

# BRI risk mitigation and dispute resolution options in the coming decade



**Martin David**  
Principal  
Baker McKenzie  
Wong & Leow (Singapore)



**Jo Delaney**  
Partner  
Baker McKenzie (Sydney)



**Nandakumar Ponniya**  
Principal  
Baker McKenzie  
Wong & Leow (Singapore)



**Mini vandePol**  
Registered Foreign Lawyer  
Baker McKenzie  
(Hong Kong)

Six years after its inception, the Belt and Road Initiative (BRI) launched by Chinese President Xi Jinping has entered a new, more mature stage. Now based on a more inclusive, transparent and sustainable approach, the global development strategy has been gaining more traction in the 130+ collaborating countries.

However, there are two sides to this particular coin: as the opportunities grow, so do the risks. Risk mitigation and compliance for BRI projects have become top considerations for all parties involved in BRI-related projects, especially after a few cases of losses that highlighted the need to take effective proactive measures.

### A new phase

The recent “BRI & Beyond Forecast” produced by Baker McKenzie and Silk Road Associates considers a few potential roadmaps for the development of the BRI in the next decade or so. The Global Cooperation Model approach estimates that BRI-related investments will reach USD 1.32 trillion in the 2020s. In contrast, the Uni-Polar Model takes into account the potential impacts of a significant recession coupled with increasing nationalism and more aggressive competition from other nations, and puts the value of potential BRI-related investments in the 2020s at only USD 560 billion.

Ben Simpfendorfer, Founder and CEO of Hong Kong-based BRI consultancy Silk Road Associates, notes that the early stage of the BRI was characterized by projects in relatively small economies with lower incomes. However, Chinese companies have now shifted their focus back to core markets in Southeast Asia such as Indonesia, Thailand and Malaysia because companies have gradually realized that the former approach left them with an international but fragmented platform.

Chinese state-owned enterprises (SOEs) are no longer the exclusive investors of BRI projects. Many non-Chinese companies and financial institutions are now involved because Chinese developers and lenders realized that these stakeholders had the specialized experience and knowledge to undertake projects in many BRI countries.

As Chinese developers gravitate toward competitive sources of project funding and move away from having to procure loans with parent company guarantees, they start to see the benefits of involving international lenders, who bring with them project finance experience and knowledge of projects in many BRI countries. This will also usher the BRI into a new phase, one marked by international and Chinese financial institutions lending alongside one another.

At the same time, even though megadeals still dominate BRI investments, there are growing signs that the scale of BRI infrastructure projects has shifted from colossal projects to mid-sized investments. This is partly due to debt problems in some BRI countries, but it is also due to a realization among Chinese investors that these mega transactions are often more difficult to implement successfully and quickly because they involve a great deal of public scrutiny and political considerations.

The new landscape of the recalibrated BRI brings a new set of opportunities, but, at the same time, companies need to be vigilant in managing and mitigating the legal risks of these projects.

“Whenever you’ve got a long-term contract in place, you need to develop risk management strategies upfront so that you are prepared for the issues when they arise,” said Baker McKenzie’s partner Jo Delaney during the firm’s seminar on “Navigating risks along the Belt and Road” in October.

### Heightened legal risks in BRI projects

In addition to the existing risks of corruption and bribery, we are seeing sudden changes in local policies and increased political turbulence in some BRI countries. Many of these countries are increasingly involved in significant foreign-funded projects. The combination of these factors poses great challenges to companies looking for profits along the Belt and Road.

A frequent lack of familiarity with the structure and operation of the contractual terms among collaborating countries, as well as their limited experience

in dealing with contractual settings, could heighten the legal risks associated with project management and execution.

A case in point is a pipeline project by Sinopec Oilfield Services that incurred an RMB 3 billion loss in 2016 due to an “unexpected” change in design by the Saudi Arabian project owner. To compound this, Sinopec was also confronted with challenges in the process for obtaining compensation.

There has also been evidence of increasing tensions between China’s approach to managing its international projects and the interests of local communities.

In June 2019, the construction of a Chinese-financed coal-fired power plant in Kenya was halted over environmental concerns and amid opposition from local residents. In the same month, Ghana cancelled an agreement on a USD 22 billion railway project due to an alleged breach of confidentiality.

Concluding the key takeaway from Baker McKenzie’s October seminar, Nandakumar Ponniya, Asia Pacific Chair of the Firm’s International Arbitration Practice, suggested companies could conduct risk analysis early on, “Businesses need to have enough flexibility in the modelling given that there are likely to be macro-economic factors that cannot be foreseen. Having an exit mechanism in place is also important — companies need to ensure they can either sell the deal or pass on the deal to some other party if it becomes unattainable or unviable economically.”

“Handling compliance and regulatory requirements is another key concern for businesses, especially if they operate in multiple markets,” says Mini vandePol, Asia Pacific Chair of Baker McKenzie’s Compliance and Investigations Group.

VandePol notes that compliance in areas such as anti-bribery and anti-corruption, trade sanctions, data privacy and cybersecurity is at the top of the list.

“If you look at all the major countries that are involved in BRI projects and China itself, the compliance issues are actually quite extensive and the risk around various compliance matters, for example, bribery and corruption, is very high,” she says.

Almost all the countries involved in the BRI are ranked as “hot countries,” with the greatest perception of corruption by Transparency International.

“These risks can have significant consequences, ranging from a reduction in profitability to heavy legal penalties and potential criminal sanctions,” says vandePol. “So, managing compliance risks cannot be an afterthought, it really does need to be considered right at the front end of the project.”

Although these risks are omnipresent, they are not necessarily deal breakers - it’s all about willingness to invest up front on appropriate risk identification, management and mitigation measures.

### Navigating the risks along the Belt and Road

Putting in place a risk management plan as part of

the overall transaction strategy is an important first step. Another is benchmarking the measures that other companies have taken.

However, vandePol warns that commercial solutions that involve taking a shortcut around compliance requirements may create significant long-term risks, even though they are tempting to businesses in the short run.

“For instance, it is extremely high risk for a company to engage a third party to manage government approvals and to shorten the compliance time frame or complexity, without performing adequate due diligence or putting in place controls around the third party’s activities,” says vandePol.

“We have seen corruption payments made by third parties to governments to obtain permits and licenses. This later resulted in a continued demand for improper payments when inspection or audits by government compliance bodies failed, or, in more extreme circumstances, when there were health and safety incidents as a result of the inadequate compliance measures.”

Additionally, the level of enforcement of anti-bribery laws is on the rise in a number of BRI countries, particularly in China. President Xi said at the second Belt and Road Forum in April this year that the Chinese government would encourage local companies engaged in BRI projects to comply with international rules and standards, in areas such as project construction and procurement. He also reiterated that there would be “zero tolerance” of corruption.

“Recent guidance from these government bodies makes it clear that there will be careful scrutiny of transactional projects to determine their risk profile and the adequacy of the risk measures undertaken by companies,” says vandePol.

“We are working closely with both majority and minority BRI JV partners and corporates to enhance their anti-bribery and corruption compliance processes, as well as satisfying the demands of various stakeholders, such as the development banks, where the funding is dependent on the existence and implementation of a credible compliance program.”

What is becoming clear is that Chinese players are not the only beneficiaries of the BRI. Non-Chinese companies can also enjoy the opportunities brought about by this ambitious global initiative.

Martin David, Asia Pacific Chair of Baker McKenzie’s Projects Group, says that the risks facing developers of projects in BRI countries are fundamentally the same whether the developer is Chinese or non-Chinese.

“The differences, however, lie in the approach to developing the projects and the sources of financing,” he notes.

“Chinese lenders have traditionally sought to mitigate lending risks through parent company guarantees instead of lending against project risks,” David explains. “But we are seeing more conventional limited and non-recourse financing structures being pursued,

and Chinese companies not being ready and willing to give such parent guarantees. They are standing up to the Chinese lenders and demanding better lending terms.”

Furthermore, the cultural issues that prevent Chinese companies from doing business in a BRI country are often overlooked.

“Chinese businesses are not used to what is often a very different approach to project development. Therefore, getting the approach right and making an agreement with the key project stakeholders, such as governments, utilities, regulators, etc., is something that can make the difference between failure and success,” says David.

Fortunately, Chinese companies are now recognizing the value of having strong local partner support throughout the project development. One of the first hurdles Chinese companies have to overcome when they are investing in a new emerging BRI market is the so-called ‘country risk’ — put simply, not just the commercial risks like will we get paid but the risks associated with doing business such as the way to navigate opaque plant import regulations. A strong local partner can help but finding a partner and then building the trust and relationship takes time which many Chinese companies are not willing to invest in.

“The end game must be to have a good understanding of the market with a supportive strong local partner; increasingly this should be a critical part of the investment decision-making process,” David adds.

To help companies navigate the risks of BRI projects, Mini vandePol, Asia-Pacific Chair of Baker McKenzie’s Compliance and Investigations Group, put together a suggested checklist for risk minimization in BRI activities:

- **Put strong, decisive, and ethical leadership in place.**  
Inexperienced and weak decision-making will lead to pressure/temptation to take risky short cuts.
- **Get the full picture when it comes to risk assessment and analysis.**  
Adequately anticipate all types of risks and ensure they are discussed and provided for in the overall project strategy.
- **Understand what is needed to manage complex laws for the movement of people and goods.**  
Approvals for immigration, customs, data

movement and tax compliance will enable projects to continue or stop them short. There are no shortcuts for gaining regulatory approvals and licenses. Alternative “faster” paths will lead to major problems and delays in the long term.

- **Be vigilant about engaging third-party providers.**  
Third-party due diligence and ongoing oversight is key to ensure companies have the right and trustworthy partners for the project.
- **Prioritize long-term project completion over racing to win opportunities.**  
Procurement processes should be closely monitored - planning for long-term project success will save companies from incurring additional costs from delays or cancellation of projects due to insufficient upfront due diligence and planning.
- **Find advisers who are dedicated to designing ethical solutions that work.**  
Challenges are inevitable, therefore, to move a project forward, companies have to have the right advisers in place from the start, who know what the risks look like on the ground and can find solutions to unexpected difficulties without cutting corners.
- **Educate the team on the risks and provide practical tools for risk management and mitigation.**  
Compliance and legal advisors are necessary guides but it’s the business personnel on the ground and those having regional oversight who need to be comprehensively trained and held accountable for effective risk management.
- **Build strong, trusting relationships with your stakeholders.**  
Strong relationships and effective communication with the various parties involved in the project is a must. The importance of doing business “the right way” needs to be an upfront commitment leaving no doubt as to expectations for the future.

#### Dispute resolution options for BRI projects

Delaney echoes David’s view. “One of the challenges that we often see in BRI projects is the

cultural misalignment between the parties,” she says. “Arbitration tries to address that to some degree although of course the misalignment may have already happened.”

However, arbitration offers the different parties an opportunity to take disputes into a neutral jurisdiction where international arbitrators from varied backgrounds can resolve them, often in either the countries involved in the BRI or in other countries where they have had similar challenges before, Delaney explains.

Careful negotiation and drafting of the contract should ensure that companies have the proper risk management and risk allocation provisions supported by clearly set out liability language. In addition, there should be clear procedures for the provision of notices and the parties should address upfront through clear drafting, the dispute resolution procedures.

“The contract shall also include dispute resolution clauses, some of which can be specifically developed for BRI projects,” says Delaney.

Once a contract is in place, it is important that the commercial teams and the project teams know the contract in order to manage any issues and claims when they arise.

Effective contract management and ensuring compliance with contractual obligations and procedures is an important element of risk management.

Nonetheless, it may be necessary to protect your contractual rights through the dispute resolution process. The parties may have agreed to negotiation and mediation as part of that process. Whether to refer a dispute to litigation or arbitration is an important consideration that should have been determined at the drafting stage.

Enforcement of court judgments remains a key consideration. China, for example, recognizes court judgments made by the courts of only a few countries. In contrast, an arbitral award may be enforced in any of 161 States (including China and Maldives) that are party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards. Nearly all of the countries on the BRI are already party to the New York Convention, with the exception of Turkmenistan, Yemen, Timor-Leste and Iraq.

“When deciding on what’s the optimal dispute resolution mechanism, there are probably a suite of factors that companies will need to take into account, ranging from confidentiality and the need to adapt the process to suit the culture of the parties to the efficiency of the process. Ultimately, what it comes down to is enforcement. Court judgments are enforced on the basis of an agreement or reciprocity between the relevant States; on the other hand, arbitration awards can be enforced in 161 countries to the New York Convention,” says Delaney.

There are new mechanisms being introduced in mainland China to address issues related to dispute resolution.

#### International Commercial Courts

In 2018, the Supreme People’s Court in China created two branches of an International Commercial Court in Shenzhen and Xi’an that act as both the first instant court as well as the final court. The mission of the court is to resolve all international commercial disputes, particularly, BRI-related disputes.

#### Singapore Mediation Convention

Chinese parties may also prefer mediation, particularly with the new Singapore Mediation Convention. Once in force, the Singapore Mediation Convention will permit parties to enforce settlement agreements entered into during mediation directly in a State that is party to the convention. Many of the states on the BRI have signed the Singapore Mediation Convention.

#### Direct Enforcement of Hong Kong Judgments

Earlier this year, the Supreme People’s Court in China signed an arrangement with the Hong Kong Government, which, once effective, will allow for the direct enforcement of legally effective civil and commercial judgments obtained from the Hong Kong courts in mainland China, which covers both monetary and non-monetary relief. This will mean greater certainty and expediency for parties litigating in Hong Kong or China and will benefit BRI investors and the Guangdong-Hong Kong-Macao Greater Bay Area.

#### Interim Measures from the Chinese Courts

A further landmark arrangement between the Supreme People’s Court in China and the Hong Kong Government came into effect on 1 October 2019, allowing parties to Hong Kong-seated arbitrations administered by certain eligible arbitral bodies to obtain interim measures from the Chinese courts that will be enforceable in mainland China. The interim measures available from the Chinese courts include the preservation of property, evidence and conduct. This arrangement is a game-changer as it offers greater protections for foreign entities that may otherwise be hesitant to participate in China’s key policy initiatives due to the lack of urgent relief available.