Hong Kong, SAR China's New Approach to Investment Treaty Arbitration

Kluwer Arbitration Blog
July 10, 2021

Julien Chaisse, Kehinde Olaoye (City University of Hong Kong)

Please refer to this post as: Julien Chaisse, Kehinde Olaoye, 'Hong Kong, SAR China's New Approach to Investment Treaty Arbitration', Kluwer Arbitration Blog, July 10 2021, http://arbitrationblog.kluwerarbitration.com/2021/07/10/hong-kong-sar-chinas-new-approach-to-investment-treaty-arbitration/

In March 2021, a major newspaper broke the story that a Hong Kong investor had filed what may be considered the very first investment treaty arbitration claim against Japan under the Hong-Kong Bilateral Investment Treaty (Hong Kong, China SAR – Japan BIT 1997). While it may take anywhere from a few months to a few years for this BIT arbitration to reach final conclusion, the dispute is significant as it allows us to examine Hong Kong's approach to investment treaty arbitration. It also becomes important to examine this BIT arbitration because unlike most capital exporting economies, Hong Kong and Japan are parties to fewer international investment agreements (IIAs) and both jurisdictions can be used as prime examples of an Asian approach to ISDS which is meant to be non-adversarial. While Hong Kong is a party to 25 Investment and Promotion Agreements (IPPAs) including the Closer Economic Partnership Arrangement (CEP) investment agreement signed with China in 2017, Japan is a party to 35 BITs and 15 treaties with investment provisions (TIPs).

In this blog post, we examine Hong Kong's modest international investment treaty framework and highlight how investor-state dispute settlement (ISDS) clauses in Hong Kong's IIAs have evolved over time and more recently in response to specific global and regional investment treaty drafting trends. This analysis is based on an

examination of the ISDS provisions of Hong Kong's recently signed treaties with Australia, Mexico and the United Arab Emirates (UAE). We argue that unlike other small jurisdictions and leading financial centres, Hong Kong has adopted a passive but consistent approach to investment treaty arbitration, but that this approach is slowly being modified. We contend that this alteration in policy reflects Hong Kong's special characteristics, especially its limited sovereignty under international law, and is consistent with its dispute avoidance objectives. Hong Kong is a leading centre of foreign direct investment. In line with its position as a leading financial centre, Hong Kong consistently promotes itself as a friendly international arbitration hub based on its proximity to mainland China, international arbitration centres, rule of law tradition and independent judiciary. Although Hong Kong's sovereignty under international economic law has recently come under scrutiny, as evidenced in a pending World Trade Organization dispute between Hong Kong and the USA, IIAs (which have been signed under the authority of its constitutional law) remain a pillar of its economic strategy.

Narrow Arbitration Clauses

Under most of Hong Kong's IIAs, disputes concerning an investment are arbitrable as long as they concern an investment made in the area of the contracting party. An example is the Hong Kong-Australia BIT which was signed in 2020 to replace the earlier 23-year old Hong Kong-Australia BIT (which was the basis for a highly publicised investment treaty arbitration between Australia and a subsidiary of the tobacco giant Philip Morris). This treaty has narrowed the definition of the term "investment" while excluding arbitration claims by a Hong Kong investor that relate to acts of the Office of Gene Technology Regulator. Investors from both Hong Kong and Australia cannot institute claims which relate to either party's control measures of tobacco products or other smoking products.

On the other hand, the Hong Kong-Mexico BIT (2020) adopts a broader arbitration clause but specifically provides that 'An investor of a Contracting Party may submit to arbitration a claim that the other Contracting Party has breached an obligation under Chapter II, and that the investor has incurred loss or damage by reason of, or arising out of, that breach.' Additionally, Hong Kong's BIT with the UAE (2019) also adopts broader language but unlike the majority of Hong Kong's BITs, it does not contain a territorial qualification that an arbitration claim must be a dispute

concerning an investment in the area of the other party.

Consistent with the recent treaty practice of most states, Hong Kong's BITs with the UAE, Mexico and Australia exclude the possibility of importing more favourable investment dispute procedures from IIAs signed with third parties. In practice, however, this does not exclude the possibility that more favourable substantive provisions can be imported from treaties signed with third party states.

Limitation Periods

Introduction of limitation periods in Hong Kong's newer BITs is consistent with newer generation treaties which introduce procedural safeguards to limit the exposure of states to frivolous and/or antiquated arbitration claims. All three investment agreements include limitation periods for instituting arbitration claims. The Hong Kong-Australia BIT adopts a limitation period of 3 years and 6 months, the Hong Kong-UAE BIT's period is 5 years while the BIT with Mexico agreement adopts a 3-year limitation period.

More Forum Options

One of the most distinct changes to Hong Kong's ISDS provisions is the inclusion of more arbitration forums. Traditionally, Hong Kong's BITs have referred to settlement of disputes using only the UNCITRAL Arbitration Rules. For example, the Hong Kong-Japan BIT provides that after a period of six months from written notification of a claim, the dispute may be submitted to a procedure for settlement as agreed by the between the parties to the dispute. However, where parties do not reach an agreement, at the request of the foreign investor, the dispute shall be submitted to arbitration under the UNCITRAL Arbitration Rules. Unlike the large majority of over 2500 BITs that have been signed; Hong Kong's BITs do not refer to arbitration under the International Centre for Settlement of Investment Disputes (ICSID) Convention rules. This is because the Hong Kong SAR is not a direct signatory to the ICSID Convention. Rather, in disputes involving Hong Kong investors or Hong Kong's territory, jurisdiction under ICSID may be derived from China's accession to the ICSID Convention.

In addition to UNCITRAL arbitration, the Hong Kong-UAE BIT provides for arbitration by the International Court of Arbitration of the International Chamber of Commerce (ICC) and the Arbitration Institute of the Stockholm Chamber of Commerce (SCC). The BITs signed with Mexico and Australia follow the text of older Hong Kong treaties and provide for the application of any other arbitration rules if the disputing parties so agree. This distinct characteristic of Hong Kong's BITs may be why to date only three investment treaty arbitration disputes have been instituted by Hong Kong investors. The very first investment treaty claim, *Asian Agricultural Products Ltd v Republic of Sri Lanka* was instituted prior to the transfer of sovereignty over Hong Kong by the United Kingdom in 1997. This arbitration claim was instituted by a Hong Kong registered company at ICSID on the basis of the UK-Sri Lanka BIT (1980). A more recent ICSID investment treaty dispute instituted by a Hong Kong subsidiary of a financial institution on the basis of the UK-Tanzania BIT (1994) was dismissed for lack of jurisdiction in 2012. The third treaty claim, *Philip Morris Asia Limited v The Commonwealth of Australia* was also dismissed for lack of jurisdiction. Together, these three investment claims raise the question whether the forums provided for in Hong Kong's IIAs are adequate for promoting and protecting foreign investment.

Conclusion

The Hong Kong SAR has recently concluded IIAs with Bahrain, Maldives, and Myanmar. Negotiations for IIAs with Iran, Russia, and Turkey are underway. These agreements will probably follow the trends identified above and confirm that investment treaty arbitration remains a preferred forum for settling disputes between host territories and foreign investors. Even though there have been limitations in respect to Hong Kong's sovereignty, its association and engagement with ISDS appears to be increasing. This is reflected in newer IIAs which give parties more forum options. While this conclusion may be counter-intuitive considering the inclusion of procedural safeguards against investment arbitration in Hong Kong's more recent IIAs, Hong Kong appears to be taking a more open approach to investment treaty arbitration.

Overall, our review of ISDS provisions in Hong Kong's recent treaties confirms that Hong Kong firstly, still favours arbitration of disputes, secondly, is willing to accommodate the needs of partner states and thirdly, is willing to conform to

emerging investment treaty drafting trends as long as they remain in line with its limited sovereignty. Although Hong Kong's modest IIA network with limited ISDS forum options may be why it has not yet been a respondent in any dispute, by signing new IIAs, Hong Kong is protecting the interests of its investors but also increasing its exposure to ISDS claims. However, only time will tell if like Japan, Hong Kong will soon face its very first investment treaty arbitration.

Acknowledgements: The authors wish to thank Luke Nottage, Esmé Shirlow, Jan Kunstyr, Ishita Mishra, Sufian Jusoh, Yashvi Jain, and Xueliang Ji for indispensable feedback and comments. This article is part of a broader research supported by the General Research Fund Project No. 11606820 of the Hong Kong SAR Research Grants Council. The opinions expressed herewith are the authors' own.