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China's Belt and Road Initiative: An Examination of Project Financing Issues and Alternatives

August Nelson Dinwiddie

CHINA'S BELT AND ROAD INITIATIVE: AN EXAMINATION OF PROJECT FINANCING ISSUES AND ALTERNATIVES

INTRODUCTION

There was a point in human history when the Eurasian continent was joined through a trade route aptly called the Silk Road.[1] This route not only served as a conduit of trade, but also aided in the transmission of religion and culture throughout Asia.[2] Notably, the connectivity provided by the Silk Road facilitated the proliferation of Buddhism from India to China and beyond.[3] In 2013, China spearheaded a vast infrastructure development initiative to realize the vision of revitalizing the Silk Road trade route.[4] This initiative, called the Belt and Road Initiative[5] (BRI), has now blossomed into an emerging network of massive infrastructure projects creating enhanced transportation routes and economic corridors.[6] From

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1. *About the Silk Road*, UNESCO, https://en.unesco.org/silkroad/about-silk-road (last visited March 26, 2020); JOHN LAWTON, SILK, SCENTS & SPICE 9 (2004) ("[T]he Silk Road was the longest overland trade route on earth. It stretched some 12,000 kilometres (7,500 miles) across the mountains, deserts and steppes of Central Asia, joining the markets of China with those of Europe and the Middle East.").

2. Carles Buenacasa Perez, *Trading Silk for Horses: The Surprisingly Simple Origins of the Silk Road,* NAT'L GEOGRAPHIC (Dec. 1, 2017), https://www.nationalgeographic.com/archaeology-and-history/magazine/2018/01-02/silk-road-history/.

3. *About the Silk Road*, *supra* note 1.

4. *Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road*, News Release, Nat'l Dev. Reform Comm'n [NDRC] (Mar. 3, 2015), https://reconasia-production.s3.amazonaws.com/media/filer_public/e0/22/e0228017-7463-46fc-9094-0465a6f1ca23/vision_and_actions_on_jointly_building_silk_road_economic_belt_and_21st-century_maritime_silk_road.pdf.

5. *See* PROSPERITY 51 (Jane Golley & Linda Jaivin eds., 2018) ("[The BRI] began in 2013 with two separate proposals, for a 'Silk Road Economic Belt' and a 'Twenty-first Century Maritime Silk Road' connecting under-developed border provinces with developing countries in the region.").

6. Biliang Hu, Qingjie Liu & Jiao Yan, *Promoting the Belt and Road Initiative by Strengthening '5+1' Cooperation*, *in* 2 CHINA'S NEW SOURCES OF ECONOMIC GROWTH: HUMAN CAPITAL, INNOVATION AND TECHNOLOGICAL CHANGE 410 (Ligang Song et al. eds., 2017). A major focus of the BRI is to revitalize and expand important economic corridors in Asia, including "the

this, the hope for the BRI is to increase connectivity between countries spanning across the Eurasian and African continents.[7] Currently, the initiative includes over 125 countries and almost half of the world's gross domestic product (GDP).[8] In May 2017, President Xi Jinping of the People's Republic of China[9] gave a speech at the Belt and Road Forum[10] addressing the five main goals of the BRI: policy coordination, facilities connectivity, unimpeded trade, financial connectivity, and people-to-people bonds.[11] The scope of this initiative is not limited to infrastructure projects, but also includes cultural and social objectives.[12]

To fund this massive infrastructure project, financing has mainly taken the form of credit lending from China.[13] Since the launch of the BRI in 2013, Chinese banks have given out hundreds of billions of US dollars in loans to participating coun-

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China-Mongolia-Russia Economic Corridor; the New Eurasian Land Bridge Economic Corridor . . . and the China-Central Asia-West Asia Economic Corridor, which stretches from the autonomous region of Xinjian in China's west to the five countries of Central Asia, including the EEU's Kazakhstan and Kyrgyzstan." *Id.*

7. NDRC, *supra* note 4.

8. Wade Shepard, *These 8 Companies Are Bringing The 'New Silk Road' To Life*, FORBES (Mar. 12, 2017, 2:36 PM), https://www.forbes.com/sites/wadeshepard/2017/03/12/8-new-silk-road-companies-that-you-can-invest-in/#16f5ae6e4db9; Matthew P. Goodman & Jonathan E. Hillman, *China's Second Belt and Road Forum*, CSIS (Apr. 24, 2019) https://www.csis.org/analysis/chinas-second-belt-and-road-forum.

9. *See* CNN Editorial Research, *Xi Jinping Fast Facts*, CNN (Jan. 6, 2020 8:28 AM), https://www.cnn.com/2013/01/04/world/asia/xi-jinping—-fast-facts/index.html.

10. *See* Jane Soukas, *China's Xi opens first major summit on New Silk Road,* GB TIMES (May 14, 2017), https://gbtimes.com/chinas-xi-opens-first-major-summit-new-silk-road ("Meeting of state leaders and delegates for the first time to discuss China's Belt and Road Initiative.").

11. *See* DELOITTE INSIGHTS, EMBRACING THE BRI ECOSYSTEM IN 2018 8 (2018), https://www2.deloitte.com/content/dam/insights/us/articles/4406_Belt-and-road-initiative/4406_Embracing-the-BRI-ecosystem.pdf.

12. PROSPERITY, *supra* note 5, at 45 ("The Belt and Road Initiative draws inspiration from the ancient Silk Road and aims to help realise the shared dream of people worldwide for peace and development. Shining with the wisdom from the East, it is a plan that China offers the world for seeking commo prosperity and development.").

13. *China Focus: Risks on Belt & Road Loans Controllable*, XINHUA (May 11, 2017, 8:42:04 PM), http://www.xinhuanet.com/english/2017-05/11/c_136274899.htm.

tries.[14] This type of financing has sparked fears of governments falling into "debt-traps," which can threaten national sovereignty.[15] Low-income, debt-distressed countries participating in the BRI are the most vulnerable to this danger.[16] To help fill the financing gap, countries have used Public-Private Partnerships (PPPs) for developing BRI projects.[17] There are many different forms of PPP models, and the type ultimately chosen will determine the scope of private sector participation and how risk will be allocated between the private and public sector.[18]

The Build-Operate-Transfer (BOT) model has become particularly popular for financing PPP project development.[19] When developing a PPP project under a BOT, the public authority will grant a concession right to a private sector entity, or project sponsor, to develop an infrastructure facility; this sponsor will also be responsible for financing, building, and operating the facility for a specified period.[20] By the end of this period, the project should have generated enough profits to cover project costs, repayment of debt principal, and promised return on

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14. *Id.*

15. Nathaniel Taplin, *One Belt, One Road, and a Lot of Debt*, WALL ST. J. (May 2, 2019, 5:33 AM), https://www.wsj.com/articles/one-belt-one-road-and-a-lot-of-debt-11556789446; Helen Davidson, *Warning Sounded Over China's 'Debtbook Diplomacy,'* GUARDIAN (May 15, 2018), https://www.theguardian.com/world/2018/may/15/warning-sounded-over-chinas-debtbook-diplomacy (explaining that a debt-trap scenario is when a state has made an initial financial commitment but then the project fails to generate sufficient profit to meet debt servicing needs, causing the state's government to take out additional loans and creating a vicious cycle that ultimately ends in the state relinquishing ownership of strategic economic assets).

16. John Hurley et al., *Examining the Debt Implications of the Belt and Road Initiative from a Policy Perspective*, 1, 3 (Ctr. for Global Dev., CGD Policy Paper 121, Mar. 2018), https://www.cgdev.org/sites/default/files/ examining-debt-implications-belt-and-road-initiative-policy-perspective.pdf.

17. EMBRACING THE BRI ECOSYSTEM IN 2018, *supra* note 11, at 19.

18. Public-Private-Partnership Legal Resource Center, *PPP Arrangements/Types of Public-Private Partnership Agreements*, WORLD BANK GROUP, https://ppp.worldbank.org/public-private-partnership/agreements (last updated Sept. 12, 2019).

19. Alan Woolston, *One Belt, One Road – addressing legal challenges to harness global opportunity in the rail sector* LEXOLOGY (Nov. 11, 2015), http://lexology.com/library/detail.aspx?g=0f79ffe3-8e1c-4c61-b934-5d0abaad4707.

20. Public-Private-Partnership Legal Resource Center, *Concessions, Build-Operate-Transfer (BOT) and Design-Build-Operate (DBO) Projects,* WORLD BANK GROUP, https://ppp.worldbank.org/public-private-partnership/agreements/concessions-bots-dbos (last updated Feb. 2, 2018).

investor equity; after which, the infrastructure facility is then transferred to the public authority free of charge.[21] The spirit behind this contracting model is to allow poorer states to gain an important infrastructure asset with little to no government spending.[22] In fact, China has actually encouraged the use of PPPs to help with BRI debt sustainability.[23] In 2018, however, BRI projects began to suffer problems resulting in delays in project performance or outright cancellation, exacerbating concerns surrounding Chinese debt-servicing.[24] In 2019, at the Belt and Road Forum, China attempted to assuage concerns, assuring that its BRI lending practices do not lead to sovereign debt distress.[25] Until China alters its debt management approach, however, there is little hope that concerns about BRI debt sustainability will fade away.[26]

The BRI, however, presents a novel challenge to the BOT model; mainly, the high level of connectivity between and integration of BRI projects requires the project company to take on risk not contemplated by the BOT model.[27] The BOT model has traditionally been used to develop a discrete asset rather than a whole network of assets.[28] The BRI, however, is an initiative promoting the development of a network of infrastructure assets and, as a result of this level of integration, project-to-project risk becomes a latent danger within the BRI.[29] The relationship between risk and PPP project performance cannot be overstated as risk management has been noted to be a top Critical Success Factor (CSF) for BOT projects.[30] If this risk is not

21. *Id.*

22. David. A. Levy, *BOT and Public Procurement: A Conceptual Framework,* 7 IND. INT'L & COMP. L. REV. 95, 103 (1996).

23. *China to Promote PPP Model in Belt and Road Initiative*, XINHUA (Jan. 15, 2017, 5:43:40 PM), http://www.xinhuanet.com//english/2017-01/15/c_135983879.htm.

24. Intelligence Unit, *China's reboot of the Belt and Road Initiative*, ECONOMIST (Apr. 29, 2019), http://country.eiu.com/article.aspx?articleid=597952843&Country=China&topic=Politics.

25. *Id.*

26. Hurley et al., *supra* note 16, at 20.

27. Woolston, *supra* note 19.

28. *Concessions, Build-Operate-Transfer (BOT) and Design-Build-Operate (DBO) Projects*, *supra* note 20.

29. Woolston, *supra* note 19.

30. Khalid Al-Azemi, *Risk management for build, operate and transfer projects within Kuwait*, 57 (2012) (unpublished Ph.D. dissertation, Lughborough

properly allocated and managed, then BOT-type PPP projects will not be a viable alternative to debt financing provided by China.[31]

A proper PPP framework can help minimize project risk and facilitate the success of the BRI. PPP projects conducted without a PPP framework have failed, such as the Dabhol Plant in Maharashtra, India.[32] The structure and quality of PPP frameworks, however, may largely depend on the development of domestic law.[33] Unfortunately, PPP-related domestic laws along the BRI lack uniformity, which might explain the disparity in the quality of PPP frameworks.[34] If stronger and more consistent domestic laws facilitating the development of PPP projects along the BRI are adopted, then it might lead to increased parity amongst PPP frameworks. The development of appropriate PPP frameworks could help mitigate the systemic project-to-project risk within the BRI. As a result, use of PPPs, particularly BOT, should become the more attractive option than the debt financing options currently available. Enabling BRI countries to be more flexible with project financing could help with BRI debt sustainability, and promoting more uni-

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University), *available at* https://pdfs.semanticscholar.org/e941/a9e5d68be414370700761acb20be9d501462.pdf.

31. EMBRACING THE BRI ECOSYSTEM IN 2018, *supra* note 11, at 9.

32. APMG, CHAPTER 2: ESTABLISHING A PPP FRAMEWORK, IN THE APMG PUBLIC-PRIVATE PARTNERSHIP (PPP) CERTIFICATION GUIDE 9–10 (2016), https://ppp-certification.com/sites/www.ppp-certification.com/files/documents/Chapter%202%20-%20Establishing%20a%20PPP%20Framework%20-%20Final%20-%20v1%203.pdf (The Dabhol Plant had many issues in its development, including the absence of a plan during project identification and not having a competitive process for choosing the private sector partner. These issues most likely would not have occurred if there had been an effective PPP framework in place to ensure that project development would be a well-planned, competitive process). *Dabhol Power Plant, Ratnagiri District, Mahashtra, India*, POWER-TECHNOLOGY, https://www.power-technology.com/projects/dabhol-combined-cycle-power-plant-maharashtra-india/ (last visited March 26, 2020) ("Dabhol Power Plant is a 1,967MW combined cycle power station located 160km south of Mumbai in the Ratnagiri District of Mahashtra, India.").

33. APMG, CHAPTER 1: PPP - INTRODUCTION AND OVERVIEW, IN THE APMG PUBLIC-PRIVATE PARTNERSHIP (PPP) CERTIFICATION GUIDE 15 (2016), https://ppp-certification.com/sites/www.ppp-certification.com/files/documents/Chapter%201%20-%20PPP%20Introduction%20and%20Overview%20v1.5.pdf.

34. EVALUATING THE ENVIRONMENT FOR PUBLIC-PRIVATE PARTNERSHIPS IN ASIA, ECONOMIST 11–12 (2018), https://infrascope.eiu.com/wp-content/uploads/2019/02/EIU_Asia-Infrascope-2018_final-report.pdf.

formity would also be consistent with a major priority of China's for the BRI; namely, policy coordination.[35]

Part I of this Note will provide background information on the BRI, including the economic, political, and social factors contributing to its rise. Part II will discuss issues surrounding the financing of BRI projects, including the dangers involved with sovereign debt financing and when to use PPPs as an alternative model for project financing. Part III will discuss challenges encountered when developing BRI projects under the BOT, specifically project-to-project risk. Finally, Part IV will propose suggested approaches to achieve a more uniform PPP framework to help address the project-to-project risk threatening the BRI.

I. HISTORICAL BACKGROUND ON THE SILK ROAD

Familiarity with the historical background of the Silk Road will help provide the necessary context to not only understand the motivation behind the BRI but also its geographical scope. This part will examine the Silk Road's historical origins and its impact on the development of culture and trade in Asia. It will also examine how the history behind the Silk Road led to one of the most ambitious infrastructure project initiatives ever, even larger than the Marshall Plan.[36]

A. Connecting the East and the West

The Silk Road was arguably one of the most important factors to the development of culture and commerce throughout Asia.[37] Silk and other goods would travel from China to Rome

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35. NDRC, *supra* note 4.

36. Sophia Yan, *China's Ambition Dealt Blow Ahead of G20 as Tanzania and Kenya Projects Grind to Halt*, TELEGRAPH (June 27, 2019), https://www.telegraph.co.uk/news/2019/06/27/tanzania-suspends-10-billion-port-project-new-blow-chinas-belt/; Dylan Gerstel, *It's a (Debt) Trap! Managing China-IMF Cooperation Across the Belt and Road*, NEW PERSP. IN FOREIGN POL'Y (CSIS) (Fall 2018), https://www.csis.org/npfp/its-debt-trap-managing-china-imf-cooperation-across-belt-and-road. The Marshall Plan was a post–World War II comprehensive aid program passed by Congress in 1948 to help rebuild a war-ravaged Western Europe. *Marshall Plan, 1948*, Office of the Historian, US DEP'T OF STATE, https://history.state.gov/milestones/1945-1952/marshall-plan (last visited April 19, 2020).

37. Perez, *supra* note 2. The ancient Silk Road was more than just a trade route as "[n]ot only products traveled along the Silk Road, but ideas too: convulsions in human thought and faith that reshaped the world. Buddhism,

along this ancient commercial corridor.[38] Systems of faith, such as Christianity, Buddhism, and Islam, also flowed across the Silk Road, developing along the way.[39] This vital trade route, however, did not share the same illustrious conception as did the BRI.[40]

Initially, ancient China was not keen on selling its silk to the outside world.[41] This policy changed when circumstances forced China's hand, particularly the relentless attacks of the Xiongnu nomadic tribes during the Qin[42] and Han[43] dynasties.[44] Today, most know the Xiongnu as the Hun, whose continuous attacks on China prompted Emperor Qin Shi Huang[45] to build and consolidate the Great Wall of China.[46] Over time, such efforts ultimately proved ineffective against the Xiongnu, and the Chinese military found itself at a disadvantage against their superior cavalry on the battlefield.[47] In 138 BC, realizing the gravity of the situation and desperate to protect border farming communities, Han Emperor Wu[48] attempted to reach out to the

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Christianity, and Islam would all travel along these paths and touch cultures along the way, shaping people's beliefs and philosophies over time." *Id.* This helps illustrate the importance the Silk Road had on the history of Asia.

38. *Id.*

39. *Id.*

40. *Id.*

41. *Id.*

42. The Qin Dynasty united ancient China and instituted a form of centralized bureaucratic government that was to characterize the regime style of future Chinese dynasties. PATRICIA BUCKLEY EBREY, THE CAMBRIDGE ILLUSTRATED HISTORY OF CHINA 60 (2d Ed. 2010).

43. The Han Dynasty took control of China immediately following the fall of the Qin Dynasty. *Id.* at 63–64.

44. *See* Nicola Di Cosmo, *Ancient Inner Asian Nomads: Their Economic Basis and Its Significance in Chinese History*, 53 J. ASIAN STUD. 1092, 1093 (1994) (the rise of the Xiongnu empire among the nomadic peoples of Inner Asia was primarily "a response to the unification of China and as a way to 'force the Chinese to deliver for political reasons what they were unwilling to sell for an inadequate economic gain.'").

45. *See* Carrie Gracie, *Qin Shi Huang: The Ruthless Emperor who Burned Books*, BBC (Oct. 15, 2012), https://www.bbc.com/news/magazine-19922863.

46. Perez, *supra* note 2.

47. *Id.*

48. *See* David Wu, *Emperor Wu of Han: Deemed Greatest Emperor in the Han Dynasty*, EPOCH TIMES (Sept. 5, 2013), https://www.theepochtimes.com/emperor-wu-of-han-deemed-greatest-emperor-of-the-han-dynasty_278724.html (explaining who Han Emperor Wu was).

Yuezhi,[49] another Central Asian tribe in a state of conflict with the Xiongnu.[50] These efforts culminated in Emperor Wu dispatching a convoy, under the leadership of famed Chinese military officer Zhang Qian, to establish diplomatic contact with the Yuezhi.[51] The mission did not go smoothly for Zhang Qian as he was captured by the Xiongnu before reaching the Yuezhi, forced to spend over a decade travelling the lands west of China as their prisoner.[52] Through these travels, Zhang Qian gained knowledge of the West that ultimately laid the foundation for the creation of the ancient Silk Road trade route.[53]

The name "Silk Road" is in fact a misnomer; the ancient trade corridor was actually comprised of multiple commercial routes.[54] As trade developed, the Silk Road expanded to include maritime routes, which started in East Asia, traveled through Southeast Asia by way of the Indian Ocean, and finally reached the Indian subcontinent, the African continent, and the Near East.[55] Trade by sea allowed markets along the Silk Road to obtain exotic spices, including "cinnamon, pepper, ginger, cloves and nutmeg."[56] Branching into maritime trade was such an important development for the Silk Road that these routes were coined the "Spice Routes" or "Spice Roads."[57]

B. The Decline of the Silk Road

After Mongolian control of China began to crumble in the fifteenth century, the Silk Road entered into a period of decline due to the absence of a single, unified regime.[58] Without such a regime, monitoring and securing areas of the overland portions of the Silk Road that ensure safe travel for merchants became

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49. *See* Di Cosmo, *supra* note 44, at 1112 (explaining that Yuezhi were an ancient nomadic peoples that were also in a state of conflict with the Xiongnu).

50. Perez, *supra* note 2.

51. David Christian, *Silk Roads or Steppe? The Silk Roads in World History*, 11 J. WORLD HIST. 1, 18 (2000); *see also* Perez, *supra* note 2.

52. Perez, *supra* note 2.

53. *Id.*

54. *About the Silk Road*, *supra* note 1.

55. *Id.*

56. *Id.*

57. *Id.*

58. *The Silk Road: A Larger View*, ASIA SOC'Y, http://sites.asiasociety.org/arts/monksandmerchants/silk.htm (last visited Apr.19, 2020).

all but impossible.[59] Such heightened risks ultimately became untenable for traders, especially after shipping technology advanced to the point where maritime trade became the faster and safer option.[60]

In 1453, the Turks captured Constantinople, signaling the end of the Byzantine Empire[61] and dealing an economic blow to the West.[62] With the fall of Constantinople, Europeans lost access to the western portion of the Silk Road.[63] Around this time, however, Europe had already begun exploring trade routes by sea to reach the East, ushering in the era of European exploration and colonization, as well as drawing the curtain on the ancient overland Silk Road.[64] The majesty and mystique of the ancient Silk Road, which took centuries to cultivate, unfortunately remain primarily through writings, such as those of Marco Polo.[65]

59. *See* Christian, *supra* note 51, at 6. During its period of decline, the importance of the Silk Roads fluctuated "partly as a function of the degree of stability to be found in the borderlands between the steppes and the agrarian civilizations of China, India, Iran, and Mesopotamia, and partly as a result of economic and political conditions in the major regions of agrarian civilization." *Id.* When agrarian civilizations controlled large sections of the Silk Road, travel was safer and less costly creating incentives for merchants to utlilize the ancient trade route; and when the Mongolian empire collapsed, so did the agrarian civilizations in Asia contributing to the decline in the amount of merchants who were willing to travel along the Silk Road.

60. *Id*.

61. LAWTON, *supra* note 1, at 15 ("[Constantinople] became the capital of the Roman Empire when Constantine, the empires first Christian emperor, moved his court there in A.D. 330 to escape decadent Rome.").

62. *See* Christian, *supra* note 51, at 6.

63. *Id*.

64. *Id*.

65. Even to this day, there is still an intense academic debate among historians about whether Marco Polo ever actually reached China. *Compare* Nick Squires, *Explorer Marco Polo 'Never Actually Went to China'*, TELEGRAPH (Aug. 9, 2011), https://www.telegraph.co.uk/news/worldnews/europe/8691111/Explorer-Marco-Polo-never-actually-went-to-China.html (explaining that evidence indicates Marco Polo was never in China), *with* Jennie Cohen, *Marco Polo Went to China After All, Study Suggests*, HIST. (Aug. 31, 2018), https://www.history.com/news/marco-polo-went-to-china-after-all-study-suggests (explaining that a German researcher has evaluated evidence that suggest Marco Polo did in fact travel to China).

C. Current Status of the Silk Road

In 2013, President Xi Jinping announced the BRI, initially called the One Belt One Road, to revitalize the all but forgotten ancient Silk Road back to its former glory.[66] The geographical scope of the BRI parallels that of its predecessor, including overland economic corridors and maritime trade routes throughout Asia.[67] In 2017, the BRI was formally adopted under China's Party Constitution during the nineteenth National Party Congress.[68] The objective of the BRI is to help China further strengthen its economic and diplomatic ties with countries not only along the original Silk Road route but also with the rest of the world.[69] This ambitious initiative hopes to revitalize the Silk Road and expand it to new regions.[70] The Chinese government has stated that this initiative is aligned with the Five Principles of Peaceful Coexistence:[71] "mutual respect for each other's sovereignty and territorial integrity, mutual non-aggression, mutual non-interference in each other's internal affairs, equality and mutual benefit, and peaceful coexistence."[72]

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66. PROSPERITY, *supra* note 5, at 45.

67. DANIEL R. RUSSEL & BLAKE BERGER, REPORT: NAVIGATING THE BELT AND ROAD INITIATIVE, ASIA SOC'Y POL'Y INST. 7 (June 2019), https://asiasociety.org/sites/default/files/2019-06/Navigating%20the%20Belt%20and%20Road%20Initiative_2.pdf.

68. Depanjan Roy Chaudhury, *Xi Jinping's BRI Raises Risk of Debt Trap for 68 Nations: US Experts*, ECON. TIMES (Mar. 14, 2018), https://economictimes.indiatimes.com/news/international/business/xi-jinpings-bri-raises-risk-of-debt-trap-for-68-nations-us-experts/printarticle/63293814.cms; *see* Katie Hunt, *China's 19th Party Congress: What You Need to Know,* CNN (Oct. 17, 2017), https://www.cnn.com/2017/10/17/asia/china-party-congress-what-you-need-to-know/index.html ("This twice-a-decade meeting is akin to a closed-door election, and will see President Xi formally granted a second-five-year term as the party's general secretary and a new generation of senior leaders anointed.").

69. NDRC, *supra* note 4.

70. *Id*.

71. *See* Ankit Panda, *Reflecting on China's Five Principles, 60 Years Later,* DIPLOMAT (June 26, 2014), https://thediplomat.com/2014/06/reflecting-on-chinas-five-principles-60-years-later/ ("The Five Principles, a major pillar in China's foreign policy even today, were originally conceived by India's first prime minister, Jawaharlal Nehru, and China's first premier, Zhou Enlai, in 1954. The principles rose to fame at the Bandung Conference in 1955, which set the stage for the Non-Aligned Movement.").

72. NDRC, *supra* note 4.

The BRI will set out to improve regional infrastructure, enhance trade, and facilitate private sector investment.[73] To accomplish these objectives, a high level of cooperation among BRI countries will be required.[74] China has urged that this cooperation should be structured around the following major goals: "[countries] should promote policy coordination, facilities connectivity, unimpeded trade, financial integration and people-to-people bonds."[75] Most notably, China has emphasized the importance of intergovernmental cooperation along the BRI to help facilitate the coordination of project development.[76] With respect to creating a coordinated development strategy and policy framework, China has encouraged engaging with international organizations, including the Asia-Pacific Economic Cooperation (APEC) and the Conference on Interaction and Confidence-Building Measures in Asia (CICA), among others.[77] These international organizations could also help settle project disputes along the BRI and facilitate private sector interest in the initiative.[78]

President Xi's BRI aims at revitalizing its predecessor, the ancient Silk Road, with respect to more than just improving the economic conditions of participating countries, such as providing much needed infrastructure development and coordination.[79] Some of the alleged goals include promoting integration and further interconnectivity on both policy and societal levels.[80] To accomplish these goals, the Chinese government has even encouraged engaging with international multilateral entities.[81] With respect to financing the BRI, however, China has not followed its own advice because it has failed to adequately engage with these entities, especially with respect to its credit lending practices along the BRI.[82] As discussed in the following section, this type of behavior on the part of China's government not only undermines the spirit upon which the BRI

73. *Id.*
74. *Id.*
75. *Id.*
76. *Id.*
77. *Id.*
78. *Id.*
79. *Id.*
80. *Id.*
81. *Id.*
82. Hurley et al., *supra* note 16, at 19.

was launched, but may also threaten the overall financial viability of the initiative.[83]

II. FUNDING THE BELT AND ROAD INITIATIVE

This part will examine the different flavors of financing available for BRI projects. Understanding the benefits and tradeoffs of the varying potential financing strategies will provide insight into the current problems plaguing the BRI.[84] Current BRI project funding mainly takes the form of debt financing from Chinese banks and not through multilateral development banks.[85] Even though this type of financing is readily available and initially offered at cheap rates, it can create problems down the road beyond just leaving a finance gap to fill.[86] As discussed below, the PPP model for project development could serve as a sound alternative to China's opaque credit-lending practices.[87]

A. Current BRI Debt Financing and its Dangers

To fund the BRI, the Chinese government has supplied large quantities of capital at very low interest rates to Chinese public financial institutions, such as the Chinese Development Bank (CDB) and the Export-Import Bank of China (EXIM).[88] The availability of affordable credit has allowed these financial institutions to lend cheaply to companies working on BRI infrastructure projects.[89] Most of this financing ultimately goes to Chinese firms, as more than "60% of Chinese-funded projects have been awarded to Chinese firms, compared to only 30% in BRI projects funded by non-Chinese financial institutions."[90]

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83. *Id.*

84. *China's OBOR expectations look gloomy: Expert*, ECON. TIMES (Jan. 4, 2019), https://economictimes.indiatimes.com/news/defence/chinas-obor-expectations-look-gloomy-expert/articleshow/67377396.cms.

85. China Power Team, *How will the Belt and Road Initiative advance China's interests?*, CHINA POWER (Oct. 18, 2019), https://chinapower.csis.org/china-belt-and-road-initiative/.

86. *Id.*

87. *China to Promote PPP Model in Belt and Road Initiative*, *supra* note 23.

88. *Id.*

89. *Id.*

90. Tania Ghossein, Bernard Hoekman & Anirudh Shingal, *Public Procurement in the Belt and Road Initiative*, WORLD BANK BLOGS: THE TRADE

By 2018, China had already invested over $1 trillion, mainly in the form of commercial loans.[91] This form of financing, however, has raised serious concerns regarding debt sustainability within the BRI.[92] The International Monetary Fund (IMF) has expressed concern that the high levels of lending to countries with heavy debt burdens threaten the viability of the BRI. [93] China's central bank governor, Zhou Xiaochuan, has even warned that such a large reliance on cheap loans will lead to "'risks and problems[,]' starting with moral hazard and unsustainability."[94]

Additionally, BRI infrastructure loans are primarily negotiated government-to-government.[95] This particular type of bilateral lending behavior has led to a lack of transparency for BRI project financing, exacerbating concerns over regional debt sustainability.[96] This poses a problem for vulnerable debt distressed low-income countries along the BRI, including Djibouti, the Maldives, Laos, Montenegro, Mongolia, Tajikistan, and Pakistan.[97]

Moreover, there is a fear among BRI countries regarding China's method of dealing with debt claims. Specifically, in 2017, Sri Lanka could no longer service its public debt as a result of participating in the BRI, and, as a result, the government of Sri Lanka relinquished an important port to China in the form of a debt-for-equity swap and 99-year lease.[98] When

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POST (Dec. 20, 2018), http://blogs.worldbank.org/trade/public-procurement-belt-and-road-initiative.

91. Gerstel, *supra* note 36, at 3.

92. *Id*.

93. Charles Clover, *IMF's Lagarde warns over debt on China's Belt and Road*, FIN. TIMES (Apr. 11, 2018), https://www.ft.com/content/7b7f9db2-3dec-11e8-b7e0-52972418fec4.

94. Shu Zhang & Matthew Miller, *Behind China's Silk Road Vision: Cheap Funds, Heavy Debt, Growing Risk*, REUTERS (May 15, 2017), https://www.reuters.com/article/us-china-silkroad-finance-idUSKCN18B0YS.

95. *Id*.

96. Hurley et al., *supra* note 16.

97. *Id*.

98. Kai Schultz, *Sri Lanka, Struggling With Debt, Hands a Major Port to China*, N.Y. TIMES (Dec. 12, 2017), https://www.nytimes.com/2017/12/12/world/asia/sri-lanka-china-port.html?_r=0; Maria Adele Carrai, *China's Malleable Sovereignty Along the Belt and Road Initiative: The Case of the 99-Year Lease of Hambantota Port,* 51 N.Y.U. J. INT'L L. & POL. 1061, 1083 (2019). China structured the lease agreement as a 99-year renwable lease "which are common in international investment contracts on land and natural resources

the lessee government represents a more powerful country than the lessor's government, this type of lease agreement is likely to raise national sovereignty concerns in that the lessor government will be unable to enforce its eviction rights if the lessee government refuses to leave.[99] Fears surrounding Chinese lending practices have been exacerbated due to China managing debt claims primarily on a case-by-case basis instead of adopting a multilateral approach,[100] such as engaging with the Paris Club.[101]

Additionally, the effects of debt instability will be far more reaching than just the success or failure of the BRI. Developing countries rely on infrastructure development as a way to lift themselves out of poverty, and public borrowing is the primary means of financing such projects.[102] If there is not sufficient economic growth and revenue generation from infrastructure projects to service the debt, it generally leads to a decline in domestic spending, particularly for social services.[103] Unfortunately, to escape such a predicament, governments usually take out additional loans as a way to service their public debt, which only serves to exacerbate the issue.[104]

B. Public-Private-Partnerships as an Alternative to Current Debt Financing Options

Debt sustainability levels vary along the BRI, forcing some governments to allocate a substantial amount of public funds to service national debt, which can result in a lack of necessary funding for vital infrastructure projects.[105] For example, when

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and follow nineteenth-century's common law, where a 99-year lease was the longest possible duration for a lease of real property." *Id.*

99. *Id.*

100. Hurley et al., *supra* note 16.

101. MARTIN A. WEISS, U.S. CONG. RESEARCH SERV., THE PARIS CLUB AND INTERNATIONAL DEBT RELIEF (2013) https://fas.org/sgp/crs/misc/RS21482.pdf ("The Paris Club is a voluntary, informal group of creditor nations who meet approximately 10 times a year, to provide debt relief to developing countries. Members of the Paris Club agree to renegotiate and/or reduce official debt owed to them on a case-by-case basis.").

102. Hurley et al., *supra* note 16, at 3.

103. *Id.*

104. *Id.*

105. JOSHUA YAU, CHINESE OUTBOUND FUNDING 5 (PwC Strategy 2015), https://www.pwc.com/gx/en/growth-markets-center/assets/pdf/china-new-silk-route.pdf.

oil prices were low in 2015, Russia experienced budget deficits resulting in its diminished ability to properly finance infrastructure projects.[106] Consequently, the majority of financing that Russia required to accomplish BRI projects came in the form PPPs.[107] Fluctuations in commodity prices have also affected the ability of other countries along the BRI to finance infrastructure projects.[108]

Realizing the financial flexibility PPPs offer, China has begun to publicly encourage this financing model for developing BRI projects.[109] Financial flexibility is crucial for debt distressed countries trying to avoid a default on their sovereign debt.[110] Debt distress is usually defined as the threshold reached where public indebtedness becomes too high and economic growth declines to such a degree that it leads to default.[111] Default usually occurs in countries with a rising debt-to-GDP ratio beyond 50 to 60 percent.[112]

Within the BRI, there are several countries identified as having severe debt sustainability problems: Pakistan, Djibouti, the Maldives, Laos, Mongolia, Montenegro, Tajikistan, and Kyrgyzstan.[113] The actions of these countries have indicated that they can no longer properly service their current debt levels.[114] For example, it is projected that Pakistan has an estimated $62 billion in additional debt due to Chinese loans used to finance the China-Pakistan Economic Corridor (CPEC) section of the BRI, which has sparked concerns about debt sustainability.[115] Pakistan, unable to properly manage its public debt, has announced its plans to approach the IMF for a multi-billion dollar bailout.[116] It is clear that Chinese lending along the BRI, especially for debt-distressed countries, can lead to a debt sustainability crisis.

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106. *Id.* at 8.
107. *Id.* at 10.
108. *Id.* at 11.
109. *China to Promote PPP Model in Belt and Road Initiative*, *supra* note 23.
110. Hurley et al., *supra* note 16.
111. *Id.* at 3.
112. *Id.* at 11.
113. *Id.*
114. *Id.* at 16–19.
115. *Id.*
116. Gerstel, *supra* note 36.

Within the context of the BRI, a debt sustainability crisis ending in a default can lead to a transfer of infrastructure asset ownership to China, leading to concerns in the international community that participation in the BRI will lead to a debt trap scenario.[117] The turnover of the port in Sri Lanka is the most glaring example of this concern.[118] Even if this is an exception and not the norm, China's bilateral lending practices and claims management process lacks transparency, which has fueled fears that China's BRI is actually a type of "debt trap diplomacy" in disguise.[119]

China has primarily taken a case-by-case approach to dealing with debt distressed countries unable to service their BRI loans.[120] Such an approach differs from those taken by other creditors who prefer to manage debt sustainability issues on a multilateral basis, such as through active participation in the Paris Club.[121] Beyond attending debt relief discussions and informal engagement with the IMF, China has yet to adopt a multilateral framework for debt management.[122] Without adopting a multilateral framework approach, and in the absence of membership to the Paris Club, it appears unlikely that China will change its ad hoc, case-by-case approach to managing BRI debt sustainability.[123] If China remains hesitant to engage with multilateral mechanisms to help manage BRI debt sustainability, then a robust PPP framework might serve as an appropriate alternative. In fact, it appears that China has recently promoted the use of PPPs in BRI project development, signaling a more PPP-focused strategy.[124]

III. OVERVIEW AND ANALYSIS OF PUBLIC-PRIVATE-PARTNERSHIPS

This section will provide a brief overview of PPP projects as well as an analysis of the development of PPP projects within the BRI. The development of a PPP project generally requires a

117. Taplin, *supra* note 15; *see also* Davidson, *supra* note 15.
118. Schultz, *supra* note 98.
119. Taplin, *supra* note 15.
120. Hurley et al., *supra* note 16, at 19.
121. *Id*.
122. *Id*.
123. *Id*.
124. *China to Promote PPP Model in Belt and Road Initiative*, *supra* note 23.

contractual agreement between a state's public authority and a private sector entity, or project sponsor, allowing for greater private sector involvement in project development.[125] Increased involvement by the private sector helps ensure adequate financing for project development.[126] Further, such a contractual agreement allocates risks and responsibilities between the parties with respect to the implementation and operation of the project, which is primarily dependent upon the expertise each party contributes to project development.[127] PPPs can serve a crucial role when a country's available funding falls far short of its infrastructure financing needs.[128] With the private sector bearing most of the financing risks, PPPs have become an attractive option for governments to develop infrastructure projects without incurring excessive debt.[129]

Recognizing the benefit of PPPs, many countries have already established the necessary legal framework and regulatory regime to facilitate their development.[130] In Asia, most developing countries have utilized PPPs to develop infrastructure projects.[131] With a few exceptions, however, many of these developing countries have not experienced considerable success in PPP development.[132] There are a few reasons for this lack of progress, including confusion about "private sector requirements and capacity constraints in the public sector, uncertainties in the administrative and approval processes, and unfavorable policy, legal and regulatory environment."[133]

The discussion of the previous section focused on the potential financing role the PPP model could serve within the BRI, but this section will discuss the mechanics of the PPP model for project development, particularly the popular BOT model. Analyzing the structural framework of PPPs will help show that even though the PPP project model is a viable alternative to

125. APMG, *supra* note 33, at 12–13.
126. *Id.*
127. TRANSP. & TOURISM DIV. UNESCAP, PUBLIC-PRIVATE PARTNERSHIPS IN INFRASTRUCTURE DEVELOPMENT, A PRIMER 1–2 (Feb. 2008), https://www.unescap.org/ttdw/ppp/ppp_primer/PPP_Primer.pdf.
128. *Id.*
129. *Id.*
130. *Id.* at 4.
131. *Id.* at 9.
132. *Id.*
133. *Id.*

debt financing, it is still subject to vulnerabilities within the BRI.

A. Advantages and Limitations of the Public-Private-Partnership

There are several advantages to using PPPs in infrastructure projects. Most obviously, it is a way for governments to develop important infrastructure without adding to public debt.[134] In developing a PPP, the private sector partner is responsible for project financing.[135] The private sector entity raises financing through "debt, equity, and government support."[136] The main source of equity comes from the private sector project sponsors, "including the contractors who will build and operate the project as well as financial institutions."[137] Sources of debt financing for the development of PPPs include lending by commercial banks and international financial institutions or directly from the capital markets by issuing bonds.[138] Debt financing usually provides the majority of needed funds for developing PPP projects, totaling about 70 to 90 percent of investment needs.[139] As for government support, this is primarily used to minimize risks that cannot be effectively managed by the private sector partner.[140] Government support is generally characterized by "public sector capital contributions, usually in the form of grants."[141] These grants can take the form of contingent support or guarantees by the public sector for the private sector partner, such as minimum revenue guarantees.[142]

Project development under a PPP model also removes the need for the host state's public authority to assign short-term

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134. *Id.*
135. APMG, *supra* note 33, at 61.
136. *Id.* at 173.
137. *Id.* at 174.
138. *Id.*
139. TRANSP. & TOURISM DIV. UNESCAP, *supra* note 127, at 48.
140. APMG, *supra* note 33, at 174–75.
141. *Id.* at 174.
142. *Id*; Ting Liu, *Minimum Revenue Guarantee Creates Value, but It's Not a Free Lunch*, STANFORD GLOBAL PROJECTS CENTER (Apr. 28, 2016), https://gpc.stanford.edu/gpcthinks/minimum-revenue-guarantee-creates-value-its-not-free-lunch ("By offering a[] [minimum revenue guarantee], the government agrees to compensate a PPP concessionaire if actual project revenue falls below the specified threshold, thus mitigating the revenue risk taken by the private sector.").

public funds to cover the costs associated with project development.[143] As a result, this prevents the need for governments to include project funds on their state's balance sheet.[144] The added financial flexibility this provides makes PPPs an attractive option for project development,[145] and the advantages of the PPP structure can be crucial when creditors are not interested in lending directly to governments.[146]

Additionally, PPPs allow for more private sector involvement in large infrastructure projects, which can increase efficiencies in construction and operations.[147] For example, the private sector is generally more efficient than the public sector at management, maintenance, and operation of project development.[148] The private sector also is not constrained by short-term budget cycles like the public sector; therefore, private entities may be better at making long term investment decisions.[149]

Finally, through PPPs, governments can transfer many of the risks associated with large infrastructure projects to the contracting private entities.[150] Some examples of these risks include increased project expenses and insufficient revenue generation.[151] The ability to allocate most or all of the financial risks in developing infrastructure projects to the private sector "is the most important driver when the state looks at the advantages of PPP projects."[152] A developing nation burdened with high public debt levels and in desperate need of an updated infrastructure system for continued economic growth might consider choosing the PPP model route, particularly if it can successfully allocate a substantial amount of financial risk to the private sector partner.

There are limitations, however, to the use of the PPP structure for infrastructure project development. The PPP method is

143. APMG, supra note 33, at 62.
144. *Id.*
145. *Id.*
146. *Id.*
147. TRANSP. & TOURISM DIV. UNESCAP, *supra* note 126, at 1.
148. *Id.*
149. *Id.* at 2.
150. APMG, *supra* note 33, at 12–13.
151. *Id.*
152. Daniela Parvu & Cristina Voicu-Olteanu, *Advantages and Limitations of the Public Private Partnerships and the Possibility of Using Them in Romania*, 27 TRANSYLVANIAN REV. ADMIN. SCI. 189, 191 (2009).

an extremely complex process that can result in an increased risk of project failure.[153] This method of project financing is also vulnerable to transitions in governance.[154] After a government undergoes a change in political administrative control, for example, "new government administrations can perceive that they are only paying for an infrastructure project that generated political benefits to others (their predecessors)."[155] With that in mind, a future transition in a host government's administration could threaten the success of project development and operation, especially if the project is limiting the new administration's budget.[156]

Additionally, high transaction costs for both the public and private sectors are endemic to PPP projects.[157] The complexity of PPP project development typically leads to these higher costs, especially at the initial procurement phase.[158] To properly manage this type of risk, the project's capital size must be sufficiently large so that the efficiencies created by project operations outweigh any anticipated expenses.[159]

Furthermore, there is a moral hazard to the fiscal advantages that the PPP project method provides.[160] If PPP project financing is not adding to public debt, then there is a risk governments will not consider the long term fiscal effects of project implementation and development.[161] In a twist of irony, the consequences of ignoring these effects will in turn threaten the long-term debt sustainability of the host nation.[162] Therefore, if these vulnerabilities cannot be adequately addressed, then a project should not be developed as a PPP.[163]

Finally, for a PPP project to perform successfully there must be effective regulatory governance.[164] Many of the risks outlined above can be properly mitigated by a sound regulatory

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153. APMG, *supra* note 33, at 70.
154. *Id.*
155. *Id.*
156. *Id.*
157. *Id.*
158. *Id.*
159. *Id.*
160. *Id.* at 71.
161. *Id.*
162. *Id.*
163. *Id.*
164. TRANSP. & TOURISM DIV. UNESCAP, *supra* note 127, at 59–60.

regime.[165] To be effective, there must be laws and a policy framework in place that delegate necessary regulatory functions to an appropriate authority.[166] This regulatory authority would generally be responsible for protecting public interests, regulatory compliance, and tariff adjustments.[167] Whether or not the regulatory authority was assigned the correct responsibilities could impact project costs and performance.[168]

B. The Build-Operate-Transfer Model

One of the more prolific types of PPP models for project implementation in developing countries, particularly in Asia, is the BOT.[169] Under this model, the public sector grants a concession right to a private sector entity to develop and operate a facility for a fixed period of time, which can be decades.[170] There are also many variations of the BOT, including Build-Own-Operate-Transfer[171] and Rehabilitate-Own-Operate-Transfer.[172]

PPP project development has often taken the form of a BOT because it uses private sector financing.[173] In a BOT, the private sector concessionaire assumes the primary responsibility for project financing and operates the infrastructure project for a specified period of time, which can last decades.[174] For BOT projects, the initial step can go one of two ways: (1) the public authority of the host state will identify a need to develop an infrastructure project; or (2) the developer will approach the

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165. *Id.*
166. *Id.*
167. *Id.*
168. *Id.*
169. I*d. at* 25.
170. *Concessions, Build-Operate-Transfer (BOT) and Design-Build-Operate (DBO) Projects, supra* note 20.
171. *Build-Own-Operate-Transfer (BOOT)*, THOMSON REUTERS PRAC. L. GLOSSARY, https://uk.practicallaw.thomsonreuters.com/3-501-2256?transitionType=Default&contextData=(sc.Default)&firstPage=true&bhcp=1 (last visited Feb. 14, 2020) (build-Own-Operate-Transfer is "[a] project delivery mechanism in which a government entity grants to a private sector party the right to finance, design, construct, own and operate a project for a specified number of years.").
172. *Concessions, Build-Operate-Transfer (BOT) and Design-Build-Operate (DBO) Projects, supra* note 20.
173. TRANSP. & TOURISM DIV. UNESCAP, *supra* note 127, at 25.
174. *Id.*

host state and make an unsolicited proposal to develop a project.[175] Next, the private sector entity obtains a concession grant from the public authority to build and operate the project for a pre-determined amount of time before the asset is transferred to the host state.[176] During this concessionary period, the private sector entity expects to derive enough revenue to realize a profit for its investors.[177] This type of contracting model allows a host state, usually a developing country with limited financial resources and technological expertise, to develop an infrastructure facility without adding to public debt or losing complete regulatory control over project operation.[178]

Furthermore, the private sector entity will usually take the form of a special purpose vehicle whose ownership is allocated amongst contributing investors.[179] The corporate form provided for by the creation of the special purpose vehicle serves to house the capital structure, which maps out how the project will be financed.[180] The special purpose entity also serves as the focal point for contract creation necessary to develop the project, such as for project supplies and construction.[181] In this type of financing structure, there is generally no initial revenue stream from the project, which in turn can make creditors reluctant to lend unless project risks are reasonably allocated to the appropriate party.[182] Revenues, however, are ultimately obtained from a single offtake purchaser, such as a major utility company or a country's government, who contracts to purchase project output from the project company.[183] Offtake purchaser contracts typically include guarantees of minimum payment required by the offtake purchaser and conditions for operational performance.[184] Once project revenues cover project costs and investors realize a profit, the infrastructure asset is transferred back to the public sector.[185]

175. *Levy,* supra *note 22, at 102.*
176. *Id.*
177. *Id.*
178. *Id.*
179. *Id.*
180. *Id.*
181. *Id.*
182. *Id.*
183. *Id.*
184. *Id.*
185. *Id.*

The contractual structure of a BOT project will have a powerful impact on risk allocation amongst the parties.[186] Typically, before the contractual structure of a BOT can be properly developed, a special purpose vehicle will need to be created to serve as the project company, and it will be this special purpose vehicle that then enters into the various agreements for project development purposes.[187] These agreements generally include a concession and "offtake purchaser" agreement with the host government, investor shareholder agreements, credit-lending contracts, operational and maintenance contracts, construction contracts, and supply agreements.[188] This contractual structure also helps appropriately allocate the risk that the project company faces when building and operating a large infrastructure facility.

Moreover, the BOT is not limited to cash-strapped developing countries. Developed countries, such as Portugal, have also used BOT financing for project development.[189] PPP project development, in general, is not uncommon in other developed countries, including the United States and Great Britain.[190] For example, in 2016, the United States Department of Transportation[191] created the "Build America Bureau" to establish a PPP office dedicated to encouraging the use of PPP in the development of transportation projects.[192] The frequency of which project development has been financed under various PPP models in both developed and developing countries, including a wide range of political and regulatory capabilities, illustrates the flexibility PPP models can offer governments looking for alternative methods for project funding.

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186. *Id.*

187. *Id.*

188. *Id.*

189. Manual Protásio & Catarina Coimbra, *Portugal*, *in* PUB.-PRIV. PARTNERSHIP L. REV. 165 (Bruno Werneck & Mário Saadi eds., 5th ed. 2018).

190. Bruno Werneck & Mário Saadi, *Preface*, *in* PUB.-PRIV. PARTNERSHIP L. REV vii (Bruno Werneck & Mário Saadi eds., 5th ed. 2018).

191. *See U.S. Department of Transportation*, USA.GOV, https://www.usa.gov/federal-agencies/u-s-department-of-transportation (last visited Feb. 4, 2020).

192. WILLIAM J. MALLETT, CONG. RESEARCH SERV., PUBLIC PRIVATE PARTNERSHIPS (P3S) IN TRANSPORTATION 9 (2017), https://fas.org/sgp/crs/misc/R45010.pdfhttps://fas.org/sgp/crs/misc/R45010.pdf.

C. Critical Factors Leading to Successful BOT Projects

The BOT model and its many variations have helped fill project development financing gaps across a diverse spectrum of countries and project types.[193] Many factors impact the outcome of BOT projects; however, successful BOT projects have demonstrated that certain factors have a greater influence on successful project development and the private sector's willingness to participate.[194] These factors include, among others, political stability, project identification, government support, private sector financing, duration of concession period, and risk allocation.[195] For example, political instability has repeatedly caused delays, as well as cancellations, for several transportation and energy projects in Kazakhstan, Bangladesh, Myanmar, and Pakistan, among others.[196]

However, among these factors, one of the most critical is the existence of a favorable legislation in the host state.[197] Studies have shown that a firm PPP policy and regulatory framework are crucial to successful BOT project development.[198] From an investor standpoint, it is important to have an effective legal framework sufficient to protect private sector interests in project development.[199] A legal framework supported by a firm PPP policy and effective governance will help reassure investors, thus facilitating private investment.[200] Without a robust legal framework, contracts may not be effectively structured within the BOT project, which could possibly create dangerous inefficiencies, such as a diminished ability to properly allocate project risk.

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193. Levy, *supra* note 22, at 95–96.
194. Hassan Sharaffudin & Abdulla AL-Mutairi, *Success Factors for the Implantation of Build Operate Transfer (BOT) Projects in Kuwait,* 10 INT'L. J. OF BUSINESS 68, 74 (2015).
195. *Id.*
196. Ken Larson, *China's Belt and Road Initiative Five Years In,* STRATFOR WORLDVIEW (June 22, 2018, 09:00 GMT) https://worldview.stratfor.com/article/chinas-belt-and-road-initiative-five-years.
197. Sharaffudin & AL-Mutairi, *supra* note 198, at 71.
198. *Id.* at 70.
199. *Id.*
200. *Id.* at 72.

D. Interconnectivity Problems: Project-to-Project Risk

In order to be successful, large infrastructure projects typically require managing a series of complex interfaces between the public and private sector.[201] In stand-alone projects involving just one host state, the BOT model has proven effective at efficiently managing these interactions by consolidating responsibility under the authority of a single private entity, which is usually the concessions-granted project company.[202] The BRI, however, is not a stand-alone project in a single host state; rather, it is an integrated network of infrastructure projects spanning many countries over a large geographical area.[203]

With that in mind, the coordination now required by contracting parties to successfully develop a PPP project has expanded to include multiple projects in a series, creating project-to-project risk.[204] BOT and other similar PPP contracting models are not suited to deal with project-to-project risk because it is nearly impossible to manage such a largescale series of interactions under the auspices of a single private entity, especially given the breadth of the BRI.[205]

E. Regulatory Disparities Amongst BRI Countries

With over 125 countries participating in the BRI, there is an inevitable lack of uniformity among participants' domestic legal frameworks in supporting PPP project implementation and development.[206] These frameworks provide the requisite structure to support and guide project participants—ranging from government agencies to private lending institutions—through the complex process of PPP implementation and development.[207] According to The Economist's Infrascope study examining the regulatory performance of countries with respect to PPPs, there

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201. Woolston, *supra* note 19.

202. *Id.*

203. *Id.*

204. Project-to-project risk is not a term of art per se, but a useful description of the type of risk inherent when there is a series of interconnected infrastructure projects that each depend on the completion of other projects within the series in order to generate sufficient revenue to cover costs and meet debt servicing needs. *Id.*

205. Woolston, *supra* note 19

206. EVALUATING THE ENVIRONMENT FOR PUBLIC-PRIVATE PARTNERSHIPS IN ASIA, *supra* note 34.

207. APMG, *supra* note 32, at 8–9.

are disparities in regulatory performance in countries participating in the BRI.[208] For example, Thailand exhibited strong regulatory performance with respect to providing conditions facilitating successful PPP project development, scoring an eighty-seven out of one hundred, while Sri Lanka scored only a thirty out of one hundred.[209] Moreover, debt distressed countries along the BRI have generally scored lower in PPP regulatory performance, including Kazakhstan, Mongolia, Pakistan, and Tajikistan.[210] This study has shown that certain countries and regions along the BRI face more challenges in developing effective PPP regulations, especially in the areas of "contract transparency, protocols for renegotiations and unsolicited proposals, and overall government coordination."[211]

Furthermore, there are unfortunate consequences that flow from a lack of uniformity, exacerbating project-to-project risk. Policy barriers are a good example of such a consequence because they are a natural result of the disparity of legal frameworks between countries.[212] Policy barriers can have a serious impact on a wide range of BRI-related areas, such as foreign direct investment (FDI),[213] the crossing of borders, and the importing and exporting of materials necessary for project development.[214] As a result, BRI projects have faced delays increasing the risk of investor withdrawal and overall financial loss.[215]

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208. EVALUATING THE ENVIRONMENT FOR PUBLIC-PRIVATE PARTNERSHIPS IN ASIA, *supra* note 34.

209. *Id.*

210. *Id.*

211. *Id.*

212. Michele Ruta, *Three Opportunities and Three Risks of the Belt and Road Initiative,* WORLD BANK BLOGS: THE TRADE POST (May 4, 2018), https://blogs.worldbank.org/trade/three-opportunities-and-three-risks-belt-and-road-initiative.

213. *See Foreign Direct Investment,* CORNELL L. SCH. LEGAL INFO. INST., https://www.law.cornell.edu/wex/foreign_direct_investment (last visited April 13, 2020) (relaying the International Monetary Fund definition of foreign direct investment "as a 'cross-border investment' in which an investor that is 'resident in one economy [has] control or a significant degree of influence on the management of an enterprise that is resident in another economy.'").

214. Ruta, *supra* note 215.

215. *Id.*

IV. SUGGESTED APPROACHES

This section contemplates possible approaches that could help make PPPs a more attractive option for BRI project financing. The first approach suggests promoting the development of a unified PPP framework with a special focus on the BRI, which would ideally facilitate higher rates of successful project growth and reduce overall project-to-project risk. To complement the robust development of BRI-appropriate PPP frameworks, the second approach suggests establishing independent regulators to help control project risks that stem from disparities in governance capabilities along the BRI.

A. Encourage the Development of a BRI-Focused PPP Framework

A PPP framework can be defined as "the established procedures, rules and institutional responsibilities that determine how the government selects, implements and manages PPP projects."[216] An effective framework helps to identify what projects are appropriate for PPP development, as well as ensure that projects are conducted with transparency.[217] A sound framework can help mitigate project risk in the following ways: standardize the way government agencies implement PPPs to help reduce inefficiencies in project development; help manage the expectations of stakeholders to promote greater cooperation; increase the transparency of PPP projects to help attract higher levels of investor interest, creating a more competitive procurement process; and increase project oversight capabilities through the clear and efficient allocation of monitoring responsibilities.[218] Further, a successful PPP framework sets forth guidelines for PPP development procedures, project selection, and decision criteria, as well as what duties should be assigned to institutional entities.[219] There can be devastating consequences to developing a PPP project without a proper framework in place, as was witnessed with the unsuccessful Dabhol Plant project.[220]

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216. APMG, *supra* note 32, at 6.
217. *Id.*
218. *Id.*
219. *Id.*
220. *Id.*

The scope of such frameworks, however, will generally be limited by the jurisdiction of the government that promulgates them.[221] PPP frameworks generally vary country-by-country, which could potentially account for the disparities in regulatory governance and policy barriers that contribute to increased project-to-project risk. The scope of any such framework can be broken down into a few fundamental factors: jurisdiction, sector, project size, and contract type.[222] In Australia, for example, "[v]alue for Money considerations mean PPPs will likely only be applicable for projects over US$50 million."[223] Since many of the issues that arise during PPP project development are similar, some countries employ unified PPP frameworks cutting across multiple jurisdictions and sectors, as well as covering different project sizes and contract types.[224] These types of frameworks can offer the advantage of more cohesive guidelines for project development, resulting in greater efficiencies that should help attract private sector investment.[225]

There can be problems in the development of a unified framework, however, when the scope spans across various industries and multiple national boundaries, leading to a greater likelihood that there will be conflicting interests from project participants.[226] This would most likely be the case within the context of the BRI due to the initiative's immense size. A unified framework, however, can mitigate the likelihood of conflicts of interests by focusing on targeted problems, which should "limit the stakeholders involved and the legislative or policy frameworks that need to be addressed."[227] For example, when the Philippines adopted its first BOT-related framework in 1990, it became clear that the project procurement process provided for under the framework presented serious difficulties for the government to procure the necessary privately financed power generators.[228] In the subsequent years after adoption, the Philippines experienced a severe energy crisis.[229] In re-

221. *Id*.
222. *Id*.
223. *Id*. at 19.
224. *Id*. at 21.
225. *Id*.
226. *Id*.
227. *Id*. at 22.
228. *Id*.
229. *Id*.

sponse to the crisis, the Philippines overhauled the BOT framework to include a focus on "crisis mitigation and by 1994 there were no brownouts."[230]

Applying this to the BRI, if participating countries were to adopt an expansive unified framework spanning multiple regions and types of infrastructure development, then there could be more consistency in the quality of PPP regulation. Due to the expansive scope of the BRI, however, there is a potentially high likelihood of conflicting interests.[231] To avoid this leading to an anti-commons issue, any proposed BRI unified framework would need to target specific problems within the BRI.[232] For example, a BRI unified framework could target problems related to project delays, which may help to harmonize the interests of stakeholders in support of adopting a framework with such a broad scope. Specifically, the framework could focus on streamlining PPP identification and implementation procedures as this can be the most time-consuming, complex part of the process.[233] In addition to reducing the time and costs of project development, the effect of streamlining these particular stages would help to establish stronger procedural standards ensuring more consistency with PPP projects along the BRI. More consistency at such crucial stages could help reduce the amount of risk taken in PPP project development thereby facilitating greater levels of private sector investment.

Additionally, if the scope of a BRI unified framework proves too expansive to be addressed by targeting specific problems, then perhaps developing separate parallel frameworks for particular regions or sectors within the BRI could prove useful.[234] As a result of more uniformity, there should be a decrease in issues, such as policy barriers, that contribute to project delays. The need to have project interactions from all the participating countries consolidated under the auspices of one entity's roof should also subsequently decrease. The prospect of a decreased project-to-project risk should also help attract greater levels of private investment for BRI projects.

230. *Id.*
231. *Id.*
232. *Id.*
233. *Id.* at 8–9.
234. *Id.* at 22.

B. Establish Independent Regulators

To complement a BRI-wide PPP framework, countries should put into place independent regulators. Delegating authority to independent regulators would help mitigate risks involving inadequate or inconsistent regulatory governance, which if left unchecked could result in decreased foreign investment and project delay.[235] The implementation of independent regulators would also help assure private investors that project development and operation will not be affected by a change in political winds.[236] PPP project development is vulnerable to the effectiveness and consistency of regulatory governance, and the establishment of independent regulators would help ensure the stability of regulatory rules regardless of regime change.[237] The existence of autonomous independent regulators with the requisite authority and technical sophistication can have a positive influence on PPP development.[238] This is already the case in the Asia-Pacific region for certain sectors, such as energy, telecoms, and water.[239]

Furthermore, increased stability to regulatory governance along the BRI should help increase private sector investment. Sufficient PPP-focused regulatory power supported by adequate control and enforcement mechanisms is crucial to the development of PPP projects.[240] When a project is considered to face significant regulatory risks, "investors attach a high risk premium, which in turn results in high prices of the services."[241] With the establishment of an independent regulator to oversee PPP project development, the host state government can provide more certainty to private sector participants that "it will not be able to arbitrarily change any rules or intervene in the market after investments are made."[242] If this were the case for the BRI, then the private sector would likely feel safer investing more into the BRI because increased regulatory stability subsequently helps decrease project-to-project risk. Moreover, independent regulators may be better positioned to

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235. TRANSP. & TOURISM DIV. UNESCAP, *supra* note 127, at 59.
236. *Id.* at 61.
237. *Id.*
238. *Id.*
239. *Id.*
240. *Id.*
241. *Id.*
242. *Id.* at 62.

resist pressures from China's government to enter into negotiations that lead to the dreaded debt trap scenario. As a result, independent regulators could serve as a counterbalance against China's influence, which could help dispel concerns that the BRI will subject participating countries to China's alleged "debt trap diplomacy.".

CONCLUSION

The BRI is one of the most ambitious projects of the twenty-first century, providing a means for developing countries to gain much needed infrastructure, as well as increasing connectivity between cultures through the promotion of interstate commerce. This initiative has mainly been funded through commercial loans from China raising debt sustainability concerns, but PPPs may offer a viable financial alternative. Such an ambitious project, however, has its risks, specifically project-to-project interface risks that result from challenges in efficiently coordinating and consolidating project-to-project interactions.[243] This risk usually exhibits itself in the uncertainties that ripple through a series of interconnected projects when one project is delayed or prematurely terminated.[244] Among the participating countries, there is no uniform standard framework for developing PPP projects.[245] By encouraging the development of a BRI-wide PPP framework, as well as establishing independent regulators, there should be a decrease in the amount of project-to-project risk shared along the BRI making PPPs a more attractive project financing option.

Those developing PPP frameworks should carefully consider factors that affect the success of PPP projects, such as risk allocation and asset transfer rights.[246] Project-to-project risk should decrease with an increase in regulatory uniformity and stability along the BRI, which in turn may help to facilitate greater private sector investment and participation. Ultimately, these proposals would have an overall positive effect on the BRI by providing a better option than the debt financing model

243. Woolston, supra note 19.
244. *Id.*
245. EVALUATING THE ENVIRONMENT FOR PUBLIC-PRIVATE PARTNERSHIPS IN ASIA, *supra* note 34.
246. APMG, *supra* note 32, at 9.

currently haunted by the specter of the dreaded "debt trap" scenario.

*August Dinwiddie**

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