China’s BIT Progress and Implications for China-Canada FTA Talks
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Introduction

Rising protectionism since Brexit in the United Kingdom and the election of Donald Trump in the United States poses challenges to the global economy. How China, the second-largest economy, responds to these threats will not only affect the direction of the global economy, but also its own interests. On January 17, 2017, Chinese President Xi Jinping delivered a keynote speech at the World Economic Forum annual meeting in Davos, Switzerland, stressing that China is the defender of globalization and the world trade order, and will continue to open up to the world (Xi 2017). On the same day, the State Council promulgated a matching document, the “Notice on Measures for the Active Use of Foreign Investment in Opening Up to the Outside World” (also known as “20 Measures”) (State Council 2017), which introduced new policies to enhance market access and promote fair competition for foreign-invested enterprises (FIEs) in China.

Despite the skepticism around the question of whether China can really take on the leadership of the global economy, pushing forward the further opening up of its economy seems to be the only choice for the country. Driven by economic slowdown and the pressure of the Trans-Pacific Partnership (TPP), China has gradually but firmly shaped an outward-looking economic strategy since the Xi-led leadership came to power in 2013. That is, it has sought to open its economy to foreign investment and...

Key Points

→ The progress of the China-US bilateral investment treaty (BIT) talks shows that China is embracing a next-generation BIT.

→ Complicated domestic politics have influenced the last stage of the China-US BIT talks. While top leadership in China must intervene to break the stalemate, the US business community has pressed hard on the US government on a variety of issues.

→ China’s acceptance of the next-generation BIT with unilateral liberalization is promising for the forthcoming China-Canada free trade agreement (FTA) talks. It could be much easier for the two sides to reach agreement on investment and service trade.

→ The talks offer China and Canada a special opportunity to stabilize the regional and world trade order currently challenged by rising protectionism.
pursue a high-standard BIT with its key trading partners, the United States and the European Union; to speed up FTA talks with high(er) standards to build China’s free trade network; and to initiate the Asian Infrastructure Investment Bank and the One Belt, One Road Initiative to improve the international governance structure and promote development and international economic cooperation in Asia and beyond. All of these policies combine to form version 2.0 of China’s vision of reform and opening up (Wang 2016).

Although BITs and FTAs have been pursued separately, they are highly related, and the offers in China’s BIT talks will inevitably spill over to the FTA negotiations. More noticeably, China has carried forward the efforts of unilateral investment liberalization while pursuing BIT and FTA talks, which has improved the business environment for FIEs in the Chinese market.

In this new context, the forthcoming China-Canada FTA talks present an unprecedented opportunity to strike a deal favourable to both economies as well as boost confidence in the international trade order under threat from rising protectionism. With the progress achieved in China’s latest BIT talks and unilateral investment liberalization, Canada and China are expected, with cautious optimism, to reach agreements in less time than might be expected.

China’s BIT Progress:
Into a Next-generation Agreement

China has signed over 100 bilateral investment agreements (BIAs), most of which were completed after the reform and opening up began in the late 1970s. Of these, 78 were signed with developing countries and 26 with developed countries, including Germany, the United Kingdom and Canada (Peterson Institute for International Economics [PIIE] 2015). Generally speaking, almost all of these BIAs are aimed at protecting rights after investment, and pre-establishment market access rights for investors are left out.

A new generation of BITs has been in development in China. In addition to investment protection,
China’s next-generation BIT talks have emphasized market access or opening up. In the ongoing China-US BIT negotiations (and the China-EU BIT), China has accepted pre-establishment national treatment combined with the negative list model in the administration of foreign direct investment. China has also agreed to advance the BIT talks by being more willing to accommodate the 2012 US model BIT text, including more issue areas, such as intellectual property, labour and environmental protection, and so on (Liang and Dong 2013).

The following factors may account for China’s stance on incorporating market-opening clauses into the BIT negotiations with the United States and the European Union.

First, since the global financial crisis of 2008, the pressure of demanding reciprocity in market access has risen among US and EU companies with investments in China. They have strong concerns about China’s industrial policies that favour state-owned enterprises (SOEs) in the form of innovation incentives, subsidies and government procurement. These foreign companies promote China to open up the market and extend them national treatment status in all activities of investment.

Second, Chinese decision makers assume that a high-standard BIT can be leveraged to lower the barriers that China’s growing outbound investment faces in host countries. For example, Chinese negotiators hope that the BIT can address the concerns Chinese investors have about the arbitrary and non-transparent procedures of the Committee on Foreign Investment in the United States in the name of national security (Shen 2016). China’s outbound investment (non-financial) is expected to jump to US$170 billion in 2016 (Renminwang 2016). Chinese investors are increasingly calling for the government to strengthen protection by negotiating high-standard agreements with host nations.

Third, the Chinese economy has been under the so-called “new normal” conditions, which should be focused on increased consumption and innovation to ensure a successful transformation. Relaxed market access for FIEs has great potential to bring in badly needed technology and skills, in particular in the service industry and high-end manufacturing.

Last, the next-generation BIT should help to relieve the competition and pressure from US-driven megaregional FTAs, including the TPP and the Transatlantic Trade and Investment Partnership, which exclude China. The Chinese leadership has set a clear goal: China should play a leading role in global economic governance, and in order to meet this objective the country should open its economy further to gain bargaining chips in reshaping the twenty-first-century rules of the international trade and investment order (He 2016; Wang 2016). Obviously, the country has adopted such proactive measures to counterbalance the TPP effects of trade diverting.

Comparison of BIT Talks with the United States and the European Union

The China-US BIT negotiations were launched in 2008, and through several rounds of talks, the differences over the core issues, including the status of SOEs, intellectual property protection, transparency and standard-setting, did not diminish. Major progress was made in July 2013 under China’s new leadership, when China conceded that the “pre-establishment national treatment plus negative list model” in the administration of foreign investment should be the basis of the BIT negotiations (Bai 2016).

China’s substantial concession on market entry put the talks on a fast track. As a result, in early 2015, both sides reached agreement on the core text and main terms of the BIT. In June 2015, they exchanged the negative list for the first time, and began negotiations on this key issue. Since then, the two sides have exchanged negative list bids three times, in September 2015, June 2016 and September 2016 (Bai 2016; Guo 2016).

As the China-US BIT talks reach the “final” stage, the negotiations are increasingly influenced by the complicated and sensitive domestic politics in the two countries. Although the Ministry of Commerce (Mofcom) acts as the chief coordinator in China, the negative list should be a combined offer from different regulatory agencies, which may harbour more substantial influence and work desperately with “vested interests” in various industries to ensure the list is as long as possible. As previous negotiations have shown, the stalemate caused by bureaucratic politics can be broken only by...
intervention from top leadership, which acts based on the domestic and foreign agenda (Wang 2002). A recent example of such intervention was the “significant” progress in the BIT negotiations on the eve of the summit meeting between President Xi and former US President Barack Obama before the Group of Twenty leaders’ meeting held in Hangzhou in early September. The political leaders clearly had a stake in substantiating the relations in the year of a US election, and the intensive talks in Beijing from August 21 to 28, 2016, and the small-scale meetings of the heads of the delegations from August 29 to September 3 achieved a much shorter negative list. At the same time, both sides once again confirmed the high-level agreement regarding the “shared goal of creating a non-discriminatory, transparent and open investment regime” (Mofcom Press Office 2016; Guo 2016).

On the US side, the United States Trade Representative (USTR) and the business community engage in a complicated political game as well. The US business community has pressed hard on the US government, not only for a shorter negative list, but also on many issues that are not included in the 2012 US model BIT, such as China’s rules surrounding data flows and other data-related requirements, SOEs, discriminatory enforcement of the anti-monopoly law and forced technology transfer. US business representatives claim that they are more concerned about the quality and scope of the BIT than on when the talks will wrap up (Caporal 2016). Therefore, the USTR acknowledged China’s efforts on the BIT talks as “full engagement,” but complained that “China has not yet decided to pursue a sufficient reduction of its investment restrictions to enable the successful conclusion of those negotiations” (USTR 2017). The Trump administration’s “America first” policy and the higher expectations of the US business community will inevitably prolong the process of BIT talks between the United States and China.

Compared to the China-US BIT negotiations, the progress of the China-EU BIT negotiations has been relatively slow. Prior to the start of the BIT negotiations in 2013, China signed a number of BIAs with European countries in the 1980s and 1990s, with the main focus on investment protection rather than on market opening. In order to deal with new challenges in the Chinese market, the European Union pushed forward the China-EU BIT negotiations to focus on issues such as higher-standard liberalization with respect to market access, transparency, labour treatment, the environment, investment arbitration and so on (Bai 2016).

Unfortunately, the China-EU BIT talks have not yet achieved significant progress. Two factors have shaped the slow pace of the negotiations. The first factor lies in the change of expectations. While the European industries insist on China meeting the principle of reciprocity in market access, there are more concerns about the rising amount of Chinese investment in Europe. The second and more important factor is the difficulty of internal coordination among the member states of the European Union because of different demands. For example, developed-country members of the European Union give priority to the protection of investment interests in China, while the Central and Eastern European members are more concerned with attracting investment from China (ibid.).

Unilateral Liberalization: China’s Preparation for BIT Risks

Shortly after the new leadership came to office in 2013, China introduced experimental Pilot Free Trade Zones (PFTZs) in Shanghai in 2013 and then in Tianjin, Guangdong and Fujian in 2015. PFTZs do not focus mainly on trade liberalization, but on testing the risks of relaxing foreign investment-related regulations, involving the establishment of FIEs based on the negative list; trade in services; capital controls; the convertibility of the Chinese currency, the renminbi; and improving the standard of intellectual property rights and trade facilitation. Streamlining the government administration structure and procedures are also part of the experiment. The PFTZs can be regarded as China’s unilateral efforts to promote liberalization on foreign investment, which is in accordance with the practice and experience of the incremental approach toward reform and opening up in the last three decades (Ma 2008; Liu 2008). The political leaders of different periods since the beginning of the reforms have emphasized that China, as a major developing country with a huge population, should try and test each step of the reform and
opening up policy before implementation. For instance, the regulators call for coping vigilantly with the potential risks of opening the financial markets to foreign investors, which is believed to easily transmit into the whole economy.

However, the extension of PFTZs and unilateral investment liberalization have gone hand in hand with the progress of the BIT negotiations, in particular those between China and the United States. In the eyes of political leaders, the BIT talks let them play a game of building pressure on domestic reform by committing to external obligations, as was demonstrated in China’s bid for World Trade Organization accession, which stimulated the reforms of SOEs and the government system. The BIT talks are also in line with the political logic of the reform of China (China Government Net 2016).

While China has offered significant concessions in the China-US BIT talks (mainly pre-establishment national treatment with the negative list), it has made several efforts to cut down the length of the negative list with regards to market access to FIEs. In preparing for the scenario of concluding the BIT with the United States in late 2016, China’s legislature, the National People’s Congress, voted to amend the four laws related to FIEs in China, granting FIEs the right of pre-establishment national treatment combined with the negative list. The results of this liberalization of unilateral investment are encouraging. From January to June 2016, more than 99 percent of the FIEs in the four PFTZs were established through filing rather than administrative approval; the government processing time was reduced to three business days down from 20; and the 93 restrictive measures in the 2015 edition of the Catalog of Foreign Investment (including 19 items in the “encouraged” category with limited share of ownership, 38 “restricted” items and 36 “prohibited” items) have been reduced to 62 items in the 2016 edition (National Development and Reform Commission 2017).

More recently, the State Council (2017) promulgated a more radical document, the “Notice on Measures for the Active Use of Foreign Investment in Opening Up to the Outside World,” which introduces new measures to enhance market access and promote fair competition for FIEs in China. This document promises to greatly improve the market access of FIEs in the sectors of services, manufacturing, mining and infrastructure (ibid.). Although the enforcement details have not yet come out, it is believed that FIEs will be granted more opportunities in China (Sun 2017).

### Implications for China-Canada FTA Talks

In policy planning, the Chinese government hopes that FTA negotiations can follow the BIT talks with the United States and the European Union, and that both BITs and FTAs are able to deepen the economic interdependence among the three major trading powers. The current harsh reality in Europe and the United States is making this blueprint more difficult to realize politically, at least in the short term.

However, one thing is certain: China will further open up its economy by engaging in more high-standard BITs and building its own FTA network for domestic and international interests. As C. Fred Bergsten argues, the progress on BITs will spill over to FTA talks (PIIE 2015), and with the raised-standard BITs China will sign, the standard of the investment-related part of FTAs will be boosted as well. In recent years, China has signed 14 FTAs, involving 22 countries and regions such as the Association of Southeast Asian Nations, Singapore, Pakistan, New Zealand, Peru, South Korea and Australia, to cover about 40 percent of China’s total foreign trade (Xia 2016). Through the BIT talks and unilateral liberalization, China is confident it will be able to offer more assertive concessions to trading partners, including in the investment area. In the context of the US withdrawal from the TPP and rising protectionism, China has set the target that it will expand market opening in the financial, educational and cultural sectors, liberalizing foreign investment in service industries such as pensions, construction, design, accounting, auditing and e-commerce (State Council 2017).

Although uncertainties have been raised on the future of a BIT under the Trump administration, it would be possible for a BIT deal to be included in the resolution of US-China trade relations.

Signed in 2012, the Canada-China Foreign Investment Protection Agreement was perceived to be the highest-standard investment agreement China ever entered, according to Chinese analysts (Mofcom 2012) — until now, that is. Although it is not known when China and the United States will
wrap up the BIT talks, China has committed to pre-establishment rights to FIEs with a shortened negative list, demonstrating the country’s strong will to open its market to foreign investors.

China’s acceptance of the new generation of BITs with unilateral liberalization undoubtedly places the forthcoming China-Canada FTA talks in a more promising and open environment. Specifically, it could be much easier for both sides to reach agreement on investment and service trade, based on the BIT offers China has made and implemented. While it is to be expected that the two countries may differ on accepting China’s SOEs investment in Canada and the restrictions on FIEs, such as data localization in the Chinese market, China and Canada have more reasons and imperatives to launch and speed up the FTA talks given the grim challenges to regional and world trade orders following the US election. Optimism may be justified in expecting that the China-Canada deal will take less time than the one between China and Australia, if both sides manage their respective expectations and are willing to make concessions.

Works Cited


The Dragon’s Footprints
China in the Global Economic Governance System under the G20 Framework

Alex He

Under the shadow of the global financial crisis, China’s participation in the Washington G20 Summit in 2008 marked the country’s first substantial involvement in global economic governance. China played a significant role in the global effort to address the financial crisis, emerging onto the world stage of international governance and contributing to global macroeconomic policy coordination in the G20 ever since.

The Dragon’s Footprints: China in the Global Economic Governance System under the G20 Framework examines China’s participation in the G20; its efforts to increase its prestige in the international monetary system through the internationalization of its currency, the renminbi; its role in the multilateral development banks; and its involvement in global trade governance.

August 2016
978-1-928096-23-8 | paperback
978-1-928096-24-5 | ebook

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Patrick Leblond and Judit Fabian

This paper proposes changes and additions that should be part of an updated NAFTA. The focus is on the NAFTA elements that have been subject to criticism since the agreement’s entry into force. It offers a fairly detailed road map to the agreement’s modernization. This paper does not, however, provide a chapter-by-chapter, article-by-article review of NAFTA. Regardless of the rhetoric coming from the Trump administration, it is the authors’ view that Canada’s position should be to approach any NAFTA renegotiation from a “best case” perspective in view of making trade and investment in North America easier for business.

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CIGI Paper No. 121

Dan Ciuriak

Intellectual property is essential for commercialization in the knowledge-based economy. However, the creation of intellectual property rights (IPRs) has led to potential stumbling blocks for industrialized research and development and continuous and massively parallel innovation. This potential has been actualized through the untrammeled proliferation of IPRs in recent decades. This paper argues that this proliferation has strategic roots at the national level, based on the potential to capture global rents through the internationalization of IPRs.

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Joël Blitz

This paper discusses the theoretical case for strong national patent regimes in the context of a globalized world. The national treatment of foreign inventors gives countries an incentive to free ride, and while this can be overcome through patent rights harmonization agreements, these present coordination challenges. Theory and empirical evidence suggest that Canada’s patent regime is doing little to promote domestic innovation, while generating significant deadweight losses for the economy. The conclusion is that Canada’s interests would best be served by a weaker national patent regime, subject to its current international obligations.

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CIGI Policy Brief No. 96

Sarah Burch

Canada has pledged to reduce its greenhouse gas (GHG) emissions by 30 percent below 2005 levels by 2030, and has developed a Pan-Canadian Framework on Clean Growth and Climate Change. Canada must seek to reduce GHG emissions while enhancing economic and environmental resilience. This policy brief examines what is known about sustainability entrepreneurship in small and medium-sized enterprises and elaborates on knowledge gaps that have stymied effective policy making.

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CIGI Policy Brief No. 95

Dan Ciuriak

China continues to grow in strategic importance as a trade and innovation partner. A new China is emerging — young, urban, university-trained and tech savvy. Driven by its singular focus on technological advance, and fuelled by heavy research and development (R&D) spending and a rapidly growing R&D workforce, China is becoming an innovation hub. China wants a free trade agreement with Canada; as globalization faces headwinds in Canada’s traditional markets, Canada should seize the offer.

A Transatlantic Perspective on CETA

CIGI Policy Brief No. 89

Patrick Leblond

As the trade deal between Canada and the European Union is signed at a ceremony in Brussels following a bumpy round of shuttle diplomacy, this policy brief suggests that the Comprehensive Economic and Trade Agreement (CETA) would generally be positive for businesses in Canada and Europe and would reinforce the transatlantic alliance between Europe and North America. CETA’s new investor protection mechanism achieves the right balance between protecting business interests and allowing governments to regulate their societies and economies according to their democratic mandates. The policy brief outlines some of the key benefits that have been identified, arguing that CETA is seen as a clear benchmark in trade policy.
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