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The BRI Legal Frameworks and Caucasian Non-Recognition Obligations

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Key Points:

- Countries in the Caucasus are keen to position themselves as providing a key link within a network of international trade routes between Europe and Asia, and thus take advantage of increasing economic benefits. One such network is China's Belt and Road Initiative, yet China's interest in the region has been minimal to date.
- The main legal challenge for BRI investments in regions of political conflict, such as the Caucasus, is the absence of mechanisms that allow for economic engagement with the non-recognised *de facto* regions present in strategically important locations for the BRI to function effectively.
- The same challenge remains for setting up dispute resolution frameworks in such regions.
- The benefits of achieving economic advantage for BRI-participating countries in the Caucasus, in light of such challenges, depends largely on their ability to deal with the cooperation dilemma.

Introduction

Territorial sovereignty issues, apart from being a cornerstone of Chinese foreign policy as “mutual respect for sovereignty and territorial integrity” *huxiang zunzhong zhuquan he lingtu wanzheng* (互相尊重主权和领土完整), are also crucial for the Belt and Road Initiative (BRI) especially with respect to setting up bilateral and multilateral trade and investment treaties and dispute resolutions frameworks with partner countries. Sovereignty is a precondition for treaty-making powers and the capacity to participate in dispute resolutions for both intergovernmental and private claims. Yet territorial integrity is a more complex element as the legal status of secession movements, border disputes and partially-recognised statelets is ambiguous in terms of investment relations.

The International Centre for Settlement of Investment Disputes (ICSID) Convention, the UN Commission on International Trade Law, and other institutionalised arbitration regimes provide dispute resolution mechanisms exclusively between signatory states and nationals of other signatory states¹ as the requirement for

¹ ICSID Convention, Article 25.

jurisdiction *ratione personae*. Parties without a separate legal status as a state have extremely limited, if any, capacity to participate in current public international law. Uncertainty with regard to non-recognised jurisdictions complicates private contracts by further conflict of law problems and multiple variations of possible *forum non conveniens*. The ownership issue of territorial and national assets that might be the most likely recipients of investment carries political and economic risks if the particular territory they are located in is an integral part of a recognised state *de jure* yet *de facto* control is maintained by self-proclaimed local regimes often supported by third parties.

Mitigation of these risks is impractical without clarifying the legal framework prior to engaging in investment or commercial relations with the regions of questionable recognition status or possible dispute resolution either on the interstate or investor-state levels for real property,

commercial or employment related claims.

The question of territorial integrity, therefore, is of key importance for the successful implementation of BRI projects especially in politically charged regions, such as the Caucasus, where separatist *de facto* regimes control strategically important trade junctions.

The Caucasus: Contrasting Aspirations

The Caucasus, a small mountainous region between the Black Sea and the Caspian Sea, is home to more than 50 different ethnic and linguistic groups living in four post-Soviet countries: three of them, Armenia, Azerbaijan and Georgia, are located in the Southern Caucasus whereas all the republics of the Northern Caucasus are part of Russian Federation. The region is a geopolitical crossroad of conflicting political interests given the distinct Euro-Atlantic aspirations of, for example, Georgia in signing the EU Association Agreement in 2012, Armenia's



The Caspian Sea - Caucasus – Black Sea Corridor in the BRI Context (the conflict regions have been marked by warning signs). Source: The Economist.

membership in the Eurasian Economic Union, and Azerbaijan which seeks to balance political ties between the Russian Federation and Turkey.²

The Caucasus has become well-known for secessionist territorial conflicts amongst and within its four sovereign states.³ Attempts by the Georgian government to regain control over the Russian-backed South Ossetian *de facto* regime resulted in a Georgian-Russian war in August 2008 and was followed by Russia's recognition of both Abkhazia and South Ossetia as independent states.⁴ The EU and NATO, on the other hand, are firmly committed to Georgia's territorial integrity and sovereignty of its government over these regions.⁵ The conflict region of Nagorno-Karabakh was the focus of another war between Azerbaijan and Armenia until Russia facilitated a ceasefire in November 2020. China has kept a non-interventionist stand on all these conflicts but publicly called for peace and stability in the region.

The New Old Silk Road

Stories of the East-West corridor in the Caucasus begin in semi-legendary times when the Argonauts crossed the Phasis river near modern Poti to seek the Golden Fleece. One branch of the

ancient Great Silk Road, entering from Shirvan, was functional until the Ottoman and Sassanid invasions and the Russian colonisation of the both sides of Caucasus Mountains.

Now the Silk Road has re-emerged in this region: the presidents of post-Soviet Georgia and Azerbaijan, both former high-ranking career politicians in the USSR, were influential in establishing the Transport Corridor Europe-Caucasus-Asia (TRACECA) initiative in May 1993;⁶ the vision of transitioning from the Iron Curtain by resurrecting the Great Silk Road that connects Central Asia to Eastern Europe via the South Caucasus has become the new regional paradigm for the Caucasian countries involved.⁷ The TRACECA was welcomed not only by Europeans but also by Americans⁸ as their development approaches to the South Caucasus and Central Asia have been framed around the new Silk Road concept.

The idea and local trajectory of the BRI has been popular in Caucasian countries for the past three decades - Georgia's warm welcome at the opening of the Asian Infrastructure Investment Bank (AIIB) in August 2015 is an example of such approval.⁹

² Russia, Armenia and Azerbaijan are members of the Commonwealth of Independent States (CIS) that was formed by the post-Soviet member states. Georgia, expressing a clear willingness to join NATO and the EU, left the CIS in 2009 subsequent to war with Russia. Azerbaijan is closely cooperating with the Non-Aligned Movement (NAM), where China as an observer state and the only Permanent Member of UN Security Council to join the NAM.
³ Abkhazia, the Tskhinvali region (South Ossetia) and Nagorno-Karabakh are examples of such conflict regions that have emerged within the South Caucasus since the 1990s. The former two have been frozen for 20 years until the Georgian-Russian war in August 2008 whereas the latter was frozen for 30 years until the war between Azerbaijan and Armenia in November 2020. The Northern Caucasus has not had such conflicts since the early 2000s.

⁴ *De Facto* Abkhazia and South Ossetia have been formally recognized only by the Russian Federation and the Kremlin-supported governments of Venezuela and Syria as well as Nicaragua, Nauru and Vanuatu. The rest of the international community recognizes them as an integral part of Georgia.

⁵ See Eastern Partnership, *Facts and Figures about EU-Georgia Relations*, https://ec.europa.eu/neighbourhood-enlargement/sites/near/files/eap_factsheet_georgia.pdf; See NATO, *Relations with Georgia*, Dossiers de l'OTAN (Apr. 12, 2021), https://www.nato.int/cps/fr/natohq/topics_38988.htm?selectedLocale=en.

⁶ TRACECA, *Milestones in History of TRACECA* <http://www.traceca-org.org/en/about-traceca/history-of-traceca/>.

⁷ Irene Cheng, *The New Silk Road*, in *RUSSIA-CHINA 1920-2004* 32 Beijing/New York: Issue 5/6 (Michael Bell ed., 2005).

⁸ The Silk Road Strategy Act of 1999 by the Senate Committee on Foreign Relations replaced the existing development framework on the South Caucasus and Central Asia. The new Silk Road was perceived in the West as an alternative development for those regions without Russian influence. See S.579, 106th Cong. (1999).

⁹ Statement by Jin Liqun at a Press Conference in Tbilisi, AIIB NEWS (Aug. 29, 2015), <https://www.aiib.org/en/news-events/news/2015/Statement-by-jin-liqun-at-a-Press-Conference-in-Tbilisi.html>.

Of course, the Chinese BRI is considerably greater in scope than the South Caucasian vision of the New Silk Road yet a major difference is the regional significance of the South Caucasus. The importance of this region has become peripheral in the current BRI, probably due to the political costs that undermine economic benefits. The minor routes of the BRI which pass through the region are the *Zhongjian zoulang* (中间走廊) [Middle Corridor] and the *Hengguan liai de dongxi maoyi he guojing zoulang* (横贯里海的东西贸易和过境走廊) [Trans-Caspian Sea Corridors] connecting China to Turkey and the Black Sea respectively via connecting land and sea routes. The World Bank estimates emphasise the relative cost-effectiveness of these corridors¹⁰ in comparison with the alternative, the northern land-only route via Russia and Belarus called the *Xin Ya Ou dalu qiao* (新亚欧大陆桥) [New Eurasian Land Bridge]. The presence of alternative BRI corridors is driving the Caucasian states to position themselves on the New Silk Road¹¹ although their emphasis on bilateralism in economic and legal cooperation with China is likely to maintain the *status quo* with regard to the BRI priorities in the Caucasus.

Challenges for benefiting from the BRI

Chinese outbound investments in the South Caucasian countries have intensified recently¹² with varying levels of infrastructure investments

mainly in the transport and logistical sectors. The most diverse flow of capital and labour has been seen in Georgia where Chinese companies have invested in ports, Free Industrial Zones (FIZs), real estate, railways, road construction and automotive industries. The AIIB's presence is prominent in Georgian and Azerbaijani economies with more than USD 1 billion loans for infrastructure projects and, more recently, emergency support for the pandemic¹³ and provision of vaccines.¹⁴ Chinese investments, particularly in the South Caucasus however, have been very modest to date in comparison with investments in other post-Soviet nations, especially the Central Asian countries.

Trade turnover between China and the South Caucasus has been increasing faster than large-scale investment projects. Georgia was one of the first countries in the region to conclude a free trade agreement (FTA) with China in May 2017 while simultaneously expanded its networks of FTAs with the EU, EFTA, Turkey and individual post-Soviet countries. The volume of trade reached around USD 3 billion for the entire region by the end of 2018. It must be mentioned that even the breakaway regions have appeared attractive to Chinese investors for certain investments that might drive BRI development in the region (e.g., the wine and agricultural potential of Abkhazia and extraction of minerals from Nagorno-Karabakh). Some of these options have been considered by Chinese investors¹⁵ and exploratory

¹⁰ WORLD BANK, SOUTH CAUCASUS AND CENTRAL ASIA: BELT AND ROAD INITIATIVE AZERBAIJAN COUNTRY CASE STUDY (June 2020).

¹¹ Franziska Smolnik, *Georgia Positions Itself on China's New Silk Road*, STIFTUNG WISSENSCHAFT UND POLITIK COMMENT (Mar., 2018).

¹² Nadège Rolland, *China's Ambitions in Eastern Europe and the South Caucasus*, THE INSTITUT FRANÇAIS DES RELATIONS INTERNATIONALES POLICY PAPER, RUSSIE.NEL.VISIONS, No. 112, (Dec., 2018).

¹³ AIIB approves \$50 mln loan for Georgia to ease impact of coronavirus, REUTERS, (July 22, 2020) <https://www.reuters.com/article/health-coronavirus-georgia-aiib/aiib-approves-50-mln-loan-for-georgia-to-ease-impact-of-coronavirus-idUKL5N2ET4T6?edition-redirect=uk>.

¹⁴ Azerbaijan praises China for vaccine commitments, opposes disparity in distribution, GCTN, (Feb. 27, 2021),

<https://news.cgtn.com/news/2021-02-27/Azerbaijan-praises-China-opposes-disparity-in-vaccine-distribution-YefNAPuEYU/index.html>; Medea Ivaniadze, *Georgian Health Minister: We have negotiations with China about the vaccines*, *ԲՈՆԵՏԻ ՆԱԾԵՐԴԵՏ ՀԱՅՅՆՆՈՒՄԻ* (China in the South Caucasus), RONDELI FOUNDATION (Feb. - Mar., 2021), <https://www.gfsis.org/ge/publications/view/2937>

¹⁵ Daniel Shapiro, *US Should Keep an Eye on Rising Chinese Investment in the South Caucasus*, RUSSIA MATTERS, (Oct. 1, 2020), <https://www.russiamatters.org/analysis/us-should-keep-eye-rising-chinese-investment-south-caucasus>; see Michael Eric Lambert, *The future of Chinese investment in the Caucasus – The case of Abkhazia*, NEW EASTERN EUROPE (Sept. 20, 2018), <https://neweasterneurope.eu/2018/09/20/future-chinese-investment-caucasus-case-abkhazia/>

efforts were made to develop potential infrastructure projects before the pandemic hit.¹⁶

		2017	2018	2019	2020
<i>Armenia</i>	M	478	664	751	674
	X	119	107	194	290
<i>Azerbaijan</i>	M	855	1197	1432	1414
	X	444	114	752	433
<i>Georgia</i>	M	733	834	859	709
	X	202	199	223	476

Export (X) and Imports (M) of the South Caucasus Countries with PRC (in USD millions). Source: *IMF Direction of Trade Statistics*.

All conflict regions in the Caucasus are located at strategic intersections of routes providing the optimal benefits in terms of connectivity. The main advantage of extending economic relations with Abkhazia would be to support the presence of Chinese investments across the north shore of the Black Sea thus facilitating access to Ukraine, Moldova and the larger Eastern European market. Since 2014, the military crisis between China and Russia in Crimea and Eastern Ukraine has meant that the development of the BRI in such an East-West direction is practically impossible.

The Tskhinvali Region and Nagorno-Karabakh are located on the axis that connects the Northern Caucasus to Iran and the Gulf countries, thus connecting Russia to the Middle East. Yet, isolation of such areas under self-proclaimed

governments¹⁷ as well as economic blockades between neighbouring state parties, is limiting potential infrastructure investments. One example of such politically motivated bypassing of the region is the connection of Azerbaijan and Turkey via Georgia. The shortest route to connect the Azerbaijani capital, Baku, with cities in Eastern Turkey (Ceyhan for an oil pipeline and Kars for the railway¹⁸) is via Armenia but the latter has closed its borders with the both neighbours.¹⁹ Such isolation from the east and the west leaves Armenia with the development of its North-South axis as a priority and the potential connection of Gulf countries to the Black Sea. Officials in Yerevan have been conducting high-level negotiations with the Chinese leadership regarding use of this axis.²⁰

The barriers restricting many land routes across the Caucasus highlight the value of Georgia's access to the Black Sea. There are two main seaports at Batumi and Poti although development of both is limited by the physical characteristics of the coastline. The coastal topography of nearby *de facto* Abkhazia would allow construction of an alternative new deep-water port to increase handling capabilities. Yet, this has not been possible despite attempts by the government of Georgia since 2011.²¹ Chinese investors have also recognised the importance of the Black Sea littoral for the BRI expressing interest in both existing and planned ports. One of the front-runners of the government bid to build a deep-water port had been a state-owned Chinese

¹⁶ Елена Заводская (Elena Zavodskaya), *Китайская компания присматривается к абхазской ГЭС* (Chinese company's look at Abkhazian Hydroelectric Power Station) Эхо Кавказа, RADIO FREEDOM EUROPE (Mar. 5, 2018), <https://www.ekhokavkaza.com/a/29080145.html>

¹⁷ The political and economic isolation of the conflict regions in the South Caucasus has little impact on the economic and legal order in the rest of the countries that are controlled by state governments and fully participate in law and development.

¹⁸ The Baku-Tbilisi-Ceyhan Pipeline is one of the most significant region-wide investments connecting Azerbaijan, Georgia, and Turkey. A rail link also serves as an essential part of the BRI *zhongjian zoulang*.

¹⁹ The border closures are caused by the Turkish-Azeri stances during the Nagorno-Karabakh conflict and their positions with regard to the international recognition of the Armenian genocide during World War I.

²⁰ Benyamin Poghosyan, *Armenia–China: Strategic Partnership for Mutual Benefits*, INDRASTRA GLOBAL, (Sept. 20, 2019), <https://www.indrastra.com/2019/09/Armenia-China-Strategic-Partnership-for-Mutual-Benefits-005-09-2019-0035.html>

²¹ One of the pending ICSID cases against Georgia concerns the construction of this port brought by a Dutch contractor. See *Bob Meijer v. Georgia* (ICSID Case No. ARB/20/28).

conglomerate which has also been awarded multiple infrastructure construction projects in Georgia.²² Chinese Limited Liability Companies are also the largest shareholders of the Poti FIZ.²³

Future Prospects

Post-pandemic estimations are difficult to make although it is expected that the Caucasus will remain at the same general level of importance within China's BRI economic strategy. The economic benefits of upgraded infrastructure for participating states depends largely on their ability to turn bilateral investment relations with Beijing into increased regional coordination. Such cooperation has not been possible in the Caucasus for the past three decades and the aforementioned complexities limit the ability of states to do so now.²⁴ The economic benefits from, for example, an integrated transport network would have undoubtedly been greater if border conflicts had not forced investors to detour from routes dictated by market logic. The sensitivity of the BRI's routes to geo-political factors is likely to have a significant impact on the feasibility of expanding projects in the region in the future, and therefore the ability of countries in the Caucasus to benefit economically.

One might suggest that multilateral economic cooperation with a neutral country such as China could encourage positive developments in certain internal conflicts.²⁵ The emergence of China in the Caucasus with such a facilitating role might be possible as long this involvement does not carry political connotations for Russian and Western interests in the region. It is highly unlikely, given

current Sino-US relations and Russia's concern about decreasing influence in the region, that such a role for China in the Caucasus would be welcomed by either.

The issue of finding a proper mechanism for dispute resolution with non-recognised entities is a major legal challenge for BRI host states and private investors in and beyond the Caucasus. For example, the absence of legal instruments has prevented investment in Abkhazia to expand the land corridor towards the west as this could violate the sovereignty of Georgia. The same issue applies to possible engagements with Nagorno-Karabakh or Transnistria in Moldova and, more recently, Crimea. The risks of engaging with these regions is too high and the only way for the South Caucasian corridor to grow with respect to the BRI is either via Turkey or by expanding the maritime trade infrastructure on the Black Sea.

There are certain practices in the current international law regime that would provide a framework for such participation while respecting the non-recognition of these territorial entities. The EU has developed Non-Recognition Engagement Plans for such regions; and China itself and the rest of the world engage with Taiwan under a regime of that sort, being able to trade with the island while firmly adhering to the *Yige Zhongguo zhengce* (一个中国政策) [One-China policy].²⁶ However, the establishment of legal parallelism between those cases and the Caucasian conflicts is tricky given differences in terms of history, context and the international recognition status. It is a topic of further consideration whether this unique case will have

²² Han Peixi (韩沛析), *Gelujia zongli jianzheng ZC gonglu xiangmu tongche* (格鲁吉亚总理见证 ZC 公路项目通车) [Georgian Prime Minister Witnesses Opening of ZC Road Project] (Aug. 26, 2020), http://www.powerchina.cn/art/2020/8/26/art_7440_856535.html.

²³ *Developments around Georgian ports: what is new?*, TRANSPARENCY INTERNATIONAL GEORGIA, (Apr. 22, 2021), <https://transparency.ge/en/blog/developments-around-georgian-ports-what-new>.

²⁴ A simple game theory model expressing such a situation would be an interactive multi-party decision-making model in which the equilibrium for each party is not to coordinate even though payoffs from coordination are high.

²⁵ INTERNATIONAL CRISIS GROUP, *ABKHAZIA AND SOUTH OSSETIA: TIME TO TALK TRADE*, REPORT 249 (May 24, 2018), <https://www.crisisgroup.org/europe-central-asia/caucasus/georgia/249-abkhazia-and-south-ossetia-time-talk-trade>.

²⁶ See Pasha L. Hsieh, *Rethinking non-recognition: The EU's Investment Agreement with Taiwan under the One-China Policy*, 33 LEIDEN J. INT'L L. 689 (2020).

any impact on China's approach to development and its legitimacy²⁷ in the Caucasus (or other regions with similar issues). The decisive factor, even if a legal solution was to be developed, would be the extent to which this solution is acceptable to sovereign states in the region.

There are the significant legal and political costs China has to assess against the expected investment benefits from working in the non-

recognised entities of the Caucasus and larger Eastern Europe. The further expansion of the BRI Trans-Caucasian corridor across the Black Sea would depend on the outcome of an analysis similar to that conducted herein.

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²⁷ See Heng Wang, *Selective Reshaping: China's Paradigm Shift in International Economic Governance*, 23 J. INT'L ECON. L. 600 (2020).