A THIRD WAY FORWARD: THE FATE OF BITS IN THE INTERNAL MARKET AND CHINA'S CHOICE

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ABSTRACT

Both the European Union (hereinafter "EU") and China reject Investor-State Dispute Settlement (hereinafter "ISDS") mechanisms in their internal market integration, but exhibit a positive stance toward ISDS reform in their external relations with third countries. However, the fate of bilateral investment treaties (hereinafter "BITs") within China is distinct from that of intra-EU BITs. While most EU Member States terminated their intra-EU BITs, China maintains its BIT-styled Mainland and Macao Closer Economic Partnership Arrangement Investment Agreement and Mainland and Hong Kong Closer Economic Partnership Arrangement Investment Agreement (hereinafter "CEPA Investment Agreements") which omit the ISDS clauses. While BITs carving out ISDS clauses do have some value in both the EU context and the Chinese context, the divergent path of China can be principally attributed to its unique "one country, two systems" framework, which limits the tools available for integration

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and allows the continued application of an "international law model" of integration. China's distinct tradition and emphasis on the rule of law further influence its approach. Nonetheless, the implementation flaws of China's CEPA Investment Agreements are more obvious when compared to the EU, due to the absence of comparable control mechanisms. Following the enactment of the Foreign Investment Law of the People's Republic of China (hereinafter "Foreign Investment Law"), the role of the CEPA Investment Agreements in facilitating cross-border investment requires reevaluation. Given the executive-led system of China, investment facilitation could be a suitable approach to protect and promote cross-border investments within the country.

KEYWORDS: *intra-EU BIT, China, ISDS, investment facilitation, "one country, two systems", CEPA investment agreement*

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I. INTRODUCTION

European countries were once the rule-makers of bilateral investment treaties (hereinafter "BITs"). They set "gold standards" for other countries in the world, particularly in the 1990s.[1] With the enlargement of the EU, the number of intra-EU BITs and intra-EU Investor-State Dispute Settlement (hereinafter "ISDS") cases increased significantly. Hostility toward intra-EU BITs began to emerge as early as 2006.[2] In 2018, for the first time, the Court of Justice of the European Union (hereinafter "CJEU") declared ISDS clauses in intra-EU BITs incompatible with EU law in the case of *Achmea*.[3] The *Achmea* ruling resulted in the termination of intra-EU BITs by 23 Member States in 2020.[4] The *Achmea* judgment was *subsequently* extended

[1] Rodrigo Polanco, *EU Investment Policy: Regional Convergence or International Standards? in* STANDARDIZING THE WORLD: EU TRADE POLICY AND THE ROAD TO CONVERGENCE 103, 122 (Francesco Duina & Crina Viju-Miljusevic eds., 2023).
[2] Christoph Herrmann & Mareike Hoffmann, *Investment in the European Union: Competences, Structures, Responsibility and Policy*, *in* HANDBOOK OF INTERNATIONAL INVESTMENT LAW AND POLICY 2213, 2219 (Julien Chaisse et al. eds., 2021).
[3] Case C-284/16, Slovak Republic v. Achmea BV, ECLI:EU:C:2018:158, ¶¶ 57-58 (Mar. 6, 2018).
[4] *See generally* Agreement for the Termination of Bilateral Investment Treaties between the Member

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to *Komstroy*[5] in 2021, *PL Holdings*[6] in 2021, and *Micula*[7] in 2022 respectively. The *Komstroy* judgment, which targets the intra-EU ISDS clause in a multilateral agreement, i.e., the Energy Charter Treaty (hereinafter "ECT"), has played an important role in the withdrawals from the ECT by some Member States and possibly by the EU after failure in the effort of ECT modernization.[8]

However, the scenario of external relations is quite different. Ten years after the EU Commission gained exclusive competence over foreign direct investment (hereinafter "FDI") through the Treaty of Lisbon, the CJEU declared in Opinion 1/17 that extra-EU ISDS clause, i.e., the Investment Court System in the Comprehensive Economic and Trade Agreement between the EU and Canada (hereinafter "CETA"), was compatible with the EU law.[9]

Interestingly, China, as a rule-taker of BITs,[10] adopts a similar approach to the ISDS clause in its internal relations. China omitted the ISDS clauses from the very beginning in its BIT-styled Mainland and Macao Closer Economic Partnership Arrangement Investment Agreement and Mainland and Hong Kong Closer Econmic Partnership Arrangement Investment Agreement (hereinafter "CEPA").[11] Nonetheless, China has no problem maintaining its internal BITs. Externally, after decades of hesitation and evolution, China has finally accepted liberalized ISDS clauses in its third-generation BITs.[12] With respect to ISDS reform, China advocates for an

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States of the European Union, May 5, 2020, 2020 O.J. (L 169) 1 (entered into force Aug. 29, 2020) [hereinafter Termination Agreement]. Austria, Finland, Ireland, Sweden and the United Kingdom did not sign the Termination Agreement. Ireland had terminated its only intra-EU BIT with the Czech Republic in 2011. The United Kingdom has left the European Union as of Feb.1, 2020. For the remaining intra-EU BITs, *see* Julian Scheu, *Note on Intra-EU BITs Not Covered by the Termination Agreement*, U. COLOGNE INT'L INV. L. CTR. COLOGNE (2020), https://iilcc.uni-koeln.de/sites/iilcc/user_upload/IILCC_Note_on_IntraEU_BITs_NOT_Covered_by_the_Termination_Agreement_05_2020.pdf.

[5] Case C-741/19, Republic of Moldova v. Komstroy LLC, ECLI:EU:C:2021:655, ¶¶ 64-66 (Sep. 2, 2021).

[6] Case C-109/20 Republiken Polen v. PL Holdings Sàrl, ECLI:EU:C:2021:875, ¶¶ 46, 56 (Oct. 6, 2021).

[7] Case C-638/19 P, Commission v. European Food and Others, ECLI:EU:C:2022:50, ¶¶ 137-38 (Jan. 25, 2022).

[8] Monika Dulian, *EU Withdrawal from the Energy Charter Treaty*, EPRS (Dec. 4, 2023), https://www.europarl.europa.eu/RegData/etudes/BRIE/2023/754632/EPRS_BRI(2023)754632_EN.pdf.

[9] Case Avis 1/17, Accord ECG UE-Canada, ECLI:EU: C: 2019:341, ¶161 (Apr. 30, 2019).

[10] Bath Vivienne, *China's Role in the Development of International Investment Law from Bystander to Participant*, 15(2) ASIAN J. WTO & INT'L HEALTH L. & POL'Y 359, 365 (2020).

[11] *See generally* Mainland and Hong Kong Closer Economic Partnership Arrangement [hereinafter CEPA] Investment Agreement, China–H.K., June 28, 2017, https://www.tid.gov.hk/english/cepa/legaltext/c.epa14.html (entered into force Jan.1, 2018); Mainland and Macao Closer Economic Partnership Arrangement (CEPA) Investment Agreement, China–Mac., Dec. 18, 2017, https://www.dsedt.g ov.mo/en_US/web/public/pg_cepa_cep a_ai (entered into force Jan.1, 2018).

[12] QINGJIANG KONG, CHINA'S FOREIGN INVESTMENT LAW AMID EVOLVING INTERNATIONAL

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appellate mechanism[13] and has not yet fully embraced the idea of the EU regarding an envisaged multilateral investment court.[14]

The fate of intra-EU BITs has been vigorously debated.[15] However, little attention has been given to "intra-China" BITs. Inspired by EU practices, this article aims to address similar issues in the Chinese context. Specifically, should China maintain the CEPA Investment Agreements? What is the best way for China to protect and promote cross-border investments within the national market? Should it follow the EU model, maintain the current CEPA model, or pursue a third way?

The EU is a supranational organization, whereas China is a unitary sovereign state. Therefore, the underlying rationales of their internal investment policies are somewhat different. For the former, the autonomy of the EU law, particularly the authority of the CJEU in interpreting EU law, is the main concern.[16] For the latter, enabling integration without jeopardizing the high degree of autonomy of the Hong Kong (hereinafter "HK") Special Administrative Region (hereinafter "SAR"), and the Macao SAR is of primary importance. Although the character and competences of the EU and China are divergent, both of their integration models are between full sovereignty and intergovernmentalism. Alternatively, the market integration in both contexts is based on "shared sovereignty".[17] The EU law has a direct effect and supremacy in Member States. However, many issues must still be addressed through intergovernmental cooperation. Owing to the "one country, two systems" policy, mainland China shall refrain from exercising sovereignty over the HKSAR and the Macao SAR on economic issues.

INVESTMENT RULES 168-69 (An Chen et al. eds., 2023).

[13] UNCITRAL Working Group III, *Possible Reform of Investor–State Dispute Settlement (ISDS): Submission from the Government of China*, at 4, U.N. Doc.A/CN.9/WG III/WP.177 (July 19, 2019).

[14] Ming Du, *Explaining Chin's Approach to Investor-State Dispute Settlement Reform: A Contextual Perspective*, 28(4-6) EUR. L.J. 281, 298 (2022).

[15] Markus Burgstaller & Auriane Negret, *Investment Protection Standards: Can EU Law Fill the Shoes of Investment Treaties?*, 41(1) ARB. INT'L 1, 17 (2024); Konstantina Georgaki, *Conflict Resolution Between EU Law and Bilateral Investment Treaties of the EU Member States in the Aftermath of* Achmea, 41Y.B. EUR. L. 374, 400 (2022); Gordon Nardell QC & Laura Rees-Evans, *The Agreement Terminating Intra-EU BITs: Are Its Provisions on 'New' and 'Pending' Arbitration Proceedings Compatible with Investors' Fundamental Rights?*, 37(1) ARB. INT'L 197, 237 (2021); Stephan Wilske & Chloë Edworthy, *The Future of Intra-European Union BITs: A Recent Development in International Investment Treaty Arbitration against Romania and Its Potential Collateral Damage*, 33(4) J. INT'L ARB. 331, 352 (2016). *See generally* DOMINIK MOSKVAN, PROTECTION OF FOREIGN INVESTMENTS IN AN INTRA-EU CONTEXT: NOT ONE BIT? (2022); MICHAEL DE BOECK, EU LAW AND INTERNATIONAL INVESTMENT ARBITRATION: THE COMPATIBILITY OF ISDS IN BILATERAL INVESTMENT TREATIES (BITS) AND THE ENERGY CHARTER TREATY (ECT) WITH THE AUTONOMY OF EU LAW (2022); JULIEN BERGER, INTERNATIONAL INVESTMENT PROTECTION WITHIN EUROPE: THE EU'S ASSERTION OF CONTROL (2021).

[16] Notably, Brexit may indicate that the EU should also care about the balance between its autonomy and the sovereignty of its Member States.

[17] Julien Chaise & Xueliang Li, *Hong Kong's Participation in International Dispute Settlement: Deviations from Conventional Sovereignty*, 17 ASIAN J. WTO & INT'L HEALTH L. & POL'Y 287, 289 (2022).

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Accordingly, the integration model under the CEPA framework involves intergovernmental cooperation, while simultaneously embodying some sovereign elements. Against this background, the EU can be an appropriate comparator for China.

This article proceeds as follows. First, the rise and fall of intra-EU BITs (Part II) and China's approach to cross-border investment protection (Part III) are examined. Next, the value of BITs without ISDS clauses is discussed, the rationales behind the EU and China's choices are explored, and the flaws of the CEPA Investment Agreements (Part IV) are highlighted. Then, a feasible alternative is suggested for China to protect and promote cross-border investments in light of its executive-led system, namely, the investment facilitation approach (Part V). Finally, it concludes (Part VI).

II. THE RISE AND FALL OF INTRA-EU BITS

A. The Rise of Intra-EU BITs

To protect overseas investment, Germany concluded the first BIT in the world with Pakistan in 1959.[18] Subsequently, European States concluded many other BITs. These efforts led to the beginning of international investment law globally after World War II. In parallel with the emergence of BITs, Western Europe began integrating into an economic union. Six countries, i.e., Belgium, France, Germany, Italy, Luxembourg, and the Netherlands established the European Coal and Steel Community, which merged into the European Economic Community (hereinafter "EEC") in 1957. The EEC and the later European Communities (hereinafter "EC") enjoyed only an incidental competence over investment matters through the freedom of establishment, which enabled investments between Member States through the establishment of businesses, but had no external competence in the sphere of investments. The two parallel legal regimes evolved in Europe. With the enlargement of the EC, some extra-EC BITs subsequently became intra-EC BITs. The first was the BIT concluded between Germany and Greece in 1961, which turned into an intra-EC BIT when Greece joined the EC in 1981. The second was the Germany–Portugal BIT signed in 1980, which turned into another intra-EC BIT when Portugal joined the EC in 1986. Most of the BITs concluded in or before the 1980s either contain no ISDS provision or contain ISDS provisions but with a limited scope of application, mostly expropriation only.

With the collapse of the Soviet bloc, most Central and Eastern European

[18] *See generally* Treaty Between the Federal Republic of Germany and Pakistan for the Promotion and Protection of Investments, Nov. 25, 1959, Ger.–Pakistan, https://investmentpolicy.unctad.org/international-investment-agreements/treaty-files/1387/download [hereinafter Germany–Pakistan BIT (1959)].

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economies intended to integrate into the then EC. After its launch in 1993, the EU still had no external competence based on the freedom of establishment.[19] Before the Treaty of Lisbon, Member States enjoyed exclusive competence in concluding BITs with third countries. To promote the accession candidates' economic development and help them transition to a market economy, the EU encouraged its Member States to conclude BITs with the former communist accession candidates.[20] In the 1990s, Member States concluded many BITs with Central and Eastern European countries. The Central and Eastern European countries also concluded BITs among themselves. Following the enlargements of the EU in the early 2000s, the majority of these countries joined the EU and became part of the internal market. As a result, 195 originally extra-EU BITs became the so-called "intra-EU BITs". These BITs remained in force and were unquestioned after the accession. Notably, most of these BITs concluded in the 1990s contain classical ISDS provisions that can be invoked in the case of any violation of a substantive provision in the BIT.

When the Treaty of Lisbon took effect in 2009, Member States transferred the exclusive competence to conclude extra-EU BITs to the EU Commission. Nevertheless, intra-EU BITs did not fall within the EU competence because the term "FDI" contained in Article 207 of the Treaty on the Functioning of the European Union (hereinafter "TFEU") refers to investments originating from non-EU countries.[21] Moreover, Regulation 1219/2012 does not cover intra-EU BITs.[22] Thus, post-establishment investment protection within the EU does not fall under the exclusive competence of the EU.

B. The Fall of Intra-EU BITs

From 2004 onward, intra-EU ISDS cases began to emerge and increase. With the unexpected rise in the number of intra-EU ISDS cases, the EU Commission attempted to assert control over investment protection within the EU.[23] As early as 2006, the EU Commission began expressing objections to intra-EU BITs.[24] It viewed them as redundant in the internal market because EU law was allegedly providing for a comparable level of investment protection. More importantly, the EU Commission was

[19] Christoph Herrmann & Judith Crämer, *Foreign Direct Investment-A "Coincidental" Competence of the EU?*, 43 HITOTSUBASHI J.L. & POL. 85, 89 (2015).
[20] BERGER, *supra* note 15, at 27.
[21] Herrmann & Crämer, *supra* note 19, at 91.
[22] *See generally* Regulation (EU) No 1219/2012 of the European Parliament and of the Council of 12 December 2012 establishing transitional arrangements for bilateral investment agreements between Member States and third countries, 2012 O.J. (L 351) 40.
[23] BERGER, *supra* note 15, at 36.
[24] *Id.* at 37.

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concerned that intra-EU BITs might distort the internal market and create an uneven playing field by establishing a different legal framework for investment protection.[25] For a long time, the compatibility of intra-EU BITs with EU law remained highly controversial among Member States. The majority of Member States wanted to maintain their intra-EU BITs and did not agree with the EU Commission's opinion.[26] They considered intra-EU BITs necessary to ensure legal protection for EU investors before an adequate alternative mechanism had been established.[27] The EU law and BITs coexisted for years until the CJEU rendered its decision in the landmark case *Achmea*.

In 2018, the CJEU ruled in *Achmea* that intra-EU BITs were incompatible with EU law. Since an investment arbitral tribunal does not constitute a court under Article 267 TFEU's preliminary reference procedure, it is unable to submit questions regarding the interpretations of EU law to the CJEU. This would harm the autonomy of EU law. In addition, the CJEU contended that ISDS clauses in intra-EU BITs also violated the principles of sincere cooperation and mutual trust enshrined in EU law.[28] Third, they discriminated among EU investors. The CJEU thus confirmed the EU Commission's view that there was no place for intra-EU ISDS in the single market. Some commentators argue that the main objective is to safeguard the authority of the CJEU in interpretations of EU law through preliminary reference procedures and to protect the integrity of EU law from external judicial scrutiny.[29]

The *Achmea* ruling has far-reaching effects. On May 5, 2020, all Member States, except Austria, Finland, Ireland, the UK, and Sweden, signed the Termination Agreement, ending their intra-EU BITs, including the sunset clauses.[30] On September 2, 2021, the CJEU expanded its ruling in the *Achmea* case to the arbitration clause of the ECT in *Komstroy*. Failing to renegotiate the ECT by, *inter alia*, carving out intra-EU arbitration, the EU advocated for a coordinated withdrawal instead.[31] The CJEU continued to

[25] Herrmann & Hoffmann, *supra* note 2, at 2219.

[26] Lucian Ilie, *What Is the Future of Intra-EU BITs?*, KLUWER ARB. BLOG (Jan. 21, 2018), http://arbitrationblog.kluwerarbitration.com/2018/01/21/future-intra-eu-bits/.

[27] BERGER, *supra* note 15, at 38.

[28] Case C-284/16, Slovak Republic v. Achmea, ECLI:EU:C:2018:158, ¶¶ 58-59 (Mar. 6, 2018).

[29] *See*, *e.g.*, Theodore Konstadinides, *Chapter 16: The Rule of Law as the Constitutional Foundation of the General Principles of EU Law*, *in* RESEARCH HANDBOOK ON GENERAL PRINCIPLES IN EU LAW: CONSTRUCTING LEGAL ORDERS IN EUROPE 287, 295 (Katja S. Ziegler et al. eds., 2022).

[30] The EU Commission once urged Finland and the United Kingdom to terminate their BITs with other EU Member States, otherwise it may initiate infringement proceedings. *See* European Commission Press Release INF/20/859, May Infringements Package: Key Decisions (May 14, 2020), https://ec.europa.eu/commission/presscorner/api/files/document/print/en/inf_20_859/INF_20_859_EN.pdf.

[31] *The Continued Push Against Investor-State Dispute Settlement in Europe and the Way Ahead,* DEBEVOISE & PLIMPTON (Mar. 13, 2023), https://www.debevoise.com/insights/publications/2023/03/the-continued-push-against-investorstate.

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push against intra-EU ISDS clauses. It ruled on October 26, 2021, in the *PL Holdings* decision that *ad hoc* arbitration agreements between EU investors and EU Member States were not compatible with EU law. The CJEU also determined the incompatibility of arbitrations governed by the ICSID Convention with EU law in the case of *Micula.* All these attempts aim at putting intra-EU ISDS to an end.

Notably, the CJEU regarded the CETA's ISDS clause compatible with the autonomy of the EU legal order because Article 8.21 of the CETA defers to the interpretation of EU law made by the CJEU.[32] The rulings on the compatibility of extra-EU BITs have sparked less controversy.[33] However, some consider its reasoning to be unconvincing. If the CETA tribunal can be precluded from the preliminary procedure by respecting the authority of the CJEU in interpreting EU law, why should the CJEU be so stringent with the *Achmea* tribunal?[34] Additionally, if mutual trust constitutes a substantial barrier to intra-EU ISDS, a multilateral investment court or an investment court system, which is a reformed ISDS mechanism, would also be perceived as unnecessary in treaties between the EU and developed countries that comply with the rule of law.[35] If so, the EU's position as a global player would be weakened.[36]

III. CHINA'S APPROACH TO CROSS-BORDER INVESTMENT PROTECTION

China's approach to cross-border investment protection is distinct from EU practices. Instead of all or nothing, China adopts a unique "international law model" to accommodate the interest and dignity of a sovereign state under the framework of "one country, two systems".

A. CEPA: "International Law Model"

According to either the Basic Law of the HKSAR of the People's Republic of China (hereinafter "PRC") or the Basic Law of the Macao SAR of the PRC (hereinafter "Basic Laws"), mainland China shall be restrained from directly exercising sovereignty in the HKSAR or the Macao SAR, except in foreign affairs and defenses. Mainland China's national legislation is generally not applicable to the HKSAR or the Macao SAR with the exception of laws listed in Annex 3 of the two Basic Laws. Under the "one country, two systems" principle, the HKSAR and the Macao SAR enjoy a

[32] Herrmann & Hoffmann, *supra* note 2, at 2248.
[33] *See generally* Case Avis 1/17, Accord ECG UE-Canada, ECLI:EU: C: 2019:341 (Apr. 30, 2019).
[34] Herrmann & Hoffmann, *supra* note 2, at 2248.
[35] BERGER, *supra* note 15, at 211-12.
[36] *Id.*

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high degree of autonomy in economics and many other areas. In particular, the HKSAR and the Macao SAR enjoy independent judicial power and final adjudication.

The "one country, two systems" principle creates a regulatory gap concerning market integration between mainland China and the two SARs. No counterparts of EU law exist in China. The degree of autonomy of the two SARs in economic areas is greater than that enjoyed by EU Member States. As a result, regional integration largely depends on intergovernmental cooperation. International law, which largely operates upon the consent of states, can act as a legal means to promote market integration within a country. A typical example is the bilateral CEPA concluded by mainland China with Hong Kong and that with Macao in 2003.[37] The CEPA is a framework agreement underpinned by four agreements, namely, the Consolidated version of Agreements on Trade in Services signed in 2015, the Agreement of Economic and Technical Cooperation signed in 2017, the Investment Agreement signed in 2017, the Consolidated version of Agreements on Trade in Goods signed in 2018.[38] It is essentially viewed as a free trade agreement (hereinafter "FTA") within a country.[39]

China has accepted the concept of BITs since its first treaty with Sweden in 1982. Although China has evolved from a bystander to an active participant in international investment law, it is still considered a rule-taker with respect to BITs, despite some modest adjustments.[40] The CEPA Investment Agreements are modeled on the third generation of BITs,[41] albeit with some innovation.[42] Nonetheless, they only follow the format of substantive provisions of BITs and exclude the investor-state arbitration regime and state-state arbitration regime.

B. Amicable Dispute Resolution Mechanism

After decades of hesitation, China has generally accepted balanced ISDS clauses in Sino-foreign BITs.[43] The same is true for the HKSAR and the

[37] Hong Kong and Macao also concluded a bilateral CEPA in 2017 between themselves. However, Hong Kong and Macao have not concluded an investment agreement under the CEPA framework yet.

[38] *See Mainland and Hong Kong Closer Economic Partnership Arrangement (CEPA)*, TRADE & INDUS. DEP'T., https://www.tid.gov.hk/english/cepa/legaltext/cepa_legaltext.html.

[39] *See Doing Business in/with the Mainland*, GOVHK, https://www.gov.hk/en/business/businessmainland/cepa/.

[40] Vivienne, *supra* note 10, at 365.

[41] JULIEN CHAISSE, HONG KONG AS AN ACTOR IN INTERNATIONAL ECONOMIC LAW: MULTILATERALISM, BILATERALISM, AND UNILATERALISM 119 (2024).

[42] For example, CEPA Investment Agreements replace "Most-Favored-Nation (MFN)" treatment with "Most-Favored" treatment.

[43] Some BITs or investment chapters in FTAs, such as the Regional Comprehensive Economic Partnership [hereinafter RCEP], have not yet incorporated ISDS clauses.

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Macao SAR. Moreover, both mainland China and the HKSAR have participated in the United Nations Commission on International Trade Law (UNCITRAL) Working Group III and are dedicated to enhancing the ISDS system and contributing to its reform endeavors. The approach of the CEPA Investment Agreements, however, is not consistent with that adopted in China's external relations. Cross-border investors within Chinese territory have no access to international arbitration according to Articles 19 and 20 of the CEPA Investment Agreements. Rather, they can resort to local judicial and administrative remedies, local mediation mechanisms, local complaint mechanisms, and coordination mechanisms by the Working Group of the CEPA Investment Agreements. Notably, investors' complaint and mediation requests are addressed by the host party. The sole mechanism at the regional level is the Working Group under each CEPA Investment Agreement which can notify the concerned party of a dispute and coordinate between the investor and the host party. In this vein, the pattern of the CEPA Investment Agreements is similar to that of the first generation of intra-EU BITs which do not provide for any ISDS procedure.[44] The treatment of cross-border investors in the national market, comparable to that of intra-EU investors after the *Achmea* judgment, is less favorable than that of foreign investors.

China disregards ISDS in the CEPA Investment Agreements for a different reason than the EU does. China lacks a counterpart to the CJEU in its cross-border integration. The CJEU safeguards the autonomy of the EU legal order through the preliminary ruling procedure. In contrast, the Supreme Court of the PRC has refrained from playing any role in regional integration, because the judicial organs of the HKSAR and the Macao SAR are totally independent and they have the final say. Although the Supreme Court of the PRC has ever issued several judicial opinions to support regional integration,[45] they are only guiding opinions for lower-level courts of mainland China. In essence, these opinions only translate party policy into legal policy, without discussing specific cases.[46] Against this background, no control mechanism akin to the preliminary ruling procedure exists across the regions.

Additionally, there is no formal obligation of mutual trust and sincere cooperation in China as in the EU. Owing to the diversity of judicial systems,

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[44] BERGER, *supra* note 15, at 26.

[45] *See, e.g.*, *Opinions of the Supreme People's Court on Providing Judicial Services and Safeguards for Accelerating the Construction of a Unified National Market*, LAWINFOCHINA, https://www.lawinfochina.com/display.aspx?id=39157&lib=law&EncodingName=big5; *Opinions on Providing Judicial Services and Safeguards for Nansha District of Guangzhou Municipality and Deepening the Comprehensive Cooperation among Guangdong, Hong Kong and Macao*, LAWINFOCHINA, https://www.lawinfochina.com/display.aspx?id=42180&lib=law&SearchKeyword=&SearchCKeyword=.

[46] Susan Finder, *Decoding the Supreme People's Court's Services and Safeguards Opinions*, U.S.-ASIA L. INST. (Oct. 31, 2022), https://usali.org/usali-perspectives-blog/decoding-the-supreme-peoples-courts-services-and-safeguards-opinions.

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there is no social foundation for mutual trust. Nonetheless, as the HKSAR and the Macao SAR are constituent parts of the PRC, they should cooperate with the central government in good faith, although no explicit obligations exist.

The approach of the CEPA Investment Agreements to dispute settlement is consistent with that of the CEPA framework agreements, which have no binding dispute resolution mechanisms. The nature of their dispute resolution mechanisms is essentially political. No official discussion or explanation about the design of the dispute resolution mechanisms can be found anywhere. However, some academic voices and debates exist. It is argued that the CEPA is a one-way concession granted to the two SARs by the central government with the purpose of helping HK and Macao recover from the economic crisis, such that binding dispute resolution is not appropriate.[47] On the other hand, it is also proposed that bilateral consultation is insufficient and ineffective, thus, China should learn from international practices and design arbitral or judicial dispute resolution mechanisms under the CEPA framework.[48] One recommendation is to establish a hybrid dispute settlement mechanism that combines political methods with arbitral procedures, modeled on the dispute settlement mechanism of the China-Association of Southeast Asian Nations (hereinafter "ASEAN") FTA.[49]

As a unitary sovereign state, "One Country is the prerequisite and basis for the Two Systems, and the Two Systems are subordinate to and derive from One Country. "[50] The central authorities enjoy overall jurisdiction over Hong Kong and Macao although the two SARs are conferred a high degree of autonomy. Obviously, the central government and the governments of the two SARs are not equal parties. However, the investor-state arbitration mechanism is designed to settle disputes between one state and nationals of the other state and they are treated equally in the process of arbitration. Furthermore, the ISDS mechanism is essentially third-party adjudication.

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[47] Chen Lihu (陈立虎) & Zhao Yanmin (赵艳敏), *CEPA Zhengduan Jiejue Guize Goujian zhi Fenxi* (*CEPA 争端解决规则构建之分析*) [*Analysis on the Dispute Resolution Rules of CEPA*], 125 JINAN DAXUE XUEBAO ZHEXUE SHEHUI KEXUE BAN (暨南大学学报哲学社会科学版) [J. JINAN U. (PHIL. & SOC. SCI. ED.)] 27, 28 (2006).

[48] *See, e.g.*, Ke Jingjia (柯静嘉), *Yue Gang Ao Da Wan Qu Touzi Hezuo de Falü Jizhi ji Qi Goujian* (*粤港澳大湾区投资合作的法律机制及其构建*) [*On the Legal Mechanism and Its Construction for Investment Cooperation in Guangdong-Hong Kong-Macao Greater Bay Area*], 160 GUANGDONG CAIJING DAXUE XUEBAO (广东财经大学学报) [J. GUANGDONG U. FIN & ECON.] 83, 94 (2018).

[49] Mu Yaping (慕亚平) & Chen Xiaoyan (陈晓燕), *CEPA Xieyi Shishi Zhong de Falü Wenti Yanjiu* (*CEPA 协议实施中的法律问题研究*) [*Analyzing the Legal Problems Appearing in the Former Two Phases of CEPA to Promote It Executing Further*], 122 JINAN DAXUE XUEBAO ZHEXUE SHEHUI KEXUE BAN (暨南大学学报哲学社会科学版) [J. JINAN U. (PHIL. & SOC. SCI. ED.)] 1, 7 (2006).

[50] STATE COUNCIL INFO. OFF. PEOPLE'S REP. CHINA, HONG KONG: DEMOCRATIC PROGRESS UNDER THE FRAMEWORK OF ONE COUNTRY, TWO SYSTEMS 44 (2021), http://download.china.cn/en/doc/fulltext1220.doc.

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Arbitrators might intervene in the internal affairs of one country through adjudication and thus jeopardize its sovereignty. Hence, domestic investors in the world generally have no access to investor-state arbitration. Therefore, the ISDS mechanism conflicts with the sovereignty of China.

Moreover, according to Article 18, contracting parties can settle their disputes concerning the interpretation, application, and implementation of the respective CEPA Investment Agreement only through consultation, rather than through traditional state-state arbitration available under other BITs. Implicitly, cross-border investors can not apply for diplomatic protection even though they are treated unfairly or inequitably in local proceedings, because contracting parties belong to one state.

On the other hand, as the WTO dispute settlement mechanism may, in theory, adjudicate trade disputes between mainland China and the HKSAR or the Macao SAR, why does China not view the WTO as jeopardizing its sovereignty? Some argue that China's approach to international adjudication is mainly driven by its selective pragmatism, depending on the field concerned.[51]

IV. THE VALUE OF BITS WITHOUT ISDS CLAUSES

The *Achmea* judgment only considered investor-state arbitration clauses in intra-EU BITs in conflict with EU law. The Termination Agreement is also "without prejudice to the question of compatibility with the EU Treaties of substantive provisions of intra-EU bilateral investment treaties". Nonetheless, most EU Member States chose to terminate their intra-EU BITs as a whole. In contrast, China maintains its CEPA Investment Agreements. Then, a question arises, i.e., whether a BIT without any investor-state arbitration clause has any value. Let us first compare BITs with the EU law and Chinese domestic law.

A. Gaps Between BITs and Union Law/Domestic Law

1. The EU — After *Achmea* and the termination of intra-EU BITs, one of the concerns is whether the EU law offers substantive and procedural safeguards to intra-EU investments equivalent to those provided in intra-EU BITs.[52] Views suggest subtle differences.

The European Commission holds that while there is room for improvement in the EU, EU law and the single market rules can generally

[51] *See* MATTHIEU BURNAY, CHINESE PERSPECTIVES ON THE INTERNATIONAL RULE OF LAW: LAW AND POLITICS IN THE ONE-PARTY STATE 220, 223 (2018).

[52] *See* DOMINIK MOSKVAN, PROTECTION OF FOREIGN INVESTMENTS IN AN INTRA-EU CONTEXT: NOT ONE BIT? 3 (2022).

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offer investors an effective system of protection.[53] The European Commission also admitted that EU law does not cover all issues, and that investors across the single market have some concerns about four key areas, i.e., property protection and compensation for expropriation, the quality of the law-making process, good administration, and effective courts.[54]

Others believe that the disparities between the two different regimes are apparent, and that the main differences concern procedural remedies.[55] Within the EU legal order, individuals have very limited direct access to EU courts. They can sue EU institutions only before an EU court. Although Member States are obliged to apply EU law and the CJEU guarantees uniform interpretation and application of EU law through preliminary procedures, most cases involving EU law fall within domestic courts' residual competence.[56] The CJEU has no competence to adjudicate disputes between investors and the host Member States. Claims for damages against a Member State must be raised before its domestic courts. In this sense, it is argued that the remedies provided by EU law are not comparable to the investor-state arbitration mechanism.[57]

With respect to substantive provisions, it is admitted that the two systems pursue different goals, albeit that some similarities and overlaps do exist. BITs are generally investor-friendly, whereas EU law focuses on balancing public and private interests to benefit all stakeholders in the Union.[58] Hence, EU law is less favorable in claims of legal certainty and legitimate expectations than are intra-EU BITs concerning changes to the regulatory framework.[59] Moreover, EU law has no explicit provisions for intra-EU investment protection but guarantees fundamental freedoms to construct a common market. In this vein, the substantive investment protection regime within the internal market mainly refers to fundamental freedoms, particularly the freedom of establishment and the free movement of capital. However, their primary function is to guarantee market access and non-discrimination, rather than compensation against expropriation in the post-establishment period.[60] The European Commission also admits that EU law offers a more competitive framework of investment rights regarding market access and fundamental freedoms, but lacks an investment protection

[53] *Keynote Speech by Commissioner McGuinness at the Forum on Protecting and Facilitating Investment in the Single Market*, EUR. COMM'N 1, 2 (June 28, 2022), https://ec.europa.eu/commission/presscorner/api/files/document/print/en/speech_22_4182/SPEECH_22_4182_EN.pdf .
[54] *Id.*
[55] *See* BERGER, *supra* note 15, at 81.
[56] *Id.* at 75.
[57] *See id.* at 230; MOSKVAN, *supra* note 15, at 199.
[58] BERGER, *supra* note 15, at 81.
[59] MOSKVAN, *supra* note 15, at 111.
[60] Herrmann & Hoffmann, *supra* note 2, at 2216.

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dimension.[61] At the EU level, investors can only rely upon the European Convention on Human Rights (hereinafter "ECHR"), its First Protocol, and the Charter of Fundamental Rights of the EU (Article 17).[62] The compensation standard thereof is lower than the average standard in investment arbitrations, thus, the ECHR may not provide investors with full and prompt compensation for expropriation.[63]

2. China — When the CEPA Investment Agreements were concluded in 2017, the Foreign Investment Law of the PRC (hereinafter "Foreign Investment Law") had not yet been established. At that time, the CEPA Investment Agreements afforded more favorable treatment to HK and Macao investors by extending national treatment to the pre-establishment stage, with some exceptions. However, since January 1, 2020, when the new law took effect, the market access privileges enjoyed by HK and Macao investors have been blurred because the new law accords the same treatment to all foreign investors beyond the negative list. More importantly, the national negative list has become increasingly shorter in recent years. The remaining value of the CEPA Investment Agreements concerning access lies in the difference between its negative list and the evolving national negative list. According to the current version of the latter, which became effective on November 1, 2024, all restrictions on foreign investment access in the manufacturing sector have been lifted. As such, HK and Macao investors enjoy more favorable treatment than foreign investors only in the educational and cultural sectors. In addition, the free transfer of funds related to investments is also guaranteed by the Foreign Investment Law. Therefore, the CEPA Investment Agreements have become less competitive with respect to establishment and free transfer.

Nevertheless, regulatory differences exist between the domestic legal framework and the CEPA Investment Agreements concerning investment protection. A salient example is that the domestic legal framework does not embrace the concept of indirect expropriation enshrined in the CEPA Investment Agreements. The Administrative Litigation Law of the PRC (2017 Revision) does not provide remedies to individuals against general legislation, administrative regulations, or decisions, even if they are illegal, violate reasonable expectations of investors, or harm their investments. In other words, cross-border investors have no access to justice in disputes arising from legislation modifications or policy changes. Rather, investors can only seek redress against specific administrative measures enacted by local governments that target their investments. Moreover, the compensation standard for (direct) expropriation in mainland China is prescribed by the vague wording "equitable and reasonable" standard, without addressing the

[61] EUROPEAN COMM'N, *supra* note 53, at 3.
[62] MOSKVAN, *supra* note 15, at 160.
[63] *Id.* at 160-61.

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issue of interest.[64] Macao has no explicit rules about expropriation at all. In contrast, the CEPA Investment Agreements provide detailed rules about compensation standards. Another salient example is the fair and equitable treatment (hereinafter "FET") clause, which is provided by the CEPA Investment Agreements but is absent in the new Foreign Investment Law. The FET clause and the indirect expropriation clause are crucial for investors to challenge adverse regulatory changes, including legislation and policy modifications, which cannot be addressed in a domestic legal framework.

In sum, not all substantive provisions of BITs have counterparts in Union law or Chinese domestic law. It seems that BITs without ISDS clauses still have value in both the EU context and the Chinese context. Historically, BITs concluded in early times, such as the German–Pakistan BIT (1965), did not contain any investor-state arbitration clause. The core function of such BITs was expected to act as a focal point in two ways, i.e., for setting general standards for investment protection and for supporting diplomatic negotiations.[65] While modern investment law is almost all about investor-state arbitration,[66] the investment chapters of some FTAs, such as the Protocol on Investment to the Australia–New Zealand Closer Economic Relations Trade Agreement, also drop ISDS clauses. This may imply that BITs that carve out ISDS still have some value worldwide.

B. Different Rationales for the EU's and China's Choices

As mentioned above, the EU has a sophisticated institutional structure and a full set of legal rules to ensure its operation. In contrast, China lacks an effective legal tool to promote market integration, because of the high autonomy granted to the two SARs. These are the primary reasons why the EU and China adopt different approaches *vis-à-vis* their internal BITs.[67] Furthermore, the underlying rationale for the distinct paths of EU Member States and China may lie in their divergent traditions regarding the rule of law.

Few public views or explanations concerning why EU Member States did not just cancel ISDS clauses and maintain the substantive provisions of

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[64] *See* Zhonghua Renmin Gongheguo Waishang Touzi Fa (中华人民共和国外商投资法) [Foreign Investment Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., Mar. 15, 2019, effective Jan. 1, 2020), art. 20, 2019(2) STANDING COMM. NAT'L PEOPLE'S CONG. GAZ. 348, 350.

[65] Jarrod Hepburn et al., *Investment Law Before Arbitration*, 23(4) J. INT'L ECON. L. 929, 934-35 (2020).

[66] *Id.* at 947.

[67] Interestingly, similar distinctions also exist in the world. While some countries, such as Ecuador, terminated their BITs, other countries, such as South Africa, abolished the ISDS regime but maintain BITs. A compromise is the practice of permitting ISDS proceedings after the exhaustion of local remedies, as in India's model.

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intra-EU BITs can be found. Nonetheless, the general principle of effective judicial protection may shed light on this issue. Within the EU, effective judicial protection is a fundamental right and constitutes a general principle of EU law.[68] This principle, born as a fundamental right and reaffirmed in Article 47 of the EU Charter of Fundamental Rights, establishes the right to a fair trial and an effective remedy. It offers the guarantee of effective protection of individual entitlements deriving from EU law at both the national and the EU levels of governance.[69] Any action or inaction of the EU and Member States violating EU law can be subject to review by the CJEU. More recently, since 2018, the principle of effective judicial protection has become the vehicle for enforcing the rule of law in Member States.[70] Member States should ensure sufficient and effective judicial remedies for individuals in the realm of EU law. Consequently, effective judicial protection is viewed not only as an expression of the rule of law in the EU but also as an essential part of the rule of law in the EU.[71] Against this background, we can draw a conclusion by analogy that EU Member States highlight the procedural guarantees provided by BITs. It is thus easy to understand why the majority of EU Member States terminated their intra-EU BITs.

The scenario in China, however, is quite different. The thoughts of Confucianism and Legalism laid down the foundations of China's pre-modern legal system. In Confucianism, *Li*, which can be translated as social virtues, is considered to represent more prominent patterns of behavior than legal rules.[72] Influenced by the thoughts of Confucianism, the Chinese would avoid lawsuits as much as possible. Legalism, or *Fa,* was distinct from the concept of the rule of law held by European countries. Rather, the school of Legalism considers law an instrument in the hands of the rulers to administer citizens.[73] The function of law was not to protect citizens against the power of rulers, but rather *vice versa*. The concepts of Confucianism and Legalism still have far-reaching impacts on China's modern governance. China's modern legal system, which is formulated mainly through legal transplant*,* is an instrument of opening up and reforms. However, the Western concept of the rule of law is not fully accepted. A salient example is the absence of "independent judiciaries" or similar words in mainland China's legal framework. Instead, the Chinese central authority prefers a "legislation-leading model"[74] Accordingly, the governance model in China is called

[68] Konstadinides, *supra* note 29, at 290.
[69] Giulia Gentile, *Effective Judicial Protection: Enforcement, Judicial Federalism and the Politics of EU Law*, 2(1) EUR. L. OPEN 128, 128-29 (2023).
[70] *Id.* at 130.
[71] *Id.* at 131.
[72] BURNAY, *supra* note 51, at 67.
[73] *Id.* at 114.
[74] *Id.*

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"law-based governance".[75] In practice, Hong Kong-based investors have made limited use of the ISDS mechanism.[76] The Hong Kong government actively advocates for mediation in the context of ISDS reforms. It has endorsed the incorporation of mediation in international dispute resolution frameworks.[77] The central government of China, together with other contracting parties, set up the International Organization for Mediation Preparatory Office in the HKSAR in 2023 to carry out preparatory work. Against this backdrop, it is easy to understand why the CEPA Investment Agreements can be maintained.

There is great divergence between the EU and China regarding the rule of law, especially the "thick rule of law". The EU once attempted to launch a sectoral dialogue on the rule of law to strengthen its strategic partnership with China. However, the initiative was resisted by China, and the EU-China 2020 Strategic Agenda for Cooperation only contains a commitment to continue developing dialogue and cooperation on "legal and administrative affairs".[78]

C. Flaws of the CEPA Investment Agreements

An empirical study reveals that local authorities do not take into account treaty obligations when making decisions because they are generally unaware of or unfamiliar with BITs.[79] It can be inferred that local executive branches in China do not consider the CEPA Investment Agreements when carrying out their day-to-day business of government. The empirical study also demonstrates that ISDS claims could trigger pressures and motivations to internalize BITs' obligations to different extents, depending on the state concerned.[80] Unlike other BITs, the CEPA Investment Agreements neither include ISDS mechanisms nor provide state-to-state arbitrations. In this vein, the downsides of the CEPA Investment Agreement are obvious. It has no bite. Alternatively, contracting parties do not bear any legal pressure to settle investment disputes.

Owing to the "legislation-leading model" mentioned above, gaps exist between "the law in the books" and "the law in action". The implementation

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[75] *Decision of the Standing Committee of the National People's Congress on Improving and Strengthening the System of Recording and Review*, THE NAT'L PEOPLE'S CONG. OF CHINA (Dec. 29, 2023), http://en.npc.gov.cn.cdurl.cn/2023-12/29/c_10006 19.htm.

[76] CHAISSE, *supra* note 41, at 253.

[77] *Id.* at 177.

[78] BURNAY, *supra* note 51, at 241.

[79] N. Jansen Calamita & Ayelet Berman, *Assessing the Rule of Law Promise: The Impact of Investment Treaties on National Governance*, *in* INVESTMENT TREATIES AND THE RULE OF LAW PROMISE: AN EXAMINATION OF THE INTERNALISATION OF INTERNATIONAL COMMITMENTS IN ASIA 299, 327 (N. Jansen Calamita & Ayelet Berman eds., 2022).

[80] *Id.* at 311.

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and enforcement of rules by competent administrative and judicial authorities remain major challenges for China in many legal fields.[81] There is a complaint in civil society that "the big door opens, but the small door closes", which means that investors cannot enjoy all of the benefits of the CEPA agreements in practice. Against this backdrop, the flexible and amicable dispute resolution mechanisms of the CEPA Investment Agreements can hardly foster a predictable and transparent rule-based business environment, which is essential for further national market integration. Without a predictable outcome and without the pressure of enforcing a predictable binding award, it becomes more difficult for the parties to reach a compromise in a specific dispute.[82] If amicable dispute resolution mechanisms fail, investors can only rely on local remedies. As such, the scenario is quite similar to that faced by cross-border investors within the EU after the termination of intra-EU BITs.

National courts of EU Member States are obliged to enforce EU law. In contrast, the CEPA Investment Agreements no longer function in the case of local remedy. Despite some scattered provisions, the Chinese legal system lacks an explicit and general rule on the exact status of international treaties in the hierarchy of the domestic legal system.[83] Strictly speaking, the CEPA agreements are neither "international treaties", nor typical domestic laws enacted by the legislative branch. Therefore, the nature of the CEPA agreements is obscure. Local courts do not apply the CEPA Investment Agreements to settle investment disputes.[84] Investors can hardly rely on the CEPA Investment Agreements to protect themselves against unlawful acts or inappropriate legislation in local courts.

Even though the CJEU and the Commission get involved in national procedures through preliminary rulings and infringement proceedings, respectively, the European Commission's 2022 Eurobarometer survey on investment protection shows that only 56 percent of companies were confident in the local remedies in Member States.[85] Many realize the limits and shortcomings of the "mutual trust" principle and raise concerns about the quality of the protection offered by domestic courts of EU Member States.[86] It is contended that despite the safeguards and enforcement

[81] BURNAY, *supra* note 51, at 114.

[82] Vivian Gabriel, *The New Brazilian Cooperation and Facilitation Investment Agreement: An Analysis of the Conflict Resolution Mechanism in Light of the Theory of the Shadow of the Law*, 34(2) CONFLICT RESOL. Q. 141, 153 (2016).

[83] Xue Hanqin & Jin Qian, *International Treaties in the Chinese Domestic Legal System*, 8(2) CHINESE J. INT'L L. 299, 300 (2009).

[84] Thus far, the author has not found any public case arising from or related to the two CEPA Investment Agreements.

[85] EUROPEAN COMM'N, *supra* note 53, at 2.

[86] Johannes Hendrik Fahner, *Anxieties About Achmea: Dutch Interim Relief Judge Refuses to Torpedo London-seated intra-EU Arbitration*, KLUWER ARB. BLOG (Dec. 15, 2022), https://arbitrationblog.kluwerarbitration.com/2022/12/15/anxieties-about-achmea-dutch-interim-relief-judge-

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mechanisms in place at the EU level, the EU is unable to guarantee a consistent level of protection across its Member States.[87] Accordingly, Julien Berger warns that turning away from the long-established international investor-protection regime without creating a substitute within the EU could create a regulatory gap or a decline in investor protection in certain Member States.[88] He thus argues for a substitute for intra-EU investment treaties to prevent the risks of forum shopping and investment restructuring.[89]

The quality and independence of China's judicial authorities differ significantly, similar to those of EU Member States, whereas there are no similar control mechanisms across the whole national market. If EU law is insufficient to protect cross-border investments, the CEPA Investment Agreements are unqualified. It is argued that the procedural remedy of international investment law cannot be completely detached from its substantive provisions.[90] China should bridge this gap by establishing an effective enforcement mechanism. Otherwise, China may also face the risk of investment relocation or restructuring. This would harm the process of market integration across the regions.

Of course, this does not mean that the CEPA Investment Agreements should incorporate the ISDS regime. As mentioned above, the ISDS clause is incompatible with the sovereignty of China. Moreover, inconsistent interpretations of the same treaty text by different arbitral tribunals mean that the investor-state arbitration mechanism is also not capable of building a coherent and integrated system and can therefore hardly create any legal certainty or predictability.[91] The negotiation history of the ICSID Convention suggests that the original assumption about the judicial function of the ISDS regime was about resolving specific disputes concerning specific parties, rather than performing public functions.[92]

refuses-to-torpedo-london-seated-intra-eu-arbitration/.

[87] Cristina Sáenz Pérez, *Mutual Trust as a Driver of Integration: Which Way Forward?*, *in* RESEARCH HANDBOOK ON GENERAL PRINCIPLES IN EU LAW: CONSTRUCTING LEGAL ORDERS IN EUROPE 530, 537 (Katja S. Ziegler et al. eds., 2022).

[88] BERGER, *supra* note 15, at 234.

[89] *Id.* at 208.

[90] Sergio Puig, *No Right Without a Remedy: Foundations of Investor-State Arbitration*, *in* THE FOUNDATIONS OF INTERNATIONAL INVESTMENT LAW: BRINGING THEORY INTO PRACTICE 235, 236 (Zachary Douglas et al. eds., 2014).

[91] BERGER, *supra* note 15, at 230.

[92] Yanwen Zhang, *The Judicial Function of Investment Tribunals: Taking Foundational Assumptions Seriously*, 25(1) J. INT'L ECON. L. 129, 146 (2022).

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V. A POSSIBLE ALTERNATIVE IN LIGHT OF THE EXECUTIVE-LEAD SYSTEM

Within the EU, some propose the establishment of an intra-EU investment court,[93] some infer that it is unlikely to be accepted by the CJEU unless the envisaged intra-EU investment court is subject to its supervision,[94] and others deem a new court not desirable within the EU without any substantive provisions to rely on.[95] Is it feasible for China to address the gap regarding ISDS mechanism by creating a tailored regional judicial or arbitral system under the CEPA framework or establishing a counterpart to the CJEU with a similar principle of effective judicial protection? The answer should be no, primarily because of the unique executive-led governance system in place across the regions.

A. The Executive-Led System of China

Hong Kong's governance model has the shape of a "separation of powers", but the executive branch is more authoritative and plays a more active role in governance than the other branches do. This creates essentially an executive-led system with the Chief Executive at the core.[96] While the Basic Law does not explicitly mention the term "executive-led system", it highlights the dominance of the executive authorities by describing the functions of the Chief Executive, the executive authorities, the legislature, the judiciary, and others in that sequence in Chapter 4 entitled "Political Structure".[97]

According to the Basic Law, the central authorities exercise power over the executive, legislature, and judiciary in the HKSAR in different dimensions and degrees.[98] Hong Kong's judiciaries are independent of the Supreme Court of the PRC. Members of the Legislative Council of the HKSAR are elected by local electorates. Although legislation passed by the Legislative Council shall be submitted to the Standing Committee of the National People's Congress for recording, the recording procedure does not prevent the laws from taking effect. In other words, HKSAR legislation does not require approval from the central government. In contrast, the locally elected Chief Executive and the principal officials nominated by the Chief Executive in the HKSAR must be appointed by the central government and

[93] *See* MOSKVAN, *supra* note 15, at 221-22; DE BOECK, *supra* note 15, at 454.
[94] Fahner, *supra* note 86.
[95] BERGER, *supra* note 15, at 218.
[96] XIAO PING, THE ORIGINAL INTENT OF "ONE COUNTRY, TWO SYSTEMS": AN INFORMAL CHAT ON "ONE COUNTRY, TWO SYSTEMS" 93 (2020).
[97] *Id.* at 94-95.
[98] *Id.* at 93.

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they must carry out directives issued by the central government.[99] Therefore, the only effective nexus between mainland China and the HKSAR is the executive authority.

The Chief Executive, who is in charge of the executive branch, is also the head and representative of the HKSAR. The Chief Executive is accountable to both the HKSAR and the central government. The Basic Law highlights the authority of the Chief Executive in the HKSAR's governance by vesting the post with "dual function" and "dual accountability".[100] The executive branch is the most direct and effective interface between the central government and the HKSAR.[101]

The political structure of the Macao SAR is almost the same as that of the HKSAR. Accordingly, market integration across the three regions has historically been, and continues to be, primarily driven by the executive branches rather than the judiciary or legislative branches. For example, to implement the CEPA agreements, the Guangdong Provincial Government and the Government of the HKSAR signed the Framework Agreement on Hong Kong/Guangdong Cooperation in 2010. Similarly, the Guangdong Provincial Government and the Government of Macao SAR signed the Framework Agreement on Cooperation between Guangdong and Macao in 2011. Each Framework Agreement on Cooperation is implemented and administered by the Cooperation Joint Conference mechanism constituted by the government staff of the two sides.

China's executive-led governance system is fundamentally different from the judicial-centric model of the EU. The preliminary procedure, carried out by the CJEU and national courts, plays a pivotal and ongoing role in promoting EU integration.[102] It establishes a constitutional nexus between the European and the national courts, and constitutes the cornerstone of the Union's judicial federalism.[103] In other words, the judiciary is the custodian of the EU legal order and it guarantees market integration. In contrast, under the principle of "one country, two systems", the decentralized judicial systems can hardly play any role in promoting national market integration across the regions. Similarly, the executive-led governance system, combined with the unequal status of the two SARs relative to mainland China, makes it impractical to establish a tailored judicial or arbitral institution under the CEPA framework.

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[99] *Id.*
[100] *Id.* at 94.
[101] *Id.*
[102] Thomas de la Mare & Catherine Donnelly, *Preliminary Rulings and EU Legal Integration: Evolution and Statis*, *in* THE EVOLUTION OF EU LAW 228, 228 (Paul Craig & Gráinne de Búrca eds., 3d ed., 2021).
[103] ROBERT SCHÜTZE, AN INTRODUCTION TO EUROPEAN LAW 170 (2023).

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B. The Compatibility of Investment Facilitation with the Executive-Led System

Given the enforcement paradox, the investment protection regime may not be the most suitable approach. China must explore viable alternatives that align with its executive-led system. Investment facilitation, which has no universally accepted definition, is an emerging investment policy to facilitate investments and contributes to an investment-friendly business environment.[104] Brazil developed an innovative model focusing on investment facilitation and dispute prevention in 2015, namely the Cooperation and Facilitation Investment Agreement (hereinafter "CFIA").[105] The CFIA model moves away from the adversarial approach of traditional agreements and adopts a cooperative approach that contributes to the mutual benefit of investors and states.[106] Brazil has thus far concluded CFIAs with 16 countries and one regional economic organization, namely the Southern Common Market (MERCOSUR for its Spanish initials), although some of them have not yet come in force.[107] The ASEAN countries adopted the ASEAN Investment Facilitation Framework (hereinafter "AIFF") in 2021,[108] which was a significant step in regional investment cooperation. The EU and Angola concluded a first-ever Sustainable Investment Facilitation Agreement (hereinafter "SIFA") in 2023.[109] At the WTO, 112 members finalized the text negotiation on an Investment Facilitation for Development Agreement (hereinafter "IFD Agreement") in 2023.[110]

Investment facilitation is generally about making it easier for investors to establish or expand their investments, and operate their businesses in host

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[104] *See generally* Shantanu Singh, *What's Happening on Investment Facilitation: A Survey of Recent Global Developments*, INV. TREATY NEWS (Sep. 30, 2023), https://www.iisd.org/itn/en/2023/09/30/whats-happening-on-investment-facilitation-a-survey-of-recent-global-developments/.

[105] *Cooperation and Facilitation Investment Agreement Between the Federative Republic of Brazil and*, UNCTAD INV. POL'Y HUB (2015), https://investmentpolicy.unctad.org/international-investment-agreements/treatyfiles/478 6/download.

[106] José Henrique Vieira Martins, *Brazil's Cooperation and Facilitation Investment Agreements (CFIA) and Recent Developments*, INV. TREATY NEWS (June 12, 2017), https://www.iisd.org/itn/en/2017/06/12/brazils-cooperation-facilitation-investment-agreements-cfia-recent-developments-jose-henrique-vieira-martins/.

[107] *See Brazil, International Investment Agreements Navigator*, UNCTAD INV. POL'Y HUB, https://investmentpolicy.unctad.org/international-investment-agreements/countries/27/brazil (last visited June 4, 2025).

[108] *ASEAN Investment Facilitation Framework*, ASEAN (2021), https://asean.org/wp-content/uploads/2021/11/ASEAN-Investment-Facilitation-Framework-AIFF-Final-Text.pdf.

[109] Sustainable Investment Facilitation Agreement Between the European Union and the Republic of Angola, O.J. (L 2024/830) 1, 1, https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:L_202400830#:~:text=This%20Agreement%20aims%20at%20facilitating%20the%20attraction%2C%20expansion,adopted%20or%20maintained%20by%20the%20Parties%20affecting%20investment.

[110] *See generally* World Trade Organization [hereinafter WTO], Investment Facilitation for Development Agreement, WTO Doc. INF/IFD/W/55 (Feb. 13, 2024).

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countries.[111] It encompasses policies, measures, and practices aimed at minimizing or eliminating ground-level obstacles to investment.[112] The scope of investment facilitation provisions differs and generally includes information provision, the transparency of the investment framework, the streamlining of administrative procedures, the predictability of the policy environment, and the accountability and efficiency of government officials.[113] Promoting investment facilitation often does not require legislative involvement. Instead, most investment facilitation practices concern how rules and regulations are accessed, applied, and complied with, rather than their substance.[114] For example, administrative procedures can be streamlined within the existing legislative frameworks.[115] In other words, facilitation can be realized by optimizing regulatory frameworks and investment administrative processes without modifying legislation. Furthermore, investment facilitation focuses primarily on removing excessive bureaucratic impediments and red tape related to administrative procedures and thus falls within the competence of the executive branch. In essence, it is a process of self-improvement of the administrative governance under which investors operate. Thus, the executive branch plays a central role in realizing facilitation.

Investment facilitation policies also include investment dispute prevention or resolution mechanisms.[116] However, they are essentially processes of self-correction or rectification at an early stage either by executive institutions or by judicial organs of the host state. Although investment facilitation agreements mention the existence or establishment of judicial remedies for investors concerning administrative decisions in the host states, these are only a constituent part of streamlining administrative procedures. Compared with BITs, which are primarily enforced and guaranteed by ISDS mechanisms, investment facilitation agreements are mainly implemented through state parties' active reform in institutional governance and voluntary improvement in administrative governance ability, although they are backed by a state-to-state arbitration mechanism as the last resort.[117] In other words, the executive authorities and agencies, rather than the judicial organs, play a dominant role in enforcing measures of investment

[111] *Global Action Menu for Investment Facilitation*, UNCTAD, at 4 (Sep. 2016), https://investmentpolicy.unctad.org/uploaded-files/document/Action%20Menu%2001-12-2016%20EN%20light%20version.pdf.
[112] *World Investment Report 2024*, UNCTAD, at 109 (2024), https://unctad.org/system/files/official-document/wir2024_en.pdf.
[113] *Id.*
[114] *Id.* at 134.
[115] United Nations Conference on Trade and Development [hereinafter UNCTAD], *Investment Facilitation: Progress on the Ground*, 6 INV. POL'Y MONITOR 1, 3 (2022), https://unctad.org/system/files/official-document/diaepcbinf2022d1_en.pdf.
[116] *World Investment Report 2024*, *supra* note 112, at 109.
[117] As mentioned above, the state-to-state arbitration mechanism is also not feasible within China.

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facilitation. Therefore, the investment facilitation approach is in line with the executive-led system of China.

C. The Harmonization of Internal and External Integration Policies

Despite its self-improvement character, the promotion of investment facilitation requires cross-border coordination and collaboration. To promote and facilitate investment projects, relevant authorities, i.e., outward investment agencies and inward investment agencies, need to establish regular consultations or formal collaborations.[118] Hence, bilateral, regional, and multilateral cooperation constitute an important aspect of investment facilitation policy.

China has made significant contributions to global governance with respect to investment facilitation. Mainland China, the HKSAR, together with eight other economies, created the Friends of Investment Facilitation for Development (hereinafter "FIFD")[119] to start informal dialogue in the WTO in 2017. Shortly thereafter, this investment facilitation initiative was echoed and embraced by an increasing number of economies, and finally contributed to the start of formal negotiations. China provided pragmatic solutions for issues of dispute during the negotiations and made key contributions to the successful conclusion of the IFD Agreement, receiving high recognition from the parties involved.[120] Hong Kong also actively participated in the process and firmly supported the work that was being done.[121]

At the regional and bilateral levels, China also advocates for and accepts provisions of investment facilitation. The G20 Guiding Principles for Global Investment Policymaking published in 2016 under the Chinese presidency highlights transparency, coherence, and predictability. Several BITs and FTAs concluded by China include provisions on investment facilitation. However, these provisions are scattered and fall short compared with frameworks such as the CFIAs, SIFA, IFD Agreement, or even the AIFF. While each CEPA Investment Agreement includes a specific provision for investment facilitation, it cannot, as a whole, be considered a comprehensive facilitation approach.[122]

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[118] UNCTAD, *supra* note 111.

[119] WTO, Proposal for a WTO Informal Dialogue on Investment Facilitation for Development, WTO Doc. JOB/GC/122 (Apr. 26, 2017).

[120] *China Played Key Role in IFD Agreement Text Negotiations: Official*, ST. COUNCIL CHINA (July 8, 2023), https://english.www.gov.cn/news/202307/08/content_WS64a8a88ec6d0868f4e8dd97c.html#:~:text=The%20IFD%20agreement%20is%20the%20first%20negotiation%20topic,and%20participating%20in%20the%20negotiation%20of%20the%20IFD.

[121] CHAISSE, *supra* note 41, at 180.

[122] Wang Shumin (王淑敏), Waizi Lifa de Touzi Bianlihua Chuangxin Zhi Lu (外资立法的投资便利化创新之路) [Research on the Innovation Road Concerning the Investment Facilitation from the

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The Foreign Investment Law and its implementation regulation[123] include promoting transparency and efficiency and establishing a complaint mechanism for foreign investors. Pilot free trade zones in mainland China have established a "single window" system. Nonetheless, these measures are preliminary. The "hard core" of investment facilitation policy, such as the participation of private entities in policy-making and regular private-public dialogue, remains unaddressed.[124]

The accumulation of experience in domestic governance is a prerequisite for effective participation in global governance. Mainland China has proposed adopting a coordinated approach to the rule of law domestically and in matters involving foreign parties.[125] The incorporation of the investment facilitation model into its national market integration efforts could align China's internal and external integration strategies and help China become a rule-maker in this respect. China can design a regional facilitation agreement and integrate it into the CEPA framework.

VI. CONCLUSION

Both the EU and China differ significantly in their approaches to internal and external integration, particularly regarding investment agreements and dispute resolution mechanisms. EU Member States, once rule-makers of BITs, terminated most intra-EU BITs after the *Achmea* judgment. While the EU has sought to reshape the international investment dispute settlement regime by advocating for a permanent investment court, it has shown no intent to establish an internal investment court to address the gap between BITs and EU law. China, a rule-taker of BITs, finally accepted ISDS clauses in almost all Sino-foreign BITs after hesitation and restrictions for approximately a decade, but excludes the ISDS regime from its internal BITs, namely, the CEPA Investment Agreements.

Despite the common fate of ISDS clauses in both contexts, the fates of internal BITs differ. While the EU disregards the international investment law regime, China maintains it, albeit in a unique way. The rationale behind China's choice is primarily due to the "one country, two systems" principle,

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Legislation of Foreign Investment], 4 ZHENG FA LUN CONG (政法论丛) [J. POL. SCI. & L.] 76, 84 (2024).

[123] Zhonghua Renmin Gongheguo Waishang Touzi Fa Shishi Tiaoli (中华人民共和国外商投资法实施条例) [Implementing Rules of the Foreign Investment Law of the People's Republic of China] (promulgated by the St. Council, Dec. 26, 2019, effective Jan. 1, 2020) ST. COUNCIL GAZ., Jan. 20, 2020, at 13, https://www.gov.cn/gongbao/content/2020/content_5469633.htm.

[124] Liang Yong (梁咏), Touzi Bianlihua Yiti de Xingqi Yu Touzi Tiaoyue de Fanshi Zhuanbian (投资便利化议题的兴起与投资条约的范式转变) [The Emergence of Investment Facilitation and the Paradigm Shift of Investment Treaties], 516 FAXUE (法学) [L. SCI.] 174, 182 (2024).

[125] *Full Text of the Report to the 20th National Congress of the Communist Party of China*, QIUSHI (Oct. 26, 2022), http://en.qstheory.cn/2022-10/26/c_824626.htm.

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which results in the lack of a counterpart of EU law regarding regional integration. The "legislation-leading model" that is prevalent in mainland China, as well as the far-reaching influence of traditional *Li* and *Fa,* is another important factor.

Nonetheless, the EU's practice may indicate that the function of BITs without an effective remedy is limited, at least in the context of an internal market. Despite the control mechanisms within the EU, concerns remain about whether EU law sufficiently protects investments, which prompts calls for alternative solutions. The enforcement issues surrounding the CEPA Investment Agreements are more apparent than those in the EU context. Without granting private investors access to international or regional forums, these agreements are rarely applied for investment protection. Since the enactment of China's Foreign Investment Law in 2020, the advantages for Hong Kong and Macao investors with respect to market access and free transfer granted by the CEPA Investment Agreements have almost disappeared. China must reassess the function of the CEPA Investment Agreements in furthering national market integration.

Given the executive-led governance systems of the HKSAR and Macao SAR, neither a regional judicial nor arbitral investment dispute resolution mechanism nor the EU's judicial approach seems suitable for China. A more promising alternative is the investment facilitation approach, as it aligns with the executive-led systems across the three regions. If adopted, this approach could harmonize China's internal and external integration strategies.

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