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## THE EU-CHINA COMPREHENSIVE AGREEMENT ON INVESTMENT — BLUNDER OR WIN?

Daniel Zigo\*

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### *Abstract*

*The article deals with the very current issue of mutual investment relations between the EU and China, especially in the context of the EU-China Comprehensive Agreement on Investment (the “CAI”). The author primarily analyzes the current legal framework and practice between the two partners and touches on possible problematic aspects and barriers that prevent the use of the full potential of these relations. Furthermore, the article addresses directly the investment agreement in question, analyzes its main parts and provisions, and puts them in context with other investment or trade agreements that the parties have concluded, namely the China-US Phase One Agreement and the EU-Vietnam Trade Agreement and the Investment Protection Agreement. Subsequently, the main goal is to analyze the changes that CAI brings and assess whether they manage to overcome the identified barriers. Based on findings and comparisons with other authors, the author answers the question of whether the CAI is an investment agreement that has the potential to take the EU-China relationship to the next level or is a wrong move for the parties.*

### I. INTRODUCTION

The topic of bilateral foreign direct investment between China and the EU is very actual in today's world. The European Union (“EU”) and the People's Republic of China (“China” or “PRC”) are two of the biggest traders in the world. In the situation when countries are taking a protectionist stance and introducing import tariffs, it is very important to understand what attitude these two vast markets have towards each other. The investment agreement between China and the EU has been negotiated for more than six years, and surprisingly, an agreement on the content was announced at the end of 2020. Despite the negotiation of the agreement, many aspects of their bilateral investment relationship remain unresolved, and some questions remain unanswered. Negotiations are also not fully completed. In the future, there are plans to conclude agreements that will further liberalize mutual trade for these two units (for example, free trade agreement). Also, mutual trade and investment relations between China and the EU is a very broad and complex issue, covering and arising not only from the recently reached investment agreement but also from their national law, international trade rules and often from informal customs or international political relations.

The basic aim of this article is to analyze the current mutual investment practices between the EU and China, focusing on their problematic aspects and barriers that prevent the use of the full potential of these relations.

Subsequently, through the analysis of the published text, the EU-China Comprehensive Agreement on Investment (“CAI”) and the synthesis of the opinions of other legal, economic or political experts on this issue, our goal is to conclude whether the CAI has managed to cope with existing problems in practice and is a win-win agreement for both parties, or is an agreement that has wasted the potential to improve the current situation and its ratification would be a mistake.

At the outset, we consider it necessary to introduce the reader to the current regulatory framework within which mutual investment relations between the EU and China are governed. From an international point of view, these will be mainly WTO rules, even though none of the agreements directly regulates foreign investment and no special agreement has been concluded for this area.<sup>1</sup> Despite this fact, however, the respective WTO agreements more or less interfere in the field of foreign investment and thus create a regulatory framework within which the Member States operate unless they have concluded bilateral agreements with each other.<sup>2</sup> From the point of view of the functioning of foreign investors in the domestic markets of the EU and China, national regulations on their territory are also very important.

In China, the most recent Foreign Investment Law of the People’s Republic of China (“FIL”)<sup>3</sup> was adopted by the National People’s Congress on March 15, 2019, and came into effect on January 1, 2020. It replaces three special laws that have applied to investors until then. Compared to previous foreign investment legislative changes, this law has been very significant since it has not only replaced laws that have been key in this sector for many years, but have also introduced a new institutional approach including previously used negative list management system, an information reporting system and a security review system. This law brought the unification of domestic and foreign companies under a uniform regime, introduced the Pre-establishment National Treatment, and the new Negative Letter associated with it brought significant openings in several sectors.<sup>4</sup> This law reflects China’s trend of gradual opening up and easing trade relations.

The situation is more complicated within the EU. As all EU Member States are sovereign and independent, the EU can exercise its competences on the basis of treaties concluded between the Member States which confer compe-

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<sup>1</sup> See, e.g., Anyuan Yuan, *China’s Entry into the WTO: Impact on China’s Regulating Regime of Foreign Direct Investment*, 35 INT’L LAW 195, 201 (2001).

<sup>2</sup> See Benedikt Heid & IsaacVozzo, *The International Trade Effects of Bilateral Investment Treaties*, 196 ECON. LETTERS 1, 4 (2020).

<sup>3</sup> Zhonghua Renmin Gongheguo Waishang Touzi Fa (中华人民共和国外商投资法) [Foreign Investment Law of the People’s Republic of China] (promulgated by the Nat’l People’s Cong., March 15, 2019, effective Jan. 1, 2020) [hereinafter “FIL”].

<sup>4</sup> See Lian Ruihua, *Further Opening-Up to Foreign Investment: The New Negative List*, 12 TSINGHUA CHINA L. REV. 143,152 (2019).

tences upon the EU.<sup>5</sup> One of the key areas over which the EU has exclusive competence is the common commercial policy, and not just its organization inside of the Union but, in particular, outwards vis-à-vis third countries.<sup>6</sup> As far as the regulation of foreign direct investment (“FDI”) within the EU is concerned, the legal norms that deal with this area are very diverse. This is because the EU, unlike China, does not have a single legal act dealing with foreign investors. On the contrary, the rules in this area will be laid down in the international treaties of which the EU is a member, in the basic provisions of the EU treaties, in particular the provisions of the Treaty on the Functioning of the European Union (“TFEU”), and also in the specific rules laid down by each Member State. However, what the EU and its Member States have in common is the fact that they are extremely active in attracting foreign capital and investors. In the area of capital movements, the EU has even provided for liberalization within the TFEU to the extent that it has unilaterally opened its territory to investors from third countries and allowed capital inflows without requiring reciprocity. However, it retained the possibility of imposing measures in this area within the meaning of Articles 64 to 66 TFEU.<sup>7</sup> The new legislation in this area, which has significantly affected FDI rules within the EU is the Regulation (EU) 2019/452 of the European Parliament and of the Council of 19 March 2019 establishing a framework for the screening of foreign direct investments into the Union (the “FDI Screening Regulation”). It came into force on 11 October 2020 and introduced new rules under which the Member States may screen foreign investment on the basis of which they may reject it. Even after the entry into force of this regulation, it is still the case that whether a Member State carries out screening is at its discretion,<sup>8</sup> but the Commission has indicated that it strongly recommends the screening process.<sup>9</sup> The FDI Screening Regulation establishes a framework for the screening of FDI by the Member States on the grounds of security or public order.<sup>10</sup> Most importantly, the question of whether the FDI is likely to affect security or public order, for example by operating in critical infrastructure (energy, transport, water, health, communications, media, data processing, defense, financial infrastructure, etc.) by using critical technologies (*e.g.*, AI or aerospace), whether the foreign investor is directly or indirectly controlled by the government of a third country,

<sup>5</sup> See Consolidated Version of the Treaty on European Union, art. 5(2), Feb. 7, 1992, 2016 O.J. (C 202) 13, 18.

<sup>6</sup> See Robert Shutze, *EU Competences: Existence and Exercise*, in OXFORD HANDBOOK OF EUROPEAN UNION LAW 75, 85-87 (Anthony Arnall & Damian Chalmers eds., 2015).

<sup>7</sup> See ANGELOS DIMOPOULOS, *EU FOREIGN INVESTMENT LAW* 50 (Oxford University Press, 2011).

<sup>8</sup> Currently, 10 out of 27 members do not screen FDI. See European Commission, *Foreign Direct Investment EU Screening Framework*, [https://trade.ec.europa.eu/doclib/docs/2019/february/tradoc\\_157683.pdf](https://trade.ec.europa.eu/doclib/docs/2019/february/tradoc_157683.pdf) (last visited Nov. 1, 2021).

<sup>9</sup> See European Commission, *Guidance to The Member States Concerning Foreign Direct Investment and Free Movement of Capital from Third Countries, and the Protection of Europe's Strategic Assets, ahead of the Application of Regulation (EU) 2019/452 (FDI Screening Regulation)*, [https://trade.ec.europa.eu/doclib/docs/2020/march/tradoc\\_158676.pdf](https://trade.ec.europa.eu/doclib/docs/2020/march/tradoc_158676.pdf) (last visited Nov. 1, 2021).

<sup>10</sup> See the FDI Screening Regulation, art. 1(1), March 19, 2019, 2019 O.J. (L 79) 1, 6.

or whether there is a serious risk that the foreign investor engages in illegal or criminal activities and other potential risk factors.<sup>11</sup> Following the adoption of this regulation, there may be legitimate concerns from the perspective of foreign investors and States that the EU has embarked on a wave of protectionism and thereby closing internal markets. Regulation is not yet widely used; therefore, such concerns would be premature. But at least it puts some pressure on foreign partners to gain access to European markets on a legal basis other than the unilateral opening up of Europe.

We considered this very brief and basic legislative delimitation of mutual investment relations between the EU and China to be important in view of the legal situation which the parties found themselves before the conclusion of the CAI while this situation may partly explain the motivations of individual parties in the negotiations.

## II. THE EU-CHINA CURRENT FOREIGN DIRECT INVESTMENT RELATIONS

In this part, we will address the current relationship between the EU and China in the field of foreign direct investment and related sectors (particularly international trade). The first, essential point for us, in terms of the importance of investment relations between the EU and China, will be the current practice and volume of mutual investment relations while also focusing on problematic aspects of these relations. At the same time, the areas of concern give us the answer to the question of why there is a need to regulate mutual investment relations between China and the EU by an investment agreement.

### A. *Key Facts on Investment Practice Between the EU And China*

The EU and China are two of the largest economic units in the world. In 2019, the GDP in China was USD 14.34 trillion and with the EU, it amounted to USD 15.62 trillion both of which accounted for 34% of total global GDP.<sup>12</sup> In terms of mutual trade and investment relations, China was for a long time the EU's second-biggest trading partner, which changed during 2020 when China overtook the United States and became the EU's biggest trading partner, while the EU remains to be China's biggest trading partner from 2004 until now.<sup>13</sup> Both the EU and China offers many opportunities for the growth of companies and can attract investments particularly in terms of market size and the number of potential customers.

Although the market, especially in China, is gradually evolving (European companies were here initially established mainly in the manufacturing sec-

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<sup>11</sup> See *id.*, art. 4, at 7.

<sup>12</sup> See The World Bank, *GDP Current US\$*, <https://data.worldbank.org/indicator/NY.GDP.MKTP.CD> (last visited Nov. 1, 2021).

<sup>13</sup> See European Commission, *Trade Policy – China*, <https://ec.europa.eu/trade/policy/countries-and-regions/countries/china/> (last visited Nov. 1, 2021).

tors<sup>14</sup>), interest has remained. Now EU companies in China are interested in settling in many other sectors. For example, the fast-growing financial or technology industries.<sup>15</sup> Also, China is no longer an interesting destination for European companies only in terms of production. As the per-capita income and the purchasing power of the population has risen rapidly, it is also interesting as a consumption market of products and services.<sup>16</sup>

On the other hand, Chinese companies are gaining a strong position from a global perspective and can compete with companies in the European market. As regards to the volume of mutual investments, cumulative investments from the EU to China were more than €140 billion and for Chinese investment into the EU, the figure is almost €120 billion. Both these figures are for the period over the last 20 years.<sup>17</sup> As indicated by other data, these figures may be partially distorted because the largest percentage of foreign investment flowing into Mainland China from Hong Kong, SAR.<sup>18</sup> Hong Kong serves to channel capital flows into and out of Mainland China for many foreign companies. Foreign companies use Hong Kong as a conduit for investments for various reasons, it may be related, for example to tax issues. Thus, part of the foreign direct investment coming to Mainland China from Hong Kong may also come from the EU. This would be also indicated by the fact that the volume of FDI from the EU to Hong Kong, SAR., has increased from € 1.4 billion in 2011 to € 19.8 billion in 2017.<sup>19</sup>

As we can see, the volume of mutual investments is very significant, even from a global perspective. The question, therefore, arises as to why the mutual relations in trade and investment need to be regulated by a bilateral agreement beyond international trade and investment norms and national regulations. The answer lies in the fact that, despite the considerable volume of investment and trade, the potential of this relationship is not fully utilized. The relationship between the EU and China is claimed to be unbalanced and there are several barriers to market access on one side or the other, and several deficiencies that discourage companies from investing.<sup>20</sup> These barriers have been identified,

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<sup>14</sup> See Frederico Mollet, *China's Grand Industrial Strategy and What It Means for Europe*, 2, EUROPEAN POLICY CENTER, [https://epc.eu/content/PDF/2021/EU-China\\_PB.pdf](https://epc.eu/content/PDF/2021/EU-China_PB.pdf) (last visited Nov. 1, 2021).

<sup>15</sup> See Alicia Garcia-Herrero et al., *EU-China Trade and Investment Relations in Challenging Times*, 15, EUROPEAN PARLIAMENT, [https://www.europarl.europa.eu/RegData/etudes/STUD/2020/603492/EXPO\\_STU\(2020\)603492\\_EN.pdf](https://www.europarl.europa.eu/RegData/etudes/STUD/2020/603492/EXPO_STU(2020)603492_EN.pdf) (last visited Nov. 1, 2021).

<sup>16</sup> See *id.*, at. 16.

<sup>17</sup> See European Commission, *Key Elements of the EU-China Comprehensive Agreement on Investment* [hereinafter "Key Elements of CAF"], [https://ec.europa.eu/commission/presscorner/detail/en/ip\\_20\\_2542](https://ec.europa.eu/commission/presscorner/detail/en/ip_20_2542) (last visited Nov. 10, 2021).

<sup>18</sup> See *News Release of National Assimilation of FDI from January to October 2018*, MINISTRY OF COMMERCE, PRC (Nov. 22, 2018, 14:54), <http://english.mofcom.gov.cn/article/statistic/foreigninvestment/201812/20181202815485.shtml> (last visited Nov. 2, 2021).

<sup>19</sup> See Garcia-Herrero, *supra* note 15, at 28.

<sup>20</sup> See Guy De Jonquières, *The EU and China: Redressing: An Unbalanced Relationship* (ECIPE Policy Briefs, Jan. 2016), <https://ecipe.org/publications/the-eu-and-china-redressing-an-unbalanced-relationship/>.

in particular, during the negotiations between China and the EU on the CAI, and this agreement should aim to remove them.

### *B. The EU-China Foreign Direct Investment Barriers*

The EU and China started negotiations on a bilateral investment agreement in 2013. During the negotiations in the initial stages, there were identified points that would need to be regulated and parties subsequently exchanged first offers.<sup>21</sup>

1. Requirements from the EU. The EU has based its requirements also on the practice of European companies in China, grouped in the EU Chamber of Commerce in China.<sup>22</sup> In 2018, this organization introduced its China position paper, which summarized the standing of European entrepreneurs on the Chinese market and presented to the Chinese government fourteen common concerns that are frequently faced by a variety of industries.<sup>23</sup> While acknowledging the progress and improvement of the business environment in China, this document also outlined areas whose change could significantly improve the operation of European companies in China. The European Commission has also carried out an extensive analysis of the Sustainability Impact Assessment (“SIA”),<sup>24</sup> which aimed to assess how the investment provisions under negotiation could affect economic, social, human rights and environmental issues in the EU and China. Of course, the problematic aspect of bilateral investment relations and possible obstacles in individual markets are also addressed by many legal or economic experts and academics. With a slight generalization, we can say that the following points have been identified as the most serious barriers to European investors’ access to the Chinese market:

*a. Access to Licenses.* Licensing requirements can serve the purpose of ensuring that a certain type of business meets certain standards that are necessary for a given sector. However, licensing also has the potential to function as a barrier to market access if the licensing requirements are excessive or if the conditions for granting them are not uniform for domestic and foreign entities. These requirements were perceived as problematic, for example, in the

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<sup>21</sup> See European Commission, *EU and China Agree on Scope of the Future Investment Deal*, <https://trade.ec.europa.eu/doclib/press/index.cfm?id=1435> (last visited Nov. 2, 2021).

<sup>22</sup> The Chamber is recognized by the European Commission and the PRC’s Authorities as the official voice of European business in China. And it has more than 1700 members.

<sup>23</sup> See the European Union Chamber of Commerce in China, *The European Business in China Position Paper 2018/2019*, Sept. 18, 2018, [hereinafter “China Position Paper 2018”], [https://www.europeanchamber.com.cn/en/publications-archive/646/European\\_Business\\_in\\_China\\_Position\\_Paper\\_2018\\_2019](https://www.europeanchamber.com.cn/en/publications-archive/646/European_Business_in_China_Position_Paper_2018_2019) (last visited Nov. 2, 2021).

<sup>24</sup> See European Commission, *Sustainability Impact Assessment (SIA) in Support of an Investment Agreement Between the European Union and the People’s Republic of China* [hereinafter “SIA”], [https://trade.ec.europa.eu/doclib/docs/2018/may/tradoc\\_156862.pdf](https://trade.ec.europa.eu/doclib/docs/2018/may/tradoc_156862.pdf) (last visited Nov. 2, 2021).

financial services sector and limited to foreign banks, or in the insurance sector.<sup>25</sup>

*b. Administrative Procedures.* Some administrative procedures were perceived by companies as too complicated or too lengthy, which makes it difficult for entrepreneurs to operate. As an example, they cited the verification of education degrees or obligation to register with the local police within 24 hours of entering China, every time the foreign employee crosses the border.<sup>26</sup>

*c. Intellectual Property Rights (“IPR”) and Research and Development (“R&D”).* These two areas are significantly interconnected, as the research is aimed at gaining new knowledge which will be protected by IP law. The issue of IP protection is a much-discussed topic in relation to China.<sup>27</sup> As for R&D, European companies report that they struggle to access government support in this area to the same extent as it is given to local companies. The initiative believed that highly innovative European companies might invest more in local R&D if given the right conditions. Also, the joint venture requirements were set in many sectors and this has often involved transfers of intellectual property to Chinese counterparts.<sup>28</sup>

*d. Market Access.* Market access can be blocked by various types of measures, some impede the possibility of investing directly, such as a negative list, others act indirectly but have the same effect, such as the above licensing requirements, different administrative procedures, or unequal status of foreign entities. The EU’s goal in this area was to negotiate a narrowing of the negative list, which would significantly lift market access restrictions in the prohibited industries for EU companies.<sup>29</sup> In the EU’s view, opening up more sectors would be mutually beneficial, as it would help China to liberalize further,<sup>30</sup> and several key sectors in the EU, namely transportation equipment industry, mining and energy extraction industry, chemical industry, food and beverage, manufacturing industry, finance and insurance industries, as well as the communications and electronic equipment industries, would benefit substantially if an agreement on better market access would be negotiated.<sup>31</sup> The EU Chamber of Commerce in China identified significant legal barriers to participating in

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<sup>25</sup> See *China Position Paper 2018*, *supra* note 23, at 10.

<sup>26</sup> See *id.*, at 11.

<sup>27</sup> See James A. Brander, Victor Cui, Ilan Vertinsky, *China and Intellectual Property Rights: A Challenge to the Rule of Law*, 48 J. INT’L BUS. STUD. 908 (2017).

<sup>28</sup> See Garcia-Herrero, *supra* note 15, at 9.

<sup>29</sup> See Wei Yin, *Challenges, Issues in China-EU Investment Agreement and the Implication on China’s Domestic Reform*, 26 ASIA PAC. L. REV. 170, 188 (2018).

<sup>30</sup> See Garcia-Herrero, *supra* note 15, at 57.

<sup>31</sup> See SIA, *supra* note 24.



the Chinese markets, for example, of the construction sector, legal services, financial services, or the transport of goods.<sup>32</sup>

*e. Public Procurement.* Given the size of China, its public procurement market is indeed large and provides many opportunities for European companies, therefore it is in the EU's interest to secure their participation in it.<sup>33</sup> Negotiations in this area also include China's access to WTO rules on public procurement.

*f. State-owned Enterprises ("SOEs").* One of the items on the agenda is the position of SOEs in the Chinese market. Several factors have been identified as problematic. In sectors such as banking, agriculture, aviation, energy, and insurance, SOEs significantly dominate and suppress competition.<sup>34</sup> This is subsequently reflected in the prices and quality of goods or services, as the market cannot function fully. As these companies are linked to the administration, they also have cheaper and easier access to financing than what is available to private enterprises. And SOEs may also use other preferential treatments.<sup>35</sup> From this point of view, it is difficult to compete with SOEs and therefore there was a requirement for a level playing field for private and public companies. However, Chinese SOEs might have a complicated position also in European markets in case of their overseas investments. Due to their allegedly low transparency, they raise concerns among European states about opaque funding, competition issues, and even national security.<sup>36</sup>

*g. Transparency and Equal Treatment.* These points also include problems with the opacity of regulations and the predictability of law enforcement, as well as transparency, especially transparency in the decision-making activities of state officials. Concerning equal treatment, European companies pointed to a different legal regime for foreign invested enterprises and domestic companies.<sup>37</sup>

In this context, it is a very interesting fact that some of these requests, which the European Commission has adopted from the EU Chamber of Commerce in China, were resolved during the negotiations, *i.e.*, before the actual publishing of the first version of the CAI. For example, in terms of access to licenses and administrative procedures, at present, an anti-corruption campaign has been ongoing in China for several years, with one of its pillars being to take measures to reduce administrative control and the issuance of various permits for busi-

<sup>32</sup> See *China Position Paper 2018*, *supra* note 23, at 19.

<sup>33</sup> See Fredrik Erixon et al., *China's Public Procurement Protectionism and Europe's Response: The Case of Medical Technology* 43 (ECIPE Policy Briefs, September 2021), <https://ecipe.org/publications/chinas-public-procurement-protectionism/>.

<sup>34</sup> See *China Position Paper 2018*, *supra* note 23, at 22.

<sup>35</sup> See Garcia-Herrero, *supra* note 15, at 52.

<sup>36</sup> See Wei Yin, *supra* note 29, at 184.

<sup>37</sup> See *China Position Paper 2018*, *supra* note 23, at 28.

nesses. In this way, the opportunities for officials to ask for a bribe are minimized. And it is not a negligible number of these measures. “At the national level, China has abolished or reduced approval requirements for thousands of procedures, at local levels for tens of thousands. Doing business in China today requires fewer than half the approvals required 10 years ago.”<sup>38</sup> Regarding the protection of IP rights, the establishment of specialized IP courts, which brought quality and professional decision-making and at the same time a certain degree of legal certainty for IP rights holders, is perceived as a very positive change.<sup>39</sup> Issues such as market access, access to public procurement, transparency and equal treatment were largely addressed by the FIL of 2019 and the new negative list, and I will address these changes in more detail in Part III. Yet, most of the named obstacles to the investment of European companies in China remain more or less valid and it was their elimination that the European Commission addressed in the negotiations on the CAI.

2. Requirements from China. The situation of Chinese entrepreneurs in European markets is different compared to their European counterparts in China. First of all, the EU is one of the most open territories in the world for foreign investment,<sup>40</sup> this position has been taken unilaterally, even if the country of a foreign investor is not reciprocally open to Europeans. For this reason, it might seem that for the Chinese side, negotiating an investment agreement was not a pressing issue. However, if we take into account other political and especially international connotations, we realize that the Chinese side also had a clear interest in concluding the agreement.

Chinese companies have prospered greatly from stable economic growth in the country, and during the previous decade, many of them gained a dominant position in the market and began to expand abroad, becoming relevant even from a global perspective.<sup>41</sup> With this prosperity also came a relatively massive wave of acquisitions in which Chinese companies began to enter foreign companies.<sup>42</sup> There have been several such acquisitions in the EU, and Chinese investors have been particularly interested in technology companies, which is in contrast to European investments in China, mostly devoted to manufacturing and established as greenfield investments.<sup>43</sup> Said high-profile acquisitions made by Chinese companies in the EU include, for example, cases such as the lease agreement of the Greek Port of Piraeus to the Chinese Ocean

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<sup>38</sup> Melanie Manion, *Taking China's Anticorruption Campaign Seriously*, 4 ECON. & POL. STUD. 3, 9 (2016).

<sup>39</sup> See *China Position Paper 2018*, *supra* note 23, at 16.

<sup>40</sup> See OECD, *FDI Regulatory Restrictiveness Index*, <https://stats.oecd.org/Index.aspx?datasetcode=FDIINDEX#> (last visited Nov 3, 2021).

<sup>41</sup> See Alan Dukes, *Practitioners Perspectives on the China EU Investment Agreement: Stakeholder Reflections from the Business Community in Beijing*, 5 CHINA-EU L.J. 73, 74 (2016).

<sup>42</sup> See Garcia-Herrero, *supra* note 15, at 30.

<sup>43</sup> See Liming Wang & Yuan Li, *The Negotiation of EU-China Comprehensive Agreement on Investment and Its Potential Impact in the Post-Pandemic Era*, 18 J. CHINESE ECON. & BUS. STUD. 365 (2020).

Shipping Company in 2009 and the subsequent acquisition by COSCO of a majority share of the Hellenic Republic Asset Development Fund which significantly expanded the company's distribution and logistics services<sup>44</sup> or the acquisitions of well-known companies like KUKA Robotics by Midea in 2015, Pirelli, the 5th largest tire manufacturer in the world, by ChemChina in 2015, Volvo Cars by Geely in 2010, entry of Beijing Automotive Group into Daimler or the HNA conglomerate into Deutsche Bank as its largest shareholder.<sup>45</sup> All these operations have attracted a great deal of attention also from the public.<sup>46</sup>

In these cases, Chinese companies acquired not only a well-known brand and its name, but also know-how and technology. These types of investment in technology sectors have been of some concern to the EU Member States, since they have perceived companies like Daimler as their national value, and its technologies can also be used in the military industry.<sup>47</sup> This in turn has led to the adoption of several measures, namely the FDI Screening Regulation, based on which the Member States may examine the planned investment of a foreign investor within its territory or even suspend a problematic investment. For this reason, there were concerns from the Chinese side that this Regulation would be used to protect the national interests of Member states against Chinese investments in Europe in the technology sector. Thus, during the CAI negotiations, China made it clear that one of its objectives under this agreement would be to protect Chinese investors in the EU and to maintain broad market access for Chinese investments, with an emphasis on the high-tech sector.<sup>48</sup>

Another reason why China may be interested in an investment agreement is the current fragmentation of regulations for Chinese investors in the EU. Despite the above-mentioned openness of European markets, Chinese investors are currently exposed to various regulatory environments within the EU. This is because China currently has investment agreements in place with all EU Member States except Ireland.<sup>49</sup> It is a fairly common practice for third-country investors in the EU to operate within several Member States. This is relatively advantageous as they can offer their products or services to more customers. However, different conditions in each Member State may increase an investor's operating costs because they require additional costs for optimization and legal services.<sup>50</sup> The situation is, of course, even more complicated, as investment agreements with individual countries can be more or less complex and WTO rules also apply. From China's point of view, it may

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<sup>44</sup> See Jeremy Clegg & Hinrich Voss, *Inside the China-EU FDI Bond*, 19 CHINA & WORLD ECONOMY 92, 99 (2011).

<sup>45</sup> See Alan Dukes, *supra* note 41, at 76.

<sup>46</sup> See Jack Ewing, *Europe Takes Steps to Block Chinese Bargain Hunters*, NY TIMES (Jun. 17, 2020), <https://www.nytimes.com/2020/06/17/business/european-union-china-deals.html> (last visited Nov. 3, 2021)

<sup>47</sup> See Wang & Li, *supra* note 43, at 370.

<sup>48</sup> See *id.*, at 372.

<sup>49</sup> See SIA, *supra* note 24, at 12.

<sup>50</sup> See Sophie Meunier, *Divide and Conquer: China and the Cacophony of Foreign Investment Rules in the EU*, 21 J. EUR. PUB. POL'Y 996 (2014).

therefore seem advantageous and beneficial for its investors to have uniform comprehensive market access or investment protection conditions in place within the whole EU.

One of the circumstances that we should not forget when we talk about the motivation of China and the EU to conclude an investment agreement is the recent trade dispute between the US and China. Following the inauguration of President Trump's administration, the United States began to approach increased protection of domestic companies and the market in international trade relations. This has been particularly evident in relation to China, where these countries have introduced new custom barriers, taxes and tariffs on imported goods on each other, but the EU has also become a target of US sanctions or threats of sanctions.<sup>51</sup> The EU has been relatively neutral in this trade dispute, as, although it has agreed to some US demands towards China, the EU generally disagrees with trade protectionism and seeks to promote a free trade policy.<sup>52</sup> This neutrality seemed very beneficial from the EU's position, as while US and Chinese companies encountered barriers to trade with each other, the EU remained open to them. Finally, the EU sought to conclude this investment agreement before the end of 2020 and before the new US administration took office, which has been criticized by many,<sup>53</sup> but this step is also logical, as the conclusion of the CAI would give European companies a competitive advantage over American ones on the Chinese market. From China's point of view, such an agreement is significant from a political perspective, as it shows that the US and the EU do not have a unified protectionist stance and the EU accepts China as a very important trading partner.

### III. THE EU-CHINA COMPREHENSIVE AGREEMENT ON INVESTMENT

In this section, I will take a closer look at the concrete wording of the EU-China Comprehensive Agreement on Investment, which was negotiated and published at the turn of 2020/2021. Here I am particularly interested in what solutions to the problematic aspects of the mutual investment relations mentioned above this agreement offers, and what might be its shortcomings. The assessment of this agreement is also possible from the perspective of the negotiating practice between China and the EU, whereas I decided to assess it in the context of the China-US Phase One Agreement ("Phase One Agreement") and the EU-Vietnam Trade Agreement and the Investment Protection

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<sup>51</sup> See Ken Itakura, *Evaluating the Impact of the US-China Trade War*, 15 ASIAN ECON. POL'Y REV. 77 (2019).

<sup>52</sup> See Sebastien Goulard, *The Impact of the US-China Trade War on the European Union*, 12:1 GLOBAL J. EMERGING MARKET ECONOMIES 56, 61 (2020).

<sup>53</sup> See e.g., Andrew Small, *Europe's China Deal: How not to Work with the Biden Administration*, EUROPEAN COUNCIL ON FOREIGN RELATIONS (Jan. 21, 2021), <https://ecfr.eu/article/europes-china-deal-how-not-to-work-with-the-biden-administration/> (last visited Nov. 3, 2021).

Agreement (“EU-Vietnam FTA”), as these agreements are relatively recent and involve types of contractual partners very similar to those in the CAI.

The negotiations on an investment agreement between the EU and China were launched in 2013 in order to provide investors on both sides with predictable and long-term access to the EU and China’s markets, as well as to protect investors and their investments.<sup>54</sup> A lot has changed on both sides during the turbulent years recently. Chinese economy has continued to grow significantly, and in the meantime the EU has lost the membership of the United Kingdom, but both sides stayed interested in reaching the agreement as the economic relation between the two has deepened during the past decade.<sup>55</sup> The length of the negotiations has suggested that it was not easy to reach an agreement. As mentioned above, the EU has a relatively broad demand for market access but does not have much leverage as a counteroffer. Subsequently, the world was hit in 2020 by the COVID-19 pandemic, which seriously complicated economic and political relations worldwide, hence the joint announcement in December 30, 2020, that “the EU and China today concluded in principle the negotiations for the Comprehensive Agreement on Investment”<sup>56</sup> was quite a surprise for the whole world. The text of CAI is agreed upon in terms of content, but the attached notes have pointed out that it may undergo further modifications as a result of the process of legal and technical revision, including the final structure.<sup>57</sup> After clarifying the text of the agreement, both parties have to ratify it. This process is more complicated in the EU, where it will require a qualified majority in the EU Council and a majority in the EU Parliament.<sup>58</sup> During these steps, ratification may be delayed or tangled, as some members of the EU Parliament may suggest that they have a problem with this agreement for various reasons.<sup>59</sup>

Although the European Commission claims that the CAI is “the most ambitious agreement that China has ever concluded with a third country,”<sup>60</sup> critics complain that it could have been much more groundbreaking in the

<sup>54</sup> See European Parliament, *Resolution of 9 October 2013 on the EU-China Negotiations for a Bilateral Investment Agreement* (2013/2674(RSP)), 2016 O.J. (C. 181) 45.

<sup>55</sup> Cumulative EU-China FDI since 2000, see Thilo Hanemann & Agatha Kratz, *Cross Border Monitor – People’s Republic of China – European Union Direct Investment 2Q 2021*, [https://trade.ec.europa.eu/doclib/docs/2021/july/tradoc\\_159761.pdf](https://trade.ec.europa.eu/doclib/docs/2021/july/tradoc_159761.pdf) (last visited Nov. 4, 2021).

<sup>56</sup> *EU and China Reach Agreement in Principle on Investment*, EUROPEAN COMMISSION (Dec. 30, 2020), [https://ec.europa.eu/commission/presscorner/detail/en/IP\\_20\\_2541](https://ec.europa.eu/commission/presscorner/detail/en/IP_20_2541) (last visited Nov. 4, 2021).

<sup>57</sup> See CAI, preamble, Dec. 30, 2020, EUROPEAN COMMISSION, [https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/china/eu-china-agreement/eu-china-agreement-principle\\_en](https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/china/eu-china-agreement/eu-china-agreement-principle_en) (last visited Nov. 4, 2021).

<sup>58</sup> See Consolidated Version of the Treaty on the Functioning of the European Union, arts. 207 & 218, March 25, 1957, 2016 O.J. (C 202) 47, 140 & 144-146.

<sup>59</sup> See Kinling Lo, *Deal or No Deal. . . What Next for China-EU Investment Pact and Why It May Fail*, SCMP (Jan. 5, 2021), <https://www.scmp.com/news/china/diplomacy/article/3116535/deal-or-no-deal-what-next-china-eu-investment-pact-and-why-it> (last visited Nov. 4, 2021).

<sup>60</sup> European Commission, *Key Elements of CAI*, *supra* note 17.

problematic areas.<sup>61</sup> The text of the agreement does suggest that changes in some areas are substantial, while in others not so much. To provide an analysis of the most fundamental changes that the CAI will deliver, I will focus on four key areas which are addressed by this agreement. These areas are: market access, a level playing field, sustainable development, and dispute settlement.

#### A. *Market Access Commitments*

Market access is one of the most crucial parts of this agreement. The opening of new market sectors is expected mainly from China, as the EU is already highly open to foreign investors. This has, of course, been confirmed by the publication of the text of the agreement, and indeed the EU has maintained its current state of openness with a few restrictions in some specific areas.<sup>62</sup> In contrast, China has made several concessions and opened up relatively interesting sectors for European companies. Of course, China has to be careful about which areas of services it would open for European investments, as these could also be claimed by other parties of GATS<sup>63</sup> in terms of the most favoured nation (“MFN”) treatment. However, this obligation does not bind parties in manufacturing, as GATT<sup>64</sup> only concerns trade but not investment, whereas the manufacturing sector, as mentioned above, is an area that the European companies in China often invest in. In the area of market access, the CAI stipulates the basic conditions in *Section II - Investment Liberalization*, which sets out the provisions concerning national treatment, MFN treatment, entry and temporary stay of natural persons for business purposes, and these provisions are in principle very similar to those contained in the Phase One Agreement. Exceptions to these rules are then provided by the Annexes, so that each party has a so-called Schedule of Commitments (Annexes), which contains 4 annexes.

Annexes I and II are based on a “negative list” approach concerning the commitments stipulated in Section II. This means that specific commitments are valid in all sectors, except those explicitly mentioned as excluded or to the extent being reserved. If a specific sector is not listed here, then it is fully covered by the terms of the agreement. Annex II lists those sectors in which the Parties have reserved the right to derogate from the obligations in Section II.<sup>65</sup>

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<sup>61</sup> See James Carafano, Arvind Gupta & Jeff M. Smith, *The Pitfalls of the China-EU Comprehensive Agreement on Investment*, THE DIPLOMAT (Jan. 22, 2021), <https://thediplomat.com/2021/01/the-pitfalls-of-the-china-eu-comprehensive-agreement-on-investment> (last visited Nov 4, 2021).

<sup>62</sup> For example, nuclear energy industry, see more in Henry Gao, *The EU-China Comprehensive Agreement on Investment: Strategic Opportunity Meets Strategic Autonomy*, SSRN (May 12, 2021), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=3843434](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3843434).

<sup>63</sup> General Agreement on Trade in Services, Apr. 15, 1994, in Marrakesh Agreement Establishing the World Trade Organization, Annex 1B, 1869 U.N.T.S. 183, 33 I.L.M. 1167 (1994).

<sup>64</sup> General Agreement on Tariffs and Trade 1994, Apr. 15, 1994, in Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 187, 33 I.L.M. 1153 (1994).

<sup>65</sup> See CAI, *supra* note 57, China’s Schedule of Commitments and Reservations; EU’s Schedule of Commitments and Reservations.

Annex III then adopts the opposite approach and, for clarification, sets out a “positive list” as regards the commitments concerning quantitative restrictions affecting market access. Hereby both parties make commitments not to impose quantitative restrictions to the relevant sectors listed in this Annex. Annex IV deals in more detail with the additional reservations and restrictions applicable to the entry and temporary stay of intra-corporate transferees and business visitors.<sup>66</sup>

Several specific sectors, in which China has granted market access concessions, have attracted attention either in terms of exceptional extend of the concessions or for other reasons, which I will discuss below. For example, in the manufacturing sector, China has provided extensive commitments with only minimal restrictions, the European Commission even claims that China specifically in this sector would match the openness of the EU.<sup>67</sup> Moreover, as we have stated, almost half of the EU’s FDI in China is in this sector, so the concessions here are very important for the EU.<sup>68</sup> In terms of automobile manufacturing after 2022, investments by foreign investors in the manufacture of passenger cars will not be subject to restrictions on the shareholding percentage (currently the Chinese party shall not have less than 50%). There will not be any limitation on new investments in electric vehicle projects valued at over USD 1 billion.<sup>69</sup> It is important to note that the EU is the biggest exporter of cars to China, accounting for 53.3% of total Chinese car imports by value,<sup>70</sup> so any opening in the automotive industry is perceived as a big gain, especially for Germany. As for health services, China will allow the establishment of fully foreign-owned private hospitals in eight cities, including Beijing, Shanghai, Shenzhen, Tianjin, Guangzhou, and Hainan Island (currently there is a joint venture requirement in this field), while most of the employees in these hospitals will need to be Chinese citizens.<sup>71</sup> The opening of the research and development sector is also interesting, China has not previously committed openness in R&D in biological resources. Exceptions to the opening in this area are related to social sciences, humanities, human stem cells, genetic diagnosis and treatment technology, and the research and development services utilizing the biological resources originated from and protected by China.<sup>72</sup>

Many telecommunication and digital services will also be opened for EU investors, except for the provision of internet access to end-users. Also, the

<sup>66</sup> See European Commission, *Commission Publishes Market Access Offers of the EU-China Investment Agreement*, <https://trade.ec.europa.eu/doclib/press/index.cfm?id=2253> (last visited Nov 5, 2021).

<sup>67</sup> See European Commission, *Key Elements of CAI*, *supra* note 17.

<sup>68</sup> See *id.*

<sup>69</sup> See CAI, *supra* note 57, China’s Schedule of Commitments and Reservations, Annex I Entry 6 – Manufacture of Transportation Equipment.

<sup>70</sup> See European Automobile Manufacturers Association, *Fact Sheet: EU-China Automobile Trade*, Feb. 19, 2019, <https://www.acea.be/news/article/fact-sheet-eu-china-automobile-trade> (last visited Nov 3, 2021).

<sup>71</sup> See CAI, *supra* note 57, China’s Schedule of Commitments and Reservations, Annex I Entry 18 – Medicine.

<sup>72</sup> See *Id.*, Annex III., 1. Business services.

investment ban for cloud services will be lifted and there will be a 50% equity cap requirement for EU investors. However, this is not a new achievement, as the same provision is contained in the Phase One Agreement and the EU has been claiming it since its conclusion in terms of GATS MFN treatment. The same situation can also be noticed in the area of financial services. China has in the past started to liberalize its approach in this area, and the joint venture requirements and foreign equity caps have been removed for banking, trading in securities and insurance (including reinsurance), as well as asset management.<sup>73</sup> However, these commitments were already included in the Phase One Agreement, therefore they are not a significant breakthrough for the EU. The opening in the field of environmental services is important, as this sector in China is not open to any other foreign partner. Current joint venture requirements will be removed in environmental services such as sewage, noise abatement, solid waste disposal, cleaning of exhaust gases, nature and landscape protection, sanitation and other services.<sup>74</sup> Other sectors that China is willing to open for European investors are, for example, business services (real estate, rental and leasing, repair and maintenance for transport, advertising, market research, management consulting and translation), construction services (eliminate the project limitations currently reserved in China's GATS), computer services, international maritime transport (cargo-handling, container depots and stations, maritime agencies, etc.), and air transport-related services (computer reservation systems, ground handling and selling and marketing services).<sup>75</sup>

Besides, as a victory for both parties, we can consider the provisions on visa and work permits. The residency and work permits will be granted for up to 3 years to senior managers and specialists working locally for a foreign investor, and representatives of investors will be allowed to visit the opposite country freely before making an investment.<sup>76</sup> The CAI will also remove restrictions such as labor market tests and quotas (except for hospitals where domestic staff must be a majority). Visa and residence procedures have been one of the obstacles pointed out by European investors in China, on the other hand, it may be more convenient for Chinese investors to employ their workers in Europe, so this agreement has addressed the problems of both parties.

### *B. The Level Playing Field*

In addition to market access itself, the European Commission and EU companies have identified an unbalanced relationship between China and the EU as a significant investment barrier. Specifically, the EU claims that its investors in China do not have the same status as domestic companies, in

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<sup>73</sup> See *Id.*, Annex III., 7. Financial services.

<sup>74</sup> See *Id.*, Annex III., 6. Environmental services.

<sup>75</sup> See European Commission, *Key Elements of CAI*, *supra* note 17.

<sup>76</sup> See CAI, *supra* note 57, section II, arts. 6, 6bis.



particular SOEs.<sup>77</sup> For these reasons, the CAI contains a significant part of the provisions aimed at leveling the playing field for investors of both parties.

One of the challenges posed to this agreement by the SOEs has been their position in the Chinese market, which is estimated to account for around 30% of China's GDP<sup>78</sup>, and therefore it is relatively important for foreign investors to be able to trade with them. The CAI obliges the SOEs to behave under normal market discretion (unless they perform a public role) and not to discriminate against EU foreign invested enterprises. In this regard, China has undertaken to provide, upon request, information on whether the conduct of a specific SOE complies with the CAI, and in the event of non-compliance, the Parties will agree on a solution, or they can resort to dispute resolution under the CAI.<sup>79</sup> The EU used its previous experience from negotiations with Vietnam where the SOEs also play an important role, and they managed to find a way to make these companies more transparent.<sup>80</sup> The provisions of the CAI regarding the SOEs' transparency, non-discrimination and commercial considerations are very similar to those of the EU-Vietnam FTA.

Another aspect that the agreement addresses involve state subsidies. While these can be a very important means for the state to support the domestic economy and strengthen these companies' competitiveness, on the other hand, they can also have a very negative impact on foreign investors who do not have access to them. This aspect has long been the subject of negotiations between the EU and China.<sup>81</sup> The CAI promotes the transparency of subsidies in the service sectors – each party shall annually publish on a publicly accessible website the objective, legal basis, form, amount or amount budgeted for, and recipient of any subsidy granted that year in the service sectors.<sup>82</sup> If one of the parties considers a specific subsidy granted by the other party to have a negative effect on the investment, the parties will engage in consultations to address such negative effects.<sup>83</sup> A similar measure was again included in the EU-Vietnam FTA, while from China's point of view, both subsidies and SOEs provisions are unique measures that were not included in the Phase One Agreement, making the CAI a more complex agreement, since the Phase One Agreement placed greater emphasis on balancing mutual imports and exports in the area of

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<sup>77</sup> See High Representative of the Union for Foreign Affairs and Security Policy, *Joint Communication to the European Parliament and the Council – Elements for A New EU Strategy on China*, 3, EUROPEAN COMMISSION (June 22, 2016), [https://eeas.europa.eu/archives/docs/china/docs/joint\\_communication\\_to\\_the\\_european\\_parliament\\_and\\_the\\_council\\_-\\_elements\\_for\\_a\\_new\\_eu\\_strategy\\_on\\_china.pdf](https://eeas.europa.eu/archives/docs/china/docs/joint_communication_to_the_european_parliament_and_the_council_-_elements_for_a_new_eu_strategy_on_china.pdf) (last visited Nov 4, 2021).

<sup>78</sup> See European Commission, *Key Elements of CAI*, *supra* note 17.

<sup>79</sup> See CAI, *supra* note 57, section III, sub-section 2.

<sup>80</sup> See Hege Merete Knutsen & Do Ta Khanh, *Reforming State-Owned Enterprises in A Global Economy: The Case of Vietnam*, in *THE SOCIALIST MARKET ECONOMY IN ASIA* 141–166 (Arve Hansen Jo Inge Bekkevold & Kristen Nordhaug eds., 2020).

<sup>81</sup> See David Hallinan, *The EU–China Bilateral Investment Treaty: A Challenging First Test of the EU's Evolving BIT Model*, 5 CHINA-EU L. J. 31, 44 (2016).

<sup>82</sup> See CAI, *supra* note 57, section III, sub-section 2, art. 8(5).

<sup>83</sup> See *id.*, section III, sub-section 2, art. 8(6).

leveling trade conditions. For example, the Phase One Agreement forces the SOEs to buy more US imports to meet the commitments, which, in stark contrast to what the CAI wants to achieve, can exert even greater influence to the SOEs within the Chinese economy.<sup>84</sup>

Forced technology transfer is also a frequently discussed issue in connection with foreign investment in China.<sup>85</sup> The CAI is taking several measures against this unpopular practice, such as obliging the parties to lift requirements to transfer technology to a joint venture partner, prohibiting the interference in contractual freedom in technology licensing, and protecting confidential business information collected by administrative bodies.<sup>86</sup> The Phase One Agreement contained almost identical provisions, the EU did not manage to negotiate for significant improvement on this point.

The CAI is also addressing one of the suggestions of the EU Chamber of Commerce in China, which concerns the practical aspect of investing in China, namely licensing requirements and administrative procedures. Both parties have undertaken to provide equal access to standard-setting bodies, enhance transparency, predictability and fairness in licensing procedures. The CAI will include transparency rules for regulatory and administrative measures to enhance legal certainty and predictability, as well as for procedural fairness and the right to judicial review, including in competition cases.<sup>87</sup>

What may be missing in the level playing field, for example in comparison with the Phase One Agreement and the EU-Vietnam FTA, is the protection of intellectual property rights. The EU has either been satisfied with the recent progress in China in this area and relies on other international legal guarantees (such as the TRIPs Agreement), or planning to address this issue more comprehensively in the future under the prospective EU - China Free Trade Agreement. Another issue, in this context, that the CAI does not address either is the public procurement. This is problematic from the point of view of the EU, who leaves its public procurement markets open to operators from third countries and tries to persuade its trading partners to follow the same approach.<sup>88</sup> China has recently allowed the foreign invested enterprises to participate in public procurement,<sup>89</sup> but cross-border access to this market of a European company that does not have a branch in China is not granted still.

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<sup>84</sup> See Chad P. Bown & Mary E. Lovely, *Trump's Phase One Deal Relies on China's State-Owned Enterprises*, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS (Mar. 3, 2020), <https://www.piie.com/blogs/trade-and-investment-policy-watch/trumps-phase-one-deal-relies-chinas-state-owned-enterprises> (last visited Nov 4, 2021).

<sup>85</sup> More about the topic, see Dan Prud'homme et al., "Forced Technology Transfer" Policies: *Workings in China and Strategic Implications*, 134 TECH. FORECASTING & SOC. CHANGE 150 (2018).

<sup>86</sup> See CAI, *supra* note 57, section III, sub-section 2, art. 1.

<sup>87</sup> See European Commission, *Key Elements of CAI*, *supra* note 17.

<sup>88</sup> See Daniel Zigo, *Access of Third Country Economic Operators to the EU Public Procurement Market*, 38 ACTA FACULTATIS IURIDICAE UNIVERSITATIS COMENIANAE 309, 318 (2019).

<sup>89</sup> See FIL, art. 16: "The State shall guarantee that foreign-funded enterprises can participate in government procurement activities through fair competition. Products produced and services provided by foreign-funded enterprises within the territory of China shall be treated equally in government procurement."

### C. Sustainable Development

What the EU insisted on during the negotiations on the CAI, and what is specific to the European bilateral investment treaties (“BITs”) policy<sup>90</sup> is the issue of sustainable development. This issue is again exceptional, as China has not agreed on similar commitments with another foreign partner, not even under the Phase One Agreement with the US. This supports the EU’s claim that in relation to China, it is not just a matter of negotiating better terms, but of a long-term value-based investment relationship grounded on sustainable development principles.<sup>91</sup>

The main areas that are addressed within the sustainable development in CAI are corporate social responsibility, labor affairs and environmental protection. Within the framework of corporate social responsibility, the parties agree to promote responsible business practices within relevant internationally recognized guidelines and principles (UN Global Compact, the UN Guiding Principles on Business and Human Rights, ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy, etc.).<sup>92</sup> Concerning environmental protection and labor conditions, the parties have committed themselves not to lower their current standards of protection in order to attract investors and at the same time not to abuse these standards to discriminate against foreign investors.<sup>93</sup> In addition, the parties have further committed themselves to higher international standards of labor and environmental protection by “effectively implement the UNFCCC and the Paris Agreement”<sup>94</sup> and “each Party . . . is committed to effectively implement the ILO Conventions it has ratified and work towards the ratification of the ILO fundamental Conventions. . . .”<sup>95</sup> In this case, this applies in particular to China, as the EU is already bound by these treaties and the European Commission presents this as a success in mutual negotiations. Nevertheless, this part is the target of the greatest criticism.<sup>96</sup> The reason for criticism is that the commitments contained in this section are not directly enforceable through dispute resolution, and their implementation is considered vague, as these are mainly political declarations for the future and their actual implementation depends on

<sup>90</sup> See Hallinan, *supra* note 81, at 50.

<sup>91</sup> See *EU-China Leaders’ Meeting: Delivering Results by Standing Firm on EU Interests and Values*, EUROPEAN COMMISSION (December 30, 2020), [https://ec.europa.eu/commission/presscorner/detail/en/STATEMENT\\_20\\_2546](https://ec.europa.eu/commission/presscorner/detail/en/STATEMENT_20_2546) (last visited Nov. 5, 2021).

<sup>92</sup> See CAI, *supra* note 57, section IV, sub-section 1, art. 2.

<sup>93</sup> *Id.*, sub-section 2, art. 2.

<sup>94</sup> *Id.*, sub-section 2, art. 6.

<sup>95</sup> *Id.*, sub-section 3, art. 4(2).

<sup>96</sup> For example, François Godement, *Wins and Losses in the EU-China Investment Agreement (CAI)*, Institut Montaigne (Feb. 18, 2021), <https://www.institutmontaigne.org/en/press/wins-and-losses-eu-china-investment-agreement-cai>; or Bart-Jaap Verbeek, *Unpacking an Empty Box . . . The EU-China Comprehensive Agreement on Investment*, CENTRE FOR RESEARCH ON MULTINATIONAL CORPORATIONS (Jul. 8, 2021), <https://www.somo.nl/unpacking-an-empty-box-the-eu-china-comprehensive-agreement-on-investment/> (last visited Nov. 4, 2021).

the will of the parties, in this case mostly on China. An interesting example, in this case, is Vietnam, where the EU-Vietnam FTA contained identical provisions and Vietnam did indeed ratify the ILO conventions, even before the ratification of the FTA.<sup>97</sup>

#### *D. Dispute Settlement*

The last and very important part is the dispute settlement section. An effective mechanism for enforcing the obligations of the parties contained in the agreement is a crucial tool for its application in practice. The CAI builds a dispute resolution mechanism on two pillars. The first is the informal way through mutual dialogue, where a party can at any time ask the other party for consultations on a specific issue, in which they can agree on a solution.<sup>98</sup> They can also proceed through mediation if they agree on this step. If the parties do not find an agreement in the mutual dialogue, formal arbitration will take place. The arbitration panel in such case would be composed of 3 experts in the field. One will be selected from a list provided by PRC, one from a list provided by the EU and one will be an individual that is not a national of either party and who will serve as chairperson to the arbitration panel.<sup>99</sup> The CAI also contains further details on the functioning of the panel and the arbitration procedures. There is also a choice of forum possibility – in the event of a breach of an obligation arising not only from the provisions of the CAI but also WTO law, the party may opt for dispute settlement procedures under the WTO Agreement or the CAI, and the chosen method is then exclusive.

An interesting tool for resolving possible disputes is the establishment of the Investment Committee, which will be co-chaired by the Vice-President of the European Commission and the Vice-Premier of the State Council of the PRC.<sup>100</sup> Among other things, this Committee will be in charge of nominating experts to the arbitration panels, but it will also meet at least once a year and will supervise the proper functioning of mutual relations in accordance with the CAI. It is a very interesting tool for resolving disputes directly at one of the highest political levels. The intention here, of course, is to prevent problems and disputes and resolve them with influence from above.

However, what needs to be noted in dispute settlement is that this part of the CAI deals only with state-to-state dispute settlement. This agreement lacks a comprehensive regulation of investment protection, which is a relatively standard part of investment agreements, but here the situation is complicated due to EU law. The protection of FDI in the EU is excluded from the EU's competences, and this competence lies with the Member States. The approval

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<sup>97</sup> See International Labor Organization, *ILO Welcomes European Parliament's Approval for Free Trade Deal with Viet Nam*, Feb. 12, 2020, [https://www.ilo.org/hanoi/Informationresources/Publicinformation/Pressreleases/WCMS\\_736139/lang=en/index.htm](https://www.ilo.org/hanoi/Informationresources/Publicinformation/Pressreleases/WCMS_736139/lang=en/index.htm) (last visited March 30, 2021).

<sup>98</sup> See CAI, *supra* note 57, section V, art. 2.

<sup>99</sup> See *id.*, section V, art. 8.

<sup>100</sup> See *id.*, section VI, sub-section 1, art. 1.

of an investment protection agreement is therefore a shared competence of the EU and the Member States, and such an agreement must be ratified not only by the EU but also by all Member States.<sup>101</sup> This process is very demanding, especially in terms of time, for example, the Canada-Europe Trade Agreement, in which negotiations were concluded in 2014, is still not ratified by all Member States.<sup>102</sup> Nevertheless, the parties have mutually committed to continuing negotiations on investment protection and investment dispute settlement agreement, with the negotiations to be concluded within 2 years of the signing of the CAI.<sup>103</sup> Therefore, to maintain the level of investor protection, all BITs concluded between the individual Member States and China will remain in force even after the entry into force of the CAI, until an investment dispute settlement agreement is reached. In this sense, it will be very interesting to follow further developments, as the EU has in the past indicated its intention to move away from the traditional investor-state dispute settlement system, to the new Investment Court System.<sup>104</sup>

#### IV. CONCLUSION

The article analyzed the mutual investment relations between China and the EU in terms of several aspects. First, a brief overview of the current volume of mutual investment relations was provided, which indicated that this relationship is substantial, but also has considerable potential for development in the future. However, various barriers currently prevent this potential. These are mostly the barriers and complications for European investors on the Chinese market that have been analyzed during the negotiations on the investment agreement, but also barriers that may arise in the future for Chinese investors in some strategic sectors of European markets due to the application of the FDI Screening Regulation. Each party intended to minimize as much as possible those barriers that could restrict their domestic investors in the foreign market. To this end, they have started negotiations on CAI. I tried to provide an analysis of the possible development of bilateral investment relations between the EU and China, especially with an emphasis on the most important investment topic today – The Comprehensive Agreement on Investment. As mentioned, this agreement is based on four basic pillars – market access, the level playing field, sustainable development, and dispute settlement. I analyzed in each of these sectors the presented changes while providing critical insight into their significance also by comparing with the negotiating practice of the parties,

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<sup>101</sup> See DIMOPOULOS, *supra* note 7, at 51.

<sup>102</sup> See European Council, *Comprehensive Economic and Trade Agreement (CETA) Between Canada, of the One Part, and the European Union and Its Member States, of the Other Part*, Oct. 30, 2016, 2017 O.J. (L11) 23.

<sup>103</sup> See CAI, *supra* note 57, section VI, sub-section 2, art. 3.

<sup>104</sup> See Ning Hongling & Qi Tong, *A Chinese Perspective on the Investment Court System in the Context of Negotiating EU-CHINA BIT*, 11 TSINGHUA CHINA L. REV. 91, 94 (2018).

especially the Phase One Agreement concerning China and the EU-Vietnam FTA in relation to the EU.

If we summarize the presented changes, in market access CAI brings a relatively extensive number of open sectors in China, the most important of which, for the EU, is the manufacturing sector – especially the automotive industry. Other sectors such as healthcare, research, fintech and business services are also a significant shift. In contrast, the EU's commitments in the CAI relate only to a slight improvement in access to the energy sector and some manufacturing sectors<sup>105</sup> as the EU is already almost completely open to investors.

The new obligations of the parties in the area of the level playing field are perhaps the most important part of the agreement. Many of these provisions are unique and contribute to improving mutual investment relations. First and foremost, new obligations and transparency concerning SOEs, further rules in state subsidies, which may distort the position of investors, a ban on forced technology transfer, but also the simplification of administrative processes and the issuance of licenses are all significant and desired changes.

Yes, as some point out,<sup>106</sup> some areas such as intellectual property protection or access to public procurement are missing in this agreement, but there is room for a complex solution in the future. The provisions on sustainable development have been the most criticized, even though they bring about completely new commitments to which China has not previously committed itself with another trading partner. It is true that sustainability commitments are soft in nature and cannot be enforced, and it is this fact that has been criticized the most.<sup>107</sup> However, one should ask what the EU could offer in return for these commitments? Besides, many of the sustainability provisions are more of a European value agenda than a matter of direct concern to investment. Nevertheless, China has pledged itself to them, albeit in the form of soft law, it is still a significant commitment.

Dispute settlement involves an informal way of resolving disputes through mutual dialogue and a formal way of arbitration, whereas it will be a state-to-state model. An innovative tool is the establishment of a mutual discussion forum on a regular basis, directly at the highest political level. In the future, it will be important to negotiate a comprehensive system of investment protection; given the ongoing discussions on the international system of protection,<sup>108</sup>

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<sup>105</sup> See CAI, *supra* note 57, EU's Schedule of Commitments and Reservations, Annex III., 19. Energy Services.

<sup>106</sup> See Karry Lai, *EU-CHINA Comprehensive Agreement on Investment*, IFLR (Feb. 23, 2021), <https://www.iflr.com/article/b1qp5tynd2h1h/primer-eu-china-comprehensive-agreement-on-investment> (last visited Nov. 8, 2021).

<sup>107</sup> See Markus Krajewski, *Dancing with the Dragon: The new EU-China Investment Agreement*, VERFASSUNGSBLOG (Jan. 5, 2021), <https://verfassungsblog.de/dancing-with-the-dragon/>.

<sup>108</sup> See UNCITRAL, *Working Group III: Investor-State Dispute Settlement Reform*, [https://uncitral.un.org/en/working\\_groups/3/investor-state](https://uncitral.un.org/en/working_groups/3/investor-state) (last visited Nov. 10, 2021).

it is questionable whether the parties will be able to negotiate it within 2 years as they committed.

If we are to evaluate the CAI overall, from my point of view, it is a very important agreement that will help mutual relations. Under this agreement, China will be reassured that European markets will remain open to its investors, that it will prevent arbitrary or discriminatory treatment to Chinese investors in the EU, and that the consolidation of European investors' rights in China will attract a new wave of investment and might be a significant stimulus to the Chinese economy. After all, the interest in an inflow of investments is mutual. Besides, China has several significant competitors in the region that attract European investors, of which have already concluded investment agreements with the EU – countries such as Vietnam, South Korea, and Singapore.<sup>109</sup> Thus, another advantage of the CAI for China is to match the regional competition in the eyes of European investors. By ratifying the CAI, the EU will gain all the analyzed benefits for European investors in China's market and the EU will, at least formally, solve many of the problems that its entrepreneurs have faced. Of course, time will tell how these commitments work in practice.

Also, China has committed itself to important value concessions that go beyond investment, thus strengthening the EU's international position as a strong negotiator. The EU has been seen in many ways as a weaker partner in its transatlantic alliance, which has proved to be disadvantageous, especially during the previous US administration. Many may not like this fact, but by concluding such a substantial investment agreement with China, the EU strengthens its strategic autonomy. Moreover, as in the case of China, European investors are interested in the Chinese market and at present not only as a place of production but also as a market for sales. By concluding the Phase One Agreement, US companies in China have gained certain advantages over other foreign competitors, and if the CAI would be ratified, EU companies gain, in some respects, even better conditions than their US counterparts, which will be a competitive advantage.

When comparing CAI with the Phase One Agreement, we must state that both aim at different goals. The CAI is a much more comprehensive and reciprocal document. While the Phase One Agreement sought to obtain mainly concessions and commitments from China, the CAI commits both parties equally. The Phase One Agreement regulated some areas that CAI does not deal with, such as currency, IP rights, and especially obligations to purchase US products. CAI, on the other hand, regulate the relationship to the longer term and builds on values and more complex issues such as government subsidies and the market position of SOEs. Comparing the CAI and the EU-Vietnam FTA, the latter is, a more comprehensive document<sup>110</sup> that addresses many issues in the same way as in CAI (EU negotiators have learned from it),

<sup>109</sup> Hallinan, *supra* note 81, p. 47.

<sup>110</sup> As it is not focused solely on the investment, but rather trade as a whole.

but also many other issues that are not included in the CAI and will be the subject of further negotiations. Compared to Vietnam, China is a larger and, in some respects, more difficult partner, therefore the negotiations take longer, and we can consider the CAI as their first partial outcome. In this regard, the CAI is paving the way for further negotiations, the first of which will be the one to which the parties have committed themselves – investor protection and the subsequent, more complex, free trade agreement.

It must be acknowledged that the CAI also has shortcomings, but perhaps the biggest of them is on the EU side, that the past statements of its representatives have raised huge expectations.<sup>111</sup> The resulting document, however, chooses gradual steps rather than radical changes, which is understandable given the EU's negotiating position, yet some are disappointed by this approach.<sup>112</sup> As for content criticism, it is necessary to be aware of the position and leverage of individual parties in the negotiations. Even the length of the negotiations suggests that the agreement was not born easily and that mutual concessions were difficult to obtain. An argument against this criticism may be the attitude of those most affected by CAI – investors. Maintaining the current regime is not advantageous for European entrepreneurs, especially compared to competition from the USA, and gradual change is much more beneficial for them.<sup>113</sup> A significant part of the criticism does not concern the content of the agreement itself, but the political context, *i.e.*, that it was concluded by the EU without cooperation with the USA and in the time before the new US administration took office.<sup>114</sup> From this point of view, however, the European position is clear and logical – to value alliances but to act autonomously and, first and foremost, in the interests of its citizens, just like the US in the case of the Phase One Agreement. It is, therefore, necessary to distinguish between substantive criticisms that can help to improve the EU-China agreement in the future and criticisms based on an aversion to the strategic independence of the European Union.

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<sup>111</sup> For example, Directorate-General for Trade, *EU and China Agree on Scope of the Future Investment Deal*, EUROPEAN COMMISSION (Jan. 1, 2016), [https://policy.trade.ec.europa.eu/news/eu-and-china-agree-scope-future-investment-deal-2016-01-15\\_en](https://policy.trade.ec.europa.eu/news/eu-and-china-agree-scope-future-investment-deal-2016-01-15_en) (last visited Nov. 8, 2021).

<sup>112</sup> See *e.g.*, Carafano et al., *supra* note 61; Eleanor Mears & Giorgio Leali, *MEPs Emerge ss Top Hurdle to EU-China Trade Deal*, POLITICO (Jan. 6, 2021), <https://www.politico.eu/article/eu-china-trade-deal-european-parliament-objections/> (last visited Nov. 8, 2021).

<sup>113</sup> See the EU Chamber of Commerce in China, *Analysis of the CAI: What's in It for European Businesses in China?*, Mar. 19, 2019, [http://european-chamber.com.cn/en/national-news/3332/analysis\\_of\\_the\\_cai\\_what\\_s\\_in\\_it\\_for\\_european\\_businesses\\_in\\_china](http://european-chamber.com.cn/en/national-news/3332/analysis_of_the_cai_what_s_in_it_for_european_businesses_in_china) (last visited Nov 9, 2021).

<sup>114</sup> See Theresa Fallon, *The Strategic Implications of the China-EU Investment Deal*, THE DIPLOMAT (Jan. 4, 2021), <https://thediplomat.com/2021/01/the-strategic-implications-of-the-china-eu-investment-deal/> (last visited Nov. 9, 2021).