US–China BIT Negotiations March On

The road ahead is challenging but worthwhile

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The first Strategic and Economic Dialogue between China and the US under the Obama administration, and the upcoming US-China Joint Commission on Commerce and Trade talks in October have grabbed headlines for the last few months. But another important set of bilateral talks is proceeding lower on the radar screen. The US and China are now in talks to negotiate a bilateral investment treaty (BIT). But despite its potential to impact the US-China economic and trade relationship significantly, it has received scant coverage. If the lengthy BIT talks are successful, the treaty would have important benefits for investors in both countries.

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A BIT ABOUT BITS

The US and China have each negotiated numerous BITs, which are intended to expand and protect foreign investors rights. BITs set out basic protections for investments, including both non-discriminatory and fair and equitable treatment, transparency of domestic laws and procedures, compensation for expropriation, and provisions for dispute resolution, including binding arbitration.

Partly as a result of the failure to achieve a multilateral agreement on investment that would apply to a wider range of countries, the way arrangements like the WTO do, there is now a web of BITs worldwide. The US has about 50 BITs or similar agreements covering investment, and China over 100. The US uses a so-called "model BIT," which is updated periodically to reflect developments in the area and which serves as a starting point for BIT negotiations with individual countries. The US is now wrapping up updates to its latest model BIT, which will serve as the starting point for the US-China negotiations. The types of treaties that China has previously negotiated provided limited protection to investors, but China has more recently expanded considerably the rights of investors in China.

CURRENT US–CHINA BIT NEGOTIATIONS

As a result of high-level agreements reached between the two countries during the Strategic Economic Dialogue talks in the summer of 2008, the US and China are now in the preliminary phases of negotiations over a possible BIT. Negotiating this will be far harder than any similar treaty the two countries have separately previously negotiated, and both sides are thus moving cautiously in light of the numerous issues raised. Additionally, treaties require approval by the US Senate, further complicating the process.

The US hopes that successful BIT talks will address numerous concerns of American investors in China. This includes perceived discriminatory treatment, particularly at provincial and local levels, regulatory delays, lack of transparency, performance requirements, such as local content requirements or export quotas, restrictions on transfer of capital, and concerns about the enforceability of rights in Chinese courts.

Like the US model BIT, any US–China investment treaty likely would set out general principles to be applied in practice by both governments and, if necessary, arbitration panels. Investors likely would be guaranteed access to independent binding arbitration concerning resolutions of disputes arising under the treaty. Those arbitrations would be governed by the terms of the BIT and international law standards, not by US or Chinese domestic law. While Chinese investors already enjoy many of these rights protecting their investments in the US, a BIT would serve to provide further assurances that Chinese investments in the US would continue to be treated in a non-discriminatory manner. Likewise, a treaty would further serve to attract much-needed US foreign investment into China. It would also serve more broadly to strengthen the rule of law in China and support market-oriented reforms further.

Agreement on a US–China BIT would provide mutual benefits to both countries, but there are clearly significant challenges ahead. For example, the US likely will want the BIT's protections to apply to all sectors of the Chinese economy, excluding only those specific sectors that China insists be exempted. China, however, to date has been reluctant to employ this "negative list" approach, and might prefer that the BIT's protections apply only to those sectors that China specifically agrees.

MORE CHALLENGES AHEAD

In addition, the US likely will want national treatment guarantees against discrimination to apply to pre-establishment activities, as well as to investments already established, to protect against discriminatory registration or application standards or conduct. China, however, likely will prefer that the national treatment guarantee apply instead only once investments are established. Possible restrictions on favorable treatment currently provided to Chinese state-owned enterprises also will be controversial.

The exact scope of any dispute resolution provisions also would also be difficult to negotiate. While the details of China's more recent BITs demonstrate a willingness to accord binding treatment to arbitration findings, including a right to monetary damages, it remains to be seen whether China will be comfortable with such an approach in negotiations with the US.

In addition, important strategic issues will also color negotiations. For example, some in the US business community will be reluctant to see the US accept less than a "gold standard" BIT tracking closely the American model BIT. This is particularly likely in light of upcoming tough BIT negotiations with other major countries, including India and Russia.

From China's perspective, leadership likely will seek assurances from the US that Chinese investments in the US will not be subject to discriminatory approval processes under the US national security review procedures involving the Committee on Foreign Investment in the US. The recent high-profile aborted attempts by CNOOC and Huawei to purchase US assets in the face of significant political backlash have created concerns in China that the US is not open to Chinese investment, at least not in key sectors such as energy or high-technology. Nonetheless, the US will almost certainly insist that any BIT not circumscribe current US national security reviews of proposed investments.

For these reasons, the successful conclusion of US–China BIT negotiations would provide substantial benefits to both countries. However, the road ahead will not be short and will present a number of challenges. We should expect that the talks may not be resolved for some time, possibly years. But at the end of the day the wait will be worth it for both countries.

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