

# Towards Greater Integration? Legal and Policy Directions of Chinese Investments in Pakistan on the Advent of the Silk Road Economic Belt

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## ABSTRACT

Pakistan has an enduring friendship with China, and the two countries have long-standing economic ties. There is an existing strong investment flow between the two countries, but the new Chinese Silk Road Economic Belt (SREB) initiative and its offshoot China–Pakistan Economic Corridor (CPEC) will substantially increase the flow of Chinese investments in Pakistan. In the auspices of the SREB, China will finance its companies to build a comprehensive regional transportation network in order to stimulate economic growth and social development. The SREB Action Plan has a more viable strategy for long-term development as compared with the existing regional economic integration and development models, and the CPEC will undoubtedly create numerous opportunities for the two countries. A scrutiny of the Chinese policies to invest in Pakistan and the prevalent strong bilateral regime for investment promotion and protection suggest that China–Pakistan investment relations reflect a move towards much deeper economic integration. However, the various legal and policy orientations of these Chinese projects reveal serious challenges in reaching the overall vision, harnessing it with the intended objectives, and enhancing the legitimacy of its implementation strategies. There is a need for proactive solutions for the transnational problems that the CPEC and the SREB are going to generate.

**KEYWORDS:** Silk Road Economic Belt, China–Pakistan Economic Corridor, bilateral investment treaty, free trade agreement, special economic zone

## INTRODUCTION

The China–Pakistan friendship is frequently described as ‘all-weather’, ‘iron’, and ‘deeper than the Arabian Sea and higher than the Himalayas’.<sup>1</sup> After the landmark

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1 See eg Laurence Vandewalle, ‘Pakistan and China: ‘Iron Brothers’ Forever?’ European Parliament Policy Department, Directorate-General for External Policies (EU Parliament Think Tank, June 2015); Iftikhar A Lodhi, ‘Pakistan Perceptions and Responses of an All-Weather Friend’ in SD Muni and Tan Tai Yong (ed), *A Resurgent China: South Asian Perspectives* (Routledge 2012) 176.

China–Pakistan Boundary Agreement in 1963,<sup>2</sup> the two countries have strengthened their friendship and cooperation with several joint agreements, memorandums of understanding, and joint declarations covering a wide variety of areas including trade, commerce, investment, energy, transport, and defence.<sup>3</sup> Although the first formal trade agreement was signed already in 1963,<sup>4</sup> the contemporary China–Pakistan trade regime started with the conclusion of a preferential trade arrangement (PTA) in November 2003.<sup>5</sup> In April 2005, the two countries concluded an Agreement on the Early Harvest Programme, which was intended to provide the working framework for the conclusion of a formal and all-encompassing China–Pakistan Free Trade Agreement (FTA).<sup>6</sup> On its implementation on 1 January 2006, the more detailed Early Harvest Programme abolished the earlier trade-only PTA.<sup>7</sup>

The two countries quickly concluded the FTA in November 2006, which took effect in July 2007.<sup>8</sup> In February 2009, the Agreement on Trade in Services was concluded in accordance with the policy framework set out in Article 83 of China–Pakistan FTA.<sup>9</sup> There is a strong perception that the establishment of a comprehensive China–Pakistan free trade area has brought more opportunities for business enterprises of the two countries.<sup>10</sup> However, a study conducted by the Pakistan Business Council in 2013 concluded that despite great potential, Pakistan has not yet achieved the full benefits from its FTA with China.<sup>11</sup> Although bilateral trade between China and Pakistan has shown rapid growth, increasing from US \$6.9

- 2 The text of the China–Pakistan Boundary Agreement was signed on 2 March 1963. The Agreement formally delimited boundary between China’s Sinkiang and Pakistan’s Kashmir.
- 3 See the description of China–Pakistan Bilateral Relations on the official website of the Consulate-General of the People’s Republic of China in Karachi <<http://karachi.chineseconsulate.org/eng/zbgx/t263901.htm>> accessed 29 September 2015. For historical developments of the China–Pakistan trade relations, see eg Samina Shabir and Reema Kazmi, ‘Economic Effects of the Recently Signed Pak-China Free Trade Agreement’ Special Edition (September 2007) *Lahore J Economics* 173; Xu Wang, ‘Sino-Pakistan Economic and Trade Relations: Status Quo and Challenges’ in Rong Wang and Cuiping Zhu (eds), *Annual Report on the Development of International Relations in the Indian Ocean Region* (2014) (Springer 2015) 97–130. See also Jafar Riaz Kataria and Anum Naveed, ‘Pakistan-China Social and Economic Relations’ (2014) 29(2) *South Asian Studies* 395; Khawar Ghumman, ‘PML-N Puts All Its MoUs in Chinese Basket’ *The Dawn News* (13 April 2015).
- 4 Shabir and Kazmi (n 3) 176.
- 5 Preferential Trade Arrangement between the People’s Republic of China and the Islamic Republic of Pakistan, 3 November 2003. See Wang (n 3) 110.
- 6 See Agreement on the Early Harvest Programme for the Free Trade Agreement between the Government of the People’s Republic of China and the Government of the Islamic Republic of Pakistan (signed on 5 April 2005). (China–Pakistan Early Harvest Programme).
- 7 *Ibid* art 4.
- 8 Free Trade Agreement between the Government of the People’s Republic of China and the Government of the Islamic Republic of Pakistan (done at Islamabad on 24 November 2006 and entered into effect on 1 July 2007). (China–Pakistan FTA).
- 9 Agreement on Trade in Services between the Government of the People’s Republic of China and the Government of the Islamic Republic of Pakistan (signed on 21 February 2009 and entered into force in October 2009).
- 10 See eg Wang (n 3) 118; Hamid Mahmood and Muhammad Sabir, *Trade Facilitation and Connectivity: Perspective from China-Pakistan Economic Corridor and Free Trade Agreement (FTA)*, Working Paper: Forum for Research in Empirical International Trade (27 September 2014).
- 11 Pakistan Business Council, *Preliminary Study on Pakistan and China Trade Partnership Post FTA*, Trade Study (2013) <[http://www.pbc.org.pk/assets/pdf/21-Oct\\_Pakistan\\_China\\_Trade\\_Study\\_2013.pdf](http://www.pbc.org.pk/assets/pdf/21-Oct_Pakistan_China_Trade_Study_2013.pdf)> accessed 29 September 2015. However, this outcome of China–Pakistan FTA (n 8) is not exceptional as

billion in 2007 to US \$16 billion in 2014 with an annual growth of about 15.3 per cent,<sup>12</sup> Chinese imports from Pakistan are far less than its exports to Pakistan.<sup>13</sup> Negotiations on the second stage of implementation of the China–Pakistan FTA are currently in progress.<sup>14</sup>

In July 2013, during Prime Minister Sharif's first official visit to China, the two countries signed a memorandum of understanding on the China–Pakistan Economic Corridor (CPEC). The CPEC is part of President Xi's Chinese Silk Road Economic Belt (SREB) initiative with the eventual aim to enhance the connectivity of Pakistan and China with all regional countries in Asia and Central Asia. The CPEC further strengthens the two countries' friendship and aims at a major overhaul of infrastructure including rail, roads, pipelines, ports, and fibre optic networks in a bid to ease the energy crisis and increase Chinese investments in Pakistan.<sup>15</sup> During Prime Minister Sharif's visit to Beijing in November 2014, Chinese companies and banks pledged US \$45.6 billion in energy and infrastructure projects related to the CPEC.<sup>16</sup>

The most important feature of the CPEC plan is that the pledged money will not be a loan to Pakistan but, rather, pure investment through Chinese companies that will operate the projects as profit-making entities.<sup>17</sup> The Chinese government and state-owned commercial banks will instead loan funds to Chinese companies that will invest in infrastructure projects in Pakistan as commercial ventures.<sup>18</sup> The Silk Road Fund Company Limited (SRFCL), a fund management company including the China Exim Bank and the China Development Bank, was established in China in December 2014 to extend investment and financing support to CPEC projects. The SRFCL had initial funds of US \$10 billion, which have now been raised to US \$40 billion. According to Reuters, there will be around US \$33.8 billion investments in various energy projects and US \$11.8 billion in infrastructure projects.<sup>19</sup>

This is a huge commitment by the Chinese government, which provides a promising opportunity for Pakistan to resolve its chronic energy shortage and develop its failing infrastructure. There is no doubt that Chinese investments will accelerate Pakistan's growth.<sup>20</sup> In addition to serving China's strategic and energy security

the same has also been the case with other FTAs. See Kazim Alam, 'Pakistan's FTAs Have Borne No Fruit So Far' *Express Tribune* (10 August 2015).

12 Chinese Ministry of Commerce (MOFCOM), *Fourth Meeting of the Negotiations in the Second Stage of China-Pakistan Free Trade Area Held in Beijing*, Press Release (8 April 2015).

13 Pakistan Business Council (n 11).

14 MOFCOM (n 12).

15 See eg *Finance Minister Ishaq Dar's Keynote Address on Future of Pakistan Economy at Investment Conference Islamabad* (28 October 2014) <[http://www.pakistanmission-un.org/investment\\_conference.pdf](http://www.pakistanmission-un.org/investment_conference.pdf)> accessed 29 September 2015; Aarish U Khan, 'Pak-China Economic Corridor: The Hopes and Reality' *Spotlight: Institute of Regional Studies* (January 2015).

16 See eg 'China Commits \$45.6 Billion for Economic Corridor with Pakistan' *Reuters* (21 November 2014).

17 See eg 'China Coming up with Investment, Not Loans: Asif (Khawaja Mohammad): Federal Minister for Water and Power' *Express Tribune* (10 September 2014).

18 Ibid.

19 'China Commits \$45.6 Billion' (n 16).

20 See eg Shahid Yusuf, *Can Chinese FDI Accelerate Pakistan's Growth?* Growth Dialogue, George Washington University Working Paper (February 2013).

interests, these investments will benefit China in competing for the more profitable parts of the supply chains where Chinese companies will ultimately have to find new avenues for some of the low value-adding processing activities.<sup>21</sup> These new and existing investments require an efficient legal framework. The two countries concluded a bilateral investment treaty (BIT) in 1989.<sup>22</sup> The China–Pakistan BIT is still in force, although the more recent China–Pakistan FTA has a comprehensive chapter on investment.<sup>23</sup> The existing bilateral legal framework for Chinese investments in Pakistan is, therefore, composed of both of these treaties.

The key question is this: how should we map out the China–Pakistan investment relations historically as well as in the context of recent SREB and CPEC developments? The Indian perspective on the China–Pakistan relationship, in which India has openly opposed the CPEC considering it to be a strategic defence alliance targeted against India,<sup>24</sup> the existing menace of terrorism and its headways to Xinjiang–Uyghur separatism, and, more generally, concerns over the rise of Chinese economic and political power from some corners of the globe have had much to say about the investment relations between China and Pakistan. President Xi’s SREB initiative is truly remarkable in this broader context, and it is likely to bring positive social and economic change in the entire region. The SREB has created a new wave of Chinese investments in the entire region, and it will likely counter the existing problems, among others, of terrorism and separatism through economic development.

In the context of the CPEC and the renewed Chinese commitment to boost investments in Pakistan, this article primarily analyses the legal regime, both national and bilateral, of Chinese investments in Pakistan. The first part gives a detailed analysis of the Chinese CPEC initiative in the broader SREB context. This analysis is broadly framed on the legal and policy orientations of the SREB as compared to the existing regional integration models and global development strategies. This part also highlights some of the most important issues that require immediate attention by both China and Pakistan for successful implementation of the CPEC specifically as well as of the SREB generally. The second part of the article gives a detailed description of the existing domestic legal regime in Pakistan for investment promotion and protection and its implications for Chinese investors and investments. The third part analyses and compares the provisions of the FTA and the BIT that the two countries have concluded. The objective is to inform the existing and future Chinese investors in Pakistan of their legal rights, potential risks, and available remedies in case of loss or harm to their investments caused by their host. The fourth part concludes the analysis confirming that although the SREB and the CPEC create great economic development opportunities in the region and reflect a move towards

21 Ibid.

22 Agreement between the Government of the People’s Republic of China and the Government of the Islamic Republic of Pakistan on the Reciprocal Encouragement and Protection of Investment (signed on 12 February 1989, entered into force on 3 September 1990) (China–Pakistan BIT).

23 China–Pakistan FTA (n 8) ch IX.

24 The Indian External Affairs Minister Sushma Swaraj’s statement that Indian prime minister has strongly opposed China–Pakistan Economic Corridor (CPEC) project during his meeting with President Xi is reported by all major media outlets in Pakistan. See eg ‘CPEC “unacceptable” to India, Modi Tells China’ *Geo News* (2 June 2015). See also Zafar Zulqurnain Sahi, ‘India’s Unhealthy Obsession with China–Pakistan Economic Corridor’ *Express Tribune* (2 June 2015).

much deeper economic integration, various legal and policy orientations of these projects reveal serious challenges to vindicate the overall vision, harnessing the vision with intended objectives, and enhancing the legitimacy of its implementation strategies. There is a need for proactive solutions for the transnational problems that the CPEC and the SREB are going to generate.

## AN OVERVIEW OF THE SREB INITIATIVE: THE DAWN OF A NEW ERA OF REGIONAL ECONOMIC INTEGRATION?

Chinese strategists have been advocating that China should reach out to the west through Central Asia and to the greater Middle East through Pakistan.<sup>25</sup> President Xi seized the idea and announced the SREB initiative in various statements, starting with his speech in Kazakhstan in September 2013.<sup>26</sup> In a later speech at the Indonesian Parliament in October 2013, he introduced the idea of the twenty-first century Maritime Silk Road to promote maritime cooperation and also proposed the establishment of the Asian Infrastructure Investment Bank.<sup>27</sup> In November 2013, the Central Committee of the Communist Party of China set the facilitation and construction of the SREB and Maritime Silk Road as a primary milestone in pursuit of its regional economic policy to accelerate the interconnection of infrastructure among neighbouring countries.<sup>28</sup> In March 2014, Premier Li stressed the need to accelerate the construction of the 'Belt and Road' in the government's work report.<sup>29</sup> The report also promoted balanced development of the Bangladesh–China–India–Myanmar Economic Corridor and the China–Pakistan Economic Corridor.<sup>30</sup>

After authorization by the State Council in March 2015, the first more coherent and comprehensive vision and roadmap of the SREB has now emerged as an 'Action Plan' issued by the National Development and Reform Commission in the Ministry of Foreign Affairs and Ministry of Commerce of the People's Republic of China.<sup>31</sup> The Action Plan explains that the SREB 'aims to promote the connectivity of Asian, European and African continents and their adjacent seas, establish and strengthen partnerships among the countries along the Belt and Road, set up all-dimensional, multi-tiered and composite connectivity networks, and realize diversified,

25 See eg Wang Jisi, 'Marching Westwards': The Rebalancing of China's Geostrategy', *International and Strategic Studies Report, Center for International and Strategic Studies*, No. 73 (7 October 2012). For some analysis of Wang Jisi, see Andrew C Kuchins, 'Why Washington Needs to Integrate the New Silk Road with the Pivot to Asia' (2013) 16 *Asia Policy* <first page?>.

26 See eg 'Chronology of China's "Belt and Road" Initiatives' *Xinhua* (5 February 2015).

27 Ibid. In January 2014, 21 Asian countries willing to join the Asian Infrastructure Investment Bank (AIIB) as founding members signed the Memorandum of Understanding on Establishing AIIB. As of 13 April 2015, there are 47 Prospective Founding Members (PFM) and 10 countries have applied for PFM. Hong Kong joins the delegation of China in the negotiations. Belgium, Canada, and Ukraine are considering joining the AIIB. Colombia, Japan, and the USA have no immediate intention to participate. North Korea and Taiwan were rejected by China to join as a PFM. See <[http://aiibank.org/yatouhang\\_02.html](http://aiibank.org/yatouhang_02.html)> accessed 29 September 2015.

28 'Chronology of China's "Belt and Road" Initiatives' (n 26).

29 Li Keqiang, *Report on the Work of the Government, Delivered at the Second Session of the Twelfth National Peoples Congress* (5 March 2014) 17.

30 Ibid.

31 'Vision and Actions on Jointly Building Belt and Road' *Xinhua* (29 March 2015) <<http://www.globaltimes.cn/content/914373.shtml>> accessed 29 September 2015.

independent, balanced and sustainable development in these countries'.<sup>32</sup> The territorial reach of the SREB is explained as 'bringing together China, Central Asia, Russia and Europe (the Baltic); linking China with the Persian Gulf and the Mediterranean Sea through Central Asia and West Asia; and connecting China with Southeast Asia, South Asia and the Indian Ocean'.<sup>33</sup> The Maritime Silk Road 'is designed to go from China's coast to Europe through the South China Sea and the Indian Ocean in one route, and from China's coast through the South China Sea to the South Pacific in the other'.<sup>34</sup>

The detailed vision set out in the Action Plan is truly remarkable and unprecedented and will effectively transform the entire region both economically and socially. The Chinese government has strived to bolster the legitimacy of this vision in accordance with international law. The Action Plan insists that the SREB initiative is in line with the purposes and principles of the UN Charter as it upholds the five fundamental principles of international engagement, namely, respect for sovereignty and territorial integrity, non-aggression, non-interference in internal affairs, equality and mutual benefit, and peaceful coexistence.<sup>35</sup> The Action Plan explains that the SREB's legal and functional *modus operandi* is based on the 'market operation'. The SREB 'will abide by market rules and international norms, give play to the decisive role of the market in resource allocation and the primary role of enterprises, and let the governments perform their due functions'.<sup>36</sup>

There are two likely benefits of this *modus operandi*. First, the market-based approach is well suited for this sort of consortium where participating States have many differences in their government systems, social structures, and legal ideologies.<sup>37</sup> This approach is different from, for example, the European approach for membership and further expansion of the European Union (EU).<sup>38</sup> The EU's approach is based on imposing political and social conditions for States willing to join the EU.<sup>39</sup> Although the 'European values' required from its prospective members are highly desirable for any State or society,<sup>40</sup> States in the SREB area do not necessarily share the same political philosophy and are at different levels of their value internalization processes.<sup>41</sup> Second, the 'trade not aid' approach is definitely a

32 Ibid.

33 Ibid.

34 Ibid.

35 Ibid.

36 Ibid.

37 See eg Imtiaz Gul, 'Pakistan, China and the Economic Corridor' *Express Tribune* (18 March 2015).

38 The Treaty on the European Union [2012] OJ C326, art 49 (TEU), read with art 2, provides that any European country may apply for membership if it respects the democratic values of the EU and is committed to promoting them.

39 Ibid.

40 TEU (n 39) art 2 reads: 'The Union is founded on the values of respect for human dignity, freedom, democracy, equality, the rule of law and respect for human rights, including the rights of persons belonging to minorities. These values are common to the Member States in a society in which pluralism, non-discrimination, tolerance, justice, solidarity and equality between women and men prevail.'

41 Here I would like to direct the reader to my earlier work where, in the context of 'Asian values', I have argued that countries that have likely followed the same path for value internalisation process may still stand at different levels of economic and social development. Therefore, it is difficult to determine minimum value standards for the developing countries. See Ahmad Ghouri, 'Determining Hierarchy between

more reliable long-term goal for regional development.<sup>42</sup> The US approach of development assistance, for example,<sup>43</sup> has not worked to a satisfactory extent.<sup>44</sup> The US aid program has mainly addressed the strategic needs set by the US policy makers for a given time and has not focused on long-term development goals.<sup>45</sup> Over the past several decades, Pakistan has received billions of dollars in development assistance from the USA, but this has failed to achieve any substantial and long-term economic goals.<sup>46</sup>

The Chinese vision of making long-term and commercially viable investments through commercial enterprises, instead of advancing loans and aids, will benefit both China and recipient countries. Instead of giving loans and aids to foreign governments, which are susceptible to corruption and inefficiency,<sup>47</sup> China will loan funds to its own companies to carry out the development goals set out in collaboration with the SREB partner countries. This will increase the global competitiveness of Chinese companies, stimulate growth in the SREB area, and create wealth.<sup>48</sup> As the Action Plan suggests, this action will ‘promote mutually beneficial cooperation to a new high and in new forms’,<sup>49</sup> which will surely reflect ‘new models of international cooperation and global governance’ to achieve the common ideals through economic and social development and inject new positive energy into world peace and development.<sup>50</sup>

Chinese commentators have listed various reasons for their insistence on the revival of the SREB area. Shuchun Wang and Qingsong Wan, for example, have

Conflicting Treaties: Are There Vertical Rules in the Horizontal System?’ (2012) 2(2) *Asian J Intl Law* 235.

42 See eg Tim Worstall, ‘Trade, Not Aid, Is What Improves Life in the Third World’ *The Telegraph* (22 May 2012); Mustapha Nabli, ‘Trade Not Aid Is the Key to Development’ *Daily Star* (10 November 2005); Yoweri K Museveni, ‘We Want Trade, Not Aid’ *Wall Street Journal* (6 November 2003). For classical views on ‘trade not aid’, see Covey T Oliver, ‘Trade Not Aid: Myth or Reality’ (1971) 8(3) *Houston L Rev* 458; AP Thirlwall, ‘When Is Trade More Valuable Than Aid?’ (1976) 13(1) *J Development Studies* 35. For a possible spill-over effect of the Chinese ‘trade not aid’ strategy, see Philip Hsiaopong Liu, ‘How China’s “Trade Not Aid” Strategy Became Construed As Charitable Help: Deconstructing the “Touching” Idyll of Li Li’s Investment in Africa’ (2011) 12(2) *J Identity, Culture, and Politics: An Afro-Asian Dialogue* 1.

43 For an overview of the US Aid program, see Curt Tarnoff and Marian Leonardo Lawson, *Foreign Aid: An Introduction to U.S. Programs and Policy*, CRS Report for Congress (20 April 2012).

44 See eg Gorik Ooms, ‘Stop Development Assistance, Globalize Social Protection’ (2010) 5(1) *Yale J Intl Affairs* 150.

45 Eg, the top recipients of US aid in 2012 were Israel, Afghanistan, Pakistan, Iraq, and Egypt. Tarnoff and Lawson (n 44) have noted that these countries of choice reflect ‘long-standing aid commitments to Israel and Egypt and the strategic significance of Afghanistan, Pakistan, and Iraq’. These countries are definitely not the poorest in the world deserving the highest attention and levels of aid from the USA stretching beyond its neighbourhood where countries such as Bolivia, Colombia, and Venezuela are touching upon the highest levels of poverty in the world.

46 S Akbar Zaidi, *Who Benefits from U.S. Aid to Pakistan?* Carnegie Endowment for International Peace—Policy Outlook (21 September 2011).

47 See eg Alberto Alesina and Beatrice Weder, ‘Do Corrupt Governments Receive Less Foreign Aid?’ (2002) 92(4) *Am Econ Rev* 1126; Mike Patton, ‘Foreign Aid: Money Down A Rat Hole?’ *Forbes* (28 January 2013); Martyn Brown, ‘Fury As Foreign Aid Goes to Top 10 Most Corrupt Nations’ *Express* (24 April 2015).

48 See eg Yusuf (n 21) 6–7.

49 ‘Vision and Actions on Jointly Building Belt and Road’ (n 32).

50 *Ibid.*

explained a mix of economic and political reasons for the SREB project.<sup>51</sup> They view the SREB as the Chinese response to the 2008 economic crisis in which China is hoping to develop regional economic cooperation with all of its neighbouring countries in order to re-ignite economic growth.<sup>52</sup> Unfortunately, however, the trade and investment debate surrounding the SREB coincides with growing global power politics and regional security challenges.<sup>53</sup> The SREB initiative is already viewed as a blueprint for China's strategy to become a comprehensive global power.<sup>54</sup> The growing Chinese power has incited researchers to draw parallels between Chinese and US political and economic interests.<sup>55</sup>

The regional security issues arising from the situation in the South China Sea have been viewed as a pretext for the USA to use the situation to its own advantage by persuading its allies and partners in the region to form a Trans-Pacific Partnership (TPP).<sup>56</sup> The Chinese SREB initiative is commonly perceived as a response to the TPP, which will open new trade routes, reducing China's dependence on the South China Sea.<sup>57</sup> Although there is a serious view that China and the USA are competing for strategic advantage in the region,<sup>58</sup> there is a more convincing broader prospect on the 'common narrative' between the two.<sup>59</sup> Kevin Rudd, a former two-time prime minister of Australia, led a study on the possibilities and impacts of a new China–US strategic relationship and concluded that, although the two countries have recently diverged on many aspects of their foreign policy, a common strategic framework for China–US relations would offer many advantages.<sup>60</sup> The promotion of a China–US

51 Shuchun Wang and Qingsong Wan, 'The Silk Road Economic Belt and The EEU: Rivals or Partners?' (2014) 15 (3) *Central Asia and the Caucasus Journal of Social and Political Studies* <[http://www.ca-c.org/online/2014/journal\\_eng/cac-03/01.shtml](http://www.ca-c.org/online/2014/journal_eng/cac-03/01.shtml)> accessed 29 September 2015.

52 Ibid.

53 In his 2015 State of the Union address, President Obama stated: 'But as we speak, China wants to write the rules for the world's fastest-growing region. That would put our workers and our businesses at a disadvantage. Why would we let that happen? We should write those rules. We should level the playing field. That's why I'm asking both parties to give me trade promotion authority to protect American workers with strong new trade deals from Asia to Europe that aren't just free but are also fair. It's the right thing to do.' See eg Roger C Altman and Richard N Haass, 'Why the Trans-Pacific Partnership Matters' *New York Times* (3 April 2015).

54 See eg Xue Li and Xu Yanzhou, 'How China Can Perfect Its "Silk Road" Strategy: The Challenges Facing China's Silk Road Strategy—and How to Overcome Them' *The Diplomat* (9 April 2015).

55 See eg John P Tuman and Shirali Majid, 'The Political Economy of Chinese Foreign Direct Investment in Developing Areas' (2015) *Foreign Policy Analysis* <<http://onlinelibrary.wiley.com/doi/10.1111/fpa.12092/abstract>> accessed 29 September 2015.

56 The Trans-Pacific Partnership (TPP) is a US led regional trade and investment liberalization and regulatory treaty. As of 2014, 12 countries throughout the Asia-Pacific region have participated in negotiations on the TPP, namely Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam. Negotiations were originally meant to conclude in 2012, but contentious issues such as agriculture, intellectual property, services and investments caused significant roadblocks. October 5, 2015, the US Secretary of State John Kerry announced the conclusion of negotiation, however, the official text of the treaty is yet to be released.

57 Wang and Wan (n 53).

58 See eg Simon Denyer, 'China Promotes "Asia-Pacific Dream" to Counter U.S. Pivot' *Washington Post* (11 November 2014).

59 See eg Kevin Rudd, *The Future of U.S.-China Relations under Xi Jinping: Toward a New Framework of Constructive Realism for a Common Purpose*, Summary Report: US-China 21, Belfer Center for Science and International Affairs, Harvard Kennedy School (April 2015).

60 Ibid.



common strategic framework will give confidence to the SREB participating countries that currently feel they have been placed in a position where they need to pick sides with either China or the USA.

What the SREB means for Pakistan is considerably different from other participating countries not only strategically but also legally. Xue Li and Xu Yanzhou have identified four categories of the SREB area countries: (i) small- and medium-sized countries; (ii) countries that have territorial disputes with China; (iii) countries that are sub-regional powers; and (iv) countries that could potentially act as 'pivot States' (meaning they are reliable partners for China and reach a certain threshold of national power).<sup>61</sup> According to Li and Yanzhou, countries in this last group are the key to Chinese SREB strategy.<sup>62</sup> In my view, Pakistan is likely to be part of the group of pivot States, keeping in view the close defence and economic ties between the two countries. Traditionally, China–Pakistan relations have been viewed in the context of their shared history of rivalry with India.<sup>63</sup> The deep rooted defence and strategic ties between the two nations do not suggest otherwise, particularly given that India has previously tested its military muscles against both nations. This joint strategic defence aspect of China–Pakistan relations is repeatedly voiced by India. Recently, for example, India expressed concerns over Chinese investment to build Gwadar Port, which is located in Balochistan province of Pakistan, and form an integral part China's Maritime Silk Road,<sup>64</sup> suggesting that the Gwadar Port will be used by China for military purposes despite both China and Pakistan insisting that the project is purely commercial.<sup>65</sup> However, despite some existing scepticism, many commentators view Chinese trade and investment agreements with its neighbouring nations as primarily driven by geopolitical concerns, where such agreements are meant to demonstrate that the rise of China will be a peaceful one.<sup>66</sup>

There is more to say about the China–Pakistan relationship than the Indian context especially when China is gradually normalizing its relations with India and trying

61 Li and Yanzhou (n 56).

62 Li and Yanzhou have identified four categories of Silk Road Economic Belt (SREB) area countries: small- and medium-sized countries; countries that have territorial disputes with China; countries that are sub-regional powers; and countries that could potentially act as 'pivot states' (meaning they are reliable partners for China and reach a certain threshold of national power). According to Li and Yanzhou, countries in this last group are the key to Chinese SREB strategy. See Li and Yanzhou (n 56). In my view, Pakistan is likely to be part of the pivot states group keeping in view the close defence and economic ties between the two countries.

63 See eg Asifa Jahangir, *Pakistan-China Strategic Partnership: Challenges and Prospects: Changing Dynamics in Pak-China Bilateral Relations after 9/11* (Lap Lambert Academic Publishing 2013).

64 'Vision and Actions on Jointly Building Belt and Road' (n 32). On the Maritime Silk Road, see eg Ziangqian Gong, 'Building of the New Maritime Silk Road: Its Constraints and Prospects' (2014) 7(1) *Journal of East Asia & Intl L* 235.

65 See eg Ziad Haider, 'Baluchis, Beijing, and Pakistan's Gwadar Port' (2005) 6(1) *Georgetown J Intl Affairs* 95.

66 See eg Axel Berger, *Investment Rules in Chinese Preferential Trade and Investment Agreements: Is China Following the Global Trend towards Comprehensive Agreements?* Discussion Paper, German Development Institute (July 2013); Barry Buzan, 'China in International Society: Is "Peaceful Rise" Possible?' (2010) 3(1) *Chinese J Intl Politics* 5; Zheng Bijian, 'China's "Peaceful Rise" to Great-Power Status' *Foreign Affairs* (October 2005).

to form a more balanced policy regarding these two neighbours.<sup>67</sup> The evolving BRICS (Brazil, Russia, India, China and South Africa) consortium is an example where the five participating countries have concluded an agreement establishing the New Development Bank (NDB).<sup>68</sup> In 2003, China and India established a joint study group to examine the potential for economic engagement between the two countries. In October 2007, the joint task force finalized its report on the feasibility of a China–India Regional Trading Arrangement (RTA).<sup>69</sup> Compared to Pakistan, China’s trade and investment relationship with India has not grown as rapidly. The pace of the China–India RTA negotiations has been slow, although the two countries concluded a BIT in 2007,<sup>70</sup> which they agreed to apply retrospectively to cover investments made before and after its coming into force.<sup>71</sup> There is no doubt that shades of shared historical rivalry with India are present in the China–Pakistan relationship and that China has realized that its economic prospects are tied to both of these nations.<sup>72</sup> During his visit to India in September 2014, President Xi announced US \$20 billion of investments in India’s infrastructure over five years.<sup>73</sup> Nevertheless, the Indian context in the China–Pakistan relationship gives interesting insights, and some of the Indian concerns regarding the CPEC may also be legitimate. In order to successfully implement the SREB Action Plan, both China and Pakistan need to devise a collective strategy to address these concerns.

Pakistan still enjoys a special place in the SREB, as Chinese Foreign Minister Wang Yi observed: ‘If comparing this “One Belt and One Road” initiative to a symphony that is participated by all countries and produces benefits to all participants, then China-Pakistan Economic Corridor is the glorious melody in the chapter one of this symphony’.<sup>74</sup> Ejaz Hussain, Zhang Yuan, and Ghulam Ali have observed that the CPEC is not only a land or rail connectivity passage between the two countries, but it is indeed a comprehensive concept that encompasses economic and strategic integration between the two countries in the long run.<sup>75</sup> In spite of the economic and geopolitical importance of the CPEC for the two nations, and for the overall success of the SREB, a number of issues surround this project. Aarish Khan, for example, has highlighted that the security situation in Pakistan, political unrest, administrative

67 Eg, China has gradually distanced itself from the ongoing Kashmir issue saying that it is a bilateral dispute between Pakistan and India requiring a bilateral solution. For an overview of China’s changing positions on the Kashmir issue, see John W Garver, ‘China’s Kashmir Policies’ (2004) 3(1) *India Review* 1. See also Sheikh M Arif, ‘A History of Sino-Indian Relations: From Conflict to Cooperation’ (2013) 1(4) *Intl J Political Science & Development* 129.

68 See ‘Sixth Brics Summit: Fortaleza Declaration, 15 July 2014’ (2014) 20(3) *Law & Business Rev of the Americas* 483.

69 See MOFCOM, China FTA Network, *China–India Regional Trade Arrangement Joint Feasibility Study* (2007).

70 Agreement between the Government of the Republic of India and the Government of the People’s Republic of China for the Promotion and Protection of Investments, done on 21 November 2006, entered into force 1 August 2007 (China–India BIT).

71 China–India BIT (n 72) art 2 ‘Scope of the Agreement’.

72 See eg Andrew Small, *The China-Pakistan Axis: Asia’s New Geopolitics* (Oxford University Press 2015).

73 See eg Harsh V Pant, ‘Why Xi Jinping’s Visit to India Is Significant’ *BBC* (16 September 2014).

74 ‘Chinese FM: China-Pakistan Brotherhood Will Never Go Rusty’ *Xinhua* (13 February 2015).

75 Ejaz Hussain, Zhang Yuan and Dr Ghulam Ali, ‘China-Pakistan Economic Corridor’ *Daily Times* (4 April 2015).

issues, and the skill level of the Pakistani workforce are going to pose major challenges for implementation of the CPEC.<sup>76</sup> However, on a broader legal and policy level, the following challenges will face the CPEC and the SREB projects in the coming years.

### Transparency

Given the overwhelming importance of the CPEC for the people of both countries, both governments have been repeatedly blamed for a lack of transparency in their dealings. The CPEC includes US \$5.9 billion for road projects and US \$3.7 billion for railway projects, along with a multi-billion dollars worth of coal, wind, solar and hydro energy projects, but both governments have been reluctant to disclose the maps for the roads and the railways to be built.<sup>77</sup> There is a degree of dissatisfaction in Pakistan over the Sharif government's handling of the controversy related to the original route and the changes made by the government to favour personal or political interests instead of real development and public interests.<sup>78</sup> Husain, for example, has lamented that the existing secrecy over the CPEC has turned it into a labyrinth.<sup>79</sup> Transparency will bring legitimacy for the CPEC, which includes not only roads but also a variety of social infrastructure in Balochistan and other areas aligned with the corridor.<sup>80</sup> Commentators from Pakistan have noted that transparency would ensure that the conversation between China and Pakistan remains focused on the country's national interests, as opposed to the parochial interests of a few.<sup>81</sup> Likewise, Irene Chan has criticized China for not having effectively opened its grand connectivity ideas for public discussion in the SREB countries in order to generate feedback and devise better understanding of the regional needs.<sup>82</sup> The continuous lack of transparency and open public discussion is likely to increase the public's existing mistrust in the projects.

### Fair distribution of benefits

The China–Pakistan economic exchange should be transformed by distributive justice so that the poor remain the priority.<sup>83</sup> The fair distribution of the benefits within society of the returns of improved trade and foreign investment are by no means automatically assured.<sup>84</sup> For example, studies from Latin American countries have shown that increased trade has not resulted in 'total development' of their societies, which is the only kind that really counts and includes social and civic development, modern innovation and improvement, as well as purely economic growth.<sup>85</sup>

76 Kahn (n 16) 16.

77 Khurram Husain, 'Analysis: China-Pakistan Corridor or Labyrinth?' *The Dawn News* (18 February 2015).

78 See eg Khawar Ghumman, 'Economists Call for More Transparency on Corridor Projects' *Dawn News* (20 April 2015).

79 Husain (n 79).

80 See eg Gul (n 38).

81 See eg 'Corridor Furore' *Dawn News* (Editorial) (5 February 2015).

82 Irene Chan, 'China's Maritime Silk Road: The Politics of Routes' *RSIS Commentary*, No 051 (12 March 2015).

83 Hussain, Yuan and Ali (n 77).

84 Oliver (n 43) 461.

85 *Ibid.*

Although a regional market is a great initiative, the primary basis for development rests in an increased exchange of goods and services within the economy itself.<sup>86</sup> Senge Sering, for example, has observed that despite the existence of PTAs, FTAs, and Early Harvest Programmes, local populations along the existing China–Pakistan road links, such as the Karakoram Corridor, have failed to derive the expected benefits.<sup>87</sup> The SREB Action Plan is based on ‘market operation’, and it assigns primary role to enterprises.<sup>88</sup> In regard to governance, the Action Plan merely states: ‘Let the governments perform their due functions’.<sup>89</sup> Although the Action Plan states that the SREB is a ‘systematic project’ and aims to ‘integrate the development strategies’ of the SREB area countries, the absence of a detailed vision on total development in the mainstream SREB agenda is worrying. If the rules of development are not aimed at achieving total development, the legitimacy of the system will be cast in doubt.

### **Implementation of labour standards**

The rubrics of the CPEC are gradually emerging although there is no concise policy statement or detailed action plan announced by either government. For example, a statement on the official website of Pakistan Ministry of Planning, Development and Reform reads: ‘CPEC will integrate all provincial capitals into the economic mesh which would help in consolidation at national level and it will also contribute to regional integration, harmony and economic development’.<sup>90</sup> The Pakistan Board of Investment has released a document on President Xi’s visit, which sheds some light on the government’s vision as to how the CPEC will help local populations.<sup>91</sup> The basic idea appears to be that special economic zones (SEZs) will be established alongside the CPEC, which will create jobs and contribute to the socio-economic development in the SEZs areas.<sup>92</sup> The Special Economic Zones Act 2012 (SEZs Act) was promulgated to facilitate the development of industrial infrastructure in Pakistan through public-private partnership and also by private developers alone.<sup>93</sup> This law provides many business incentives, including allowing for the duty-free import of machinery and equipment for developers and enterprises established in SEZs.<sup>94</sup>

Some SEZs already exist in Pakistan,<sup>95</sup> and the overall SEZs policy looks positive. A study spanning 30 years of global SEZs practice has revealed the positive impacts of SEZs on a country’s economy, but it has criticized the poor working conditions, exploitation of women workers, and poor implementation of environmental

86 Ibid.

87 Senge H Sering, *Expansion of the Karakoram Corridor: Implications and Prospects*, IDSA Occasional Paper No 27 (September 2012) 20.

88 ‘Vision and Actions on Jointly Building Belt and Road’ (n 32).

89 Ibid.

90 See CPEC <<http://www.pc.gov.pk>> accessed 29 September 2015.

91 The undated document of 56 pages is entitled ‘Pak–China Economic Corridor’ (on file with the author).

92 Ibid.

93 Special Economic Zones Act (No XX) of 2012 (SEZs Act).

94 Ibid ss 34–7.

95 Eg, in Khairpur, Korangi Creek, and Bin Qasim.

standards in the SEZs.<sup>96</sup> The SEZs Act provides for the application of all existing labour laws to the SEZs;<sup>97</sup> however, no special provisions have been made for the enforcement of those laws in the SEZs specifically. In view of the existing poor implementation records generally, the SEZs Act could have suggested a special monitoring and enforcement mechanism of labour standards in SEZs. The SEZs law appears to have created everything special for the business community—from special land registration to tax regimes—silence on the labour and environment standards is disquieting and harmful for the overall legitimacy of the CPEC.

### New models of global governance

According to the Action Plan, the SREB is an endeavour to ‘seek new models of international cooperation and global governance’, which is intended to ‘inject new positive energy into world peace and development’.<sup>98</sup> Before the SREB initiative, China had mainly used bilateral arrangements to invest in other countries. These investments have so far been mainly executed by State-owned corporations, which, according to Javier Solana, do not often adhere to international best practices.<sup>99</sup> The emphasis on new models of global governance in the SREB Action Plan clearly indicates that China is now moving towards replacing bilateral arrangements with multi-lateral processes. Although China must have a greater role in global governance commensurate to its economic success, it must also ensure that its corporations meet international standards of corporate governance and social responsibility.

There is no compelling evidence of wrongdoing by Chinese companies abroad; however, absence of corporate governance and social responsibility agendas in the actions plan will attract criticism. For example, Andrew Kuchins has contended that since Chinese companies are unconstrained by legislation such as the US Foreign Corrupt Practices Act of 1977 or shareholder reporting, they ‘will continue to line the pockets of local, regional, and national officials in Central Asia to strengthen their access to the region’s mineral and hydrocarbon resources and will build more transit infrastructure to ship these goods to the Chinese market’.<sup>100</sup> Although President Xi’s crackdown on corruption and his recent ‘four comprehensives’ send strong signals to the world that he seriously means to solve the menace of corruption at home,<sup>101</sup> there is more to be done to ensure best practices by Chinese companies abroad in order to both develop goodwill and prevent future malpractices.

This is particularly important when dealing with countries such as Pakistan, which ranks among the most corrupt countries in the world.<sup>102</sup> Since most of the Chinese business with Pakistan is based on the ‘trade-not-aid’ model and the Pakistani

96 See World Bank Group, *Special Economic Zones: Performance, Lessons Learned, and Implications for Zone Development* (April 2008).

97 SEZs Act (n 95) s 30.

98 ‘Vision and Actions on Jointly Building Belt and Road’ (n 32).

99 Javier Solana, ‘China and Global Governance’ *Project Syndicate* (30 March 2015).

100 Kuchins (n 26).

101 See eg Zheng Yongnian, ‘China Needs a Strong Leader Like Xi—but the Rule of Law Like Singapore’ *World Post* (19 April 2015).

102 See eg Ram Mashru, ‘Pakistan: As Corrupt As Ever? Pakistan’s Corruption Problem Remains Serious and a Major Impediment to Good Governance’ *The Diplomat* (8 January 2014).

government will not have direct access to the funds, which is usually the case with foreign aid,<sup>103</sup> Chinese legislation targeting foreign corrupt practices of both individuals and companies will be a welcome step. It is encouraging that the SREB Action Plan requires Chinese companies to take social responsibility in protecting local biodiversity and eco-environment, since there is a lot more that can be done to enhance the legitimacy of the SREB initiative. Domestic legislation in China to mitigate the problems of a transnational nature, such as laws remedying foreign torts, including environmental, labour, and human rights protection clauses in the new free trade and investment agreements, should also be considered to ensure the rule of law in Chinese business abroad.

### Legal transformation

China is using a huge cache of its foreign exchange reserves to fund investments abroad, which will strategically disperse its industries in line with its changing domestic comparative advantage and enable it to acquire overseas assets.<sup>104</sup> In response, countries such as Pakistan are depending heavily on Chinese investments for growth and development.<sup>105</sup> However, there is an increasing worry of over-domination by China in its neighbouring economies in the pretext of investments. For example, Kuchins has noted that increasing Chinese domination of the Mongolian economy has stirred the Parliament in Ulaanbaatar to pass legislation requiring prior legislative approval of foreign investments over US \$70 million.<sup>106</sup> In contrast, when more countries strive to make their investment environment more attractive to a wider set of bidders, the government of Pakistan has facilitated this action by handing over development projects to Chinese companies and bypassing the international competitive bidding process.<sup>107</sup> Although China–Pakistan relations are based on long-standing mutual trust, both China and Pakistan should ensure that large-scale Chinese investments in Pakistan are aimed at improving governance, ensuring transparent and effective rule of law, and strengthening property rights. If this is not done, China’s economic presence is likely to be viewed as a dominating device in the longer run, which may push the SREB partners away. If Chinese foreign investments are not aligned with these objectives, reviving the network of regional transit corridors may not achieve its potential.

The Chinese government needs to pay careful attention to these concerns in order to forge the broader legitimacy of the SREB and the CPEC projects and to make them a realistic and efficient tool for sustainable development in the region. As is clear from the above discussions, these concerns may not be applicable to all

103 See eg Azeem Ibrahim, *U.S. Aid to Pakistan: U.S. Taxpayers Have Funded Pakistani Corruption*, Belfer Center Discussion Paper no 2009-06, International Security Program, Harvard Kennedy School (July 2009).

104 See eg Yusuf (n 21) 10.

105 See eg Khawar Ghumman, ‘PML-N Puts All Its MoUs in Chinese Basket’ *The Dawn News* (13 April 2015).

106 Kuchins (n 26).

107 See eg Khaleeq Kiani, ‘Chinese Firms to Get Contracts for Two CPEC Projects’ *Dawn News* (13 August 2015); Iftikhar Alam, ‘Rules Being Bypassed to Facilitate China Investment’ *The Nation* (26 August 2014).

SREB partners in the same way and may require a pragmatic approach depending upon the internal political and legal conditions in a SREB partner State. However, a clear and coherent statement of policy on these issues by the Chinese government is required to mitigate potential damage in the execution of the SREB Action Plan. Such policy will not only legitimize the overall SREB vision but will also harness the vision with intended objectives and will initiate a new era of regional development.

#### LEGAL FRAMEWORK FOR CHINESE INVESTMENTS IN PAKISTAN

China has recently made several changes in its outward investment policy, clearly indicating a shift towards the industrialized country approach of free movement of investment capital.<sup>108</sup> This shift is illustrated by the actions undertaken by the relevant bodies to implement the government's 'go-global' policy.<sup>109</sup> For example, the State Administration of Foreign Exchange (SAFE) lifted restrictions on the amount of foreign exchange that is available annually to domestic investors' outbound investments and announced in 2009 that Chinese firms can seek financing from multiple sources. The Ministry of Commerce simplified and shortened the approval procedures in 2009, and the National Development Reform Commission reiterated in 2011 its desire to decentralize the outward investment approval decision process.<sup>110</sup> In addition to increasing the Chinese companies' share in the global marketplace, these regulatory changes will facilitate the implementation of the CPEC and other SREB projects.

Over three hundred Chinese companies are actively doing business in Pakistan, and the existing volume of Chinese investments in Pakistan is about US \$1 billion.<sup>111</sup> Chinese investments in Pakistan have flowed in multiple sectors and have taken several forms. Chinese private companies, for example, have entered Pakistan through the compulsory licensing regime put in place in Pakistan for a particular sector (for example, in the telecom sector, China Mobile Pakistan, or Zong) and through joint ventures with local business partners for consumer products business (for example, joint venture of the Haier Group and the Ruba Group, Hair Pakistan). The investments of Chinese State-owned companies in Pakistan have ranged from joint defence productions (for example, joint production of military jets),<sup>112</sup> to mining and infrastructure development.<sup>113</sup> Most of the infrastructure development projects

108 See eg Peter J Buckley, *Foreign Direct Investment, China and the World Economy* (Palgrave Macmillan 2009). For the evolution of different patterns of Chinese outward investments, see Nargiza Salidjanova, 'Going Out: An Overview of China's Outward Foreign Direct Investment' USCC Staff Research Report (30 March 2011) 4–5.

109 See eg Duncan Freeman, *China's Outward Investment: Institutions, Constraints and Challenges*, BICCS Asia Paper no 7(4) (12 May 2013).

110 Ibid.

111 See eg Danial Khan, 'Working Together to Strengthen China-Pakistan Relations' <<http://www.cctv.com>> accessed 29 September 2015.

112 See eg Syed Fazl-e-Haider, 'Pakistan and China Prove Powerful Combination in Aviation' *The National* (25 November 2013).

113 See eg Kataria and Naveed (n 3) 404–8. For an overview of outward investments by Chinese State-owned companies, see Freemann (n 112).

are conducted through build, operate, and transfer (BOT) arrangements.<sup>114</sup> There is no existing research showing different levels of Chinese investment in Pakistan dividing the volumes of investment between private companies and Chinese State-owned companies. The trend is mixed, but clearly a majority of Chinese investments in Pakistan are made by State-owned companies.

The volume of Chinese investments in Pakistan is going to increase tremendously following the implementation of the CPEC. The stakes are high, with multiple legal and policy implications for these investments concerning both countries. Although investments in Pakistan made by some Chinese State-owned companies may have strategic ambitions, these investments will be financed by the Chinese State-owned banks and are expected to make profits just like other commercial enterprises.<sup>115</sup> According to Li and Yanzhou, an unprofitable investment made by a Chinese State-owned company, which turns into a bad debt, is a serious violation of the Chinese principles of foreign exchange reserves management.<sup>116</sup> The longer-term commitments usually required in the BOT arrangements for infrastructure and energy-related projects are always susceptible to an array of challenges, and a pre-defined and concrete legal framework is necessary to cushion against political and policy turmoil. Although Pakistan's friendship with China has been perhaps the only consistent element in the country's foreign policy throughout its history, a solid domestic regime on foreign investment governance is imperative to satisfy both the legitimacy (that is, through proper implementation of domestic validating rules and procedures) and success (that is, through the proper definition and allocation of rights and responsibilities) of foreign investments.

Additionally, the two countries have special arrangements to facilitate the flow of investments. A company named the Pakistan–China Investment Company Limited (PCICL) was established as a development finance institution (DFI) for the promotion of trade, investment, and economic growth of Pakistan.<sup>117</sup> The PCICL was incorporated in Pakistan as a non-banking finance company (NBFC),<sup>118</sup> with an authorized capital of US \$200 million and was formally launched in December 2007. The company is a joint venture with equal equity contribution by the Government of Pakistan (GOP) and the China Development Bank (CDB), which is a Chinese State-owned bank. The main objective of the PCICL is to invest in the financial sector and infrastructure projects.<sup>119</sup> According to the information provided on its official website, the PCICL aims to become a hub for investment activity and add value to sectors such as industry, agriculture, services, information and technology, manufacturing, real estate, and infrastructure. The PCICL also aims to offer conventional and innovative solutions to investors and projects through a full range of investment

114 See eg Syed Irfan Raza, 'Bids Invited for Pak-China Economic Corridor Project' *Dawn News* (24 December 2014). For detailed analysis of the government administrative procedures for build, operate, and transfer (BOT) contracts in Pakistan, see S Mubin and A Ghaffar, 'BOT Contracts: Applicability in Pakistan for Infrastructure Development' (2008) 3 *Pakistan J Engineering & Applied Sciences* 33.

115 Salidjanova (n 111) 6.

116 Li and Yanzhou (n 56).

117 See <<https://www.pakchinatest.com/>> accessed 29 September 2015.

118 See Companies Ordinance (No XLVII) of 1984, ss 282 A and 282 B; Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003.

119 Pakistan–China Investment Company Limited (PCICL), *Financial Statement* (2013) 6.



banking services. The CPEC-related projects that are based on joint ventures between Chinese and Pakistani companies can be conveniently financed through the PCICL.<sup>120</sup>

In view of its particular character and mandate, the PCICL will operate as a special vehicle—that is, a DFI—to transport Chinese investments in Pakistan. However, there are potential legal uncertainties with regard to the joint venture DFIs. The international practice is that DFIs are based in the country where the investments are coming from rather than in the country where the investments are being made and are tied to the interest of home country firms.<sup>121</sup> The joint venture structure of the PCICL is entirely different, both legally and operationally, from the investors' home country-based DFIs.<sup>122</sup> Perhaps the idea behind joint venture DFIs is to make them more bilateral rather than home country driven. A few other bilateral DFIs exist in Pakistan, which are also established as joint ventures between the GOP and other friendly countries.<sup>123</sup> Although these joint venture companies are dubbed as DFIs, the term DFI is not defined in Pakistani law. Essentially, the PCICL remains an NBFC incorporated under Pakistani company law.<sup>124</sup> From the international law perspective, the PCICL kind of DFIs would likely be classified as foreign investments covered under a typical bilateral investment treaty. Since the PCICL has been created with equal equity contribution by the GOP and the CBD, it is unclear if the CPEC projects will also be financed through the same arrangements.

Overall, Pakistan has a relatively open foreign investment regime.<sup>125</sup> The Pakistan Board of Investment (BOI) announced a fairly detailed foreign investment policy in 2013.<sup>126</sup> With an attractive taxation regime and financial exchange and remittance regulations, Pakistan is one of the most favourable regulatory regimes for foreign investors. The existing laws on the protection of property are also fairly comprehensive and balanced. The right to own property is established in the Constitution of Pakistan.<sup>127</sup> Although there is no constitutional maximum limit to property ownership, the Constitution authorizes Parliament to place limits upon ownership.<sup>128</sup> In regard to the protection of property rights, Article 24 of the Constitution provides:

- No person shall be deprived of his property save in accordance with law.

120 See eg Khaleeq Kiani, 'Pak-China Investment Company to Be Revived' *Dawn News* (6 September 2014).

121 Christian Kingombe, Isabella Massa and Dirk Willem te Velde, Overseas Development Institute, *Comparing Development Finance Institutions Literature Review* (20 January 2011) ix.

122 Ibid.

123 A list of development financial investments (DFIs) is available at <<http://www.sbp.org.pk/ecib/members.htm>> accessed 29 September 2015.

124 State Bank of Pakistan, *Financial Stability Review* (2007–8) 181.

125 Shahid Yousaf, *Can Chinese FDI Accelerate Pakistan's Growth?* Growth Dialogue, George Washington University Working Paper (February 2013).

126 The policy can be found on the Pakistan Board of Investment (BOI) website <<http://boi.gov.pk/Home.aspx>> accessed 29 September 2015 (Pakistan Investment Policy 2013).

127 Constitution of Pakistan 1973 (as modified up to 28 February 2012) arts 22 and 23. It may be noted that art 22, which gives the right to own property, is limited to citizens only; whereas art 23, which deals with the protection of property rights, has general application.

128 Constitution of Pakistan (n 130) art 253.

- No property shall be compulsorily acquired or taken possession of save for a public purpose, and save by the authority of law which provides for compensation therefor and either fixes the amount of compensation or specifies the principles on and the manner in which compensation is to be determined and given.

Article 24(3) of the Constitution further provides a fairly reasonable list of public purposes that may give rise to the taking of property. Article 173 of the Constitution specifically empowers the executive authorities of the federal and provincial governments to acquire properties within their respective territories. However, Article 24(4) states that the adequacy of compensation paid on the expropriation by governments cannot be called in question in any court in Pakistan. This may be viewed as a violation of due process of law. However, the law specifically dealing with the protection of foreign investments—that is, Foreign Private Investment (Promotion & Protection) Act 1976 (FPIA)—provides rules on the calculation of compensation.<sup>129</sup> This law is applicable to ‘foreign private investment’, covering investments made in goods and services.<sup>130</sup> The law provides that foreign investment shall not be acquired except under the due process of law<sup>131</sup> and also states the following three elements of the due process of law:<sup>132</sup>

- payment of adequate compensation;
- in the currency of the country of origin of investors; and
- specification of the principles on, and the manner in, which compensation is to be determined and given.

The FPIA also provides for the protection of agreements between a foreign investor or creditor and any person in Pakistan in the event that the government decides to take over or acquire a foreign investment in the public’s interest.<sup>133</sup> The law further prohibits discrimination against foreign investments and accords them no less favourable treatment in the application of laws, rules, and regulations generally<sup>134</sup> and particularly requires equal treatment of foreign and national investors for taxation purposes.<sup>135</sup> These provisions cover both contractual and regulatory matters. The law also clarifies that its provisions are not in derogation of protection to foreign investment under a BIT,<sup>136</sup> therefore, any additional or more stringent protections offered to foreign investors under a BIT would override the provisions of this law.

The Protection of Economic Reforms Act of 1992 (PERA) safeguards foreign-owned industrial or commercial property against acquisition by the government.<sup>137</sup>

129 Foreign Private Investment (Promotion and Protection) Act (No XLII) of 1976 (FPIA).

130 *Ibid* s 2.

131 *Ibid* s 5, para 2.

132 *Ibid*.

133 FPIA (n 132) s 5, para 1.

134 *Ibid* s 9. See also Pakistan Investment Policy 2013 (n 129) para 3.1.2, 15.

135 FPIA (n 132) s 8.

136 *Ibid* s 1.

137 Protection of Economic Reforms Act (No XII) of 1992, s 8 (PERA).

This law also legitimizes the privatization process and prohibits the retaking of privatized property or enterprise ‘for any reason whatsoever’.<sup>138</sup> Additionally, PERA preserves financial obligations incurred by the government with respect to privatized industries or enterprises.<sup>139</sup> It would be fair to conclude that these laws create a level playing field between foreign investors and local competitors at the post-entry stage and meet the international law standards of treatment of foreign investments. However, since no Pakistani court has yet deliberate on these laws, it is uncertain if the courts will interpret these provisions in accordance with international law.

One issue with these two laws is that neither of them provides procedures for their judicial enforcement and dispute resolution. Article 199 of the Constitution of Pakistan would fill this gap, which empowers the High Courts to entertain cases concerning the infringement of legal rights.<sup>140</sup> An act in violation of law by government officials can be remedied by the High Courts where no other appropriate remedy is provided by law. However, despite fairly stringent provisions of the FPIA or PERA, no foreign investor has so far approached the Pakistani High Courts alleging violation of their rights under these laws, although cases brought at international arbitration by foreign investors include claims of expropriation against the GOP.<sup>141</sup> Whereas, at least one foreign investor has also claimed before an international arbitration tribunal that the GOP has accorded less favourable treatment compared to local and other international investors.<sup>142</sup>

Although the Pakistan BOI publicizes that foreign investments are protected by the 1976 and 1992 laws,<sup>143</sup> it is not surprising that foreign investors have not yet brought legal actions in Pakistani courts on the bases of these laws and have instead preferred to bring BIT claims before supra-national arbitration tribunals. Pakistani courts have a poor reputation and an atrocious record when it comes to the enforcement of foreign investors’ rights.<sup>144</sup> In addition to making good laws in accordance with international standards, there is a need to build trust in the Pakistan legal system in order to attract more foreign investments. Adequate enforcement mechanisms and a concrete strategy of Pakistani courts from a clear line of decided cases would boost investor confidence. In particular, this would attract medium- and small-size investors who would not be willing, or able, to take their disputes to costly international arbitration.

138 Ibid s 7.

139 Ibid s 10.

140 Constitution of Pakistan 1973 (n 130) art 199.

141 See eg *Bayindir Insaat Turizm Ticaret Ve Sanayi AS v Islamic Republic of Pakistan*, ICSID Case No ARB/03/29, Final Award (27 August 2009) paras 97(iv), 113, 115, 395, 424–39 (*Bayindir*); *Impregilo SpA v Islamic Republic of Pakistan*, ICSID Case No ARB/03/3, Decision on Jurisdiction, (22 April 2005) paras 34(4), 55, 56, 272 and 274; *SGS Société Générale de Surveillance SA v Islamic Republic of Pakistan*, ICSID Case No ARB/01/13, Decision of the Tribunal on Objections to Jurisdiction (6 August 2003) para 35; *Tethyan Copper Company Pty Limited v Islamic Republic of Pakistan*, ICSID Case No ARB/12/1, Decision on Claimant’s Request for Provisional Measures (13 December 2012) paras 52, 64.

142 *Bayindir* (n 144) paras 97(iii), 149, 386–90.

143 Pakistan Investment Policy 2013 (n 129) paras 3.1.1, 3.1.2, 15.

144 See eg Ikram Ullah, ‘Reko Diq Case: Another Intervention from Supreme Court of Pakistan’ (2014) 17(6) *Intl Arbitration L Rev* 61; Umer Akram Chaudhry, ‘Pakistani Court Interference in Arbitration Proceedings—Yet Again!’ *Kluwer Arbitration Blog* (27 February 2012).

Arbitration, as we know, has become a popular system for the resolution of disputes between commercial parties as well disputes between commercial parties and government bodies. Even disputes arising from within a business enterprise, such as employment and labour disputes<sup>145</sup> and owner-participant disputes,<sup>146</sup> are now increasingly decided through arbitration. In Pakistan, arbitration in such ‘intra-enterprise disputes’ is possible,<sup>147</sup> but there are only a few existing examples.<sup>148</sup> This is mainly because the arbitration law in Pakistan has not kept pace with the needs of the business community. There is no formal institution in Pakistan to provide administrative support to arbitrate intra-enterprise or enterprise-to-enterprise disputes. An arbitration institute was proposed in 2009, but the proposal could not pass the legislative process.<sup>149</sup>

The current arbitration law in Pakistan dates from 1940,<sup>150</sup> which prescribes rules for arbitration with or without the intervention of a court.<sup>151</sup> The 1940 law applies to both domestic and international commercial arbitrations, however, the rules to distinguish between these two types of arbitrations are problematic.<sup>152</sup> The law also allows a degree of uncertainty regarding the enforcement of foreign arbitration agreements and awards.<sup>153</sup> In 2010, a new item was inserted in the legislative list of the Constitution of Pakistan, authorizing the Pakistani federal government to make laws on international treaties and international arbitration.<sup>154</sup> The difficulties regarding the enforcement of international commercial arbitration agreements and awards are now almost certainly resolved by the Recognition and Enforcement (Arbitration Agreements and Foreign Arbitral Awards) Act, 2011, which implements the New York Convention in Pakistan.<sup>155</sup> Some recent cases decided by Pakistani courts under this new law also suggest that courts are now willing to enforce foreign arbitration agreements between private parties more aptly than before.<sup>156</sup>

Pakistani law does not distinguish between purely private disputes and public-private disputes. However, courts are very sensitive to this distinction and are shy of

145 See eg Jean R Sternlight, ‘Creeping Mandatory Arbitration: Is It Just?’ (2004) 57 *Stanford L Rev* 1631; Christopher Bovis, ‘Labor Arbitration As an Industrial Relations Dispute Settlement Procedure in World Labor Markets’ (1994) 45(3) *Labor L J* 147.

146 Hal S Scott and Leslie N Silverman, ‘Stockholder Adoption of Mandatory Individual Arbitration for Stockholder Disputes’ (2013) 36 *Harvard J L & Public Policy* 1187; ‘Notes: Arbitration As a Means of Settling Disputes within Close Corporations’ (1963) 63(2) *Columbia L Rev* 267.

147 See Companies Ordinance (n 121) part IX.

148 For trends in arbitration on labour related disputes, see Riffat Bawa and Waqar Hashmi, ‘Labor Unionization in Pakistan: History and Trends’ (2010) 2(2) *Pakistaniaat: A Journal of Pakistan Studies* 78, 81.

149 See Arbitration Bill 2009, Part V. For some analysis of the Arbitration Bill, see Ahmad Ghouri, *Law and Practice of International Arbitration and Enforcement of Foreign Arbitral Awards in Pakistan* (Springer 2012) 3–4.

150 Arbitration Act (No X) of 1940.

151 Ghouri (n 152) 5-6.

152 Ibid 11–19.

153 Ibid.

154 Constitution of Pakistan 1973 (n 130) Fourth Schedule, part I, item 32.

155 Ghouri (n 152) 39–42. Convention on Recognition and Enforcement of Foreign Arbitral Awards, 7 *ILM* 1046 (1968).

156 Ibid. See also *Fal Oil Company Ltd. v Pakistan State Oil Company Ltd*, 2014 Pakistan Legal Decisions (Sindh) 427; *Abdullah v Messrs CNAN Group SPA*, 2014 Pakistan Legal Decisions (Sindh) 349.

enforcing arbitration agreements between private parties and government bodies.<sup>157</sup> Although Pakistan has also implemented the International Convention for the Settlement of Investment Disputes (ICSID Convention) through domestic legislation,<sup>158</sup> courts have struggled to distinguish the international investment arbitration from international commercial arbitration.<sup>159</sup> Recently, a few commercial arbitration awards rendered by ad hoc tribunals composed of local arbitrators have been reported in Pakistan.<sup>160</sup> The new law on SEZs, which will have direct implications for the execution of the CPEC and the SREB policy agendas, also makes provisions for arbitration as an alternate system for dispute resolution.<sup>161</sup> In the absence of an established institute to provide dispute resolution and arbitration services, growth of domestic commercial arbitration as a suitable alternative to litigation will remain dormant. Since the CPEC has brought the two countries closer than ever, it would be pertinent to establish a China–Pakistan arbitration centre at the roundabouts of the CPEC to serve the existing and future needs of the business community.

With regard to the protection of intellectual property (IP), Pakistan became party to the World Trade Organization's (WTO) Agreement on Trade-Related Intellectual Property Rights (TRIPs Agreement) on 1 January 1995.<sup>162</sup> The corresponding domestic legislation at that time was outdated.<sup>163</sup> The first copyright laws were enacted in 1962,<sup>164</sup> but recent legislation on patents, trademarks, and the layout designs of integrated circuits and registered designs have comprehensively updated the Pakistani IP regime.<sup>165</sup> The Intellectual Property Organization (IPO) of Pakistan was created in 2005<sup>166</sup> and is tasked with the integrated management of all types of intellectual property and enforcement coordination.<sup>167</sup> Now Pakistan has a fairly modern intellectual property regime, but there are still issues related to efficient enforcement. The 2012 IPO legislation has facilitated the establishment of special

157 This is evident from the consolidated judgment of the Pakistan Supreme Court in several cases filed against and by Tethyan in Pakistani courts on the Rico Diq mining licence dispute. The consolidated judgement and detailed decision was reported as *Maulana Abdul Haque Baloch v Government of Balochistan*, 2013 Pakistan Legal Decisions (Supreme Court) 641. See also (2012) Supreme Court Monthly Review 402.

158 Arbitration (International Investment Disputes) Act (No IX) of 2011. For some analysis of this Act, see Ghouri (n 152) 44–7.

159 *Lakhra Power Generation Company Limited (LPGCL) v Karadeniz Powership Kaya Bey*, 2014 Corporate Law Decisions (Sindh) 337.

160 See eg *Wi-Tribe Limited v Telecard Limited*, Award of 7 January 2010, 2010 Corporate Law Decision 500 (Justice (R) Saiduzzaman Siddiqui, Chairman, Justice (R) Nasir Aslam Zahid and Justice (R) GH Malik).

161 SEZs Act (n 95) s 39.

162 Agreement on Trade Related Intellectual Property Rights 1869 UNTS 299 (1994).

163 The regime was based on the Patent Act of 1911 and the Trademarks Act of 1940, which Pakistan inherited from the British India.

164 Copyright Ordinance (No XXXIV) of 1962.

165 Patents Ordinance of 2000, Trade Marks Ordinance of 2001, Registered Layout-Designs of Integrated Circuits Ordinance of 2000, Registered Designs Ordinance of 2000.

166 An Ordinance to Provide for the Establishment of the Intellectual Property Organization of Pakistan (No XXI) of 2005. Subsequently, the Intellectual Property Organization of Pakistan Act of 2012.

167 Intellectual Property Organization of Pakistan Act (n 169) s 13.

Intellectual Property Tribunals with the power for trial and prosecution of offences, but the Tribunals are yet to be established.<sup>168</sup>

The Pakistani domestic legal regime for foreign investments is based on both constitutional guarantees and statutory protections. These legal provisions are fairly extensive and cover all of the important aspects of foreign investment, including standards of treatment and payment of compensation for expropriation. The Pakistani government is keen to attract foreign investments and has put in place good incentives for investors. This existing combination of a legal and policy framework provides strong foundations for the implementation of the CPEC projects and other investments by Chinese companies. The PCICL can provide an institutional base and financial conduit for joint ventures between Chinese companies and Pakistani counterparts. However, certain weaknesses exist such as poor enforcement of legal rights by Pakistani courts and the absence of an arbitration institution to provide an alternative dispute resolution mechanism to formal litigation in courts.

### CHINA–PAKISTAN BILATERAL INVESTMENT REGIME

Pakistan has a good network of BITs in place, and 47 of them are currently in force.<sup>169</sup> Pakistan's BIT regime began in the 1950s, and, in fact, the first-ever contemporary BIT was signed between Pakistan and Germany in 1959.<sup>170</sup> Recently, however, Pakistan has taken a cautious approach in signing BITs. For example, Pakistan has refused to sign a BIT with the USA, although the USA is so far the largest investor in Pakistan.<sup>171</sup> The Board of Investment Ordinance 2001 has mandated the Pakistan BOI to negotiate and conclude BITs.<sup>172</sup> The BOI has so far signed four agreements and is also developing its own model BIT in order to modernize Pakistan's BIT regime.<sup>173</sup>

The China–Pakistan BIT was signed in 1989 and came into force in September 1990.<sup>174</sup> Article 13 of the BIT provides that it can be terminated after 10 years from the date of coming into force by either contracting party with a notice to the other party, and the termination will take effect one year after service of notice of termination by either party. Since no notice of termination has been served, the BIT remains in force. The China–Pakistan FTA,<sup>175</sup> which has been in force since July 2007, also includes a comprehensive chapter on investments.<sup>176</sup> Since both the BIT and FTA

168 Ibid, ss 15–19.

169 Pakistan Investment Policy 2013 (n 129) para 3.1.3, 15.

170 See eg Ahmad Ghouri and Nida Mahmood, 'Deciphering Pakistan's Foreign Investment Policy: A Review of Pakistani BITs' (2012) 13 *J World Investment & Trade* 812.

171 Office of the United States Trade Representative, Executive Office of the President United States, *Pakistan Begin Bilateral Investment Treaty Negotiations*, Press Statement (28 September 2004). See eg Shahbaz Rana, 'Why (Not) So Serious?: US Keen to Revive Bilateral Investment Treaty' *Express Tribune* (1 August 2013); Mehtab Haider, 'Pakistan Refuses to Accept US Model on Investment Treaty' *The News* (13 March 2015); 'Pakistan Rejects US Draft of Investment Treaty' *Pakistan Today* (13 March 2015).

172 Board of Investment Ordinance of 2001, s 9.

173 Amin Ahmed, 'New Bilateral Investment Treaty Model' *The Dawn News* (2 March 2015).

174 China–Pakistan BIT (n 23).

175 China–Pakistan FTA (n 8).

176 Ibid ch IX.

are simultaneously in force, the overlap of their respective provisions creates a degree of anxiety regarding the convergences and divergences of the standards of protection available to investors under both instruments. It is also important to note that the FTA has no retrospective application,<sup>177</sup> and investments entered before its entry into force are likely to be governed by the BIT provisions.<sup>178</sup> Likewise, investments made after the entry into force of the FTA can be governed by the FTA, the BIT, or either of them, subject to the fulfilment of the respective criteria set out in these two treaties.

When both the FTA and the BIT deal with the same subject matter (that is, investments, although the FTA also deals with trade), it would be appropriate to compare their respective provisions in order to attain a clearer view of the standards of investment protection provided by the two instruments. The comparison will also reveal if the FTA has enlarged or restricted the scope of BIT provisions. Additionally, Article 31 of the Vienna Convention on the Law of Treaties requires every treaty and each treaty clause to be interpreted in accordance with its ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.<sup>179</sup> It is, therefore, important to discuss the particular language used in different clauses of both the BIT and the FTA and its implications for investors and their investments. This will help the Chinese and Pakistani investors seeking to rely on these treaties to better understand their rights and reducing the risk of investment disputes.

The China–Pakistan BIT follows a standard format. The preamble sets forth the primary objectives as ‘to encourage, protect and create favourable conditions for investments by investors’ moving between party states. This language is different from some other BITs, for example, when their preambles associate the need to promote and protect foreign investments ‘with the aim to foster the economic prosperity’ of contracting states.<sup>180</sup> This latter type of objectives can possibly mean that in order for an investment to be protected under a BIT, it must have contributed to the development of the host State. Investor–State arbitration tribunals have interpreted this kind of BIT preamble, in conjunction with the preamble to the ICSID Convention, to apply this threshold for the protected investment under BITs.<sup>181</sup> However, given the various type of language used in BIT preambles and due to the

177 Ibid art 81.

178 There is a degree of uncertainty surrounding the issue if, under VCLT (n 182) art 59, a new treaty dealing with the same subject matter between the same parties impliedly terminates the earlier treaty or the parties required to specifically give notice of termination of the earlier treaty under VCLT art 65. However, international courts and tribunals have rejected the view of implied termination of treaties and clarified that a notice of termination is a compulsory requirement. See Ahmad Ghouri, *Interaction and Conflict of Treaties in Investment Arbitration* (Kluwer Law International 2015) 164–8.

179 Vienna Convention on the Law of Treaties 1155 UNTS 331 (1969) (VCLT).

180 Agreement between the Swiss Confederation and the Republic of Uzbekistan on the Promotion and Reciprocal Protection of Investments (signed on 16 April 1993, entered into force on 05 November 1993). See also *Romak SA v The Republic of Uzbekistan*, UNCITRAL – PCA Case No AA280, Award, 26 November 2009) para 181.

181 See my analysis on this in Ghouri (n 181) 141–3. The most famous investor–State reported cases that applied this threshold are *Salini Costruttori SpA and Italstrade SpA v Morocco*, ICSID Case No ARB/00/4, Decision on Jurisdiction (23 July 2001) and *Malaysian Historical Salvors Sdn Bhd v Malaysia*, ICSID Case No ARB/05/10, Award on Jurisdiction (17 May 2007) (*Malaysian Historical Salvors*).

imprecise meaning of the concept of ‘contribution to the host state’s development’, this requirement for protected investments has remained controversial.<sup>182</sup>

The China–Pakistan FTA has more detailed objectives listed in its preamble, including the following:

[T]his Agreement should be implemented with a view toward raising the standard of living, creating new job opportunities, and promoting sustainable development in a manner consistent with environmental protection and conservation.<sup>183</sup>

This preamble statement clearly lists the objectives in plain and neat language, stating precisely what the contracting parties intend to achieve through the implementation of the FTA. Although, as will be discussed in more detail below, the FTA defines the term investment broadly as ‘every kind of asset’,<sup>184</sup> this broad definition should be interpreted in light of the general objectives set forth in the preamble. In practice, this could mean that any conceivable investment in financial or business terms made by Chinese investors in Pakistan or vice versa will not amount to protected investment within the meaning of the FTA unless it meets the specific objective conditions listed in the preamble.

Both the BIT and the FTA define ‘investment’ as ‘every kind of asset’ invested as investment in accordance with the laws and regulations of the contracting parties.<sup>185</sup> For the purposes of clarity, both instruments provide a near identical non-exclusive list as examples of possible investments, including moveable and immovable property, shares and other form of interest in companies, claims to money or performance, intellectual property rights, and government concessions.<sup>186</sup> These definitions effectively cover both direct and portfolio investments. However, the BIT and the FTA take different approaches to define the term ‘investor’. The BIT gives two different definitions for Chinese and Pakistani investors. A Pakistani investor includes any ‘physical person’ who is a national of Pakistan or a company incorporated in Pakistan. Whereas a Chinese investor can be any ‘natural person’ who is Chinese national or ‘economic entities’ established in China having Chinese domicile.<sup>187</sup>

This is an interesting distinction. For example, the PCICL, which was discussed above, may be treated as neither a natural person who is a Chinese citizen nor an economic entity established and domiciled in China and may not amount to an investor according to this definition. However, given their wider definitions of the term ‘investment’, the PCICL is likely to qualify as an investment under both the BIT and the FTA. In terms of the application of protections to both investors and

182 Eg, the *Malaysian Historical Salvors* (n 184). The Award of Jurisdiction was subsequently annulled by an ad hoc Annulment Committee. See *Malaysian Historical Salvors Sdn Bhd v Malaysia*, ICSID Case No ARB/05/10, Decision on the Application for Annulment (16 April 2009). See also *Victor Pey Casado et Fondation ‘Presidente Allende’ c République du Chili*, ICSID Case No ARB/98/2, Sentence arbitrale (8 May 2008). Omar E García-Bolívar, ‘Defining an ICSID Investment: Why Economic Development Should be the Core Element’ *Investment Treaty News* (13 April 2012).

183 China–Pakistan FTA (n 8) preamble, para 5.

184 Ibid art 46.

185 China–Pakistan BIT (n 23) art 1(a); China–Pakistan FTA (n 8) art 46(1).

186 China–Pakistan BIT (n 23) art 1(a) I–V; China–Pakistan FTA (n 8) art 46 (1) (a) to (e).

187 China–Pakistan BIT (n 23) art 1(b).



investments, the FTA clearly states that its protections apply equally to both investments and investors.<sup>188</sup> This is different from the BIT's approach, which states that 'investments and activities associated with investments of investors' are protected.<sup>189</sup> The BIT's distinction between Chinese and Pakistani investors appears to be unnecessary and misleading, and the FTA eliminates this distinction by providing only one definition for investors belonging to both countries. The FTA defines investors as both 'natural persons' who are citizens and 'legal entities' constituted and have seats in a contracting party. This is a simple and better approach, which covers all forms of business enterprises.

Both the BIT and the FTA subject the admission of investment by party States to their respective laws and regulations.<sup>190</sup> This necessarily means that all CPEC projects will have to go through the domestic validation procedures. If no specific validation procedures are required by Pakistani law for a particular type of investment at the time of its entry, the validity of investment will be judged in view of its conformity with local laws.<sup>191</sup> An interesting comparison can be made between the definitions of investor and investment in the BIT and the FTA with that found in the FPIA. The FPIA conflates the terms investors and investment, and instead of defining investor it uses the term 'foreign capital', denoting it as an investment made by a foreigner in an 'industrial undertaking' in Pakistan:

- in the form of foreign exchange, imported machinery and equipment, or
- in any other form which the Federal Government 'may approve for the purpose'.<sup>192</sup>

The law defines 'foreign private investment' as an 'investment in foreign capital by a person who is not a citizen of Pakistan or who, being a citizen of Pakistan, is also the citizen of any other country or by a company incorporated outside Pakistan, but does not include investment by a foreign Government or agency of foreign Government'.<sup>193</sup> It is clear that the law does not extend its protections to investors and protects only investments. The law further limits the 'industrial undertakings' to such establishments engaged in the production of goods or services or extractive business 'as may be specified in this behalf by the Federal Government'.<sup>194</sup> The obvious limitation with 'as may be specified' and 'may approve for the purpose' is that the law does not cover investments that have not been specified and approved by the federal government. This is perhaps the reason why Pakistan did not set forth any domestic laws or regulations providing for a specific definition of investment in the *Bayindir* case.<sup>195</sup> These provisions of the FPIA should be amended to align them with the investment treaties.

188 China–Pakistan FTA (n 8) art 47(2).

189 China–Pakistan BIT (n 23) art 3(1).

190 Ibid art 2; China–Pakistan (n 8) art 47(1).

191 *Bayindir* (n 144) paras 109, 31.

192 FPIA (n 132) art 2(a).

193 Ibid art 2(b).

194 Ibid art 2(c).

195 *Bayindir* (n 144) paras 108, 31. It is noteworthy that although several investment treaty claims have been brought against Pakistan, *Bayindir* is the only case in which a detailed and publicly available final award has been rendered by an investor–State arbitration tribunal.

In term of protections, the BIT requires 'equitable treatment' and 'protection in the territory of other contracting party'.<sup>196</sup> This is not the language usually used in most contemporary BITs, which require 'fair and equitable treatment' (FET) and 'full protection and security'.<sup>197</sup> The basic idea of FET is to bring the application of 'good faith' and 'rule of law' to the investor–State relationship.<sup>198</sup> FET also works as an overarching principle to fill any gaps left by specific standards of protection set out by particular treaty clauses.<sup>199</sup> The different factors that emerge from decisions of investment tribunals as forming part of the FET standard comprise the obligation to act transparently and grant due process, to refrain from taking arbitrary or discriminatory measures, from exercising coercion, or from frustrating the investor's reasonable expectations with respect to the legal framework affecting the investment.<sup>200</sup> The use of 'equitable treatment' instead of 'fair and equitable treatment' merely reflects the evolutionary phase through which the standard has passed,<sup>201</sup> and the application of 'equitable treatment' without the prefix of 'fair' may bring the same results as FET because fairness is always a precondition in any legal relationship.

Similarly, the omission of the prefix 'full' and the post-fix 'and security' is likely to be of lesser significance because the 'full protection and security' standard by itself does not place a state under an obligation to provide absolute protection.<sup>202</sup> However, the FTA uses the fuller expression 'fair and equitable treatment'<sup>203</sup> and requires 'constant protection of and security' for both investors and investments.<sup>204</sup> The word 'constant' in place of 'full' for the protection and security is sensible because the addition of 'full' does not obligate contracting parties to provide absolute protection,<sup>205</sup> whereas consistency of the applicable protection should be a necessary condition.

The BIT does not have the 'national treatment' provision, which is meant to create a level playing field between the Chinese investors and local competitors. The BIT's 'no less favourable' treatment provision is limited to the most-favoured-nation (MFN) treatment, which ensures level playing field between investors from the BIT parties and investors coming from third states.<sup>206</sup> The 'no less favourable' standard generally requires a host State, at the time of implementation of its rules and regulations, to: (i) place foreign investors in a comparable setting as local competitors; (ii) treat them as favourably as the local competitors; and (iii) if treatment of the foreign

196 China–Pakistan BIT (n 23) art 3(1).

197 See eg Rudolf Dolzer and Christoph Schreuer, *Principles of International Investment Law* (2<sup>nd</sup> edn, Oxford University Press 2012) 130–2.

198 Ibid 132–4.

199 Ibid.

200 *Bayindir* (n 144) paras 178, 50.

201 See eg Fair and Equitable Treatment, (1999) UN Publication Sales No E.99.ILD.15, UNCTAD/ITE/IIT/11 (Vol III) 29–31.

202 Dolzer and Schreuer (n 201) 161.

203 China–Pakistan FTA (n 8) art 48(1).

204 Ibid art 47(2).

205 See eg *AAPL v Sri Lanka*, ICSID Case No ARB/87/3, Award (27 June 1990) para 48; *Wena Hotels Ltd v Arab Republic of Egypt*, ICSID Case No ARB/98/4, Award (8 December 2000) para 84.

206 China–Pakistan BIT (n 23) art 3(2). See eg Noah Rubins and N Stephan Kinsella, *International Investment, Political Risk and Dispute Resolution: A Practitioner's Guide* (Oceana Publications 2005) 225–6.

investor is less favourable than that of local competitors, justify as to why the foreign investor has been given the different treatment.<sup>207</sup> The FTA, however, covers both national treatment and MFN treatment.<sup>208</sup> Since both national treatment and MFN treatment standards require a comparison between a claimant foreign investor and another local or foreign investor, investor–State arbitration tribunals assess whether the claimant was in a ‘similar situation’ to that of other investors.<sup>209</sup> Once a claim has passed the ‘similar situation’ test, tribunals then inquire whether the claimant investor was granted less favourable treatment than other investors.<sup>210</sup> Claimant investor has the responsibility to identify appropriate comparators who were in a similar situation and also the burden to prove that the host State treated those comparators more favourably.<sup>211</sup>

Both the BIT and the FTA have the so-called Regional Economic Integration Organization (REIO) exception to the MFN treatment.<sup>212</sup> The REIO exception in both treaties cover customs unions, free trade zones, and special taxation regimes.<sup>213</sup> The FTA includes an additional REIO exception for small-scale trade in border areas.<sup>214</sup> The existence of an REIO depends on many factors such as mere political commitments or formal and legally binding obligations to dismantle market access obstacles for investors or investments coming from states forming part of an REIO.<sup>215</sup> The exact characteristics of an REIO are not fully established, but it connotes a multilateral consortium with some kind of institutional setup.<sup>216</sup> The practical effect of an REIO exception to MFN treatment in an investment treaty (a BIT or an investment chapter in a bilateral FTA) is that any investment concessions or other favourable treatment allowed by party States to investors or investments coming from their REIO partners will not be available as comparators to prove violation of MFN treatment under the investment treaty.

Both the BIT and the FTA include provisions on expropriation.<sup>217</sup> Although the FTA’s expropriation clause has used a negative construction in comparison to the BIT (that is, ‘[n]either Party shall expropriate’ in the FTA as compared to ‘[e]ither Contracting Party may . . . expropriate’ in the BIT), the conditions imposed for expropriation in both the BIT and the FTA are the same.<sup>218</sup> These conditions are in line with the international rules and allow expropriation only on the bases of public interest, under domestic legal procedures, without discrimination, and on payment

207 Dolzer and Schreuer (n 201) 199.

208 China–Pakistan FTA (n 8) art 48, clauses (2) and (3).

209 *Bayindir* (n 144) paras 389, 114.

210 *Ibid* paras 390, 114.

211 *Ibid* paras 419, 122.

212 China–Pakistan BIT (n 23) art 3(3); China–Pakistan FTA (n 8) art 48(4). On Regional Economic Integration Organization (REIO) clauses, see eg ‘The REIO Exception in MFN Treatment Clauses’ UNCTAD Series on International Investment Policies for Development, United Nations (New York and Geneva 2004).

213 China–Pakistan BIT (n 23) art 3(3); China–Pakistan FTA (n 8) art 48(4).

214 China–Pakistan FTA (n 8) art 48 (4)(c).

215 See ‘The REIO Exception in MFN Treatment Clauses’ (n 216) 11.

216 *Ibid*.

217 China–Pakistan BIT (n 23) art 4; China–Pakistan FTA (n 8) art 49.

218 China–Pakistan BIT (n 23) art 4; China–Pakistan FTA (n 8) art 49.

of compensation.<sup>219</sup> Instead of the requirement of ‘prompt, adequate and effective’ compensation,<sup>220</sup> the BIT requires calculation of compensation in accordance with the laws of host State, paid in convertible currencies, and without unreasonable delay.<sup>221</sup> The FTA uses slightly different language and requires the compensation to be made ‘without delay, be effectively realisable and freely transferable’.<sup>222</sup>

However, where the BIT requires the calculation of compensation in accordance with the laws of host State, the FTA provides that the value of an expropriated property ‘shall be determined in accordance with the generally recognised principles of valuation’.<sup>223</sup> Since there is no single method for valuation of claims in international investment law, this FTA provision may produce unexpected outcomes.<sup>224</sup> The FTA further provides that compensation shall be equivalent to the value of expropriated investments immediately before the expropriation or when the impending expropriation becomes public knowledge, whichever is earlier.<sup>225</sup> This compensation does not cover the loss of the business opportunity and future profits. In case of delay in the payment of compensation, the FTA requires payment of interest ‘at a normal commercial rate’ for the period between expropriation and the actual payment of compensation.<sup>226</sup> It goes without saying that the reference to the ‘normal commercial rate’ for the calculation of interest on unpaid compensation is susceptible to more than one interpretation.

Pertinent to the BIT’s provision that compensation will be calculated in accordance with the laws of the host State, the BIT has required unsatisfied investors to move the competent domestic court of the host State to review whether the amount of compensation is in accordance with the applicable domestic laws.<sup>227</sup> There is no equivalent provision in the FTA. Both the BIT and the FTA have a *force majeure* clause.<sup>228</sup> Both *force majeure* clauses are identical and cover loss arising from war, state of emergency, insurrection, and riots; however, the clause in the FTA clarifies that it applies to both investors and their investments and requires, as opposed to only MFN treatment in the BIT, both national and MFN treatment in regard to restitution, indemnification, compensation, and other settlement.<sup>229</sup> Similarly, both the BIT and the FTA have near identical clauses on the free transfer of fund guarantee,<sup>230</sup> however, the provision in the FTA extends this guarantee to the

219 China–Pakistan BIT (n 23) art 4; China–Pakistan FTA (n 8) art 49. See eg Andrew Newcombe and Lluís Paradell, *Law and Practice of Investment Treaties: Standards of Treatment* (Kluwer Law International 2009) 369–77.

220 See eg Peter D Isakoff, ‘Defining the Scope of Indirect Expropriation for International Investments’ (2013) 3(2) *Global Business Law Revw* 189, 191.

221 China–Pakistan BIT (n 23) art 4(2).

222 China–Pakistan FTA (n 8) art 49(2).

223 *Ibid* art 49(2).

224 Eg, if the compensation will be calculated on the bases on discounted cash flow, fair/full market value, and/or will include future lost profits.

225 China–Pakistan FTA (n 8) art 49(2).

226 *Ibid* art 49 (2).

227 China–Pakistan BIT (n 23) art 4(3).

228 *Ibid* art 4(4); China–Pakistan FTA (n 8) art 50.

229 China–Pakistan FTA (n 8) art 50.

230 China–Pakistan BIT (n 23) art 5; China–Pakistan FTA (n 8) art 51.

compensation paid to an investor against expropriation or *force majeure*.<sup>231</sup> Both the BIT and the FTA have subrogation clauses by which the rights and claims of investors can be assigned to, and exercised by, their respective home states or a designated agency.<sup>232</sup>

Both treaties have provisions on the settlement of disputes between the party States as well as between an investor and a party State. In both treaties, the first means for dispute resolution between party States is consultation through diplomatic channels.<sup>233</sup> If consultations fail to resolve the dispute within six months, disputes between party States will be resolved through an ad hoc arbitration tribunal consisting of three members, where each party will appoint one arbitrator and the two appointed arbitrators will appoint the third arbitrator who will preside over the tribunal.<sup>234</sup> The ad hoc tribunal shall decide the dispute in accordance with the provisions of the respective treaties (the BIT or the FTA) and principles of international law recognized by both parties.<sup>235</sup> The requirement of principles of international law 'recognized by both parties' is very subjective and can create friction in the absence of specific criteria to determine if a principle is recognized by both parties. This kind of subjective provision is likely to allow an arbitration tribunal to exercise value judgment in determining the application of applicable principles of international law and may serve as a tool for balancing private rights against the public's interest and the host State's right to regulate. The tribunal shall reach its award on the basis of a majority vote, and this award will be final and binding upon the parties.<sup>236</sup>

The investor–State dispute resolution provision in the BIT has a very narrow scope.<sup>237</sup> It is restricted to disputes involving the amount of compensation for expropriation and does not cover any other violations of the standards of treatment provided in the BIT. An investor can file a complaint with a competent authority of the expropriating State to challenge the amount of compensation paid for expropriation. If such a complaint is not resolved within a year, the investor can take the dispute to the competent domestic court of the host State or to an international arbitral tribunal.<sup>238</sup> The BIT does not provide any details on the formation and procedures of the international arbitral tribunal or the law such a tribunal will apply.

As compared to the BIT, the FTA contains a more detailed clause on investor–State dispute resolution.<sup>239</sup> The FTA extends the application of the investor–State dispute resolution provision to 'any legal dispute' that is 'in connection with an investment'.<sup>240</sup> The first step for dispute resolution is negotiations between disputing parties, and if negotiations do not resolve the dispute within six months, the investor can choose to take the dispute to the domestic court of the host State or to

231 China–Pakistan FTA (n 8) art 51(2).

232 China–Pakistan BIT (n 23) art 7; China–Pakistan FTA (n 8) art 52.

233 China–Pakistan BIT (n 23), art 9(1); China–Pakistan FTA (n 8) art 53(1).

234 China–Pakistan BIT (n 23) art 9; China–Pakistan FTA (n 8) art 53.

235 China–Pakistan BIT (n 23) art 9(5); China–Pakistan FTA (n 8) art 53(5).

236 China–Pakistan BIT (n 23) art 9(5); China–Pakistan FTA (n 8) art 53(6).

237 China–Pakistan BIT (n 23) art 10.

238 Ibid.

239 China–Pakistan FTA (n 8) art 54.

240 Ibid art 54(1).

International Centre for Settlement of Investment Disputes (ICSID).<sup>241</sup> The choice of ICSID is subject to any domestic administrative review procedures specified by the laws and regulations of the host State.<sup>242</sup> The FTA further provides that once the investor has submitted the dispute to the competent domestic court of the host State or to ICSID, the choice of the forum shall be final.<sup>243</sup> This is an interesting provision as typical investor–State dispute resolution provisions in investment treaties allow parallel proceedings before domestic courts of host States and international arbitration.<sup>244</sup> By limiting the investors’ choice to only one of these at a time, the FTA has effectively pre-empted possible conflicting outcomes from the two separate decision-making bodies. The choice of ICSID in the FTA as the only forum for international arbitration appears to be unnecessarily restrictive. However, since there is no similar arbitration centre present in the region, ICSID appears to be the only sensible option.

The FTA further requires that the arbitration award shall be based on the domestic law of the host State including rules on the conflict of laws, the provisions of the FTA, and the ‘universally accepted principles of international law’.<sup>245</sup> The application of universally accepted principles of international law is meant to ensure that the investors’ rights are protected in accordance with the most civilized standards of treatment that exist in international law, although they may not have formed part of the FTA or have not been legislated domestically by the party States. This is also in sharp contrast with the earlier-mentioned BIT’s requirement of principles of international law recognized by party States. Although what would be universally acceptable principles of international law is also highly subjective, it reflects a move away from the individual or regional notions of international law principles and towards the main stream universalism.

The FTA also contains an ‘umbrella clause’ requiring contracting States to observe the commitments they have made with investors of the other party in regard to their investments.<sup>246</sup> This provision serves to bring independent contracts made by a party State with investors from another party State under the umbrella of the FTA’s protections. A breach of such contract will be treated as a breach of the FTA, allowing investors to use the dispute resolution provisions of the FTA.

The combination of the FTA and the BIT provide the most modern and comprehensive bilateral regime for the protection of Chinese investments in Pakistan. The

241 Ibid art 54(2).

242 Ibid art 54(2) (b).

243 Ibid art 54.

244 See eg Agreement between the Government of the Australia and the Government of the Islamic Republic of Pakistan on the Reciprocal Encouragement and Protection of Investment (entered into force on 14 October 1998) arts 13 and 14; Agreement between the Government of the United Kingdom and the Government of the Islamic Republic of Pakistan on the Reciprocal Encouragement and Protection of Investment (entered into force on 30 November 1994) art 8. The FTA’s restriction is comparable with the investor–State dispute resolution provision in the Pakistan–Japan BIT, which does not allow investors to initiate international arbitration until the final judicial settlement of dispute by domestic court of the host state. See Agreement between the Government of Japan and the Government of the Islamic Republic of Pakistan on the Reciprocal Encouragement and Protection of Investment (entered into force on 29 May 2002) art 10(3).

245 China–Pakistan FTA (n 8) art 54(3).

246 Ibid art 55(2).

standards of protection are in line with the international rules, however, since both treaties subject the creation of investments to domestic laws of the host State, the CPEC projects will have to go through the domestic validation procedures in order to qualify as investments within the scope of protections offered by the treaties. Although there is a need to create local arbitration institution, the FTA and the BIT create a bilateral investment regime befitting the deep-rooted economic ties between the two countries.

## CONCLUSIONS

The detailed SREB Action Plan has clarified that the SREB is intended to guide the entire region into a new era of cooperation and economic development. The broader legitimacy of the project is ensured through the cautious commitment that the SREB rules of engagement will follow the principles of international law. The commitment to a balanced development of the different parts of the SREB involving both long-time friends, such as Pakistan, and yet to be tested partners, such as India, shows the Chinese government's commitment to take particular perceptions and viewpoints of all stakeholders on board. This could effectively mean that different parts of the SREB will evolve at a different pace depending on the particular partners requiring a continued commitment of the Chinese government to the project. However, where the SREB has a larger regional impact, its offspring, the SPEC, has special importance for both Pakistan and China, and both countries need to develop a collective strategy to address Indian concerns in order to enhance the greater legitimacy and integrity of the project.

The SREB's market-based approach to regional integration is quite innovative and is well suited for regional partners that have many differences in their government systems, social structures, and legal ideologies. The SREB initiative is based on economic development through trade instead of aid and long-term investments through commercial enterprises, and it clearly has the potential to bring more sustainable development. These innovative approaches reflect new models of international cooperation and global governance to achieve common ideals. The SREB will enable partner countries to learn from each other's experiences and to devise collective strategies to fulfil mutual economic and development needs. The increased regional economic integration and interdependency will promote mutual trust and the ability to produce a collective response to global economic challenges.

Where the SREB initiative is largely conducive to the economic needs of participating states, there are a number of issues that need to be addressed in order to earn the broader socio-legal cogency. In the context of the CPEC, for example, there is a need to bring more transparency and public debate, to ensure the fair distribution of benefits of the project and proper enforcement of labour standards and to have effective laws and procedures in place to pre-empt corrupt practices of corporate and government officials. The reference to social responsibility of corporations in the SREB Action Plan is a good initiative; however, effective laws and procedures for the enforcement of this cross-border corporate responsibility need to be incorporated into the domestic legal systems. Overall, the relations among all SREB partners should be based on mutual trust, ensuring that the large-scale Chinese investments set a path to improve governance, transparency and the effective rule of law, and

strengthened property rights. If this is not done, China's economic presence is likely to be viewed as a dominating device in the longer run.

Investments by Chinese companies in Pakistan cover a variety of sectors and will adapt to different legal and transactional formats suitable to the kind of investments made, depending upon whether the investor is a private or a state-owned company and the nature of the projects. The CPEC will bring a new wave of Chinese investment in Pakistan, and a solid domestic regime of foreign investment governance is imperative to satisfy both the legitimacy (that is, through proper implementation of domestic validating rules and procedures) and success (that is, through proper definition and allocation of rights and responsibilities) of foreign investments. Pakistan has well-defined and fairly modern national investment laws that provide adequate protection to foreign investors. The Pakistani law requires expropriation to follow the due process of law and against the payment of adequate compensation. In the case of expropriation, the rights of third parties and creditors are protected under the law. The law requires non-discrimination and no less favourable treatment to foreign investors. The reacquisition of privatized government companies is expressly prohibited even for a public purpose. The higher courts in Pakistan are competent to entertain and enforce any breaches of these laws; however, there is a need to build the confidence of foreign investors in the domestic courts.

Other forms of dispute resolution, such as arbitration, are also available to foreign investors under the Pakistani laws, although there is no established arbitration institute in Pakistan to provide administrative support to disputing parties willing to arbitrate. The recent cases decided by Pakistani courts suggest that courts are now willing to enforce foreign arbitration agreements between private parties more aptly than before. The new legislation implementing the New York Convention and the ICSID Convention in Pakistan have brought certainty to the enforcement of arbitral awards in Pakistan. However, in anticipation of a rapid increase in the volume of Chinese investments in Pakistan after the implementation of the CPEC and also to facilitate existing investments, the two countries should consider establishing a joint arbitration centre. Pakistan also has a modern IP regime in place, but the enforcement infrastructure has not yet been created, which will potentially discourage some foreign investors.

The two countries have put a fairly strong bilateral investment regime in place with the BIT and a chapter on investments in the FTA. The BIT and the FTA have many similar provisions, however, the language used in the FTA reflects the most recent jurisprudence of investor protection. For example, the FTA uses the fuller expression of 'fair and equitable treatment' in comparison to the BIT, which merely requires 'equitable treatment'. The FTA has also covered gaps in the BIT's provisions on the treatment of investors, for example, by providing both national treatment and MFN treatment as opposed to the BIT's only MFN treatment. There is also significant variation in the language of provisions on expropriation where a negative construction in the FTA appears to discourage expropriation. The FTA also requires the calculation of compensation for expropriation in accordance with 'generally recognised principles of valuation' as opposed to the BIT, which allows calculation according to the domestic laws of the host State. However, the reference to 'generally recognised principles of valuation' in the FTA is subject to interpretation as there is



no standard or unified principle of calculation of compensation in international law. The same problem may arise with respect to the FTA's provision on interest on the unpaid compensation, which requires the calculation of interest at a 'normal commercial rate'.

Compared to the BIT, the FTA has more extensive and modern provisions on investor-State dispute settlements covering any legal dispute in connection with an investment. The FTA allows a dispute to proceed directly to international arbitration without requiring exhaustion of local remedies. However, the FTA does not allow parallel proceedings before domestic courts and international arbitration preventing possibly opposing outcomes from the two different avenues. The choice of ICSID as an arbitration centre is both restrictive and unwieldy as the two countries should endeavour to develop local capacities and create regional centres for international arbitration.

Overall, the SREB initiative has great potential for the entire region and will bring the participating countries closer than ever. It provides a great opportunity for the participating countries to resolve their existing differences and join hands with China to strive for the total development of the entire region. The earlier-mentioned challenges, regardless if they are purely political or legal in their nature, are certainly manageable. A careful re-evaluation of the SREB Action Plan is required in order to reflect the awareness of these challenges and to display a broader vision and determination to address them. The Chinese 'go global' policy will remain unrewarding both socially and economically in the long run if Chinese domestic legal structures are not tuned to cope with the problems of a global and transnational nature. Building transnational roads and infrastructures must go hand in hand with the development of sophisticated and effective rights enforcement mechanisms at both the national and transnational levels.