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The Dilemma of Investor Rights Protection in the Belt and Road Initiative and Institutional Reconstruction

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Abstract. The Belt and Road Initiative (BRI) has spurred overseas investment by Chinese enterprises. However, investors in host countries face risks of "regulatory takings" arising from fragmented environmental legislation and arbitrary enforcement, alongside systemic governance gaps due to ineffective regulatory oversight in host states. These issues underscore deficiencies in the investment protection regimes of BRI partner countries. Concurrently, the current Investor-State Dispute Settlement (ISDS) mechanism exacerbates conflicts of interest between host states and investors by excessively prioritizing investor rights. This study focuses on the core issue of balancing investor rights protection with host states' public interests. Applying normative analysis, case studies, and comparative research methods, conducts an in-depth examination of the institutional dilemmas affecting investor rights protection under the BRI and their underlying causes. The research proposes that institutional reconstruction hinges on establishing a dynamic equilibrium framework: on the one hand, International Investment Agreements (IIAs) require optimization through clarifying indirect expropriation criteria, defining the scope of Fair and Equitable Treatment (FET), and incorporating exception clauses for social responsibilities and public interests; on the other hand, dispute resolution mechanisms should be innovated by exploring a multi-tiered settlement system integrating mediation and arbitration, while advancing the top-level design of a BRI Investment Protection Convention. This study aims to provide institutional solutions for reconciling investment protection with host states' regulatory sovereignty, thereby facilitating the rule of law and sustainable development of the Belt and Road Initiative.

Keywords: Belt and Road Initiative, dispute settlement mechanism, governance restructuring, interest balancing, investor rights protection.

1. Introduction

Since the implementation of the BRI in 2015, China has fostered economic development in participating countries through policy-backed financing, cross-border infrastructure connectivity, and bilateral trade agreements. Concurrently, this has accelerated the entry of Chinese enterprises into overseas markets. Nevertheless, international investment practices reveal persistent institutional risks and operational challenges. Specifically, the foreign direct investment (FDI) regimes in most BRI partner countries suffer from inadequate transparency and legal unpredictability [1]. Within

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host states' environmental governance frameworks, investors face risks of regulatory takings-a consequence of fragmented environmental legislation and arbitrary enforcement practices [2]. For example, in Tza Yap Shum v. Republic of Peru, the tribunal found that Peru's freezing of bank accounts constituted indirect expropriation without compensation. The convergence of environmental regulatory measures and expropriation risks further exacerbate legal uncertainty in investments. On the other hand, based on the complex social background of the host country, the virtual absence of the host country's right to regulate may also lead to the proliferation of non-traditional risks, which may cause investment projects to suffer great losses. Illustratively, in Occidental v. Ecuador, the host state's unilateral termination of investment contracts without prior consultation and its abuse of proportionality tests epitomized systemic deficiencies in procedural justice. Currently, the ISDS mechanism remains the primary recourse for foreign investors. In this context, scholars have advanced the "State Exit and Re-Entry" thesis, contending that the ISDS regime's pro-investor bias excessively constrains host states' regulatory space, potentially inducing "regulatory overcompensation". This phenomenon manifests as heightened foreign investment scrutiny by host states, thereby perpetuating irreconcilable conflicts of interest between investors and sovereign regulators [3]. On the contrary, an excessive bias in favor of investors may also lead to a regulatory chilling effect, resulting in the host country's avoidance of regulation in the public interest. Therefore, how to build an institutional framework that balances investor rights and host country’s public interests has become an urgent scholarly imperative. Based on this, this study employs normative analysis method, case study method, and comparative study method to address the equilibrium between investor rights protection and the public interest of the host country, exploring the ways of remedies for investor rights under the balance of interests. Specifically, on the basis of exploring the investment protection model and foreign investment regulatory system of other countries, combining with China's national conditions and international investment agreements, this paper innovates the relief path for investors' overseas investment, provides institutional support for protecting investors' rights and interests, which will in turn promote the long-term development of China's BRI.

2. Literature review

At present, scholars focus on the difficulties of protecting investors' rights in the BRI, mainly from the host country's institutional deficiencies and the limitations of Bilateral Agreements (BITs) and put forward strategies to deal with them.

At the host country level: Firstly, some countries have ambiguous environmental legislation, weak regulation of foreign investment, administrative opacity and other problems. Scholars suggest refining the dispute clauses in BITs and utilizing overseas investment insurance to reduce the risk. Secondly, the host country through the "exhaustion of local remedies doctrine" and other systems designed to strengthen the right of initiative, resulting in investors having to protect their rights through cumbersome procedures and increased costs, so the need to establish dispute prevention and alternative dispute resolution mechanisms. Thirdly, the rise of international investment protectionism impedes the flow of foreign investment, which is advocated to be resolved by investment liberalization and facilitation [4-6].

From the perspective of international investment agreements, China's early agreements emphasize the protection of the interests of the host country, the entity norms are insufficient, the need to reform the mechanism and the addition of exception clauses; the agreement has a narrow scope of coverage, the preliminaries are complex, even if the agreement to expand the arbitrable matters, the investor is still subject to procedural constraints; litigation costs are expensive,

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prompting enterprises to tend to non-litigation methods of settlement, such as soft law, diplomacy, etc. [7,8].

In summary, this study argues that although existing studies analyze the dilemma from multiple dimensions, more attention needs to be paid to the balance of interests when reconstructing the system. The current institutional conflict between host countries and investors is essentially a contradiction between development needs and interest protection. The future system design should break through the thinking of protecting the interests of a single subject and build a dynamic balance framework. On the one hand, through the improvement of international investment agreements, the boundaries of the host country's right to regulate and the provisions of investor rights and interests protection should be clarified; on the other hand, innovative dispute resolution mechanisms should be developed, integrating mediation, arbitration and other multifaceted means to enhance the efficiency and fairness of dispute resolution, so as to realize a win-win situation for the interests of all parties in the BRI investment.

3. Experience of the international investment protection system

3.1. Institutional dilemmas and root causes of the BRI investor protection system

3.1.1. Institutional risks and regulatory deficiencies in the host country: a perspective on tax retrospectives and sudden policy changes

Tza Yap Shum v. Republic of Peru highlights the risk of arbitrariness in the implementation of the host country's policies. The Peru tax authorities took surprise preservation measures (e.g., freezing accounts and withholding debts) against Technical Specifications for Special Equipment (TSG), which directly cut off the enterprise's capital chain, leading to a short-term plunge in its sales and asset value, and putting its operation in serious difficulties. Ultimately, the ICSID tribunal ruled that the Peru government's actions violated the fair and equitable treatment provisions of the China-Peru BIT and constituted an indirect expropriation. The tribunal found that the measure suffered from a lack of public purpose (e.g., retroactive taxes for five years beyond a reasonable period of time), an uncontrolled procedure (deprivation of operational capacity without hearing), and a serious imbalance in proportionality, among other core issues.

A similar risk was further highlighted in Occidental v. Ecuador. The Government of Ecuador unilaterally terminated an oil contract and retroactively modified the sharing clause, which the tribunal found to constitute an expropriation based on a "stabilization clause" in the investment contract.

Together, the two cases expose the flaws in the system of reconstructing foreign investment interests through retroactive enforcement in resource-rich countries. First, the collapse of policy predictability, as Peru retroactively applied the old tax rate and Ecuador overturned the existing contract without a transition period or consultation mechanism; second, the deflation of the boundaries of the right to regulate, as SUNAT arbitrarily expanded the definition of "industrial enterprise" to impose compliance obligations, and Ecuador denied the stability of the contract in the name of sovereignty, which emphasized the hollowing out of the rules of the law by the administrative power; and finally, the remedial mechanism failed, and the administrative review filed by TSG was formally dismissed by the Peru Tax Court, confirming the judicial system's connivance with administrative arbitrariness.

According to UN Trade and Development (UNCTAD), developing country expropriation disputes have centered on such sudden changes in tax and resource policies. Both cases show that

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the conflict between the short-term fiscal needs of host countries and the long-term stable expectations of investors has become a systemic threat to the sustainability of BRI investments.

3.1.2. Institutional limitations of BITs and dispute settlement mechanisms

Another important reason for the difficulties faced by China's overseas investors stems from the lagging rules and imbalances in investment agreements and the lack of efficiency and fairness in dispute settlement mechanisms. The lagging, broad and unbalanced nature of existing investment agreements and bilateral treaties is a source of inefficiency and unfairness in the ISDS mechanism.

In Tza Yap Shum v. Republic of Peru, the vague definition of "expropriation" and the lack of a clear definition of the concept of "indirect expropriation" in the BIT between China and Peru created additional costs and obstacles for Chinese investors to defend their rights. Most of the BITs signed between China and other countries are outdated due to the age of the agreements, and the outdated provisions are difficult to adapt to the development of the emerging era and are unable to effectively protect the legitimate rights and interests of investors. In recent years, China's outbound investment agreements have paid more attention to the concretization of conceptual definitions. For example, the 2012 China-Canada BIT and the 2015 China-Korea FTA define indirect expropriation as "measures with the same effect as expropriation or nationalization," clarifying the concept of "indirect expropriation". The concept of "indirect expropriation" has been clarified. However, China's legal system has not been optimized as a whole, and the Foreign Investment Law and other domestic laws still do not establish a relevant legal framework [9].

In addition to this, there is an imbalance of skewed protection in BITs. Given that BITs are established to safeguard investors' rights and stabilize the development order, a certain degree of bias is the goal, but excessive bias will inevitably lead to the opposite result. Therefore, a certain degree of favoritism is justified by the purpose, but excessive favoritism will inevitably lead to the opposite result. The excessive bias of the ISDS regime in favor of investors can lead to both regulatory chilling effects in host countries and excessive State returns. When the regulatory chilling effect reaches a critical point, the host country will turn to a “sovereignty return" to counter the ISDS regime, but it may slip into the extreme of exclusionary regulation or fragmentation of rules. Thus, dynamic equilibrium is the only sustainable path.

At the same time, the ISDS mechanism's high cost of defending rights and excessive time for defending rights have also been criticized by many investors, based on the fragmentation of bilateral and regional agreements and other characteristics, the inefficiency and high cost of the system limitations make it difficult to become a universal dispute resolution mechanism.

4. Experiences and institutional reconstruction paths for the protection of investors' rights in the Belt and Road Initiative

4.1. Critical absorption of the international investment rules system: the United States-Mexico-Canada Agreement (USMCA) as an example

Limitations on the scope of justiciability and institutional innovation. At present, the disputes between investors and host countries are generally characterized by the phenomenon of the host country's regulation being constrained by international arbitration tribunals due to the excessive scope of justiciability, which has also caused the so-called "regulatory chilling effect". At the same time, the subjective tendency of arbitrators in ICSID is often criticized by scholars. Therefore, in the

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USMCA, corresponding solutions and innovative systems have been proposed, which are worthy of our reference.

Firstly, a significant change from the North American Free Trade Agreement (NAFTA) to the USMCA is the limitation of the scope of justiciability. On the one hand, the USMCA grants full ISDS to industries that are sensitive to government contracts; on the other hand, it excludes "indirect investment" arbitration. To explore the intention of its establishment, in the ICSID arbitration cases, sensitive industry disputes are frequent, the host country's regulatory risk is high, so it is necessary to give investors complete rights of action to attract foreign investment; at the same time, exclude the arbitration of "indirect expropriation", to avoid the challenge of public policy by the ISDS, the host country's regulation of the difficulty, reflecting the At the same time, the exclusion of arbitration for "indirect expropriation" avoids public policy being challenged by ISDS and poses difficulties for host country regulation, and reflects the reservation of the host country's right to regulate and avoids negative host country regulation.

Secondly, the institutional innovation on impartiality and independence of arbitration. First, the IBA Guide is used as a soft law tool to guide the conflict of interest in international arbitration, and the types of conflict of interest are clarified; second, the phenomenon of "changing hats" is prohibited, and the rotation of roles is strictly limited [10].

Criticize the trade protectionist tendency of the USMCA, which explicitly prohibits investors from filing ISDS on the basis of host country market access discrimination and preserves the right to regulate access to the host country. The restriction on market access discrimination is ostensibly a protection of the host country's right to regulate, but in fact reflects a hidden trade protectionist tendency. Trade agreements should adhere to the principles of openness, transparency and inclusiveness to create a freer and more convenient environment for global trade, and there should not be any form of double standards and trade protection. Therefore, people are critical of the relevant provisions of the USMCA and do not agree with them.

In conclusion, the USMCA reflects a balanced design for the interests of investors and host countries, and improves some of the problems in the ISDS, which is worthy of our reference. However, people still need to continue to explore the improper provisions and tendencies as well as the imperfections in it.

4.2. Optimization of rules and balance of interests in IIAs: refinement and differentiated designs

4.2.1. Refinement of substantive provisions: taking "indirect expropriation" as an example

As previously noted, definitional lacunae regarding indirect expropriation in the China-Peru BIT precipitated excessive litigation costs in the Tza Yap Shum case. Vague clauses in prevailing agreements-notably the FET standard-have been subject to expansive arbitral interpretations, triggering regulatory chilling effects. Investment treaties concluded in earlier eras inevitably contain ill-defined provisions, regulatory omissions, and operational disconnects from contemporary practice. To address these deficiencies, this study proposes the following groundbreaking remedial approaches.

First, the application of the principle of proportionality requires that the degree of intervention in investment by host country measures be proportional to the public purpose, and that the interests of investors not be unduly jeopardized for the sake of the public interest, and that the degree of intervention in investment should be minimized on the basis of the protection of the public interest; second, procedural due process is required, and procedures such as hearings and consultations are

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mandatory for host countries before taking expropriation measures, as a check on administrative power.

While avoiding the subjective discretion of the arbitral tribunal, it also leaves room for proper regulation by the host country for environmental protection and taxation.

4.2.2. Differentiated strategy development and rejection of one-size-fits-all universal strategies

As the level of economic development and the rule of law vary from country to country, it is natural that the same investment strategies cannot be applied consistently. Therefore, in the face of different types of countries, it is necessary to formulate appropriate and differentiated investment agreements. For example, in countries where the rule of law is relatively mature, the application of international standards can be appropriately liberalized and the ISDS regime and high-standard levy provisions can be fully applied to meet actual investment development needs. Conversely, in countries with more vulnerable economies, such as Laos, in order to safeguard the rights of investors and encourage the entry of foreign capital to promote development, the focus could be on improving investment insurance to reduce the risks of outward investment.

4.3. Top-level design of the BRI investment protection convention: pluralistic innovation of dispute settlement mechanisms

ISDS is costly and time-consuming, which is not conducive to the sustainable development of the BRI. Therefore, to address the existing problems of ISDS, this paper creates a multifaceted dispute resolution mechanism based on the timeline of dispute resolution. From the preventive organization of disputes to the mandatory mediation procedure after the disputes occur to the arbitration and judicial procedures after the mediation fails, through the design of the whole process of dispute resolution system, the efficiency of dispute resolution is improved, and the rights and interests of investors and host countries are safeguarded.

5. Conclusion

This paper comprehensively utilizes the normative analysis method, case study method and comparative study method to explore the dilemma of protecting the rights of Chinese overseas investors in the host country under the background of the BRI, as well as its institutional roots. The study focuses on the core contradiction between the protection of investors' rights and interests and the host country's right to regulate in public interest and analyzes the risk of "regulatory expropriation" triggered by the fragmentation of the host country's environmental legislation and arbitrary law enforcement, which reveals the inherent vulnerability of the host country's institutional environment. At the same time, this paper critically examines the institutional limitations of the current ISDS mechanism, which exacerbates the conflict of interest between the host country and investors, and is not conducive to the long-term stability and sustainable development of BRI investment.

Based on the analysis of the above dilemma, this paper concludes that the key to institutional restructuring lies in the construction of a dynamic and balanced framework to harmonize investment protection with the host country's legitimate right to regulate. At the rules level, the core lies in optimizing the substantive provisions of the IIA and implementing a differentiated strategy to customize the content of the agreement according to the host country's level of rule of law and stage of development, so as to avoid a "one-size-fits-all" approach. At the mechanism level, in view of the

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shortcomings of traditional ISDS, this paper advocates innovating the dispute settlement system, exploring the top-level design of establishing a BRI investment protection convention, and constructing a hierarchical and diversified settlement path of "prevention-mediation-arbitration/judicial", with particular emphasis on the role of dispute prevention organizations and the introduction of mandatory mediation procedures to enhance settlement efficiency, reduce costs and promote reconciliation.

However, this study is limited to not analyzing in-depth the links between investors, home countries and host countries, the role of third-party subjects and the legal construction of home countries. Future research can be expanded to the dynamic balance between the three subjects and continue to deepen the exploration of the multi-governance system. To summarize, only through the rules of investors, host countries and home countries to discuss and share the benefits, can people find a balance between the protection of rights and interests and sustainable development, and lay the cornerstone of the rule of law for the BRI.

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