China and WTO Review (CWR)
2024, 10(2), 19-37
ISSN: 2384-4388
https://cwto.net
Research Article

The Alignment of the EU-China Comprehensive Agreement on Investment with the Chinese SOE Governance Framework

Rudolf Kampf [1*]

[1] S.J.D Candidate, Guanghua Law School, Zhejiang University, Hangzhou, China
* **Corresponding Author:** 2630529734@qq.com

Citation: Kampf, R. (2024). The alignment of the EU-China comprehensive agreement on investment with the Chinese SOE governance framework. *China and WTO Review, 10*(2), 19-37. https://doi.org/10.52152/cwr.2024.10.2.02

ARTICLE INFO

Received: 18 Sept 2024
Accepted: 17 Oct 2024

ABSTRACT

The following article analyzes the EU-China Comprehensive Agreement on Investment (CAI) and its ability to discipline state-owned enterprises (SOEs) within China. The CAI aims towards more balanced and reciprocal trade and investment relations between the European Union (EU) and China. The analysis scopes the contemporary legal and regulatory framework governing SOEs and explores their alignment with the CAI. The analysis adopts doctrinal and comparative research analysis, comparing the provisions featured within the CAI with China's foreign investment and SOE regulations. The findings suggest that the CAI features strong mechanisms for the purposes of investment protection, the fast-evolving investment protection framework within China is bound to soon outpace it. The presence of the Communist Party of China (CPC) however complicates the efforts towards market liberalization with CAI lacking the tools to address both CPC and state interference. The article concludes that, while CAI is a crucial step towards better investment protection, its impact on the overall liberalization of the Chinese market might be limited in scope.

Keywords: EU-China Comprehensive Agreement on Investment, Chinese State-owned Enterprises, SOE Regulatory Framework, State Economic Interventions, State Capitalism.

INTRODUCTION

The EU-China Comprehensive Agreement on Investment (CAI) promises to reshape the trade and investment relationship between the parties. The first step is the replacement of the existing European Union (EU) member state Bilateral Investment Agreements (BIT) with China, supplanting them with the CAI.[1] It provides for greater harmonization of standards of treatment between EU member states in their investments within the Chinese host state, combined with a unique opportunity to address Chinese state interference in the national economy.[2]

The CAI contains provisions aimed at disciplining the behavior of state-owned enterprises (SOEs), entities over which the state holds either partial or complete ownership control. Due to their ownership nature, the undertakings are prone to not only pursue commercial objectives but also serve the purpose of pursuing state policies. The dual nature of these undertakings can contribute towards market distortions, which can manifest as distortion of market competition, reduction in transparency of the market, and unfair competition conditions for foreign investors. The predominant cause of these distortions is the enactment of governmental objectives, which are pursued at the behest of the state via its ownership stake within the SOE. The policies can be enacted regardless of the profitability or market efficiency.

[1] European Union has already terminated a number of EU member BITs with non-EU countries and replaced them with singular EU centric BIT; see for instance "Free trade agreement between the EU and Singapore" (2019); "Free trade agreement between the European Union and Vietnam" (2020)

[2] This includes schemes such as "market-for-technology", which is usually accompanied by joint ventures with local enterprises, which may include state enterprises; on the topic see M. Zhang (2020); Lee (2020)

Copyright © 2024 by Author/s and Licensed by China and WTO Review (CWR). This is an open access article distributed under the Creative Commons Attribution License which permits unrestricted use, distribution, and reproduction in any medium, provided the original work is properly cited.

CAI aims to liberalize the Chinese market, a process of reducing barriers in trade, and investment, reducing the state's role in the economy, and providing for a fairer playing field between foreign and domestic investors.[3] Chinese liberalization, while advanced, is complicated due to the close entanglement of the leading Communist Party of China with the economic management.[4]

According to the literature, SOEs and the state sector play a major role in China's economic development, although their privileged position has diminished over time (L. Zhang, Coulson, Liu, & Zhao, 2023). Their relevance has been maintained through a series of reforms. Company law for instance affords the board of directors' elementary power. Limitations are however presented for instance by the shareholders meetings, where stakeholders are government-affiliated and outvote the board (Xun & Weng, 2024). This contributes to the belief that SOEs should be under governmental directives. Their competitiveness is maintained due to preferential treatment, particularly in cases of large central SOEs (Chang & Lin, 2021). The countries have increasingly begun to rely on the WTO framework to discipline their behavior. The Agreement between the United States of America, the United Mexican States, and Canada for instance includes provisions restricting signatory states' ability to conclude free trade agreements with non-market economies ("Agreement between the United States of America, the United Mexican States, and Canada", 2020). The inclusion of SOE provisions in international agreements may contribute towards the reform of the international framework for disciplining SOE behavior (Kong, 2023). The inclusion of the provisions invariably affects investment agreements, which have become to features SOE related provisions (Chaisse & Sejko, 2018). The CAI is not an exception but has been criticized for the lack of effective coverage of the issue as it relies on untransparent Chinese laws (Xu, 2022). The agreement is also restricting the effectiveness of its provisions by focusing on operations of foreign investors established within China, excluding EU companies without physical presence. The only major addition to the agreement is the delineation of the scope of application to various forms of governmental control (Gao, 2021).

The increased transnational proliferation of SOEs and interest in their operations raises the question of the alignment between the international perceptions exemplified by multilateral and bilateral treaties and national regulatory frameworks. The presented article seeks to analyze but one facet of a complex framework governing international investment by focusing on the alignment between a singular BIT, the CAI, and the SOE governing framework within China. The article examines whether CAI's provisions align with China's evolving regulatory framework for market liberalization and SOE management framework. It explores the capability of the CAI to tackle state interference and promote a level playing field for EU investors.

The article argues that while CAI offers various mechanisms for disciplining SOEs, it fails to address the role of the CPC within the SOEs. Through doctrinal and comparative analysis, comparing CAI's provisions with those of China, the paper highlights obstacles in the way of true liberalization, just as the limitations of the CAI.

The first section, that being the introduction, provides introductory remarks on the issue of both CAI and Chinese SOE governance. The second section dubbed "China's National Legal Framework Governing SOEs" provides the legal historical framework underneath which the Chinese SOEs operate, introducing their role and key laws that dictate their *modus operandi*. The third section "The Compatibility of CAI Provisions with China's SOE Legal Framework" follows the objectives of exploring the legal framework that governs investment frameworks within China and its alignment with the provisions stipulated within the CAI. The fourth section "The Limitations and Challenges" provides a critical analysis of the existing framework governing state interventions in the Chinese economy, including the subsidies and predominantly the political interference, which is the core issue facing Chinese SOEs. The last section, the conclusion, summarizes the article, while also featuring concluding remarks.

CHINA'S NATIONAL LEGAL FRAMEWORK GOVERNING SOES

The country since its inception on the 1st of October, 1949 followed the principles of socialist economic models, centralizing the power over the market and means of production within the Central government akin to its Soviet Union counterpart. Banks, factories and other property were sized from the previous Nationalist government, contributing towards the formation of the first SOEs (L. Wang, Liu, Fu, & Wu, 1989, footnote 1). The complete transition towards state ownership and a planned economy has been cemented by the 1954 Constitution,

[3] The concept of liberalization itself can take many forms but is generally described as the act of allowing more freedom in laws, systems, or opinions, see Liberalization (n.d.).

[4] Due to the extent of the SOE proliferation and their importance, liberalization is inevitably bound to impact SOEs, either directly or indirectly, for an example of entanglement between market liberalization and SOEs from the case of Cuba, see Sokol (2017)

which establishes the Communist Party of China (CPC) as the principal guiding force of the economy under the supervision the of the working class ("Constitution of the People's Republic of China (1954)", 1954). The shift towards a planned economy saw the significantly fluctuating performance, with the World Bank data outlining that the GDP growth per year between 1961 and 1964 saw rapid growth from -27.3 to 18.3 per cent respectively. The performance was subsequently reduced by -5.8 per cent in 1967 and recovered to 19.3 per cent by 1970, signaling significant deficiencies in the economic model and the need for action[5] (World Bank, n.d.).

The 1970s brought an era of limited reforms, focusing on improving efficiency but maintaining state control without introducing meaningful private ownership (Nolan & Ash, 1995). These reforms intended to introduce incentives for the management of the SOEs to pursue market-oriented objectives.[6] Facilitation of rapid modernization for the purposes of increasing the competitiveness of the enterprises has been undertaken by encouraging both private and foreign investments under the joint venture (JV) arrangements, to allow the Chinese economy access to more advanced technologies in a scheme that would be known as technology for access to market approach.[7] For instance, the Law of the People's Republic of China on Chinese-Foreign Equity Joint Ventures demanded the use of up-to-date technology, otherwise being at risk of having to pay compensation for losses caused by deception by using outdated technology ("Law of the People's Republic of China on Chinese-Foreign equity joint ventures", 1979).

The oversight over economic development has been established by having both JVs and foreign capital enterprises encouraged to make deposits within China. The point of contact for foreign transfers and currency exchange is set as the Bank of China. Alterations were subject to the relevant state agencies under the "Law of the People's Republic of China on foreign-capital enterprises (1986)" (2014). The government could thus more easily monitor the flow of currency in a relatively closed economic environment and exercise foreign exchange control. It also allowed for adjustments to the "cost of foreign exchanges", a system, which remained in place until late 1970.[8] It followed an era of partial liberalization of the market by loosening currency controls and a slow movement towards pegging Yuan to US dollars.

The economic reforms have had an effect on stabilizing national growth by reducing the volatility of the GDP growth with the only tangible negative growth occurring in 1976, with -1.6 per cent (World Bank, n.d.). The contributing factor is also the decade-long cultural revolution, which officially ended in October 1976. The SOEs were still nonetheless plagued with excessive amounts of non-performing loans. The model of dedicated state ownership was no longer sustainable but simultaneously offered an opportunity for the SOEs to denationalize (W. Zhang, 2015).

Major restructuring into larger and more profitable enterprises has been undertaken while selling or merging existing smaller SOEs. Conducted under the umbrella of the "grasping the large and letting go of the small" policy conferred under the 15th National Congress of the CPC in 1997 (Xinhua, 2008). The Fourth Plenary Session underlined the key role of the SOEs as the centerpiece of national economic development but also stipulated the need for enterprises to be unburdened of any associated debt within three years and the need to reform the medium to large enterprises into enterprises that are fit for the new century. The management was to be overhauled, introducing reorganization and transformation, while at the same time promoting various ownership types, presumably both private and public, simultaneously. Promotion of technological innovation, just as market competition, also appeared on the agenda (People's Daily, 1999). Reforms additionally reduced policy regulations of the SOEs, while strengthening the respective state ownership rights. The results of the policy at the break of the millennium saw a significant increase in the profitability of the enterprises, emerging as significant competitors to privately owned enterprises (Rui, 2013).

The state thus began a slow shift towards becoming a shareholder in the SOEs, a major change from being the principal singular owner. The transition becomes codified with the rise of the State-owned Assets Supervision and Administration Commission (SASAC), the preeminent state organ responsible for the management of the state enterprises under the Interim Regulations on the Supervision and Administration of State-owned Assets of Enterprises. The regulation establishes the State-owned assets supervision and management system under the purview of the State Council, outlining the objective to address the needs of the socialist market economy,

[5] The Great Leap Forward between the years 1958 and 1960 significantly contributed towards the economic volatility; see Walder (2016)

[6] These reforms are commonly referred to as "management responsibility system"; see W. Zhang (2015)

[7] China under joint ventures would predominantly provide the land and improvements, while the foreign investor would provide the know-how and cash; see Heller (1986)

[8] China during this period practiced what could be called dual exchange rates; the official rates, which were usually overvalued, while also implementing internal exchanges, which were artificially set by the government; see Yu (2018)

established on May 13th, 2003 (“Interim regulations on the supervision and administration of state-owned assets of enterprises”, 2003). The SASAC is tasked to guide the SOEs into a modern enterprise system, including implementation of reforms, with wholly state-owned enterprises being under the sole control of the SASAC in regards to bankruptcy, dissolution, mergers, investments, and so on, following approval process at the same governmental level as the applicable SASAC branch for the former three.

The SASAC was later intended to become the principal stakeholder under The State Council with the principle being enshrined under the China Law on State-owned Assets of Enterprise, established on October 28th, 2008. It establishes SASAC as the foremost institution for the management of state property, while also delegating the role of an investor to the State Council and governments at the local levels, with the former being responsible for the management of larger SOEs.

The local governments may establish or delegate their duties as investors to other departments at their discretion. The law promoted the development of the socialist market economy and established the leading role of the SOEs as the engine of the state-led economic model. The main objective of the presented regulations has been to administer state-owned assets, just as their transfers, sales and liquidation (“The People's Republic of China Law on state-owned assets of enterprises”, 2009) The SASAC is established as the preeminent investor under Article 11, which grants it the associated benefits, allocating it the ability to appoint the board of supervisors under Article 19 in wholly state-owned enterprises and other key personnel under Article 22. It additionally gains the ability to propose candidates for the positions of directors and supervisors to the shareholders meetings in cases of state-owned capital holding companies and state-owned capital shareholding companies. The expanding scope of the SASAC’s ability to coordinate and participate in the running of the supervised SOEs permits the State Council and the Central Government to exercise significant control over the Chinese economy.

The overall true privatization has however never truly materialized, predominantly due to the CPCs unwillingness to let go of such a significant instrument for the management of the economy. The Party has repeatedly stressed, both within the constitution and relevant laws, that the CPC leadership is paramount to the economy and the SOEs are, if not subject, then at the very least obligated to provide for the establishment of the Party organizations within their structures (Qiushi Journal, 2021).

The mixed-ownership reforms introduced in 2015 follow the established goals of the previous decades to improve the efficiency of the SOEs. It aims to do so via a slow and gradual introduction of the private element into the ecosystem of the state managed assets, while preserving elements of state presence. The Guiding Opinions of the Central Committee of the Communist Party of China and the State Council on Deepening the Reform of State-Owned Enterprises underline that the existing SOE reform has generally achieved its goals of improving the efficiency of the SOEs. They have introduced incentives to pursue business oriented and sound objectives, strengthening the managerial roles as professional positions. The Central government plans to deepen the established trajectory by promoting independence and market-oriented policies within SOEs (Xinhua, 2015a). The reform explicitly underlines a shift from factor driven to an innovation driven model of operations for the future of SOEs, indirectly indicating an objective of matching the productivity of the enterprises of the United States featured on the Fortune 500 list, which is 2.5 more profitable than the Chinese SOEs featured on the same list.

Key areas and areas subject to national security however remain locked behind monopolistic or majority state control, while commercial SOEs are open to foreign investment, even majority foreign ownership with listing under 2018 indicating liberalization within telecommunications, aviation, petroleum and petrochemicals and energy industry, alongside closely unspecified military industries (Economic Daily, 2018).

The reforms continue to exhibit similar issues as in the past, namely the state control. Under the existing proposals, the state maintains majority control in most SOEs subject to privatization (Yang, 2015). Additionally, the existing regulation preserves the establishment of the Party leadership as key to the national economic development and the core of the SOE, which includes the Party organizations.[9] The leadership of the CPC in the economy is codified under the Constitution of the People’s Republic of China, highlighting Party’s key role in the development of the country. Article 1 of the constitution stipulated that “Leadership by the Communist Party of China is the defining feature of socialism with Chinese characteristics.” The Party as a result seeks to embed itself into the corporate structures despite increased privatization (The State Council of the People's Republic of China, 2018).

China’s road from the state controlled economic model towards embracing elements of free market has been

[9] It should be noted that even outside of the Party organizations embedded into the SOEs, members of political bodies have shown increased presence at the positions of CEOs, rising from 8.1% to 19.4% between the years 2002 and 2010 respectively; see L. Lin (2013)

exceedingly long and complex overall. The establishment of SASAC for instance, signified a major shift from the state's direct involvement, towards delegating its powers to specific organizations for the management of state property. The persistent challenge despite the longstanding reforms is the prevalence of party policy priorities over commercial considerations, superseding even state policy objectives. The balancing efforts between the state objectives and Party policies remain at the forefront of the issues facing China today.

Going forward, the prevalence of the Party's influence is likely to remain in the long term. The enshrining of the CPC organizations within the corporate structures is likely to hinder the true privatization of the state sector.

THE COMPATIBILITY OF CAI PROVISIONS WITH CHINA'S SOE LEGAL FRAMEWORK

Market Liberalization

The EU has long sought to gain greater access to the lucrative Chinese market, which has been characterized by stringent restrictions on investments. These restrictions include both access and operational autonomy. These have been exacerbated by performance requirements. China pledges under Section II, Article 2, to lift restrictions on the number of enterprises within select industries, just as the total number of transactions, assets, operations, options, and the number of natural persons ("EU-China comprehensive agreement on investment", 2020). The CAI retains a positive list for the purposes of market access, a unique feature as the standard of treatment provisions is almost exclusively established upon the principle of a negative list (Mavroidis & Sapir, 2022).

The actual long-term impact of the CAI remains uncertain when compared to the established negative list published by the Chinese government ("EU-China comprehensive agreement on investment", 2020; "Special administrative measures (negative list) for the access of foreign investment (2021)", 2021). Although the EU has positioned the agreement as the major breakthrough for its investments in China, the provisions closely mirror existing restrictions (Grieger, 2021). The Internet services for instance under CAI become unbound, with the exception of internet access services, which are limited to majority Chinese owned JV, a restriction present under the contemporary negative list regulations, using the term value-added telecommunications services (Xinhua, 2024).

The highly anticipated manufacturing sector under the Chinese negative list features very limited restrictions comparatively to the limitations imposed under the CAI. While the latter does not directly forbid investments into the manufacturing sector, focusing on limiting the ability of foreign investors to establish new enterprises and exceed national quotas in select industries. The negative list forbids investments into the, broadly speaking, areas of prepared Chinese medical herbs subject to patents. Additionally, the negative lists subject investments into the printing of publications to a majority Chinese stake. Due to fast evolving Chinese market, the CAI provisions may soon be rendered redundant by the increasing openness of the Chinese market towards foreign investments.[10]

The standard of treatment provisions within the CAI will be crucial for maintaining the agreement's relevance as the Chinese investment landscape continues to evolve. The EU, in its new generation of IIAs, follows a standardized approach towards the national treatment provisions for the basis of the agreement. It underlines the very basic understanding that the investors are to be afforded treatment no less favorable than the domestic investors. The differences in the additional provisions between the agreements generally come from the unique national circumstances between the signing parties.[11]

The present most-favored nation treatment (MFN) under CAI follows the general objective to afford the foreign investor's treatment no less favorable than investors from third countries within the territory of the host state in like situations. The MFN treatment under the EU tends to feature exemptions to substantive provisions featured in IIAs with other countries. The CAI, like its counterparts, specifically provides for exemptions to investment dispute settlement systems under Article 5 of Section II ("EU-China comprehensive agreement on investment", 2020). The MFN additionally does not provide for pre-establishment clause, weakening the utility of the CAI.

It should be pointed out that the CAI does not contain explicit provisions for the purposes of providing fair

[10] The negative list published for the year 2024 further reduces the existing industries with restricted or prohibited access to foreign investment from 31 to 29; see "Special administrative measures (negative list) for the access of foreign investment (2024)" (2024)

[11] EU-South Korea FTA for instance includes provisions for instances of Violation in Cases of Modified Treatment in Favor of Domestic Investors or Establishments; Not Liable for Foreign Character of the Establishments or Investors; Governing composition of the board of directors subject to positive list under Annex 7-A; see "EU-South Korea free trade agreement" (2015)

and equitable treatment (FET). The EU has historically set forth a list of relevant applicable acts under which FET applies or relegated the provision under intellectual property protection, which is absent under the agreement, weakening the investment protection.[12] The conservative approach towards FET could be attributable to the historically competing interests between the protection of legitimate investment interests and the right of the states to regulate.[13]

In the context of market liberalization, the extensive proliferation of SOEs throughout the Chinese market suggests that any openness to foreign investments could be indicative of a major shift in their operations. The increased investments in liberalized sectors could introduce pressure on their operations via competition.[14] The willingness to open the Chinese market in such a manner could be indicative on the part of the Central government of a possible sell-off of select SOEs as a part of the existing mixed-ownership reforms and gradual privatization.[15] However, the existing liberalization undertaken by the Chinese side has to be undertaken sequentially to avoid hampering the existing reforms undertaken while simultaneously taking steps to prevent other countries under MFN treatment from seeking increased access (Zigo, 2021).

Investment Protection

The Foreign Investment Law (FIL) of the People's Republic of China contains many similarities with the CAI. They provide for instance for the national treatment under Article 9 alongside providing for various administrative benefits, including consultations and participation in procurement activities.[16]

Unlike its predecessors, the investment protection clause in the FIL makes transfers of technology via cooperative endeavors voluntary with no requirements on the types of technologies used, aligning with the CAI's anti-performance requirements clauses. The governmental agencies and staff are expressly mandated to keep confidential information a secret ("Foreign investment law of the People's Republic of China", 2019). The requirements for the use of the most advanced technologies in JVs are mostly absent, easing tensions in a process that has been perceived as a part of the larger forced technology transfer policies.[17]

The relevant Chinese legal framework additionally no longer includes mandates for the use of the national banking system for storing or exchanging currency or proceeds from commercial or investment activities conducted within China, loosening currency and exchange control. Additionally, it permits investments without approval from the Chinese government agencies assuming the investment is made in areas and industries not covered by the negative list.

These provisions generally align with the CAI's own framework for the standards of treatment, including performance requirements, which limits the ability of the state to directly interfere in the operations of an enterprise or investments. The CAI however promises to limit the ability of the contracting Parties to influence the behavior of the relevant undertakings by imposing various limitations and/or quotas on produce or sourcing of materials, *inter alia* ("EU-China comprehensive agreement on investment", 2020). This represents a challenge to the CAI due to ambiguity in interpretation as the FIL states that

The State may, according to the requirements of national economy and social development, encourage and

---

[12] For an example of the inclusion of FET treatment in EU investment agreements, see "Free Trade Agreement between the European Union and Vietnam" (2020), Chapter 12, Section C, Subsection 1, Article 12.43.1

[13] For instance, in a case concerning plain packaging law for the purposes of protecting public health, the Australian government has been subject to arbitration by Philip Morris. The arbitration had caused significant delays in the ability of the Australian and New Zealand governments to pass legislation; See "Philip Morris Asia Limited v. The Commonwealth of Australia" (2017); Kelsey (2017)

[14] OECD estimates that the overall contribution of the SOEs towards the Chinese GDP ranges between 23-28%, while the EU makes an estimation of around 30%, with the discrepancy being caused by the overall lack of transparency in their functioning; see respectively C. Zhang (2019); "Key elements of the EU-China comprehensive agreement on investment (IP/20/2542)" (2020)

[15] Increased privatization of the SOEs is likely to draw in an ever greater number of foreign direct investments, potentially creating a self-perpetuating cycle by promoting further privatization via increased investments; see Trakman (2023)

[16] The Foreign investment law under the Article 9 stipulates that "All national policies on supporting the development of enterprises shall equally apply to foreign-funded enterprises in accordance with the law"; see The State Council of the People's Republic of China (2019)

[17] Under the WTO Case DS549: China–Certain Measures on the Transfer of Technology, the EU raised a complaint with the WTO, raising concerns over the Chinese treatment and protection of foreign IP, additionally the United States, Japan and Chinese Taipei requested to join the consultations, highlighting the broader international interest in the subject matter, see "China–Certain measures on the transfer of technology" (2018); see also "China–Certain measures concerning the protection of intellectual property rights" (2018)

guide foreign investors to invest in specific industries, fields and areas. Foreign investors and foreign-funded enterprises may enjoy preferential treatments in accordance with laws, administrative regulations or provisions of the State Council (The State Council of the People's Republic of China, 2019, Article 14).

Interpreting the key terms "encourage" and "guide" based on dictionary definition suggests a less coercive approach and might be indicative of an incentive-based approach towards performance requirements rather than a more forceful performance for market access. The word "encourage" in the English dictionary provided by Cambridge describes it as "to make someone more likely to do something, or to make something more likely to happen". The word "guide" is listed as "to influence someone's behaviour", or "to make something move in the direction in that you want it to go". This is in contrast to more forceful wording such as "must" which is described as "used to show that it is necessary or very important that something happens in the present or future" or "shall" which is described as "used to say that something certainly will or must happen, or that you are determined that something will happen" (Encourage, n.d.; Guide, n.d.; Must, n.d.; Shall, n.d.).

The CAI provides under Section II, Article 3.3 "Neither party shall pressure an investor or natural person of a Party, both directly or indirectly to transfer technology." ("EU-China comprehensive agreement on investment", 2020, Section II, Article 3.3). The exact scope and whether the relevant provisions are mutually exclusive or compatible is relatively unclear. It should nonetheless be stated that the approach taken from the perspective that such incentives, *exempli gratia* subsidies and grants, which are employed with the express purpose of attracting investments, are common across both developed and developing worlds, the provisions could be considered compatible.[18] Additionally, the CAI's own following provision

Nothing in paragraph 2 shall be construed to prevent a Party from conditioning the receipt or continued receipt of an advantage, in connection with the establishment or operation of any enterprise in its territory, on compliance with a requirement to locate production, provide a service, train or employ workers, construct or expand particular facilities, or carry out research and development in its territory ("EU-China comprehensive agreement on investment", 2020, Section II, Article 3.4).

The paragraph permits the transfer of technologies and other performance requirements subject to paragraph 2 based on voluntary or incentive-based policy, sidestepping performance requirements regulations under the CAI, and in compliance with the FIL. The limitation is however stipulated under Section II, Article 3(2) as it remains unclear whenever the incentive-based approach falls under the definition of an "advantage", and should be examined on a case-by-case basis ("EU-China comprehensive agreement on investment", 2020). The preference for using *inter alia* domestic produce, complying with domestic accreditation, and/or conducting investments into research and development can heavily disadvantage foreign-sourced produce contrary to investments made within the country ("Brazil–Certain measures concerning taxation and charges", 2018)[19]. Differential treatment may also manifest itself by the type of differential treatment; usage of domestic resources for the purposes of export versus sourcing of external materials for the purposes of assembly within the host state, putting into question the definition of national treatment under GATT 1994, predominantly the Article III ("Brazil–Certain measures concerning taxation and charges", 2018). Depending on the type of subsidy given, the various incentives may also become advantageous for foreign investors, who may become attracted by the prospects of increased returns on their investments. The potential subsequent withdrawal can damage the investor's interests.[20] The lack of FET provisions within CAI hinders the ability of the investors to pursue arbitration but the sudden withdrawal can nonetheless be detrimental towards attempts to attract investment due to perceived risks by the prospecting investors that are associated with possible sudden withdrawal of benefits.

---

[18] Australia for instance employs tax incentives to promote investments in technology and innovation; see "Tax laws amendment (research and development) act 2011" (2011)

[19] Panel Reports, para. 7.181. The European Union and Japan also raised a claim regarding the aspect of the mechanism for the calculation of the amount of resources required to be invested in R&D under the Informatics and PADIS programmes, where the amounts paid when purchasing incentivized products are deducted from the calculation. (Ibid.) The Panel found that "the mechanisms under the Informatics and PADIS programmes for the calculation of the amount of resources required to be invested in R&D accord to imported products treatment less favourable than that accorded to like domestic products, and thus are inconsistent with Article III:4 of the GATT 1994." (Panel Reports, para. 7.243) On appeal, Brazil does not challenge this finding by the Panel. (Brazil's response to questioning at the oral hearing)

[20] For instance, under Micula v. Romania, the tribunal established that the discontinuation of incentive-based policy which drew investors into the Romanian underdeveloped regions, falls under the preview of violating fair and equitable treatment, including minimal standard of treatment; see "Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania [I]" (2013)

Ownership and Control in SOEs

Chinese state capitalism is characterized by the significant presence of SOEs, which permeate with a dominant position within key economic sectors, such as banking, telecommunications, audiovisual services, and energy sectors. These enterprises can be roughly divided into two categories

1. Central SOEs, spearheading Governmental policies;

2. Locally governed/local SASAC, catering to local needs and receiving preferential treatment from their local governments, undermining competitive dynamics.[21]

The economic contribution of the SOEs is difficult to estimate but their operations are considered to make a significant contribution towards the national economy (State-owned Assets Supervision Administration Commission of the State Council, 2021). They also serve as a vehicle for spearheading the policy objectives set forth by the Central Government in Beijing. The World Bank estimates that the overall contribution of the SOEs within the country toward GDP ranges between 23 to 28 per cent, making up almost one-third of the total (C. Zhang, 2019).

The company law sets forth SASAC as the principal stakeholder, affording the enterprises a greater degree of autonomy from the state interventions (Xinhua, 2023). The law however stresses that the governance over the enterprises shall lie with the principal stakeholders alongside the board of directors, with the former, in cases of wholly state-owned enterprises, the seats are expected to be filled by both SASAC and company employees.[22] SASAC also serves as a supervisory body over the state assets, being responsible for their management, while answering to the State Council.

This position challenges the CAI, which stipulates that the supervisory bodies responsible for overseeing the assets are expected to be independent of the enterprises ("EU-China comprehensive agreement on investment", 2020). The EU could raise concerns over the involvement of the state in the enterprise operations, as was the case for their internal market in the case of Soffin/ Hypo Real Estate.

The EU in this case has established that the German Länder, acting in association with the German publicly owned SoFFin and bank Kreditanstalt für Wiederaufbau, acquired a controlling stake in Hypo Real Estate. The acquisition put into question the independence of the company by the European Commission considering the extensive leverage the state had in the decision making of the company. The control was achieved via the Financial Market Stabilisation Fund Agency, which in turn was managed by the Management Committee, which was/is composed of members of the German Federal Government and German Federal States. The potential additional negative impact on the market competition raised concerns over breaching the European Competition Law.[23] ["Regulation (EC) No 139/2004 Merger Procedure (Case No COMP/M.5508-Soffin/Hypo Real Estate)", 2009].

The EU's internal policy highlights its position on institutions such as SASAC. Being the principal stakeholder and supervisory entity may conflict with CAI provisions in the eyes of the EU. The tribunals may evaluate the role of the SOEs based on commercial considerations or if the state's actions influenced their directives. The tribunals may thus consider the ILC Articles and evaluate the role of the SOEs and whenever their actions were empowered by the state. Article 5 of the ILC Articles for instance stipulates that,

The conduct of a person or entity which is not an organ of the State under Article 4 but which is empowered by the law of that State to exercise elements of the governmental authority shall be considered an act of the State under international law, provided the person or entity is acting in that capacity in the particular instance ("Responsibility of states for internationally wrongful acts", 2001, Article 5).

The case of Jan de Nul v. Egypt concerning the dispute over the widening of certain sections of the Suez Canal serves as an illustrative example. The Dredging International N.V. and Jan de Nul N.V., the claimant won a tender submitted by the Suez Canal Authority, a public body, for the construction. The dispute arose due to unexpected difficulties during their expansion works, such as the volume and distribution of material and rocks, which the respondent failed to compensate the Claimant. After a series of court battles for allegedly breaching the contractual obligations for ten years and the court subsequently dismissing the case, the Claimants opted for arbitration under ICSID ("Jan de Nul NV and Dredging International NV v Egypt", 2008).

The tribunal had to determine whether the Suez Canal Authority, under the respective interpretation of Article 5 of the ILC Articles, constitutes an entity empowered by the state. It stipulated that the featured article

[21] The SOEs can for instance receive preferential treatment in terms of procurement of goods and services over their competitors, see Du (2014)

[22] See for instance Xinhua (2023), Article 172

[23] For detailed discussions on the subject of EU competition law and SOEs, see Lallemand-Kirche, Tixier, and Piffaut (2017)

refers to entities empowered, even if to a limited extent or context, to exercise governmental authority. Under such conditions, the Suez Canal Authority would be acknowledged by the tribunal as falling under Article 5 of the ILC under that definition ("Jan de Nul NV and Dredging International NV v Egypt", 2008).

The tribunal's definition could encompass SASAC, which is vested with governmental authority by the Central government to manage governmental property. The tribunal has however stated that the entity must also at the time of the violation act with governmental authority for Article 5 to be applicable ("Jan de Nul NV and Dredging International NV v Egypt", 2008) The definition could cover SOEs that would deviate from activities covered under the CAI under the assumption that such acts are in pursuit of governmental directives at the time.

THE LIMITATIONS AND CHALLENGES

Subsidies and State Aid

China as a socialist economy has a long history of subsidies, permeating across the state dominated economy. Following the ascension to the WTO, China has made commitments towards their reduction as a part of broader transitional reforms towards a market-oriented model of governance, which includes the reforms of SOEs. Despite these reforms, subsidies have persisted alongside policy burdens (K. J. Lin, Lu, Zhang, & Zheng, 2020). The subsidies have a tendency to be awarded to industries that are export focused, competitive, innovative, and have a higher share of state ownership (Howell, 2017). The CAI seeks to address the issue by attempting to encourage the SOEs in China to comply with market conditions and prioritize commercial consideration over public policy objectives. It achieves this by linking the CAI to the existing WTO Subsidies and Countervailing Measures (SCM) regulations, elevating the rules to take precedence. However, the CAI does not explicitly preclude the provision of subsidies for the purposes of fulfilling a public mandate, allowing an enterprise, including the government owned, to be the recipient of governmental subsidies ("EU-China comprehensive agreement on investment", 2020).

The CAI does not provide clear punitive measures for non-compliance. Monitoring and punitive measures rely on the cooperation of the signatory parties, leaving enforcement somewhat vague. Arbitration is considered the last measure, with the preceding consultation and the implementation of corrective measures not being considered subject to arbitration ("EU-China comprehensive agreement on investment", 2020).

The approach contrasts with various other new-generation EU IIAs containing subsidy disciplining provisions. EU-New Zealand Free Trade Agreement for instance contains a provision forbidding subsidies in fisheries, while also stipulating that "...the responding Party shall endeavour to eliminate or minimise any negative effects..." ["EU-New Zealand free trade agreement, 2024, Article 16.6.2(a)]. It also restricts subsidies to insolvent enterprises, a provision that is lacking from the CAI.

In China, the governmental objectives could supersede market orientation as certain state- and privately-owned enterprises could continue operating despite suffering being unprofitable. The enterprises in such instances are sustained through state aid to employment that would otherwise be either unavailable or the closure could cause disruption in the region. These enterprises are referred to as "zombie companies" as they are both too unprofitable to sustain themselves while also serving an exceptionally relevant public policy role to be closed (People's Daily, 2019). The problem is particularly prevalent among SOEs, which according to a study by the National Academy of Development and Strategy, are at high risk of becoming zombie enterprises (National Academy of Development and Strategy, n.d.). China's WTO accession protocol reveals that the process towards restructuring of unprofitable SOEs has been on-going since at least 1990, when China reported issuing subsidies to address the issue, suggesting a longstanding issue ("Accession of the People's Republic of China", 2001).

This makes CAI's provisions to enhance access to information in an economic environment where transparency varies across different levels of government a key.[24] The investors could see their investments devalued as they could not compete against local enterprises that could afford to consistently run at a loss. The aim is to provide investors with all the necessary information for making informed decisions in regard to their investments. The CAI could additionally serve a supplementary role towards the existing mechanisms within the WTO, which have faced significant scrutiny over the years,[25] which rely heavily on the state's cooperation to disclose its subsidy regime. States are more likely to disclose subsidies that are compliant with the existing

[24] Chinese submissions on subsidies to the WTO under the Agreement on Subsidies and Countervailing Measures have been accused of being incomplete; see Bungenberg and Van Vaerenbergh (2020)

[25] The SCM for instance doesn't include any substantive measures that would discipline subsidy reports containing missing information; see Collins-Williams and Wolfe (2010)

regulatory framework, while non-compliant subsidies remain obscure, reducing the ability of state actors and investors to attain accurate information. The difficulty is further exacerbated by the prerequisite for the injured party to prove the existence of a subsidy and that the subsidy is responsible for harming its interests. Additionally, the existence of the subsidy regime should be analyzed in comparison to normal prices in the relevant market, which is difficult to undertake in a non-market-oriented economy due to market distortions (Bown & Hillman, 2019).

Within China, the subsidies are not limited to direct state aid but permeate from its assets. The Chinese SOEs can provide extensive support at the behest of the government towards supporting governmental policies that would overwise be untenable. The participation of enterprises in the distribution of aid to the economy has the effect of undermining the international framework for disciplining the subsidies, distorting legitimate business strategies by their ties to the state (Chi, 2022).

The WTO panel, in an appeal from China, has discussed the issue of subsidies granted by state enterprises. The dispute concerned anti-dumping duties imposed on China by the United States in accordance with the premise that China is fundamentally a non-market economy following an investigation by the United States Department of Commerce. It presented its findings that the comparison of prices for the purposes of determining the benefits in the provision of hot-rolled steel to producers via SOEs was unfeasible due to the nature of the Chinese economic model. Similar conclusions were reached in an analysis of the preferential loans issued by Chinese banks for the purposes of light-walled rectangular pipe and tubes, laminated woven sacks, and certain new pneumatic off-the-road tires, which were distorted by the lack of competition and the prevalence of state control. Additionally, during investigations for circular welded carbon quality steel tubes and its associated subsidies via land use rights, the benefits conferred were region specific and required the United States to use out of country benchmarks. In all investigations listed, the public bodies were the main providers of subsidies ("United States–Definitive anti-dumping and countervailing duties on certain products from China", 2011).

China argued that the majority ownership of an enterprise is not sufficient to establish it as a public body under the dictionary definition of the SCM Article 1.1. China instead relied upon the ILC Articles, stipulating that the undertaking has to be vested (imbued) with the governmental authority. The tribunal has concluded that the existence of governmental ownership is not sufficient to establish the ability of the government to direct the actions of the undertaking and the claim that it is vested with governmental authority ("United States—Definitive anti-dumping and countervailing duties on certain products from China", 2011).

The case highlights both the difficulty in distinguishing between private and public undertakings, just as the individual role of the SOEs and the motivations behind their actions. In other words, state enterprises can be directed to perform functions that are more closely associated with governmental functions, but the existing WTO mechanism lacks sufficient tools to discipline such behavior. This is due to the SOEs that are performing such roles being excluded from the traditional definitions of subsidies ("United States—Definitive anti-dumping and countervailing duties on certain products from China", 2011).

The CAI could address this shortcoming by integrating the subsidy provisions with the covered entities clauses. This approach would mandate disclosure of subsidies while complying with commercial considerations ("EU-China comprehensive agreement on investment", 2020). The focus on these provisions could overcome limitations under the WTO framework by raising concerns not solely via subsidy provisions but as a matter of commercial considerations under the Covered Entities provisions at the investment tribunal.

The existence of the Party organizations within the corporate structures of the enterprises presents additional layers of complexity via their connection to the government. Their connection to the CPC can serve the purpose of fulfilling Party objectives. The existence of governmental structures could overcome previously mentioned limitations of the WTO framework level given their vested authority.

The investment tribunals can set their reasoning and final award based on judgements issued by WTO. The investment dispute settlement is nonetheless established as an ad-hoc institution, independent of the WTO, offering the possibility of different interpretation of the ILC articles.[26] It represents an opportunity for their direct application to the conduct of SOEs in the context of investment arbitration and disciplining of the SOEs.

[26] It should be noted however that the ISDS suffers from the lack of consistency in the investment arbitration proceedings, alongside predictability, which is subject to much debate in the scholarly circles. This could translate into different perspectives on the role of SOEs between individual tribunals; for the discussions regarding consistency and predictability of investment arbitration see Connolly (2007); Behn, Langford, and Létourneau-Tremblay (2020); Sachetim and Codeco (2019)

Political Participation

The systems of governance of the EU and China reflect political and economic differences and their respective approaches toward the corporate management of SOEs. The EU, characterized by the multi-party competition-based system with electoral cycles, favors short-term flexible planning of economic development and renders the proposition of individual political parties being incorporated into corporate governance unrealistic.

China comparatively favors a multi-party cooperation system with the CPC forming the leading role in both political and economic areas of governance and working in consultations with other political parties (Wu, 2008). The consistent leadership role of the CPC allows for long-term planning and the CPC's participation in corporate governance, reflecting the historical and cultural legacy of the state-led development.

The contemporary mixed-ownership reforms aim to introduce private investors into enterprises (Xinhua, 2015b). The Chinese Company Law as amended on Seventh Session of the Standing Committee of the 14th National People's Congress on December 29, 2023, however mandates the establishment of the Party organization within the corporate structures of an enterprise and provides for its functioning (Xinhua, 2023). The State Council additionally stipulates in its advice on the development of mixed ownership economy that the responsibilities for the management of the mixed-ownership companies should lie with shareholders', the board of directors, managers the board of supervisors and the Party organizations (The State Council of the People's Republic of China, 2015). The proposed reforms underline the key role of the CPC leadership in the reforms' focus on removing unseemly competition, just as the management and reform of SOEs (Xinhua, 2015b)

Historically, the government implemented reforms meant to decrease regulatory oversight of the CPC over the economy through systematic reduction of regulatory bodies and affording greater autonomy to the SOEs, while the Party has maintained entangled with corporate governance (L. Zhang, 2009; Qiushi Journal, 2021). The CPC would ideally segregate itself from corporate governance and leave the state to act as a responsible stakeholder in the context of the reforms, completely insulating existing corporate governance mechanisms from political interference. The decentralization and separation from the ruling CPC would however require relinquishing of the power the CPC wields over the economy. Instead, the CPC's own constitution stipulates[27]

...Primary-level Party organizations in state-owned or collective enterprises should focus their work on the operations of their enterprise. Primary-level Party organizations shall guarantee and oversee the implementation of the principles and policies of the Party and the state within their own enterprise and shall support the board of shareholders, board of directors, board of supervisors, and manager (or factory director) in exercising their functions and powers in accordance with the law... (Xinhua, 2022, Article 33)

Additionally, the constitution mandates inspections of the embedded party organizations within the enterprise with the aim of promoting and ensuring that party members strive "...to defend the Constitution and other regulations of the Party, to monitor the implementation of the lines, principles, policies, and resolutions of the Party..." (Xinhua, 2022, Article 45).

The Party organizations are to be consulted in major decisions in the "three important and one large" policy. This covers major decisions, such as strategy developments, bankruptcy, restructuring, mergers and acquisitions, asset management, personal appoints and dismissals at key positions, etc. The Party organizations decisions are binding in cases, where an enterprise does not have a board of directors (Xinhua, 2010).

The Industrial and Commercial Bank of China (ICBC) under its articles of association for instance stipulates that the party organization shall be established and play a key role in the development and be responsible for the management. The ICBC is to provide sufficient funding for the purposes of ensuring the functioning of the organization. Eligible members of party organizations, such as party committees, shall be permitted to participate as members of the board of directors, board of supervisors and senior management through legally-prescribed procedures, while members of the said positions are eligible to enter the Party committees. The constitution in regards to the specific role of the committees most prominently outlines their key role in the selection of key appointments and building of the ICBC's leadership, while also outlining its role in the implementation of the Party policies (Industrial and Commercial Bank of China, 2023). In essence, the Party organizations within ICBC have the capacity to appoint party members to key positions, while also being entrusted with providing guidance on key issues.

The contemporary reforms in this context indicate a standing policy of maintaining Party leadership within SOEs, despite reforms and privatization to improve efficiency (Li, 2023). The two approaches constitute a "twin governance" model:

[27] Notably, the significant portion of party organizations' involvement, such as consultations with board members in a scheme dubbed "three important and one large" decisions lacks transparency; see L. Y. H. Lin (2020), p. 478

1. Legal governance is based upon the company law, prioritizing the interests of the state.

2. Political governance is driven by Party influence towards fulfilling the objectives of the leading CPC (J. Wang, 2014).

Legal governance is largely known and well documented as it encompasses the state exercising its effective control over the decision-making process via its controlling stake in the enterprise.

Political governance is somewhat of a novelty in its emergence from the proverbial shadows. Historically, the CPC control over the enterprises has been shielded by the presence of the state, which took an active part in corporate governance, as discussed above. The constitution enshrining the role of the CPC as a key player and mandates in the form of the CPC organizations within corporate structures are however signaling the emergence of the CPC as an entity that could be classified as separate from the state in terms of SOE governance. The expanding scope of the Party can be for instance seen in its ability to appoint CEOs, with at least fifty-three largest SOEs (Groswald Ozery, 2022)

CAI lacks the ability to effectively engage political influences, being predominantly tailored towards limiting state influence over the enterprises through ownership stake and voting rights.[28] The question remains whether the CPC's influence via the Party organizations within SOEs can be interpreted as an extension of state control under the investment law.

The tribunals in cases concerning the Party's influence over SOEs are most likely to rely upon the ILC articles as one of the major methods for establishing the state and its role in corporate actions. This is due to the fact that the CAI does not address political interference and lacks alternative instruments within the scope of investment law for disciplining SOEs. CAI however establishes state-state investment arbitration, which allows it to bypass tribunal concerns over jurisdiction under traditional ISDS in cases, where SOE would be classified as acting as an agent of the state.[29]

The tribunals could thus assess the role of the Party organization imbedded into the corporate structures of the SOEs, which are imbued with the power to propose and alter legislation.

Article 8 of the ILC outlines "The conduct of a person or group of persons shall be considered an act of a State under international law if the person or group of persons is in fact acting on the instructions of, or under the direction or control of, that State in carrying out the conduct." ("Responsibility of states for internationally wrongful acts", 2001, Article 8).

The case Georg Gavrilovic and Gavrilovic d.o.o. v. Republic of Croatia concerns the dispute over the privatization of previously state-managed enterprises in the food production industry, which were subsequently divided into nine new enterprises under the umbrella of the Holding d.o.o. During the proceedings for the purposes of our analysis of ILC Articles, the tribunal interprets Article 8 of the ILC Articles that the actions of the public officials fall under its sway should they be conducted at the behest of the government, be bound by an agreement, contract must establish contractual rights capable of expropriation, violation of legitimate expected, respondent must breach FET standards. The question of effective control has also been raised, stipulating that the existence of an agency for the management of property, the Croatian Fund is sufficient to establish separation of power. The tribunal however also stated that the agency appointed six out of seven officials to the Emergency

[28] CAI expressly states applicability of the Article 3bis to the enterprises in which government exercises control directly or indirectly "owns more than 50 per cent of the share capital; controls, through ownership interests the exercise of more than 50 per cent of the voting rights; holds the power to appoint a majority of members of the board of directors or any other equivalent management body; holds the power to control the decisions of the enterprise through any other ownership interest, including minority ownership"; Additionally "Enterprise in which a Party has the power to legally direct the actions or otherwise exercise an equivalent level of control in accordance with its laws and regulations; Any entity, public or private, including where relevant any subsidiary thereof, or a consortium, which in a relevant market in the territory of a Party is authorized or established formally or in effect by that Party as the sole supplier or purchaser of a good or service, but does not include an entity that has been granted an exclusive intellectual property right solely by reason of such grant; Two or a small number of enterprises, public or private, including where relevant any subsidiary thereof, designated by a Party, formally or in effect, as the only suppliers or purchasers of a particular good or service in a relevant market in the territory of that Party". The reading does not stipulate political influence, nor does it contextually arise. The closest to the applicability is the Section II, Article 3bis, 1. (b) as the state establishes the Party organizations within the SOEs but simultaneously does not explicitly state their role, nor does the state itself stipulate any active role of the organizations within the enterprise; see "EU-China comprehensive agreement on investment" (2020), Section II, Article 3bis.1

[29] Under the Beijing Urban Construction Group Co. Ltd. v. Republic of Yemen, the respondent argued that "...BUCG's claims should be barred, as the Tribunal lacks jurisdiction under ICSID Convention Article 25(1) over State-to-State disputes."; see "Beijing Urban Construction Group Co. Ltd. v. Republic of Yemen" (2017), paragraph 29; Q. Wang et al. (2023), p. 48

board, which were not state officials ("Georg Gavrilovic and Gavrilovic d.o.o. v. Republic of Croatia", 2018). The tribunal establishes that governmental agencies could operate without breaching the ILC Article 8 as long as they are separate from the supervised entities. SASAC and CPC organizations within SOEs could still be subject as they maintain an active presence within the enterprises' board.

The existence of a link within the Chinese company law, The Chinese Constitution and the CPC could also be conductive towards the application of the ILC Article 5. This is due to the close links between the imbedded organization's status with the leading political as being empowered by law. The tribunal has ruled on the matter, stipulating the actions of an organization acting in an official capacity, empowered by law and in breach of relevant IIA are subject to Article 5[30] ("Georg Gavrilovic and Gavrilovic d.o.o. v. Republic of Croatia", 2018).

Challenging the position of the CPC organizations via arbitration could have a definitive impact on their functioning. The section has illustrated their intended role within corporate structures, which would have to be altered to create greater separation between the state, the CPC and the organizations in order to comply with global standards, just as their ability to make key appointments would have to become transparent to ensure equal treatment in appointments.

CONCLUSION

The CAI presents a significant step towards reshaping the investment and trade landscape between the EU and China. It introduced increased access to the lucrative Chinese market for the EU investors under the collective protective umbrella of a unified, EU centric IIA. CAI additionally introduced mechanisms addressing concerns over SOEs and state economic interventions. It however faces a number of challenges, ranging from the inability to grasp the true scope of the fast-evolving investment landscape, to not extensively addressing the true scope of the state and CPC's involvement within the economy.

China's ongoing liberalization efforts in terms of investment is a fast-accelerating process that seeks to attract foreign capital through strengthening the investment protection framework and lifting barriers. China has for instance removed mandated use of the most advanced technologies, consolidated foreign investment legislation into the Foreign Investment Law of 2019 and began lifting monetary control by removing restrictions for using only the Bank of China for foreign exchange. China has also collectively begun transferring from the positive list to the negative, with the list of 2021 featuring 31 restricted or forbidden areas for investment, with a further reduction to 29 in 2024. The CAI fails to fully grasp the speed of the liberalization, with the existing provisions being at risk of becoming redundant. The CAI's longevity may have to rely on its standard of treatment provisions for its continued relevance. In terms of the advertised successes of the CAI in opening up the Chinese market to EU investment, it reveals the agreement as a more political victory for the EU than an actual breakthrough.

The liberalization of the Chinese market inevitably affects the SOEs, which are considered the workhorses of the Chinese economy with a nationwide presence. The CAI disciplines their behavior via commercial conduct requirements, monitoring of state's participation conducted through its ownership and features a state-to-state on-demand reporting mechanism.

While being a solid foundation, the provisions are undercut by the symbiotic relationship between the state, the CPC and the SOEs, allowing for continued state interference in corporate governance. This dynamic hinders both true market neutrality and liberalization. The lack of provisions that would directly tackle subsidies to insolvent companies or the ability to discipline subsidies granted via SOEs hinders the CAI's effectiveness. It additionally lacks the ability to tackle CPC influence, which has ingrained itself within the corporate structures of the SOEs.

The tribunals' ability to discipline the behavior of the SOEs will have to eventually fall down unto ILC articles, which have historically been interpreted narrowly. They have been focusing both on the vested authority of an undertaking overall, just as whenever they acted on behalf of a government at the time of the breach.

The CAI nonetheless offers the EU an opening springboard, both for its investors and for future negotiations. It can offer an excellent platform for addressing issues, such as subsidies and CPC's role in SOEs.

Future reforms should focus on addressing the insolvency of SOEs; clarify the role of CPC organizations within the state framework and not as a matter of the CPC itself especially delineating the different roles the CPC can play in wholly-state owned enterprises and mixed-ownership enterprises. Additionally, the SASAC should either become a supervisory entity or an active shareholder, not both, with the board being composed of non-

[30] The tribunal under the para. 814 stipulates that it could not identify any other wrongful conduct in violation of the BIT

government-associated personnel in order to create sufficient separation between the state and the SOEs. The future framework should also address the blurry line between official China policy and CPC policy as it is currently difficult to discern individual objectives. Lastly, state-owned banks should disclose additional information in regard to their lending practices when issuing loans to other SOEs and state-affiliated entities, bolstering transparency and opening the door towards tackling SOE based subsidies. Their activities could afterwards be challenged as a matter of commercial considerations and lead towards disciplining their practices.

REFERENCES

Accession of the People's Republic of China (WT/L/432). (2001). Retrieved from https://www.worldtradelaw.net/document.php?id=misc/ChinaAccessionProtocol.pdf&mode=download

Agreement between the United States of America, the United Mexican States, and Canada. (2020). Retrieved from https://ustr.gov/trade-agreements/free-trade-agreements/united-states-mexico-canada-agreement/agreement-between

Behn, D., Langford, M., & Létourneau-Tremblay, L. (2020). Empirical perspectives on investment arbitration: What do we know? Does it matter?. *The Journal of World Investment & Trade*, *21*(2-3), 188-250.

Beijing Urban Construction Group Co. Ltd. v. Republic of Yemen (ICSID Case No. ARB/14/30). (2017). Retrieved from https://www.italaw.com/sites/default/files/case-documents/italaw8968.pdf

Bown, C. P., & Hillman, J. A. (2019). WTO'ing a resolution to the China subsidy problem. *Journal of International Economic Law*, *22*(4), 557-578. https://doi.org/10.1093/jiel/jgz035

Brazil—Certain measures concerning taxation and charges (WT/DS472/AB/R). (2018). Retrieved from www.worldtradelaw.net/document.php?id=reports/wtoab/brazil-taxation(ab).pdf&mode=download

Bungenberg, M., & Van Vaerenbergh, P. (2020). Countervailing measures and China's accession protocol to the WTO. *Journal of World Trade*, *54*(5), 749-772

Chaisse, J., & Sejko, D. (2018). The latest on the best? Reflections on trade defence regulation in EU-Vietnam FTA. In M. Bungenberg, M. Hahn, C. Herrmann, & T. Müller-Ibold (Eds.), *European Yearbook of International Economic Law* (pp. 295-313). Cham, Switzerland: Springer. https://doi.org/10.1007/978-3-319-95306-9_13

Chang, Y., & Lin, L. Y. (2021). Do State-Owned enterprises have worse corporate governance? An Empirical study of corporate practices in China. *European Business Organization Law Review*, *23*(3), 711-734. https://doi.org/10.1007/s40804-021-00223-1

Chi, M. (2022). International regulation of industrial subsidy. *Journal of International Economic Law*, *26*(1), 146-153. https://doi.org/10.1093/jiel/jgac052

China–Certain measures concerning the protection of intellectual property rights (WT/DS542/8). (2018). Retrieved from https://docs.wto.org/dol2fe/Pages/SS/directdoc.aspx?filename=q:/WT/DS/542-8.pdf&Open=True

China—Certain measures on the transfer of technology (WT/DS549/1/Rev.1). (2018). Retrieved from https://www.worldtradelaw.net/document.php?id=cr/ds549-1R1(cr).pdf&mode=download

Collins-Williams, T., & Wolfe, R. (2010). Transparency as a trade policy tool: The WTO's cloudy windows. *World Trade Review*, *9*(4), 551-581. https://doi.org/10.1017/S1474745610000303

Connolly, K. (2007). Say what you mean: Improved drafting resources as a means for increasing the consistency of interpretation of bilateral investment treaties. *Vanderbilt Journal of Transnational Law*, *40*(5), 1579-1610.

Constitution of the People's Republic of China (1954). (1954). Retrieved from https://hdl.handle.net/1813/104273

Du, M. (2014). China's State Capitalism and World Trade Law. *International and Comparative Law Quarterly*, *63*(2), 409-448. https://doi.org/10.1017/s0020589314000062

Economic Daily. (2018). *Hunhe suoyouzhi gaige yi zai shuangying* [The goal of mixed-ownership reform is mutual benefit]. Retrieved from www.sasac.gov.cn/n2588025/n2588134/c9603101/content.html

Encourage. (n.d.). In *Cambridge Online Dictionary*. Retrieved from https://dictionary.cambridge.org/dictionary/english/encourage

EU-China comprehensive agreement on investment. (2020). Retrieved from https://www.europarl.europa.eu/RegData/etudes/BRIE/2020/652066/EPRS_BRI(2020)652066_EN.pdf

EU-New Zealand trade agreement. (2024). Retrieved from https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/new-zealand/eu-new-zealand-agreement_en

EU-South Korea free trade agreement. (2015). Retrieved from https://trade.ec.europa.eu/access-to-markets/en/content/eu-south-korea-free-trade-agreement

Free trade agreement between the European Union and Singapore. (2019). Retrieved from https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A22019A1114%2801%29

Free trade agreement between the European Union and Vietnam. (2020). Retrieved from https://policy.trade.ec.europa.eu/eu-trade-relationships-country-and-region/countries-and-regions/vietnam/eu-vietnam-agreement/texts-agreements_en

Gao, H. (2021). The EU-China comprehensive agreement on investment: Strategic opportunity meets strategic autonomy. In M. Chi, M. Bungenberg, & A. K. Bjorklund (Eds.), *Asian Yearbook of International Economic Law 2022*. Cham, Switzerland: Springer. https://doi.org/10.1007/16517_2021_1

Georg Gavrilovic and Gavrilovic d.o.o v Republic of Croatia (ICSID Case No. ARB/12/39) (2018). Retrieved from https://www.italaw.com/sites/default/files/case-documents/italaw9871.pdf

Grieger, G. (2021, March). EU-China Comprehensive Agreement on Investment—Levelling the playing field with China (PE 679.103). Retrieved from http://www.europarl.europa.eu/RegData/etudes/BRIE/2021/679103/EPRS_BRI(2021)679103_EN.pdf

Groswald Ozery, T. (2022). The politicization of corporate governance: A viable alternative?. *The American Journal of Comparative Law*, *70*(1), 43-94.

Guide. (n.d.). In *Cambridge Online Dictionary*. Retrieved from https://dictionary.cambridge.org/dictionary/english/guide

Heller, G. L. (1986). Controlled foreign companies in PRC joint ventures. *International Financial Law Review*, *5*, 15-19.

Howell, A. (2017). Picking 'winners' in China: Do subsidies matter for indigenous innovation and firm productivity? *China Economic Review*, *44*, 154-165. doi:10.1016/j.chieco.2017.04.005

Industrial and Commercial Bank of China. (2023). *Zhongguo gongshang yinhang gufen youxian gongsi zhangcheng* [Articles of Association of Industrial and Commercial Bank of China]. Retrieved from https://v.icbc.com.cn/userfiles/Resources/ICBCLTD/download/2023/ICBCCharter20231114.pdf

Jan de Nul NV and Dredging International NV v Egypt (ICSID Case No ARB/04/13). (2008). Retrieved from https://jusmundi.com/en/document/decision/en-jan-de-nul-n-v-and-dredging-international-n-v-v-arab-republic-of-egypt-award-thursday-6th-november-2008

Kelsey, J. (2017). Regulatory chill: Learnings from New Zealand's plain packaging tobacco law. *QUT Law Review*, *17*(2), 21-45. https://doi.org/10.5204/qutlr.v17i2.701

Key elements of the EU-China comprehensive agreement on investment (IP/20/2542). (2020). Retrieved from https://ec.europa.eu/commission/presscorner/api/files/document/print/pt/ip_20_2542/IP_20_2542_EN.pdf#:~:text=For%20Chinese%20FDI%20into%20the%20EU%20the%20figure%20is%20almost

Kong, Q. (2023). Emerging international rules on fair trade and their revelation for reform of state-owned enterprises in China. In *State and enterprise* (pp. 387-399). Cham, Switzerland: Springer. https://doi.org/10.1007/978-3-031-10473-2_14

Lallemand-Kirche, G., Tixier, C., & Piffaut, H. (2017). The treatment of state-owned enterprises in EU competition law: New developments and future challenges. *Journal of European Competition Law & Practice*, *8*(7). https://doi.org/10.1093/jeclap/lpx027

Law of the People's Republic of China on Chinese-Foreign equity joint ventures (1979). (1979). Retrieved from http://www.law-lib.com/law/law_view.asp?id=99135

Law of the People's Republic of China on Foreign-capital Enterprises (1986). (2014). Retrieved from https://english.www.gov.cn/archive/laws_regulations/2014/08/23/content_281474983043654.htm

Lee, J. (2020). Forced technology transfer in the case of China. *Boston University Journal of Science and Technology Law*, *26*(2), 324-352.

Li, H. Y. (2023). Understanding the corporate governance of China's state-owned enterprises in the context of the state-owned enterprises reform: The party, the state, and the enterprises. *Ohio State Business Law Journal*, *17*(1), 210-264.

Liberalization. (n.d.). In *Cambridge online dictionary*. Retrieved from https://dictionary.cambridge.org/dictionary/english/liberalization

Lin, K. J., Lu, X., Zhang, J., & Zheng, Y. (2020). State-owned enterprises in China: A review of 40 years of research and practice. *China Journal of Accounting Research*, *13*(1), 31-55. https://doi.org/10.1016/j.cjar.2019.12.001

Lin, L. (2013). State ownership and corporate governance in China: An executive career approach. *Columbia Business Law Review*, *3*(3), 743-800. https://doi.org/10.7916/cblr.v2013i3.2873

Lin, L. Y. H. (2020). Institutionalizing political influence in business: Party-building and insider control in Chinese state-owned enterprises. *Vermont Law Review*, *45*, 441-480.

Mavroidis, P. C., & Sapir, A. (2022). What is so special about CAI?. *Asia Pacific Law Review*, *30*(2), 348-366. https://doi.org/10.1080/10192557.2022.2085414

Micula, Viorel Micula, S.C. European Food S.A, S.C. Starmill S.R.L. and S.C. Multipack S.R.L. v. Romania [I] (ICSID Case No. ARB/05/20). (2023, December). Retrieved from http://www.italaw.com/cases/697

Must. (n.d.). In *Cambridge online dictionary*. Retrieved from https://dictionary.cambridge.org/dictionary/english/must

National Academy of Development and Strategy. (n.d.). Renda guo fa yuan fabu guonei shou fen wanzheng de jiangshi qiye yan jiu baogao [The Institute for National Development releases China's first comprehensive report on zombie enterprises]. Retrieved from http://nads.ruc.edu.cn/yjdt/c9ed3bc346b047d689d7436108e142a2.htm

Nolan, P., & Ash, R. F. (1995). China's economy on the eve of reform. *The China Quarterly*, *144*, 980-998. https://doi.org/10.1017/s0305741000004690

People's Daily. (1999, September). Kaichuang guoyou qiye gaige he fazhan de xin jumian [Forging a new path for SOE reform and development]. Retrieved from http://cpc.people.com.cn/GB/64162/64168/64568/65403/4429272.html

People's Daily. (2019, September). Jia da lidu tuoshan chuzhi "jiangshi qiye" [Increasing efforts to properly handle "Zombie enterprises"]. Retrieved from http://www.sasac.gov.cn/n2588025/n2588139/c10379257/content.html

Philip Morris Asia Limited v. The Commonwealth of Australia, UNCITRAL, PCA Case No. 2012-12. (2012). Retrieved from http://www.italaw.com/cases/851

Qiushi Journal. (2021, January). Hao Peng: Shenru shishi guoqi gaige san nian xingdong tuidong guozi guoqi gao zhiliang fazhan [Hao Peng: Deepening the implementation of the three-year SOE reform action plan to promote the high-quality development of state-owned assets and enterprises]. Retrieved from http://www.gov.cn/xinwen/2021-01/16/content_5580396.htm

Qiye guoyou zichan jiandu guanli zhanxing tiaoli [Interim regulations on the supervision and administration of State-owned assets of enterprises] (Order No. 378). (2003). Retrieved from https://www.gov.cn/gongbao/content/2003/content_62164.htm

Regulation (EC) No 139/2004 Merger Procedure (Case No COMP/M.5508-Soffin/Hypo Real Estate). (2009). Retrieved from https://ec.europa.eu/competition/mergers/cases/decisions/M5508_20090514_20310_265129_EN.pdf

Responsibility of states for internationally wrongful acts. (2001). Retrieved from https://legal.un.org/ilc/texts/instruments/english/draft_articles/9_6_2001.pdf

Rui, G. (2013). The creation of modern state ownership: Legal transplantation and the rise of modern state-owned big businesses in China. *Peking University Journal of Legal Studies*, *4*, 69-91.

Sachetim, H., & Codeco, R. (2019). The investor-state dispute settlement system amidst crisis, collapse, and reform. *Arbitration Brief*, *6(1)*, 20-59.

Shall. (n.d.). In *Cambridge online dictionary*. Retrieved from https://dictionary.cambridge.org/dictionary/english/shall

Sokol, D. D. (2017). State capitalism in Cuba: the lessons of the literature on state owned enterprises and market liberalization. *Florida Journal of International Law*, *29*, 209-222.

State-owned Assets Supervision Administration Commission of the State Council. (2021, August). 82 Chinese SOEs listed among 2021 Fortune Global 500. Retrieved from http://en.sasac.gov.cn/2021/08/03/c_7528.htm#:~:text=A%20total%20of%2082%20Chinese%20state-owned%20enterprises%20(SOEs),one%20more%20than%20their%20numbers%20of%20last%20year

Tax laws amendment (research and development) act 2011, No. 93, 2011. (2011). Retrieved from https://www.ato.gov.au/law/view/pdf/acts/20110093.pdf

The State Council of the People's Republic of China. (2015, September). Guowuyuan guanyu guoyou qiye fazhan hunhe suoyouzhi jingji de yijian [The State Council on state-owned enterprises advice on the development of a

mixed-ownership economy] (Guo Fa [2015] No. 54). Retrieved from https://www.gov.cn/zhengce/content/2015-09/24/content_10177.htm

The State Council of the People's Republic of China. (2018). *Constitution of the People's Republic of China*. Retrieved from https://english.www.gov.cn/archive/lawsregulations/201911/20/content_WS5ed8856ec6d0b3f0e9499913.html

The State Council of the People's Republic of China. (2019). *Foreign Investment Law of the People's Republic of China* (Order of the President of the People's Republic of China No. 26). Retrieved from https://english.www.gov.cn/services/investment/202102/24/content_WS6035aa38c6d0719374af9609.html

Trakman, L. (2023). China's investment strategies: Where to post pandemic. *Transnational Law and Contemporary Problems*, *32*(2), 255-298.

United States—Definitive anti-dumping and countervailing duties on certain products from China (WT/DS379/AB/R). (2011, March). Retrieved from https://www.wto-ilibrary.org/content/reports/25189840/99

Waishang touzi zhun ru tebie guanli cuoshi (fumian qingdan) (2021 nianban) [Special Administrative Measures (Negative List) for the Access of Foreign Investment (2021)] (Order No. 47). (2021). Retrieved from https://www.ndrc.gov.cn/xxgk/zcfb/fzggwl/202112/P020211227540591870254.pdf

Waishang touzi zhun ru tebie guanli cuoshi (fumian qingdan) (2024 nianban) [Special Administrative Measures (Negative List) for the Access of Foreign Investment (2024)] (Order No. 23). (2024). Retrieved from http://www.ndrc.gov.cn/xxgk/zcfb/fzggwl/202409/P020240907514493057643.pdf

Walder, A. G. (2016). Bending the arc of Chinese history: The cultural revolution's paradoxical legacy. *The China Quarterly*, *227*, 613-631. https://doi.org/10.1017/s0305741016000709

Wang, J. (2014). The political logic of corporate governance in China's State-Owned enterprises. *Cornell International Law Journal*, *47*(3), 631-669.

Wang, L., Liu, Z., Fu, X., & Wu, Y. (1989). On the property rights system of the state enterprises in China. *Law and Contemporary Problems*, *52*(3), 19-42. https://doi.org/10.2307/1191745

Wang, Q., Xu, L., Ling, F., Huang, R., Bai, Q., He, K., & Sun, J. (2023). The standing of state-owned enterprises under the ICSID convention: Chinese perspective. *Journal of WTO and China*, *13*(2), 47-68.

World Bank. (n.d.). GDP growth (annual %)—China. Retrieved from https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?locations=CN

Wu, Y. (2008). Commentating constructing the mechanism of political participation in multi-party cooperation system. *Journal of Politics and Law*, *1*(4), 29-32.

Xinhua. (2008, October). Zai kanke zhong fenjin zai biange zhong chengzhang—Ji guoqi gaige sanshi nian [Striving through ups and downs amidst reforms—A record of 30 Years of SOE reforms]. Retrieved from https://www.gov.cn/ztzl/2008-10/02/content_1110911.htm

Xinhua. (2010, July). Zhonggong zhongyang bangong ting, Guowuyuan bangong tīng yinfa "guanyu jinyibu tuijin guoyou qiye guanche luoshi 'sanchong yi da' juece zhidu de yijian" [General Office of the CPC Central Committee and General Office of the State Council, 'Opinions on Further Promoting the Implementation of the "Three Important and One Large" Decision-Making System in State-Owned Enterprises]. Retrieved from https://www.gov.cn/jrzg/2010-07/15/content_1655395.htm

Xinhua. (2015a, September). *Zhonggong zhongyang, Guowuyuan guanyu shenhua guoyou qiye gaige de zhidao yijian* [Guiding opinions of the Central Committee of the Communist Party of China and the State Council on deepening the reform of state-owned enterprises]. Retrieved from https://www.gov.cn/zhengce/2015-09/13/content_2930440.htm

Xinhua. (2015b, September). Zhonggong zhongyang guowuyuan yinfa "guanyu shenhua guoyou qiye gaige de zhidao yijian" [The State Council of the People's Republic of China issued the "guiding opinions on deepening the reform of state-owned enterprises"]. Retrieved from https://www.audit.gov.cn/n4/n18/c75001/content.html

Xinhua. (2022). Constitution of Communist Party of China. Retrieved from http://en.qstheory.cn/2022-10/27/c_824864.htm

Xinhua. (2023). *Zhonghua renmin gongheguo gongsi fa* [Company law of the People's Republic of China]. Retrieved from www.gov.cn/yaowen/liebiao/202312/content_6923395.htm

Xinhua. (2024, April). *China to lift foreign ownership limit in value-added telecom services in pilot areas*. Retrieved from https://english.www.gov.cn/news/202404/10/content_WS66164db2c6d0868f4e8e5e93.html

Xu, Q. (2022). Scoping the impact of the comprehensive agreement on investment: Liberalization, protection, and dispute resolution in the next era of EU–China relations. *Asia Pacific Law Review*, *30*(1), 93-122. https://doi.org/10.1080/10192557.2022.2045708

Xun, S. X., & Weng, C. X. (2024). Reining in the behemoths for the Common Good? An analysis of state control of State-Owned Enterprises and the pathway to better governance in China. *European Business Organization Law Review*. https://doi.org/10.1007/s40804-024-00322-9

Yang, X. (2015). Deleveraging China Inc. *International Financial Law Review*, *34*(4), 20-21.

Yu, Y. (2018). The reform of China's exchange rate regime. In *China's 40 years of reform and development 1978–2018* (pp. 313-328). https://doi.org/10.22459/cyrd.07.2018.17

Zhang, C. (2019). How much do State-Owned enterprises contribute to China's GDP and employment?. Washington, DC: World Bank.

Zhang, L. (2009). Convergence or divergence: Evidence from Chinese state-controlled listed companies. *Asian Business Lawyer*, *4*, 41-56.

Zhang, L., Coulson, N. E., Liu, Y., & Zhao, Y. (2023). State-owned enterprises and industrial land reform in China. *The Annals of Regional Science*, *72*, 255-286. https://doi.org/10.1007/s00168-022-01197-9

Zhang, M. (2020). Change of regulatory scheme: China's new foreign investment law and reshaped legal landscape. *UCLA Pacific Basin Law Journal*, *37*(1), 179-238. https://doi.org/10.5070/p8371048806

Zhang, W. (2015). The power of ideas and leadership in China's transition to liberal society. *Cato Journal*, *35*(1). Retrieved from https://www.cato.org/sites/cato.org/files/serials/files/cato-journal/2015/2/cj-v35n1-1.pdf

Zhonghua renmin gongheguo qiye guoyou zichan fa (zhuxi ling di wu hao) [The People's Republic of China Law on state-owned assets of enterprises (Presidential Decree No. 5)]. (2009). Retrieved from https://www.gov.cn/flfg/2008-10/28/content_1134207.htm

Zigo, D. (2021). The EU-China comprehensive agreement on investment—Blunder or win?. *Tsinghua China Law Review*, *14*(1), 126-148.

ETHICAL DECLARATION

Conflict of interest: No declaration required. **Financing:** No reporting required. **Peer review:** Double anonymous peer review.