Hong Kong

Tel: +852 3976 8888
Fax: +852 2110 4285

Shanghai

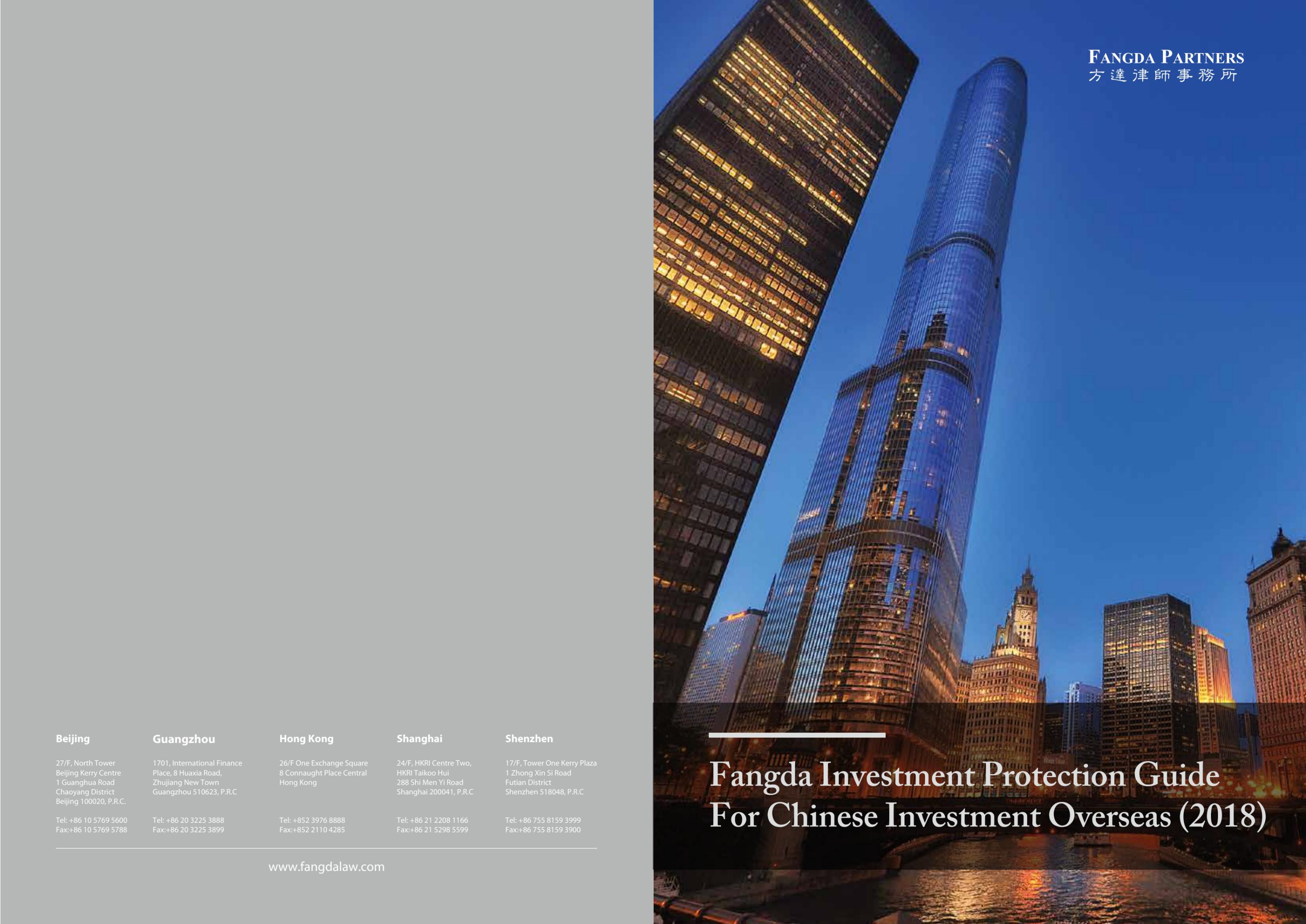
24/F, HKRI Centre Two,
HKRI Taikoo Hui
288 Shi Men Yi Road
Shanghai 200041, P.R.C

Tel: +86 21 2208 1166
Fax: +86 21 5298 5599

Shenzhen

17/F, Tower One Kerry Plaza
1 Zhong Xin Si Road
Futian District
Shenzhen 518048, P.R.C

Tel: +86 755 8159 3999
Fax: +86 755 8159 3900



Fangda Investment Protection Guide For Chinese Investment Overseas (2018)



Chinese ODI and Sovereign Risks

In the past 20 years, China has become one of the largest ODI (Overseas Direct Investment) exporters in the world. Chinese capital – encouraged by the Belt & Road initiative – funds large-scale complex infrastructure and natural resources projects in over sixty jurisdictions that form the Belt & Road area.

Along the Belt & Road area, particularly in Southeast Asia and in Africa, Chinese capital funds and implements large infrastructure and natural resources projects, including railways, ports, roads, mining infrastructure, and other projects.

These investments, while lucrative, present increased sovereign risks given the nature of the host States government policies in these jurisdictions. These risks include expropriation, nationalization, and other forms of interference by the host States with Chinese investment projects.

Protection of Chinese Investment in Challenging Jurisdictions

It is open to Chinese companies investing in challenging jurisdictions to seek investment protection to either safeguard their investment projects, or to receive compensation for the projects that may have been lost.

Investment protection offers a broad range of measures – from political risk insurance to investor-State arbitration – to guarantee that foreign investment made in the territory of a recipient host State is not lost, damaged, expropriated, nationalized, or in any other way undermined by the acts and omissions to act of the organs of the host State.

Contemporary investment protection mechanisms include:

- Investor-State arbitration;
- Mediation and conciliation of investment disputes;
- Resolution of investment disputes through Investment Agreements with the host State;
- Diplomatic protection;
- Resolution of investment disputes through litigation in the courts of the host State; and
- Political risk insurance.

The availability of investment protection options facilitate foreign direct investment by making it cheaper (political risk insurance is typically offered at lower rates if there is an investment treaty with a functional investor-State dispute mechanism), more predictable (it guarantees to foreign investors that they will be in a position to engage international law to recover their investment), and more fast-paced (due diligence of potential investment is faster if there is a network of investment treaties in place).

China's Investment Protection Practice

China became involved with investment treaty-making practice in the early 1980s, when it started negotiating its first bilateral investment treaties (BITs).

■ *Three Generations of China's Bilateral Investment Treaties (BITs)*

The Chinese BITs of the first generation were negotiated between China's adoption of its open door policy in 1978 and the beginning of the 1990s. The first generation of Chinese BITs were signed primarily with European countries who were looking to invest in China and were seeking stronger international law protection of their investment projects. This generation of Chinese BITs is protective of China's regulatory space. The investor-State dispute resolution clauses in those treaties are limited to disputes "concerning the amount of compensation for expropriation". This wording makes it harder (but not impossible) for investors to engage the host State's liability under such treaties.

The Chinese BITs of the second generation were negotiated and concluded between 1992 and 2000. This generation of BITs offer ICSID as a dispute resolution forum. ICSID (International Centre for Settlement of Investment Disputes) is an arm of the World Bank, headquartered in Washington DC, that offers a procedural framework for the resolution of disputes between foreign investors and host States. The scope of the majority of the second generation BIT's dispute resolution clauses is still limited to disputes "concerning the amount of compensation for expropriation", although certain other substantive investment protections are broader in scope than those included in the first generation of Chinese BITs.

The third generation of China's BITs was negotiated in the 2000s. By that time, China has achieved a unique position in the global investment and trade community. It became both the largest recipient of foreign investment and one of the largest exporters of capital. The third generation of BITs was negotiated against this economic backdrop. These treaties grant National Treatment guarantee to foreign investors, as well as a guarantee of Fair and Equitable Treatment and Full Protection and Security, protection against unlawful expropriation, along with other substantive protections that are typical for contemporary investment treaties. Importantly, most of these treaties no longer contain "the amount of compensation for expropriation" wording, and as such, allow for much stronger international law protection.

■ *Investment Treaty Protection for Chinese Companies Overseas: Cases Brought by Chinese Investors*

Chinese investors have in recent years started to make use of the wide range of protections for their investments abroad under China's investment treaties by initiating arbitration. For example:

- In 2007, a Chinese investor brought a claim against Peru under the China-Peru BIT in relation to certain actions of the Peruvian tax authorities. An award was rendered in 2011 in favour of the Chinese investor (ICSID Case No. ARB/07/6).
- In 2012, the Chinese Ping An insurance company brought a claim against Belgium in relation to its investment in a Belgian bank that was nationalized and sold off by the Belgian government following the 2008 financial crisis. An award was rendered in 2015, dismissing the claim on jurisdictional grounds (ICSID Case No. ARB/12/29).
- In 2014, a third case was registered by Beijing Urban Construction Group Co Ltd against the Republic of Yemen. In 2018, the dispute was discontinued as the parties reached a settlement agreement.
- In 2015, a Hong Kong bank (Standard Chartered Bank (Hong Kong) Limited) brought a claim against Tanzania in relation to an agreement related to the construction of a power plant. The final award has not been rendered (ICSID Case No. ARB/15/41).

Claims have also been brought by Chinese investors in ad-hoc proceedings, outside of the ICSID forum:

- In 2010, an UNCITRAL claim was brought before the Permanent Court of Arbitration under the China-Mongolia BIT in relation to a Chinese investment in a Mongolian mine, which was dismissed in 2017 on jurisdictional grounds (China Heilongjiang International Economic & Technical Cooperative Corp. et al. v. Mongolia, PCA Case No. 2010-20).
- The Permanent Court of Arbitration also administered an UNCITRAL claim under the China-Laos BIT in 2012 relating to a Chinese company's gaming operations in Laos, which claim was subsequently settled (Sanum Investments Limited v. Lao People's Democratic Republic, PCA Case No. 2013-13). In 2017, the Chinese company registered an ad-hoc ICSID claim in relation to Laos' conduct after the settlement, which decision is pending (ICSID Case No. ADHOC/17/1).

■ *Investor-State Disputes Brought against China*

To a lesser extent, foreign investors into China have utilized the same protections against China. Despite the large number of BITs signed by China, there have only been three ICSID cases registered against China in the 25 years that China has been a member of ICSID:

- The most recent claim was brought in 2017 by Hela Schwarz GmbH, a German food and spice manufacturer, in relation to an expropriation of its Chinese subsidiary's right to use state-own industrial land in Shandong Province. The claim was submitted to arbitration based on the 2003 China-Germany BIT (ICSID Case No. ARB/17/19). On 10 August 2018, the Tribunal denied Hela Schwarz's request for provisional measures. The award in this dispute has not yet been issued.
- A claim was registered in 2014 by a South Korean property developer, Ansung Housing Co., Ltd., alleging that the Sheyang-Xian government's actions caused it losses of more than 100 million RMB (US\$16.3 million). Ansung's claim was brought pursuant to the dispute resolution clause in the 2007 China-Korea BIT. Ansung's claim was dismissed as time-barred in 2017 (ICSID Case No. ARB/14/25).
- The first case was brought in 2011 by Ekran Berhad, a Malaysian construction company, in relation to the revocation of the company's rights to its 900 hectares of leasehold land in the Hainan province. The case was settled three months after registration [(ICSID Case No. ARB/11/15).

■ *What the Case Law Shows*

The disputes that the Chinese investors brought to date have varying outcomes. In a number of cases, the respondent States prevailed on jurisdiction. In other cases, Chinese investors prevailed. There are cases where the Chinese investors would reach mutually acceptable settlements with respondent States at early stages of the arbitration proceedings.

These outcomes are in line with the general statistics of investor-State arbitration outcomes published by ICSID on a regular basis.

The disputes brought by the Chinese investors against respondent States demonstrate that investment protection is a tool that many Chinese companies are now familiar with, and that they will use this tool to safeguard their investments overseas.

Investor-State Arbitration

Investor - State Arbitration

Investor-State arbitration is a practice that allows foreign investors to take their disputes with the host States out of the jurisdiction of the recipient State and before an international investment tribunal for final and binding resolution through arbitration.

Since 1990, when the first investor-State dispute was brought to resolution, investor-State arbitration has grown into a highly dynamic practice area. A vast majority of investor-State disputes are based on investment protection treaties, either bilateral or multilateral.

Investment protection treaties typically guarantee to foreign investors:

- Protection from unlawful expropriation and nationalization;
- Protection against arbitrary, discriminatory measures that impair the investor's usage and enjoyment of the investment;
- The right to be treated no less favourably than domestic investors or investors from other countries (the "most favoured nation" clause in investment treaties);
- The right to "fair and equitable treatment";
- The right to "full protection and security";
- The right to transfer capital and returns out of the host State without delay; and
- A guarantee that the host state will observe any obligation it has undertaken with regard to a qualifying investment.

Investment protection treaties provide for recourse to investor-State arbitration to enforce these substantive guarantees.

Investor-State arbitration provisions are integral parts of the vast majority of investment protection treaties, both multilateral and bilateral. The UNCTAD counts over 2,950 bilateral investment treaties, and over 380 treaties with investment protection provisions in them.

Investment Structuring

Investor-State arbitration is only available if both States – the host State and the jurisdiction of the investor – have agreed to resolve their investment disputes through arbitration. This consent is typically found in investment treaties – bilateral or multilateral – between the host State where the investment is made and the State of the investor. For that reason, it is crucial to structure investment projects with a view to accessing the most beneficial investment protection treaty. Our team advises Chinese investors on this aspect of investment structuring having regard to the network of investment treaties to which China is a party.

Investment Agreements

The majority of Chinese ODI, in particular in the Belt & Road area, is structured through investment agreements, whereby the Chinese investors would either be awarded a concession at a public procurement tender in the host State and sign the concession agreement on that basis, or negotiate with host States a separate set of investment agreements.

When negotiating investment agreements with host States, and when participating in public tender proceedings, it is crucial to make sure that the agency signing the agreements on behalf of the host State acts on behalf of the State such that the State's international law liability may be engaged in case of breaches. Other crucial elements in investment agreements include a carefully drafted sovereign immunity clause, as well as a disputes clause with the choice of the dispute resolution forum.

Prior to signing investment agreements, it is advisable to record all and any representations made by the host State and its officials to the investor during negotiations as to their treatment and support for the Chinese investment. Such representations may later form evidentiary record in support of a fair and equitable treatment claim (breach of investor's legitimate expectations) in cases of undue interference with investment by the host State.

Our team advises Chinese investors on these aspects of negotiations of investment agreements, with a view to enhancing international law protection to Chinese investment overseas.

Political Risk Insurance

Political risk insurance is a sophisticated tool to hedge the risks of undue government interference with investments in fragile economies and developing States. It is costly, but it guarantees compensation in cases of expropriation, adverse regulation, political instability, or physical destruction of investments. A number of insurers are adjusting their political risk insurance products to offer coverage of denial of justice and breach of investors' legitimate expectations, as well.

Most political risk insurance products do not require the insured investor to obtain an investor-State arbitration award to receive compensation. Public insurers, such as MIGA (Multilateral Investment Guarantee Agency), have the additional leverage of resolving disputes with local governments before the disputing parties reach a point of no return and before a full treaty dispute crystallizes.

Political risk insurance and investment arbitration should be seen as complementary concepts that exist to increase investors' confidence in exporting capital to developing markets.

Our team advises Chinese investors on political risk insurance options.

Dispute Avoidance and Investment Crisis Management

Often expropriation or other forms of undue Government interference by host States manifest in an unexpected, abrupt manner. Our team assists clients with managing investment crisis situations by developing a result-oriented strategy to avoid disputes and control investment crisis situation. Our team will focus in particular on preservation of evidence, building of an evidentiary paper trail, and assistance with emergency measures.



Fangda Partners Investment Protection Practice

Founded in 1993, Fangda Partners is one of the largest Chinese law firms with over 500 lawyers working across Hong Kong, Shanghai, Beijing, Shenzhen, and Guangzhou. Members of our team include former senior justices, a former deputy secretary general of the China International Economic and Trade Arbitration Commission, active arbitrators, as well as well-published academics and arbitration practitioners.

Fangda is a part of the developing legal hub in China's Greater Bay Area. Through its offices at the heart of the Greater Bay Area – in Hong Kong, Shenzhen, and Guangzhou - Fangda caters to China's Belt & Road initiative by providing legal services to Chinese and international clients for their investment projects in over 60 jurisdictions in the Belt & Road area.

Fangda is the first Chinese law firm to launch a dedicated investment protection practice. Our transactional partners have assisted Chinese State-owned and private corporations with their investment projects in the Belt & Road jurisdictions. We are therefore familiar with investment protection issues that Chinese companies face overseas, in particular in the Belt & Road area. Fangda's transactional practice thus serves as a valuable resource and as an excellent partner to Fangda's investment protection team.

We pride ourselves on the quality of our work, which has been repeatedly recognized in the media. Our team members are Chinese-English bilingual, and many have foreign qualifications or considerable experience overseas or in foreign-headquartered law firms.

Chambers Asia Pacific 2018 ranks Fangda Partners Band 1 for dispute resolution among Chinese firms. In 2017, China Business Law Journal awarded to Fangda Partners its Dispute Resolution Award, saying that Fangda Partners are "an impressive bench of highly reputed litigators and arbitration counsel based across the firm's offices in Mainland China and Hong Kong."

Recent recognition for Fangda includes: GAR 100 Law Firm, 2018 – Global Arbitration Review; In-House Community Firm of 2016 – International Arbitration, Asia-MENA Counsel; China PRC Law Firm of the Year – Dispute Resolution, 2016 – Chambers Asia.

Key Contacts at Fangda Investment Protection Practice



Peter Yuen
peter.yuen@fangdalaw.com



Helen Shi
helen.shi@fangdalaw.com



Damien McDonald
damien.mcdonald@fangdalaw.com



Olga Boltenko
olga.boltenko@fangdalaw.com

