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International Investment Law and the Rule of Law: The Case of China

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INTERNATIONAL INVESTMENT LAW AND THE RULE OF LAW: THE CASE OF CHINA

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Abstract: This article purports to discuss the impact of international investment law on domestic governance and the rule of law of a nation state. Using China as a case study, this article argues that the role of international investment law in advancing domestic rule of law has long been overstated. The prevailing narrative is premised on some deeply flawed assumptions of the nature and function of international investment law as well as how international investment law may affect domestic legal change. These assumptions include, inter alia: (1) international investment norms possess the rule of law ideals; (2) improving good governance and the rule of law is part of the mandate of international investment law; (3) powerful investor-state dispute settlement is effective in guarding the rule of law; and (4) the state is readily receptive to all direct and indirect influences of economic globalization. A close examination of the limits of international investment law in this article explains why its role in promoting the rule of law in China is rather limited, contrary to what was widely expected in the Western world.

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INTRODUCTION

International Investment law commits states to afford specific standards of protection to foreign investors from other states and bind themselves to dispute settlement mechanisms for enforcement of those commitments. But what is the rationale of international investment law? The traditional claim was that, by offering special protections to foreign investors, international investment agreements (IIAs) help attract foreign investment and contribute to economic development in host countries.[1] However, this claim has become increasingly untenable in view of empirical evidence.[2] More recently, the narrative of IIAs securing and promoting the rule of law at both domestic and international levels has been advanced to provide another justification to legitimize the existence and operation of the international investment regime.[3]

The conventional account of international investment law's positive impact on domestic rule of law is almost intuitive. To start with, the same principles required by the core rule of law requirements are embodied in IIAs.[4] Fair and equitable treatment (FET), a core international investment law concept in all modern IIAs, offers the best example. Over the years, international investment arbitral tribunals have described FET as requiring host states to afford foreign investors, among other things, a stable and predictable legal framework, due process, transparency, and the protection of legitimate expectation.[5] The articulations of the FET standard effectively translate the declaratory rule of law

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[1] Jeswald W. Salacuse, *Of Handcuffs and Signals: Investment Treaties and Capital Flows to Developing Countries,* 58 HARV. INT'L. L.J. 127, 130 (2017).

[2] Jason W. Yackee, *Bilateral Investment Treaties, Credible Commitment, and the Rule of (International) Law: Do BITs Promote Foreign Direct Investment*?, 42 LAW & SOC'Y REV. 805, 827–28 (2008) (finding that BITs have little or no impact on foreign investment decision); JONATHAN BONNITCHA, LAUGE N. SKOVGAARD POULSEN & MICHAEL WAIBEL, THE POLITICAL ECONOMY OF THE INVESTMENT TREATY REGIME 155–60 (2017). *But see* Eric Neumayer & Laura Spess, *Do Bilateral Investment Treaties Increase Foreign Direct Investment to Developing Countries*?, 33 WORLD DEV. 1567, 1582 (2005) (finding that developing countries that sign more BITs with developed countries receive more FDI inflows).

[3] AUGUST REINISCH, & STEPHAN W. SCHILL, INVESTMENT PROTECTION STANDARDS AND THE RULE OF LAW 1 (2023); N. Jansen Calamita & Ayelet Berman, *The Rule of Law, Investment Treaties, and Economic Growth: Mapping Normative and Empirical Questions*, in INVESTMENT TREATIES AND THE RULE OF LAW PROMISE 1, 2–3 (N. Jansen Calamita and Ayelet Berman eds., 2022); MAVLUDA SATTOROVA, THE IMPACT OF INVESTMENT TREATY LAW ON HOST STATES: ENABLING GOOD GOVERNANCE? 7–9 (2018); Susan D. Frank, *Foreign Direct Investment, Investment Treaty Arbitration, and the Rule of Law*, 19 PAC. MCGEORGE GLOBAL BUS. & DEV. L.J. 337, 340 (2007).

[4] Stephan W. Schill, *Fair and Equitable Treatment, the Rule of Law, and Comparative Public Law*, in INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 151, 157–59 (Stephan W. Schill ed., 2010); Kenneth J. Vandevelde, *A Unified Theory of Fair and Equitable Treatment*, 43 N.Y.U. J. INT'L. L. & POL. 43, 49–50 (2010).

[5] Schill, *supra* note 4, at 159–71; Tecnicas Medioambientales Tecmed S.A. v. United Mexican States, ICSID Case No. ARB (AF)/00/2, Award, at 154 (May 29, 2003).

commitments of states into palpable investment law requirements.[6] Out of the desire to avoid draconian liability for breaches of IIAs, host states internalize their international investment law obligations and reform their policy-making process.[7] Furthermore, IIA rules represent the rule of law for foreign investment. The rule of law, however, is not easily compartmentalized to a single sector. It will create spillover effects on a host state's legal system because the host state needs to gradually develop better rule-oriented governance practices to comply with IIA rules.[8]

More importantly, the normative framework of international economic order changed from the original embedded liberalism to a neoliberal project in the late 1970s.[9] The neoliberal paradigm promotes privatizing public enterprises, reducing government intervention in economic and social activities, liberalizing flows of trade and investment, limiting government subsidies, protecting private property, and establishing neutral dispute resolution mechanisms to ensure compliance with standards of global governance.[10] The neoliberal dimension was then formalized and technicalized in international investment law.[11] IIAs have become a channel through which neoliberal commitments are formalized and key norms of free markets and good governance are learned and internalized. In the end, international investment law will strengthen democratic accountability and participation, promote good and orderly state administration, and generally improve the protection of individual rights.[12] Therefore, domestic firms and citizens will ultimately benefit from the "halo effect" provided by stronger constraints on arbitrary government action.[13]

The prevailing narrative of the relationship between international investment law and the rule of law is of particular relevance for a state like China. With a

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[6] Velimir Živković, *Fair and Equitable Treatment between the International and National Rule of Law*, 20 J. WORLD INV. & TRADE 513, 522–24 (2019).

[7] Benedict Kingsbury & Stephan W. Schill, *Investor-State Arbitration as Governance: Fair and Equitable Treatment, Proportionality and the Emerging Global Administrative Law* 16–17 (N.Y.U. Sch. L. Pub. L. & Legal Theory Rsch. Paper Series, Working Paper No. 09-46, 2009).

[8] Thomas Schultz & Cédric Dupont, *Investment Arbitration: Promoting the Rule of Law of Over-Empowering Investors? A Quantitative Empirical Study*, 25 EUR. J. INT'L L. 1147, 1161 (2015); Roberto Echandi, *What Do Developing Countries Expect from the International Investment Regime*?, *in* THE EVOLVING INTERNATIONAL INVESTMENT REGIME: EXPECTATIONS, REALITIES, OPTIONS 3, 13–14 (Jose E. Alvarez & Karl P. Sauvant eds., 2011).

[9] Ntiza Tzouvala, *The Ordo-Liberal Origins of Modern International Investment Law: Constructing Competition on a Global Scale*, *in* NEW VOICES AND NEW PERSPECTIVES IN INTERNATIONAL ECONOMIC LAW 37, 37–54 (John D. Haskell & Akbar Rasulov eds., 2020); ANDREW LANG, WORLD TRADE LAW AFTER NEOLIBERALISM: REIMAGINING THE GLOBAL ECONOMIC ORDER 221–40 (2011).

[10] DAVID M. KOTZ, THE RISE AND FALL OF NEOLIBERAL CAPITALISM 12 (2015); Elaine Hartwick & Richard Peet, *Neoliberalism and Nature: The Case of the WTO*, 590 ANNALS AM. ACAD. POL. & SOC. SCI. 188, 190–92 (2003).

[11] M. SORNARAJAH, RESISTANCE AND CHANGE IN THE INTERNATIONAL LAW ON FOREIGN INVESTMENT 10–16 (2015).

[12] Stephan W. Schill & Vladislav Djanic, *International Investment Law and Community Interests*, *in* COMMUNITY INTERESTS ACROSS INTERNATIONAL LAW 221, 228–29 (Eyal Benvenisti & George Nolte eds., 2018).

[13] World Bank, *World Development Report 2005: A Better Investment Climate for Everyone*, Rep. No. 28829, at 179 (Jan. 1, 2004).

long history of official intervention in all aspects of life, the rise of the neoliberal paradigm in global economic governance challenges core ideas about the proper role of Chinese government in society and could trigger broader regulatory changes.[14] Indeed, this narrative points to Western elites enthusiasm about the prospect that China's integration into the liberal rules-based international economic order would encourage China to evolve into a market economy, instill a sense of the rule of law, and drive China towards Western liberal democratic values.[15]

Previous research on the topic has revealed a promising relationship. Since its first bilateral investment treaty (BIT) with Sweden in 1982, China has created an extensive network of IIAs. By February 2024, China has signed 146 BITs and 30 treaties with investment provisions, second only to Germany in terms of the number of IIAs concluded.[16] China was the second largest recipient of foreign direct investment (FDI) inflows and the third largest source of outward FDI in 2022.[17] It is, therefore, only natural for international investment law scholars to expect that China's extensive network of IIAs has had a positive and palpable impact on the rule of law in China.[18] There is also some evidence showing that the Chinese regions in which the rule of law is better realized are those in which foreign investors play a considerable role in economic development.[19]

More recently, however, a new consensus has emerged that China's increased participation in the liberal international economic order had not effectuated China's deeper engagement with market economy transformation or respect for the rule of law.[20] Though rhetoric about law has been prominent in Chinese official statements, reality has fallen short of official promises.[21] Accordingly, the political will to deepen economic engagement so as to promote the rule of law

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[14] *See* Gregory Shaffer, *How the World Trade Organization Shapes Regulatory Governance*, 9 REGUL. & GOVERNANCE 1, 2 (2015); Richard H. Steinberg, *International Trade law as a Mechanism for State Transformation, in* BACK TO BASICS: STATE POWER IN A CONTEMPORARY WORLD 187–90 (Martha Finnemore & Judith Goldstein eds., 2013).

[15] *Decades of Optimism about China's Rise Have Been Discarded*, THE ECONOMIST (Mar. 1, 2018), https://www.economist.com/briefing/2018/03/01/decades-of-optimism-about-chinas-rise-have-been-discarded; Charlene Barshefsky, *Trade Policy and the Rule of Law*, 9 MINN. J. GLOB. TRADE 361, 367 (2000).

[16] *International Investment Agreements Navigator*, UNCTAD (last visited Apr. 11, 2024), https://investmentpolicy.unctad.org/international-investment-agreements/countries/42/china.

[17] U.N. Conference on Trade and Development., *World Investment Report 2023: Investing in Sustainable Energy for All*, [T/D]/UNCTAD/WIR/2023 8, 17 (2023). China received 189 billion USD in FDIs and had an outward amount of 147 billion USD.

[18] Kate Hadley, *Do China's BITs Matter – Assessing the Effect of China's Investment Agreements on Foreign Direct Investment Flows, Investor Rights, and the Rule of Law*, 45 GEO. J. INT'L. L. 255, 310 (2013); Shen Wei, *Expropriation in Transition: Evolving Chinese Investment Treaty Practices in Local and Global Contexts*, 28 LEIDEN J. INT'L L. 579, 600 (2015) (arguing that the liberalization of investment flows portends the fundamental transformation of China from within by embracing the rule of law).

[19] YUHUA WANG, TYING THE AUTOCRAT'S HANDS: THE RISE OF THE RULE OF LAW IN CHINA 3–4 (2015)

[20] *National Security Strategy*, WHITE HOUSE 11 (Oct. 2022), https://www.whitehouse.gov/wp-content/uploads/2022/10/Biden-Harris-Administrations-National-Security-Strategy-10.2022.pdf; *see generally* CARL MINZNER, END OF AN ERA: HOW CHINA'S AUTHORITARIAN REVIVAL IS UNDERMINING ITS RISE (2018).

[21] Jacques DeLisle, *Law in the China Model 2.0: Legality, Developmentalism and Leninism under Xi Jinping*, 26 J. CONTEMP. CHINA 68, 69–70 (2017).

in China has been significantly eroded in the United States.[22] Instead, the United States and its allies have adopted a "de-risking" economic strategy toward China.[23] The strategy seeks to choke off the flow of advanced technologies critical for national security to China and prevent China from becoming a technology and military superpower. Additionally, it aims to reduce dependence on Chinese products by having resilient, effective supply chains outside China.[24] As part of the de-risking strategy, President Biden banned certain U.S. outbound investment in specific sensitive technologies in China in August 2023.[25]

Similarly, the European Commission stated that China was, simultaneously, a "cooperation and negotiating partner," an "economic competitor," and "a systemic rival" in 2019.[26] Since then, the political and economic environment has changed drastically with tit-for-tat sanctions for human rights violations in Xinjiang and the suspension of the legislative process for ratifying the EU-China Comprehensive Agreement on Investment (CAI)—the most ambitious agreement that China has ever concluded with a third country.[27] China-EU relations hit a new low point when China refused to condemn Russia's invasion of Ukraine.[28] Systemic rivalry is now at the core of Europe's relationship with China.[29]

This article seeks to engage critically with the narrative that international investment law may impact domestic governance and the rule of law of a nation state. Using China as an example, this article argues that contrary to what was widely expected in the literature, the role of international investment law in advancing the domestic rule of law in China is rather limited. The prevailing narrative was premised on some deeply flawed assumptions of the nature and function of international investment law as well as how international investment law may affect domestic legal change. These assumptions include: (1) IIAs possess the rule of law ideals; (2) powerful investor-state dispute settlement (ISDS) is effective in guarding values of the rule of law; (3) improving good

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[22] Alastair I. Johnson, *The Failures of the 'Failure of Engagement' with China*, 42 WASH. Q. 99, 100 (2019) (stating the argument that engagement with China has failed is increasingly a bipartisan claim in Washington).

[23] *G7 Hiroshima Leaders' Communiqué*, WHITE HOUSE (May 20, 2023), ¶ 51, https://www.whitehouse.gov/briefing-room/statements-releases/2023/05/20/g7-hiroshima-leaders-communique/.

[24] *Remarks by President Biden in a Press Conference in Hiroshima, Japan*, WHITE HOUSE (May. 21, 2023), https://www.whitehouse.gov/briefing-room/speeches-remarks/2023/05/21/remarks-by-president-biden-in-a-press-conference/; *Remarks by National Security Advisor Jake Sullivan on Renewing American Economic Leadership at the Brooking Institution*, WHITE HOUSE (Apr. 7, 2023), https://www.whitehouse.gov/briefing-room/speeches-remarks/2023/04/27/remarks-by-national-security-advisor-jake-sullivan-on-renewing-american-economic-leadership-at-the-brookings-institution/.

[25] Demetri Sevastopulo, *White House Unveils Ban on US investment in Chinese Tech Sectors*, FIN. TIMES (Aug. 9, 2023), https://www.ft.com/content/64ef2042-9ece-4b0c-ad02-184c3454f43b.

[26] *European Commission and the HR/VP contribution to the European Council on EU-China – A Strategic Outlook*, at 1 (Mar. 12, 2019), https://commission.europa.eu/system/files/2019-03/communication-eu-china-a-strategic-outlook.pdf.

[27] Jack Ewing, *European Lawmakers Block a Pact with China, Citing Human Rights Violations*, N.Y. TIMES (May 20, 2021), https://energybuster.com.au/wp-content/uploads/2023/06/New-York-Times-20-May-2021-European-lawmakers-block-a-pact-with-China-citing-human-rights-violations.pdf.

[28] *The Ukraine War Will Define EU- China Relations*, FIN. TIMES (Apr. 5, 2023), https://www.ft.com/content/e94bf5a7-f015-4fd4-a79d-61cc8a67000e.

[29] IAN BOND ET AL., GERMAN INST. INT'L SEC. AFFS., REBOOTING EUROPE'S CHINA STRATEGY 15 (2022).

governance and rule of law is part of the mandate of IIAs; and (4) the state is readily receptive to all direct and indirect influence of economic globalization. A close examination of the limits of IIAs explains why they failed to catalyze the rule of law in China, contrary to what was widely expected.

The rest of this article proceeds as follows. Part II clarifies the concept of rule of law and recaps the theoretical account of the relationship between international investment law and the domestic rule of law. Part III discusses the limits of the development of the rule of law in China over the past two decades. Part IV explains why international investment law only plays a limited role in promoting the rule of law in China. The article concludes with the proposition that linking the rule of law to IIAs does not achieve the touted goal of promoting rule of law. Instead, it may only represent "a typical example in the rule-of-law world of an appealing hypothesis that is repeated enough times until it takes on the quality of a received truth."[30]

I. THE IMPACT OF INTERNATIONAL INVESTMENT LAW ON THE RULE OF LAW

A. Defining the Rule of Law

International law has increasingly prescribed the rule of law as a way of organizing states.[31] However, the rule of law is an "essentially contested concept" subject to a variety of divergent definitions and usages.[32] The precise meaning and content of the rule of law remain deeply ambiguous, and the progress in rule of law performance is difficult to measure.[33]

Theoretical formulations of rule of law can be roughly divided into two general types: formal (thin) and substantive (thick).[34] The formal rule of law focuses on the proper sources and form of legality. It is concerned with the instrumental aspects of the rule of law that a state must possess to effectively function as a system of law. These aspects include the manner in which the law is promulgated, the clarity of the ensuing norms, and the temporal dimension of the enacted norm, i.e., prospective or retrospective.[35] There are different formulations of the formal conception of the rule of law. The most influential

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[30] Thomas Carothers, *The Problem of Knowledge, in* PROMOTING THE RULE OF LAW ABROAD: IN SEARCH OF KNOWLEDGE 15, 23–24 (Thomas Carothers ed., 2006).

[31] André Nollkaemper, *Introduction*, *in* THE RULE OF LAW AT THE NATIONAL AND INTERNATIONAL LEVELS: CONTESTATIONS AND DEFERENCE 1, 5 (Machiko Kanetake & André Nollkaemper eds., 2012).

[32] Margaret Jane Radin, *Reconsidering the Rule of Law*, 69 B.U. L. REV. 781, 791 (1989); Richard H. Fallon, *The Rule of Law as a Concept in Constitutional Discourse*, 97 COLUM. L. REV. 1, 6–7 (1997).

[33] Martin Krygier, *The Rule of Law: Legality, Teleology, Sociology in* RELOCATING THE RULE OF LAW 45 (Gianluigi Palombella & Neil Walker eds., 2009).

[34] BRIAN TAMANAHA, ON THE RULE OF LAW: HISTORY, POLITICS, THEORY 91 (2004); David S. Rubenstein, *Taking Care of the Rule of Law*, 86 GEO. WASH. L. REV. 168, 182 (2018); RANDALL PEERENBOOM, CHINA'S LONG MARCH TOWARDS RULE OF LAW 3 (2002).

[35] Paul Craig, *Formal and Substantive Conceptions of the Rule of Law: An Analytical Framework*, PUB. L. 467 (1997).

articulation, by Lon Fuller, constitutes what he called the "internal morality of law." [36] According to Fuller, characteristics of the formal rule of law include publicity, prospectivity, generality, clarity, consistency, performability, stability over time, and congruity between the rules that are announced and the enforcement of them in actual practice. [37] Fuller's aspirational list of characteristics for the rule of law is not exhaustive. For instance, Joseph Raz advanced a similar set of principles and divided them into two groups: (1) formal standards that provide certainty and predictability to guide action and (2) legal machinery such as an independent judicial system and open and effective law-enforcement agencies to apply the rules with due process, ensuring those standards.[38]

The fundamental feature of the formal conceptions of the rule of law is that it does not seek to pass judgment upon the actual content of the law. The formal rule of law is not concerned with whether the law was in that sense a "good" or "bad" law, provided that the formal precepts of the rule of law were met.[39] In other words, all the basic characteristics of a formal rule of law are consistent with an instrumental view of law—that is, the use of legal rules by a government to achieve whatever substantive ends it chooses.

Thus, the rule of law in its formal conception evaluates systemic virtues of regularity, predictability, and certainty over the concern with substantive justice in particular instances.[40] It is possible for a legal system to comply with the formal conception of the rule of law and still be undemocratic, unjust, and inconsistent with human rights requirements.[41]

Critics of the formal rule of law theories argue that it is devoid of political and economic morality. In the absence of substantive moral content, a formal conception of the rule of law could be used instrumentally by an authoritarian government to strengthen the regime and deprive individuals of their rights.[42] But this would run counter to the long tradition of the rule of law, which has essentially been to protect the rights of citizens from arbitrary infringement from state actors. Under the rule of law, the law constrains all members of society, including government actions.[43] To these critics, a formal conception of the rule of law shares much in common with "rule by law," where the state uses law to control its citizens but prevents the law from being used to control the state

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[36] LON L. FULLER, THE MORALITY OF LAW 44 (1969).

[37] *Id*. at 46–73.

[38] JOSEPH RAZ, THE AUTHORITY OF LAW- ESSAYS ON LAW AND MORALITY 214–19 (1979).

[39] Craig, *supra* note 35, at 467.

[40] Allan C. Hutchinson, *The Rule of Law Revisited: Democracy and Courts, in* RECRAFTING THE RULE OF LAW: THE LIMITS OF LEGAL ORDER 196, 199 (David Dyzenhaus ed., 1999).

[41] Raz, *supra* note 38, at 211.

[42] Peerenboom, *supra* note 34, at 69.

[43] Nicolas Fegen, *Thick or Thin? Defining Rule of Law: Why the "Arab Spring" Calls for a Thin Rule of Law Theory*, 80 UMKC L. REV. 1187, 1197 (2012).

itself.[44] There is no guarantee that the formal conception of the rule of law will change the life of society members for the better. As one theorist argues, "a state which savagely represents or persecutes sections of its people does not genuinely follow the rule of law simply because it undertakes those acts according to detailed laws duly enacted and scrupulously observed."[45]

Still, even a formal conception of the rule of law has many important virtues. It provides some protection of individual rights and freedoms by promising at least some degree of predictability of how citizens should plan their actions and imposing some constraint on how states wield their power. As Neil MacCormick observed:

> There is always something to be said for treating people with formal fairness, that is, in a rational and predictable way, setting public standards for citizens' conduct and officials' responses thereto, standards with which one can choose to comply or at least by which one can judge one's compliance or non-compliance, rather than leaving everything to discretionary and potentially arbitrary decision . . . This has real value, and independent value, even where the substance of what is done falls short of any relevant ideal of substantive justice.[46]

In view of the criticisms levelled at formal legality as "an impoverished account of the rule of law,"[47] some scholars espouse a thick, substantive approach to defining rule of law that attempts to provide additional normative elements of political morality or justice to the formal aspects of the rule of law. They argue that certain substantial rights are based on, or derived from, the rule of law. To these scholars, the rule of law is used as the foundation for those rights, which are then used to distinguish between "good" laws which comply with these rights and "bad" laws which do not.[48] For example, the United Nations defines the rule of law as follows:

> A principle of governance in which all persons, institutions and entities, public and private, including the State itself, are accountable to laws that are publicly promulgated, equally enforced and independently adjudicated, and *which are consistent with international human rights norms and standards*. It requires, as well, measures to ensure adherence to the principles of supremacy of law, equality before the law, accountability to the law, fairness in the application of the law,

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[44] Jeremy Waldron, *Rule by Law: A Much-Maligned Proposition* 3-4 (N.Y.U Sch. L. Pub. L. & Legal Theory Rsch. Paper Series, Working Paper No.19-19, 2019).

[45] TOM BINGHAM, THE RULE OF LAW 67 (2011).

[46] Neil MacCormick, *Natural Law and the Separation of Law and Morals, in* NATURAL LAW THEORY: CONTEMPORARY ESSAYS 105, 123 (Robert P. George ed., 1992).

[47] Jeremy Waldron, *The Concept and the Rule of Law*, 43 GA. L. REV. 1, 61 (2008).

[48] Craig, *supra* note 35 at 467.

> separation of powers, participation in decision-making, legal certainty, avoidance of arbitrariness and procedural and legal transparency.[49]

The UN definition is but one among many competing substantive conceptions of the rule of law. Despite their differences, all substantive conceptions of the rule of law seek to impose normative and political theories pertaining to the relationship between the state and a legal system. For example, within Western liberal democracies, the most common substantive version includes democracy and individual rights within the rule of law.[50] Other versions include freedom, equality, dignity, fairness, free market capitalism, and even various social welfare rights to establish necessary social, economic, educational, and cultural conditions.[51]

However, despite the desirability of these substantive elements of the rule of law, they cannot be justified as the necessary or inherent meaning of the rule of law but only a collective understanding within Western societies. Moreover, there are potential clashes among the variegated substantive rule of law attributes advocated, such as conflicts among individual rights and between individual rights and democracy.[52] It is precisely because substantive theories of the rule of law require "a complete moral and political philosophy," as Raz argued, that they present particular challenges to cross-cultural dialogues. This is due to cultural differences between nations and across regions, as well as among individuals with different political persuasions.[53] This challenge explains why the World Bank and other development agencies are more likely to employ a formal conception of the rule of law in their development aid activities.[54]

In summary, it is too simplistic to suggest an overarching coherence to the rule of law concept. At its core, the rule of law requires not only formal legality, or the thin conception of the rule of law, but also the notion that the state and its officials must operate within a limiting framework of the law. In this respect, rule of law is distinct from rule by law. Moreover, in addition to the requirement that government officials abide by the currently valid positive law, there are legal limits on the government's law-making power so that the state cannot mold the positive law to its will. While divine law or "natural law" provided the limits in the past, human rights declarations are said to be the common phraseology in Western liberal societies today.[55]

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[49] U.N. Secretary-General, *Rule of Law and Transitional Justice in Conflict and Post-Conflict Societies*, ¶ 6, U.N. Doc. S/2004/616 (Aug. 23, 2004).

[50] Tamanaha, *supra* note 34, at 110–12;

[51] RONALD DWORKIN, LAW'S EMPIRE 407–10 (1986); Peerenboom, *supra* note 34, at 75–80.

[52] Tamanaha, *supra* note 34, at 113.

[53] *See generally* Ruti Teitel, *Global Rule of Law: Universal and Particular, in* HUMAN RIGHTS WITH MODESTY – THE PROBLEM OF UNIVERSALISM 231–47 (Andras Sajo ed., 2004).

[54] Lawrence Tshuma, *The Political Economy of the World Bank's Legal Framework for Economic Development*, 8 SOC. & LEGAL STUD. 75, 83 (1999).

[55] Tamanaha, *supra* note 34, at 118.

B. How does International Investment Law Impact Domestic Rule of Law?

The conventional account of how international investment law may have a positive impact on domestic rule of law has been extensively outlined in the literature.[56] According to those accounts, international investment law can contribute to domestic rule of law both directly and indirectly. The direct contribution of international investment law derives from the fact that the purpose and norms of IIAs embody core rule of law requirements.[57]

First, a stable and predictable legal system is a hallmark of the rule of law.[58] The primary function of IIAs is precisely to provide a stable and predictable legal framework for investment.[59] In other words, the very existence of the IIA regime evinces a concern for ensuring the presence of the rule of law.

Second, the content of IIAs embodies key rule of law values. FET, a core investment law concept in all modern IIAs likely to be found in all investment disputes, was said to offer the best example for the interlinkage of investment protection and the rule of law.[60] Schill identifies seven rule of law requirements that emerged in investment arbitral awards on FET, all of which figure prominently as expressions of the broader concept of the rule of law in domestic legal systems: (1) the requirement of stability, predictability, and consistency of the legal framework; (2) the principle of legality; (3) the protection of legitimate expectations; (4) procedural due process and denial of justice; (5) substantive due process and protection against discrimination and arbitrariness; (6) transparency; and (7) the principle of reasonableness and proportionality.[61] These developments have also been codified in the new generation of IIAs, such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), United States-Mexico-Canada Agreement (USMCA), and the Canada-EU Comprehensive Economic and Trade Agreement (CETA). The transformation of the rule of law principles into concrete and enforceable investment rules whose breach can entail costly consequences upholds the rule of law in host states.[62] Third, access to justice is a vital component of the rule of law. ISDS has arguably the strongest rights enforcement mechanism existing in international law.[63] It improves access to justice for foreign investors by enabling them to bring an arbitral proceeding against a State, generally without having to

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[56] Kingsbury & Schill, *supra* note 7, at 16–17; Benjamin K. Guthrie, *Beyond Investment Protection: An Examination of the Potential Influence of Investment Treaties on Domestic Rule of Law*, 45 N.Y.U. J. INT'L. L. & POL. 1151, 1186-1200 (2013).

[57] Schill, *supra* note 4, at 157–59.

[58] Waldron, *supra* note 44, at 7.

[59] KENNETH VANDEVELDE, BILATERAL INVESTMENT TREATIES: HISTORY, POLICY, AND INTERPRETATIONS 2–3 (2010).

[60] VELIMIR ŽIVKOVIĆ, FAIR AND EQUITABLE TREATMENT AND THE RULE OF LAW 1–2 (2023).

[61] Schill, *supra* note 4, 159–171.

[62] Živković, *supra* note 6, at 522–24.

[63] Beth A. Simmons, *Bargaining Over BITs, Arbitration Awards: The Regime for Protection and Promotion of International Investment*, 66 WORLD POL. 12, 17 (2014).

go first through the host state's domestic courts.[64] The potentially outsized liability for breaching the rule of law requirements embodied in IIAs forces host states to internalize and implement their international investment law obligations. The rule of law in host states is improved accordingly.[65]

More significant than international investment law's direct contribution to domestic rule of law, its indirect social, legal, and political implications trigger broader regulatory changes and nurture a rule of law culture in host states. The rise of neoliberalism since the late 1970s has had a profound impact on international investment law. Neoliberalism has seen markets as optimally efficient means of organizing economies and state intervention as disturbing the natural tendency for competition, specialization, trade, and investment to generate economic growth.[66] As neoliberalism has become the dominant ideology in guiding the conclusion and interpretation of IIAs, IIAs have become a channel through which neoliberal commitments are formalized and key norms of free markets and good governance are learned and internalized. Consequently, international investment law could trigger broader regulatory changes that permeate the state, including changes in national law and practice; changes in the boundary between the market and the state; changes in the relative authority of institutions within the state; changes in professional expertise engaging with state regulation (such as the role of lawyers); and changes in normative frames and accountability mechanisms for national regulation.[67]

In addition, IIA disciplines represent the rule of law in international investment. The implementation of IIA disciplines creates a "spill over" effect on a host state's legal system as the host state gradually develops better rule-oriented governance practices to comply with IIA disciplines.[68] In the end, domestic firms and citizens will benefit from the halo effect provided by stronger constraints on arbitrary government action.[69] Seen from this perspective, the integration of China into the liberal international economic order is part of a larger strategy of massive and fundamental economic and socio-legal reform in China.

The idea that international economic norms profoundly impact or even transform state behavior has a distinguished intellectual tradition in social sciences. For instance, the constructivist theory contends that state identity and state interests are defined by forces unleashed by the norms of behavior embedded in international society.[70] International norms can teach states what their interests should be, decisively influence national policies by pushing states

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[64] Francesco Francioni, *Access to Justice, Denial of Justice, and International Investment Law*, 20 EUR. J. INT'L L. 729, 731–32 (2009).

[65] Kingsbury & Schill, *supra* note 7, at 16–17.

[66] JAMIE PECK, CONSTRUCTIONS OF NEOLIBERAL REASON (2010) (neoliberalism is the philosophical view that a society's political and economic institutions should be robustly liberal and capitalist but supplemented by a constitutionally limited democracy and a modest welfare state).

[67] Shaffer, *supra* note 14, at 2; Steinberg, *supra* note 14, at 187–90.

[68] Echandi, *supra* note 8, at 13–14.

[69] World Bank, *supra* note 13, at 179.

[70] MARTHA FINNEMORE, NATIONAL INTERESTS IN INTERNATIONAL SOCIETY 2 (1996).

to adopt these norms and help them learn good behavior in international society.[71] Therefore, the concomitant myriad of interests and interactions will entangle China in a dense mesh of rules, norms, multilateral regimes, and procedures that will inevitably turn it into a stakeholder of the existing rule-based, institutionalized and normative liberal international economic order.[72] From this perspective, IIAs could help socialize China to conform to global legal norms in the same manner as China's behavioral change in the WTO dispute settlement system.[73] Similarly, the new institutional economics school has long argued that IIAs could facilitate the development of market economies and provide member states "policy anchoring" to improve good governance.[74] A flourishing market economy requires not only physical facilities but also the rule of law.[75] The desire for fast economic growth requires a national government to create the framework of rules and institutions and to develop a judicial branch capable of enforcing binding legal rules. Otherwise, the state risks the loss of international capital and significant foreign trade.[76] Once a state has committed to provide foreign investors standard rule of law protection, it will be difficult for it to renege on its commitments without incurring considerable political and economic costs. Reform-minded leaders could then wield the IIAs as an external force to lock in and further domestic economic and political reforms.[77] In conclusion, the argument that international investment law may have a positive impact on domestic rule of law is well established in the existing theories.

II. THE RULE OF LAW DEVELOPMENT IN CHINA: FROM THEORY TO PRACTICE

It is well known that the rule of law has been weak in traditional Chinese legal culture. The two dominant intellectual traditions of Confucianism and legalism

[71] ALEXANDER WENDT, SOCIAL THEORY OF INTERNATIONAL POLITICS 317 (1999).

[72] ALISTAIR IAIN JOHNSON, SOCIAL STATES: CHINA IN INTERNATIONAL INSTITUTIONS 1980-2000 27 (2008); Jeffery T. Checkel, *International Institutions and Socialization in Europe: Introduction and Framework*, 59 INT'L ORG. 801, 804–05 (2005).

[73] Xiaojun Li, *Understanding China's Behavioral Change in the WTO Dispute Settlement System*, 52 ASIAN SURV. 1111, 1128–35 (2012).

[74] Susan Ariel Aaronson & M. Rodwan Abouharb, *Does the WTO Help Member States Improve Good Governance*?, 13 WORLD TRADE REV. 547, 549 (2014) (arguing that empirical evidence provides support for the hypothesis that the norms of good governance promoted by the WTO transcend the trade sphere and affect the country's approach to governance in general); Michael J. Ferrantino, *Policy Anchors: Do Free Trade Agreements and WTO Accessions Serve as Vehicles for Developing Country Reform*? 3 (U.S. Int'l Trade Comm'n Off. Econ., Working Paper No. 2006-04-A, 2006).

[75] RONALD H. COASE, THE FIRM, THE MARKET, AND THE LAW 10 (1988).

[76] Dominic Grieve, Speech at City of London Guildhall: The Value of the Rule of Law to International Trade and Finance (Oct. 15, 2013) (transcript available at https://www.gov.uk/government/speeches/the-value-of-the-rule-of-law-to-international-trade-and-finance); Liu Wujun (刘武俊), *Shenke Lijie Shichang Jingji shi Fazhi Jingji* (深刻理解市场经济是法治经济) [Deep Understanding of Market Economy as Rule of Law Economy], PEOPLE'S DAILY (人民日报) (July 2, 2012), http://www.npc.gov.cn/zgrdw/npc/xinwen/rdlt/sd/2012-07/02/content_1728672.htm

[77] Jappe Eckhardt & Hongyu Wang, *China's New Generation Trade Agreements: Importing Rules to Lock in Domestic Reforms*, 15 REGUL. & GOVERNANCE 581, 584–85 (2021).

are more accommodating to the notion of "rule by man" and "rule by law," respectively.[78] In particular, law was traditionally viewed as an instrument of governance for rulers to impose their will on the people and not something that protected the weak individual from the state. This is fundamentally different from the Western notion of the rule of law, in which law has the capacity to restrain government behavior.[79]

A. Formal Rule of Law in China

How should we evaluate the progress of China's long march toward the rule of law? To begin with, law has been playing an increasingly significant role in supporting economic development and preserving social order in contemporary China. China has advanced from "rule by law" in the imperial period and the Mao era and has been transitioning toward at least a "thin" or "formal" version of the rule of law.[80] This is particularly true horizontally. Unlike the vertical rule of law, which addresses the public or administrative aspect of governance, the horizontal rule of law addresses the relationships among private entities, such as commercial laws, excluding state and party-related entities.[81] Taking a horizontal perspective, "there is an ever-increasing emphasis on the internationalization of legal standards and rule-based governance in China."[82] The Chinese government's proclamation that it is committed unwaveringly to pushing forward the project of "ruling the country according to law" has sparked much enthusiasm for observers who emphasize the formality of the Chinese legal system and its effective implementation through concrete legislative, administrative, and judicative institutions.[83]

Even if the dense IIA networks have had a positive impact on the formal rule of law in China, such impact is far more limited than conventionally assumed. The Chinese government's conception of law is still highly instrumentalist in the sense that law in China is merely a tool to maintain the power of the ruling Chinese Communist Party (CCP) and stabilize society.[84] Even worse, the formal version of the rule of law is only partially achieved in China with varying degrees of adherence in different regions and domains. It

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[78] Qiang Fang & Roger Des Forges, *Were Chinese Rulers Above the Law? Toward a Theory of the Rule of Law in China from Early Times to 1949 CE*, 44 STAN. J. INT'L L. 101, 103 (2006).

[79] *See* Benedict Sheehy, *Fundamentally Conflicting Views of the Rule of Law in China and the West and Implications for Commercial Disputes*, 26 NW. J. INT'L L. & BUS. 225, 245 (2006).

[80] *See* Zhang Taisu & Tom Ginsburg, *China's Turn Toward Law*, 59 VA. J. INT'L L. 306, 348 (2019). For an explanation of "formal" or "thin" version of the rule of law, *see supra* Part II.A.

[81] *See* Martin Kwan, *China's Rule of Law Development: The Increasing Emphasis on Internationalization of Legal Standards and the Horizontal Rule of Law*, 53 N.Y.U. J. INT'L. L. & POL. ONLINE 51, 53 (2021).

[82] *Id.*

[83] WANG, *supra* note 19, at 3–4; Randall Peerenboom, *Fly High the Banner of Socialist Rule of Law with Chinese Characteristics: What Does the 4th Plenum Decision Mean for Legal Reforms in China*?, 7 HAGUE J. RULE L. 49, 63–71 (2015).

[84] *See* Susan Trevaskes, *A Law Unto Itself: Chinese Communist Party Leadership and Yifa zhiguo in the Xi Era*, 44 MOD. CHINA 347, 367 (2018) (arguing that law can be effective only through strong and moral party leadership).

remains the case that law and legal procedure are sometimes used selectively and inconsistently in China.[85] Examples include the persistence of shuanggui;[86] interception of petitioners; local policy experimentation; and crackdown on lawyers, journalists, religious believers, and civil society activists.[87] Some even argue that China is moving away from the rule of law because it does not comply with core elements such as the separation of powers, the supremacy of law, an independent judiciary, and the protection of human rights.[88]

In the domain of foreign investment, China committed in the WTO accession agreement to apply, implement, and administer its laws, regulations, and other measures uniformly, impartially, and reasonably at all levels of government.[89] This commitment to uniform administration is significant because, if successful, it could reduce a major obstacle—local and departmental protectionism—strengthening at least a formal conception of the rule of law in China.[90] Nevertheless, foreign investors continue to voice concerns about inconsistent enforcement of laws and regulations in different areas including customs trade administration, taxation, investment, and intellectual property rights.[91] One example is China's alleged selective enforcement of the Anti-Monopoly Law (AML). China has used AML against foreign companies in merger reviews to advance China's industrial policy goals and boost national champions, whilst the law has rarely been applied to powerful Chinese state-owned enterprises (SOEs). In fact, a review of China's AML enforcement activities since the law took effect in 2008 shows that all transactions blocked or conditionally approved to date have involved foreign companies.[92] Moreover, China applies the AML in ways that are openly discriminatory against foreign firms, forcing them to sell assets to China's SOEs or to provide Chinese domestic firms access to technology (intellectual property) at below market rates.[93]

Chinese courts' lack of independence is another symptom of the weak rule of law in China. Independent courts are widely considered "emblematic of a

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[85] *See* Hualing Fu, *Duality and China's Struggle for Legal Autonomy*, 116 CHINA PERS. 3, 4–5 (2019); Kwai H. Ng, *Is China a "Rule-by-Law" Regime*?, 67 BUFF. L. REV. 793, 797–809 (2019).

[86] "Shuanggui" refers to a practice whereby the CCP disciplinary authorities—not state authorities—coercively detain Party members (sometimes even non-party members) for investigation, typically on suspicion of corruption. There is wide agreement that "Shuanggui" is illegal as a matter of formal law in China. *See* Donald Clarke, *Order and Law in China*, 2022 U. ILL. L. REV. 541, 564–76.

[87] *Id.*

[88] *See generally* KATRIN BLASEK, RULE OF LAW IN CHINA: A COMPARATIVE APPROACH (2015); Carl Minzner, The Great China Crackdown is Here (and Why You Should Worry), Nat'l Interest (Apr. 25, 2016), https://nationalinterest.org/blog/the-buzz/the-great-china-crackdown-here-15915.

[89] *See* Ming Du & Qingjiang Kong, *Explaining the Limits of the WTO in Shaping the Rule of Law in China*, 23 J. INT'L ECON. L. 885, 896 (2020).

[90] *See* Stanley Lubman, *A Key Move to Protect Courts in China*, WALL ST. J. (July 30, 2014), https://www.wsj.com/articles/BL-CJB-23364.

[91] *See* U.S. TRADE REP., 2019 REPORT TO CONGRESS ON CHINA'S WTO COMPLIANCE A-118 (2020).

[92] *See* U.S. CHAMBER OF CONG., COMPETING INTERESTS IN CHINA'S COMPETITION LAW ENFORCEMENT: CHINA'S ANTI-MONOPOLY LAW APPLICATION AND THE ROLE OF INDUSTRIAL POLICY 2 (2014).

[93] *See* Daniel C.K. Chow, *China's Enforcement of Its Anti-Monopoly Law and Risks to Multinational Companies*, 14 SANTA CLARA J. INT'L L. 99, 104–05 (2016).

commitment to the rule of law."[94] Chinese courts have come a long way in their reforms.[95] The Chinese government has made substantial efforts to improve judicial professionalism, make the rule of law more transparent, take meddling by local officials out of the judicial process, improve the fairness of judicial decisions, and ensure better implementation of laws.[96] However, Chinese judges continue to be influenced by political, governmental, or business pressures, especially outside of China's major cities.[97] In particular, the CCP has serious concerns about the independence of China's judiciary. Ample evidence shows that despite all the reforms, the party retains systematic and structural control over the courts. The party has the power to command courts to develop judicial policies consistent with its political objectives and to instruct courts regarding specific decisions in individual cases, or categories of cases, that the party deems important.[98] Chief Justice Zhou Qiang, China's top judicial official, publicly denounced the idea of an independent judiciary and warned judges not to fall into the "trap" of "Western" ideology in 2017.[99] Consequently, though judicial power in China is separate from other state powers, it is always a pliant agent to the supreme power of the CCP. Indeed, as President Xi Jinping stated unequivocally, the "cornerstone" of socialist rule of law with Chinese characteristics is the leadership of the CCP.[100] Discussion of judicial independence from the party at the central level is currently a forbidden subject in China.[101] If judicial independence is the hallmark of the rule of law, then China certainly falls short of the rule of law requirements.

B. Substantive Rule of Law in China

It is fair to say that China has gradually moved away from a purely formal conception of the rule of law toward a substantive conception where law is meant to protect human rights and binds not only citizens but also government officials

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[94] Ratna Rueban Balasubramaniam, *Judicial Politics in Authoritarian Regimes*, 59 U. TORONTO L. J. 405, 405 (2009).

[95] *See* Information Office of the State Council, *Judicial Reform in China* (Oct. 2012), http://www.scio.gov.cn/zfbps/ndhf/2012n/202207/t20220704_130083.html

[96] Recent significant reforms in the Xi Jinping era include centralization of control over court finances and personnel, professionalisation of the judiciary, creation of circuit courts of appeal delinked from provinces and localities, and lifetime responsibility of judges for errors in decisions. *See* Ernest Liu et al., *Judicial Independence, Local Protectionism, and Economic Integration: Evidence from China* 8–9 (Nat'l Bureau of Econ. Rsch., Working Paper No. 30432, 2022).

[97] *See* U.S. TRADE REP., *supra* note 91, at A-118.

[98] *See* Ling Li, *The Chinese Communist Party and People's Courts: Judicial Independence in China*, 64 AM. J. COMP. L. 37, 72 (2016).

[99] Michael Forsythe, *China's Chief Justice Rejects an Independent Judiciary, and Reformers Wince*, N.Y. TIMES (Jan. 18, 2017), https://www.nytimes.com/2017/01/18/world/asia/china-chief-justice-courts-zhou-qiang.html.

[100] Jamie P. Horsley, *Party Leadership and Rule of Law in the Xi Jinping Era,* BROOKINGS INST. 1 (Sept. 2019), https://www.brookings.edu/articles/party-leadership-and-rule-of-law-in-the-xi-jinping-era/.

[101] *See* Jerome A. Cohen, *A Looming Crisis for China's Legal System*, FOREIGN POL'Y (Feb. 22, 2016), https://foreignpolicy.com/2016/02/22/a-looming-crisis-for-chinas-legal-system/.

and the party.[102] However, it remains true that, although legal reforms in service of China's economic development are taken seriously, similar formal commitments to more democratic governance, protection of individual civil and political rights, and effective control of the state and its actors are largely empty words. Pils suggests that even if China has shown progress extending some form of governance by law, its system cannot be described as rule of law because the rule of law has not penetrated politically sensitive domains where the party's important interests are at stake.[103] In this sense, the rule of law in China is still a "bird in a cage" due to various institutional, cultural, and ideological limitations.[104]

The impact of IIAs on the substantive rule of law in China is even more limited. The ultimate goal of China's rule of law is not the same as understood in the West, but rather a socialist rule of law with Chinese characteristics, which seeks to repurpose Western law and institutions.[105] As Ye argues, "China's journey towards the rule of law is one in which China becomes more confident in using sophisticated legal tools to achieve its goals; it is also one in which China travels further away from the Western rule of law."[106] China shows no intent of incorporating Western rule of law concepts such as separation of powers, human rights, and democracy.[107] Even optimistic observers of China's rule of law project would agree, to the extent one expects to see profound indirect impact of WTO membership in terms of moving China towards a Western style liberal democratic version of rule of law, that hope was completely dashed.[108] The World Justice Project's Rule of Law Index ranked China 97 out of 140 jurisdictions in its 2023 report.[109] China scored significantly higher in many economic categories than it did in political ones.[110] It remains true that advocacy for the rule of law cannot be used to undermine the CCP's monopoly of power in China.[111] Given China's current authoritarian party-state regime, the possibility of adopting a liberal democratic version of the rule of law in China in the near

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[102] *See* Jianfu Chen, *The Transformation of Chinese Law: From Formal to Substantial*, 37 H.K. L. J. 689, 735–36 (2007).

[103] *See generally* EVA PILS, CHINA'S HUMAN RIGHTS LAWYERS: ADVOCACY AND RESISTANCE (2015).

[104] *See* Stanley Lubman, *Bird in a Cage: Chinese Law Reform After Twenty Years*, 20 NW. J. INT'L L. & BUS. 383, 389–410 (2000).

[105] *See* Clarke, *supra* note 86, at 556–57.

[106] Ruiping Ye, *Shifting Meanings of Fazhi and China's Journey Toward Socialist Rule of Law*, 19 INT'L J. CONST. L. 1859, 1861 (2021).

[107] *See* Tom Ginsburg, *Authoritarian International Law*? 114 AM. J. INT'L. L. 220, 255-256 (2022); Eva Pils, *Autocratic Challenges to International Human Rights Law: A Chinese Case Study*, 75 CURR. LEG. PROBL. 189, 191-192 (2022).

[108] *See* Albert H.Y. Chen, *China's Long March Towards Rule of Law or China's Turn Against Law*?, 4 CHINESE J. COMP. L. 1, 10–11 (2016); Ji Li, *The Evolving Rule of Law with Chinese Characteristics and Its Impacts on the International Legal Order*, 8 UCI J. INT'L, TRANSNAT'L & COMPAR. L. 151, 158-161 (2023).

[109] *See* WORLD JUSTICE PROJECT, WORLD JUSTICE PROJECT RULE OF LAW INDEX 2023 64 (2023), https://worldjusticeproject.org/rule-of-law-index/downloads/WJPIndex2023.pdf.

[110] *Id*.

[111] *See generally* Horsley, *supra* note 100.

future is dim. Any legal reforms that are designed to challenge the CCP's grip on power are set up to fail.

III. EXPLAINING THE TENUOUS NEXUS BETWEEN INTERNATIONAL INVESTMENT LAW AND THE RULE OF LAW

A. Does International Investment Law Possess the Rule of Law Ideals?

Were international investment law to instill in host states a sense of the rule of law in host states, one would expect international investment law, itself, to comply with the rule of law ideals. A failure to do so would undermine the credibility of its external rule of law policies.[112] That is, if international investment law holds host states to stringent standards of conduct, such as the duty to maintain transparency, stability, consistency, and predictability, international investment law should also similarly embody these qualities.[113] However, as discussed below, international investment law does not necessarily possess rule of law characteristics. Thus, its capacity to induce host states to adopt rule of law domestically is uncertain.

International investment law, in its current form, lacks some of the vital characteristics necessary to fulfill its promise to transform domestic governance in host states.[114] First, because rules governing investor-state arbitration were designed for the resolution of commercial disputes, ISDS has placed a strong emphasis on privacy and confidentiality in arbitral proceedings.[115] For instance, the investment arbitration rules have long favored the exclusion of third parties from participating in the proceedings and precluded awards from being published without the parties' consent.[116] Confidentiality and privacy may be appropriate for purely private commercial disputes.[117] But investor-state arbitration is not strictly private or commercial: states frequently pursue legitimate public policy objectives such as the protection of environmental and human rights.[118] Investment arbitration "often involves the regulation of governmental actions,

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[112] *See* MICHAEL ZÜRN, ANDRÉ NOLKAEMPER & RANDALL PEERENBOOM, RULE OF LAW DYNAMICS IN AN ERA OF INTERNATIONAL AND TRANSNATIONAL GOVERNANCE 308 (2012).

[113] SATTOROVA, *supra* note 3, at 125–26.

[114] *See* Martti Koskenniemi, *It's not the Cases, It's the System*, 18 J. WORLD INV. & TRADE 343, 351 (2017); Gus Van Harten, *Investment Treaty Arbitration, Procedural Fairness, and the Rule of Law*, *in* INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 627, 627–57 (Stephan Schill ed., 2010)

[115] *See* Alessandra Asteriti & Christian J. Tams, *Transparency and Representation of the Public Interest in, Investment Treaty Arbitration, in* INTERNATIONAL INVESTMENT LAW AND COMPARATIVE PUBLIC LAW 787, 789-91 (Stephan W. Schill ed., 2010).

[116] *See* Org. for Econ. Co-operation and Dev., *Transparency and Third-Party Participation in Investor-State Dispute Settlement Procedures* 2–4, OECD Working Papers on International Investment 2005/01 (June 2005).

[117] Alexis C. Brown, *Presumption Meets Reality: An Exploration of the Confidentiality Obligation in International Commercial Arbitration*, 16 Am. U. Int'l. L. Rev. 969, 972-74 (2001).

[118] Crina Baltag, Riddhi Joshi & Kabir Duggal, *Recent Trends in Investment Arbitration on the Right to Regulate, Environment, Health, and Corporate Social Responsibility: Too Much or Too Little*? 38 ICSID REV. 381, 382-83 (2023).

and its effects can often ripple far beyond the instant dispute."[119] In these settings, confidentiality and privacy may actually undermine the legitimacy of investor-state arbitration.[120] In response to growing concerns about ISDS's lack of transparency, there has been a move towards promoting greater transparency and public participation in investment arbitration. The adoption of the United Nations Commission on International Trade Law (UNCITRAL) Rules on Transparency in Treaty-based ISDS and the subsequent opening for signature of the Mauritius Convention on Transparency illustrate this point.[121] Despite the recent reforms, the investment treaty regime continues to fall below the benchmark of transparency which host states are expected to comply with when dealing with foreign investors.[122] Enhancing transparency of investment treaty law is currently considered "perhaps the single most important avenue for bringing the system more into line with principles of democratic governance under the rule of law."[123]

Furthermore, both IIAs and ISDS have been strongly criticized for lack of clarity, consistency, and predictability.[124] Substantial rules in IIAs are typically brief and written at a high level of generality. Inevitably, the succinct and abstract formulation of substantive protections gives arbitral tribunals considerable interpretative discretion.[125] Coupled with the absence of a rule of binding precedent and the lack of an appeals mechanism, arbitral tribunals periodically issue inconsistent awards with respect to the interpretation and application of similar, if not identical, provisions in IIAs. For instance, several arbitral awards dealt with the necessity defense raised by Argentina in disputes following its 2001 economic crisis. Notwithstanding almost identical circumstances and the fact that all disputes were based on the same IIAs, the disputes were decided in irreconcilable ways.[126] Thus ISDS has produced a piecemeal jurisprudence that is difficult for investors and states to decipher and develop an ex-ante understanding of the law.[127] Clarity, consistency and predictability are essential rule of law requirements. If a host state does not know what type of conduct may be considered a breach of an IIA, then how can it internalize investment treaty

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[119] Sundaresh Menon, *A Tale of Two Systems: The Public and Private Faces of Investor-State Dispute Settlement*, 37 ICSID REV. 619, 621 (2022).

[120] *See* Asteriti & Tams, *supra* note 115, at 791-92.

[121] *See* Lise Johnson, *The Transparency Rules and Transparency Convention: A Good Start and Model for Broader Reform in Investor-State Arbitration*, 126 COLUM. FDI PERSPS. 1 (2014).

[122] *See id.* at 1–2.

[123] Stephan W Schill, *Editorial: Five Times Transparency in, International Investment Law*, 15 J. WORLD INV. & TRADE 363, 364 (2014).

[124] *See* Susan Franck, *The Legitimacy Crisis in Investment Treaty Arbitration: Privatising Public International Law Through Inconsistent Decisions*, 73 FORDHAM L. REV. 1521 (2005).

[125] STEVEN R. RATNER, THE THIN JUSTICE OF INTERNATIONAL LAW: A MORAL RECKONING OF THE LAW OF NATIONS 350 (2015).

[126] Giovanni Zarra, *The Issue of Incoherence in Investment Arbitration: Is there Need for a Systemic Reform*?, 17 CHINESE J. INT'L L. 137, 141 (2018).

[127] N. Jansen Calamita, *The (In)Compatibility of Appellate Mechanisms with Existing Instruments of the Investment Treaty Regime*, 18 J. WORLD INV. & TRADE 585, 587 (2017).

prescriptions of the rule of law requirements and organize its regulatory and administrative decision-making processes in a way that ensures its conduct will not incur liability under the IIA? Indeed, the lack of clarity, consistency, and predictability of investment treaty law is antithetical to the rule of law.

Moreover, while one key assumption of international investment law and the rule of law nexus theory is that foreign investors exert positive influence on domestic governance, there is ample evidence demonstrating that foreign investors are just as likely to entrench poor governance practices in a host state. This is evident through their contribution to normalizing corruption, bribery, regulatory capture, and other forms of illegal acts.[128] In particular, foreign investors may no longer be portrayed merely as victims of host state corruption. Rather than countering corruption in host states, foreign investors have been known to find "unclear legislation and a weak, opaque, unpredictable and corrupt system were at times highly desirable."[129] By supplying bribes, foreign investors may have contributed to the worsening of an already weakened governance in host states. If investment treaty instruments and the arbitral tribunals applying them turn a blind eye to illegal actions committed by foreign investors in host states, it is hardly plausible that they could instill confidence in international investment law as a force for positive change in the rule of law at the national level.[130]

Regrettably, the asymmetrical structure of the international investment regime is designed to redress the mistreatment of foreign investors, not foreign investors' wrongdoings.[131] Some arbitral tribunals have creatively resorted to treaty provisions that investments made in breach of domestic laws of the host state ought not to benefit from IIA protection to fill the void.[132] However, other arbitral tribunals have not been prepared to consider the relevance of investor misconduct in determining the outcome of investor-state disputes.[133] The failure to address the lack of investor accountability in IIAs is at odds with the investment treaty regime's proclaimed commitment to the ideals of rule of law and good governance.

Finally, the IIA system results in unwarranted discrimination of national investors and other members of society at domestic level. For example, special forums for resolving investor-state disputes are made de facto available only to wealthier foreign investors.[134] Rather than enhancing the rule of law in host countries, outsourcing investment disputes to international arbitral tribunals

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[128] ALOYSIUS P. LLAMZON, CORRUPTION IN INTERNATIONAL INVESTMENT ARBITRATION 100 (2014).

[129] John Hewko, *Foreign Direct Investment: Does the Rule of Law Matter?* 10 (Carnegie Endowment for Int'l Peace: Rule L Series, Working Paper No. 26, 2002).

[130] SATTOROVA, *supra* note 3, at 154.

[131] Jean Ho, *The Creation of Elusive Investor Responsibility*, 113 AM. J. INT'L L. UNBOUND 10, 10–15 (2019).

[132] Stephan W. Schill, *Illegal Investments in Investment Treaty Arbitration*, 11 L. & PRAC. INT'L CTS. & TRIBUNALS 281, 301–02 (2012).

[133] SATTOROVA, *supra* note 3, 156–60.

[134] Anil Yilmaz Vastardis, *Justice Bubbles for the Privileged: A Critique of the Investor-State Dispute Settlement Proposals for the EU's Investment Agreements*, 6 LONDON REV. INT'L L. 279, 286 (2018).

might undermine the quality of the local legal system. Because, if governments and foreign investors can turn to external sources of dispute resolution, then there is little incentive to make marginal investments in improving local judicial quality.[135]

In summary, international investment law itself may fall short of the rule of law benchmark of consistency, clarity, transparency, and predictability. In addition, the asymmetric structure of international investment regime idealizes the positive role of foreign investors in promoting the rule of law in host states. This in turn calls into question to what extent international investment law can instill in host states a sense of the rule of law.

B. The Limited Mandate of Chinese International Investment Agreements

Despite enthusiasm about the direct and potential role of international investment law in improving the rule of law, international investment law does not say much about the rule of law at the national level. This is particularly the case in China. As will be discussed below, there are four reasons accounting for Chinese IIAs' limited impact on the rule of law in China: (1) the nature of modern IIAs; (2) IIAs do not automatically have domestic legal effects in China; (3) the limited scope of Chinese IIAs; and (4) the lack of empirical evidence that China has internalized the international investment law norms.

Since their inception, IIAs have always been about promoting international investment and economic growth through protection of foreign investments against expropriation and regulatory uncertainty in host countries.[136] For that purpose, IIAs typically specify standards of treatment for foreign investors and provide for extra-jurisdictional dispute resolution and enforcement, lowering the risk of bias in the host state jurisdiction. More recent IIAs go further to require substantial liberalization, for example, by requiring market access and prohibiting technology transfer, as well as provisions on environment, labor protection, and sustainable development.[137] Although IIAs may have a bearing on the rule of law and good governance and some spill over effects can be expected to the benefit of domestic individuals and business operators, they do not address substantive justice or any structural issues that have hindered a country from being a rule of law country.[138] The relationship between international investment law and the rule of law is indirect and flimsy at best.

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[135] Tom Ginsburg, *International Substitutes for Domestic Institutions: Bilateral Investment Treaties and Governance*, 25 INT'L REV. L. & ECON. 107, 121 (2005).

[136] KATE MILES, THE ORIGINS OF INTERNATIONAL INVESTMENT LAW 69 (2013).

[137] David Gaudkroger (Director, OECD Directorate for Financial and Enterprise Affairs), *The future of investment treaties – possible directions* 8–13 (OECD Working Papers Int'l Inv., Working Paper No. 2021/3, 2021), https://www.oecd-ilibrary.org/docserver/946c3970-en.pdf.

[138] Peter-Tobias Stoll, *International Investment Law and the Rule of Law*, 9 GOTTINGEN J. INT'L L. 267, 278–79 (2018).

Furthermore, international treaties do not automatically become part of national law and consequently do not automatically have domestic legal effect in China.[139] Therefore, China's IIAs are not part of Chinese law, and they are not binding on Chinese courts and government bodies. The implementation of IIAs in China is dependent on the enactment of appropriate domestic legislation and regulations incorporating those obligations. And, even if domestic laws are enacted to implement the treaty obligations, having rules on paper does not mean that they are fairly enforced in practice. As an ancient Chinese saying goes, 徒法不能以自行(laws alone cannot carry themselves into practice).[140] It is meaningful to talk about the impact of IIAs on the rule of law in China only if China faithfully and promptly implements IIA commitments, including adverse arbitral awards against it.[141]

It also appears that the complex mechanism that controls the domestic application of treaties in China enables the Chinese government to limit the effectiveness of implementation of IIA obligations within the domestic legal systems.[142] There are various instances of inconsistencies between China's domestic investment regulations with key commitments of market access, non-discrimination, and transparency in Chinese IIAs and other international instruments. For example, China's extremely stringent domestic law on data governance features mandatory business-to-government data sharing, data localization requirements, and restrictions on data transfer to overseas territories.[143] Such laws may collide with substantive standards of protection in Chinese IIAs such as FET or indirect expropriation, given their arbitrary or opaque enforcement, lack of administrative or judicial remedies, and general disproportionality for achieving proclaimed goals such as data sovereignty or cybersecurity.[144] Further, China undertook a firm commitment to abstain from forcing technology transfer from foreign investors operating within its territory when it acceded to the World Trade Organization in 2001. However, the United States argued that China obliged foreign investors to transfer technology to Chinese firms as a prerequisite for accessing the Chinese market through administrative guidance and licensing procedures.[145] In 2020, China's new foreign investment law prohibited the forced technology transfer through

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[139] Xue Hanqin and Jin Qian, *International Treaties in the Chinese Domestic Legal System*, 8 CHINESE J. INT'L. L. 299, 322 (2009).

[140] MENCIUS, MENCIUS 73 (Philip J. Ivanhoe ed., Irene Bloom trans., 2003).

[141] Eckhardt & Wang, *supra* note 77, at 584–85; *see also* Amy Gurowitz, *Mobilizing International Norms: Domestic Actors, Immigrants, and the Japanese State*, 51 WORLD POL. 413, 416 (1999).

[142] Björn Ahl, *Chinese Law and International Treaties*, 39 HONG KONG L. J. 737, 752 (2009).

[143] Alex He, *State-Centric Data Governance in China* 14–15 (Ctr. Int'l Governance Innovation, Paper No. 282, 2023).

[144] Cheng Bian, *Data as Assets in Foreign Direct Investment: Is China's National Data Governance Compatible with its International Investment Agreements?*, 13 ASIAN J. INT'L. L. 342, 362–63 (2023).

[145] Peter K. Yu, *The U.S.- China Forced Technology Transfer Dispute*, 52 SETON HALL L. REV. 1003, 1007–14 (2022).

administrative measures. The prohibition was later included in China's recent IIAs such as the CAI.

Moreover, it is doubtful that the current international investment rules are capable of constraining China' unique economic model.[146] A prominent issue relates to Chinese SOEs. SOEs hold a prominent position in China's socialist market economy system.[147] There are more than 150,000 SOEs in China today. In 2017, they contributed 23-28% of China's gross domestic product (GDP) and 5-16% of employment.[148] More than one thousand SOEs are listed on China's stock markets, accounting for 44% of total market capitalization and 50% of revenues of publicly listed companies.[149] In 2023, 142 Chinese firms appeared on the list of Fortune Global 500, among which 97 were SOEs.[150] Thus, it has been widely accepted that SOEs are, and will be, a hallmark of China's state capitalism model, rather than a transitional phenomenon leading to liberal capitalism as many critics of SOEs had expected.[151]

Not only do Chinese SOEs play a key role in China's domestic economy, but they are also a major force in implementing China's ambitious "Go Out" strategy and, more recently, the Belt and Road Initiative (BRI)—the Chinese paramount leader Xi Jinping's signature foreign policy undertaking.[152] Statistics show that at least 80% of all China's outbound foreign direct investment were funded by SOEs.[153] With the growing strength of privately owned enterprises (POEs) in China, a smaller proportion of China's outbound investment is coming

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[146] Jeffrey N. Gordon & Curtis J. Milhaupt, *China as a "National Strategic Buyer": Towards a Multilateral Regime for Cross-Border M&A*, COLUM. BUS. L. REV. 192, 198 (2019).

[147] There is no uniform definition of SOEs in part because of the ambiguity about the degree of state ownership or control needed to be call an SOE. The OECD defines it as "any corporate entity recognized by national law as an enterprise, and in which the state exercises ownership." Ownership is understood to imply control, either by the state holding full or majority of voting shares or otherwise exercising an equivalent degree of control. Examples of equivalent degree of control would include, for instance, cases where legal stipulations or corporate articles of association ensure continued state control over an enterprise or its board of directors in which it holds a minority stake. Entities in which the government holds equity stakes of less than ten percent that do not confer control are excluded. *See* OECD*,* OECD GUIDELINES ON CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES 14–15 (2015).

[148] *See* CHUNLIN ZHANG, WORLD BANK, HOW MUCH DO STATE-OWNED ENTERPRISES CONTRIBUTE TO CHINA'S GDP AND EMPLOYMENT? 10 (2019).

[149] Xianchu Zhang, *Integration of CCP Leadership with Corporate Governance: Leading Role or Dismemberment?*, 2019-1 CHINA PERSPS. 55, 57 (2019); Curtis J. Milhaupt, *The State as Owner–China's Experience*, 36 (2) OXFORD REV. ECON. POL'Y 362, 362 (2020).

[150] *2023 Fortune China 500,* FORTUNE CHINA (Jul. 25, 2023), https://www.fortunechina.com/fortune500/c/2023-07/25/content_436290.htm. These 97 firms are either state-owned or state-controlled and subject to the supervision of central or local SASACs. *See* Liu Qingshan, *97 Chinese SOEs Listed among 2023 Fortune Global 500* (97 家国企入选 2023 年度财富世界 500 强名单), https://www.sohu.com/a/708420486_100082376#google_vignette

[151] *See* Jude Blanchette, *Confronting the Challenge of Chinese State Capitalism*, CTR. STRATEGIC & INT'L STUD. (Jan. 22, 2021), https://www.csis.org/analysis/confronting-challenge-chinese-state-capitalism.

[152] *See* Andrew Chatzky & James McBride, *China's Massive Belt and Road Initiative Backgrounder*, COUNCIL ON FOREIGN RELS. (Feb. 2, 2023), https://www.cfr.org/backgrounder/chinas-massive-belt-and-road-initiative; Robert J.R. Elliot & Ying Zhou, *State-Owned Enterprises, Exporting and Productivity in China: A Stochastic Dominance Approach* 36 WORLD ECON. 1000, 1001 (2013).

[153] OECD, OECD INVESTMENT POLICY REVIEWS-CHINA 2008: ENCOURAGING RESPONSIBLE BUSINESS CONDUCT 77 (2008).

from SOEs. Still, the evidence shows that, of 650 Chinese investments in Europe from 2010 to 2020, roughly 40% have moderate to high involvement by state-owned or state-controlled companies.[154] As of October 2018, Chinese SOEs contracted about one-half of BRI projects by number and more than 70% by project value.[155] In this sense, Chinese SOEs still play a key role in Chinese outbound FDI.

The expansion of Chinese SOEs' global footprint has caused widespread concerns about their implications for national security, fair competition, reciprocity, transparency, corruption, the function of free market at home, and the future of the rules-based liberal international economic order.[156] Importantly, it is argued that international investment law is poorly designed to deal with Chinese SOEs because it is premised on some untenable assumptions.[157] First, all business actors, be it a SOE or a POE, in international investment are motivated by private economic gain-seeking.[158] Second, commercial acts and governmental acts can be readily distinguished by national regulators or international tribunals.[159] However, both assumptions break down when applying to Chinese SOEs. As Chinese SOEs operate in the interface of competing dimensions of the public and private, there are considerable conceptual and practical difficulties in ascertaining where the sovereign ends and the investor begins, and whether the activities they perform are private or, rather, sovereign. But the extent to which states are entitled to use commercial transactions to pursue strategic, geopolitical ends lies at the very heart of the ideological drift between liberal capitalism and state capitalism countries.[160]

The challenges of Chinese SOEs have posed to international investment law have manifested in several thorny legal issues. For instance, should SOEs be considered on equal footing as POEs as "investors" in international investment law?[161] Should SOEs be subject to more stringent national security review in

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[154] *See* Daniel Michaels, *Behind China's Decade of European Deals, State Investors Evade Notice*, WALL ST. J. (Sept. 30, 2020), https://www.wsj.com/articles/behind-chinas-decade-of-european-deals-state-investors-evade-notice-11601458202.

[155] *See* Rafiq Dossani, Jennifer Bouey, & Keren Zhu, *Demystifying the Belt and Road Initiative* 13–15 (Rand Corp., Working Paper No. 1338, 2020).

[156] *See* OECD, STATE-OWNED ENTERPRISES AS GLOBAL COMPETITORS: A CHALLENGE OR AN OPPORTUNITY? 52–53 (2016).

[157] Ming Du, *Chinese State-Owned Enterprises and International Investment Law*, 53 GEO. J. INT'L. L. 627, 633–34 (2022).

[158] *See* Gordon & Milhaupt, *supra* note 146, at 196–97.

[159] *See* Gus Van Harten, *The Public-Private Distinction in the International Arbitration of Individual Claims Against the State*, 56 INT'L & COMPAR. L. Q. 371, 373–74 (2007). Other commentators observed the distinction of commercial and governmental acts but questioned it on both practical and theoretical grounds. *See* Christin Chinkin, *A Critique of the Public/Private Dimension*, 10 EUR. J. INT'L L. 387, 389 (1999); Anne Van Aaken, *Blurring Boundaries Between Sovereign Acts and Commercial Activities: A Functional View on Regulatory Immunity and Immunity from Execution*, in IMMUNITIES IN THE AGE OF GLOBAL CONSTITUTIONALISM 131, 147–50 (Anne Peters, Evelyne Lagrange, Stefan Oeter & Christian Tomuschat eds., 2014).

[160] Bianca Nalbandian, *State Capitalists as Claimants in International Investor-State Arbitration*, 81 QUESTIONS OF INT'L L. 5, 12–14 (2021).

[161] Du, *supra* note 157, at 671–92.

foreign investment laws?[162] One key concern of Chinese SOEs is that they often benefit from credits extended by state banks or other forms of financing, implicit guarantees, capital injections, and preferential access to inputs. Thus, Chinese SOEs have tilted the playing field and created distortive effects on international investment. Moreover, there are no international investment rules regulating subsides granted by foreign governments to facilitate cross-border acquisitions.[163] Precisely because the current international investment regime does not anticipate many of the special features of Chinese SOEs and their associated impact on international investment, states have become norm entrepreneurs and resorted to unilateral measures designed to counteract Chinese SOEs' competitive advantages in international investment. For instance, the European Commission adopted the Foreign Subsidies Regulation in November 2022 under which the Commission now has the power to investigate subsidies granted by foreign public authorities to facilitate acquisition of European enterprises.[164] On the international front, states have adopted new rules in regulating SOEs' behavior through bilateral and regional free trade agreements (FTAs) or BITs. Yet some question whether the new mechanisms are effective in dealing with the challenges arising from Chinese SOEs' global expansion, such as unfair competition, non-commercial objectives, and ideological conflict.[165]

Finally, to the extent that we see improvements in certain aspects of the rule of law in either a formal or substantive conception in China, it is not clear whether the key driver of change in the Chinese legal system is international investment law, the internal developments within China, or simply a convergence of interests between the Chinese government and other foreign stakeholders. For more than four decades, China has pushed for proactive and unilateral economic liberalization and the rule of law construction. It seems plausible that the Chinese government's decision to pursue a large network of IIAs was a part of China's grand development strategy because it was consistent with China's domestic reform agenda. To be sure, this claim is not to dismiss the positive influence of the extensive network of Chinese IIAs on the rule of law in China. Rather it calls for a clearer articulation of the causal mechanisms through which China has internalized the international investment law norms and how these norms are

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[162] *Id.* at 695–97.

[163] *See* Gary Hafbauer et al., *Investment Subsidies for Cross-Border M&A: Trends and Policy Implications* 15 (U.S. Council Found., Paper No. 2, 2008).

[164] Regulation (EU) 2022/2560 of the European Parliament and of the Council of 14 December 2022 on foreign subsidies distorting the internal market. The European Commission has launched its first investigation under the Foreign Subsidies Regulation in February 2024 concerning CRRC Corporation Limited, a Chinese state-owned rolling stock manufacturer. *See* the European Commission Press Release, *Commission Opens First In-depth Investigations under the Foreign Subsidies Regulation* (Feb. 16, 2024), https://ec.europa.eu/commission/presscorner/detail/en/ip_24_887.

[165] Ming Du, *Unpacking the Black Box of China's State Capitalism*, 24 GERMAN L. J. 125, 141–49 (2023); Xueji Su, *Liberalising the Chinese Market: State-Owned Enterprise Disciplines in CAI*, 23 J. WORLD INV. & TRADE 545, 570–71 (2022).

primary drivers underlying the progress in rule of law in China.[166] After all, international norms can matter only when they are adopted domestically and integrated into the political process.[167]

C. The Underutilized Investor-State Dispute Settlement Processes

Judicialization has expanded in contemporary world politics. In many issue-areas, but especially in international economic relations, the world witnessed a move to the strengthen delegation to increasingly independent and powerful third-party judicial and quasi-judicial arbitral tribunals.[168] The highly judicialized ISDS mechanism included in over 3,000 IIAs is a defining attribute of modern international investment law. Allowing foreign investors to bring claims against host states without the need for home state espousal, the ISDS mechanism was designed to "de-politicize" investment disputes and create a forum that would offer investors a fair hearing before an independent, neutral, and qualified tribunal.[169] In the process, ISDS has become more judicialized, acquiring some of the trappings of judicial procedures.[170] By the end of 2022, the total number of publicly known ISDS claims reached 1,257 and at least 890 ISDS proceedings had been concluded.[171]

A key argument supporting the international investment law-rule of law nexus is that foreign investors may utilize the powerful ISDS mechanism to challenge a host state's arbitrary domestic laws and regulations. To avoid liability for breaches of IIAs, host states will internalize their international investment law obligations and reform their policy-making process. However, if foreign investors rarely utilize the ISDS mechanism against a host state, then the deterrent force of ISDS is likely to diminish and the impact of ISDS on the domestic rule of law of a host state is limited. This is precisely the case in China.

International investment lawyers have been debating the puzzle of the so-called "China disequilibrium" in international investment arbitration.[172] Even though China is a signatory of almost 150 IIAs in which comprehensive ISDS procedures are a common feature, there are only few investor-state investment disputes

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[166] Calamita and Berman, *supra* note 3, at 6–7; Björn Ahl, *Interaction of National Law-making and International Treaties: Implementation of the Convention against Torture in China*, *in* CHINESE LEGAL REFORM AND THE GLOBAL LEGAL ORDER: ADOPTION AND ADAPTATION 136, 137 (Zhao Yun & Michael Ng eds., 2017).

[167] Gurowitz, *supra* note 141, at 416; Jonathan Bonnitcha & Zoe Phillips William, *The Impact of Investment Treaties on Domestic Governance in Developing Countries*, 46 L. & POL'Y 140, 159–60 (2024).

[168] Judith Goldstein, et al., *Legalization and World Politics*, 54 INT'L ORG. 385, 389 (2000).

[169] Ibrahim Shihata, *Towards a Greater Depoliticization of Investment Disputes: The Roles of ICSID and MIGA*, 1 ICSID REV. 1, 4–5 (1986).

[170] Alan Redfern, *The Changing World of International Arbitration*, *in* PRACTISING VIRTUE: INSIDE INTERNATIONAL ARBITRATION 45, 49–50 (David D. Caron et al. eds., 2015).

[171] U.N. Conference on Trade and Development., *supra* note 17, at 77–79.

[172] Wei Shen, *Guarding the Great Wall? Jurisprudential Review of Treaty Interpretative Tools in Chinese BIT-Based Arbitration Cases*, 37 ARB. INT'L 239, 240 (2021).

involving the Chinese government, Chinese investors, or Chinese IIAs.[173] According to public records, the Chinese government is the respondent in nine reported cases by August 2023. Excluding five cases in which the claimant investors discontinued the proceedings, the number would be reduced to four.[174] Moreover, different from other developing countries which are more likely to suffer net losses when getting involved in ISDS proceedings,[175] China has so far enjoyed a triumphant exposure to ISDS proceedings. It has never experienced first-hand the pains of "losing face," i.e., being found of breaching her international legal obligations to foreign investors and being ordered to divert public funds to compensate foreign investors' financial loss by an arbitral tribunal.[176]

The reasons why foreign investors are reluctant to bring investment arbitration against the Chinese government are due to several factors, including the lack of the rule of law in China. For instance, one argument attributes the low utility rate of Chinese IIAs to the fact that early Chinese IIAs often incorporate restrictive terms of investor, investment, fork-in-the road, the inclusion of mandatory administrative review procedures and temporary jurisdictional limitations, among others with the practical effect of discouraging foreign investors to initiate ISDS against China.[177] Another more positive explanation is that the Chinese government has always appreciated the important role of foreign investment in Chinese economic development and offered sufficient investment protection to foreign investors.[178] For example, China used to accord foreign investors super-national treatment because they enjoyed favorable treatment when compared with Chinese domestic enterprises in terms of tax rates and other conditions of competition.[179] Therefore, the risk of the Chinese government violating BIT obligations is low.[180] However, the optimistic narrative runs counter to the fact that foreign companies established in China have reported significant issues relating to unequal treatment with local companies, inconsistent application of

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[173] *See* Fredrik Lidmark, Daniel Behn & Ole Kristian Fauchald, *Explaining China's Relative Absence from Investment Treaty Arbitration, in* THE LEGITIMACY OF INVESTMENT ARBITRATION: EMPIRICAL PERSPECTIVES 424, 424 (Daniel Behn et al., eds, 2022).

[174] Ming Du, *Explaining China's Approach to Investor-State Dispute Settlement Reform*, 27 Eur. L. J. 281, 301 (2022). Nevertheless, with China's position as the largest FDI destination in the world, there is little doubt that the number of investment disputes involving the Chinese government will rise in the future. Since 2019, six investment arbitration cases (two of which were later discontinued) were filed against China by Japanese, UK, and Singaporean investors. This number is more than what China had experienced over nearly 30 years since its accession to the ICSID Convention in 1992.

[175] Tim R. Samples, *Winning and Losing in Investor-State Dispute Settlement*, 56 AM. BUS. L. REV. 115, 163 (2019).

[176] Du, *supra* note 174, at 294.

[177] Lidmark, Behn & Fauchald, *supra* note 173, at 437–55.

[178] Yuqing Zhang, *The Case of China*, *in* INVESTOR-STATE ARBITRATION – LESSONS FOR ASIA 159 (Michael Moser ed., 2008)

[179] Xianjun Feng and Chuanhui Wang, *China's Foreign Investment Law: Moving Toward Greater Liberalization*?, 10 PA. ST. J.L. & INT'L AFFS. 115, 127 (2022).

[180] Wenhua Shan, Norah Gallagher & Sheng Zhang, *National Treatment for Foreign Investment in China: A Changing Landscape*, 27 ICSID REV. 120, 125–30 (2012).

regulations, hidden subsidies, and business environment that is perceived as increasingly politicized.[181]

Contrary to this optimistic explanation, a competing argument holds essentially that a dearth of ISDS claims against China is precisely due to the lack of the rule of law in China. Foreign investors may fear that initiating an ISDS claim could jeopardize their relationship with the Chinese government and in turn put their business dealings in China at risk. By contrast, foreign investors may find greater benefits in non-adversarial means, such as negotiation and mediation, to resolve their disputes with the Chinese government, given its preference for informal dispute settlement.[182]

Moreover, even though China has changed its position on state immunity from absolute immunity to restrictive immunity with the adoption of the Foreign State Immunity law in September 2023,[183] there is no guarantee that investor-state arbitral awards may be enforced in China. To begin with, China made a commercial reservation when joining the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention) in 1986. The commercial reservation by the Chinese government explicitly provides that the New York Convention only applies to contractual and non-contractual disputes arising from commercial legal relationships and that it does not include the dispute between foreign investors and the host government.[184] Moreover, China does not have any domestic law permitting enforcement of arbitral awards against state property.[185] Initiating arbitration against the Chinese government is therefore only the last resort.

Whatever the reasons may be, the point here is that China has rarely been involved in ISDS and that the powerful ISDS mechanism prescribed in IIAs has little direct impact on the rule of law in China.

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[181] Fabian Jintae Froese et al., *Challenges for Foreign Companies in China: Implications for Research and Practice*, 18 ASIAN BUS. & MGMT. 249, 251–53 (2019) (describing various regulatory challenges unfavourable to foreign investors in China).

[182] Leon E. Trakman, *Geopolitics, China, and Investor-State Arbitration* in CHINA IN THE INTERNATIONAL ECONOMIC ORDER 279 (Lisa Toohey, Colin B. Picker & Jonathan Greenacre eds., 2015); Dae Un Hong & Ju Yoen Lee, *Why Are There So Few Investor-State Arbitrations in China? A Comparison with Other East Asian Economies*, CHINA & WTO REV. 35, 47–51 (2018).

[183] Hayley Wong, *Why China is Changing its Laws to Allow Court Action against Foreign States*, SOUTH CHINA MORNING POST (Sept. 11, 2023), https://www.scmp.com/news/china/diplomacy/article/3234177/why-china-changing-its-laws-allow-court-action-against-foreign-states.

[184] Mariana Zhong & Zeyu Huang, *PRC Foreign State Immunity Law: A Gateway to Judicial Review of Investor-State Arbitration by the PRC Courts*, KLUWER ARBITRATION: ARBITRATION BLOG (Dec. 1, 2023), https://arbitrationblog.kluwerarbitration.com/2023/12/01/prc-foreign-state-immunity-law-a-gateway-to-judicial-review-of-investor-state-arbitration-by-the-prc-courts/; Gao Xiaoli, *Chinese Courts Have Taken a Positive Attitude towards Arbitration*, CHINA INT'L COM. CT. (May 15, 2018), https://cicc.court.gov.cn/html/1/219/199/203/1056.html.

[185] Wang Guiguo, *Chinese Mechanisms for Resolving Investor-State Disputes*, 1 JINDAL J. INT'L AFF. 204, 226–28 (2011).

D. The Resilience of the Chinese Authoritarian Regime

In hindsight, much of the original optimism about the profound impact of international investment law on China's domestic rule of law, both in formal and substantial conceptions, was founded on a flawed assumption that the investment liberalization would automatically trigger the adoption of rule of law. There may be a powerful spill over effect on the rule of law in China from China's integration into the liberal international economic order. However, contrary to what many hoped, the investment liberalization and the rule of law process is not at all automatic, but heavily dependent on the existence of many other preconditions such as political will, expertise, funds, an independent judiciary benefitting from embedded judicial authority, and an established tradition of broad interpretation of judicial rules and doctrines.[186] In fact, empirical studies attempting to measure the impact of IIAs commitments on the domestic rule of law found that they create—at best—a weak rule of law effect in countries with a poor record of respect for the rule of law.[187]

Moreover, increased economic and cultural exchange will not necessarily lead to political pressure for democratic reform and a Western liberal conception of the rule of law. National policymakers may at times be unwilling or unable to effectively change behavior, institutions, and culture.[188] As Acharya emphasizes, many local beliefs and practices condition the acceptance of international norms. Local actors will not either wholly accept the existing international norms or totally reject them. Instead, localization involves both resisting and reframing international norms in a particular context.[189] In addition, the cultural disruption ensuing from economic globalization and trade liberalization may encourage a greater exertion of central government authority to maintain societal stability and national identity.[190]

This is arguably the case in China. After forty years of reform and opening up policy, China's remarkable economic liberalization stands in marked contrast to its political conservativeness, characterized by the monopoly of political power by the CCP and the blurred line between Chinese national interests and the security of the CCP regime.[191] To ensure its iron-clad hold on state power, the party-state is constantly on the alert for threats—big or small, real or imagined—to its authority at home. When the CCP perceives potential threats to its power, such as the Western conception of the rule of law, it may slow or block any spill over effects that international economic norms may have on the rule of law. In

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[186] Gordon Silverstein, *Globalization and the Rule of Law: A Machine that Runs of Itself?*, 1 INT'L J. CONST. L. 427, 430 (2003); Guthrie, *supra* note 56, at 1153.

[187] Calamita & Berman, *supra* note 3, at 325–26; Schultz & Dupont, *supra* note 8, at 1163.

[188] Amitav Acharya, *How Ideas Spread: Whose Ideas Matter? Norm Localization and Institutional Change in Asian Regionalism*, 58 INT'L ORG. 239, 247–50 (2004).

[189] *Id.*

[190] Eric W. Orts, *The Rule of Law in China*, 34 VAND. J. TRANSNAT'L L. 43, 109 (2001).

[191] Xiangfeng Yang, *The Anachronism of a China Socialized: Why Engagement is Not All It's Cracked Up to be*, 10 CHINESE J. INT'L POL. 67, 88–90 (2017).

fact, this can be done effectively, efficiently, and constitutionally, at no discernible cost to its economic standing in the world community.[192]

Further, the root problem of global economic liberalization and rule of law nexus is that it implicitly assumes the state as docile, readily receptive to all direct and indirect influences of economic globalization. It assumes that their national policies and identities could be easily transformed along liberal democratic lines. Indeed, the rule of law thesis is rooted in a traditional, rational-choice theory of the state as an actor making preference-maximizing decisions based on cost-benefit analyses. Given the benefits of compliance with international obligations and the costs of violation, a rational choice model predicts that states will gain more from internalizing their obligations and complying with them.[193] In reality, as Ian Hurd proposes, "states are both socialised to norms and strategic calculators that manipulate them."[194] State power co-exists with global governance institutions. States may retreat under exogenous normative forces, but it is equally possible that the pendulum may swing towards the opposite direction. In the two-way interactive process, states are not merely passive actors in the implementation and internalization of international obligations, but also proactive participants during international and transnational interaction.[195] In particular, states and domestic politics recursively affect the development and change in internal economic norms.[196]

China's sprawling BRI is a typical example. Rather than being fully receptive to current international economic norms, the BRI presents a new model for global economic ordering by integrating Chinese norms into existing legal infrastructures. Specifically, China employs extralegal and nonlegal norms alongside instruments of formal international economic law.[197] In this way, China seeks to create a Sino-centric, transnational legal order in which the Chinese state plays the nodal role and projects an alternative values system compared to Western globalization.[198] In short, although liberalization of international investment may contribute to the rule of law, it is not a guaranteed outcome.

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[192] Silverstein, *supra* note 186, at 442.

[193] Jansen N. Calamita, *The Rule of Law, Investment Treaties and Economic Growth: Mapping Normative and Empirical Questions*, *in* RULE OF LAW SYMPOSIUM 2014: THE IMPORTANCE OF RULE OF LAW IN PROMOTING DEVELOPMENT 103, 125–26 (Jeffery Jowell, J. Christopher Thomas, & Jan Van Zyl Smit eds., 2015).

[194] Ian Hurd, *Breaking and Making Norms: American Revisionism and Crises of Legitimacy*, 44 INT'L POL. 194, 209 (2007).

[195] Pu Xiaoyu, *Socialisation as a Two-way Process: Emerging Powers and the Diffusion of International Norms*, 5 CHINESE J. INT'L POL. 341, 349 (2012).

[196] Terence C. Halliday & Bruce G. Carruthers, *The Recursivity of Law: Global Norm Making and National Lawmaking in the Globalization of Corporate Insolvency Regimes*, 112 AM. J. SOC. 1135, 1138 (2007).

[197] Matthew S. Erie, *Chinese Law and Development*, 62 HARV. INT'L L.J. 51, 54–56 (2021).

[198] Gregory Shaffer & Henry Gao, *A New Chinese Economic Order*, 23 J. INT'L ECON. L. 607, 632–35 (2020); Bruno Macaes, BELT & ROAD: A CHINESE WORLD ORDER 189 (2018).

CONCLUSION

The belief that trade policy, to which investment protection is an integral part, plays an important role in promoting the rule of law abroad is deeply embedded in national trade policies of some Western countries. Trade policy has been a bedrock of U.S. foreign policy dating from the Second World War. Since then, the United States has entered into trade negotiations based upon the belief that open markets foster democracy which, in turn, supports the maintenance of world peace.[199] Similarly, the EU trade policy has become increasingly linked to "values," especially addressing the rule of law as a political commitment.[200] Amid the EU's growing ambition to use its trade policy as a linchpin or a leverage for the pursuit of value-driven policies, the significant extent to which the trade policy is capable of promoting the rule of law is readily assumed.[201]

Based on such beliefs, China's integration into the liberal international economic order was long considered an unprecedented opportunity to put China's economic, legal, and political system under strict scrutiny and to reform its legal system towards the rule of law. An alternative view, however, argues that China only selectively incorporates international norms most conductive to its economic growth and preferable to its elites.[202] In doing so, China undertakes minimum commitments to the international legal regime while extracting the benefits of global institutions. While China has made great strides in the rule of law construction, it is not clear that international investment law or international economic law are responsible for influencing China's positive behavioral evolution.

I do not contend to completely reject the positive role international investment law may play in promoting the rule of law in China. Rather, the purpose of this article is to challenge the degree, depth, and scope of such effects. Indeed, it is at least partly due to the U.S. policymakers' growing disillusionment with China's economic and political reform through engagement within the liberal international economic order that the United States has started a new China strategy.[203] Regardless of how attractive it may be to link rule of law to IIAs, it

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[199] Alan Wolff, *Paradigm Lost? U.S. Trade Policy as an Instrument of Foreign Policy*, LAW WIRE (Feb. 5, 2018), https://www.wcl.american.edu/impact/lawwire/paradigm-lost-us-trade-policy-as-an-instrument-of-foreign-policy/.

[200] Maryna Rabinovych, *The Rule of Law as Non-trade Policy Objective in EU Preferential Trade Agreements with Developing Countries*, 12 HAGUE J. RULE L. 485, 507 (2020).

[201] Jacques Pelkmans, *Linking "Values" to EU Trade Policy - A Good Idea*?

26 EUR. L. J. 391, 395 (2020) (arguing that few ask the question whether the coupling of values with EU trade policy is good for the objectives behind it).

[202] Samuel S. Kim, *China's International Organization Behavior*, *in* CHINESE FOREIGN POLICY: THEORY AND PRACTICE 401, 419 (Thomas W. Robinson & David Shambaugh eds., 1994); Pitman B. Porter, *China and the International Legal System: Challenges of participation*, 191 CHINA Q. 699, 701 (2007).

[203] Antony J. Blinken, Secretary of State, Speech at George Washington University: The Administration's Approach to the People's Republic of China (May 26, 2022) (transcript available at https://www.state.gov/the-administrations-approach-to-the-peoples-republic-of-china/).

is merely one of many appealing hypotheses found in rule of law scholarship that has been repeated enough times that it has taken on the quality of a received truth.