China's Belt and Road Initiative – opportunities and challenges for Australian contractors

China's 'Belt and Road Initiative' (**BRI**) is the world's largest economic development agenda, and is providing the scaffolding for infrastructure projects across countries forming part of either the land-based 'Silk Road Economic Belt' or the sea-based '21st-Century Maritime Silk Road'. The BRI is further explained in the article titled 'China's Belt and Road Initiative' by Monica Sun, Hilary Lau and Jie Li. BRI projects will be many and varied, but will uniformly have an early focus on infrastructure, including ports, railways, airports and utilities.

Through the BRI, China is said to be investing close to US$1 trillion into planned projects, with BRI host nations similarly expected to significantly boost their infrastructure budgets.

Despite the vast opportunities presented by the BRI, Australian construction and infrastructure firms have, to date, been relatively slow to invest. The Australian Government has also been reticent to endorse the BRI, and as yet has not entered into a memorandum of understanding with China on the BRI (whereas many other nations, including New Zealand, were relatively quick to embrace the prospects the BRI presents). This, coupled with the perception that the legal and regulatory landscapes of BRI nations are difficult to navigate, may also be deterring investment.

Without doubt, the level of legal and regulatory sophistication across BRI nations is varied; which complicates investment decisions. Using South East Asia as an example, Singapore has a very advanced legal system and stable political affairs, which is attractive to foreign investors. By contrast, Myanmar has a developing legal system complicated by both political and social unrest, which is in turn deterring some foreign investors.

This article aims to provide an insight for Australian contractors (with applicability to other international contractors) considering participating in BRI projects into the:

- opportunities presented by the BRI; and
- mechanisms for managing the risks inherent in BRI projects and jurisdictions.

Competitive advantages for Australian firms

Australian firms are well respected internationally. They are considered to have strong technical expertise in major infrastructure projects and a depth of knowledge in delivering complex projects. Australia's infrastructure investment model of public private partnerships (**PPP**) is widely applauded as an innovative example of project delivery.

Australian construction firms have skills and expertise which present obvious synergies for BRI host nations, particularly in developing nations where local expertise may be limited. Specifically, BRI nations may look to Australian firms for their expertise, including:

- leveraging their technical and project management skills. Particularly, many BRI projects are long-term infrastructure projects which require sophisticated design and construction expertise;
- familiarity with PPP models. This method of contracting is expected to be increasingly adopted in order to address the anticipated shortfall in government investment for BRI projects; and
- significant experience in sustainable development, which China has announced as a key driver in BRI investment.

Australian firms' reputation for good governance and best practice building and development standards also provides a counterbalance of risk to investors from other nations looking to take advantage of the BRI, as well as local firms wishing to shore up their own credentials when bidding for roles in projects.

Leveraging local expertise

While Australian contractors have much to offer BRI host nations, partnering with local entities may be the key to successful local investment. Many BRI countries lack capital and construction skills, but can provide a strong labour force and knowledge of the local culture. Local firms understand the local market and its inherent challenges, and can therefore play a valuable role in navigating legal and regulatory requirements. That said, having high level executives or directors "on the ground" in host nations may also be a key competitive advantage.

Establishing a local subsidiary in the host nation or forming joint ventures with local partners allows Australian contractors to access growth opportunities not otherwise available domestically. For example:

- John Holland Pty Ltd, in joint venture with Zhenhua (Singapore) Engineering PL, was awarded the contract to construct the two-level underground Saglap Station along the 43km Thomson-East Coast metro line in Singapore; and
- Lendlease, in joint venture with TRX City Sdn Bhd (a wholly-owned subsidiary of Malaysia's Ministry of Finance), is developing the TRX Quarter in Malaysia. This is Lendlease's largest mixed-use development in Asia.

It should be noted that foreign investment laws across BRI nations vary widely from jurisdiction to jurisdiction. As a result, when it comes to structuring foreign investment, foreign investors should engage with local counsel early in the transaction timeline. It is important that time is spent considering the investment structure to ensure it complies with local law – whether the investment is structured via a special purpose vehicle incorporated in the host jurisdiction, a partnership in the form of a JV, or otherwise.

Certain local government or regulatory approvals may be required before Australian contractors can enter overseas markets, or acquire or invest in certain assets or sectors, or participate in greenfield and brownfield projects, in foreign jurisdictions. For this reason, investors should engage with local authorities and regulators in the initial stages of any transaction. Failure to obtain the necessary regulatory approvals may cause significant delays to a transaction or, worse, result in the deal falling over.

Anti-bribery and corruption

The BRI runs through some countries that are perceived as being highly susceptible to corruption, including countries rated as high risk by Transparency International's Corruption Perceptions Index. It is likely that, with the increase in BRI related investments and projects in which Australian firms will engage, Australian authorities will increase their focus on these activities.

The Australian Criminal Code makes it an offence for an Australian person or firm to provide a benefit to a public official with an intention to influence that public official. It is important that Australian firms participating in the BRI have sufficient processes and procedures in place to manage any bribery and corruption risks.

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Proactive risk mitigation

The BRI presently traverses more than 60 countries, all with vastly differing legal and economic systems. As a result, the risks and rewards on offer to participants in BRI projects are many and varied.

There is currently no single, multi-lateral treaty governing the BRI. Australian investors must therefore take an ad-hoc approach to risk management. Key categories of risk that must be managed include:

- foreign investment restrictions;
- regulatory challenges;
- anti-bribery and corruption;
- political risks (which differ from country-to-country);
- commercial and contractual risks against counterparties;
- litigation in local courts; and
- language and cultural differences.

The above factors will influence all aspects of the transaction, spanning the investment decision itself, across structuring the investment, and to drafting the relevant project documentation. Careful and considered attention must be paid when negotiating project documentation to mitigating the significant risks involved in these projects. This includes how the dispute resolution procedures are crafted in order to minimise uncertainty in relation to the interpretation and enforcement of contractual rights.

Highlighted below are some common provisions within transaction documents that play a key role in managing these risks.

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Governing law provisions

All key transaction documents should contain a "governing law" provision, nominating the law under which the agreements are to be construed. Failure to nominate a governing law can give rise to serious uncertainty as to the interpretation and operation of the agreements themselves, as well as how disputes will be resolved.

In the absence of a governing law provision, a court or tribunal will be required to determine which laws apply. As indicated above, the legal systems of BRI countries differ significantly. Again, using South East Asia as an example, Indonesia and the Philippines are civil law jurisdictions, while Singapore and Hong Kong are both common law countries. As such, participants would ideally look to nominate the laws of a country with which they are familiar, and which is unlikely to be biased towards the counterparty. Participants commonly opt for the laws of Singapore, Hong Kong, England and Wales and even New York to govern their contracts.

Escalation procedures

Parties should consider whether their chosen contractual dispute resolution process should require certain steps to be taken before either party can commence proceedings. Whilst short and simple escalation procedures, such as notices of dispute and negotiation or mediation requirements, can be useful, contracts with complex escalation procedures are not uncommon. More complex escalation

procedures can be appropriate, depending on the circumstances. However, as a general rule, the more complex or proscriptive the procedure, the greater the delay before the dispute can be referred to arbitration. This delay can translate into increased uncertainty and cost to the participants, including the risk of arguments regarding whether or not the escalation procedures have been strictly complied with. Such arguments are generally costly distractions from the substantive dispute.

Mediation

Mediation is a flexible process and can be a commercially expedient way to resolve a dispute. It can be adopted at any stage of the dispute resolution process and can be managed in any way that the parties choose, including through use of a private mediator agreed by the parties, or being administered by an institution.

Importantly, there are currently no international rules or standards recognising the enforceability of mediated (or negotiated) settlements. Practically, this means that a party is unable to enforce a settlement directly, but must instead sue in a competent jurisdiction or commence arbitration proceedings to obtain judgment in the terms of the settlement agreement. Therefore, if reaching a negotiated or mediated outcome is anticipated, parties should seek legal advice as to how the terms of the mediation clause or agreement can be drafted in order to minimise enforcement risk.

Arbitration

It will be of primary importance for most BRI projects, in the dispute resolution context, to avoid litigation in the local courts. To avoid that eventuality, the parties should carefully draft their dispute resolution clauses to contain an express and clear agreement between the parties to submit disputes to arbitration and for any arbitral award to be binding.

Depending on the circumstances, arbitration is often the preferred dispute resolution forum for cross-border disputes, due to the relative ease of enforcement of arbitral awards pursuant to the terms of the New York Convention. The majority of countries participating in the BRI are signatories to the convention.

When agreeing an arbitration clause, conscious decisions should be made regarding:

- **The seat of arbitration**, which determines the applicable arbitration law. If parties wish to challenge an award, or in some situations seek interim relief, that must occur in the courts of the jurisdiction of the seat. Choosing a seat within a jurisdiction that is a member of the New York Convention is important.
- Nominating a reputable **arbitral institution and institutional rules**, or if the parties prefer ad-hoc arbitration, setting out detailed procedures to which the parties agree to adhere. Importantly, some institutions (such as the Singapore International Arbitration Centre, Hong Kong International Arbitration Centre and International Chamber of Commerce International Court of Arbitration) allow arbitrators to grant emergency interim relief, whereas others may not. Institutional rules also differ in the way they manage matters such as consolidation of disputes and joinder of additional parties.
- The **language or languages** of arbitration, which will also affect time and cost.

Investor State Dispute Settlement

Political risk is a feature not all Australian contractors will be experienced in managing, but is an important issue to grapple with in the context of the BRI. In circumstances where bilateral investment treaties (including free trade agreements) exist between Australia and a BRI host nation, Australian firms can rely on the protection of Investor State Dispute Settlement (**ISDS**) provisions.

Under ISDS provisions, a party aggrieved by a host government's breaches of its investment obligations can bring arbitral proceedings directly against the host government. ISDS provisions may apply where the host nation has discriminated against the applicant's economic interests in that country. This may include:

- nationalisation of foreign owned assets without adequate compensation (often referred to as expropriation);
- being treated in a manner that is not fair and equitable; or
- preventing funds of an investor relating to an investment from being transferred freely off-shore.

ISDS provisions are sometimes viewed sceptically by the media and public in host nations. However, they are an important tool for Australian firms to protect their interests and investments. As with commencing any contentious proceedings, the decision to take advantage of ISDS provisions should not be taken lightly.

In summary

Australian companies are perfectly placed to take advantage of the opportunities presented by the BRI. By realising the opportunities, and being aware of the mechanisms to carefully manage the associated risks, Australian companies stand to gain significantly in this new wave of infrastructure development.

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