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# UNIDROIT/ICC Principles and Model Clauses for International Investment Contracts

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## LIST OF ABBREVIATIONS

| | |
|---|---|
| ALIC Guide | UNIDROIT-IFAD Legal Guide on Agricultural Land Investment Contracts (2021) |
| BIT | Bilateral Investment Treaty |
| CISG | UN Convention on Contracts for the International Sale of Goods |
| FIDIC | International Federation of Consulting Engineers |
| ICC | International Chamber of Commerce |
| IIA | International Investment Agreement |
| IIC | International investment contract |
| ISDS | Investor-State Dispute Settlement |
| MoU | Memorandum of Understanding |
| PRICL | Principles of Reinsurance Contract Law (2025) |
| UPICC | UNIDROIT Principles of International Commercial Contracts (2016) |
| UN | United Nations |

# INTRODUCTION

## A. Background and purpose

1. The development of international investment has been one of the driving features of the global economy over the past several decades. Foreign investment plays a vital role in contributing to economic development, generating employment, facilitating the transfer of technology, and providing other benefits to host States. At the same time, international investment projects often involve complex, long-term contractual arrangements between States (or State-related entities) and foreign investors, which present unique legal challenges that require specialised guidance.

2. International investment contracts (IICs) occupy a distinctive position in the landscape of transnational commercial relationships. These contracts typically concern projects of public interest or public purpose and frequently involve the exercise of public authority, the allocation of public resources, and sustained interaction between private investors and State officials. The public purpose element is generally reflected in the contract itself, for example through clauses advancing public policy goals such as sustainable investment. Moreover, IICs are typically long-term and high-value agreements, which necessitate particular attention to issues of stability, predictability, and the management of change over time.

3. The present Instrument was developed by UNIDROIT and the International Chamber of Commerce (ICC), through its Institute of World Business Law, in response to a recognised need for comprehensive, balanced, and internationally harmonised guidance on IICs. While instruments addressing international commercial contracts do exist – most notably, at the global level, the UNIDROIT Principles of International Commercial Contracts (UPICC) – and while a substantial body of international investment law has been developed through bilateral and multilateral investment treaties, there has been no comparable instrument providing tailored guidance specifically for investment contracts concluded directly between States (or State-related entities) and foreign investors. This Instrument aims to fill that gap by providing Principles and Model Clauses, both accompanied by detailed commentary, that address issues relevant to IICs.

4. The present Instrument is built upon and incorporates by reference the UPICC, as further explained in Section F below on the relationship between this Instrument and the UPICC.

5. Its purpose is to assist contracting parties – whether States, State enterprises, or investors – in negotiating, drafting, interpreting, and performing IICs in a manner that reflects contemporary best practices and achieves an appropriate balance between the legitimate interests of all stakeholders. The Instrument is also intended to serve as a resource for adjudicators called upon to resolve disputes arising from IICs, as well as for legislators and policymakers seeking guidance on normative frameworks for foreign investment.

6. The development of this Instrument takes place against the backdrop of a broader reconsideration of the general principles underpinning international investment law. The international investment regime, largely constructed through a dense network of bilateral investment treaties (BITs) and other international investment agreements (IIAs) concluded over the past several decades, is currently undergoing significant scrutiny and reform. Many of these treaties were negotiated in circumstances that have since evolved substantially – economically, politically, and in terms of the expectations placed upon both States and investors regarding human rights, environmental protection, and social and governance issues. Concerns have emerged that traditional investment treaty protections, while to some extent successful in attracting foreign capital, may in certain cases have unduly constrained States' regulatory freedom or created imbalances between investor rights and broader public interests.

7. This Instrument responds to these developments by seeking to ensure, through contractual mechanisms, a level of protection for investors that is functionally comparable to that traditionally provided by IIAs and BITs, while simultaneously reflecting the current state of debate on the appropriate balance between investment protection and other legitimate policy objectives.

8. By situating these protections within the framework of a contract – where obligations are negotiated, agreed upon by both parties, and enforceable through contractual remedies – the Instrument avoids the asymmetries that have sometimes characterised treaty-based investment protection, where investors enjoy rights without correlative obligations enforceable against them. In an IIC, by contrast, both the State (or State-related entity) and the investor assume contractual obligations, and both have access to contractual remedies in the event of non-performance.

9. At the same time, this Instrument embeds within the framework of IICs the modernisation efforts currently underway in international investment law, particularly with respect to the inclusion of principles on sustainability. Contemporary investment agreements increasingly incorporate provisions addressing issues such as environmental protection, labour standards, human rights, anti-corruption, and sustainable development in general. This Instrument draws upon and advances these developments, integrating sustainability considerations as a core element of the IIC framework rather than as an afterthought or optional addition. In doing so, it seeks to demonstrate that robust investor protection and meaningful sustainability commitments are not mutually exclusive, but can and should be pursued together in a balanced and coherent manner.

**B. Key features of international investment contracts**

10. An IIC is a contractual arrangement with contractual consequences between the parties. It is neither an IIA entered into between States, nor a treaty in any other form. This distinction is fundamental to understanding the scope and purpose of the present Instrument.

11. IICs possess certain characteristics that distinguish them from ordinary commercial contracts. On one side of the contractual relationship is a party connected to the State – whether the State itself, an organ or ministry of the State, a State enterprise, or another entity competent to enter into IICs on behalf of the State. On the other side is one or more foreign investors. This asymmetry between the parties and the potential for the exercise of sovereign power by the State party give rise to concerns not typically present in contracts between private parties.

12. IICs may take various forms, including concession contracts, joint venture agreements, share purchase agreements, construction contracts, and public-private partnerships. They may exist across diverse sectors – resource extraction, oil and gas, construction, telecommunications, water management, and electric power distribution, among others. Regardless of their specific form or sector, IICs share common features that justify specialised treatment: their long-term duration, their high value, their public-interest dimensions, and the involvement of parties with fundamentally different positions and powers.

13. Model clauses and standard contract forms to be used internationally exist in various sectors that may be relevant to IICs. In the construction sector, for example, organisations such as the International Federation of Consulting Engineers (FIDIC) have developed widely used standard contracts and model clauses that address matters such as delay damages, dispute adjudication boards, and other sector-specific concerns. These industry instruments serve an important purpose in standardising commercial practices within their respective sectors. While drawing upon these and other practices of specialised bodies, this Instrument proposes model clauses that specifically address the issues that arise from the fact that the

project constitutes an investment, and the particular concerns that flow from the involvement of a State (or State-related entity) as a contracting party.

14. The rationale of this Instrument differs fundamentally from that of industry-specific standard forms. While such instruments focus on the technical, commercial, and procedural aspects of projects as between employer and contractor, the present Instrument addresses the distinctive features of contracts that involve a foreign investor and a State party, and that typically concern matters of public interest and public purpose and have a systemic effect in the host State. These features include the potential exercise of sovereign authority by the State party, the long-term nature and high value of the investment, the public-interest dimensions of the project, and the need to balance investor protection with the State's regulatory freedom. The present Instrument complements rather than replaces sector-specific standard contracts: parties to an IIC in the construction sector, for example, may choose to incorporate relevant FIDIC provisions for technical and operational matters while also incorporating the present Principles to address investment-specific concerns.

15. A further matter that warrants clarification concerns the classification of certain contracts involving State parties as "administrative contracts" or "public contracts" under some domestic legal systems. In several jurisdictions, particularly those within the civil law tradition, contracts concluded by States or public entities for public purposes are subject to a distinct legal regime – often characterised by public-law rules that confer upon the State certain prerogatives not available to private contracting parties, such as the power to modify or terminate the contract unilaterally in the public interest. These public-law rules may also impose specific procedural requirements for contract formation, performance, and dispute resolution.

16. For purposes of this Instrument, the distinction between administrative contracts and private law contracts under domestic law is not determinative of the Instrument's applicability or operativity. This Instrument is designed to provide guidance on IICs regardless of how they may be classified under the domestic law of the host State. The Principles contained herein address matters that are relevant to all IICs – whether they are characterised as administrative contracts, public contracts, concession agreements, or ordinary commercial contracts under the applicable domestic law.

17. The consequence of this approach is twofold. First, this Instrument may be applied by contracting parties to inform the drafting and negotiation of their IIC, regardless of the contract's classification under domestic law. Second, when adjudicators – whether domestic courts, administrative tribunals, or arbitral tribunals – are called upon to interpret or apply an IIC, they may take this Instrument into account to interpret and supplement the applicable domestic law, including any public-law rules that may govern the contract by virtue of its classification as an administrative contract. The Instrument does not purport to displace mandatory rules of domestic law, including mandatory rules specific to administrative contracts, but it may serve to corroborate and inform the application of such rules in light of internationally accepted principles for investment contracting.

### C. State's regulatory freedom

18. One of the core issues that this Instrument seeks to address is the tension between the protection of the stability and predictability of the legal framework and the preservation of the State's sovereign right to regulate in the public interest. This tension has been at the centre of contemporary debates concerning international investment law and investor-State dispute settlement (ISDS) reform.

19. Investment protection cannot come at the cost of unduly constraining States' ability to adopt and modify regulations necessary to address evolving public needs. States must remain free to develop policies in areas such as human rights protection, environmental preservation, climate change mitigation, labour

standards, and public health – even where such measures may affect existing investments. The recognition of this principle is essential to maintaining the legitimacy of the international investment regime and to ensuring that investment serves broader developmental and societal goals.

20. The Model Preamble for IICs included in this Instrument reflects this balance: it specifies the goal of balancing the principle of *pacta sunt servanda* and the need to provide adequate protection to foreign investors through stability of contractual relations, on the one hand, with the freedom of States to adopt and change regulations, on the other. This balance finds expression throughout the Instrument, most notably in the provisions on stabilisation and renegotiation clauses in Chapter 6.

21. Stabilisation clauses in IICs have been subject to significant criticism for their potential to constrain the implementation by governments of measures addressing sustainability concerns. General freezing clauses, intangibility clauses, and allocation-of-burden clauses have been characterised as having a severe constraining effect on the regulatory freedom of States. In response, contemporary contract practice has been moving toward economic equilibrium clauses that encourage the maintenance of contractual stability through renegotiation mechanisms rather than through rigid prohibitions on regulatory change.

22. This Instrument reflects that evolution. Rather than endorsing freezing clauses, it suggests that States and investors (and particularly the State) consider whether it is appropriate to include stabilisation clauses, with full awareness of the consequences of such inclusion. Where the inclusion of a stabilisation clause is deemed appropriate, this Instrument provides alternatives – economic equilibrium clauses, fiscal stabilisation clauses, and hybrid approaches – that preserve essential investor protections while respecting the State's inherent authority to regulate in the public interest. Furthermore, the Instrument includes a carve-out provision excluding from the scope of stabilisation clauses measures adopted in good faith, on a non-discriminatory basis, and in the public interest to protect human rights and public health, the environment (including in relation to climate change), or labour standards.

23. By articulating investor protection through contractual mechanisms rather than through treaty-based standards such as that of fair and equitable treatment (FET, and the role of legitimate expectations), this Instrument provides a framework that is both more predictable and more responsive to the concerns that have animated contemporary debates on investment law reform. The scope of protection is defined by the contract; the mechanisms for addressing regulatory change are negotiated by the parties; and the remedies available are contractual in nature. This approach respects both the investor's need for stability and the State's sovereign prerogative to regulate in the public interest.

### D. Modernisation of investment law and "sustainable investment" contracts

24. As highlighted, the development of this Instrument reflects and contributes to broader efforts to modernise the international investment law framework. Over the past two decades, there has been a growing recognition that the traditional architecture of investment protection – focused primarily on the bilateral relationship between State and investor – fails to adequately account for the broader societal context in which investment projects operate. Investment projects, particularly those of significant scale and duration, inevitably affect a range of stakeholders beyond the contracting parties themselves, including local communities, workers, Indigenous peoples, and the environment.

25. This Instrument embraces the principle that sustainable investment must be at the core of modern investment contracting. Sustainability, as understood in this Instrument, encompasses human rights, environmental protection (including an important component on climate change), social responsibility, and good governance (including anti-corruption). It requires that investment projects not only generate economic returns for investors and benefits for host States, but also contribute positively – or at minimum

do no harm – to the communities and environments in which they operate. The Instrument reflects the understanding that long-term investment success depends upon maintaining a social licence to operate, which in turn requires attention to the interests of affected third parties.

26. A significant innovation of this Instrument is its treatment of the interests of third parties, particularly local communities. Traditional contract law, grounded in the principle of privity, generally does not recognise rights or obligations running to parties outside the contractual relationship. However, the public-interest dimensions of IICs, and the significant impact that investment projects may have on local populations, justify a departure from this traditional approach. This Instrument encourages and facilitates the incorporation of provisions that address the interests of local communities, including through mechanisms such as community benefit agreements, local content requirements, stakeholder consultation processes, and grievance mechanisms.

27. The consideration of third-party interests also extends to the protection of human rights. International standards such as the United Nations (UN) Guiding Principles on Business and Human Rights have established the expectation that business enterprises – including foreign investors – should respect human rights throughout their operations. This Instrument translates these expectations into contractual obligations by incorporating provisions on human rights due diligence, the prevention of adverse human rights impacts, and remediation where such impacts occur. By embedding human rights considerations within the contractual framework, the Instrument ensures that both contracting parties – State and investor – share responsibility for the human rights dimensions of the investment project.

28. Environmental protection constitutes another pillar of the modernisation agenda reflected in this Instrument. Climate change, biodiversity loss, and environmental degradation pose existential challenges that require urgent action at all levels, including in the context of international investment. The Instrument encourages the inclusion of environmental obligations in IICs, including commitments to environmental and social impact assessment, compliance with environmental standards, and contribution to climate change mitigation and adaptation. The carve-out provisions for environmental measures in the stabilisation clauses ensure that contractual commitments do not impede necessary environmental regulation.

29. The modernisation of investment contracts also encompasses governance concerns, including the fight against corruption. Corruption undermines the Rule of Law, distorts markets, and diverts resources from public purposes. This Instrument includes robust anti-corruption provisions that apply to both parties to the IIC, reflecting the shared responsibility of States and investors in combatting corrupt practices.

30. These considerations are reflected throughout the Instrument, including in the provisions on sustainable investment (Chapter 2), sustainability due diligence in the pre-contractual phase (Chapter 3), and shared investor-State obligations on sustainability (Chapter 5).

31. In sum, this Instrument seeks to position IICs as vehicles not merely for the protection of private investment but for the advancement of broader sustainable development objectives. By integrating sustainability into the core of the contractual framework, the Instrument reflects the contemporary understanding that investment must serve not only the interests of the contracting parties but also the broader public interest and the interests of affected third parties.

### E. Striking a balance between rights and obligations

32. A central objective of this Instrument is to strike an appropriate balance between the rights and obligations of both parties to an IIC. Investment contracts necessarily involve competing interests: the investor's interest in a stable and predictable legal environment, protection against expropriation, and the

ability to reap the economic rewards of its investment; and the State's interest in preserving regulatory authority, protecting the public interest, and ensuring that the investment contributes to sustainable development. As said, this Instrument acknowledges that development through international investment cannot be conceived of without taking into account the rising importance of sustainability – requiring the support of social, economic, and environmental benefits and notably protecting human rights, the environment, and the health and safety of people and workers, as well as sustaining good governance, local community development, and the fight against corruption. At the same time, the Instrument recognises that predictability and stability of the contractual relationship are essential for the successful completion of the contract, and that the obligations of the parties shall not be interpreted and applied in a manner that disrupts that predictability and stability.

33. The balancing of interests in an IIC operates according to a logic that is fundamentally different from that of investment treaty protection. Under an investment treaty, the investor benefits from standards of protection – such as FET, protection against expropriation, and the protection of legitimate expectations – that are defined by international law and applied by international tribunals, often without a corresponding set of obligations imposed on the investor. The scope and content of these standards are determined not by the parties' agreement but by the treaty text and its interpretation – often inconsistent – in arbitral case law, which can generate uncertainty. In a contractual framework, by contrast, the balance is expressed in the contract itself. In many IICs, this balance is the product of direct negotiation between the parties. They mutually agree on the scope of investor protection and safeguards for the State (e.g., to protect regulatory freedom) as well as both parties' obligations.

34. It must be acknowledged, however, that not all IICs are the result of freely negotiated agreements between parties of equal bargaining power. In a significant number of cases – particularly where the IIC takes the form of an administrative or public law contract, or where the contract is awarded through a competitive bidding or public tendering process – the terms of the contract are largely pre-determined by the State and offered to the investor on a take-it-or-leave-it basis, with limited or no scope for negotiation on core provisions. As noted elsewhere in this Introduction, the classification of a contract as an administrative or public contract under domestic law does not affect the applicability of the Principles contained in this Instrument. Nor does the manner of contract formation alter the fundamental logic of the contractual framework: regardless of how the terms of the IIC came into being, once the contract is concluded, both parties are bound by it and both have access to the remedies it provides.

35. In this context, the present Principles serve an additional and particularly important function: they represent internationally recognised best practices and standards that may guide the State in the design of its tender documents and contract templates, ensuring that even contracts concluded through non-negotiated procedures reflect a balanced allocation of rights and obligations. The investor, for its part, may rely on the Principles as a benchmark against which to assess the fairness of the terms offered and, where appropriate, to inform the interpretation and application of those terms by adjudicators.

36. Both the State and the investor assume contractual obligations, and both have access to contractual remedies in the event of non-performance. By articulating investor protection through contractual mechanisms rather than through treaty-based standards, this Instrument provides a framework that is both more predictable and more responsive to the concerns that have animated contemporary debates on investment law reform.

37. This contractual logic has direct implications for how the balance between the State's regulatory freedom and the investor's need for stability is achieved. The State must remain free to adopt and modify regulations necessary to address evolving public needs – in areas such as human rights protection and public health, environmental preservation, climate change mitigation, and labour standards – even where

such measures may affect existing investments. As said, this Instrument does not question that principle. At the same time, where the exercise of regulatory freedom disrupts the economic equilibrium of the contract, the investor is not left without recourse. The contractual framework provides the investor with remedies that are calibrated to restore the balance: renegotiation to achieve the economic equilibrium of the contract, fiscal stabilisation mechanisms that preserve the fiscal regime for the agreed duration, and, where those mechanisms fail, access to the dispute resolution procedure agreed in the IIC. The carve-out provision for measures adopted in good faith, on a non-discriminatory basis, and in the public interest for the protection of human rights, public health, the environment, climate change, or labour standards further ensures that the State's most essential regulatory prerogatives are not constrained by the stabilisation framework, while the investor retains its right to invoke other contractual remedies for non-performance.

38. Remedies, however, are not conceived solely for the benefit of the investor. The Instrument recognises that the State, too, must have effective contractual tools at its disposal. Where the investor fails to comply with its obligations – including sustainability obligations, construction milestones, or operational standards – the State may resort to a range of contractual remedies, from specific performance and the imposition of penalties, to the hiring of third parties at the defaulting party's expense, to the suspension or, ultimately, termination of the IIC in cases of fundamental non-performance. In the particular context of sustainability obligations, the Instrument provides for a structured, multi-step process to dispute settlement – beginning with cooperation and dialogue, including through a possible joint sustainability committee, and progressing to third-party amicable dispute settlement mechanisms, such as expert determination, before any recourse to adjudicative proceedings. In terms of remedies, termination would be a last-resort measure, with the Instrument favouring a collaborative approach to curing a breach of a sustainability obligation and preserving the investment relationship to the greatest extent possible. The State may also compel specific performance of the investor's obligations, including in the context of public utility concessions where continued service delivery is essential. In this way, the remedial framework operates symmetrically: just as the investor has contractual remedies to address the consequences of regulatory change, the State has contractual remedies to enforce the investor's commitments and to protect the public interest.

39. The balance reflected in this Instrument is thus expressed through several interconnected elements: the emphasis in the commentary to Art. 1.5 of the UPICC (exclusion and modification) regarding the need for the parties to maintain the balance between the rights and obligations of both parties and consider the Instrument as a whole; the introduction of scalability of sustainability obligations in light of the principle of proportionality, considering the risk, size and nature of the project, as well as parties' features and capabilities; strong investment protections balanced by reasonable exceptions, allowing the weighing of competing interests; and an overall conception inspired by State-investor cooperation – through good faith and mutual assistance – and sharing of burdens with reciprocal benefit. In all of these dimensions, the contractual nature of the IIC ensures that the balance – whether it is the product of direct negotiation, of the State's design of the contractual framework in a bidding process, or of a combination of both – is embedded in the contract and enforceable by both parties through the remedial tools available under the contract and the applicable law. Where the terms of the IIC have been largely pre-determined by the State, the remedial framework assumes a particularly significant role: it is the availability of effective and symmetrical remedies and dispute resolution options that ensures that a balance of interests is maintained in practice, even in the absence of prior negotiation on each individual term. The present Principles, by articulating the standards that a balanced IIC should reflect, thus serve both a preventive function – guiding the drafter of the contract, whether in a negotiated or non-negotiated setting – and a corrective function, providing adjudicators with a benchmark for assessing whether the contractual framework, as applied, achieves the balance of interests that international best practice requires.

## F. Relationship with the UPICC and interpretation[1]

40. The present Instrument is built upon and incorporates by reference the UPICC. They provide a comprehensive framework of general contract law rules that have achieved widespread international acceptance. Rather than duplicating that framework, this Instrument takes the UPICC as its foundation and provides specialised guidance only where the particular characteristics of IICs require it. The UPICC, first published by UNIDROIT in 1994 and most recently revised in 2016, set forth general rules for international commercial contracts. They are designed for use throughout the world, irrespective of the domestic legal traditions and the economic and political conditions of the countries in which they are to be applied. The UPICC address most of the important topics of general contract law, including formation, validity, interpretation, content, performance, and non-performance, and have been widely used in practice as chosen governing law, as a means of interpreting or supplementing domestic law and international uniform law instruments, and as a model for national and international legislators.

41. The UPICC constitute a solid foundation for this Instrument. First, they represent a neutral and balanced body of rules that is not tied to any single domestic legal tradition, having arrived at common ground between civil law and common law systems. This neutrality is essential in the context of IICs, where the parties typically come from different legal backgrounds and seek a predictable, internationally oriented standard of interpretation. Second, the UPICC have achieved broad acceptance in the practice of courts and arbitral tribunals at both the national and international levels, where they have frequently been used as a tool to supplement and corroborate the application of domestic law in international commercial disputes. Third, certain UPICC provisions are mandatory in nature – including the fundamental duty of good faith and fair dealing under Article 1.7 – and reflect principles and standards of behaviour that are of a mandatory character under most domestic law, thereby reinforcing the coherence of the contractual framework. Fourth, combining a set of rules specifically adapted to IICs with a widely accepted transnational set of general contract rules such as the UPICC allows contracting parties to introduce a standard of interpretation that is predictable, balanced, and internationally oriented, reducing transactional and litigation costs and enhancing the bankability of investment projects.

42. A further consequence of building this Instrument upon the UPICC concerns the standard of interpretation that applies to both. Article 1.6(1) of the UPICC provides that, in the interpretation of the Principles, regard is to be had to their international character and to their purposes, including the need to promote uniformity in their application. This provision – modelled on Article 7(1) of the UN Convention on Contracts for the International Sale of Goods (CISG) – reflects the fundamental principle that an international instrument must be interpreted autonomously, without filtering its concepts and terms through the lens of any single domestic legal tradition. The notions used in the UPICC – such as good faith and fair dealing, fundamental non-performance, hardship, or agreed payment for non-performance – are intended to carry an autonomous, internationally oriented meaning, informed by a comparative analysis of the world's major legal systems rather than by the domestic law concepts of any particular jurisdiction.

43. Article 1.6(2) of the UPICC complements this interpretive standard by providing that issues within the scope of the Principles but not expressly settled by them are, as far as possible, to be settled in accordance with their underlying general principles. This gap-filling mechanism ensures the internal coherence and self-sufficiency of the UPICC as a body of law, reducing the need to resort to domestic law to resolve questions that fall within the scope of the Principles.

[1] On the approach towards the treatment of individual UPICC provisions in this Instrument, see Section L of this Introduction.

44. The same standard of interpretation applies, by necessary implication, to the present Instrument. Since this Instrument incorporates the UPICC and is itself designed for use in an international context – involving parties from different legal traditions, operating across borders, and often subject to international arbitration – its Principles, Model Clauses and commentaries must likewise be interpreted with regard to their international character and purposes. The concepts and terms used in this Instrument – including those that are specific to IICs, such as stabilisation, economic equilibrium, regulatory freedom, and the duty to pursue the highest international standards – are intended to carry an autonomous meaning, not dependent on the interpretation that any particular domestic legal system would give to analogous concepts (see also Section K below). This autonomous standard of interpretation is essential to the proper functioning of the Instrument: it ensures that the Principles are applied consistently across different jurisdictions and legal traditions, and that the balance of interests carefully struck in this Instrument is not distorted by the application of domestic interpretive frameworks that may favour one party's legal tradition over the other's. As stated in the commentary to Model Clause A in Chapter 8, choosing this Instrument as the governing law of an IIC introduces a standard of interpretation that is "predictable, balanced, and internationally oriented as per Article 1.6(1) of the UPICC".

**G. Applicable law and concerns regarding internationalisation of investment contracts**

45. A fundamental question in any IIC concerns the law applicable to the contractual relationship. The determination of the applicable law affects virtually every aspect of the contract, including its formation, validity, interpretation, performance, and the consequences of non-performance. Given the long-term nature and high value of IICs, clarity regarding the applicable law is essential for both parties.

46. In most cases, the applicable law of an IIC will be determined by the parties' choice-of-law clause. Party autonomy – the freedom of contracting parties to choose the law governing their contractual relationship – is a widely recognised principle in international commercial practice and is generally respected in the context of IICs. In the absence of a choice-of-law clause, the applicable law will typically be determined by the conflict-of-laws rules of the forum or, in the case of arbitration, by the applicable arbitration provisions.

47. The most common choice of law in IICs is the domestic law of the host State. This choice reflects the close connection between the investment project and the host State's legal order: the investment is typically located within the host State's territory, the project is subject to the host State's regulatory framework, and the State party itself is bound by its own legal system (principle of legality). The choice of host State law also ensures that the IIC operates within a comprehensive legal framework that addresses matters not specifically covered in the contract itself.

48. However, parties to IICs have also employed other approaches. Some IICs designate the law of a third State as the applicable law, particularly where the parties seek a neutral legal framework or where the host State's legal system is perceived as underdeveloped or unstable. Other IICs choose the host State's law but supplement it with reference to international law, general principles of law, or instruments such as the UPICC. Still others may designate general principles of law or the *lex mercatoria* as the applicable law, though such choices are relatively rare in practice.

49. This Instrument is designed to accommodate all these approaches. As set out in Principle 2, the Principles in this Instrument may serve as the primary governing law where so chosen by the parties; they may supplement or interpret a chosen domestic law; or they may be applied by adjudicators where the parties have chosen general principles of law or similar sources, or where no choice of law has been made. Model Clauses A and B in Chapter 8 illustrate these different options.

50. Against this background, an issue that has attracted considerable scholarly attention concerns the "internationalisation" of contracts concluded between States and foreign investors. Historically, certain legal theories suggested that contracts between States and foreign nationals could be "internationalised" and thereby removed from the exclusive governance of domestic law – becoming instead subject to international law as their proper law.

51. The present Principles are not intended to internationalise IICs in the sense of making them generally subject to public international law as the governing law of the contractual relationship. IICs remain contracts governed by the rules of law chosen by the parties – which, in most cases will be the domestic law of the host State, either alone or in combination with other sources, including, where so agreed, this Instrument. When choosing this Instrument as the governing law, in combination with or to supplement the law of the host State (or that of a third State), the parties select a set of principles firmly grounded in the UPICC, reflecting standards of general contract law widely recognised in domestic legal systems and by the business community, as adapted to investment contracts. This approach is fundamental to the design of this Instrument.

52. Where the parties choose a domestic law as the governing law of their IIC, that choice carries with it the application of the mandatory rules of the chosen law, as well as any overriding mandatory rules that may apply regardless of the parties' choice. If the parties choose this Instrument as the governing law for the elements it covers (including general contract law, investor protection and sustainability), in accordance with Article 1.4 of the UPICC – which is incorporated by reference into this Instrument – such choice does not restrict the application of mandatory rules applicable under the relevant rules of private international law. In an arbitration context, these Principles would apply only subject to the application of "overriding" mandatory rules, as explained in Chapter 8. In addition, in either case, the domestic law chosen by the parties (or otherwise applicable) would continue to apply to matters not covered by the Instrument.

53. Investment treaties often contain provisions requiring an investment to comply with the law of the host State or not to relax or lower environmental and social standards under its legislation. Such provisions may be part of the definition of "covered investment" or operate elsewhere as a condition for treaty protection. They serve to prevent investors from benefiting from treaty protections where the investment was made or carried out in violation of domestic law. Since this Instrument focuses on IICs rather than IIAs, such provisions are not included here. However, as noted, contracting parties are free to choose the host State's domestic law as applicable law to their contract and, in line with contracting practice, references to host State law are included in the Model Clauses on investors' sustainability obligations (Chapter 5, Section D.2). Furthermore, in accordance with Articles 1.4 and 3.3.1 of the UPICC, it is recalled in this Instrument that IICs must not violate the applicable mandatory rules, including those of the host State, where applicable.

**H. Dispute settlement**

54. Given the long-term, high-value, and complex nature of IICs, the approach to dispute settlement adopted in this Instrument is aimed at ensuring that disputes are resolved effectively, predictably, and in a manner consistent with the broader objectives of the contractual framework.

55. To that end, this Instrument favours a multi-tiered approach that prioritises amicable settlement as the first step before escalating to binding adjudicatory mechanisms. IICs are fundamentally long-term cooperative relationships in which the preservation of the investment relationship is itself a value worth protecting. Direct negotiations between the parties, mediation, conciliation, expert proceedings, and dispute boards are each recognised as valuable tools for resolving disputes without the costs, delays, and adversarial dynamics that adjudicative proceedings – arbitration and judicial proceedings – entail. At the

same time, this Instrument does not impose a mandatory sequential process: the Model Clauses on dispute resolution in Chapter 8 are intentionally flexible, allowing parties to structure the dispute resolution sequence according to their specific needs and to retain the freedom to pursue amicable settlement at any stage, including after the commencement of arbitral or judicial proceedings.

56. As regards the forum for adjudicative proceedings, while acknowledging that some States may prefer to resolve disputes in their domestic courts, investors frequently consider a neutral third-party mechanism to be of paramount importance. International arbitration is identified as the mechanism that most naturally responds to this concern, affording the parties a neutral, specialised, and effective method of dispute resolution with a globally enforceable regime. The Instrument does not prescribe a single arbitral institution but instead provides flexible model clauses that accommodate a range of options — including institutional arbitration (such as arbitration administered by the ICC or ICSID, given their experience in administering arbitrations arising out of IICs) and *ad hoc* arbitration under the UNCITRAL Arbitration Rules — leaving the choice to the parties in light of their particular needs for structure, administrative support, cost-efficiency, and procedural flexibility.

57. Further, in arbitration, parties enjoy substantial freedom to choose non-State rules of law – including soft-law instruments such as the Principles in this Instrument – as the rules on which the arbitrators are to base their decisions. This freedom is generally broader than that available before domestic courts, where most national law does not allow parties to choose non-State rules of law to govern the contract, although there is a growing recognition of this possibility. Even in States that do not give direct effect to the choice of non-State rules, such rules may still be applied indirectly by way of incorporation by reference, namely, as terms of the contract. International arbitration thus provides the most natural and effective forum for the direct application of this Instrument as governing law.

58. On the other side, as described in Section I below, when adjudicators – whether at the national or international level – are applying domestic law to an IIC, they may take the present Principles into consideration to corroborate and inform the application of that law; the practice of courts and tribunals indicates that the UPICC have frequently been used in this manner to supplement and corroborate the application of domestic law in international commercial disputes. By combining these Principles with domestic law, parties who choose arbitration introduce a predictable and internationally oriented standard of interpretation, thereby reducing transactional and litigation costs and enhancing the bankability of investment projects.

59. The risk of parallel and overlapping proceedings is also addressed. Given that investors may have access to multiple fora – including treaty-based arbitration, contract-based arbitration, and domestic courts – the Instrument encourages parties to designate one exclusive dispute resolution forum in the IIC and to explicitly waive their rights to pursue adjudicative dispute resolution elsewhere. Parallel proceedings increase costs, decrease predictability, and may lead to conflicting decisions and abuses of the international dispute resolution mechanisms, all of which are detrimental to the stability of the investment relationship. To enable the consolidation of related disputes, the Instrument also recommends that all contracts governing a single investment project contain the same arbitration clause.

60. The public-interest dimension inherent in IICs is also relevant. Issues of transparency and conflicts of interest in arbitral proceedings are addressed in recognition of the legitimate interest of States and other stakeholders in the conduct and outcomes of proceedings that affect public resources and public policy. At the same time, the Instrument does not prescribe a uniform approach; rather, it encourages parties to consider the procedural rules applicable to their chosen arbitration forum and to reach an informed agreement on the degree of transparency or confidentiality appropriate to their specific context.

61. Finally, a symmetrical approach to dispute initiation and counterclaims is warranted. Because an IIC stipulates rights and obligations for both the investor and the counterparty on the State side, both parties have the right to initiate proceedings and to bring counterclaims. This is a significant distinction from treaty-based investment arbitration, where the investor typically initiates the claim unilaterally and the scope for State counterclaims is often contested. In contract-based arbitration, the scope of the responding party's claims extends to all aspects relating to the IIC, with the objective that the entirety of the dispute be resolved in one forum. This symmetry of rights is a natural consequence of the contractual logic that underpins this Instrument.

62. Chapter 8 of this Instrument provides detailed Principles, commentary, and Model Clauses on dispute settlement, offering parties flexible and adaptable tools for structuring their dispute resolution framework.

**I. The corroborative function of the instrument**

63. While this Instrument is designed to be capable of serving as the primary source of law governing an IIC (when so chosen by the parties), it is equally designed to serve a corroborative and supplementary function in relation to domestic law. Principle 2 sets forth the various ways in which the Principles in this Instrument may be applied. They may apply as a primary source of law where the parties have agreed that their contract shall be governed by them. They may also be applied where the parties have agreed that their contract be governed by general principles of law, the *lex mercatoria*, or similar sources. Where the parties have not chosen any law to govern their contract, the Principles may be applied by adjudicators, where appropriate.

64. Beyond these applications as a primary source, the Principles may serve to interpret or supplement international uniform law instruments and domestic law. This secondary, corroborative function is of particular importance. When adjudicators – whether at the national or international level – are applying domestic law to an IIC, they may take the present Principles into consideration to corroborate and inform the application of that law. The practice of courts and tribunals indicates that the UPICC have frequently been used as a tool to supplement and corroborate the application of domestic law in international commercial disputes; this Instrument is intended to serve a similar role in the context of IICs.

65. Model Clause B provided in Chapter 8 illustrates this approach. It contemplates that an IIC may be governed by a particular domestic law (typically the law of the host State), with that law being "interpreted and supplemented by" the present Principles. This formula enables a harmonised interpretation of domestic law and provides a neutral benchmark against which to assess rights and obligations. By assigning an interpretative role to the Principles, parties can achieve greater predictability and reduce transactional and litigation costs.

66. The corroborative function also extends to ensuring that IICs reflect the highest international standards on sustainability. By referring to this Instrument to interpret and supplement the applicable domestic law, parties can support the achievement of sustainable investment objectives, including through a corporate due diligence process integrating national impact assessment standards.

67. This aspect of the corroborative function warrants particular attention. International investment projects, by their nature, engage with a complex web of international standards relating to sustainability, including human rights, environmental protection, and labour rights. These standards are articulated in numerous international instruments, including the UN Guiding Principles on Business and Human Rights, the OECD Guidelines for Multinational Enterprises, the ILO Declaration on Fundamental Principles and

Rights at Work, the Paris Agreement on climate change, the Sustainable Development Goals, and relevant instruments of multilateral development banks, including regional development banks.

68. There is a growing consensus that investment projects should adhere to these international standards, regardless of where they are located. However, a practical challenge arises in the implementation of these standards through the contractual framework of an IIC. Where the applicable law of an IIC is the domestic law of the host State, and where that domestic law has not fully implemented or incorporated the highest international standards on sustainability, a gap may emerge between the standards to which the contracting parties aspire and the standards that the applicable law actually requires or recognises. In such cases, this Instrument may serve to bridge that gap by providing a benchmark that integrates less strict standards in force in the host State with internationally recognised best practices.

69. This Instrument does not purport to override mandatory rules of the applicable domestic law, and it cannot compel adjudicators to disregard clear provisions of domestic law in favour of international standards. Where there is an irreconcilable conflict between the applicable domestic law and an international sustainability standard, the domestic law will generally prevail unless the parties have expressly agreed otherwise and such agreement is given effect by the adjudicator.

70. For this reason, the Instrument encourages parties to incorporate sustainability standards expressly into their IIC as contractual obligations, thereby ensuring that such standards are binding as a matter of contract even where the domestic law may be less developed.

### J. The role and utility of Model Clauses

71. A distinctive feature of this Instrument is the inclusion – following a long-standing tradition at the ICC – of Model Clauses alongside the Principles and commentary. These Model Clauses serve a practical function that complements the normative and interpretive roles of the Principles themselves. While the Principles articulate general rules and standards applicable to IICs, the Model Clauses translate those rules and standards into concrete contractual language that parties may adopt, adapt, or use as a reference point in their negotiations.

72. The Model Clauses are designed to be of immediate practical utility to negotiators and drafters of IICs. Negotiating an IIC is a complex undertaking that typically involves parties with different levels of experience, different legal traditions, and different negotiating capacities. The Model Clauses provide a common starting point for negotiations, offering language that reflects internationally accepted best practices and that has been developed through a balanced process involving input from both State and investor perspectives.

73. By providing such a starting point, the Model Clauses can help to level the playing field between parties with unequal bargaining power or expertise, and can reduce the transactional costs associated with drafting complex contractual provisions from scratch.

74. Importantly, when read together, the Model Clauses provide a comprehensive indication of how the Principles contained in this Instrument are intended to be integrated into a coherent contractual framework. Each Model Clause addresses a specific issue or set of issues relevant to IICs, but the clauses are designed to work together as an integrated whole. For example, the Model Preamble language on sustainable investment in Chapter 2 connects with the Model Clauses on sustainability due diligence in Chapter 3 and the Model Clauses on sustainability obligations of the investor and State party in Chapter 5. Similarly, the Model Clauses on stabilisation and renegotiation in Chapter 6 are designed to complement the Model

Clauses on State obligations for investment protection in Chapter 5, while respecting the carve-outs for regulatory measures in the public interest.

75. A negotiator who reviews the Model Clauses in their entirety will gain a clear picture of how a balanced IIC can be structured – one that provides meaningful protection to investors while preserving the State's regulatory freedom, that incorporates sustainability considerations as core obligations of both parties, and that provides effective mechanisms for managing change and resolving disputes. The Model Clauses thus serve not only as individual drafting tools, but also as a template for a comprehensive, modern approach to investment contracting.

76. It should be emphasised that the Model Clauses are not intended to be adopted without consideration of the specific circumstances of each investment project. IICs vary widely in their subject matter, the sectors in which they operate, the regulatory environments of the host States, and the particular interests and concerns of the contracting parties. The Model Clauses are designed to be adaptable: parties may adopt them as drafted, modify them to suit their particular needs, or use them as a reference point for developing their own bespoke provisions. The accompanying commentary provides guidance on the purpose and operation of each Model Clause, as well as on potential variations that parties may wish to consider.

77. The Model Clauses also serve an educational function. For negotiators who may be less experienced in the drafting of IICs, the Model Clauses illustrate how abstract principles can be translated into operative contractual language. They demonstrate how different provisions of an IIC interact with one another, and how potential conflicts between competing interests – such as investor protection and regulatory freedom – can be addressed through careful drafting. In this way, the Model Clauses contribute to capacity-building and to the broader dissemination of best practices in investment contracting.

### K. Terminology and future-proofing

78. This Instrument employs a number of key terms and expressions that are used consistently throughout the Principles, Model Clauses and commentary. A brief overview of the most significant terminological choices is warranted, as these choices reflect substantive decisions about the scope and orientation of the Instrument.

79. The term "Instrument" is used to refer to the entirety of this work, encompassing Principles, Model Clauses, commentary, and illustrations. References to "this Instrument" are therefore intended to capture all of these components, not only the normative Principles.

80. On the side of the State, this Instrument refers to the "party on the State side" or "State party" to encompass the various entities that may enter into an IIC with a foreign investor. The party to an IIC on the State side may be the State itself, an organ or ministry of the State, a State enterprise, or any other entity that is competent to enter into IICs on behalf of the State. This broad and functionally neutral terminology was chosen to accommodate the wide range of institutional arrangements through which States organise their participation in investment projects, without prescribing a particular model of State involvement.

81. On the other side, the term "Investor" refers to one or more foreign investors that are party to the IIC. The qualification of the investor – whether foreign or domestic – may be an issue covered by the applicable law and is therefore not definitively resolved by this Instrument, which leaves it to the parties and adjudicators to make their determinations in accordance with the applicable law and the circumstances.

82. A deliberate and significant terminological choice concerns the term "international investment contract" or "IIC" itself. This Instrument does not provide a formal definition of an IIC, nor does it set out qualifications for an investor. This approach reflects a conscious decision to ensure that the Instrument remains broadly applicable and adaptable. As said, IICs take many forms – concession contracts, joint venture agreements, share purchase agreements, construction contracts, and public-private partnerships, among others – and exist across diverse sectors, from resource extraction and energy to construction, telecommunications, and water management. Rather than attempting to confine such a heterogeneous category of contracts within a rigid definitional framework, the Instrument identifies a set of common characteristics that typically distinguish IICs from ordinary commercial contracts: the involvement of a party connected to the State, an investor, a subject matter typically relating to projects of public interest or public purpose, a long-term duration, and a high value. These characteristics serve as guidance for determining whether a particular contract falls within the scope of this Instrument, but the ultimate determination is left to the contracting parties and, where applicable, to adjudicators. This Instrument may be applied where the parties or adjudicators deem it appropriate, in accordance with Principle 2.

83. This open and non-prescriptive approach to the definition of an IIC also serves the broader objective of ensuring that the Instrument remains future-proof. The landscape of international investment is not static: new forms of contractual arrangements, new sectors, new technologies, and new regulatory frameworks continue to emerge. A rigid definition would risk excluding contractual arrangements that share the essential features of IICs but do not fit neatly within a pre-determined category. By anchoring the scope of the Instrument in functional characteristics rather than in a closed definition, and by leaving the determination of applicability to the parties and adjudicators, this Instrument is designed to remain relevant and useful as investment practices evolve. The same logic of adaptability extends to the substantive content of the Instrument: the Principles are formulated at a level of generality that allows them to be applied across sectors and contractual types, while the Model Clauses provide concrete drafting options that parties may adopt, adapt, or use as a reference point in light of the specific circumstances of their investment project. Similarly, the Instrument's approach to sustainability standards – encouraging the parties to pursue the "highest international standards" and to update their contract, management and mitigation plans in light of evolving standards – ensures that the contractual framework can keep pace with developments in international norms and expectations regarding sustainability.

### L. Structure of the instrument and methodology on its relationship with the UPICC

84. This Instrument is organised into eight Chapters. Each Chapter consists of: (i) an introduction explaining whether and how the corresponding Chapter in the UPICC applies, including its commentary; (ii) Principles (which may be normative or descriptive) that cover specificities of IICs, accompanied by commentary; (iii) IIC-specific guidance on aspects covered in the UPICC; and (iv) Model Clauses with commentary, where relevant.

85. Chapter 1 provides general provisions concerning the Instrument, including its scope, relationship with the UPICC, and application. Chapter 2 addresses general principles applicable to IICs, including form requirements, interdependent contracts, sustainable investment, anti-corruption, and the preamble to an IIC. Chapter 3 deals with formation, including freedom to negotiate, sustainability due diligence in the pre-contractual phase, and legal capacity. Chapter 4 addresses validity. Chapter 5 concerns rights and obligations, including State obligations on investment protection and shared investor-State obligations on sustainability. Chapter 6 addresses change of circumstances, including stabilisation and renegotiation clauses, hardship, and force majeure. Chapter 7 deals with remedies, including compensation and damages. Chapter 8 addresses choice of law and dispute settlement.

86. The relationship between this Instrument and the UPICC is operationalised through a consistent methodology that governs both the structure of each Chapter and the treatment of individual UPICC provisions. Each Chapter of this Instrument follows a uniform internal architecture: it begins with an introduction that maps the relationship between the Chapter and the corresponding provisions of the UPICC, explaining which UPICC rules apply as they are, which are specified or supplemented, and which are departed from; it then sets forth Principles – which may be normative or descriptive – that address the specificities of IICs, accompanied by commentary and illustrations; it provides IIC-specific guidance on aspects already covered in the UPICC; and it offers Model Clauses with commentary, where relevant.

87. Within this architecture, four methodological approaches govern the treatment of individual UPICC provisions. First, where a UPICC provision is deemed appropriate in the context of IICs without the need for specific guidance, that provision is not repeated but is deemed incorporated into this Instrument by virtue of Principle 1(4); the parties' reference to this Instrument thus entails a concomitant reference to the UPICC on all issues of general contract law not otherwise addressed herein.

88. Second, where a UPICC provision is appropriate but IIC-specific guidance would be useful, the UPICC provision is briefly recalled and additional guidance is provided through commentary and, where appropriate, a Model Clause. This approach is followed, for example, in the treatment of withholding performance (Article 7.1.3 of the UPICC) in Chapter 7, where the commentary explains the particular constraints that arise in IICs involving the provision of essential public services, and Model Clauses offer alternative formulations reflecting the principle of continuity. Similarly, the UPICC provisions on exemption clauses (Article 7.1.6) and specific performance (Article 7.2.2) are recalled in Chapter 7 and supplemented with commentary that addresses the particular dynamics of State-investor relationships.

89. Third, where a UPICC provision requires adaptation in the context of IICs, an IIC-specific Principle and/or Model Clause is provided as a replacement, with accompanying commentary. This is the case, notably, for the UPICC provisions on form: whereas Articles 1.2 and 2.1.1 of the UPICC provide that no specific form is required for the conclusion of a contract, Principle 4 of this Instrument departs from this rule and imposes a written form requirement for IICs, reflecting the high-value, complex, and long-term nature of these contracts. Likewise, the UPICC rules on pre-contractual good faith and inconsistent behaviour are adapted through Principle 10, which specifies the scope of the duty of good faith in the particular context of IIC negotiations – including the recognition that a change of policy during negotiations does not by itself constitute bad faith.

90. Fourth, where an issue is not covered in the UPICC but is deemed relevant in the context of IICs, an IIC-specific Principle is provided in addition to the UPICC, with accompanying commentary and, where appropriate, a Model Clause. This is the case for a significant body of provisions that address matters unique to IICs, including sustainable investment and the duty to pursue the highest international standards (Principle 6), anti-corruption (Principle 7), specific arrangements duly approved by competent bodies (Principle 8), sustainability due diligence in the pre-contractual phase (Principle 11), stabilisation and renegotiation clauses (Principle 23), and the provisions on investment protection in Chapter 5, none of which find a counterpart in the UPICC.

91. This layered methodology ensures that, when the parties to an IIC refer to this Instrument, they benefit from the full body of general contract law rules contained in the UPICC – as a comprehensive and self-standing foundation – while also receiving specialised guidance tailored to the unique characteristics of investment contracts. Where this Instrument has modified the application of specific UPICC provisions, the Principles and commentary in this Instrument prevail; on all other issues, the UPICC apply as they are.

## CHAPTER 1. GENERAL PROVISIONS CONCERNING THE INSTRUMENT

### A. Introduction

92. This Chapter provides the foundations for the rest of this Instrument. Section B sets out the scope of the Instrument and its relationship with the UPICC (Principle 1). It clarifies that the scope concerns "international investment contracts" (IICs), explaining key characteristics of such contracts while leaving it to contracting parties and adjudicators to decide whether they deem a specific contract to be an IIC. It also clarifies that, unless otherwise provided, the provisions of the UPICC (2016 version) apply to IICs. More specifically, with the UPICC as a starting point, there are four options:

(i) A UPICC provision is deemed appropriate in the context of IICs, without the need for specific guidance; in this case, the UPICC provision is not repeated but should be deemed incorporated into this Instrument.

(ii) A UPICC provision is deemed appropriate in the context of IICs, but it was felt that IIC-specific guidance would be useful; in this case, the UPICC provision is briefly recalled and additional guidance is provided by means of commentary and, where appropriate, a Model Clause.

(iii) A UPICC provision requires adaptation in the context of IICs; in this case, an IIC-specific Principle, and/or a Model Clause, is provided as a replacement for the relevant UPICC provision, with accompanying commentary.

(iv) An issue is not covered in the UPICC but is deemed relevant in the context of IICs; in this case, an IIC-specific Principle is provided, in addition to the UPICC, with accompanying commentary and, where appropriate, a Model Clause.

93. Principle 2 explains how this Instrument can be used in practice. It is modelled on the Preamble to the UPICC. It explains that the Principles can serve as a primary source of law (the substantive law governing an IIC), as a secondary source (to interpret or supplement domestic law or international uniform law instruments), or as an inspiration for legislators. The Principles can also be used by negotiators of IICs to determine the content of their contract or to reach a settlement agreement in case of dispute. Use by negotiators is particularly relevant, since this Instrument not only provides Principles and commentary, but also Model Clauses accompanied by commentary.

94. Section C explains that, since this is an instrument of soft law, the parties may choose to exclude the application of specific Principles, or adapt them to their specific needs. Moreover, they can decide whether to incorporate the recommended Model Clauses. However, it is recommended that any adaptations respect the overall balance between the interests of investors and States, and of the civil society as a whole, as sought in this Instrument. It also recalls that, pursuant to Article 1.5 of the UPICC, certain UPICC provisions are mandatory in nature and remain so in the context of IICs.

95. Principle 3 provides guidance on the interplay between this Instrument and relevant industry usages and practices, against the background of Article 1.9 of the UPICC. It recognises that IICs may explicitly refer to sector-specific industry usages as interpretative guidance for the contract and that, even in the absence of explicit references, sectoral or technical industry usages may be relevant for the interpretation of certain terms in IICs.

96. In summary, compared to the UPICC, this Chapter explains this Instrument's tailored scope, provides *lex specialis* rules on its purpose (replacing the Preamble of the UPICC), and provides additional guidance specifically on Articles 1.5 and 1.9 of the UPICC.

## B. Scope and application of the Principles

### Principle 1

### Scope of the Instrument and relationship with the UPICC

**(1) This Instrument sets forth rules and guidance on issues relevant to international investment contracts (IICs).**

**(2) For the purposes of this Instrument, an IIC is a contract between a party on the State side, on the one hand, and a foreign investor, on the other.**

**(3) Where appropriate, this Instrument modifies the application of specific provisions of the UNIDROIT Principles of International Commercial Contracts (UPICC) to account for the specificities of IICs.**

**(4) Issues not settled in this Instrument shall be settled in accordance with the UPICC.**

**Commentary**

*A. This Instrument*

97. This "Instrument" comprises Principles, commentary, illustrations, and Model Clauses. Therefore, references to "this Instrument" include all such elements.

*B. Rules and Guidance*

98. This Instrument provides a combination of rules and guidance on issues that are relevant in the practice of IICs. The parties have the freedom to choose whether to apply all the Principles and Model Clauses or only a part thereof. Additionally, some sections provide alternatives for the parties to choose from (see also Section C below).

*C. International Investment Contracts*

99. An IIC possesses certain characteristics that distinguish it from other commercial contracts. IICs are contracts between a party on the State side, on the one hand, and an investor, on the other. On the side of the State, the party to an IIC may be the State or an organ of the State that is a department or ministry of the State, a State enterprise, or any other entity that is competent to enter into IICs on the side of the State. The last category of other entities is residual and could include a wide variety of entities that may be within or outside the control of the State, as long as they have the competence to enter into an IIC on the side of the State. Some of the examples of the competence to enter the contract on the side of the State include their competence to enter into IICs through legislation or an administrative or other order issued by the State that gives them that competence; they may be controlled by the State through shareholding or appointment of key positions, etc.; or they may be independent and not controlled by the State, yet authorised or allocated public assets, public resources or other public functions that constitute the subject matter of the IIC. Unless one of the entities on the side of the State is specifically referred to

in this Instrument, the reference to "the party on the State side" (or "State party") is a reference to all the entities as described in the preceding sentences. On the other side, the party would be one or more investors. The investor may be an entity incorporated, having its place of business, control of business, or principal activity outside the host State or inside the host State (*e.g.*, an investor that is located in a foreign jurisdiction may operate through a local company in the host State or be otherwise associated with it under specific circumstances). The nature of the parties and their relationship may entail relevance of a variety of sources of law. Another distinctive feature concerns the subject matter of an IIC, which typically relates to projects of public interest or public purpose. The public purpose element is generally also reflected in the contract itself (*e.g.*, through clauses advancing public policy goals such as sustainable investment). Moreover, IICs are typically long-term and high-value agreements.

100. An IIC may take various forms such as concession contracts, joint venture agreements, share purchase agreements, construction contracts, or public-private partnerships (PPPs), or any other form of contractual arrangement. An IIC may exist in diverse sectors, some examples being resource extraction, oil and natural gas, construction, and public services and utilities, such as telecommunication, water management or electric power distribution services. An IIC may be entered into through various processes, such as direct negotiations between the parties or through a tender process. The present Principles cover major areas that apply across various types of contracts and sectors, as well as manners of entering into them.

101. An IIC is a contractual arrangement with contractual consequences between the parties. It is neither an international investment agreement (IIA) entered into between States providing protection, nor a treaty in any other form. Therefore, issues of definition (investor, investment) that are determinative in IIAs do not pose the same jurisdictional hurdles in IICs. Additionally, several other issues that are specific to IIAs (*e.g.*, denial of benefits clauses) are not relevant for IICs.

102. Generally, IICs involve an international element. This Instrument does not define an IIC or provide qualifications for an investor. This Instrument may be applied where the parties or adjudicators deem it appropriate in accordance with Principle 2.

*D. Relationship with the UPICC*

103. Paragraph (1) states that the present Principles are dedicated to IICs. In principle, the UPICC apply to IICs for issues of general contract law. Paragraph (3) clarifies that, where appropriate, this Instrument modifies the application of certain provisions of the UPICC to account for the specific characteristics of IICs. In such instances, the Principles and commentary in this Instrument prevail over those in the UPICC. Paragraph (4) further specifies that, if this Instrument has not modified the application of specific UPICC provisions, the UPICC shall apply to IICs "as they are". Consequently, when the parties to an IIC refer to these Principles, such a reference is also intended as a referral to the UPICC applying to issues not settled in this Instrument.

**Principle 2**

**Application of the Principles**

**(1) These Principles apply to IICs where the parties have agreed that their contract shall be governed by them or where the parties have incorporated them in their contract.**

**(2) They may be applied when the parties have agreed that their contract be governed by general principles of law, the *lex mercatoria* or the like.**

**(3) They may be applied where appropriate when the parties have not chosen any law to govern their contract.**

**(4) They may be used to interpret or supplement international uniform law instruments.**

**(5) They may be used to interpret or supplement domestic law.**

**(6) They may serve as a model for national and international legislators.**

**(7) The Principles and Model Clauses in this Instrument may serve as a model for negotiators of IICs.**

**Relevant UPICC provision**

Preamble of the UPICC (Purpose of the Principles)

**Commentary**

104. Principle 2 sets out the various ways in which the present Principles may be applied. It is modelled on the Preamble to the UPICC but tailored to this Instrument. It follows from Principle 2 that the Principles in this Instrument can serve three main functions: (i) as a primary source of law, *i.e.,* the substantive law governing an IIC (paragraphs (1) to (3)), (ii) as a secondary source to interpret or supplement domestic law or international uniform law instruments (paragraphs (4) and (5)), and (iii) as an inspiration for legislators and for negotiators of IICs (paragraphs (6) and (7)).

105. Paragraph (1) specifies that these Principles will apply if the parties have agreed that their contract shall be governed by them or where the parties have incorporated them in their IIC. The incorporation of the Principles into an IIC may be used as a means of achieving partial application of the Principles in situations where the direct choice of non-State rules of law as the governing law may not be recognised under the applicable private international law rules. In such a case, the Principles do not operate as governing law but rather as contractual terms agreed between the parties. An adjudicator would be allowed to apply their substantive content, subject to any mandatory provisions of the otherwise applicable law. By contrast, where the parties choose the Principles as the law governing their contract, they are generally advised to combine such a governing law clause with an arbitration clause, since parties in international arbitration are generally permitted to select non-State rules of law. In such a case, the Principles would apply, subject only to overriding mandatory rules that would apply irrespective of the governing law of the contract (see also Chapter 8). Furthermore, the parties may also choose to incorporate the Model Clauses provided in this Instrument into their IIC. Paragraph (1) makes it amply clear that the present Principles do not seek to provide prescriptive or obligatory principles and that the decision to apply them is left to the freedom of the parties. Parties can apply the present Principles in their present form or with appropriate modifications (see also Section C below). The freedom of the parties to apply the present Principles to an IIC is subject to the applicable law to the IIC since the applicable law may limit, exclude, modify, adapt, or supplement the present Principles.

106. Paragraph (2) specifies the situations where the present Principles may be implicitly applicable. If the parties have agreed that their contract is governed by general principles of law, the *lex mercatoria* or other similar legal systems, that may be deemed to be the choice to apply the present Principles. These Principles may serve as a manifestation of legal principles that fall under the sources specified in paragraph (2). The reference to general principles of law is to be understood as general principles of commercial law. The term *lex mercatoria* or the like is used to indicate the situations where the parties have agreed to apply

practices in a certain sector. The choice of other similar legal systems such as supranational or transnational law would also be treated as an implied choice to apply the present Principles.

107. Paragraph (3) refers to the possible use of the Principles if the parties have not chosen any law to govern their contract. These Principles may then be applied "where appropriate". The term "where appropriate" is used to indicate that they may be chosen by adjudicators, in accordance with applicable rules on how to determine the applicable law, where the parties have not agreed on the applicable law. This may occur when it can be inferred from the circumstances that the present Principles are the most appropriate instrument to apply. It is rare in modern contract practice (and particularly IICs) not to have a choice-of-law provision. Paragraph (3) addresses those exceptional situations.

108. Paragraph (4) indicates that the present Principles may also be used to interpret or supplement the application of international uniform law instruments, which, in the context of this Instrument, should be interpreted broadly and include relevant treaties and soft-law instruments. International uniform law instruments may give rise to questions concerning the precise meaning of their individual content or may present gaps when it comes to their application to IICs. These Principles may form the basis to interpret such instruments and fill in their gaps by performing a supplementary role. The Model Clauses provided may help to operationalise – at the contractual level – relevant international uniform law instruments.

109. Paragraph (5) refers to the corroborative function of the Principles. When adjudicators – whether at the national or international level – are applying domestic law, they may take into consideration the present Principles to corroborate the applicable law. The practice of courts and tribunals at the national and international level indicates the use of the UPICC as a tool to supplement and corroborate the application of domestic law. Paragraph (5) is aimed at encouraging the use of the present Principles in a similar manner. When a dispute relates to an IIC, the present Principles can serve as a source of inspiration. The interpretation and application of domestic law in question could benefit from the international guidance provided in this Instrument in relation to the special needs of IICs.

110. Paragraph (6) is an encouragement to national and international legislators to use the present Principles as models for legislation. At the international level, the present Principles could become an important term of reference for the drafting of conventions and model laws. Equally, at the national level, they could be the basis for legislation, executive orders, and model contracts. Since alternatives are provided at various places in this Instrument, legislators can choose their preferred approach from those alternatives.

111. Paragraph (7) refers to the possibility for drafters and negotiators of IICs to use this Instrument as a source of inspiration in the design of investment contracts. While the Preamble to the UPICC does not expressly refer to such a function, the commentary thereto (point 8) acknowledges that the UPICC may serve as a guide for contract drafting. In the context of this Instrument, it was considered particularly important to make explicit reference to its potential use in contract drafting and negotiation, given that it comprises not only a set of Principles but also Model Clauses.

112. The list of functions in Principle 2 is not exhaustive. This Instrument may also be used to perform other functions that have not been specifically spelled out in the black-letter Principle. In particular, this Instrument (like the UPICC) may also be used for educational purposes, in the context of academic activities, or for the training of government officials, consultants, or practitioners involved in the negotiation and drafting of IICs. The use of this Instrument for such purposes may be particularly relevant for countries in which institutional and financial constraints may limit the availability of specialised training and technical resources to inform the negotiation and drafting of IICs.

### C. Exclusion or modification by the parties

**Relevant UPICC provision**

Article 1.5 (Exclusion or modification by the parties) of the UPICC

**Commentary**

113. The rules laid down in these Principles are non-mandatory in nature. Accordingly, the parties may, in any given case, exclude their application in whole or in part, or modify their content to adapt them to their specific needs. The same applies to the Model Clauses in this Instrument. Such exclusion or modification by the parties may be either express or implied. There is an implied exclusion or modification when the parties expressly agree on contract terms that are inconsistent with provisions of the Instrument. For certain matters, the Instrument provides alternative options, from which the parties may select the solution most appropriate to their contractual context.

114. At the same time, the Principles included in the Instrument, particularly on investment protection and sustainability, are in principle all essential. The Instrument as a whole seeks to strike a balance among different interests. For this reason, contracting parties are encouraged to use the Principles and Model Clauses as they are formulated in the Instrument, clarifying the chosen approach where alternative options are provided. Where the parties adapt any of these Principles in shaping their IIC, such adaptations should respect the overall balance of interests reflected in the Instrument.

115. A limited number of provisions of the UPICC are mandatory in nature (see Article 1.5 of the UPICC), *i.e.*, their importance in the system of the UPICC is such that parties should not be permitted to exclude or derogate from them as they wish. This includes, for example, Article 1.7 of the UPICC on good faith and fair dealing.[2] It is true that given the particular nature of the UPICC, the non-observance of this precept may have no consequences. On the other hand, it should be noted that the provisions in question reflect principles and standards of behaviour which are of a mandatory character under most domestic law as well. Since this Instrument incorporates the UPICC for issues of general contract law, those mandatory provisions of the UPICC also remain mandatory in the context of IICs.

### D. Usages and practices

**Principle 3**

**Usages and practices**

> **(1) The parties to an IIC are bound by any usage to which they have agreed and by any practices which they have established between themselves.**
>
> **(2) A usage of a particular industry or sector that is widely known and regularly observed in the investment context may be used to interpret or supplement an IIC but does not prevail over these Principles or express terms of the contract.**

**Relevant UPICC provision**

Article 1.9 (Usages and practices) of the UPICC

[2] For the full list of mandatory UPICC provisions, see Article 1.5 of the UPICC, point 3 of the Commentary.

**Commentary**

116. Article 1.9 of the UPICC lays down the principle according to which the parties are, in general, bound by any practice which they have established between themselves, and any usage to which they have agreed or that is widely known and regularly observed in international trade by parties in the particular trade concerned. While this provision is applicable in the context of IICs, its application requires certain clarifications specific to the particular features of such contracts.

117. Paragraph (1) of Principle 3 establishes that, in line with Article 1.9(1) of the UPICC, the parties to an IIC are bound by any usage to which they have agreed. They may expressly stipulate the application of any usage in their contract. In IICs, such references are generally meant as interpretative guidance. For instance, IICs may refer to sector-specific industry usages (*e.g.*, generally accepted principles, practices or trade usages and customs in the international petroleum industry) in the governing law and/or dispute resolution clause to signal that the contract should be interpreted in light of the relevant usage. Reference may also be made to industry practices as benchmarks for the performance of contractual obligations (*e.g.*, record-keeping requirements or the establishment of production rates), for determining whether an event constitutes force majeure, or in termination clauses (*e.g.*, permitting contract termination if production is interrupted without justification acceptable under relevant industry practices).

118. IICs may also reference industry standards and practices in clauses relating to sustainability commitments (*e.g*., related to the use of the most up-to-date green technologies or accepted practices on site abandonment, cleaning, restoration and decommissioning). As explained in other sections of this Instrument, the parties to an IIC are encouraged to pursue the investment in accordance with the highest international standards on sustainability, and to specify in their contract (*e.g.*, in an exhibit) which standards they jointly consider relevant to the investment project (see Chapter 2, Principle 6).

119. In the investment context, it is generally less likely than in the commercial context for the parties to have established a practice between themselves, since IICs are less commonly concluded repeatedly between the same parties. Consequently, opportunities for the development of consistent conduct are more limited. In this respect, the commentary to Art. 1.9 of the UPICC clarifies that behaviour occurring in the context of only one prior transaction between the parties will not normally be sufficient to establish a practice. States may rely on standard clauses or model contracts (particularly in sectors such as natural resources, infrastructure, or public–private partnerships) that reflect a State's general contracting policy or practice. However, this is conceptually distinct from a practice established between contractual parties.

120. Paragraph (2) provides an adaptation of Article 1.9(2) of the UPICC. The latter allows usages to supplement or interpret a contract even when the parties have not expressly agreed to them, provided that the usages are "widely known to and regularly observed [...] by parties in the particular trade concerned". Pursuant to the UPICC, such usages prevail over conflicting provisions contained in the UPICC (see Article 1.9 of the UPICC, point 6 of the Commentary). In the context of IICs, a more restrictive approach is warranted. Since IICs are typically negotiated individually between States and investors or arise from specific tender processes, the development of widely accepted usages across the "investment industry" is less common than in international commercial contracts. While sectoral or technical industry usages may be relevant for the interpretation of terms in IICs, they should not supersede the Principles in this Instrument or the express terms in the contract. In other words, usages that are not explicitly referenced in an IIC may serve a gap-filling role, but they should not override the terms of the contract or conflicting provisions contained in these Principles.

## CHAPTER 2. GENERAL PRINCIPLES APPLICABLE TO IICs

### A. Introduction

121. This Chapter deals with general principles that apply to all IICs. The Principles in this Chapter cover the following aspects of an IIC:

(1) Form,

(2) Interdependent contracts,

(3) Sustainable investment,

(4) Anti-corruption,

(5) Specific arrangements duly approved by competent bodies,

(6) Notice,

(7) Preamble to an IIC.

122. With respect to the form of an IIC, given the nature of IICs as complex, high-value, long-term contracts, Principle 4 sets out the requirement of writing for these contracts. This is a departure from Articles 1.2 and 2.1.1 of the UPICC, which deem that no specific form is required to create a binding contract (*i.e.*, a contract may be formed orally) and that a contract may be inferred from the conduct of the parties sufficient to show an agreement has been reached. Technology has evolved to where electronic communications such as e-mail and electronic signatures are now commonly used in the formation of binding contracts, and legal concepts such as "written form" have also evolved to take into account these developments. Principle 4 acknowledges these developments and recognises that the requirement that an IIC be in writing may be met by electronic communications. Principle 4 also acknowledges that, before a contract can come into force and bind the parties, it may need to comply with domestic law requirements that apply to it. Approvals may be required by competent bodies of the parties, such as the parliament in the case of the State party and the board of directors of the investor. A Model Clause provides that a modification to the IIC also needs to be made by an agreement in writing by the parties, and reiterates the need to obtain the required approvals to make any modification binding and effective.

123. Investment projects are often regulated by multiple contracts. Principle 5 recognises this and encourages parties to consider regulating the interdependence of the contracts, for instance with regard to interpretation, non-performance, invalidity, illegality or unenforceability, and choice of law and dispute settlement.

124. Principle 6 provides a general principle on sustainable investment, requiring parties to endeavour to pursue the investment in accordance with the highest international standards on sustainability and to incorporate adequate sustainability provisions in their contract. As explained in the Introduction (Section D), sustainability is a cross-cutting theme in this Instrument. Principle 6 provides general direction to the parties, accompanied by model language for the preamble of an IIC, while further Principles on sustainability are provided in Chapters 3, 5, and 7. Principle 7 covers anti-corruption, which is of particular significance in the investment context, where large-scale, long-term projects often involve public authority and substantial resources, creating heightened exposure to bribery and other corrupt practices. This Instrument only addresses corruption from a contractual perspective, including by offering a Model Clause.

125. IICs may provide for arrangements that may deviate from the regime generally applicable in the host State (*e.g.*, a more favourable tax regime or other investment incentives). Principle 8 clarifies that

such specific arrangements, if duly approved by the competent bodies of the host State (*e.g.*, the parliament), are valid and enforceable at the moment in which the IIC is signed. It is accompanied by a Model Clause whereby the State party declares and assures the validity and enforceability of such arrangements. Principle 9 addresses notice requirements. The UPICC adopt a flexible approach to notice, allowing communications to be made by any appropriate means. In the context of IICs, however, written notice – including electronic communications such as e-mail – is preferable to ensure legal certainty, traceability, and evidentiary clarity, given the long-term and complex nature of such agreements.

126. Section H provides model language for the preamble of an IIC, to guide its interpretation, application and performance. It recognises the special features of IICs, the need to balance competing interests and promote sustainable investment.

## B. Form

**Principle 4**

**(1) The IIC shall be in writing.**

**(2) The requirement that an IIC be in writing is met by an electronic communication if the information contained therein is accessible so as to be useable for subsequent reference.**

**(3) Nothing in paragraphs (1) and (2) above restricts the application of special requirements as to form contained in the applicable domestic law, or the relevant company constitutional documents of the investor, at the time of the conclusion of the IIC.**

**(4) The IIC shall be considered binding and in force when it is concluded and approved by the competent bodies of the host State and the investor, as may be applicable. Conclusion of the IIC may be confirmed by one of the means specified, or otherwise: physical signature, exchange of letters, secure electronic signature, or confirmation via electronic means such as electronic mail.**

**(5) Any subsequent modification to the IIC shall be by mutual agreement in writing. A modification shall be considered binding and in force when approved by the competent bodies of the host State and the investor, as may be applicable.**

**Relevant UPICC provisions**

Article 1.2 (No form required) and Article 2.1.1 (Manner of formation) of the UPICC

**Commentary**

127. In the context of international commercial contracts between private parties, it is generally accepted that contracts are valid regardless of the form (oral or otherwise) in which the consent of the contracting parties has been expressed (*e.g.*, Article 1.2 of the UPICC, Article 11 of the CISG).

128. On the other hand, when a contract is an IIC and involves a State party, the applicable law usually requires that such contracts be made in writing, and that certain procedures be followed. In addition, given their nature (high-value, complex, long-term), IICs are invariably concluded by way of written agreement. The IIC will also need to comply with special or mandatory requirements as to form contained in the

domestic law of the host State at the time of its conclusion. The relevant company constitutional documents of the investor may also require that the IIC be in written form. Further, where compliance with requirements for approval by the respective competent body of each party is necessary before the contract can be considered effective and binding, there may need to be confirmation of compliance with these requirements. This confirmation may take place by way of affixing physical signatures on a document, an exchange of letters, or electronic communication. See also Principle 14, which deals with purported confirmations and the addition or amendment of terms to the contract.

129. Paragraphs (1) and (2) are an adaptation of Article 7 of the UNCITRAL Model Law on International Commercial Arbitration.[3] Articles 1.2 and 2.1.1 of the UPICC do not apply in the context of IICs. For the meaning of "electronic communication", see Article 4 of the UN Convention on the Use of Electronic Communications in International Contracts.[4] Prior to this Convention, the Model Law on Electronic Commerce[5] had been adopted by UNCITRAL in 1996, with the aim of enabling and facilitating commerce conducted using electronic means by providing national legislators with a set of internationally acceptable rules.

130. With the advancement of technology and the evolution of language, the understanding of "written form" has evolved over time in international legal instruments, and may continue to evolve in the future. This may have an impact on how contracts are concluded and may equally apply to IICs.

131. In addition to requirements as to form, the IIC would also typically require approval by the competent body of the State, as well as the competent body of the investor.

132. It follows from the above that any modification of the IIC should also be in writing and be executed and approved by the same processes and comply with the same special requirements, if any, as the original contract.

**Model Clause**

This Contract may be modified by mutual agreement in writing. Writing includes electronic communications such as electronic mail. A modification may be confirmed by [*select one or more: physical signature, exchange of letters, secure electronic signature, or via electronic communications such as electronic mail*]. A modification shall be considered binding and in force when approved by the competent bodies of the Host State and the Investor, as may be applicable.

## C. Interdependent contracts

**Principle 5**

**When an IIC consists of multiple contracts, the parties may wish to consider these contracts' interdependence on one another and regulate the interplay among them.**

**Commentary**

[3] The UNCITRAL Model Law on International Commercial Arbitration (1985), as amended in 2006, is available at https://uncitral.un.org/en/texts/arbitration/modellaw/commercial_arbitration.

[4] The UN Convention on the Use of Electronic Communications in International Contracts (2005) is available at https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/06-57452_ebook.pdf.

[5] The UNCITRAL Model Law on Electronic Commerce (1996) is available at https://uncitral.un.org/en/texts/ecommerce/modellaw/electronic_commerce.

133. Often IICs reflect complex projects that are regulated by a plurality of contracts. These contracts may be entered into between the same parties and may regulate separate issues (for example, in a contract for development and production of mineral resources, the State and the investor may have entered into, in addition to the main agreement regulating the cooperation, separate contracts for the supply of power to the production facility, for the use of local infrastructure, etc.), they may be entered into with different entities within the same group of companies (for example, the ultimate parent company of the investor may be requested to issue a guarantee or a comfort letter), or they may be entered into with third parties (for example, with suppliers or subcontractors; the investment may be financed by credit facilities provided by a pool of banks; the investment may be financed in part by sale to third parties of part of the production, etc.).

134. Considerable complexity arises out of multiple contracts, whether they are between the same parties or with multiple parties. While all connected contracts are functionally and economically meant to contribute to the unitary purpose of the investment, each of them is an independent contract from a formal point of view. This formal fragmentation may, under certain circumstances, have undesirable effects, as it may lead to interpreting or performing each of the contracts on the basis of one individual contract and without having regard to the impact that this may have on the interpretation or performance of the interdependent contracts or of the overall project. Similarly, questions of illegality or invalidity, as well as contract breaches or supervening circumstances, may be addressed simply with respect to the contract in connection with which they arise, without considering how they affect the parties' interests in the context of the project in its entirety.

135. While it is correct to regard each contract as a self-standing legal relationship based on its own terms, this fragmentation may have detrimental effects on the project originally envisaged by the parties. Fragmentation may lead to binding one party to obligations arising under some of the contracts, without reflecting circumstances affecting other contracts that may have had a considerable impact on that party's overall position in the project. Furthermore, fragmentation may lead to dealing with overlapping obligations without regard to each other, thus creating inefficiencies and possibly inconsistent results.

136. Furthermore, in the case of a dispute between the parties, fragmentation may lead to multiple, parallel proceedings, which in turn has negative consequences in terms of effectiveness and possible inconsistencies – not only for the involved parties, but for the legal framework for investment in general.

137. To address these issues in the context of IICs, parties may wish to consider regulating the interdependence of the contracts so that their uniform economic purpose is reflected at the contractual level as well. Coordinating individual contracts may be easier to achieve when these contracts are entered into between the same parties, but in any case it requires thorough consideration by all the interested parties.

138. Parties may also wish to consider how multiple contracts shall be interpreted and, to that end, may wish to establish an order of preference or hierarchy among the various contracts. While all contracts should be written and interpreted in a systematic and coherent way so as to further the purpose of the IIC, inconsistencies may still arise between them. Often, interdependent contracts contain a clause specifying the hierarchy between the contracts or parts thereof. This may be useful to determine the parties' rights and obligations in case of inconsistency among the different contracts.

139. The parties may also wish to regulate the effects that non-performance of an individual contract may have on interdependent contracts. While all contracts form part of the IIC, if they are independent legal instruments, it may be unclear to what extent non-performance under an individual contract affects other contracts. The parties may wish to specify which obligations in each or certain of the interdependent

contracts are so important for the overall project that their non-performance should have effects on the other contracts. They may also wish to specify what these effects should be, on some or all of the interdependent contracts.

140. Similarly, in case of invalidity, illegality or unenforceability of an individual contract, it may be unclear how the interdependent contracts may be affected. Parties may want to specify the consequences for some or all of the other related contracts. While some aspects fall outside the scope of freedom of contract and are subject to the applicable law, parties to an IIC may wish to regulate the contractual effects that invalidity, illegality or unenforceability of an individual contract may have on the interdependent contracts. Depending on the relevance of the affected provision, parties may wish to provide that the other related contracts remain in force, even in the case of invalidity, illegality or unenforceability of an individual contract. To that end, they may regulate an obligation to adapt the interdependent contracts, or the way in which the IIC may be terminated.

141. In addition to considering regulation of interdependent contracts in the context of an IIC, parties should be aware of the advisability to subject the whole complex of contracts to the same applicable law (see Chapter 8, Section B). The applicable law has a crucial role for the scope and effects of a contract – not only because it may contain both mandatory rules and default rules that may correct or supplement the contract, but also because it informs the interpretation and construction of a contract. Thus, contracts containing the same language may produce different legal effects if they are subject to different applicable law. To avoid inconsistencies in the interpretation and performance of interdependent contracts, parties may wish to ensure that each contract contains a choice-of-law clause subjecting it to the same governing law as the others. Specific contracts may be subject to different law that is more appropriate for that particular type of contract. However, parties should carefully consider whether the choice of different law for some contracts may create difficulties in the interpretation or performance of the IIC as a whole.

142. Furthermore, it may be advisable to consider coordinating dispute resolution clauses (see Chapter 8, Section C). Interdependent contracts may give rise to overlapping disputes. Thus, resolving a dispute arising out of an individual contract may depend on, or have an impact on, the solution of a dispute arising out of another related contract. In order to ensure effectiveness and to avoid inconsistent results, parties may wish to choose compatible means of resolving disputes and establish the means for consolidating disputes arising out of different contracts relating to the same IIC. Parties may want to consider whether it is appropriate that the clauses contain a consent to cumulation of disputes arising out of (some of) the interdependent contracts.

**Model Clause** (to be inserted into each of the interdependent contracts)

1. Interdependence of contracts

This Contract is part of a complex of contracts between the Parties, all aimed at achieving [*purpose of the IIC*]. The following contracts and documents are deemed to be interdependent on one another (the "Interdependent Contracts"):

A. [*Name the contract*] with all annexes [*or only specific annexes*]
B. [*Name the contract*] with all annexes [*or only specific annexes*]
C. [*Name the contract*] with all annexes [*or only specific annexes*]
D. […]

2. Interpretation

All documents and provisions in the Interdependent Contracts shall be read so as to be consistent to the fullest extent possible. In the event of a conflict or inconsistency between them, the contract or

documents shall prevail in the order listed below, with the first document or provision listed having the highest precedence:

A. [*Name the contract* [*specific clauses of*]]
B. [*Name the contract* [*specific clauses of*]]
C. [*Name the contract* [*specific annexes of*]]
D. […]

3. Cross-default

If a Party fails to perform on one of the following obligations [*list of the obligations in each Interdependent Contract that are so important that their non-performance is meant to have effect on the other Interdependent Contracts*], the other Party may, after having given the non-performing Party a reasonable time to remedy the non-performance, declare that the non-performing Party is in default also on [*name the Interdependent Contracts for which cross-default is triggered*].

4. Severability

If any provision of the Interdependent Contracts, other than those listed below, is found to be invalid, illegal, or unenforceable, such provision shall be severed and the remaining provisions shall remain in full force and effect unless the invalid provision materially affects the purpose or performance of the IIC.

If any of the following provisions [*insert specific provisions in specific contracts*] is found to be unenforceable, the Interdependent Contracts shall be modified in a manner that preserves the original intent of the Parties as closely as possible.

If any of the following provisions [*insert specific provisions in specific contracts*] is found to be unenforceable, the Interdependent Contracts shall terminate immediately.

5. Choice of law

The interdependence of these contracts is reflected also in the choice-of-law clause contained in each of the Interdependent Contracts.

6. Dispute resolution

The interdependence of these contracts is reflected also in the dispute resolution clause contained in each of the Interdependent Contracts.

## D. Sustainable investment

**Principle 6**

**(1) In line with the objective of promoting sustainable investment under the IIC, the parties shall consider environmental, social, governance and human rights factors when making their investment decision. This principle is to be understood as implying commitments for each party.**

**(2) The parties shall endeavour to pursue the investment covered by the IIC in accordance with the highest international standards with regard to achieving the goals of sustainable development and climate change mitigation and adaptation.**

**(3) The parties shall therefore include in their IIC adequate provisions imposing commitments as to the social, economic and environmental benefits of the project, including obligations to protect human rights, the environment, the health and safety of**

**people and workers, local communities' protection and development, and the fight against corruption, all in accordance with the highest international standards.**

**Commentary**

143. This Principle reflects a general overarching commitment to sustainable investment. It is intended to be reflected in the preamble of the contract (see the model preamble language in Section H of this Chapter). Accordingly, it would have interpretative value and would inform the specific sustainability obligations included in the contract (for which detailed Principles are provided in Chapter 3 (Principle 11), Chapter 5 (Principles 20 to 22) and Chapter 7 (Principle 26)). Principle 6 aims at ensuring an adequate level of awareness and commitment of the parties on sustainable development. It must be stressed that this Principle is of equal importance for the host State and the investor. As a result, it shall not be conceived of as representing a specific and limited obligation applicable only to a specific party, but as reflecting an overall and joint commitment of the parties, which should be articulated in a manner proportionate to their capabilities.

144. This Principle thus gives general direction to the parties, which should include specific sustainability obligations in their IIC. The concept of "sustainability" should be understood as an overarching concept. It was favoured over ESG (Environment, Social and Governance) or CSR (Corporate Social Responsibility) since "sustainability" is considered broader, less affiliated with specific legal systems, and more future proof. Nonetheless, the concepts of ESG and CSR shall be viewed as forming an integral part of the notion of sustainability.

145. Parties should understand that, once sustainability commitments are incorporated in the IIC, they constitute contractual obligations that survive changes in political climate or regulatory reversals in the investor's home State or internationally. Furthermore, while Principle 6 uses the softer language "shall endeavour to pursue", this does not undermine the binding character of the specific sustainability obligations set out in Chapters 3, 5, and 7, which remain expressed in mandatory terms. Sustainability commitments should be catered to the capacity, means and size of the parties to the contract.

146. The definition of sustainability can be linked back to the UN Sustainable Development Goals (UNSDGs) and their future iteration(s). This ensures clarity as to the definition and a shared understanding of sustainability. It also ensures that the monitoring of measures implemented to comply with sustainability obligations be considered *vis-à-vis* the attainment of the UNSDGs (and future iterations).

147. An important aspect in the way that Principle 6 is formulated is the requirement to take into account the "highest international standards" since the topic is considered as too critical to envisage being satisfied by a reference to lower standards. Certain notions or expressions were explored as an alternative to "highest international standards", but in the end it was felt that this terminology was the most adequate to encompass modern expectations as to sustainable investment. It may very well be the case that, in certain situations, national standards applicable to the parties, such as regulations in the host country, will be stricter (more ambitious) than international standards. In such case, priority should be given to the stricter national standards.

148. It is recognised that it may not be easy to precisely identify the delimitation of "highest international standards" for at least two reasons. First, these standards can derive from a disparate pool of hard law,[6]

[6] Relevant hard-law instruments in the area of environmental protection include, but are not limited to, the Convention on Wetlands of International Importance; the World Heritage Convention; the Convention on International Trade in Endangered Species of Wild Fauna and Flora (CITES); the Convention on Long-Range Transboundary Air

such as international conventions, or from soft law,[7] such as guidelines or other advisory opinions issued by international organisations. This, by necessity, would make a conclusive list of such legal (and soft-law) instruments inappropriate in this Instrument. Second, these standards can rapidly evolve due to improvements in scientific research or growing concerns expressed by civil society. For this reason, the quest for the "highest international standards" has been expressed as an aspiration ("the parties shall endeavour to") rather than a firm and absolute obligation. It is expected that doing so will facilitate the acceptance level of the Principle, relying on the parties' spontaneous willingness to assess what is best in terms of sustainable goals for their investment. In making such an assessment, it is expected that the parties will articulate their sustainability commitments in a manner that is catered to their size and means (see on this point Chapter 3, Principle 11) and that they will adapt them to evolving national and international sustainability standards while making sure that their commitments will be also respected by their supply chain (see Chapter 5, Principle 22).

149. To address the above-described difficulties linked to a precise delimitation of "highest international standards", the parties are encouraged to identify, in their IIC or through an exhibit, the key sustainability standards and regulations that they deem applicable to their investment project and to the specific commitments they sought to include in their IIC (see also Chapter 3, the commentary to Principle 11). In such respect, relevant instruments to be referenced may run from due diligence to substantive standards, such as, but not limited to, the UN Guiding Principles on Business and Human Rights, UN Global Compact, the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, or other global, regional or sectoral instruments, such as those enacted by other international organisations, international lenders and multilateral or regional development banks, or those established by industry associations and similar entities[8] (for more details, see Chapter 3, Principle 11). It is acknowledged that there may be a complex hierarchy of norms in relation to sustainability standards, encompassing national, regional and international norms. The parties are therefore encouraged to perform a contextualised analysis of relevant norms with a view to identify and assess how best to handle potential conflicts between these norms, all towards interpreting and performing the specific obligations included in their IIC in a spirit of collaboration. In line with contemporary expectations and international practice, the Principle recalls a multifaceted conception of sustainability and extends to its environmental, social and governance dimensions, including governance and human rights, the health and safety of people and workers, environmental, climate change and biodiversity concerns, local community development, and the fight against corruption. Since it is one of the most critical concerns in today's world, climate change mitigation and adaptation is given a high



Pollution; the UN Convention on the Law of the Sea; the International Convention for the Prevention of Pollution from Ships; the Vienna Convention for the Protection of the Ozone Layer; the Montreal Protocol on Substances that Deplete the Ozone Layer; the Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and their Disposal; the Convention on Biological Diversity and the Cartagena Protocol on Biosafety to the Convention on Biological Diversity; the UN Framework Convention on Climate Change; the UN Convention to Combat Desertification; the Kyoto Protocol; the Convention on the Law of the Non-Navigational Uses of International Watercourses; the Rotterdam Convention on the Prior Informed Consent Procedure for Certain Hazardous Chemicals and Pesticides in International Trade; the Stockholm Convention on Persistent Organic Pollutants; the Minamata Convention on Mercury; the Paris Agreement; and the High Seas Treaty. Relevant hard-law instruments in the field of human, social rights, and governance include, but are not limited to, the International Covenant on Economic, Social and Cultural Rights; the UN Convention on the Elimination of All Forms of Discrimination against Women; the Convention on the Rights of the Child; the Forced Labour Convention; the Freedom of Association and Protection of the Right to Organise Convention; the Occupational Safety and Health Convention; and the UN Convention against Corruption.

[7] Relevant soft-law instruments include, but are not limited to, the Declaration of the UN Conference on the Human Environment (the Stockholm Declaration); the Rio Declaration on Environment and Development; the UN Guiding Principles on Business and Human Rights; the OECD Guidelines for Multinational Enterprises; the Agenda 2030 for Sustainable Development; UN Resolution (A/76/L.75) on the human right to a clean, healthy and sustainable environment; the Pact for the Future; the ILO Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy.

[8] See, for instance, the World Bank Environmental and Social Standards, the IFC Performance Standards, the Asian Development Bank Safeguard Standards, the UNESCO standards on cultural heritage or the Extractive Industry Transparency Initiative (EITI) Standard.

level of priority in the Principle. This is even more pertinent as climate change mitigation and adaptation are a typical example of a sustainability commitment where expectations are placed on States, through the adoption of adequate regulations, just as they are on private investors. This also serves the purpose of ensuring that environmental protection not be understood in a narrow sense as covering mainly the prevention of pollution.

### E. Anti-corruption

**Principle 7**

**An IIC shall not be procured or performed through corruption.**

**Relevant UPICC provision**

Article 3.3.1 (Contracts infringing mandatory rules) of the UPICC

**Commentary**

150. Integrity is a fundamental element in fostering a reliable investment environment. Anti-corruption considerations assume particular significance in the investment context. Large-scale, long-term investment projects often involve the exercise of public authority and substantial resources, creating heightened exposure to bribery and other corrupt practices. Such practices can distort investment decisions, undermine the legitimacy of the investment, and erode public confidence in both the host State and the investor. Combatting corruption is therefore essential not only to protecting shareholders and taxpayers, but also to preserving the integrity of the investment regime and the credibility of the State–investor relationship as a whole.

151. The focus in this Instrument is on contractual means to address corruption, without prejudice to any other means (*e.g.*, criminal law). In the UPICC, anti-corruption is addressed in the context of Article 3.3.1 (contracts infringing mandatory rules). Given the specific relevance of anti-corruption in the investment context, Principle 7 explicitly recalls that an IIC shall not be procured or performed through corruption.

152. It is strongly recommended that the parties to an IIC include an anti-corruption clause in their contract, such as the ICC Anti-corruption Clause ("the ICC Clause"),[9] with appropriate adaptations where necessary (see below).

153. The ICC Clause provides three options: a short text with the technique of incorporation by reference to the ICC Rules on Combatting Corruption 2023[10] (**Option I**), the incorporation of the full text of those ICC Rules (**Option II**), or a reference to a corporate compliance programme, as described in Article 11 of the ICC Rules on Combatting Corruption 2023 (**Option III**).

154. Options I and II of the ICC Clause are provided below. Option III is not included in this Instrument, given that it has been drafted as part of a broader compliance or business integrity clause, in which other risks, such as human rights, ESG, money laundering, anti-fraud and/or economic sanctions, are integrated, while these matters are addressed separately in other parts of this Instrument. It is advisable that the

[9] See ICC, ICC Anti-corruption Clause (2025 edition).

[10] The ICC Rules on Combatting Corruption (2023) can be found in the document ICC Anti-corruption Clause (2025 edition).

parties to an IIC adopt broader business integrity models and if this is the case they may refer to Option III and Article 11 of the ICC Rules on Combatting Corruption 2023.

**Model Clause**

**Option I**

1. Each Party hereby undertakes that, at the date of the coming into force of the Contract, it and its directors, officers or employees have not offered, promised, given, authorised, solicited or accepted any undue pecuniary or other advantage of any kind (or implied that they will or might do any such thing at any time in the future) in any way connected with the Contract and that it has taken reasonable measures to prevent subcontractors, agents or any other third parties, subject to its control or determining influence, from doing so.

2. The Parties agree that, at all times in connection with and throughout the course of the Contract and thereafter, they will comply with and that they will take reasonable measures to ensure that their subcontractors, agents or other third parties, subject to their control or determining influence, will comply with the ICC Rules on Combating Corruption 2023, which is hereby incorporated by reference into the Contract, as if written out in the Contract in full.

3. Each Party declares that it has no conflict of interest with respect to the execution of this Contract and agrees to promptly inform the other Party in the event that such a situation should arise during execution thereof.

4. If a Party, as a result of the exercise of a contractually-provided audit right, if any, of the other Party's accounting books and financial records, or otherwise, brings evidence that the latter Party has been engaging in material or several repeated breaches of the provisions of the ICC Rules on Combating Corruption 2023, it will notify the latter Party accordingly and require such Party to take the necessary remedial action within a reasonable time and to inform it about such action.

If the latter Party fails to take the necessary remedial action, or if such remedial action is not possible, it may invoke a defence by proving that by the time the evidence of breach(es) had arisen, it had put into place adequate anti- corruption preventive measures, as described in or comparable to Article 11 of the ICC Rules on Combating Corruption 2023, adapted to its particular circumstances and capable of detecting corruption and of promoting a culture of integrity in its organisation.

If no remedial action is taken or, as the case may be, said defence is not effectively invoked, the first Party may, at its discretion, either suspend the Contract or terminate it, it being understood that all amounts contractually due at the time of the suspension or termination of the Contract will remain payable, as far as permitted by applicable law. If the contract is suspended, the suspension is for such time the Party deems fit to allow the remedial action to be taken, and should the same not be effected, the Party may then terminate the Contract.

5. Any entity, whether an arbitral tribunal or other dispute resolution body rendering a decision in accordance with the dispute resolution provisions of the Contract [*see Chapter 8 of this Instrument*], shall have the authority to determine the contractual consequences of any alleged non-compliance with this Clause.

**Option II**

1. Each Party hereby undertakes that, at the date of the coming into force of the Contract, itself, its directors, officers or employees have not offered, promised, given, authorised, solicited or accepted any undue pecuniary or other advantage of any kind (or implied that they will or might do any such thing at any time in the future) in any way connected with the Contract and that it has taken reasonable measures

to prevent subcontractors, agents or any other third parties, subject to its control or determining influence, from doing so.

2. The Parties agree that, at all times in connection with and throughout the course of the Contract and thereafter, they will comply with and that they will take reasonable measures to ensure that their subcontractors, agents or other third parties, subject to their control or determining influence, will comply with the following provisions:

2.1. Parties will prohibit the following practices at all times and in any form, in relation to a public official at the international, national or local level, a political party, party official or candidate to political office, and a director, officer or employee of a Party, whether these practices are engaged in directly or indirectly, including through third parties:

A. Bribery: the offering, promising, giving, authorising or accepting of any undue pecuniary or other advantage to, by or for a public official and a director, officer or employee of an enterprise, or for anyone else with intent to improperly obtain or retain a business or advantage*, e.g.*, in connection with public or private procurement contract awards, regulatory permits, taxation, customs, judicial and legislative proceedings.

B. Extortion or Solicitation: the demanding of a bribe, whether or not coupled with a threat if the demand is refused.

Bribery often includes:

(i) kicking back a portion of a contract payment to Public Officials or to employees of the other contracting party, their close relatives, friends or third parties or

(ii) using intermediaries such as agents, subcontractors, consultants or other Third Parties, to channel payments to Public Officials, or to employees of the other contracting party, their relatives, friends or third parties.

Bribery has a narrower meaning than Corruption, which is sometimes used to include practically any perversion of integrity.

C. Trading in Influence: the offering or solicitation of an undue advantage in order to exert an improper, real, or supposed influence with a view to obtaining from a public official an undue advantage for the original instigator of the act or for any other person.

D. Laundering the Proceeds of the corrupt practices mentioned above: the concealing or disguising the illicit origin, source, location, disposition, movement or ownership of property, knowing that such property is the proceeds of crime.

E. Acting with a Conflict of Interest: Conflict of Interest with respect to the execution of this Contract is prohibited.

2.2. With respect to third parties, subject to the control or determining influence of a Party, including but not limited to agents, business development consultants; sales representatives; customs agents; general consultants; resellers; subcontractors; franchisees; lawyers; and accountants or similar intermediaries, acting on the Party's behalf in connection with marketing or sales, the negotiation of contracts, the obtaining of licences, permits or other authorisations, or any actions that benefit the Party or as subcontractors in the supply chain, Parties should instruct them neither to engage nor to tolerate that they engage in any act of corruption; not use them as a conduit for any corrupt practice; hire them only to the extent appropriate for the regular conduct of the Party's business; and not pay them more than an appropriate remuneration for their legitimate services.

3. If a Party, as a result of the exercise of a contractually-provided audit right, if any, of the other Party's accounting books and financial records, or otherwise, brings evidence that the latter Party has been engaging in material or several repeated breaches of Paragraphs 2.1 and 2.2 above, it will notify the latter Party accordingly and require such Party to take the necessary remedial action in a reasonable time and to inform it about such action.

If the latter Party fails to take the necessary remedial action or if such remedial action is not possible, it may invoke a defence by proving that by the time the evidence of breach(es) had arisen, it had put into place adequate anti-corruption preventive measures, as described in or comparable to Article 11 of the ICC Rules on Combating Corruption 2023, adapted to its particular circumstances and capable of detecting corruption and of promoting a culture of integrity in its organisation.

If no remedial action is taken or, as the case may be, the said defence is not effectively invoked, the first Party may, at its discretion, either suspend or terminate the Contract, without prejudice to the right of this Party to compensation for damages suffered as a consequence of the breach(es) above mentioned, it being understood that all amounts contractually due at the time of suspension or termination of the Contract will remain payable, as far as permitted by applicable law. If the contract is suspended, the suspension is for such time the Party deems fit to allow the remedial action to be taken, and should the same not be effected, the Party may then terminate the Contract.

4. Any entity, whether an arbitral tribunal or other dispute resolution body, rendering a decision in accordance with the dispute resolution provisions of the Contract [*see Chapter 8 of this Instrument*], shall have the authority to determine the contractual consequences of any alleged non-compliance with this Clause.

Commentary to the Model Clause (both Options)[11]

155. The Model Clause is written with the aim of achieving a balance between the interest of Parties to avoid corruption and their need to ensure the attainment of the objectives of the IIC. It builds on the doctrine of good faith, the presumption of innocence, good cooperation between parties, and the idea that many illicit practices can be remedied without bringing the contractual relationship to an end.

156. The wording of paragraph 1 mirrors that used in the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions (1997) and the UN Convention against Corruption (2003), as well as several other regional and domestic anticorruption legislation and guidance.

157. With regard to third parties, a party to an IIC is not required to prevent by all means all of its subcontractors, agents or other third parties, subject to its control or determining influence, from committing any form of corrupt practice. Each party shall, however, based on a periodical assessment of the risks it faces, put into place an effective corporate compliance programme, adapted to its particular circumstances; exercise, on the basis of a structured risk management approach, appropriate due diligence in the selection of subcontractors, agents or other third parties, subject to its control or determining influence; and train its directors, officers and employees accordingly. If a party becomes aware that the other party has committed material or several repeated breaches of the provisions of the ICC Rules on Combatting Corruption 2023, it will notify the other Party accordingly. Such breaches may come to light through an audit.

158. The reference in the Model Clause to a contractually-provided audit right does not, however, imply that an audit right can be easily obtained in all circumstances nor that such audit right will be suitable for

[11] For a detailed commentary to the ICC Clause, see ICC Anti-corruption Clause (2025 edition), pp. 8-11.

all situations. The parties to an IIC will have to determine if their relationship allows for an audit right, and if the circumstances surrounding the negotiation, execution and future implementation of the IIC warrant the need for such right.

159. If a party fails materially or on several repeated occasions to comply with the anti-corruption clause incorporated in the IIC, the non-complying party will first be given the opportunity to remedy the non-compliance. Such party will also have the opportunity to invoke as a defence that it has put into place adequate anti-corruption preventive measures, as provided by Article 11 of the ICC Rules on Combatting Corruption 2023. The anti-corruption preventive measures will be adapted to the particular circumstances and capable of detecting corruption and of promoting a culture of integrity in its organisation. If the party allegedly infringing the provisions of the ICC Rules on Combatting Corruption 2023 does not remedy the situation within a reasonable period of time or if no such remedy is possible, and no defence of adequate anti-corruption preventive measures is effectively invoked, the other party will have the right, at its discretion, to suspend the IIC or terminate it, it being understood that the amounts contractually due at the time of suspension or termination will remain payable, as far as permitted by applicable law. When the other party exercises its right of suspension or termination, it bears the full burden of proof that a breach or breaches of the provisions of the ICC Rules on Combatting Corruption 2023 has taken place. Applicable law may determine whether the party may be held accountable for a breach or breaches of the provisions of the ICC Rules on Combatting Corruption 2023.

## F. Specific arrangements duly approved by competent bodies

**Principle 8**

> **Specific arrangements agreed for an IIC are valid and enforceable upon the coming into force of the IIC to the extent that they have been duly approved by the competent bodies of the host State. They remain in force according to the applicable law and the principles set out in Chapter 6.**

**Relevant UPICC provision**

Article 1.4 (Mandatory rules) of the UPICC

**Commentary**

160. This Principle is meant to clarify that Article 1.4 of the UPICC (mandatory rules), according to which the UPICC do not restrict the application of applicable mandatory rules, is not intended to restrict the application of specific arrangements duly approved in accordance with the applicable law.

161. Often, IICs are subject to the law of the host State. In turn, the law of the host State reserves various issues to the discretion of administrative bodies and excludes these issues from the sphere of contract freedom. Also, certain issues, such as taxes, may fall within the exclusive competence of certain bodies, such as the parliament. At the same time, in order to facilitate foreign investment, IICs and public tender documentation may stipulate, as contract terms, specific arrangements for these issues that are not necessarily consistent with the regime generally applicable in the host State (for example, the IIC may provide for a more favourable tax regime or other incentives).

162. Assuming that the specific arrangement has been duly ratified by the competent bodies (usually, the parliament) and that it was offered in accordance with the applicable rules on, *e.g.*, competitive bidding, the ratification renders the specific arrangement valid and applicable. However, the incongruity with the generally applicable regime remains.

163. The discrepancy between the specific arrangement and the generally applicable regime may create some uncertainty as to the applicability of the specific arrangement, when the law applicable to the IIC (often, the contract law of the host State) is interpreted in light of the UPICC. In particular, according to Article 1.4, the UPICC (and, *a fortiori*, the contract) may not derogate from mandatory rules of the applicable law.

164. The proposed contract language confirms that any such specially-agreed terms duly approved by the competent bodies (such as the parliament) are valid and enforceable at the moment in which the IIC is signed – notwithstanding that they may deviate from rules of the host State that are generally applicable in that area.

165. The proposed contract language differs from stabilisation clauses (see Chapter 6, Section B) because it does not regulate the future validity and enforceability of the contract terms. It is a declaration by the State that the agreed terms of the specific arrangement have been approved and are valid and enforceable at the time of the coming into force of the contract. It is meant to draw the parties' attention to the necessity to comply with the applicable requirements to ensure effectiveness of any agreed specific arrangements.

166. The effectiveness of the proposed language assumes that the bodies signing the IIC have the competence to bind the State in respect of the investment and the specific arrangement (see Chapter 3, Section D).

167. The proposed language is modelled on the widespread practice, for international commercial contracts, to use so-called "representations and warranties". The purpose of these clauses is to allocate specific risks between the parties by clearly specifying what each party is guaranteeing to the other. This contract practice has its origin in the common law legal tradition, where a representation and a warranty each have different legal effects. It has become customary to use this terminology in international commercial contracts irrespective of whether the contract is subject to a domestic law belonging to the common law tradition, even though interpreting the clauses in light of the laws belonging to different legal families may in some cases create unexpected results. While harmonisation instruments take recognised practices into consideration, to ensure neutrality, they do not utilise legal terms that belong to specific legal traditions. Therefore, the proposed language is modelled on the contractual practice to include "representations and warranties", but utilises the neutral terminology "declarations" and "assurances".

**Model Clause**

| |
|---|
| The terms of the Investment, and particularly the terms regulated in [*specify the contract provisions containing terms that deviate from the law generally applicable in the Host State*], have been specifically approved by [*the competent bodies of Host State*]. [*The State Party*] declares and assures that, at the time of the coming into force of this Contract, they are valid and enforceable under its laws. |

## G. Notice

**Principle 9**

**(1) Where notice is required, it shall be made in writing.**

**(2) A notice is effective when it reaches the person to whom it is given.**

**(3) For the purpose of paragraph (2), a notice "reaches" a person when delivered at that person's place of business or mailing address or by any other means agreed by the parties.**

**(4) For the purpose of this Article, "notice" includes a declaration, demand, request or any other communication of intention.**

**Relevant UPICC provision**

Article 1.10 (Notice) of the UPICC

**Commentary**

168. Article 1.10(1) of the UPICC lays down the principle that notice or any other kind of communication of intention (declarations, demands, requests, etc.) required by the UPICC is not subject to any particular requirement as to form, but may be given by any means appropriate in the circumstances.

169. However, in the context of IICs, it is common and preferable that notice be made in writing. Requiring written notice promotes legal certainty, traceability, and evidentiary clarity. It is also in line with Principle 4, which requires IICs themselves to be in writing (in deviation from the UPICC, which do not require a particular form for international commercial contracts) since IICs are typically long-term, high-value and complex contracts.

170. Notice in writing includes electronic communication such as e-mail.[12] Which means of notice are appropriate in a specific case will depend on the circumstances (*e.g.*, the availability of various modes of communication) and the importance and/or urgency of the message to be delivered.

171. Article 1.10 of the UPICC adopts the so-called "receipt" principle, meaning that notice is not effective unless and until it reaches the person to whom it is given. For notice in writing, it requires the message to be delivered to the addressee personally or to its place of business or (electronic) mailing address. It is not necessary for the communication to come into the hands of the addressee; it can also be handed over to an employee authorised to accept it. For notice by electronic mail, pursuant to the UN Convention on the Use of Electronic Communications in International Contracts, receipt occurs when the electronic communication becomes capable of being retrieved by the addressee at the designated electronic address; this is presumed to occur when the communication reaches that address.[13] The same rules should apply in the investment context. The Model Clause below translates these rules into contractual language. It is important that parties specify in advance to whom notice should be addressed (*i.e.*, who qualify as representatives). Such specification should be included in the IIC itself, or be notified to the other party separately.

172. For notice requirements in the context of change of circumstances, see Chapter 6; for termination, see Chapter 7; for dispute settlement, see Chapter 8.

**Model Clause**

[12] For the meaning of "electronic communication" see Article 4 of the UN Convention on the Use of Electronic Communications in International Contracts (2005), available at https://uncitral.un.org/sites/default/files/media-documents/uncitral/en/06-57452_ebook.pdf. See also the commentary to Principle 4.

[13] See Article 10(2) of the UN Convention on the Use of Electronic Communications in International Contracts (2005).

Any Notice required under this Contract shall be in writing and shall be delivered by hand, courier, registered mail, e-mail or other agreed means to the address of the relevant Party specified in this Contract.

Notice shall be sent for the attention of the representative(s) of the Parties specified in this Contract, or to such other representative(s) as a Party may notify in writing.

Notice shall be deemed to have reached the relevant Party:

(a) if delivered by hand, on the date of delivery;

(b) if sent by courier or registered mail, on the date of receipt;

(c) if sent by electronic mail, on the date at which it becomes capable of being retrieved by the addressee at the e-mail address designated in this Contract.

For the purposes of this clause "Notice" includes a declaration, demand, request or any other formal communication of intention.

[Informal communications, including meetings or oral discussions, shall not constitute notice for the purposes of this Contract unless confirmed in writing in accordance with this Article.]

## H. Preamble

173. The preamble to an IIC is important to guide the contract's interpretation, application and performance. The model preamble language provided here below recognises the special features of IICs and the need to balance competing interests. Particular emphasis is placed on the importance of balancing adequate investment protection with the State's right to regulate in the public interest and on promoting sustainable investment, in line with Principle 6.

### Model Preamble Language

1. Whereas recognising the role of foreign investment in the contribution to development, expected generation of employment, transfer of technology, and other benefits for the host State;

2. Whereas recognising the long-term nature of the contract and the peculiarities associated with the contract due to elements of public interest involved;

3. Whereas recognising the need to provide adequate protection to investment through the terms of contract agreed by the parties and balancing them with the right of the State to undertake legitimate regulations in the public interest;

4. Whereas development through international investment cannot be conceived of without taking into account the rising importance of sustainability, which requires supporting the social, economic and environmental benefits of the project and, notably, protecting human rights, the environment, the health and safety of people and workers, as well as sustaining good governance, local community development and the fight against corruption, in accordance with the highest international standards;

5. Whereas the focus on sustainability shall include adequate measures for climate change mitigation and adaptation;

6. Whereas freedom of investment must be guaranteed as long as it takes place within the applicable legal framework and the relevant international standards;

7. Whereas an important objective of the Contract is to ensure compliance with international obligations on human rights, environmental protection, and the fight against corruption;

8. Whereas the present Contract recognises that the Parties shall endeavour to pursue the highest international standards with regard to achieving the goals of sustainable development, corporate social responsibility and good governance;

9. Whereas the Investor and the State recognise the importance of cooperating in good faith towards the goals expressed above and the implementation of this Contract;

10. Whereas predictability and stability of the contractual relationship is essential for the successful completion of the contract;

Commentary to the Model Preamble Language

174. The task of the preamble is to guide the interpretation, application and performance of the IIC. It does not provide specific obligations. The obligations would be contained in the text of the contract.

175. The first preambular paragraph recognises the role of foreign investment in contributing to development in the host State. Additionally, foreign investment is expected to generate employment, facilitate technology transfer, and provide other benefits to the host State. These considerations are among the reasons why protection is given to foreign investors.

176. The second preambular paragraph recognises the peculiarities of IICs and their long-term nature. The relationship between the parties needs to be stable so that the parties can perform their part of the contract. Also, due to the long-term nature of the contract and the nature of the activities undertaken under the contract, issues of sustainability, human rights, and protection of the environment would be especially pertinent.

177. The third preambular paragraph specifies the goal of balancing the competing interests involved in IICs. On the one hand, there are the principle "*pacta sunt servanda*" and a need to provide adequate protection to investors through stability of the contractual relations and physical protection of the assets and personnel employed. On the other hand, the freedom of States to adopt and change regulations shall not be excessively constrained. This preambular paragraph is given an expression in the form of stabilisation and renegotiation clauses, contained in Chapter 6.

178. The fourth preambular paragraph goes to the very heart of the Instrument. Parties shall promote sustainability by including provisions as specified in the Instrument in their IIC, and the preamble will guide their interpretation, application and performance. The provisions on sustainability are broad and would require supporting the social, economic and environmental benefits of the project and, notably, protecting human rights, the environment, the health and safety of people and workers, good governance, local community development, and the fight against corruption, in accordance with the highest international standards. Chapters 3 and 5 stipulate the obligations relating to sustainability.

179. The fifth preambular paragraph singles out climate change to emphasise its importance. This is also reflected in Principles 6, 11, 20, and 22.

180. The sixth preambular paragraph specifies that the protection granted to foreign investment is available only as long as the investor is acting within the permissible legal framework at the national and international level. This framework includes obligations arising out of sustainability and beyond, to the extent provided in this Instrument (see *e.g.*, Chapter 5, Section D).

181. The seventh preambular paragraph emphasises the need to comply with international obligations in relation to human rights, environmental protection, and the fight against corruption. The fight against corruption is an essential and integral aspect of this Instrument. It has been specifically stipulated in Principle 7.

182. The eighth preambular paragraph stipulates that the parties shall endeavour to pursue the highest international standards with regard to achieving the goals of sustainable development, corporate social responsibility, and good governance. These are obligations on all parties to IICs and have been specifically provided in Principle 6 and Chapters 3 and 5.

183. The ninth preambular paragraph focuses on performance of the IIC. It indicates that the parties shall perform their obligations in good faith. Principle 15 specifies this obligation in the contract. Good faith continues to be the guiding factor that applies to the entire Instrument.

184. The tenth preambular paragraph is dedicated to the importance of predictability and stability of the contractual relationship to ensure successful completion of the IIC. The obligations of the parties under the contract shall not be interpreted and applied in a manner that disrupts predictability and stability. Being long-term contracts involving substantial financial investments, risks and exposure to the investor, predictability and stability are essential.

# CHAPTER 3. FORMATION

## A. Introduction

185. This Chapter is devoted to the phase preceding the conclusion of the IIC. IICs are usually concluded following an extensive pre-contractual process that may vary depending on the type and size of the investment project. Some IICs may be formed following individual negotiations between the parties, others may be based on competitive biddings within the framework of a public tendering process, yet others may be based on a combination of both methods.

186. Depending on the process leading to the conclusion of the IIC, duties between the parties may arise to a variety of extents. In the UPICC, this phase is addressed specifically in Chapter 2, Section 1, which in turn relies on certain general provisions laid down in Chapter 1. Many of the principles contained in Chapter 2 of the UPICC may be applied to IICs without need for adjustment. These principles will apply to the extent they are relevant and are not specifically mentioned here. Where the process leading to the conclusion of IICs requires some specification of the UPICC or adjustments to certain provisions, these are made in this Chapter, as briefly presented below.

187. In the investment context, the need to balance regulatory freedom with the requirement of predictability is particularly important. This is reflected in this Chapter by Principle 10, which specifies the duty of good faith in the pre-contractual phase when one of the parties is a State party. As explained in the commentary thereto, Principle 10 specifies certain UPICC provisions. It is accompanied by a Model Clause that permits addressing the issue contractually.

188. Furthermore, it is of particular importance to ensure that IICs are concluded after a thorough evaluation of the environmental, social and human rights impact of the investment. To ensure that this is carried out in a manner consistent with the highest international standards, Principle 11 provides a system for extensive corporate sustainability due diligence to be carried out by the investor in cooperation with the State party. Principle 11 does not specify or adjust any UPICC principles, but is an addition thereto. It is accompanied by a Model Clause permitting parties to incorporate a sustainability due diligence requirement in their contract.

189. In IICs, due to the public nature of one of the parties, special attention must be devoted to the issue of the parties' legal capacity. The UPICC regulate certain aspects of legal capacity in Chapter 2, Section 2, which in turn relies on certain general provisions laid down in Chapter 1. These are specified and supplemented by Principle 12 in this Chapter, which reflects the particular aspects relevant to IICs. Rather than being a normative provision, Principle 12 recommends that the parties clarify the matter contractually. A Model Clause is suggested.

190. The need to create certainty about the scope of the parties' respective rights and obligations is particularly important in IICs. As explained in the commentary to Principle 13 below, the UPICC contain certain principles on the scope of the contractual obligations and the impact that the pre-contractual phase may have thereon. To enhance certainty, these UPICC provisions are specified and supplemented by Principle 13. Rather than being a normative provision, Principle 13 recommends that the parties clarify the matter contractually. A Model Clause is suggested.

191. In IICs, as reflected in Principle 4 above, there is a written form requirement. This is a derogation from the UPICC. This Instrument also recognises that all the terms of the IIC are contained in the written contract, which forms the entire agreement between the parties. Following on from the requirement of writing and the principle that the contract contains the entire agreement between the parties (Principle

13), Principle 14 in this Chapter refers to the situation where a written document is sent following the conclusion of the terms of the IIC and purporting to confirm the contract. In such a situation, Principle 14 makes clear that if any additional or different terms are contained in the purported confirmation, such terms will need to undergo the same approval process required of an amendment to the contract. A Model Clause is suggested. Regarding terms deliberately left open, there is no need to adjust the relevant UPICC provision, but a Model Clause tailored to IICs is suggested.

## B. Freedom to negotiate

**Principle 10**

> **Throughout the negotiations, each party shall act in accordance with good faith and fair dealing. In this context, this includes the duty to cooperate and to not intentionally mislead, accepting that each party is entitled to achieve its reasonable objectives. In particular, the change of policy of the negotiating parties during the negotiation process shall not by itself be considered to be contrary to good faith or fair dealing.**

**Relevant UPICC provisions**

Articles 1.7 (Good faith and fair dealing), 1.8 (Inconsistent behaviour) and 2.1.15 (Negotiations in bad faith) of the UPICC

192. Under Article 1.7 of the UPICC, parties must act in accordance with good faith and fair dealing in international trade. Under Article 1.8 of the UPICC, parties are under a duty to conduct themselves consistently and to not contradict their previous statements or actions upon which the other party may have relied.

193. Furthermore, under Article 2.1.15 of the UPICC, while parties who engage in contract negotiations are not bound to reach an agreement, negotiations in bad faith (including negotiating without having the intention of concluding a contract) may expose the party who negotiated in bad faith to liability for damages.

**Commentary**

194. Principle 10 is meant to specify, in the context of negotiations of IICs, the scope of the duty to act in accordance with good faith and fair dealing that applies under the UPICC.

195. IICs may be formed on the basis of individual negotiations, of competitive biddings, or following a hybrid process. The process leading to formation of the contract may create duties between the parties to a variety of extents, under both domestic law and investment law.

196. Under domestic law, the parties' conduct in the negotiations may create expectations that may enjoy different degrees of protection. While some domestic law privileges contractual freedom and emphasises that each party is free to pursue its own interests during negotiations, other domestic law emphasises the need to act in good faith during negotiations and protect expectations that one party's conduct may have created in the other party. Under Articles 1.8 and 2.1.15 of the UPICC, the parties' expectations enjoy a high degree of protection.

197. Within investment law, there is an increasing awareness of the need to balance the public interest and the investors' interest. Among other things, this regards the need to ensure that the host State enjoys

a regulatory space for legitimate governmental interventions, even when this may affect the investors' interests. This may need coordination with the protection of expectations flowing from the duty to act in good faith, which may be seen as a restriction to the scope of public interest regulatory activity in the pre-contractual phase. An analogy could be made with the rationale contained in a comment made by the UNIDROIT-IFAD Legal Guide on Agricultural Land Investment Contracts (ALIC Guide) in the context of stabilisation clauses.[14] According to the ALIC Guide, extensive protection of expectations by means of stabilisation clauses "could constrain the implementation by a government of deserving social, environmental, or economic measures ... [as] States may have to exempt projects from the new measures; [or] if States must bear the costs incurred by said measures, they may be discouraged from acting in the first place, particularly where public finances are under strain".[15] Applying this rationale to the pre-contractual phase, it results that expectations created under negotiations need to be balanced with the regulatory space afforded to States.

198. While competitive biddings generally follow a regulated procedure, individual negotiations of IICs may sometimes last several years, and during this time the host State may be faced with developments that may require regulatory measures to safeguard the public interest. Such regulatory measures may affect the IIC negotiations, contradicting or restricting the host State's previous negotiating position.

199. Furthermore, States are free to develop their policies – for example, to allocate resources to the development of a certain sector, or to give priority to certain interests. Often, to facilitate foreign investment, a State may informally suggest the possibility of adjusting the tax treatment of the investment, or of giving similar incentives. If, during negotiations (that can sometimes last years), the State changes strategy or policy, it may lose interest in pursuing the negotiations or in granting these incentives.

200. Not only States but also investors are free to change their business strategy – for example, to leave a certain market, or to concentrate their resources on a certain sector that promises to be profitable.

201. Furthermore, a contract that has been negotiated and drafted in its final form may need approval by each of the parties' competent bodies, such as, for State parties, the executive or parliament, and, for commercial parties, the board of directors. The outcome of the approval process is not always predictable – when negotiating an IIC, therefore, sometimes it is not possible to predict that its terms will be approved by the competent bodies.

202. The protection of expectations granted by the UPICC needs to be reconciled with the above-mentioned need to safeguard the host State's regulatory scope, as well as both parties' freedom to change strategy or policy, and the unpredictability of the approval process.

203. When transactions of considerable complexity are involved, such as with IICs, it is quite frequent that, after prolonged negotiations, the parties sign a document such as a "Preliminary Agreement", "Memorandum of Understanding", or "Letter of Intent" containing the terms of the agreement reached thus far, but at the same time stating their intention to provide for the execution of a formal or definitive document at a later stage ("Subject to Contract", "Formal Agreement to follow"). Assuming that the parties did not consider their contract as already being concluded and the execution of the formal or definitive document only as confirmation of the already complete agreement, and that the wording makes clear that the parties, or only one of them, do(es) not intend to be bound unless the formal document has been drawn up, there will be no contract until that time, even if the parties have agreed on all the relevant aspects of

[14] On stabilisation and renegotiation clauses, see Chapter 6.B of this Instrument.

[15] ALIC Guide, para. 4.138.

their transaction. These documents often contain a clause specifying that failure to reach an agreement does not expose any party to liability.

204. Such contract practice is recognised in Article 2.1.13 of the UPICC. However, this Article only provides that the parties are not deemed to be bound by the contract that was being negotiated. It does not explain the relationship with the above-mentioned Article 2.1.15(2), which imposes damages for having negotiated without the intention to conclude the contract.

205. A party may have initiated negotiations without necessarily having the certainty that the contract will be approved. Having inserted language specifying that the contract is not binding until it has been formalised (including approval by the competent bodies), the party may have assumed that it had informed the other party that it maintained the discretion to evaluate whether the result of the negotiations fit that party's strategy or policy at any time. This, however, may turn out not to be sufficient to prevent the application of Article 2.1.15(2) of the UPICC on damages.

206. The contract language proposed below clarifies that good faith and the duty to be consistent under Article 1.8 of the UPICC do not restrict a party's freedom to develop its original negotiating position (including contradicting it by exercising regulatory power in the public interest, or by acting on a change in policy or strategy). Neither does it prevent the competent bodies from independently evaluating the contract for approval.

207. Furthermore, the proposed contract language clarifies that the parties are not bound by pre-contractual documents describing the envisaged transaction if the pre-contractual documents made clear that they were subject to formalisation in a final document.

208. Because the rationale of the declaration is relevant for each of the parties, the clause is drafted as a reciprocal declaration.

209. In IICs that are concluded on the basis of competitive bidding, the dynamics of contract formation may be different. The tender documents usually regulate the tender process in detail, and bidders are often required to provide security, thus regulating the consequences of a withdrawal from the process by the bidders. Similarly, bidders may rely on their right to enter into the contract, if they win the competitive bidding, subject to the applicable law. The suggested contract language, therefore, may not be relevant in the context of competitive bidding.

**Model Language for pre-contractual documents**

Suggested contract language for pre-contractual documents such as Letters of Intent (LoI) or Memoranda of Understanding (MoU) entered into in the course of individual negotiations:

> Throughout the negotiations, each Party shall act in accordance with good faith and fair dealing. In this context, this includes the duty to co-operate and to not intentionally mislead, accepting that each is entitled to achieve its reasonable objectives.
>
> In particular, the change of policy of the negotiating parties during the negotiation process shall not by itself be considered to be contrary to good faith or fair dealing, subject to such restrictions as are expressly agreed upon by and between the Parties [*in this Contract*].

A Party may not be held to have acted in breach of a duty of good faith if, prior to the conclusion of a binding contract, it departs from its negotiating position or if it fails to obtain the approval of the competent body or bodies, if so required.

Unless otherwise provided, the terms of this [*MoU/LoI/etc.*] are not binding on the Parties, and are subject to a [*name of definitive agreement/formal agreement*] being executed between them and duly approved by the competent bodies.

### C. Sustainability due diligence in the pre-contractual phase

**Principle 11**

**(1) The investor, in cooperation with the State party, must perform a sustainability due diligence assessment, including a component on climate change, with the double aim of preventing and minimising risks thereto to the extent possible, as well as putting in place adequate mitigation measures concerning adverse effects that could be avoided. This principle applies at the preparation phase of the investment, during the implementation of the investment and for a reasonable period of time after the investment has ended.**

**(2) As part of the sustainability due diligence assessment, the investor is responsible for conducting an environmental, social and human rights impact assessment report for the project that includes a management plan.**

**(3) An essential component of sustainability due diligence is the requirement to consult with potentially affected stakeholders, including local communities and Indigenous populations, to the extent the investment has the potential to affect these communities and populations. Such consultation shall be performed according to the free, prior, and informed consent principle, which ensures the active involvement of local communities and Indigenous peoples in decision-making processes related to projects or activities that may significantly impact their lives, territories, or resources.**

**Commentary**

210. The first paragraph of this Principle establishes that the investor, in cooperation with the host State, should carry out a corporate sustainability due diligence assessment. Such assessment should be understood to encompass an assessment of the environmental (including climate change), social and human rights impact of the investment in a manner consistent with the highest international standards. Such due diligence shall be informed by relevant soft-law instruments, including, but not limited to, the UN Guiding Principles on Business and Human Rights, UN Global Compact, and the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, which provide for corporate due diligence obligations with respect to human rights, social and environmental protection. Reference may also be made, when chosen or required by the parties or by lenders, to the instruments, standards and guidelines adopted by global, regional or sectoral international organisations, including development banks, industry associations or other entities, and where applicable, to national and regional instruments setting out advanced standards in the field.

211. In line with the highest international standards and relevant soft-law instruments, the corporate sustainability due diligence on the environmental, social and human rights impact of the investment should address in particular issues of possible damage to persons, the natural environment and depletion of

biodiversity (including due to emergencies or accidents); security and safety of workers (including access to a decent livelihood and basic services); critical labour relations and gender issues (including non-discrimination in the workplace and anti-harassment policies); the contribution to the social and economic development of local communities (access to a decent livelihood and basic services, social and cultural infrastructures, local training and recruitment, local sourcing policies) and no or minimised interference with land rights and property, livelihood, social and economic activities and access to resources (such as local markets and production sites, agriculture, fisheries, food, water, sanitation), culturally and historically significant traditions or locations and religious or sacred sites; resettlement of persons and local communities (if a temporary or permanent displacement of people is necessary); decommissioning and rehabilitation measures upon closure of the operations and abandonment of the investment site; and other issues as they may be relevant under the international standards specifically agreed between the parties.

212. In addition, special attention should be paid to due diligence as to the project's potential impact on climate change, given the specific nature of the phenomenon and the priority that must be given to it. Due diligence must take into account the so-called "best available science", the standards of which emerge, *inter alia*, from the work of the Intergovernmental Panel on Climate Change (IPCC), reflecting the consensus of the scientific community on the subject. Corporate due diligence obligations may vary according to the economic activity that is the subject of the project, also depending on the degree of risk of occurrence of adverse effects on the environment and the local community by the activity in question. Particular attention shall be paid to projects involving the extraction of fossil fuels such as gas, oil and coal, in light of national emission reduction targets and the climate goals of the Paris Agreement. In the context of cooperation between the State and the investor during the sustainability due diligence process, and when establishing climate commitments to be included in the IIC, the State should take into consideration that it may conclude other contracts, including with different investors, for activities that may also affect climate objectives. The commitments under the IIC should therefore be balanced, with investor obligations relating to climate being limited to activities within its sphere of control.

213. Due diligence considerations should operate as early as possible in the development, and at the latest prior to the commencement, of a new project, given that environmental, social and climate-related risks can increase or be mitigated already at the initial stage, and a proper assessment of such risks may help shape the content of the contract and of the sustainability commitments therein, or of other agreements related to the project (see Chapter 5, Section D.2). Contractual practice indicates that corporate sustainability due diligence, as a private-law process, usually interacts with impact assessment procedures legislated by the host State as a matter of public law, which provide for certain sustainability due diligence requirements to be complied with after the conclusion of contract and prior to the commencement of the project as a condition precedent for the investor to obtain the relevant approvals by the competent authorities in the host State and start the operations. In such case, the evaluations and assessments carried out by the investor under the corporate sustainability due diligence operated prior to the conclusion of the contract should be incorporated into and integrated with the due diligence process mandated by State law.

214. The first step in conducting appropriate due diligence in the field should consist of the identification and assessment of the nature of the project's potential social, environmental and climate-related impacts, as well as its repercussions on human rights for the investment site and the neighbouring areas. The reason is that of facilitating early appreciation of the risks of adverse impacts on key stakeholders, based on the specific context of activities regulated by any given contract. Typically, this entails a comprehensive assessment of the scope, context and related factors involved in the project and those potentially affected by it, to the extent possible. This includes identification of the potentially affected stakeholders, cataloguing the relevant international environmental and social standards and issues, and projecting how the proposed project activity and associated business relationships may adversely affect those identified.

215. Where the investor's activity inevitably causes or is likely to cause an adverse impact that can be mitigated or prevented, it should take the necessary steps to prevent or cease the continuation of the adverse impact and implement adequate mitigation measures to minimise the consequences that cannot be avoided. In this context, it is recalled that the scope of sustainability obligations should be applied proportionately to the risk, size, and nature of the project. The aim is to avoid situations where small or low-impact projects are subject to disproportionate obligations, which may be impractical for both the State and the investor.

216. The second paragraph of this Principle lays out the investor's responsibility of conducting, within the broader corporate sustainability due diligence, an environmental and social impact assessment (ESIA), with a component on climate change, and accordingly a management plan, as an integral part of the investor's due diligence duty, which should include a local community resettlement plan (when necessary) and a decommissioning and rehabilitation plan upon relinquishment of the site at completion of the Project. Such a duty represents a key aspect of the interconnection between the corporate and State dimension of due diligence obligations for the investor and the host State relevant to any given foreign investment in the scope of an IIC. Indeed, the submission of an ESIA report by the investor normally falls within the framework of an authorisation regime, which is compulsory for the host State under international law. This stresses the importance for the host State to set up an authorisation regime providing for the ESIA, into which the evaluations and risk assessment conducted by the investor under its corporate due diligence should be incorporated, as a key precondition for the issuance of the authorisation of the investment in question. In the unlikely event in which the host State would not provide for an authorisation regime requiring an ESIA, under the corporate dimension of due diligence, the investor should raise the issue at the negotiating stage.

217. The environmental impact assessment (EIA) requirement has been recognised as a pillar of international environmental law since the 1972 UN Stockholm Conference. It consists of the requirement – within a compulsory authorisation regime to be put in place by States, through their local entities – for the investor to produce a written report for use in decision-making by local authorities, for purposes of providing decision-makers with insights into the environmental implications of the proposed economic activity, and/or their potential alternatives, ensuring that governmental decisions are fully informed concerning the environmental impact of any proposed investment subject to authorisation, also establishing a framework for the involvement of relevant stakeholders in the decision-making process. First developed in relation to international environmental law, generally, the impact assessment approach has more recently been adapted in relation to climate change. The IPCC's Preliminary Guidelines for Assessing Impacts of Climate Change (1992) provide for a multi-stage general framework for conducting an assessment of climate change impact and adaptation. Climate change impact, vulnerability and risks assessments are crucial for effective adaptation planning and implementation.[16]

218. Similarly, the impact assessment methodology has been progressively extended from a purely environmental dimension to the social sphere in pursuit of a more holistic approach, such as by including the assessment of the human rights, social, economic and cultural impact of the investment on the local community.[17] As a consequence, such methodology requires to an ever greater extent that the investor and the State move from EIAs to ESIAs to fulfil their due diligence duties. In line with the Environmental and Social Policies of the World Bank Group (1999) – established in order to prepare borrowing governments to tackle the environmental and social hazards of investments in order to be eligible to obtain financing from the World Bank in support of investment projects – an essential element of the ESIA is the

[16] See *e.g.*, climate assessment methodologies developed by the IPCC, in the context of the UN Framework Convention on Climate Change, and the IFC.

[17] See *ALIC Guide*, paras 3.49 and 3.53, pp. 64 *et seq*.

environmental and social management plan, consisting of "the set of mitigation, monitoring, and institutional measures to be taken during implementation and operation to eliminate adverse environmental and social impacts, offset them, or reduce them to acceptable levels", including "the actions needed to implement these measures".[18] The rationale behind the environmental and social management plan is also shared by the IPCC Technical Guidelines for Assessing Climate Change Impacts and Adaptations (1994), which followed the 1992 Preliminary Guidelines. The IPCC has identified the "assessment of autonomous adjustments and evaluation of adaptation strategies" (mitigation and adaptation) as an essential step in the broader assessment of climate change impact.

219. As emphasised under the International Finance Corporation (IFC) Environmental, Health, and Safety Guidelines, special attention concerning the application of ESIA must be given to investment projects that are characterised by significant sources of air emissions, or that are located in vulnerable airsheds or environmentally sensitive regions. Similarly, significant efforts should be undertaken in ESIAs with a view to ensuring that the investment in question does not pose potential risks to biological diversity.

220. Within the context of environmental and climate change due diligence, the parties may consider establishing an investment facilitation mechanism, in line with the UNECE Aarhus Convention on Access to Information, Public Participation in Decision-making and Access to Justice in Environmental Matters, the Escazù Regional Agreement on Access to Information, Public Participation and Justice in Environmental Matters in Latin America and the Caribbean, and the African Charter on Human and Peoples Rights.

221. The third paragraph of this Principle emphasises the need for the investor to consult with key stakeholders – individuals or any form of associative or corporate bodies such as, but not limited to, those representing local communities and populations (including Indigenous populations, when relevant), local NGOs and other relevant interest groups, trade unions, and governmental bodies. Effective consultations are crucial for an accurate identification and assessment of the risks and potential adverse effects of the project on local communities and Indigenous populations. The investor should seek to appreciate the concerns and knowledge of potentially affected stakeholders by consulting with them, also taking into account language and other potential barriers to effective engagement. Consultations help to effectively implement the investment project and ensure that the rights, interests, and cultural heritage of these groups are respected and upheld. Such consultations foster mutual understanding, build trust, and help identify potential social, environmental, and economic impacts of the project on such communities.

222. Consultation may be conducted through surveys, interviews with leaders, group meetings, debates, consultative forums, and online dialogues.[19] It is important to note that the information collected during the consultations should be publicly accessible and should not violate privacy or generate risks for stakeholders (such as security risks or risks of retaliation in hostile or repressive contexts).[20]

223. In situations where direct consultation is not possible, the investor should consider reasonable alternatives, such as consulting credible, independent expert sources from civil society, including environmental human rights defenders and others.[21] The assessment of environmental and climate-related impacts will inform subsequent steps in the due diligence process.



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18 World Bank Group, *Environmental and Social Policies, OP 4.01, Annex C*, art 1.

19 *OECD Due Diligence Guidance for Meaningful Stakeholder Engagement in the Extractive Sector, Annex B "Engaging with indigenous peoples"*, p. 63.

20 *Ibid.*, p. 68.

21 See also UN Guiding Principles on Business and Human Rights, Principle 18 and commentary.

224. The need to apply the free, prior, and informed consent (FPIC) principle when consulting with local communities and Indigenous populations is expressly set out in the third paragraph of this Principle. FPIC guarantees those communities and populations the right to participate freely and voluntarily in consultations, with sufficient and culturally appropriate information, and to make decisions – whether to approve or reject a proposed project – before any activities commence. It serves as a safeguard to protect their rights, interests, and well-being from the potential adverse effects of such projects.[22]

225. Finally, the Principle contains an express reference to the requirement of continuous due diligence and monitoring activities, since this is the concrete and practical manner through which the parties will identify, include, adapt and abide by their commitments on sustainability matters during the entire lifecycle of the contract. The investor, in cooperation and with the assistance of the host State, must conduct the above-mentioned due diligence throughout the different phases of the project's lifecycle, covering the preparation of the project, the implementation of the investment, and a reasonable period following its conclusion. This temporal scope of due diligence must account for potential future developments in international social, environmental and climate change law, including key international standards in these areas (see also Chapter 5, Section D.3 on continuous monitoring). This is particularly relevant in the area of sustainability, considering rapid evolutions of norms and standards, such that monitoring activities should help the parties with the follow-up on these norms and standards.

**Model Language**

Contract language for pre-contractual documents such as LoIs or MoUs (to the extent intended as pre-contractual due diligence), or for a clause in the IIC (to the extent intended as pre-commencement due diligence):

1. Considering the foregoing declarations by the Parties on their endeavour to pursue the investment covered by the Contract in accordance with the highest international standards on sustainability, as required by various international and national laws, guidelines, and protocols applicable to the Parties or relevant to the Project and its economic sector, the Parties hereby agree to organise and implement sustainability due diligence on the Project appropriate to its size and circumstances pursuant to the terms and conditions set out in this clause.

2. The due diligence shall serve the purpose of assessing the risks of potential adverse effects of the Project on the environment (including the potential impact of the Project on climate change), the health and safety of people and workers, and the human rights of the communities and individuals affected by the investment (and its supply chain) with a view (i) to prevent these risks if they can be avoided or (ii) to put in place adequate mitigation measures to minimise the consequences of adverse effects that cannot be avoided. The due diligence shall also cover related topics where relevant, such as governance aspects (including issues of corruption and local community development).

3. The due diligence shall be performed according to [i*nsert generally accepted impact assessment methodologies*] and shall include consultations with relevant stakeholders that could be negatively

[22] UN Declaration on the Rights of Indigenous Peoples (UNDRIP); Food and Agriculture Organization of the United Nations (FAO), *Respecting Free, Prior and Informed Consent: Practical Guidance for Governments, Companies, NGOs, Indigenous Peoples and Local Communities in Relation to Land Acquisition, Governance of Tenure Technical Guide No. 3* (2014), p. 4 *("[FPIC] should be considered as a collective right of indigenous peoples to make decisions through their own freely chosen representatives and customary or other institutions and to give or withhold their consent prior to the approval by government, industry or other outside party of any project that may affect the lands, territories and resources that they customarily own, occupy or otherwise use. It is thus not a stand-alone right but an expression of a wider set of human rights protections that secure indigenous peoples' rights to control their lives, livelihoods, lands and other rights and freedoms*").

affected or potentially affected by the Project. These include [*insert list of affected and potentially affected stakeholders and/or criteria to select them, including local populations and their representatives, Indigenous populations and vulnerable local communities, NGOs and other relevant interest groups, trade unions and governmental bodies*].

4. In accordance with the relevant applicable law and agreed standards and methodology, the Investor shall prepare, with the cooperation of the State Party, an environmental and social impact assessment (ESIA), a climate change risk and vulnerability assessment, and a human rights due diligence report, as well as the related management and mitigation plan, including a local community resettlement plan (if necessary) and a decommissioning plan, serving the purposes highlighted under paragraph 2.

7. The consultations with local communities and Indigenous populations (when applicable) and other stakeholders should start at the earliest possible stages of the Project, leaving enough time for the results of the consultation to be considered in the context of Project-related decisions. Consultation is an ongoing process and shall be maintained throughout the lifecycle of the Project.

8. The Investor shall ensure that its employees or representatives involved in consultations with local communities and Indigenous populations have sufficient knowledge about the culture and traditions of the relevant community or population, including language, dress code, dietary considerations, protocol and etiquette. During the consultations, the Investor shall seek to explore the intangible value associated with sacred sites or areas of cultural significance for the involved community or population.

9. Consultations shall be performed according to the free, prior, and informed consent (FPIC) principle, which is a fundamental principle that ensures the active involvement of Indigenous peoples in decision-making processes related to projects or activities that may significantly impact their lives, territories, or resources.

10. The responsibility to perform the due diligence, and to establish any ensuing mitigation plan, lies primarily with the Investor. However, the State shall fully cooperate with the Investor on the performance of the due diligence and shall provide its support as may reasonably be required by the Investor, in particular for consultations with local communities and Indigenous populations, and other local stakeholders. The Investor and the State warrant that they shall disclose information on all matters they deem relevant to the sustainability due diligence process in a timely and accurate manner.

11. Impact study experts with relevant track records and familiarity with impact assessment methodologies shall be involved to assist with the performance of the due diligence. The Investor shall inform the State of the selection of the impact study experts it will involve in the due diligence.

12. Should the State have a major objection to the choice of a specific impact study expert, it shall inform the Investor promptly with motivated grounds to enable the Investor either (i) to provide adequate assurances on the profile and expertise of the expert to the reasonable satisfaction of the State or (ii) to select another expert. If the State does not object within a reasonable time after having been made aware by the Investor of the envisaged involvement of an impact study expert, the State shall be deemed to be satisfied with the choice of this expert.

13. The due diligence shall be performed with sufficient lead time to enable processing its results and working out mitigation measures through the mitigation plan prior to the finalisation of the Contract and, at the latest, prior to the commencement date of the operations on the Project. The mitigation plan shall allocate roles and responsibilities to the Parties for the implementation of mitigation measures based on who, between the Investor and the State, is in the best position to efficiently deploy these measures.

14. It is hereby expressly acknowledged and accepted by the Parties that a mitigation plan cannot include set-off mechanisms resulting in intolerable detrimental effects such as, for example, set-off

mechanisms proposing solutions to treat illnesses caused by health hazards instead of putting in place prevention measures to avoid such illnesses.

15. Upon completion of the due diligence, the Investor shall share the due diligence report with the State in order for the Parties to jointly review its results and jointly determine and validate the mitigation plan to be implemented as part of the Project. As part of this joint review, the State shall be entitled to comment on and propose improvements to the due diligence report and the actions recommended in this report.

16. The completion of the due diligence, and the agreement between the Parties on any ensuing mitigation plan, shall preferably be reached when finalising the Contract and, at the minimum, shall be a condition precedent to the commencement of the works on the Project.

Commentary to the Model Clause

226. As a preliminary observation, it is recognised that the proposed Model Clause may be perceived as setting out a very high level of detail on due diligence requirements. It shall be emphasised, though, that it serves the purpose of offering flexible guidance, adaptable to the type and scale of investment projects. While minimum due diligence requirements should be reflected in IICs, it can be expected that the extent of these requirements will depend on the size and capabilities of the Parties and the concrete risk of adverse impact of the project in the particular circumstances of the case, and therefore will be broader for large-scale, high-risk projects.

227. The main purposes of this clause are to (i) define roles and responsibilities for the implementation of sustainability due diligence on the project and (ii) set out the sequence of actions with respect to this due diligence.

228. The clause first sets out the scope of the due diligence and its objectives, namely an assessment report on the possible adverse impact of the project on (i) the natural and social environment, (ii) the health and safety of people and workers, and (iii) human rights, which are three key pillars of sustainability policies, and provides through a management and mitigation plan the concrete measures envisaged to address such impact. The due diligence process should also consider aspects related to the positive impact of the project (for example, local community development commitments).

229. The clause expressly requires the parties to adhere to generally accepted impact assessment methodologies, as established by international and regional organisations or by industry associations and other entities in their standard documents. A non-exhaustive list includes the UN Guiding Principles on Business and Human Rights, the OECD Guidelines for Multinational Enterprises, the UN Global Compact, the Equator Principles, and the ILO Declaration on Fundamental Principles and Rights at Work. Other standard methodologies that may be considered are the Environmental and Social Policies of the World Bank Group, the IFC Performance Requirements, the Asian Development Bank Safeguard Requirements, and the IPCC Technical Guidelines for Assessing Climate Change Impacts and Adaptations. The Model Clause contains a placeholder in this regard.

230. In line with standard expectations for sustainability due diligence, the clause expressly requires the involvement of, and consultation with, key stakeholders in the impact assessment. To that end, the clause contains a placeholder for contracting parties to specify the list of people, organisations and bodies to be approached.

231. The clause expects the investor to ensure active, free, effective, meaningful, and informed participation of key stakeholders affected by the investment, such as local communities and Indigenous

populations, in consultations. The consultations shall provide space for affected people to articulate their views free from undue influence, in an inclusive, timely, and transparent manner. To achieve meaningful participation in consultations, local communities and Indigenous populations shall be involved in the design, planning and implementation of consultations. The design and implementation of consultations shall take decision-making institutions of local communities and Indigenous populations into account.

232. The consultations should not consist of one-way communication but a dialogue and exchange of information. The investor shall ensure that local communities and Indigenous populations have an opportunity for meaningful feedback and questions about the project. Prior to the start of consultations, the investor should clearly articulate the objectives of consultations to local communities and Indigenous populations.

233. Taking power imbalances into consideration, it is recommended that the investor and the State party assess the extent to which local communities and Indigenous populations have the support necessary to conduct meaningful consultations. In this regard, translation of the negotiation process and consultation documents into a language that local communities and Indigenous populations understand, should be considered. It is important to take into account that local communities and Indigenous populations may speak unique dialects or have an oral tradition of communication, which in turn may require innovative methods of consultation. Therefore, the content of the documents shall be explained in a tone and with a lexicon understood by the relevant communities or populations. The specific resources necessary for consultations as well as compensation for costs to communities and populations for engaging in the consultations should be discussed and agreed in consultation with them. The support may include engaging a local facilitator for communication with the affected group(s) or financing neutral third-party professionals (*e.g.*, lawyers or technical experts). To ensure the independence of third-party professionals, the investor and the State party shall use their best efforts to develop new mechanisms (*e.g.*, trust funds over which the business has no control, or contributions to basket funds that apply beyond individual projects) to finance neutral third-party professionals.

234. For an effective consultation, it is important that local communities and Indigenous populations have access to the information they may require to effectively participate. Such information may include the investment's location, size, scope, timeline, operational model, projected revenue, projected costs, risks, benefits, and milestones. Access to this information shall be provided subject to information deemed to be commercially sensitive or otherwise confidential. Local communities and Indigenous populations shall also have access to the consultation record, reflecting the milestones and conclusions of consultations.

235. With respect to the requirement in the clause to effectively carry out an FPIC process, the following key stages can be distinguished.[23]

236. First, it is essential to identify the rights-holders or affected communities. This process involves determining the number of individuals and communities inhabiting the area or its surroundings, as well as understanding how they use it, such as the natural resources they rely on. This information can lead to the creation of a detailed map of land claims and uses, a process where the collaboration of local communities is indispensable.[24]



[23] See *FAO 2014,* p. 13-38.

[24] *Ibid*., p. 20*: "Consistent with international law, however, the Guidelines require state agencies and investors to ensure that legitimate tenure rights, including customary rights, are respected and the FPIC of the indigenous peoples is obtained for any investment project affecting such rights. The resulting legal complications also need to be addressed."*

237. Second, it is essential to understand the legal status of the land. Investments may often require land acquisition, making it crucial to be apprised of the legal status of the land in question. This step may necessitate the involvement of expert legal consultants to assess how the investment could affect land ownership or usage rights. Combined with the first step, this analysis provides a comprehensive understanding of the legal and practical implications for the communities involved.[25]

238. Third, consultations must be conducted based on information-sharing. Consultations must be conducted with a foundation of transparent and thorough information-sharing. The information provided to rights-holders and interested communities must be relevant, accurate, complete, and presented in a culturally appropriate manner. This ensures that the communities are well-informed and better equipped to decide whether the project should proceed.[26]

239. Fourth, access to independent sources of information and advice must be ensured. To foster a fair and unbiased decision-making process, local communities must have the freedom to access independent sources of information and advice. This could include support from local NGOs, independent experts, or other trusted third parties who can provide alternative perspectives and empower communities to make informed decisions.[27]

240. Fifth, monitoring mechanisms must be established. Once consent is obtained and an agreement is reached, a monitoring mechanism must be established to ensure compliance with the agreed terms during the implementation of the project. This mechanism should involve the participation of the affected communities to guarantee accountability and transparency in the execution phase.[28]

241. FAO has also provided guidance on the key elements of FPIC:[29]

- **Free:** Consent must be given voluntarily, without coercion, intimidation, or manipulation. Communities must have the freedom to express their views and make decisions without undue influence.

- **Prior:** Consent must be sought well in advance of any authorisation or commencement of activities. Adequate time should be allowed for Indigenous communities to engage in their internal discussions and reach consensus through their customary decision-making processes.

- **Informed:** Information about the proposed project or activities must be complete, objective, accurate, and presented in a culturally appropriate and understandable manner. This includes



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25 *Ibid.*, p. 19*: "In expressing or withholding their FPIC to proposed agricultural investments, the people concerned need to be assured that the full extent of their customary rights and current system of land use are recognized and respected. Exactly because the legal systems of many countries do not formally recognize customary rights, communities' right to give or withhold consent for what happens on their lands is all the more vital."*

26 *Ibid*., p. 28*: "The purpose of iterative consultation is to share, in a multi-directional process, all relevant information pertaining to the projected development with relevant actors and rights-holders. With this information, communities are better placed to decide whether a project should or should not go ahead, and to discuss any modifications necessary to secure their consent."*

27 *Ibid*., p. 33*: "Communities have the right to access independent sources of information throughout the process of respecting FPIC, including during the process of reaching consent and, in particular, prior to decision-making and agreement."*

28 *Ibid*., p. 35*: "Once consent has been reached, it is important to ensure that agreements made through the consultation process are respected in their practical implementation. If agreements are not respected, sanctions and/or mechanisms of redress need to be activated."*

29 *Ibid.*, p. 5; see also, UN Human Rights Council, Expert Mechanism on the Rights of Indigenous Peoples, *Final Study on Indigenous Peoples and the Right to Participate in Decision-Making*, UN Doc A/HRC/EMRIP/2011/2 (26 May 2011) at para. 26.

details about the project's purpose, scope, duration, potential impacts (environmental, social, and cultural), and mitigation measures.

- **Consent:** Indigenous peoples have the right to provide or withhold consent, or to set conditions for their approval. Consultations must be conducted with the communities' freely chosen representatives, ensuring an environment that respects their views, traditions, and decision-making processes. The outcomes of consultations should reflect the communities' positions and priorities, forming a substantive basis for decisions.

242. The clause assigns the main responsibility to perform the due diligence to the investor. The rationale here is that the investor is expected to be in the best position not only to carry out the due diligence but also to establish the ensuing mitigation plan. The State, though, should not remain passive and is expected to provide a reasonable level of support and assistance to the investor, especially on matters where the State will have better local insight or better access to information, or which are subject to the exercise of public power. It may also be the case that the State will carry out activities with potential impact or that, under domestic law, States have particular obligations to Indigenous communities (for instance) and their consultation in relation to certain projects. For avoidance of doubt, the expected cooperation between the parties on due diligence matters should not have the effect of attenuating the primary obligations that are assigned to the investor or the State on these matters. The clause also makes clear that both parties are expected to disclose information relevant to the assessment and decisions to be taken during the sustainability due diligence (*e.g.*, geological data and maps on the side of the State, or results of prospections and analytics of the project on the side of the investor) in a timely and accurate manner.

243. Since thorough sustainability due diligence demands specific skills and expertise, the clause requires recourse to impact study experts with adequate professional knowledge. While the clause does not go as far as establishing an approval process by the State on the selection of experts, the investor shall nevertheless inform the State of the experts who will be involved. This shall give the State an opportunity to challenge the choice of experts in the event of major objections. It was determined that this approach is a sensible "happy medium" between an imperative pre-approval process and a mere information process.

244. The clause anticipates that the due diligence will be performed sufficiently in advance of starting the works on the project, such that mitigation measures can be worked out efficiently. This is the reason why the clause imposes the completion of the due diligence, and the finalisation of an agreed mitigation plan, preferably when finalising the contract and, at the minimum, as a condition precedent to the commencement of the operations of the project.

245. While there is a strong focus in the clause on the completion of the due diligence activities in the pre-investment operations phase of the project, the due diligence obligations of the parties shall not expire with the start of the project. On the contrary, it is expected that the parties will put monitoring actions in place to follow up on the measures agreed in any mitigation plan they will have elaborated. To that end, the clause sets out continuous due diligence obligations of the parties once the project has started, while additional guidance on how such sustainability obligations are implemented, monitored and updated during contract performance is provided in Chapter 5.

## D. Legal capacity

**Principle 12**

**The parties to an IIC may wish to include wording (i) regulating the respective duty to verify the other party's capacity and to answer to the other party's requests**

**regarding capacity, (ii) acknowledging the legal capacity of the other party within the scope of authority ascertained in the manner agreed between the parties, and (iii) acknowledging that the other party is not bound beyond the scope of the other party's authority as ascertained pursuant to the contractual regulation.**

**Relevant UPICC provisions**

Article 1.7 (Good faith and fair dealing) and Chapter 2, Section 2 (Authority of agents) of the UPICC

**Commentary**

246. As a matter of contract law, the extent to which a party (including a State) is bound by a contract is regulated by the domestic law on legal capacity applicable to that party. If one party is a State, it will be that State's own law that determines whether a State organ or entity has the authority to bind the State. The legal capacity to enter into a contract, with the consequence that the contract is binding for the parties who entered into it, has parallels with the question of attribution. Attribution of conduct to a State as a matter of public international law is based on criteria determined by international law.

247. For IICs, both dimensions are relevant: questions of investment protection are matters of public international law, whereas questions of contractual effects are matters of domestic contract law and domestic law on legal capacity.

248. While there is no convention on the attribution of conduct to a State as a matter of public international law, the Articles on State Responsibility for Internationally Wrongful Acts (ASRIWA), drafted by the International Law Commission (ILC) and taken note of by the UN General Assembly in 2001, are largely regarded as reflective of customary international law. The ASRIWA provide a comprehensive set of principles governing the responsibilities and liabilities of States for breaches of their international obligations. Among other things, they specify when conduct can be attributed to a State as an action or omission, allowing for the determination of responsibility. This includes acts by State organs, entities exercising government authority, and even private individuals in certain circumstances. While not directly regulating breach of contractual obligations, these principles may be considered in the context of breach of investment protection obligations connected with contractual obligations.

249. According to Article 7 of the ASRIWA, *"The conduct of an organ of a State or of a person or entity empowered to exercise elements of the governmental authority shall be considered an act of the State under international law if the organ, person or entity acts in that capacity, even if it exceeds its authority or contravenes instructions."* This means that conduct of a State organ or entity is attributable to the State even if it is *ultra vires*. Articles 8 and 9 are also relevant for entities that are not organs of the State.

250. That a State cannot invoke its own internal distribution of competence to avoid the effects of *ultra vires* acts by its organs or entities, also flows from Article 3 of the ASRIWA, according to which *"The characterization of an act of a State as internationally wrongful is governed by international law. Such characterization is not affected by the characterization of the same act as lawful by internal law."*

251. In the field of IICs, these principles may become relevant if the investor carried out negotiations with and received assurances from, or entered into the contract with, an organ or an entity which, under the laws of the host State, *does not* have the authority to bind the State as far as concerns the specific legal relationship or parts thereof. For example, the investor may have relied on assurances of favourable tax treatment that were made by a ministry which did not have competence in the field of taxes. To the

extent that an investor invokes a breach of the State's obligations regarding investment protection, the ASRIWA suggest that the assurances made by the incompetent ministry are attributable to the State.

252. What if these assurances were included in the IIC as a contract term – do they have contract law effects? The ASRIWA concern States' responsibility for conduct which is incompatible with States' *international obligations*, and do not concern private law effects such as the binding effects of an IIC. The contractual effects of a commitment taken by an organ or an entity without authority will be regulated by the applicable contract law (often, the law of the host State). The applicable contract law will give due consideration to the legal capacity of each of the parties, which in turn is regulated by the law applicable to each of the parties.

253. Unlike the principle contained in Articles 3 and 7 of the ASRIWA, therefore, the law of the host State *distributing* competence among its organs will be decisive for the contractual effects of the IIC. The host State's law on its internal distribution of authority, therefore, has different effects depending on whether the IIC is looked upon from the point of view of investment law or contract law.

254. The legal capacity of the investor is regulated by the investor's own law – which, depending on the applicable private international law, can be the law under which the investor was incorporated, or the law of the place in which the investor has its main place of business. The UPICC's principles on agency laid down in Section 2.2 can, to a certain extent, apply to the capacity of a corporate body to bind the legal entity, although the applicability of these provisions is often restricted by mandatory rules of the applicable law.

255. When determining the role of the host State's and the investor's law for legal capacity, consideration should be given to the *effects* that the UPICC may have on the interpretation of the applicable contract law, as well as to commercial contract practice.

256. While the UPICC do not regulate legal capacity of contract parties, they contain extensive requirements to act in good faith during negotiations. Under Article 1.7 of the UPICC, the parties are under a duty of good faith that cannot be excluded or restricted by their agreement. As will be seen below, this may have an impact on the issue of validity of assurances made *ultra vires*. In the comment to Article 2.2.5(2) of the UPICC on apparent authority, reference is made to the circumstance that, in dealing with a legal entity, "a third party may find it difficult to determine whether the persons acting for the organisation have actual authority to do so and may therefore prefer, whenever possible, to rely on their apparent authority. For this purpose the third party only has to demonstrate that it was reasonable for it to believe that the person purporting to represent the organisation was authorised." The comment further explains that "Whether or not the third party's belief was reasonable will depend on the circumstances of the case."

257. The duty of good faith may thus lead to assuming that the host State or, as the case may be, the investor, is responsible for the other party's understanding of the State's or the investor's organisation and internal division of competence. This may suggest that neither party has a need to actively ascertain the scope of authority of the organ or entity with which it negotiates, even when the relevant information is publicly available and can be ascertained by exercising due diligence. As far as concerns the State's liability, this would lead to applying Articles 3, 7, 8 and 9 of the ASRIWA (attributing to the State the contractual effects of *ultra vires* conduct by its organs or entities) to contract matters as well. As far as concerns the investor's liability, this would lead to a result confirming the UPICC's support of apparent authority, albeit only as long as this is not against the applicable law – see comment 5 to Article 2.2.1 of the UPICC: "If under the special rules governing the authority of its organs or officers a corporation is prevented from invoking any limitation to their authority against third parties, that corporation may not rely on Article

2.2.5(1) to claim that it is not bound by an act of its organs or officers that falls outside the scope of their authority."

258. On the other hand, the duty of good faith applies not only to protect one party's reliance on the other party's apparent authority, but also to that party's diligent conduct during negotiations. The conduct of a party who fails to ascertain the competence of the body with which it negotiates does not necessarily meet the required standard of good faith.

259. That the duty to act in good faith may require that parties exercise a certain diligence is supported by commercial contract practice. Commercial contract practice often requires parties to exercise due diligence in ascertaining the legal framework of the legal relationship they are negotiating. It is customary for professional parties, as part of the negotiations, to carry out an analysis of all the relevant legal, financial, technical and commercial issues. This also applies to issues such as restrictions to the other party's capacity to make stipulations in certain areas, or the internal division of competence among administrative bodies. It is up to the party carrying out the due diligence to collect the information it considers to be relevant, to ask for it if it is not publicly available, to assess it, and to make provisions for the connected risks. Only if a party could not reasonably be aware of the existence of information that the other party possessed would it not be in the position to request disclosure of information.

260. Among other things, the commercial practice of carrying out a due diligence examination of the legal framework regularly results in each party requesting the other to supply an independent legal opinion confirming that the requested party has the power to enter into the given contract, and that the person signing the contract has the authority to bind that party.

261. Transposed to the contractual effects of IICs, particularly IICs that are concluded on the basis of individual negotiations, commercial contract practice contradicts the above-mentioned assumptions that seem to be suggested by the ASRIWA and possibly by the UPICC, according to which parties can rely on the apparent authority of the other party without making any effort to verify its compliance with the applicable law.

262. This commercial contract practice is more in line with the private international law principle that the authority of a party is determined by that party's law. To align with contract practice, and to enhance predictability in the determination of whether the parties' reliance on each other's apparent authority was reasonable, it is advisable to insert into the IIC contract language that specifies each party's respective duty of diligence in this context.

263. The contract language suggested below is meant as a declaration given by each party to the other and confirming that (i) each party carries the burden of verifying the applicable law on the other party's legal capacity as far as this is publicly available; (ii) each party has a duty to disclose relevant information that was requested by the other party; (iii) a party does not infringe any good faith obligations if it did not provide all relevant information, as long as the withheld information had not been requested by the other party and as long as withholding it did not amount to a material omission with intent to deceive (carving out special knowledge the existence of which the requesting party could not reasonably be aware); (iv) a party acknowledges the legal capacity of the other party within the scope of authority as ascertained in this manner; and (v) a party acknowledges that the other party is not bound beyond the scope of the other party's authority as ascertained in this manner.

264. Because the rationale of the declaration is relevant for each of the parties, the clause is drafted as a reciprocal representation. The parties may want to consider providing for corresponding contract language in connection with each modification (if any) they may enter into after the formation of the IIC.

265. In IICs that are concluded on the basis of competitive bidding, the dynamics of contract formation may be different. In some cases, the bidder may only carry out limited due diligence even with respect to publicly available information and may rely on the information disclosed in the invitation to bid. In this setting, the host State's duty of disclosure is not restricted to the information expressly requested by the bidder. The suggested contract language may not be relevant in this context – although, in this context, the investor can also follow the practice of requesting a legal opinion confirming that the subject matter of the IIC falls within the scope of the signing party's power, and that the person signing the IIC has the authority to bind that party.

266. The aim of this declaration is to clarify that each of the parties has to diligently ascertain the legal capacity of the other party and that it cannot excuse its passivity by blindly relying on the duty of good faith enshrined in Article 1.7 of the UPICC and specified in Article 2.2.5 of the UPICC. Given that under Article 1.7(2) of the UPICC the parties may not contractually restrict their duty of good faith, any contractual language intended to clarify that a certain regulation has been accepted by the parties is exposed to the risk of being overridden if the interpreter of the IIC operates with an expansive understanding of the principle of good faith in the UPICC. This risk may be reduced, although not completely eliminated, through the proposed Model Clause. Such a clause would reinforce the parties' own evaluation of the clause's compatibility with Article 1.7 of the UPICC, thus in part neutralising the circularity of the reasoning.

267. An agreement between the parties to the extent described above may also have significance for the level of investment protection and for the attribution to the State of *ultra vires* conduct: if the investor has committed to diligently assess the legal capacity of its contracting partner, and any restrictions in the scope of capacity were publicly accessible or disclosed after the investor's request, expectations that the State nevertheless be bound by *ultra vires* conduct may not be deemed to be legitimate.

**Model Clause**

Each Party declares that it has the legal capacity to enter into this Contract, including that the subject matter of this Contract falls within the scope of that Party's power, and that the person signing the Contract has the authority to bind that Party.

Each Party has collected and examined all publicly available information relevant to the scope of authority of the other Party – such as published statutory, administrative or judicial regulations and decisions, or registered articles of association.

Each Party has made available to the other Party any and all information requested by the other Party regarding the scope of authority of each of the Parties.

Each Party acknowledges that the other Party has not acted in breach of a duty of good faith if the latter has not disclosed information that was not requested by the former. This does not apply if that Party failed to request disclosure of information that it could not reasonably be aware existed, that only the other Party possesses, and that is essential to the issue of the other Party's legal capacity.

Each Party acknowledges the legal capacity of the other Party within the scope of authority as ascertained according to [*this section*].

Each Party acknowledges that the other Party is not bound beyond the scope of the other Party's authority as ascertained according to [*this section*].

## E. Relevance of the pre-contractual phase to determine the scope of contractual obligations

### 1. Entire Agreement

**Principle 13**

**The parties may wish to insert a clause confirming that all their obligations are spelled out in the contract and that no additional obligations may be implied into the contract on the basis of the pre-contractual phase, of considerations of reasonableness or of a duty of good faith, unless they are necessary to implement the contract or are obvious, and do not contradict the express terms of the contract.**

**Relevant UPICC provisions**

Article 4.3 (Relevant circumstances), Article 2.1.17 (Merger clauses), Article 4.8 (Supplying an omitted term) and Article 5.1.2 (Implied obligations) of the UPICC

268. Point (a) of Article 4.3 (relevant circumstances) of the UPICC mentions pre-contractual negotiations as an important element in determining the scope of the contract. According to Article 2.1.17 (merger clauses) of the UPICC, entire agreement clauses do not prevent using pre-contractual documentation to interpret the scope of the contract. In addition, Article 4.8 (supplying an omitted term) of the UPICC mentions the intentions of the parties and good faith as a source to supplement the contract. Finally, point (c) of Article 5.1.2 (implied obligations) of the UPICC mentions the intentions of the parties and good faith as a source for implied duties between the parties.

**Commentary**

269. Often, IICs are drafted according to the contract style commonly adopted in international commercial contract practice. In turn, international contract practice operates with long and detailed contracts that are meant to be exhaustive. Among other things, contracts extensively regulate the scope of the parties' obligations, stating which remedies may be exercised in case of default, and under what conditions. Furthermore, they often contain an entire agreement clause, which is usually understood to ensure an objective interpretation of the contract language, as well as limiting liability and remedies.

270. The practice of contract negotiations and contract drafting does not always reflect the rules of interpretation laid down in the UPICC. Sometimes, parties may employ considerable resources in detailed negotiations of the contract wording and may assume that the carefully negotiated contract language will be the sole source of obligations between them. These parties may be surprised if pre-contractual negotiations are subsequently considered to be relevant to determine the scope of the contract, good faith is used as a source of duties or to contradict express contract terms, or duties are implied even though they are not necessary to implement the contract and contradict express contract terms. Furthermore, strict reliance on the contract language may be useful when contracts are to be interpreted objectively based on their terms to make sure that third parties such as financing institutions and insurance companies can accurately assess the contract's implications. These parties' expectations may, to varying degrees, be supported by the governing law, depending on which law is applicable.

271. In this context, it may be advisable to specify to which extent the parties' conduct during negotiations and good faith may be relied on when construing the contract. According to the UPICC, they shall be taken into consideration when determining the content of the contract. By specifying to which extent contract obligations may be added to or restricted, the parties may preserve predictability. At the

same time, excessive rigidity should be avoided. A balance between these two interests may be struck if the possibility to imply contract terms is granted as far as the implied terms are necessary for the implementation of the agreed terms.

272. The proposed contract language clarifies that the UPICC are not intended to replace or override the express terms of the contract or the otherwise governing law.

**Model Clause**

Suggested contract language for contract documentation, to be added to the standard Entire Agreement clause accompanying Principle 14:

> No obligations for either Party can be implied on the basis of the Parties' conduct or exchange of documents in the pre-contractual phase, of considerations of reasonableness or of a duty of good faith, unless they are necessary to implement the Contract or are obvious, and do not contradict express terms of the Contract.

**Illustration**

> If an IIC provides that a certain payment shall be made to a certain bank account abroad, it is necessary for its implementation that the documentation required to justify payment abroad be provided and that the permits required to effect payment abroad be given. The parties will be under an implied obligation to meet these requirements, even though the contract does not spell this out.
>
> On the contrary, if the IIC provides that certain goods shall be delivered at a certain place, the obligation will be fulfilled when the delivery is made at the agreed place. It is not possible to imply an obligation to provide documentation for subsequent export of the goods.

273. The proposed contract language would not affect the application of Article 2.1.7 of the UPICC regarding the interpretation of ambiguous terms of contracts.

**Illustration**

> An IIC provides that the investor performing some work linked to the construction of an electrical powerplant performs such work "at its own expense and risk and has to indemnify the other party against any loss, damage and liability resulting from injury to property arising out of the performance of the contract". The IIC contains an entire agreement clause.
>
> If the State party considers that the indemnity clause covers damage to any item, regardless of whether it is State property or not and, on the contrary, the investor understands that the indemnity clause only covers injury to property of third parties and not State property, the entire agreement clause does not preclude either party to look for extrinsic evidence (Article 4.3 of the UPICC), *i.e.*, evidence that is not contained within the four corners of the document, to interpret the expression "injury to property arising out of the performance of the contract".
>
> However, the entire agreement clause does not allow to read into the contract additional elements, such as a cap of damages, even if this was part of the negotiations between the parties, if not reflected by a term of the contract.

## 2. Writings in confirmation

**Principle 14**

**If a writing which is sent after the conclusion of the contract and which purports to be a confirmation of the contract contains additional or different terms, such terms will be subject to any applicable approval requirement that the State entity or investor would need to satisfy for any modification of the contract.**

**Relevant UPICC provision**

Article 2.1.12 (writings in confirmation) of the UPICC

**Commentary**

274. In the context of IICs, no new terms should be allowed to be added to an already concluded agreement by "writings in confirmation" as such additions or alterations may prove problematic and give rise to disputes subsequently. Further, any new terms or amendments may also need to go through an approval process applicable to the State party or to the investor. Therefore, the inclusion of an entire agreement clause in the contract is recommended, such that any additional terms or alteration of terms through a confirmation of the contract will be ineffective.

275. An entire agreement clause may limit the parties' ability to add new obligations or restrict them from reading new terms into the contract; the parties may thus wish to preserve predictability. At the same time, excessive rigidity should be avoided. A balance between these two competing interests may be struck if (a) the possibility to imply contract terms is granted as far as the implied terms are necessary for the implementation of the agreed terms (see above explanations under Principle 13), (b) when a term is ambiguous, *i.e.*, when it is reasonably susceptible to more than one interpretation, the court or arbitral tribunal is allowed to use extrinsic evidence to interpret such term of the contract, despite an entire clause, in conformity with Article 4.3 of the UPICC. In determining whether the writing is ambiguous, a court or arbitral tribunal may admit any evidence which could be relevant to prove a meaning to which the language of the instrument is reasonably susceptible to have.

**Illustration**

State party A concludes an IIC with investor B that provides for the construction of an electrical power plant and its operation for a 20-year period.

Shortly thereafter, State party A receives a letter from investor B purporting to confirm the terms of their agreement but adding an arbitration clause to the IIC. Such additional term, not previously agreed between the parties, cannot become part of the contract unless it has been formally approved as an amendment to the IIC.

The same conclusion would be reached if investor B had received a letter from State party A purporting to confirm the terms of their agreement but adding a duty to allow inspections of the works at any time by officials of State A.

**Model Clause**

This Contract sets forth the entire agreement and understanding of the Parties with respect to the subject matter contained herein and terminates and supersedes all prior understandings, agreements,

representations and correspondence, whether written or oral, relating to the subject matter herein. Any communication purporting to confirm the terms of the Contract shall not add to or alter in any way the terms of this Contract.

### 3. Terms deliberately left open

**Relevant UPICC provision**

Article 2.1.14 (Contract with terms deliberately left open) of the UPICC

**Commentary**

*A. Open terms not in themselves an impediment to valid conclusion of an IIC*

276. If the parties intended to conclude a contract, the fact that they have intentionally left a term to be agreed upon in further negotiations or to be determined by one of the parties or by a third person, does not prevent the contract from coming into existence. It should be noted, though, that in the case of IICs, any approval requirement that may be applicable to a modification to the contract must also be complied with for any term to be agreed subsequently.

**Illustration**

State party A concludes an IIC with investor B that provides for the construction of an electrical power plant and its operation for a 20-year period.

Given the substantial investment made in the construction of the power plant, the parties agree that State party A will purchase all the energy produced during the first three (3) years at a premium price. The IIC contains a clause stating that, following that initial three-year period, the energy price and the periodicity of its determination will be established (i) in further negotiations between the parties or, in case of failure, (ii) by a third person or an adjudicator.

Should the parties resort to a third party or to an adjudicator to establish the energy price and the periodicity of its determination, the IIC shall continue to be performed as per the parties' original agreement until a final decision is reached.

*B. Failure of mechanism provided for by parties for determination of open terms*

277. Where the mechanism to which the parties have initially agreed for the determination of an open term fails, an alternative means of resolving the issue should be made available, such as providing for the question to be referred to arbitration. This would be important to preserve the continuation of the contract, particularly in the case of IICs, which are typically complex, long-term and high-value contracts.

*C. Open terms in long-term contracts*

278. As stated above and particularly in the case of IICs, which are frequently long-term contracts, the parties may leave a term to be agreed when that term applies only to obligations at a later stage of the contract.

**Model Clause**

For the avoidance of doubt, the mere fact that in Clauses [*set out clauses*] certain matters are to be agreed upon by the Parties at a future date, does not affect the existence or validity of this IIC as a binding and effective contract.

With respect to Clauses [*set out clauses*], where the Parties have agreed on a mechanism to determine a matter at a future date and such mechanism is unable to achieve a determination of the matter at the relevant time, the Parties agree to submit the matter to arbitration in accordance with Clause [*arbitration clause*] for determination.

# CHAPTER 4. VALIDITY

## A. Introduction

279. Validity plays a central role in IICs, including PPP contracts. As with any contract, IICs require that both parties possess legal capacity (see Principle 12) and that the contract terms are legal and enforceable under the governing law.

280. Chapter 3 of the UPICC contains several provisions on the validity of contracts – such as those governing the validity of mere agreement (Article 3.1.2), initial impossibility (Article 3.1.3), and grounds for avoidance (Articles 3.2.1–3.2.11) – which may apply to IICs either directly or with contextual adaptation. As IICs frequently incorporate legality clauses and declarations and assurances (representations and warranties) clauses, such clauses may influence the way the UPICC provisions on validity apply to an individual IIC.

281. IICs may result from individual negotiations or from public tenders, the latter often conducted under strict regulatory conditions that limit the investor's ability to negotiate. Where an IIC is preceded by a public tender, the investor voluntarily adheres to the predefined terms and conditions set by the host State. In such cases, certain rules on defective consent may not operate in their ordinary manner.

282. The following paragraphs explain how some of the UPICC provisions on validity apply in the specific setting of investment contracting. Other UPICC provisions on validity may apply directly to the IIC without any further elaboration.

## B. Substantive validity

**Relevant UPICC provisions**

Articles 3.1.2 (Validity of mere agreement) and 3.1.3 (Initial impossibility) of the UPICC

**Commentary**

283. Subject to any formalities, substantive or procedural requirements imposed by the domestic law of the host State or by the internal rules governing the investor, an IIC is concluded, modified, or terminated by the mere agreement of the parties (Article 3.1.2 UPICC). No additional requirement – such as "consideration" or "cause" – is necessary for the substantive validity or enforceability of the contract.

284. This confirms that the UPICC's consensual model of contract formation applies fully in the investment context: the agreement of the State party and the investor is sufficient to create a valid and binding IIC.

285. The UPICC rule on initial impossibility (Article 3.1.3) clarifies that the validity of an IIC is not affected merely because performance was impossible at the moment of contract conclusion. Likewise, the fact that a party lacked legal title or the right to dispose of the relevant assets at that time does not invalidate the contract.

286. Any rights and duties arising from a party's inability to perform must instead be addressed under Chapter 7 of the UPICC (Non-performance) and/or the Principles set out in this Instrument. Under those provisions, an adjudicator will be able to consider whether the State party or investor knew – or should have known – of the impossibility at the time of contracting.

287. If impossibility to perform arises from a legal prohibition, such as an export or import embargo, the question of validity depends on whether the underlying law intends to invalidate the contract or merely prohibit performance. Issues relating to whether a State may rely on its own legislation (*e.g.*, currency controls, licensing restrictions) to excuse non-performance are addressed in Chapter 7 of this Instrument.

### C. Grounds for renegotiation, adaptation or avoidance

**Relevant UPICC provisions**

Articles 3.2.1 (Definition of mistake), 3.2.2 (Relevant mistake), 3.2.4 (Remedies for non-performance), 3.2.6 (Threat), 3.2.7 (Gross disparity), 3.2.14 (Retroactive effect of avoidance) of the UPICC

**Commentary**

288. Although mistake is rarely invoked in practice, the relevant UPICC provisions (Articles 3.2.1 and 3.2.2) may apply to situations where, at the time of contract conclusion, one or both parties made an erroneous assumption concerning facts or law sufficiently serious to vitiate consent. In such cases, the IIC may be avoided.

289. In the IIC context, (i) investors may be unfamiliar with the host State's legal system; (ii) host State officials may lack specialised knowledge of the investor's activities; and (iii) the long-term, technical, and complex nature of many IICs may increase the possibility of erroneous assumptions by the contracting parties.

290. Under the principle of good faith (Article 1.7 of the UPICC), which also applies during pre-contractual dealings (see Chapter 3 of this Instrument), both parties have a duty to disclose relevant information. This duty manifests differently depending on the method of formation of the IIC. For individually negotiated IICs, the investor must disclose information essential to the project and conduct comprehensive due diligence; the State must disclose all legal, financial, technical and commercial information necessary for the performance of the contract. For an IIC formed through a competitive bidding, although due diligence remains mandatory for investors, the State is generally required to disclose all essential legal and technical information – unless the request for proposals expressly shifts this risk to bidders.

291. In line with the UPICC, avoidance for mistake should be permitted only where the mistake is such that a reasonable person in the same situation would not have entered the IIC, or would have done so only on materially different terms. Errors of commercial judgment (*e.g.*, miscalculating profitability) are not considered "mistakes" in the sense of Articles 3.2.1–3.2.2 of the UPICC. For example, if a party has a correct understanding of the surrounding circumstances but makes an error of judgment as to its prospects under the contract, and later refuses to perform, then the case is one of non-performance rather than mistake.

292. Where both avoidance for mistake and remedies for non-performance are available, Article 3.2.4 of the UPICC gives preference to the latter, as remedies for non-performance allow more flexible and graduated solutions than the drastic remedy of avoidance.

293. Questions relating to mistake may overlap with declarations and assurances (representations and warranties) provisions in the IIC, particularly where such clauses allocate informational risks between the parties.

294. The UPICC provision on threat (Article 3.2.6) may be relevant in the context of IICs. However, a threat constitutes a ground for avoidance only when it is so serious and imminent that the aggrieved party – whether the State or the investor – has no reasonable alternative but to conclude the contract. The seriousness of the threat must be assessed objectively, having regard to all the circumstances of the case.

295. Given the long-term and phased nature of many IICs, there may be situations in which one party becomes vulnerable to undue influence. For example: (i) an investor dependent on sequential permits may be pressured into accepting additional obligations under the IIC, or (ii) a State seeking to retain or expand investment may be pressured where an investor conditions the continuation of existing operations on favourable contractual terms.

**Illustration**

> Upon failure of negotiations between investor A and State party B to expand the former's operations in the territory of B, State party B's authorities threaten A's officers to revoke A's licences to operate in State B unless A commits to additional investment in the building of a new power plant and the signing of a new concession agreement.
>
> The new concession agreement signed between A and B may be avoided on the grounds of threat.

296. The UPICC principle on gross disparity (Article 3.2.7) may be relevant in situations of extreme inequality of bargaining power at the conclusion of an IIC. Under this provision, gross disparity between the obligations of the parties must be such that it gives one party an unjustifiably excessive advantage. Gross disparity may justify renegotiation, adaptation, or – in exceptional cases – avoidance of the contract.

297. Article 3.2.7 of the UPICC applies only to gross disparity existing at the moment of conclusion. It does not address gross disparity arising from subsequent events, a situation which may fall under hardship and change of circumstances (addressed in Chapter 6 of both the UPICC and this Instrument).

298. Any claim based on gross disparity must rely on objective indicators and meet a high threshold, reflecting the gravity of the remedy. Two factors deserve special attention in this connection: (i) the first – unequal bargaining position – consists of one party having taken advantage of the other party's dependence, economic distress or urgent needs, or its improvidence, ignorance, inexperience, or lack of bargaining skill; superior bargaining power due to market conditions alone is not sufficient; and (ii) the second factor to which special regard must be had is the nature and purpose of the contract.

**Illustration**

> In State A, devastated by civil war and lacking both financial and human resources, investor B proposes to reconstruct the country's energy facilities. The parties adopt a Design-Build-Operate-Transfer (DBOT) model of contracting whereby, in the case at hand, State A undertakes to supply coal for an extremely low price for the entire 99-year concession period and to purchase 95% of the electricity produced for the same period.
>
> This situation may amount to gross disparity and lead to a request for the renegotiation, adaptation or avoidance of the IIC.

299. In case of contract avoidance, Article 3.2.14 of the UPICC states that it takes effect retroactively. In other words, the contract is considered never to have existed. In the case of partial avoidance, the rule

applies only to the avoided part of the contract. There are, however, individual terms of the contract that may survive even in the event of total avoidance. Dispute resolution and choice-of-law clauses are considered to have a separate nature justifying their upholding notwithstanding the avoidance of the contract in whole or in part. Whether in fact such clauses remain operative is to be determined by the applicable domestic law.

300. Avoidance of an IIC may affect a significant number of legal relations, either when the IIC project is regulated by multiple contracts (see Principle 5) or when it is linked to supply chain contracts. In this context, the UPICC rule on the retroactive effect of avoidance may be adjusted in order to preserve, for example, the continuity of public services provided under the contract or to otherwise protect the public interest. Thus, the adjudicator may modulate the effects of a judgment or an arbitral award that declares the avoidance of an IIC, for example calibrating it by the fixing of a specific moment from which avoidance produces all of its effects.

**Illustration**

The facts are the same as in the illustration about avoidance for threat.

Upon failure of negotiations between investor A and State party B to expand the former's operations in the territory of B, State party B's authorities threaten A's officers to revoke A's licences to operate in State B unless A commits to additional investment in the building of a new power plant and the signing of a new concession agreement.

Under threat, a new concession agreement is then signed between A and B. Only ten years later a final court judgement is rendered against State party B declaring the new concession agreement void for threat. Meanwhile, A has built the new power plant and fully complied with the new concession agreement.

According to the retroactive approach, the contract is void *ab initio* (*ex tunc*), which means that the parties are placed in the situation they would be in had the concession agreement never been concluded. Accordingly, all performances received must be returned or restitution of their value made.

It would be both inconvenient and impracticable in the instant case to treat the new concession agreement as being retrospectively cancelled. Due to social and public interests, the court may determine that, while damages must be paid in favour of investor A, the concession agreement must stay in force until State party B finds a new concessionaire for the venture.

## D. Illegality

**Relevant UPICC provision**

Article 3.3.1 (Contracts infringing mandatory rules) of the UPICC

**Commentary**

301. While parties are free to enter into a contract and to determine its content, subject to the requirements of good faith and fair dealing, freedom of contract is not without limit. In accordance with Article 3.3.1 of the UPICC, the contract must not violate the applicable mandatory rules. This provision is particularly relevant in the context of IICs, given that by their very nature investment contracts typically pursue public-interest purposes.

302. For the purposes of Article 3.3.1 of the UPICC, the concept of mandatory rules refers to those under Article 1.4 of the UPICC. In other words, the scope is limited to contracts that violate mandatory rules that are applicable in accordance with the relevant rules of private international law. These can have a national, international or supranational origin, be specific statutory previsions or be unwritten general principles of public policy. This implies that an IIC may be considered illegal if its conclusion or performance violates applicable mandatory rules of the host State, the investor's home State, or the mandatory rules of any other jurisdiction that may apply under private international law.

303. The IIC may contain an illegal provision, severable or not. If a court or arbitral tribunal finds that one or more terms of the IIC is illegal or unenforceable, the remaining terms may still be considered valid.

304. As a consequence, an IIC, despite being declared illegal by a court or arbitral tribunal, may be declared to have full effect, some effect, no effect, or be subject to modification.

305. An IIC may be declared illegal because of its purpose or object. For example, an investment contract providing for mining activities in a protected area where such activities are prohibited by law would be illegal. An IIC may also be contrary to public policy, for instance, where it unreasonably restricts competition or economic freedom, such as by granting exclusivity rights to an investor in a manner inconsistent with constitutional or other mandatory economic principles of the host State. An IIC is likewise illegal where it involves bribery or corruption. The applicable mandatory rules may be found in specific statutory provisions or may derive from broader principles of public policy.

306. An IIC may also become illegal in the course of its performance. This may occur, for example, where the subsequent imposition of international sanctions, trade embargoes, or other mandatory measures render performance of the contract unlawful. Thus, the delivery of equipment necessary for the investment project may become prohibited if it would violate an applicable embargo. An IIC may also infringe mandatory rules through the manner in which it is formed or performed. Furthermore, illegality may arise indirectly where the breach of a contractual obligation – such as an anti-corruption undertaking – results in conduct that violates applicable mandatory rules.

307. In some cases, the applicable mandatory rule or the IIC itself expressly specifies the consequences of its infringement, including the contractual or restitutionary remedies, if any, available to the parties. For example, Article 101(2) of the Treaty on the Functioning of the European Union (TFEU) provides that agreements between businesses prohibited under Article 101(1) "shall be automatically void" where they have as their object of effect the prevention, restriction, or distortion of competition and may affect trade between Member States of the European Union. Where the mandatory rule expressly prescribes the consequences of its infringement, those consequences take precedence and leave no room for the application of the general rules contained in this Section.

308. Where the mandatory rule does not expressly prescribe the consequences of its infringement for the contract, the court or arbitral tribunal must determine the appropriate consequences in light of the circumstances of the case. In doing so, it may grant such contractual or restitutionary remedies as are reasonable in the circumstances.

**Model severability clause**

| |
|---|
| If any part, term or provision of this Contract is held to be illegal, invalid or unenforceable, in whole or in part, such term or provision shall, to the extent of its illegality, invalidity or unenforceability, be deemed severable from the remainder of the Contract and shall not affect the validity or enforceability |

of the remaining provisions. The rights and obligations of the Parties shall be construed and enforced as if the Contract did not contain the term or provision so affected.

Where the severance of an illegal, invalid, or unenforceable term or provision materially alters the contractual equilibrium originally intended by the Parties, the Parties shall negotiate in good faith appropriate modifications to restore, to the extent possible, the original balance of rights and obligations under the Contract. Failing agreement, the Contract may be adapted by the adjudicator to the extent reasonable in the circumstances.

### E. Restitution in case of illegality

**Relevant UPICC provisions**

Article 3.3.2 (Restitution) of the UPICC

**Commentary**

309. When an IIC is declared illegal, Article 3.3.2 of the UPICC applies with contextual adaptation, and restitution may be granted where reasonable under the circumstances.

310. Even where, as a consequence of the IIC being declared illegal, the parties are denied any remedies, it remains to be seen whether they may at least claim restitution of what they have rendered in performing the contract. According to Article 3.3.1(1) of the UPICC, the answer first of all depends on the applicable law itself, which may or may not expressly address the issue.

311. If the applicable law is silent on the issue, Article 3.3.2(1) of the UPICC, in line with the modern trend, adopts a flexible approach and provides that where there has been performance under a contract declared illegal, restitution may be granted if this would be reasonable in the circumstances.

312. The criteria laid down in Article 3.3.1(3) of the UPICC for determining whether granting of restitution is reasonable in case a contract is declared illegal may also be used in the context of IICs. Hence, if an IIC is declared illegal and the question of whether restitution should be granted arises, the adjudicator should take into consideration the following criteria: (a) the purpose of the rule which has been infringed; (b) the category of persons for whose protection the rule exists; (c) any sanction that may be imposed under the rule infringed; (d) the seriousness of the infringement; (e) whether one or both parties knew or ought to have known of the infringement; (f) whether the performance of the contract necessitates the infringement; and (g) the parties' reasonable expectations.

**Illustration**

State A's copper mining company (State-owned) enters into a contract with investor B for the re-opening and expansion of a copper mine in its territory.

Some time after the signing of the contract, a new government comes to power in State A and files a lawsuit against its mining company and investor B, alleging that the IIC is illegal because of corruption. Five years later, when the expansion of the copper mine is already completed and fully operational, the court finds that the conclusion of the IIC was indeed influenced by corruption and declares it illegal, null and void.

The anti-corruption legislation in force in State A denies any remedies to the parties but is silent about restitution. Under the circumstances it would not be fair to let State A and its mining company have the

expansion of the copper mine already in operation for free. Thus, investor B may claim restitution of what it rendered in performing the contract.

**Illustration**

State A's state-owned mining company enters into an investment contract with investor B for the re-opening and expansion of a copper mine in its territory.

Some time after the contract is concluded, an NGO brings proceedings against State A, its mining company and investor B, alleging that mining activities in the relevant area are prohibited under applicable environmental legislation. The proceedings remain pending for several years. During that period, the legality of the investment project is repeatedly questioned in public debate and in the course of litigation. Despite these challenges, investor B continues and further expands its mining activities.

Five years later, the court determines finds that the mining activities are indeed prohibited under the environmental laws in force in State A. As a result, the IIC is held to be illegal.

The applicable law denies the parties any contractual remedies and is silent regarding restitution. In these circumstances, investor B may be denied restitution for the performance it has rendered under the contract. Having regard to the protective purpose of the environmental legislation, the fact that investor B continued and expanded the mining activities after their legality had been repeatedly called into question, and the seriousness of the environmental harm that the legislation sought to prevent, granting restitution may be considered unreasonable.

313. Where restitution is granted following the illegality of an IIC, guidance may be drawn from Article 3.2.15 of the UPICC, which governs restitution in cases of avoidance. Under that provision: (a) upon avoidance, either party may claim restitution of whatever it has supplied under the contract, or the part of it avoided, provided that it concurrently makes restitution of whatever it has received under the contract, or the part of it avoided; (b) where restitution in kind is impossible or inappropriate, a monetary allowance must be made whenever reasonable; (c) the recipient of the performance is not required to make a monetary allowance where the impossibility to make restitution in kind is attributable to the other party; and (d) compensation may be claimed for expenses reasonably incurred in preserving or maintaining the performance received.

# CHAPTER 5. RIGHTS AND OBLIGATIONS

## A. Introduction

314. This Chapter sets the stage for investment-related contractual rights and obligations assumed by both the State party and the investor. Such rights and obligations are specific to IICs and cannot be found in the UPICC. It does not provide a comprehensive list of rights and obligations as they are agreed to by the parties and provided in detail in specific IICs. The Principles provided in this Chapter prioritise some general substantive aspects, such as investment protection and sustainability obligations that apply across sectors and are relevant to address critical issues for the modernisation of investment contracting. It also provides, when appropriate, relevant Model Clauses. Depending on the sector and the specific nature of the IIC, the parties will consider the inclusion of further clauses providing substantive commitments specific to that particular type of IIC.

315. The general Principle, Principle 15, in Section B, first states that both parties shall perform their obligations under the contract in good faith and that they must not act arbitrarily or unreasonably. Section C contains four Principles regarding the obligations of the State to protect the investment: namely Principles 16, 17, 18 and 19. Finally, Section D deals with the shared obligations of both the investor and the State party on sustainability, and it consists of three Principles: namely Principles 20, 21 and 22.

316. In Section B, Principle 15 requires the parties to perform the obligations under the IIC in good faith. It is a specific application to investment contracting of the principle of good faith contained in Article 1.7 of the UPICC. It states the need for the specific substantive obligations in the IIC, including those set out in the subsequent Principles in this Chapter (including on sustainability) to be performed in accordance with the principle of good faith. Given the importance of cooperation in IICs as long-term contracts governing a common project, it also relates, more specifically, to Article 5.1.3 of the UPICC, which enshrines the duty to co-operate when such co-operation may reasonably be expected for the performance of the parties' obligations. In addition, it relates to Principle 3 in Chapter 1 of this Instrument on usages and practices and to Article 5.1.2 of the UPICC on express and implied obligations to the extent that an IIC cannot provide or foresee all cases during the lifecycle of an IIC; therefore such principles can assist in determining the precise content of the contract and particularly all acts and conduct required to carry out the agreed performances. Thus, in the context of the performance of the obligations under the IIC, based on Principle 15, the parties must act fairly and reasonably, and not arbitrarily, as well as promptly cooperate to carry out the steps necessary to enable the other party to perform its obligations in line with the usages and practices of the sector.

317. The choice made in this Instrument has been to provide a fully independent contractual standard with fully contractual consequences, meaning that any breach of Principles 16 to 19 entails the right for the party suffering the non-performance to activate the contractual remedies provided in Chapter 7 against the non-performing party. Principle 16 requires the host State or an organ of the State to ensure the necessary physical protection and security of the personnel and assets of the investor in connection with the IIC. It does not include other kinds of legal security. Principle 17 conditions expropriation or nationalisation of the investor's assets by the State or by an organ of the State, or measures of an equivalent nature, upon the pursuit of a public purpose, non-discrimination, observance of due process, and the standard of prompt, adequate and effective compensation. In the case of both Principles 16 and 17**,** the obligation is upon the State or an organ of the State; however, in both cases, where the counterparty is a State enterprise, the relevant Model Clause, rather than imposing a duty on the State or organ of the State to ensure the investor's right, requires the State enterprise to take such steps without which the State or organ of the State would not be placed in a position to uphold the right. This reflects an application of Article 5.1.3 of the UPICC concerning co-operation between the parties. Principle 18 upholds

the investor's right to make all payments and transfers relating to the IIC freely and without delay into and out of the territory of the host State. It includes the right to transfer in a freely usable currency at the market rate of exchange prevailing at the time of transfer. Importantly, the right is not absolute; indeed, the Principle provides for limited temporary exceptions in the public interest by which the host State may prevent or delay a transfer through the equitable, non-discriminatory, and good faith application of its law. Principle 19 imposes upon the State a duty to operationalise and sustain the investment by collaborating with the investor to facilitate smooth administrative processes and enable day-to-day project execution. Its purpose is to foster a transparent and predictable investment climate and treat the investor in a fair and non-discriminatory manner. Additionally, and because of its purpose, Principle 19 is also related to the operation of stabilisation clauses; however, it creates a new cause of action in the event of non-performance of the obligation in Principle 19. The four Principles in Section C relate to Principle 15 (as well as to Article 1.4, Article 5.1.2 and Article 5.1.3 of the UPICC) in that the rights and obligations therein provided shall be exercised or performed in good faith and with a cooperative attitude, such an obligation implying that they have to collaborate to carry out all the reasonable expected steps to enable the other party's performance in line with usages and practices.

318. In Section D, Principles 20 through 22 describe the respective obligations of the State party and the investor on sustainability matters. To that end, Principle 20 emphasises that the commitment to uphold and respect the highest international standards of sustainability is a shared obligation of the State party and the investor. As a result, they shall cooperate to enable compliance with the sustainability obligations they have included in the IIC. Principle 20 also contains a focus on the prevention of adverse effects of the investment project on climate change. Section D.2 provides Model Clauses on sustainability obligations of the investor in the area of human rights, social and environmental commitments, local sourcing of goods and services, community development agreements [and third-party beneficiaries], which the parties may tailor in accordance with the highest international standards they selected as relevant or applicable and in line with the impact of the project. Principle 21 addresses the requirement to put in place a continuous monitoring mechanism on sustainability matters, which is to be viewed as a continuation of the pre-contractual due diligence phase (see Principle 11). The primary responsibility for this continuous monitoring requirement lies with the investor, who shall, however, benefit from the support and assistance of the State party. Finally, Principle 22 seeks to cascade the sustainability obligations undertaken by the investor towards the project's supply chain, thereby promoting an adequate vertical spread of sustainability compliance.

## B. General principle

### Principle 15

**Parties to an IIC shall perform their obligations under the contract in good faith and not act arbitrarily or unreasonably.**

**Commentary**

319. The parties to an IIC shall perform and cooperate for the fulfilment of their obligations in good faith. The parties must perform the obligations under the contract true to their letter and spirit and assume a cooperative attitude when required by the circumstances of the performance. The parties must not act in a manner that frustrates the content and the objectives of the IIC to which they are a party. Equally, the parties shall not act arbitrarily or unreasonably. Performance will be contrary to good faith, arbitrary or unreasonable if it is unsupported by justification, if actions are aimed at inflicting damage on the other party, are abusive towards the other party, arising out of caprice, based on bias or prejudice, or if measures are taken and rights exercised for reasons other than those put forward or for which rights had been

granted, if the exercise of rights is disproportionate to the originally intended result, and in case of wilful disregard of due process.

320. Cooperation in the performance of rights and obligations is especially crucial in IICs, which typically involve complex sequences of interrelated performances. The IIC cannot provide for or foresee all the specific steps that may be necessary to carry out the project's performance in the concrete circumstances. Under this Principle, the duty of cooperation provides guidance on this and implies to refrain from hindering the other party's interests and taking all the affirmative steps reasonably expected to enable the other party's performance, without altering the allocation of duties agreed in the contract or contradicting its express terms.

321. The obligation contained in this Principle applies equally to all the parties to the IIC and must be construed in light of the special conditions that prevail in investment contracting in accordance with usages and practices of the sector and depending on the socio-economic environment in which the parties operate, their capabilities and size.

322. Not hindering, refraining from abuse, not acting arbitrarily or unreasonably, and cooperating are all essential to the performance of IICs. This is due to their distinctive features: the State is a party and may be in the position to exercise its public authority and sovereign powers in a manner that is arbitrary, unreasonable, emulative, or otherwise; the investor is often a powerful player in the sector.

323. On the side of the State, examples of breaches of this Principle might include granting rights or licences to third parties that might interfere with the project; unjustifiably withdrawing or delaying permits, certifications, or licences required for the project; unreasonably refusing to comply with formalities necessary to obtain services; or failing to provide data necessary to run the project. On the side of the investor, examples might be not complying with local laws or regulations, or invoking as an excuse the lack of formalities (*e.g.*, a permit or the registration of a company) for which the investor has not carried out the necessary steps.

324. Both parties are expected under this Principle not to infringe declarations and assurances that have been given to the other party, and not to exert any right under the contract (including triggering expert proceedings, dispute boards, or other dispute settlement procedures) with the intention not to perform, delay performance or exit the contract, or without considering one's own fault or contribution to a non-performance or otherwise harmful event. However, a party performing the IIC according to its terms, even though such performance may negatively affect the other party, does not violate by itself the principle of good faith.

325. Principle 15 reflects a specific application, in the context of IICs, of the principle of good faith embodied in Article 1.7 of the UPICC and the duty of co-operation set out in Article 5.1.3 of the UPICC. In this Principle, good faith is given concrete expression in relation to parties' conduct in the performance of their contractual obligations under an IIC. At the same time, good faith constitutes a broader guiding principle of this Instrument. Its application, as adapted to the particular characteristics of IICs, is specified in several other contexts. It is reflected, *inter alia*, in the pre-contractual phase (Principle 10 in Chapter 3, which specifies the duty of good faith during negotiations), in the context of renegotiation under the economic equilibrium clause (Principle 23(2) in Chapter 6, requiring the parties to renegotiate in good faith), in relation to sustainability obligations (Principle 20 in this Chapter 5, requiring good-faith cooperation between the parties), and in dispute settlement (Chapter 8, where the multi-tiered dispute resolution framework is premised on good-faith engagement at each stage of the process).

**Model Clause**

Each Party shall perform its obligations under this Contract in good faith and shall not act arbitrarily or unreasonably.

In particular, each Party shall:

(a) cooperate with the other Party to carry out all steps reasonably necessary to enable the other Party to perform its obligations under this Contract;

(b) refrain from taking any action that would frustrate the purpose of this Contract or prevent or impair the other Party from receiving the benefits of this Contract;

(c) not exercise its rights under this Contract in an abusive, disproportionate, or vexatious manner; and

(d) have due regard to any declarations, assurances, or undertakings given to the other Party in connection with this Contract.

## C. Obligations of the State on investment protection

326. This Section specifies the obligations of the party on the State side to an IIC.

327. The Principles contained in this Section C are not comprehensive. The aim is to provide obligations that could be frequently found in IICs. Each IIC, depending on the sector and the requirements of the negotiating parties, may provide additional obligations.

### 1. Physical protection and security

**Principle 16**

**Where the counterparty to an IIC under these Principles is a State, that counterparty shall ensure that the personnel and the assets of the investor have necessary physical protection and security in relation to the IIC.**

**Commentary**

328. This Principle aims to ensure the physical protection and security of the personnel and assets of the investor. This protection extends only to physical protection and security and shall not extend to any other form of legal security. The words "ensure" and "necessary" indicate the diligence standard, that is, the extent of action the State is required to take shall be decided based on the overall circumstances of the host State, including its available resources, institutional capacity, and security context. This Principle will be contravened if the State fails to undertake necessary steps to ensure physical protection and security even where the threat has arisen from persons and entities not related to or functioning under the control or guidance of the State.

329. The protection under this Principle applies to activities "in relation to the IIC", *i.e.*, there has to be some connection between the protection sought for the persons and the assets concerned and the IIC. The words in "relation to the IIC" shall be understood broadly. However, activities unrelated to the IIC would not fall under this protection. If the personnel or the assets of the investor are engaged in any activity outside of the IIC, the obligation of the State does not extend thereto.

330. The obligation specified in the Principle applies where the counterparty to the IIC is the State or an organ of the State, which has the direct obligation to ensure the physical protection and security of the

assets and personnel of the investor. In situations where the counterparty is a State enterprise or an entity not controlled by the State, which is not infrequent in IICs, the obligation would not apply. In this situation, the counterparty would not be in the position to provide physical protection and security of the assets and personnel of the investor. The second model clause below suggests that, in such situations, the parties to an IIC agree to add a clause whereby the counterparty which is not the State or controlled by the State undertakes to take necessary steps to persuade the State to ensure physical protection and security of the assets and personnel of the investor. Such a party may have a relationship with the State and its relevant organs with the possibility of encouraging the State and its relevant organs to provide full protection and security.

**Illustration**

If there is general and widespread violence and the forces of the State are occupied addressing equally or more serious security threats on a non-discriminatory basis, this will not constitute failure to provide physical protection and security.

If there is targeted violence against the assets of the investor by private persons, the State will be acting contrary to this Principle if it fails to take necessary action to provide physical protection and security from the threat of action of private persons.

**Model Clause**

Model Clause where a State is the counterparty:

The [*name of the State/name of the ministry or department*] undertakes to ensure that the personnel and the assets of the Investor have necessary physical protection and security to be able to perform the Contract.

Model Clause where a State enterprise or other entity related to the State is the counterparty:

The [*name of the State enterprise or other entity related to the State*] undertakes to take necessary steps to persuade the State to ensure that the personnel and the assets of the Investor have necessary physical protection and security to be able to perform the Contract.

## 2. Expropriation

**Principle 17**

**Where the counterparty to an IIC under these Principles is a State, that counterparty shall not expropriate or nationalise or take other measures which have the same effect or are tantamount to expropriation or nationalisation, of the assets of the investor in relation to the IIC unless**

**(a) for a public purpose;**

**(b) in a non-discriminatory manner;**

**(c) following due process of law; and**

**(d) accompanied by prompt, adequate and effective compensation.**

**Commentary**

331. In this Instrument, the protection from expropriation in Principle 17 is an entirely contractual protection with contractual consequences as specified in the present Principles. Therefore, a breach of the obligation set out by this Principle by the State party shall be treated as a non-performance of the contract, particularly an event of default, and makes available to the investor the relevant remedies as per Chapter 7 of this Instrument, including termination and restitution in Section D as well as compensation and damages in Section F.

332. The parties are invited to consider that the application of this Principle and the drafting of the related model clause may raise issues that need careful consideration during the negotiation. Indeed, the State may wish or be bound to incorporate in the IIC its national standard on expropriation (as likely reflected in its BITs), particularly if deemed to be of a mandatory nature. Whatever standard the parties may wish or be bound to consider, they are invited to assess the beneficial effects of the expropriation standard provided in this Instrument, which is in line with an international understanding of expropriation, and particularly of applying to any non-performance the set of remedies provided in Chapter 7, which provides a framework for a fair and proportionate calculation of compensation and damages, including by resorting to agreed payments for non-performance, limitation of damages and allocation of liability clauses to avoid disproportionate compensation.

333. This Principle protects the IIC as well as the assets of the investor in relation to the IIC from expropriatory measures. An expropriatory measure may be in the form of direct or indirect expropriation. Direct expropriation includes expropriation or nationalisation, whereas indirect expropriation may take any other form of measure adopted by the State party which has the same effect or is tantamount to expropriation or nationalisation. In the case of indirect expropriation, the property may not have been taken but the value of the property would have been lost. The inquiry of whether the measure constitutes indirect expropriation has to be carried out based on the nature or character of the measure and not solely on the effect on the investor.

334. A measure would be of the nature of expropriation or nationalisation if the assets of the investor are transferred to an organ of the State or any other entity, or if the rights under the IIC or the assets of the investor are confiscated or destroyed. A measure would not be of the nature of expropriation or nationalisation if the measure is a legitimate exercise of regulatory freedom and is adopted in good faith (*bona fide*) for protection of the public interest without discriminating against the investor.

335. The adoption of an expropriatory measure is not *per se* illegal as long as it is for a public purpose, applied in a non-discriminatory manner following due process of law and accompanied by prompt, adequate and effective compensation.

336. The contractual obligation specified in this Principle applies where the counterparty to the IIC covered by the present Principles is the State, an organ of the State, or any other entity controlled by the State, depending on how the applicable law regulates their relationship (see commentary under Principle 12 on Legal capacity). In this case, the counterparty has an obligation of result whereby it shall not expropriate or nationalise. The same may hold true in case an IIC entered into by an entity other than the State was formally approved by the State (*e.g.*, through legislation or executive authorisation). By contrast, where the counterparty is a State enterprise or an entity not controlled by the State, such entity would not be in the position to undertake a measure that would constitute expropriation or nationalisation. Also, it may not have control over the State or the organ of the State that would undertake a measure that would

constitute expropriation or nationalisation. The second Model Clause below suggests that, in such situations, the parties to an IIC agree to add a clause whereby the counterparty which is not the State or controlled by the State is limited to "take necessary steps to persuade the State" not to expropriate or nationalise. In such situations, the counterparty has an obligation of conduct and not result.

**Model Clause**

Model Clause where the State is the counterparty:

> The [*name of the State/name of the ministry or department*] undertakes to not expropriate or nationalise or take other measures which have the same nature as expropriation or nationalisation, the Contract or the assets of the Investor in relation to the Contract unless
>
> (a) for a public purpose;
>
> (b) in a non-discriminatory manner;
>
> (c) following due process of law; and
>
> (d) accompanied by prompt, adequate and effective compensation.

Model Clause where a State enterprise or other entity related to State is the counterparty:

> The [*name of the State enterprise or other entity related to the State*] undertakes to take necessary steps to persuade the State not to expropriate or nationalise or take other measures which have the same nature as expropriation or nationalisation, the Contract or the assets of the Investor in relation to the Contract unless
>
> (a) for a public purpose;
>
> (b) in a non-discriminatory manner;
>
> (c) following due process of law; and
>
> (d) accompanied by prompt, adequate and effective compensation.

## 3. Payments and Transfers

**Principle 18**

**(1) The investor has the right to make all payments and transfers relating to the IIC freely and without delay into and out of the territory of the host State.**

**(2) The right of payments and transfers recognised in paragraph (1) includes but is not limited to:**

**(a) contributions to capital, including the initial contribution and additional amounts to maintain or increase the covered investment;**

**(b) profits, dividends, interest, capital gains, royalties, management fees, technical assistance fees, other fees, and other current incomes accruing from covered investments;**

**(c) proceeds from the sale or liquidation of all or any part of the IIC;**

**(d) payments made under the IIC, including payments made pursuant to a loan agreement;**

**(e) payments made by the State for any other purpose relating to the IIC; and**

**(f) payments arising out of a dispute.**

**(3) The right of payments and transfers under paragraphs (1) and (2) above includes the right to transfer in a freely usable currency at the market rate of exchange prevailing at the time of transfer.**

**(4) Notwithstanding paragraphs (1), (2) and (3), the State may prevent or delay a transfer through the equitable, non-discriminatory, and good faith application of its law relating to:**

**(a) the payment of taxes and duties;**

**(b) bankruptcy, insolvency, or the protection of the rights of a creditor;**

**(c) issuing, trading, or dealing in securities, futures, options, or derivatives;**

**(d) criminal or penal offences;**

**(e) financial reporting or record keeping of transfers when necessary to assist law enforcement or financial regulatory authorities;**

**(f) ensuring compliance with an order or judgment in judicial or administrative proceedings; or**

**(g) serious balance-of-payments and external financial difficulties or threat thereof where, in exceptional circumstances, payments or transfers cause or threaten to cause serious difficulties for macroeconomic management.**

**Commentary**

337. The right of payments and transfers, freely and without delay into and out of the territory of the host State, is an essential and indispensable right necessary for the investor to be able to effectively perform the IIC. The recognition of this right under the IIC imposes a corresponding obligation on the State to respect this right. Even where the counterparty is not a State but a State enterprise or other entity on the State side, the right of the investor is recognised. It is immaterial whether that State enterprise or other entity on the State side has any control over the policy of the Government. The absence of such protection will make it impossible for the investor to perform its part of the IIC; hence the right to transfer freely lies with the investor, irrespective of the identity of the counterparty on the State side. To this end, where a State-related entity is party to the IIC, the parties should seek to obtain a specific arrangement, duly approved by the competent authorities, confirming the investor's rights under Principle 18 pursuant to the applicable law and addressing their enforceability vis-à-vis the State entity (see Principle 8, Chapter 2).

338. The right of payments and transfer is wide-ranging and relates to all aspects of the IIC. Such aspects range from all contributions to capital, whether initial contributions or additional amounts, to all amounts received from all transactions undertaken in relation to the IIC, including those relating to the repatriation of investments or the sale of assets or shares. It also extends to payments arising from dispute

settlement proceedings (*e.g.*, amounts awarded pursuant to court judgments, arbitral awards, or settlement amounts).

339. Paragraph (3) specifies that the right of payments and transfers includes the right to transfer in a freely usable currency at the market rate of exchange prevailing at the time of transfer.

340. The right of payments and transfers of the investor is not absolute and is subject to the limitations contained in paragraph (4). These conditions are exhaustive and no additional limitations on the right of payments and transfers of the investor can be imposed by the host State.

**Model Clause**

1. The Investor has the right to make all payments and transfers relating to the Contract freely and without delay into and out of the territory of the Host State.

2. The right of payments and transfers recognised in paragraph 1 includes:

   (a) contributions to capital, including the initial contribution and additional amounts to maintain or increase the covered investment;

   (b) profits, dividends, interest, capital gains, royalties, management fees, technical assistance fees, other fees, and other current incomes accruing from covered investments;

   (c) proceeds from the sale or liquidation of all or any part of the Contract;

   (d) payments made under the Contract, including payments made pursuant to a loan agreement;

   (e) payments made by the State for any other purpose relating to the Contract; and

   (f) payments arising out of a dispute.

3. The right of payments and transfer under paragraphs 1 and 2 above includes the right to transfer in a freely usable currency at the market rate of exchange prevailing at the time of transfer.

4. Notwithstanding paragraphs 1, 2 and 3, the State may prevent or delay a transfer through the equitable, non-discriminatory, and good faith application of its law relating to:

   (a) the payment of taxes and duties;

   (b) bankruptcy, insolvency, or the protection of the rights of a creditor;

   (c) issuing, trading, or dealing in securities, futures, options, or derivatives;

   (d) criminal or penal offences;

   (e) financial reporting or record keeping of transfers when necessary to assist law enforcement or financial regulatory authorities;

   (f) ensuring compliance with an order or judgment in judicial or administrative proceedings; or

   (g) serious balance-of-payments and external financial difficulties or threat thereof where, in exceptional circumstances, payments or transfers cause or threaten to cause serious difficulties for macroeconomic management.

### 4. State cooperation and assistance

**Principle 19**

**The State party has a duty to operationalise and sustain the investment by collaborating with the investor to facilitate administrative processes and enable day-to-day project execution in order to foster a transparent and predictable investment climate and treat the investor in a fair and non-discriminatory manner.**

**Commentary**

341. Principle 19 imposes upon the State a duty to operationalise and sustain the investment by collaborating with the investor to facilitate administrative processes and enable day-to-day project execution. Its purpose, as stated in the Principle, is to foster a transparent and predictable investment climate and treat the investor in a fair and non-discriminatory manner. It represents an application of Article 5.1.3 of the UPICC in the context of IICs. Additionally, Principle 19 is also related to the operation of stabilisation clauses; however, Principle 19 creates a new cause of action in the event of a breach of the obligation contained in this Principle.

342. In IICs, the parties typically provide for cooperation and investor assistance clauses. An assistance clause typically imposes a one-directional obligation on the State to help remove bureaucratic obstacles (such as providing support for visas, permits, or customs clearance), while a cooperation clause would aim to establish a more reciprocal, joint effort framework and imply that the State is not merely a facilitator but a collaborative partner in the success of the investment. However, in practice, the two terms "assistance" and "cooperation" may be used interchangeably.

343. "State cooperation and assistance" provisions normally denote a host-State (or State entity) duty to operationalise and sustain the investment by collaborating with the investor to facilitate administrative processes and enable day-to-day project execution. Such clauses typically cover issues such as: administrative facilitation across land and rights of access, permits, approvals, decrees, and clearances; access to government-held data and provision of relevant information; freedom of movement and rights of access for personnel and equipment; utilities and infrastructure support (such as connection to electricity, water, and sewer networks); security coordination (with possible overlap with PPS); financing interface or recognition of lenders; and providing assistance with obtaining or renewing visas, work permits, and licences. Taken together, these clauses evidence a State commitment to an efficient, smooth and full implementation of the project through collaboration, regulatory compliance, infrastructure development, and targeted governmental support, thereby fostering a transparent and predictable investment climate and aligning with fair and non-discriminatory treatment principles in international investment law.

**Model Clause**

The State must cooperate with and assist the Investor in all matters necessary, which shall include:

(a) promptly processing and issuing all permits, licences, approvals, authorisations, and consents required for the Investor to carry out the Project, and renewing or extending them as necessary;

(b) making available to the Investor, upon reasonable request, all government-held data, geological, geophysical, technical, and other information relevant to the Project, subject to applicable confidentiality restrictions;

(c) facilitating the entry, residence, and work of the Investor's personnel, contractors, and their dependants by processing visas, work permits, and residence permits without undue delay;

(d) facilitating the Investor's access to utilities and infrastructure, including connection to electricity, water, telecommunications, and transport networks, on terms no less favourable than those available to comparable users;

(e) coordinating among its ministries, agencies, and other governmental bodies to avoid conflicting regulatory requirements or administrative delays that would impede the Project;

(f) [*other matters as may be agreed between the Parties having regard to the specific nature of the Project*].

The State's obligation under this Clause is one of best efforts. A failure by the State to fulfil any of the above obligations within a reasonable time, after having been given written notice specifying the failure, shall constitute a non-performance of this Contract entitling the Investor to the remedies provided in [*cross-reference to Chapter 7*].

Commentary to the Model Clause:

344. This Model Clause translates the State's cooperation and assistance obligation into specific, actionable commitments. Sub-paragraph (a) addresses the administrative facilitation of permits, licences, approvals and authorisations, which are essential prerequisites for the commencement and continuation of project operations. Sub-paragraph (b) concerns access to government-held data and information relevant to the project, subject to applicable confidentiality restrictions; this is particularly important in sectors such as natural resources, where geological, geophysical and technical data held by the State may be critical to the investor's operational decisions. Sub-paragraph (c) addresses the facilitation of entry, residence and work permits for the investor's personnel, contractors and their dependents, reflecting the practical reality that international investment projects typically require the deployment of foreign skilled workers. Sub-paragraph (d) addresses access to utilities and infrastructure on non-discriminatory terms. Sub-paragraph (e) requires inter-agency coordination to avoid conflicting regulatory requirements or administrative delays, a frequent source of friction in the implementation of investment projects. Sub-paragraph (f) is a flexible placeholder for additional sector-specific cooperation matters that the parties may wish to include. The closing paragraph establishes that the State's obligation is one of best efforts – a standard that reflects the reality that some matters may be beyond the State's direct control – and provides that a failure to fulfil these obligations, after written notice, constitutes a non-performance of the contract entitling the Investor to the remedies provided in Chapter 7.

## D. Sustainability obligations requiring the cooperation of the State party and the investor

345. As a preliminary observation, it shall be noted that the sustainability obligations described in this Section D do not profess to be exhaustive on the rights and obligations of the parties, such that the parties shall be at liberty to supplement them as they may deem proper.

346. This Section first discusses a joint obligation of the parties towards sustainability (Principle 20) and then focuses on investor obligations (Principles 21 and 22). However, while certain sustainability obligations, such as the obligation to perform continuous sustainability monitoring as described in Principle 21, will be viewed and expressed as obligations falling primarily within the responsibility of the investor, the State party should undertake its best endeavours to support the investor and facilitate the implementation of its obligations. This is important since the State party typically enjoys powers and influence that can be beneficial to the sound accomplishment of numerous sustainability obligations, such as those relating to the consultation of local populations and communities, or may be best placed to provide information relevant to the project, such as data on subsoil, forests and water courses.

### 1. Joint obligations of the State party and the Investor towards sustainability

**Principle 20**

**(1) The parties shall cooperate to perform and abide by the specific sustainability obligations included in their IIC.**

**(2) The parties shall make their best efforts to ensure that the project does not contribute to increasing adverse effects on climate change, in line with the most relevant international and regional instruments in this area.**

**(3) The parties shall make their best efforts to anticipate and adapt to future developments and emerging international sustainability standards and, where necessary, adjust their contractual obligations accordingly.**

**Commentary**

347. This provision establishes the principle of cooperation between the parties in pursuit of the specific sustainability obligations included in their IIC. In particular, it sets out their general obligation to cooperate with each other in order to perform and abide by the specific sustainability obligations that they have jointly decided to include in their IIC, following the pre-contractual due diligence assessment (see Principle 11) and considering relevant hard- and soft-law instruments in the field as agreed or identified as applicable by the parties (see Principle 6). As explained in the commentary to Principle 11 and the accompanying Model Clause, it is expected that the parties will articulate the specific sustainability obligations in their IIC in a manner that is proportionate to the size and capabilities of the parties, and the nature and concrete risk of adverse sustainability impact of the investment project. The aim is to avoid situations where small or low-impact projects are subject to disproportionate obligations, which may be impractical for both the State and the investor, while sustainability obligations are generally expected to be more expansive for large-scale, high-risk projects.

348. It is emphasised that the investor's obligations under this Principle in relation to environmental and social sustainability correspond to the rights of the State (and its local population or parts thereof) to protect the natural and social environment as well as local communities, including Indigenous populations where present in the investment area. Furthermore, the specific reference to the best-efforts obligation of both parties to cooperate in mitigating the adverse effects of climate change also underscores that this obligation ultimately benefits present and future generations.

349. Sustainability is central to the activities of both the State party and the investor (*e.g.*, in the context of consumer protection, financial conduct, mining and extractives, labour and human rights). Sustainability-related issues cover all sectors of business or commerce which encompass the pre-contractual stage (when the contract is negotiated), its delivery and termination, and clean-up activities, where relevant.

350. Regulation of sustainability is governed by a diverse body of hard and soft-law instruments, some of which are rapidly evolving in line with scientific developments. This Instrument therefore does not set out an exhaustive list of such instruments.[30] However, the parties are encouraged to identify, in their IIC or through an exhibit or similar document, the key sustainability standards and regulations that they deem applicable to their investment project and to the specific commitments they included in their IIC (see also the commentary to Principle 6 on "sustainable investment" in Chapter 2 and Principle 11 on "sustainability due diligence in the pre-contractual phase" in Chapter 3).

351. Paragraph 3 of this Principle requires both parties to adjust their contractual obligations to future developments and emerging international standards in the field of sustainability, while taking into account issues of predictability in the mutual interest to preserve the investment relationship and keep a balance

[30] For some examples, see footnotes 6 and 7 under Principle 6.

between rights and obligations. For that purpose, they shall monitor key international fora on environmental and social sustainability and climate change (see also Principle 21 below).

352. In line with the principle enshrined in Article 1.4 of the UPICC, the present provision is without prejudice to the application of mandatory rules of domestic law, whether of national, international or supranational origin, applicable in accordance with the relevant rules of private international law, including general principles of international or transnational public policy.

**Model Clause**

> The Parties shall cooperate to perform the specific sustainability obligations they have undertaken in this Contract. The Parties shall make their best efforts to ensure that the Project does not contribute to increasing the adverse effects of climate change, as well as to anticipate and adapt to future developments in international standards on sustainability relevant to the investment project.

**2. Obligations of the investor on sustainability**

353. IIAs increasingly include sustainability provisions. This is important as similar provisions in IICs need to track those in IIAs. Indeed, IIAs of the third generation often invite States to require the investors of the other State party(ies) to abide by sustainability obligations, with only a few to date using more peremptory language or directly targeting investors with specific obligations.

354. The core differences (for purposes of drafting these clauses) between IIAs and IICs are (i) that the clauses in the IICs will be negotiated (or at least open to negotiation) between the State party and the investor, and (ii) the investor will have obligations against which the State can pursue redress against the investor. On the other hand, in IIAs, the investor does not negotiate the provisions, though it takes the benefit from them, and States may be able to raise a counterclaim but not proactively bring a claim against the investor for breaches of its obligations which the IIAs do not impose on the investor.

355. Specific obligations on investors as to sustainability should be negotiated and included by the parties in their IIC based on the highest international standards that the parties have determined to apply to their IIC (including international agreements and soft-law instruments), domestic policy considerations and relevant applicable norms in the host State, and the results of the pre-contractual due diligence process (see in this regard Principle 6 in Chapter 2, Principle 11 in Chapter 3, and Section D.1 in this Chapter).

356. IICs often include obligations to comply with specific human rights, environmental and social legislation or standards (including on specific emission targets, environmental and social liability, non-discrimination and gender issues, prohibition of child labour, anti-harassment measures, retribution and welfare of workers including services and healthcare, corporate social responsibility and corporate transparency, resettlement of local communities and related indemnification, decommissioning upon site relinquishment). In addition, IICs often include obligations to conclude local development agreements with the host State and/or with representatives of the local community (including by contributing to social, infrastructural or cultural projects, providing financial contributions to local development funds or arranging specific benefit-sharing mechanisms), or to comply with local content obligations (acquisition of local goods and services, contracting local firms, hiring and training local personnel, know-how and technology transfer subject to specific conditions or host State policy on such a matter).

357. The parties may wish to articulate specific sustainability obligations flexibly in accordance with what they deem appropriate to their IIC and the concrete circumstances of the project. The Model Clauses below

are inspired by the ALIC Guide and the IISD Model Contract Clauses for Responsible Investment in Agriculture[31] (as adapted to the scope of this Instrument) as well as available IIC practice. They are offered for the parties' consideration and may be customised, simplified, integrated (including by adding further sector-specific obligations) or supplemented with specific implementation mechanisms in accordance with the parties' needs and any law or standards agreed or identified as applicable. For instance, an agriculture land investment contract may include additional clauses addressing water-use permits and soil management, while a hydrocarbon production sharing contract may include clauses on exploration and drilling operations, the use of water in connection with such operations, or the preservation of the marine environment and fisheries in relation to off-shore operations.

358. [Certain contract clauses may provide to different degrees, depending on the parties' agreement and the law they identified as applicable, enforceable rights against the investor (or the State) in favour of affected third parties (third-party beneficiaries). Such rights, and the procedures for their enforcement, may also be provided under Community Development Agreements, concluded by the Investor with selected subjects, local communities and Indigenous peoples.]

359. The specific sustainability obligations in the contract will be informed by the pre-contractual sustainability due diligence process and any separate negotiations between the parties. Such clauses translate the outcomes of that process into binding obligations applicable throughout the entire lifecycle of the contract. They align with and reinforce the operational measures provided in the management plan and provide the benchmark for reporting, updating, and adaptation under the continuous sustainability monitoring process (see also Principle 21 below).

360. Even though the specific obligations considered under this Section reflect a responsibility of the investor, the Principle on the investor-State obligation to cooperate on sustainability in Section D.1 in this Chapter is to be understood as placing on the State party the obligation to cooperate with the investor in the performance of the latter's sustainability obligations. In addition, the State party itself is bound to respect the highest international standards on sustainable investment that it agreed to respect in the IIC.

361. The parties, and especially the State party, need to keep in mind that numerous obligations suggested in the Model Clause, especially those relating to social commitments or environmental financial securities (*e.g.,* environmental damage bond), will come with certain costs, and these costs will need to be integrated in the price model of the project, failing which the investor will not have the funds to finance the implementation of these obligations. A judgment call will therefore be required by the parties to reach an adequate balance between the economic viability of the project and the desire for a high social impact of the project.

362. Furthermore, it shall be noted that several commitments suggested in the Model Clause, such as those relating to the involvement of local vendors and suppliers, will likely have been expressed in compulsory public bidding documents of the host State and will therefore be transposed to the contract.

**2.1 Model clause on the respect, protection and promotion of human rights**

| |
|---|
| 1. The Investor commits to respect, protect and promote the human rights of all individuals, right holders, workers – with special regard to women and weaker categories of workers – the Local Community, Indigenous Peoples, and any other person likely to be impacted by the Project in the Project |

[31] IISD, The IISD Model Contract Clauses for Responsible Investment in Agriculture, available at https://www.iisd.org/publications/guide/model-contract-clauses-responsible-agriculture-investment.

Area and neighbouring areas, including those human rights relating to health, labour, education, and welfare, including childcare, and the security of persons and groups.

2. The Investor undertakes to avoid causing or contributing to adverse impacts on such rights and to adopt appropriate measures to prevent discrimination and promote equality for marginalised and vulnerable categories, including through a specific gender policy.

Where certain adverse impacts are unavoidable due to the mere fact of implementing the Project, the Investor undertakes to put in place set-off measures to efficiently compensate these adverse impacts.

3. The Investor adheres to, and commits to implement, the following international standards in the field of human rights [*insert relevant documents*].

4. The Investor shall ensure that its operational policies integrate and reflect its commitment to respect human rights under paragraphs 1, 2 and 3 and have the objective of preventing, mitigating, and remediating any potential or actual negative human rights impact.

Commentary to the Model Clause

363. This Model Clause on human rights commitments serves several interconnected functions. Paragraph 1 establishes the overarching obligation of the investor to respect, protect and promote human rights across the full range of individuals and communities likely to be affected by the Project, including workers, local communities, Indigenous Peoples and other potentially impacted persons in the project area and neighbouring areas. This obligation reflects the principles enshrined in the UN Guiding Principles on Business and Human Rights (UNGPs), which articulate the corporate responsibility to respect human rights as a baseline expectation for all business enterprises. Paragraph 2 requires the investor to adopt measures to avoid causing or contributing to adverse human rights impacts and, where such impacts are unavoidable, to implement set-off measures. This mirrors the due diligence approach under the UNGPs and the OECD Guidelines for Multinational Enterprises on Responsible Business Conduct. Paragraph 3 calls on the investor to adhere to and implement specific international standards identified by the parties. The documents to be referenced under this paragraph may include both general instruments – such as the Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural Rights, and the ILO Declaration on Fundamental Principles and Rights at Work – and more specialised instruments related to specific industry sectors. Examples of sector-specific instruments include the Extractive Industries Transparency Initiative (EITI) Standards, which promote transparency in the management of natural resources; the Voluntary Principles on Security and Human Rights, which guide extractive sector companies on maintaining the safety and security of their operations within a framework that respects human rights; and the FAO Voluntary Guidelines on the Responsible Governance of Tenure of Land, Fisheries and Forests and the Principles for Responsible Investment in Agriculture and Food Systems (RAI Principles), particularly relevant for agricultural investments. Paragraph 4 requires the investor to integrate its human rights commitments into operational policies, ensuring that the protection of human rights is embedded in day-to-day management practices and is not merely declaratory.

**2.2 Model clause on social commitments**

1. General commitment. The Investor commits to respect the applicable labour and social legislation in the Host State and to uphold the highest international standards identified as applicable to this Contract in agreement with the State Party, in particular as regards employment, non-discrimination, health and safety, livelihood, basic services and healthcare.

2.1 Employment. The Investor envisages that from the [*Effective*] Date the Project will generate the following positions (the Job Targets):

(a) [*insert number/percentage*] unskilled permanent positions, of which [*insert number*]% shall be held by women;

(b) [*insert number/percentage*] unskilled seasonal positions, of which [*insert number*] % shall be held by women; and,

(c) [*insert number/percentage*] financial, accounting, technical, administrative, supervisory, and senior management positions and other skilled positions (Skilled Positions), of which [*insert number*]% shall be held by women.

2.2 The Investor shall use its best endeavours to achieve the Job Targets.

2.3 One year after the [*Effective*] Date, if the Investor has failed to achieve any one of the Job Targets, the Parties [*and representatives of the workers and the Local Community*] shall [*convene a meeting of the Joint Sustainability Committee (provided under Section D.3 of this Chapter) and*] meet to discuss the reasons for the failure and to negotiate in good faith any necessary variations to the Agreement, including but not limited to:

(a) variations to the Investor's obligations under paragraph 1;

(b) revisions to the Job Targets;

(c) additional obligations regarding training and skills development programmes that can facilitate the achievement of the Job Targets, with special regard to new technology that has impacted the achievement of the Job Targets; and

(d) [*insert other as appropriate*].

2.4 Where the Parties cannot agree as to any necessary variations in accordance with paragraph 2.3, the Parties shall refer the matter to an Independent Expert for final determination [*in accordance with the relevant dispute settlement clause – see Chapters 7 and 8*].

2.5 Access to employment. The Investor shall hire only [*members of the Local Community*]/[*Citizens of the Host State*]/[*Residents in the Project Area*] for unskilled positions.

2.6 The Investor shall provide equitable access to employment for women and men, and shall take all reasonable measures to facilitate women's access to work at the Project Area including:

(a) providing transportation from the local residential areas to the Project Area;

(b) providing [*free*]/[*low-cost*] childcare to Workers with children younger than school age, and for children of school age outside of school hours; and

(c) [*insert other as appropriate for the Project*].

2.7 The Investor shall give preference to qualified [*members of the Local Community*]/ [*Citizens of the host State*]/[*Residents in the Project Area*], and in particular to women, for employment in Skilled Positions, it being the objective of the Parties that the local operations and activities of the Investor under this Contract should be conducted and managed primarily by [*members of the Local Community*]/[*Citizens of the host State*]/[*Residents in the Project Area*], subject, however, to the possibility of involving certain expatriates especially in the early phase of the Project to support its launch and facilitate knowledge transfer.

2.8 The Investor shall ensure that [*members of the Local Community*]/[*Citizens*]/[*Residents*] hold at least [*insert*]% of all management positions within [*insert*] years of the [*Effective Date*] and at least [*insert*]% of such positions within [*insert*] years of the [*Effective*] Date.

2.9 Succession plan. For each management position held by a Worker who is not a Citizen or Resident of the Host State, the Investor shall prepare and submit to the State party a plan for transitioning that position to be held by a Citizen or Resident (a Succession Plan).

2.10 The Succession Plan shall include, where necessary, provision for on-the-job mentorship by the incumbent in the position of a Citizen or Resident who shall take over the position. The State Party may, at its discretion, transmit the Succession Plan to the immigration authorities for their consideration in reviewing any application for immigration permits made by the Investor.

2.11 Subject to this clause, the Investor shall be entitled to freely choose its senior management [*and the Host State shall facilitate such Persons to obtain the necessary immigration approvals and permits for themselves, their spouses, and dependents*] in accordance with the applicable law.

2.12 The Investor shall report annually on its compliance with this clause, within a dedicated section of the report on implementation under the continuous monitoring mechanism [*provided under Section D.3 of this Chapter*], using gender-disaggregated data, indicating:

(a) the status of the Investor's achievement of the Job Targets;

(b) the number of unskilled positions and Skilled Positions held by [*members of the Local Community*]/[*Citizens of the Host State*]/[*Residents in the Project Area*];

(c) the percentage of senior management positions held by [*members of the Local Community*]/[*Citizens of the Host State*]/[*Residents in the Project Area*]; and

(d) the measures taken by the Investor to facilitate women's access to jobs and to ensure equal pay for equal work.

3.1 Training and skills development. In order to meet the objectives of paragraph 2 of this clause, the Investor shall:

(a) develop and implement on-the-job training for [*Members of the Local Community*]/[*Citizens of the Host State*]/[*Residents in the Project Area*], to enable them to qualify for Skilled Positions, including programmes for women adapted to their needs;

(b) provide a total of [*insert amount and currency*] annually in scholarships for [*Members of the Local Community*]/[*Citizens of the Host State*]/[*Residents in the Project area*] through a programme to be administered by the Investor, and establish a quota for women and girl scholarship recipients;

(c) provide [*insert amount and currency*] annually in support to the [*nominate a relevant national research or academic institution*] setting aside [*insert amount*]% for research and academic training for [*Members of the Local Community*]/[*Citizens of the host State*]/[*Residents in the Project area*], and establish a quota dedicated to women and girls;

(d) deliver or contract to deliver adult literacy (including digital literacy) and basic education programmes for Workers, separately for women and men upon request;

(e) deliver or contract to deliver social and economic education programmes for Workers on topics such as human rights, environmental, social and health awareness, household nutrition, managing personal finances, adapted separately to the needs of women and men; and

(f) [*insert other as appropriate for the Project*].

3.2 The Investor shall prepare a detailed Training and Skills Development Plan including:

(a) a description of how the Investor intends to meet each of its obligations in paragraph 3.1;

(b) provisional training schedules, content, and curricula;

(c) an indication of the amount of funding committed to the delivery of the Training and Skills Development Plan; and

(d) any other information as the State party may reasonably request.

3.3 The Investor shall submit the Training and Skills Development Plan to the State Party no later than [*XX*] months from [*the Effective Date*]. The Training and Skills Development Plan submitted by the Investor shall be subject to review, comment, and request for modification by the State Party.

3.4 The Investor shall report annually within a dedicated section of the report on implementation under the continuous monitoring mechanism [*provided under Section D.3 of this Chapter*] on its progress in implementing the Training and Skills Development Plan, detailing outcomes separately for women and for men, and notifying the State party of any challenges to implementation and necessary adjustments to the Training and Skills Development Plan.

4.1 Labour standards. The Investor, its Affiliates, contractors, and subcontractors shall follow internationally recognised labour standards enshrined in the International Labour Organization agreements or any other international agreement to which the Government of the Host State is or becomes a party, and shall respect as provided therein the right of its Workers to associate and organise to promote their rights.

4.2 The Investor, its Affiliates, contractors, and subcontractors shall not use forced labour, or child labour [*as defined by international standards and the applicable law on labour*], or employ a child in any manner that is likely to be hazardous or to interfere with the child's education, or to be harmful to the child's health or physical, mental, spiritual, moral, or social development.

4.3 The Investor shall adopt a health and safety management system that shall meet or exceed [*IFC Performance Standard 2*] and [*the World Bank Group Environmental, Health and Safety (EHS) Guidelines or any other standard relevant to the industry sector the parties identified as applicable to their IIC*].

4.4 The Investor shall provide a legally binding written contract of employment stipulating at a minimum a job description, working hours, appropriate retribution and rate of pay to all Workers, including temporary Workers engaged for 7 days or more, and an appropriate welfare scheme in line with the applicable law and international labour standards.

4.5 For all Workers engaged for at least 3 months in the year, the Investor shall provide [*XX*] days of sick leave, which shall apply to the needs of women to attend medical appointments related to pregnancy or other reproductive health matters.

4.6 The Investor shall provide paid maternity leave [*in accordance with the applicable law*]/[*for a minimum duration of 14 weeks*[32] *and at a minimum of two-thirds pay*].

5.1 Non-discrimination in labour practices. The Investor shall not engage in or support discrimination in hiring, remuneration, access to training, promotion, termination, or retirement based on race, national or social origin, caste, birth, religion, disability, gender identity, family responsibilities, marital status, HIV/AIDs status, pregnancy, union membership, political opinions, or age.

5.2 The Investor shall develop and implement a policy prohibiting such forms of discrimination referred to in paragraph 5.1 and outlining fair disciplinary measures to be taken against any Worker or manager found to engage in such practices.

[32] Convention No. 183 concerning the Revision of the Maternity Protection Convention (Revised), 1952, Article 4.

5.3 The Investor shall not engage in testing for pregnancy or HIV/AIDS status when hiring.

5.4 The Investor shall not dismiss any woman for becoming pregnant or for taking or requiring maternity leave.

5.5 The Investor shall provide at least two daily breaks for breastfeeding mothers for up to 1 year after the birth of a child.

5.6 The Investor shall put in place a policy to prevent, mitigate, and sanction sexual harassment, sexual exploitation, and sexual abuse of and by its Workers. For the purposes of this clause:

(a) "Sexual exploitation" means any actual or attempted abuse of a position of vulnerability, differential power or trust for sexual purposes, including, but not limited to, profiting monetarily, socially, or politically from the sexual exploitation of another.

(b) "Sexual abuse" means actual or threatened physical intrusion of a sexual nature, whether by force or under unequal or coercive conditions.

(c) "Sexual harassment" means any unwelcome sexual advances, request for sexual favours, and other verbal or physical conduct of a sexual nature.

5.7 The Investor shall appoint a female ombudsman or female senior manager to receive sexual harassment grievances put forth by women and direct them to managers with disciplinary authority, ensuring that the identity of the survivor is not disclosed and her safety is guaranteed.

6.1 Health and safety standards. The Investor shall comply with the applicable law and observe Good Industry Practice for the protection of the general health and safety of its Workers, other persons contracted by the Investor on the Project Area, and all other persons near the Project Area whose health and safety are affected by Project activities, including women and children being subjected to sexual violence, in line with or exceeding [*IFC Performance Standard 4 or any other standard identified and agreed by the parties*].

6.2 The Investor shall install and use such recognised modern safety devices and equipment and observe such recognised modern safety precautions as are provided for under the applicable law and observed under Good Industry Practice.

6.3 Workers shall have the right to recuse themselves from tasks they consider dangerous to their safety or health, including risks faced by pregnant or nursing mothers to the health of their unborn or newly born children, without risk or fear of punishment or retaliation.

6.4 Pregnant and nursing women shall not engage in, nor shall they be asked to engage in hazardous or arduous work, such as handling chemicals and heavy lifting.

6.5 The Investor shall train its Workers in accordance with the applicable law and generally accepted health and safety procedures and practices, including those associated with [*specify depending on the type of investment project, e.g., the management of chemicals, the operation of machinery, equipment, and infrastructure*,] and the provision of first aid.

6.6 The Investor shall produce within a dedicated section of the report on implementation under the continuous monitoring mechanism [*provided under Section D.3 of this Chapter*] an annual health and safety report documenting, separately for women and men, health and safety trainings conducted, accidents and injuries in the workplace, complaints received from Workers, and actions taken by management in response to Worker accidents, injuries, and complaints.

6.7 The Investor shall clearly indicate workplace hazards, safety guidelines, and hygiene requirements with signage in the languages spoken by Workers and including pictograms wherever possible to ensure accessibility for Workers with low literacy.

6.8 Health and safety committee. The Investor shall facilitate the creation by Workers of a Health and Safety Committee in representation of Workers, including an equitable representation of women and men, and to serve as mechanism for communicating Workers' concerns and complaints about workplace safety and health to the senior management. The Health and Safety Committee shall be co-headed by one male and one female health and safety representative.

6.9 Emergency Preparedness Plan. The Investor shall prepare for submission to the State party, in consultation with the Local Community and local authorities, an emergency preparedness plan to respond to extreme hazardous events or accidents, including climate change-related extreme weather events and other emergencies at or near the Project Area, including:

(a) a clear identification of the emergency response measures that are the responsibility of the Investor in times of emergency, such as early warning and evacuation;

(b) a clear identification of lines of communication between the Investor, Local Community, and local authorities during times of emergency; and

(c) a communication and outreach strategy to convey the emergency preparedness plan to the Local Community and local authorities.

7.1 Livelihood, water services and healthcare. The Investor shall provide secure, safe, and suitable residential facilities for women and men Workers and related secure tenure, adequate sanitation, including indoor bathrooms, energy for cooking, heating, lighting, food storage and waste disposal, and safe areas for children's recreation, including by building new facilities or restructuring available ones, if so agreed. The Investor shall ensure that all public spaces and shared sanitation facilities are well-lit, secure, and safe.

7.2 The Investor shall ensure all Workers' residential facilities a regular supply of clean and safe drinking water if they reside at the Project Area, and shall ensure that providing that all common water sources are easily accessible from the Workers' residential facilities within the Project Area and that Workers are provided with equipment to facilitate carrying and storing water, if supplied from a common source.

7.3 The Investor shall construct, maintain, and operate a [*hospital]/[clinic*]/[*health center*]/[*insert other health or medical facility*] to serve Workers and their Dependents [*and the Local Community*], using modern health devices and equipment and practising modern health procedures and precautions, in accordance with the applicable law and accepted international medical standards.

7.4 The Investor shall provide, free of charge:

(a) annual medical examinations at the Project Area to Workers [*and members of the Local Community*];

(b) medical treatment on demand to Workers suffering a work-related accident, injury, or illness; and

(c) regular medical examinations to pregnant and nursing mothers and their children under the age of 5 who are [*Dependents of Workers*]/[*Members of the Local Community*].

The Investor shall facilitate Workers and their Dependents to access specialised care beyond the Project Area where necessary.

7.5 The Investor shall establish and implement policies to prevent and deal with the spread of infectious and contagious diseases in and around the immediate Project Area. In the event of an epidemic, pandemic, or outbreak of disease, the Investor shall work with the local authorities in taking measures to ensure health and safety within the Project Area.

7.6 The Investor shall facilitate access for Workers and their Dependents to gender-based violence protection services operated by public, private, or civilian institutions.

7.7 The Investor shall contribute [*insert amount and currency*] annually to a government-administered and operated health education and awareness programme in the Project Area, with priority for women and children who are [*members of the Local Community*]/[*Dependents*].

Commentary to the Model Clause

364. This Model Clause on social commitments is one of the most detailed in this Instrument, reflecting the critical importance of social outcomes in IICs. The clause is structured around several groups of provisions, each addressing a distinct aspect of the Investor's social obligations. Paragraphs 1 to 2.12 address the Investor's employment obligations, including the establishment of quantitative job targets (including gender targets), preferential hiring of local community members and host State citizens (including in management positions for the purpose of facilitating knowledge transfer), equitable access to employment for women and men, and annual reporting requirements using gender-disaggregated data. These provisions interact closely with host State labour and social legislation: the clause requires compliance with applicable domestic law while also mandating adherence to the highest applicable international standards, thereby creating a dual compliance framework that ensures that the more protective standard prevails. Paragraphs 3.1 to 3.4 establish obligations on training and skills development, including scholarships, support for national research institutions, and adult literacy programmes, all with dedicated quotas for women and girls. Paragraphs 4.1 to 4.6 address labour standards, including the prohibition of forced and child labour, the adoption of health and safety management systems (referencing IFC Performance Standard 2 and the World Bank Group EHS Guidelines), and the provision of written employment contracts and paid maternity leave. Paragraphs 5.1 to 5.7 address non-discrimination in labour practices, including a comprehensive prohibition on discrimination, mandatory anti-discrimination policies, and specific provisions on the prevention, mitigation and sanctioning of sexual harassment, sexual exploitation and sexual abuse. The emergence of gender-sensitive and anti-sexual harassment provisions in IICs reflects a growing trend in international contracting practice, as demonstrated by the inclusion of such requirements in the FIDIC Conditions of Contract (2017 editions and subsequent updates) and in the procurement and safeguard policies of multilateral development banks such as the Asian Development Bank (ADB), the World Bank and the European Bank for Reconstruction and Development (EBRD). Paragraphs 6.1 to 6.9 deal with health and safety standards, including the establishment of health and safety committees with equitable gender representation and the preparation of emergency preparedness plans. Paragraphs 7.1 to 7.7 address livelihood, water services and healthcare, requiring the Investor to provide residential facilities, clean drinking water, medical facilities and health education programmes. These provisions are designed to be adapted to the specific characteristics and needs of each project and local community.

**2.3 Model clause on local sourcing of goods and services**

1. Upon purchase of goods, services or materials, the Investor shall follow an efficient, open, transparent, non-discriminatory and competitive purchasing and award procedure in accordance with the applicable law and best international industry practices, including applicable anti-corruption standards. In this context, the Investor shall provide local enterprises opportunities, in competition with foreign entities, to provide any goods and services required in connection with the Project Operations in line with the commitments undertaken in this Contract and with the host-State policy under the applicable law. The procurement procedures shall contain appropriate measures to ensure the Investor's compliance in this regard.

2. In particular, in the procurement related to the Project with external vendors, suppliers and subcontractors, the Contractor shall give preference to goods that are produced or available in the Host State and services that are rendered by natural or legal persons which are, or which are controlled by, [*members of the Local Community*]/[*Citizens or Residents of the Host State*], provided that such goods and services are offered on terms equal [*comparable*] to or better than imported goods and services with regard to price, quality, availability at the time and in the quantities required, and performance. The Investor shall further give preference to local goods and services supplied by [*women*]/[*Indigenous Peoples*].

3. Price under paragraph 2 shall be determined based on Market Rules or, in the case of transactions with related parties, based on the Transfer Pricing Guides for Multinational Companies and Tax Administrations approved by the Council of the Organization for Economic Cooperation and Development.

4. Locally produced or available equipment, materials, supplies and services shall be deemed equal [*or comparable*] in price to imported items or services if the local cost of such locally produced or available items and services at the Investor's operating base in the Host State is not more than ten percent (10%) higher than the cost of such imported items before customs duties after transportation and insurance costs have been added.

5. To ensure compliance with the previous paragraphs, the Investor shall:

(a) ensure that subcontracts are sized, as far as it is economically feasible and practical, to match the capability (time, finance and manpower) of Local Enterprises and shall manage the risk to allow their participation, including where practicable by dividing large contracts for the procurement of goods and services into smaller contracts to facilitate suppliers of local goods and services to bid for those contracts and by incorporating high weighting on local value added in the tender evaluation criteria;

(b) provide annually to the State party [*together with the Project Operations work programme*] a list of all projects to be undertaken as well as all goods and services that are required for the conduct of the Project Operations [*and establish in agreement with the State party the estimated value of local goods and services to be allocated to Local Enterprises if conditions under previous paragraphs are met*];

(c) elaborate, in agreement with the State party, in a transparent manner and in consultation with the Local Community, a list of suppliers of local goods and services [*Local Enterprises*] [*further identifying women/Indigenous Peoples suppliers*];

(d) give equal treatment to Local Enterprises by ensuring access to all tender invitations, particularly by advertising, evaluating and awarding such tenders in the Host State, providing in a publicly assessable format and in local languages information about upcoming tenders, and disseminating information on the bids through widely accessible media [*and forms of communication known to be used by women and Indigenous Peoples*].

6. The Investor shall give assurance to Local Enterprises in respect of prompt payment for goods and services actually provided to the Investor and its Subcontractors both foreign and local.

7. The Investor shall report annually within a dedicated section of the report on implementation under the continuous monitoring mechanism [*provided under Section D.3 of this Chapter*] on the value of local goods and services procured for the purposes of the Project [*which shall specify the value of local goods and services procured from* [*women*]/[*Indigenous Peoples*].

8. The Investor shall include in each contract for the procurement of goods or services in relation to the Project a clause indicating the monetary value of [*insert amount and currency*] relating to the goods

and services to be purchased from Local Enterprises and requiring the other contracting Party, and any of its subcontractors, to comply with the requirements provided under the previous paragraphs, when applicable.

Commentary to the Model Clause

365. This Model Clause on local sourcing of goods and services addresses a subject of considerable importance in IICs: the requirement that the investor contribute to local economic development through the procurement of goods and services from local enterprises. The clause is structured to reconcile the legitimate interest of the host State in promoting local content and industrial development with the investor's need for efficient and competitive procurement. Paragraphs 1 and 2 establish the general principle of local preference, subject to the condition that local goods and services are offered on terms equal or comparable to imported alternatives in terms of price, quality, availability and performance. This conditionality is essential to ensure compatibility with the international trade framework, including the obligations that host States may have under the WTO Agreement on Government Procurement (GPA) or regional trade agreements. Paragraph 3 provides that prices shall be determined based on market rules or, for related-party transactions, the OECD Transfer Pricing Guidelines, thereby introducing an objective standard to prevent manipulative pricing practices. Paragraph 4 provides a practical tolerance threshold (10% price differential) to facilitate the participation of local suppliers, recognising that strict price parity may not always be achievable for local enterprises that face structural cost disadvantages. Paragraph 5 details the operational measures the Investor must take to ensure compliance, including the sizing of subcontracts to match the capability of local enterprises, the annual provision of procurement lists to the State party, and the elaboration of lists of local suppliers in consultation with the local community. These measures are intended to promote transparency and to create tangible opportunities for local enterprises to participate in the investment project. The purpose of local content clauses in IICs extends beyond the immediate procurement of goods and services: they are instruments of industrial policy aimed at fostering know-how transfer, building local productive capacity, and contributing to the long-term economic growth of the host State. In this respect, the local sourcing provisions should be read in conjunction with the Model Clauses on Community Development Agreements (Section D.2.5 below), which address the broader framework for the Investor's contributions to local community development.

**2.4 Model Clause on environmental and climate commitments**

1. Compliance with International Standards and Domestic Environmental Laws. The Investor shall comply at all times during the term of this Contract with the international standards (including internationally recognised practice of the industry) and the Host State legislation identified as applicable by the Parties relating to the environment, including standards and laws relating to protection of flora and fauna, water quality, air quality, quality of land and soils, sea and water courses, the preservation of living natural resources, the protection of biodiversity, the disposal of hazardous and non-hazardous wastes, and the reduction and capture of greenhouse gas emissions.

2.1 Commitment to continuous improvement in production methods and green technologies. The Investor commits to pursuing continuous improvements in methods of production and green technologies, in ways that produce equal benefits for people of all genders and social groups, including Indigenous Peoples, in order to:

(a) reduce greenhouse gas emissions generated by the Project;

(b) capture and store carbon through the Project Operations;

(c) support to the Local Community to build resilience and adapt to climate change, [*access climate-resilient production technologies*]/[*access payments for ecosystem services*]/[*insert other as appropriate for the project*];

(d) prevent deforestation and desertification, restore deforested areas, and restore and protect biodiversity [*including through agro-ecological practices such as agroforestry and [insert other practices)*];

(e) reduce air and freshwater pollution and land [*and sea*] contamination; and

(f) [*insert other environmental objectives*].

2.2 The Investor further commits to upgrading production technology where new technologies become available that would improve production methods in pursuit of the objectives described in paragraph 2.1.

2.3 The Investor shall outline how it intends to implement this clause in the Environmental and Social Sections of the Management Plan (as provided under the clause on pre-contractual sustainability due diligence), including by identifying specific priority areas and actions; a list of indicators and time-bound targets for those actions, the distinct or shared benefits for the Local Community from improvements to methods of production, and a description of how the priority areas and actions contribute to or align with the Host State's environmental policy under [*national adaptation plan*]/[*nationally determined contributions under the Paris Agreement under the United Nations Framework Convention on Climate Change*]/[*just energy transition investment plan*]/[*insert other policies of the Host State relating to climate change, biodiversity, pollution reduction, or the environment*].

2.4 Environmental Performance Payments. Where the Investor identifies a possible improvement in methods of production, acquisition of new technology, or other positive environmental outcome from the Project that is likely to incur a non-minor cost to the Investor, the Investor may request the [*State Party/Competent Authority in the Host State*] to consider the provision of a performance-based incentive or other benefit (the Environmental Performance Payment) agreed by the Parties for the implementation of that method of production, acquisition of that technology or achievement of that environmental outcome. Any such agreement for the provision of an Environmental Performance Payment shall be evidenced in writing and shall be incorporated into this Contract subject to [*the relevant requirements for the modification of this Contract as provided in (insert clause)*]. The [*State Party/Competent Authority in the Host State*] shall give priority consideration to a request for an Environmental Performance Payment for an improvement in methods of production or positive environmental outcomes in the area of [*insert priority areas as appropriate*]. The Investor shall report annually on measures undertaken to comply with this clause and provide, where necessary, a review and update of the priority areas, indicators, and time-bound targets referred to in paragraph 2.3.

2.5 Carbon and other Environmental Credits. The Investor shall have the right to apply for or obtain any Greenhouse Gas (GHG) Reduction Benefits that could be generated from the Project, the Project land or any aspect of the Investor's operations. To the extent any GHG Reduction Benefits are generated by the Investor from the Project, such Benefits shall be co-owned by the Parties save the right of the Investor to market and sell all the GHG Reduction Benefits generated by the Project, the Project land or any aspect of the Investor's operations and to determine the timing and circumstances of such sale. If and when any revenues are received from any sale of GHG Reduction Benefits, the revenues less costs and expenses associated with pursuing, applying for, obtaining, marketing and selling such GHG Reduction Benefits shall be distributed to the Parties as follows: (a) [*fifty per cent (50%)] to the Investor*; and (b) [*fifty per cent (50%) to the State [State entity*].

3.1 Climate change commitments. The Investor shall quantify and report annually on the greenhouse gas emissions generated by the Project, in accordance with the [*Applicable Law*]/[*Greenhouse Gas*

*Protocol Corporate Accounting and Reporting Standard or [insert reference documents as identified by the Parties as applicable and/or appropriate]*].

3.2 The Investor shall reduce the greenhouse gas emissions of the Project annually [*and shall in any event aim to achieve net-zero emissions by no later than [XX] years after the Signature Date. Where, at least [XX*] years after the Signature Date, the Investor has not reduced the greenhouse gas emissions of the Project such that the Project is on track to achieve net-zero emissions within this timeframe, the Parties shall meet to discuss the reasons for this and to negotiate in good faith any necessary variations to this Contract, including but not limited to changes to Project Operations practices, transportation, land use, acquisition of new technologies, or any other aspect of Project Operations, and [*insert other as appropriate*].

3.3 The Investor shall contribute [*insert amount and currency*] annually to a local climate change adaptation fund that shall be used to finance climate change adaptation projects identified by the Local Community in accordance with the Community Development Agreement(s) referred to in [*insert relevant clause, see Model Clause in Section D.2.5 of this Chapter*].

3.4 The Investor shall commit [*insert amount and currency*] annually to providing technical support and capacity development for [*the Local Community*] on [*climate-resilient technologies and practices]/[accessing markets for payments for ecosystem services*]/[*insert other as appropriate for the Project*]. The Investor shall report annually on its implementation of this paragraph.

3.5 The State Party, in collaboration with the Competent Authority of the Host State, reserves the right at any time to seek renegotiation with the Investor of any term of this Contract as it deems necessary for the Government of the Host State to meet its nationally determined contributions under the Paris Agreement under the United Nations Framework Convention on Climate Change, as may be adopted or amended from time to time [*subject to stabilisation obligations assumed by the State Party and to agreed exclusions to the stabilisation commitment*].

3.6 The Parties recognise that the Government of the Host State retains the right to enact and enforce *bona fide* laws and regulations in relation to the production and distribution of carbon-based energy sources and measures to address climate change, and other public-interest issues such as air quality. Nothing in this Contract shall restrict or alter this right or create or imply any limitation on the Government of the Host State, or any obligation to pay compensation with respect to future measures in this regard [*subject to stabilisation obligations assumed by the State Party and to agreed exclusions to the stabilisation commitment*].

4.1 Waste and chemical management. The Investor shall comply with the international standards (including internationally recognised industry practices) and Host-State legislation agreed and identified by the Parties as applicable to this Contract regarding the handling, transport, storage, and use of all waste and chemical substances in the Project Area, including [*insert as appropriate*]. This shall include, where applicable, international standards, laws and regulations governing Workers' safety and human health as well as environmental protection.

4.2 The Investor shall ensure that all Workers working with chemical substances are trained and certified (where applicable) in the handling and use of all chemicals. This includes, when appropriate, separate training for women and men that is adapted to the specific activities they perform, the hazards to which they are exposed and the different health consequences of those hazards, and to their literacy levels. The Investor shall ensure that pregnant and breastfeeding women are not engaged in any work with hazardous chemicals.

4.3 The Investor shall follow manufacturers' guidelines and directions regarding the dosage, dilution, application, and expiry dates of all chemicals, and shall report all chemical accidents or spills to the relevant authorities.

4.4 The Investor shall maintain a record, using gender-disaggregated data that distinguishes accidents, illnesses, and other incidents related to damage or potential damage from chemicals experienced by women and men.

4.5 The Investor shall comply with the international standards and applicable law, as referred to in paragraph 4.1, relating to waste management and shall endeavour to develop approaches to reduce the consumption of the Project and to recycle production materials and waste products generated by the Project.

5. Traditional knowledge. The Investor shall respect and protect the traditional knowledge, the biodiversity-related traditional knowledge, and the cultural heritage, archeologic, traditional, religious and sacred sites of the Local Community and the Indigenous Peoples settled in the investment and neighbouring areas and shall comply with all international standards and the applicable law relating to the same.

6. A significant and persistent failure to comply with the international standards and applicable law relating to the environment, as well as of the terms of any applicable licence relating to the environment or of the provisions of the Environmental and Social Sections of the Management Plan, as they may be revised or changed from time to time, constitutes a fundamental non-performance of this Contract.

7. Monitoring, reporting, and disclosure. The Investor shall at all times cooperate with the State Party [*and the Competent Authorities*] for the monitoring, reporting and enforcement of all provisions of this Contract, the agreed international standards and the applicable law in relation to the environment, and shall in particular:

(a) ensure that all reports required under this clause, as dedicated sections of the broader continuous monitoring process under [*insert clause*], are provided in a timely manner and with the requisite level of detail, so as to facilitate effective monitoring by the State Party [*and the Competent Authorities*] of the Investor's obligations under this Contract, the agreed International standards and the applicable law relating to the environment;

(b) disclose in a prompt and transparent manner any environmental risks or damage that arises during the term of this Contract, in such a manner as to enable a prompt and effective response to that risk or damage by the Parties.

8.1 Certification and Environmental Audit: The Investor shall, within [*XX*] years from the Signature Date, obtain certification of the Project from the [*insert applicable scheme*] and shall at all times comply with the requirements of that certification scheme so as to maintain certification for the duration of this Contract.

8.2 The Investor shall engage an independent professionally qualified auditor to conduct an environmental audit that shall comply with the requirements of [*the applicable law*]/[*ISO 14001*]/[*insert other relevant standard*] and that shall be carried out:

(a) within [*insert number*] month(s) of the Signature Date (the Initial Environmental Audit); and

(b) within [*insert number*] month(s) of the end of this Contract in accordance with its terms (the Final Environmental Audit); and

(c) every [insert number] years during the term of this Contract.

8.3 Each environmental audit shall be carried out [*at the expense of the Investor*]/[*at the joint expense of the Parties whereby the Investor contributes [insert number]% and the State party [the Competent Authority] contributes [insert number]%*].

8.4 The Investor shall provide to the State party [*and the Competent Authority*] the results of each environmental audit, accompanied by an action plan detailing any steps which the Investor intends to take to address any areas of concern or non-compliance identified in the environmental audit, and to remediate or compensate for any environmental damage identified by the environmental audit, in accordance with this clause.

9.1 Liability for environmental damage. The Investor shall bear all responsibility for any environmental damage or contamination caused to the Project Area, surrounding areas and nearby natural resources caused by Project Operations including the Investor's use of chemicals, release of pollutants, depletion of [*air, land, water courses or sea*] quality or other adverse environmental impacts [*insert other environmental impacts as appropriate*] (the Environmental Damage).

9.2 The Investor shall bear all costs associated with the prevention, control, and clean-up of Environmental Damage and shall be liable for the costs of remediation and repair of Environmental Damage and compensation to any affected persons suffering loss caused by the Environmental Damage.

10.1 Project closure and restoration of the environment (decommissioning): at the end of this Contract by way of expiry or termination in accordance with its terms, the Investor shall return the Project Area to the State Party in substantially the same or better condition as that in which it was granted, as identified by the Initial Environmental Audit.

10.2 Where the Final Environmental Audit identifies Environmental Damage that was not identified in the Initial Environmental Audit, such Environmental Damage shall be attributed to the Project Operations and shall be remediated, restored, or compensated at the expense of the Investor in accordance with this clause, international standards (including internationally recognised industry practices) and the applicable law.

10.3 Within one month after the submission of the Final Environmental Audit to the State Party [*the Competent Authority*], the Parties shall meet to negotiate in good faith an action plan outlining actions to be taken by the Investor to remediate or restore any Environmental Damage, and timeframes for the Investor to take those actions.

10.4 Where there is Environmental Damage that cannot be reasonably remediated or restored by the Investor, the Parties shall negotiate in good faith an amount of monetary compensation payable by the Investor to the State party and/or other parties affected by the Environmental Damage, and the currency and payment plan for such compensation.

11.1 Environmental Damage Bond: The Investor shall provide and deliver, within one (1) month after the Signature Date, to the State Party an unconditional and irrevocable bank guarantee as security for the remediation or restoration of any Environmental Damage (the Environmental Damage Bond) which shall:

(a) be in favour of the State Party [*the Competent Authority/any other entity, as appropriate*];

(b) be issued by a bank acceptable to all Parties;

(c) be valid until [*insert*];

(d) be in the amount of [*insert amount and currency*];

(e) constitute an on-demand, unconditional, and irrevocable commitment to pay by the bank by which it is issued; and

(f) be enforceable and drawable by the State Party [*the Competent Authority/any other entity, as appropriate*] in the amount required to remediate or restore any Environmental Damage identified in accordance with this clause and/or to compensate any affected persons in accordance with this clause.

11.2 Unless drawn upon by the State Party [*the Competent Authority*] [*any other entity, as appropriate*] in accordance with this Contract, the Environmental Damage Bond shall be returned to the Investor upon the return of the Project Area in substantially the same condition as it was granted, in accordance with paragraph 10.1.

11.3 Where the Parties cannot agree as to remedial actions or compensation for the Environmental Damage, and/or the amount to be withdrawn from the Environmental Damage Bond to remediate, restore, or compensate for the Environmental Damage, the Parties shall refer the matter to an Independent Expert for final determination in accordance with [*clause XX on dispute settlement – see Chapter 8*].

11.4 Paragraphs 11.1 to 11.3 are without prejudice to the rights of the State Party, the Competent Authorities, any third-party beneficiary, or any other party affected by Environmental Damage to seek recourse under the applicable law for such damage that has not otherwise been remedied or compensated in accordance with this Section.

Commentary to the Model Clause

366. This Model Clause on environmental and climate commitments is among the most comprehensive in this Instrument, reflecting the critical importance of environmental protection and climate change mitigation in contemporary investment contracting. The clause is structured around several key thematic areas. Paragraph 1 establishes the overarching obligation of the investor to comply with both international standards (including internationally recognised industry practices) and the host State's environmental legislation. The interaction between these two normative layers is of fundamental importance: where the applicable domestic law sets a lower standard than the applicable international standards, the parties are encouraged to apply the higher standard, consistent with the general approach of this Instrument (see Principle 6). Paragraphs 2.1 to 2.4 address the Investor's commitment to continuous improvement in production methods and green technologies, covering greenhouse gas emissions reduction, carbon capture, support for climate change adaptation in local communities, prevention of deforestation and desertification, and reduction of pollution. Paragraph 2.4 introduces the concept of Environmental Performance Payments, an emerging practice whereby the host State provides performance-based incentives to encourage the investor to adopt production methods or technologies that generate positive environmental outcomes beyond what is strictly required by the contract. This mechanism reflects the principle that environmental objectives are most effectively achieved when they are supported by appropriate economic incentives. Paragraph 2.5 regulates the right of the investor to apply for greenhouse gas reduction benefits generated by the Project's operations (such as carbon credits or other environmental credits) and establishes parties' co-ownership on such benefits subject to the investor's right to sell them and distribute the resulting revenues. Paragraphs 3.1 to 3.6 deal with climate change commitments specifically, including obligations to quantify and report on greenhouse gas emissions, to reduce such emissions towards a net-zero target, and to contribute to local climate change adaptation funds. Paragraph 3.5 preserves the State's right to seek renegotiation of the contract to meet its nationally determined contributions under the Paris Agreement, subject to any stabilisation obligations assumed by the State party. Paragraph 3.6 contains a regulatory freedom carve-out for *bona fide* environmental and climate measures. These two provisions illustrate the interaction between environmental commitments and the stabilisation framework addressed in Chapter 6: while the State retains its regulatory freedom in environmental matters, the investor's interests are protected through the stabilisation and renegotiation mechanisms, and the parties may agree

on exclusions from the stabilisation commitment for specified categories of environmental measures. Paragraphs 4.1 to 4.5 address waste and chemical management, including sector-specific integrations that parties may wish to add depending on the industry sector concerned (*e.g.*, mining, oil and gas, agriculture, manufacturing). Paragraph 5 addresses the protection of traditional knowledge and cultural heritage. Paragraph 6 establishes that a significant and persistent environmental breach constitutes a fundamental non-performance of the Contract. Paragraphs 7 to 8.4 address monitoring, reporting, disclosure, certification and environmental audit, while paragraphs 9.1 to 9.2 address the Investor's liability for environmental damage, both vis-à-vis the State party and *vis-à-vis* affected third parties who suffer loss caused by such damage. Paragraphs 10.1 to 10.4 address project closure and restoration of the environment (decommissioning), and paragraphs 11.1 to 11.4 introduce the concept of an Environmental Damage Bond – an unconditional and irrevocable bank guarantee securing the investor's environmental remediation obligations. The Environmental Damage Bond is an emerging instrument in investment contracting practice that provides the State party with a financial guarantee that environmental damage will be remediated even if the investor is unable or unwilling to do so. The bond mechanism complements the liability provisions and provides an additional layer of security for the protection of the environment and affected communities.

**2.5 Model Clause on Community Development Agreements**

1. The Investor [*upon finalisation of the sustainability due diligence assessment and management plan, including the resettlement plan*] shall enter into one or more Community Development Agreements (CDA) with the Local Community(ies) settled in the Project Area and neighbouring areas. Such a CDA shall be entered no later than [*insert number of months/years*] from the Signature Date and in any event prior to the commencement of Project Operations.

2. General commitment to local and sustainable development: The CDA shall be entered in accordance with the relevant international standards, recognised industry practices and the Host-State legislation as agreed or identified as applicable by the Investor and the State Party and shall aim to promote the general welfare of the Local Community(ies) and improve the quality of life of its members and inhabitants as well as recognise and respect the rights, customs, religions and traditions of the Local Community(ies) and Indigenous Peoples.

3. Amount of resources to be invested through the CDA: The amount to be invested in social projects, under the terms of the CDA, must be the equivalent of [*insert value*] at the end of the Project Operations, of which the equivalent of [*insert value*] must be spent during the first [*insert period*] years after the signing of the CDA, and the remainder will be spent during the term and within the end of the Project Operations.

4. Identification of the Local Community(ies): The Local Community(ies) is(are) one or more communities of people settled in the Project Area and/or in neighbouring areas as mutually agreed between the Investor and the [*State Party/Competent Authority(ies)/Local Administration(s) of (insert data)*].

5. Contents of the Community Development Agreement: The CDA shall contain certain necessary terms and provisions that the Investor shall negotiate with the Local Community representatives [*and must be submitted for the approval of the State Party/competent Authority*]. During the negotiations, as well as in any further step that involves negotiations or consultations, the principles on involvement and consultation of Local Communities and Indigenous Peoples, including the Free, Prior and Informed Consent Principle [*as per clause [xx] and Principle 11 of the Instrument*] shall apply. The CDA must include at least the following provisions:

a) The person, persons or entity representing the Local Community for the purposes of the CDA;

b) The means by which a registry of persons comprising the Local Community for the purposes of the CDA will be developed, maintained, and updated;

c) The objectives of the CDA and the parties' commitment to the principles of cooperation, mutual respect, and good faith in the pursuit of those objectives;

d) The obligations of the Investor towards the Local Community, including but not necessarily limited to:

i. commitments regarding socio-economic contributions that the project will make to the sustainability of the Local Community, with the identification of specific projects and social infrastructure to be built as well as the resources to be allocated to such projects;

ii. the establishment of a process for the Local Community to identify local climate change adaptation projects and the resources to be allocated to such projects;

iii. assistance in the creation of self-supporting and income-generating activities, such as the production of goods and services needed by the Project Operations and the Local Community;

iv. establishment of benefit-sharing mechanisms designed to empower the Local Community to reap social and economic gains deriving from the Project (*e.g.*, fiscal revenues derived from the Project that will be distributed to the Local Community, allocation of shares of the [*insert Investing Company*] to selected subjects of the Local Community, distribution of ownership or co-ownership of verified carbon credits generated by the Project, and so forth);

v. the identification of other fields for social and economic development stemming from the Project to the benefit of the Local Community, including opportunities for women and other selected categories;

vi. undertakings with respect to financial contributions to support Local Community livelihoods during the Project lifecycle and after Project Closure through an escrow account controlled by the Parties, including the method of disbursing such funds and the parties to whom such funds are to be paid;

vii. consultations with the Local Community for the development of a Resettlement Plan, if the Projects Operations require the displacement of peoples occupying land in the contract area and other solutions are not practicable or rejected by the Local Community;

viii. provisions on investor's liabilities, indemnification or compensation rights directly enforceable by the members of the Local Community affected by Project Operations, individually or jointly, in accordance with the applicable law;

ix. consultations with the Local Community for the development of a Project Closure Plan that prepares the Local Community for the eventual closure of the Project Operations;

x. undertakings with respect to the overall financial contributions that the Project will make to the Local Community, including the amount the Investor will pay to a Community Development Fund in place or to be established, and provisions outlining the means by which funds are to be disbursed, for what purposes they may be

disbursed, what accounts must be kept and by whom, and reporting and auditing requirements;

e) The Local Community's roles and obligations towards the Investor;

f) A Community Development Agreement Plan (CDAP) stating the operational goals of the CDA, steps to achieve the objectives and metrics to measure progress, an implementation timetable, schedule of anticipated expenditures and periodic reporting requirements as to actual expenditures, linkages between the CDAP and other government plans, services, infrastructure and activities provided to or affecting the Local Community, provisions on termination or transfer of the services provided by the Investor to the Local Community, and other content as may be mutually agreed by the Parties;

g) The rules and means by which the CDA and the CDAP shall be reviewed, updated and adjusted by the Investor and the Local Community every [*five (5)*] calendar years, including on how variations will be agreed and ratified by the Local Community, and the commitment that the agreement in force shall remain binding in the event that any modifications to the agreement requested by one of the Parties are not accepted by the other Party;

h) The systems of consultation and oversight between the Investor and the Local Community, and the means by which the Local Community may participate in the planning, decision-making, implementation, management and oversight of the CDA and the activities conducted under the agreement, with a special accent on the participation of an equal number of women and men and the means by which the interests of women, youth, Indigenous Peoples, and minority and marginalised groups and sub-communities of the Local Community will be represented in decision-making processes related to the CDA and implementation of the CDA;

i) The provisions under point h) shall include the identification of the person(s), board, committee, or other entity (such as the Joint Sustainability Committee established under this Contract) that shall oversee the implementation of the CDA with guarantees on a fair representation of representatives of the Local Community, the frequency and form of information sharing by the Investor with respect to the implementation of the CDA and any other relevant information with respect to the Project, and mechanisms available to the Local Community and sub-Communities or members of the Local Community to lodge a grievance with the Investor;

j) A commitment that the Investor and the Local Community agree that any divergence regarding the agreement will in the first instance be resolved by direct consultation between the Investor and representative(s) of the Local Community, and if the divergence is not so resolved, either party may submit the matter for [*an Independent Expert to make a determination*] [*for the [State Party/Competent Authority*] to decide, in consultation with the Local Administration, and the [*State Party/Competent Authority*]'s decision shall be final and binding on the Investor and the Local Community.

k) rules on duration, termination, assignment of the CDA and any right or obligation thereunder, transfer of all CDA rights and obligations to any party to whom the Investor assigns its rights under the IIC, notifications to respective parties, locations where the CDA may be accessed by members of the Local Community, CDA signatories (including representatives of the Local Community and/or sub-Communities and NGOs as may be necessary), and the applicable law.

6. The Parties recognise that, in relation to the obligations under d) and e) of paragraph 5, the CDA will need to consider the unique circumstances of the Project and the Local Community, and the matters to be considered cannot be pre-determined. Accordingly, the CDA may include all or some of the following matters where relevant to the Local Community:

(a) School education, apprenticeship, technical training and employment opportunities for the people of the Local Community;

(b) Financial contributions or other support in the development and maintenance of infrastructure in the field of education, health or other local services, roads, water and energy, protection of natural, cultural, archeologic, religious and sacred sites;

(c) Guaranty of access to resources including land, water courses, sea, and no interference with traditional economic activities, such as agriculture, fisheries, breeding, and other activities relevant to the life of the Local Community;

(d) Assistance in the creation, development and support of small-scale companies and micro-enterprises;

(e) Commercialisation of local products and preservation of traditional productions and markets, including by developing local geographical indications;

(f) Diseases prevention and healthcare awareness; and

(g) Methods and procedures for environmental and socio-economic management and local government capacity building.

7. The Investor agrees and undertakes with effect from the date on which this Contract comes into force to make a financial contribution to:

(a) Improving the road from [*insert data*] to [*insert data*] in accordance with annex [*insert reference and attach annex*];

(b) Expansion of the electricity network from the national grid to [*insert data*] in accordance with annex [*insert reference and attach annex*];

(c) Financing the association of producers of [*insert data*] and the traditional market of [*insert data*] in accordance with annex [*insert reference and attach annex*];

(d) Building a hospital in [*insert data*] in accordance with annex [*insert reference and attach annex*];

(e) Building a cultural centre in [*insert data*] in accordance with annex [*insert reference and attach annex*].

[8.1 The CDA shall be approved by the [*State Party/Competent Authority*] if the conditions are met. To this end, the CDA agreed and signed between authorised representatives of the Investor and the Local Community shall be submitted in writing for approval by the [*State Party/Competent Authority*], who shall approve it within [*45 (forty-five)*] Calendar Days if the agreement meets the requirements set out in paragraph 5 above. If the application for the approval of the CDA is rejected, the [*State Party/Competent Authority*] shall notify in writing the representatives of the Investor and the Local Community, and such notification shall set out the specific reasons for the rejection and the means or guidelines that may remedy such reasons. The Investor and the Local Community may submit any proposal for revision of the CDA in accordance with such guidelines. The Investor shall not commence the Project Operations within the Contract area until the CDA has been tacitly or explicitly approved by the [*State Party/Competent Authority*].

8.2 The [*State Party/Competent Authority*] may impose a CDA in exceptional circumstances. If the Investor and the Local Community are unable to conclude a CDA after reasonable endeavours by the date on which the Investor is ready to commence the Project Operations in the investment area, the Investor or the Local Community may, jointly or individually, submit, by written notice, the subject matter of the agreement to the [*State Party/Competent Authority*] for resolution, and the decision of

the [*State Party/Competent Authority*], in consultation with the Local Administration, shall be final. Such a notice from either or both Parties must include the draft CDA proposed by the notifying Party(ies), a description of the efforts made to negotiate the agreement, matters that have been agreed, matters on which there is disagreement, and a proposal for resolving the matter. The [*State Party/Competent Authority*] must submit a decision within [*60 (sixty)*] calendar days from such notification.

9. Archive of copy of CDAs: the [*State Party/Competent Authority*] shall keep a copy of all Community Development Agreements on a medium accessible to the public.

10. A fundamental non-performance by the Investor of a CDA shall constitute a fundamental non-performance of this Contract and entitles the State party to avail itself of the remedies available under the applicable law.

Commentary to the Model Clause

367. This Model Clause on Community Development Agreements (CDAs) addresses one of the most distinctive features of modern IICs: the formalisation of the Investor's obligations towards local communities in a dedicated contractual instrument. The clause is designed to ensure that the benefits of the investment project are shared with the communities most directly affected by the project operations. Several important points merit explanation. First, the clause contemplates the possibility of concluding more than one CDA with different sub-communities addressing specificities within or near the project area (paragraph 1). This recognises that the impacts of an investment project may be unevenly distributed across different communities, and that the specific needs and concerns of each community may vary. The parties may therefore wish to negotiate separate CDAs with distinct sub-communities, each tailored to the particular circumstances, vulnerabilities and aspirations of that community. Second, the contents of CDAs are both procedural and substantive. The procedural elements include the identification of the persons or entities representing the local community (paragraph 5(a)), the means of developing and maintaining a registry of community members (paragraph 5(b)), and the systems of consultation and oversight between the Investor and the local community (paragraph 5(h)). The substantive elements include the investor's commitments regarding socio-economic contributions, climate change adaptation, benefit-sharing mechanisms, financial contributions, and resettlement planning where applicable (paragraph 5(d)). Third, the relevance of FPIC should be stressed. Paragraph 5 provides that during the negotiations and any further consultations, the principles on involvement and consultation of local communities and Indigenous Peoples as per Principle 11 shall apply. This cross-reference ensures that the CDA process is conducted in accordance with the highest applicable standards on community engagement, including the FPIC principle as articulated in the UN Declaration on the Rights of Indigenous Peoples (UNDRIP) and the ILO Convention No. 169. Fourth, issues of local community representation deserve careful attention. The identification of legitimate and genuinely representative interlocutors is a recurring challenge in CDA negotiations, particularly where the local community is heterogeneous, includes sub-communities with distinct interests, or where traditional governance structures coexist with formal administrative structures. The clause encourages parties to address these issues transparently and to ensure equitable representation of women, youth, Indigenous Peoples and marginalised groups. Fifth, the clause allows the parties to negotiate and include in the IIC itself specific contributions to projects of general interest (paragraph 7) even before the CDA is negotiated and concluded. This pragmatic provision recognises that certain community needs may be urgent and should not await the completion of the CDA process. Sixth, the legal effects of the CDA and the enforceability of its provisions by the signatories, particularly the members of the local community, are addressed. Paragraph 10 establishes that a fundamental non-performance of a CDA constitutes a fundamental non-performance of the IIC itself, thereby elevating the CDA obligations to the level of the main contract and providing the State party with the full range of contractual remedies. The enforceability

of CDA rights by local community members directly is further addressed in the Model Clause on third-party beneficiaries (Section D.2.6 in this Chapter).

**[2.6 Model Clause on third-party beneficiaries**

1. The Parties hereby expressly agree that all members of the Local Community, Indigenous Peoples, and Workers are Third-Party Beneficiaries of this Contract and shall be entitled to receive and enforce, including through the use of the procedures set out in the clauses [*insert clauses*] and the Community Development Agreement stipulated under this Contract [*insert relevant CDA*], all of the benefits of this Contract [*other than the following clauses [insert exclusions as appropriate]*].

2. Without prejudice to the generality of the foregoing paragraph, no Third-Party Beneficiary shall be subject to any liability whatsoever to any Party under this Contract.

Commentary to the Model Clause

368. This Model Clause on third-party beneficiaries addresses the enforceability of contractual rights by persons who are not parties to the IIC but who are intended to benefit from its provisions. The clause expressly designates members of the local community, Indigenous Peoples and workers as third-party beneficiaries of the contract, thereby creating directly enforceable rights in their favour. This designation has several important implications. First, it establishes a connection with the grievance mechanisms provided elsewhere in the contract: third-party beneficiaries may avail themselves of the dispute settlement procedures established in the IIC (see Chapters 7 and 8) and in the CDA to seek redress for any non-performance of the contractual provisions from which they benefit. The enforceability of third-party beneficiary rights through the contract's own dispute resolution mechanisms represents a significant advantage over reliance on general domestic law remedies, which may be less accessible, less predictable or less effective. Second, the level of enforceability of the rights deriving from contract clauses by third-party beneficiaries may be graduated by the parties. The clause provides that third-party beneficiaries shall be entitled to receive and enforce all of the benefits of the contract, with the possibility for the parties to specify exclusions for particular clauses. This flexibility allows the parties to calibrate the scope of third-party enforcement rights to the specific circumstances of their project, excluding from third-party enforcement those provisions that relate exclusively to the bilateral relationship between the State party and the investor (such as dispute resolution clauses, stabilisation provisions, or financial terms) while preserving full enforceability of the provisions that directly affect the welfare and rights of the beneficiaries (such as sustainability obligations, environmental commitments, labour standards and community development obligations). Third, the clause provides that no third-party beneficiary shall be subject to any liability under the contract, thereby ensuring that the designation as beneficiary does not create reciprocal obligations or exposure for the beneficiaries.]

### 3. Obligation to perform a continuous sustainability monitoring

**Principle 21**

**The investor, with the strong support and assistance of the State party, shall put in place a continuous sustainability monitoring mechanism with the aim of monitoring and reporting on the implementation, update and adaptation of parties' sustainability obligations as identified by the pre-contractual due diligence and agreed in the IIC. The principles on consultation of local communities and populations shall apply.**

**Commentary**

369. This Principle recalls and specifies in the context of this Chapter on rights and obligations the duty of the parties (the investor in cooperation with the State party) to an IIC to put in place efficient monitoring activities concerning the implementation of sustainability commitments and obligations during the lifetime of the project, as stated in Principle 11 in Chapter 3.

370. Such continuous monitoring process shall first ensure that the parties' sustainability commitments, as identified in the pre-contractual (or pre-operations) due diligence assessment and the ensuing management and mitigation plan and subsequently specified as concrete obligations in the IIC, are properly implemented. This should happen in line with the highest international standards as applicable, identified and agreed by the parties upon conclusion of their IIC, through continuous monitoring by qualified experts and appropriate annual reporting. Secondly, the process should make sure that, based on the outcome of the monitoring activities and the annual reporting, the management and mitigation plans are properly updated on a periodical basis in light of supervening factual conditions (such as the availability of new data, discoveries, or events like emergencies or accidents) and evolving standards on sustainability, keeping the process aligned with scientific evidence and international practice. Such an adaptation obligation shall ensure the attainment of the highest international standards in every moment of the project's lifecycle, subject to the application of the stabilisation principle in Chapter 6, where relevant.

371. The Principle makes clear that standards on consultation of local communities and populations, including Indigenous populations when applicable, as established in Principle 11 in Chapter 3, also fully apply in the context of the continuous due diligence process.

372. In addition, the parties may decide to include a grievance mechanism to hear complaints from individuals or representative bodies or associations of local communities and populations concerning the breach of sustainability commitments that directly affect them, in line with the highest international standards of the sector and the methodologies they decided to refer to for such matter.

**Model Clause on continuous sustainability monitoring**

1. The Investor covenants to establish and maintain, with the support of the State Party, a continuous sustainability monitoring process to implement the results of the pre-contractual due diligence consistent with the highest international standards as applicable and agreed by the Parties upon conclusion of this IIC.

2. Each Party shall conduct the Investment with due diligence, in an efficient, environmentally and socially responsible manner, fully adhering to the applicable environmental and social management and mitigation plan, the environmental and social legislation, the environmental and social standards, guidelines and sustainability policies, and ensuring that all its operations are carried out in accordance therewith.

3. The Investor shall prevent or mitigate potential adverse direct or indirect impacts of its activities or those of third parties under its control and fully remediate the actual adverse impacts of sustainability-related harm caused by the Investment.

4. The Investor, in cooperation with the State Party, shall provide periodic reports on the implementation of the management and mitigation plan resulting from the pre-contractual sustainability due diligence, and shall conduct on a multi-year basis the update of such plans in light of relevant factual conditions, as well as their adaptation to evolving international standards on sustainability, if relevant and appropriate.

5. In conducting such a process of reporting, updating and adapting the plans, the Investor, in cooperation with the State, shall provide for the continued application of the principles on consultation of local communities and Indigenous populations (including the FPIC standard).

6. Grievance mechanisms shall be provided for to hear complaints from individuals and representatives of key stakeholders, local communities and Indigenous populations regarding possible breaches of sustainability obligations that directly affect such individuals or such communities and populations.

7. The Parties agree and undertake to file any sustainability-related reporting, certification or measurement requirements in accordance with the law or rules applicable to the Investment.

8. Any material breach of the provisions of this sustainability due diligence clause may trigger the right for the non-breaching Party to exercise the remedies applicable in this Contract in the event of a sustainability breach.

373. The IIC may provide for the establishment of a project "Joint Sustainability Committee" to oversee the continuous sustainability monitoring having special regard to the implementation, update and adaptation of the management and mitigation plan, and to facilitate consultations and address environmental, social and human rights issues related to the project as they may occur during and after the implementation of the investment, including hearing complaints through grievance mechanisms, when agreed and applicable. The terms and procedures of such Committee may be specified in an annex to the IIC. For instance, the establishment and functioning of the Joint Committee may be governed by model terms formulated below.

**Model Clause**

**1. Establishment of the Joint Sustainability Committee**

The Parties (the Investor and the State Party) agree to form a Joint Sustainability Committee ("the Committee") to serve as a platform for consultation and collaboration on environmental, social and human rights matters affecting the Project.

**2. Purpose and Mandate**

The Committee shall:

(a) Facilitate dialogue and collaboration between the Investor and the State Party regarding the issuance of environmental licences and permits;

(b) Monitor the implementation of environmental, social and human rights standards in the Project having special regard to the obligations set out in this Contract and the mitigation plans;

(c) Address and resolve environmental, social and human rights concerns raised during the Project lifecycle;

(d) Ensure transparency and accountability in decision-making processes affecting the environment and the social aspects of the Project;

(e) Oversee the continuous monitoring process, particularly as regards annual reporting on implementation of sustainability commitments, periodical update and adaptation of management and mitigation plans, and the operation of grievance mechanisms.

In particular, it will:

(a) Establish its own rules of procedure;

(b) Supervise the implementation and execution of the Contract;

(c) Discuss and disclose opportunities for the expansion of the Investment;

(d) Coordinate the implementation of the mutually agreed cooperation and facilitation agendas;

(e) Consult with civil society, when applicable, on specific issues related to the work of the Committee;

(f) Seek to resolve any issues or disputes concerning sustainability-related aspects of the Project between the Parties to this Contract in an amicable manner.

**3. Composition of the Committee**

The Committee shall include:

(a) Representatives of the Investor;

(b) Designated officials of the State with expertise in environmental, social and human rights regulation;

(c) Optionally, representatives of local communities and key stakeholders directly affected by the Project, as agreed by the Parties.

**4. Meetings and Procedures**

The Committee shall convene regularly and as required to address urgent matters.

Agendas and minutes of meetings shall be documented and shared with all members.

Decisions and recommendations of the Committee shall be advisory unless otherwise agreed.

**5. Focal Point Designation**

The State Party shall designate a focal point within its administration to liaise with the Investor on all environmental, social and human rights matters, including, but not limited to:

(a) Providing guidance on legal and procedural requirements for environmental permits;

(b) Providing guidance on environmental, social and human rights matters;

(c) Coordinating with relevant governmental agencies to expedite approvals and resolve delays;

(d) Facilitating access to information relevant to environmental, social and human rights compliance.

**6. Stakeholder and Community Participation**

Where appropriate, the Committee shall:

(a) Invite local community representatives and other key stakeholders to participate in discussions on specific issues affecting them;

(b) Ensure that their concerns are considered in decision-making processes;

(c) Provide regular updates on environmental and social measures to maintain transparency and trust.

**7. Confidentiality and Reporting**

The Parties shall ensure the confidentiality of sensitive business and governmental information exchanged during Committee meetings.

The Committee shall prepare periodic reports summarising its activities and recommendations, which may be shared with relevant stakeholders.

## 4. Supply Chain

### Principle 22

**The investor shall make its best efforts to ensure that the highest environmental, social, human rights and climate-change-related standards applicable to it or to the project are complied with by its subcontractors and suppliers.**

**Commentary**

374. This Principle establishes a best-efforts obligation requiring the investor to seek to ensure that the highest sustainability standards to which it has committed are also observed by its subcontractors and suppliers. This may be achieved by (i) incorporating a corresponding best-efforts obligation in the IIC, and (ii) including appropriate sustainability clauses in contracts concluded between the investor and its subcontractors and suppliers.

375. The investor can make use of written and easily accessible sustainability policies and the conducting of periodical audits and inspections to assess the sustainability impact of subcontractors within the project. In addition, the investor shall conduct continuous monitoring on adverse environmental, social, human rights and climate-related impacts throughout the project's supply chain in accordance with Section D.3 of this Chapter. If the investor lacks the leverage to prevent or mitigate adverse impacts on the social and natural environment or human rights and climate change generated at the supply chain level and is unable to increase its leverage, it should consider terminating the relationship with relevant counterparties, taking into account credible assessments of the potential adverse impact of doing so. Influence over local subcontractors and suppliers (for instance, based on local development commitments) can be increased by the investor through training and capacity-building. The State party can support these efforts by explaining expectations on responsible business conduct based on applicable law to local entities.

376. It is recognised that compliance with the best-efforts obligation pursuant to Principle 22 may give rise to additional costs. The parties are therefore encouraged to negotiate a fair allocation of such costs, having regard to the specific circumstances of the investment and the measures required.

**Model Clause**

The Investor shall make its best efforts to ensure that the environmental, social, human rights and climate change-related standards under [*insert cross-reference to relevant clause*] are respected at all the stages of the Project's supply chain, including (but not limited to) subcontractors. This requirement includes, but is not limited to, complying with applicable laws and international instruments, maintaining written and easily accessible policies, assessing the impact of their activities within the broader Project, obtaining and maintaining any needed authorisations or permits, and undertaking periodical reports and audits.

The Investor, with the cooperation of the State Party, shall perform the due diligence and impact assessment required under [*insert cross-reference to clause on sustainability due diligence*] and [*insert cross-reference to clause on impact assessment*], taking into account the entire Project's supply chain.

The Investor shall take appropriate measures to ensure that contracts with its subcontractors and other subjects or partners in its supply chain, where appropriate, incorporate clauses prescribing compliance with the terms set out in this IIC as regards sustainability commitments.

377. Below is a set of proposed Model Clauses to be incorporated in contracts between the investor and its business relationships, including subcontractors and entities in the supply chain. These Model Clauses may provide the framework within which to incorporate environmental, social, human rights and climate change standards into supply chain agreements. By including clear obligations, monitoring mechanisms and enforcement provisions, the investor will ensure that the project meets broader sustainability objectives.

378. The principle of proportionality, which has been highlighted in other parts of this Instrument on sustainability issues (see the commentary to Principle 6, Principle 11, Principle 20), is also relevant here.[33] The degree of contractual cascading of sustainability obligations may vary depending on the type of relationship the investor has with its business partners, subcontractors and entities in the supply chain. It will typically be easier to incorporate more robust sustainability clauses in contracts with subcontractors that are directly involved in the project than in one-off contracts with suppliers.

379. While this Instrument offers general guidance from an international perspective, the parties should consider that regional and domestic supply-chain due diligence regimes may also be relevant for the design of supply chain clauses in IICs and subcontractor/supply chain contracts, including those of the home State of the investor.

**Model Clauses for inclusion in subcontractor/supply chain contracts**

**1. General Commitment to Environmental Standards**

The Supplier/Subcontractor shall comply with all applicable environmental and social laws, regulations, and international standards relevant to its operations, as well as any environmental, social and human rights policies provided by the Investor, attached as Annex [*X*].

**2. Due Diligence and Impact Assessment**

The Supplier/Subcontractor agrees to conduct and document regular assessments of its environmental, social and human rights impact and to cooperate with the Investor in identifying and mitigating risks to the environment.

**3. Permits and Compliance Documentation**

The Supplier/Subcontractor warrants that it holds all necessary permits, licences, and certifications required for its operations and that it will provide the Investor copies of these documents upon request.

**4. Reporting Obligations**

The Supplier/Subcontractor shall provide the Investor with regular environmental, social and human rights performance reports, which shall include: (i) compliance status with applicable laws and standards; (ii) actions taken to address any identified deficiencies or risk; (iii) measures implemented to reduce the environmental, social and human rights impact, including emissions and waste.

**5. Audit and Inspection Rights**

[33] See OECD Guidelines for Multinational Enterprises on Responsible Business Conduct, Chapter 2, paragraphs 20 and 23-26.

The Investor reserves the right to conduct audits or inspections of the Supplier/Subcontractor's operations, facilities, and records with a view to ensuring compliance with the agreed standards. Such audits may be conducted periodically or in response to specific concerns.

**6. Remedial Measures and Sanctions**

In case of non-compliance, the Supplier/Subcontractor shall: (i) propose and implement corrective actions within [*X*] days of receiving notice from the Investor; (ii) be subject to penalties or contract termination if the non-performance persists or is deemed severe.

# CHAPTER 6. CHANGE OF CIRCUMSTANCES

## A. Introduction

380. This Chapter covers three legal situations of change of circumstances that may affect an IIC. Section B contains stabilisation and renegotiation clauses. Section C addresses hardship and force majeure.

381. The first change of circumstances addressed in Section B concerns the stabilisation and renegotiation clause. There is no comparable provision in UPICC for stabilisation and renegotiation clauses since they are unique to IICs (because one of the parties is a State or another entity related to the State). There is a possibility that changes to the State's regulatory framework may affect IICs. At the same time, a State has to make and change regulations to address public interest arising from time to time. Section B is founded upon the objective of maintaining a balance between the stability of contracts and the need for States to legitimately regulate. Due to the sensitivities involved around stabilisation clauses, parties are encouraged to exercise caution while including stabilisation and renegotiation clauses. General freezing clauses, intangibility clauses, and allocation of burden clauses have been widely criticised for their severe constraining effect on the regulatory freedom of States. Indeed, contract practice has been moving away from such clauses towards economic equilibrium clauses that encourage the maintenance of stability of the contract through renegotiations if the investor suffers losses due to changes to the regulatory framework. The focus of these provisions is on stability through renegotiation. Hence the title of this Section addressing "stabilisation and renegotiation clauses". Apart from the economic equilibrium clause, an alternative is provided in the form of fiscal stabilisation clauses, which continue to be used in practice since they provide certainty to the investor that the fiscal regime will be maintained for the duration of the contract or the period so agreed. Also, if the State fails to maintain the fiscal framework, remedies different from and in lieu of monetary compensation can also be agreed between the parties.

382. In this regard, the OECD Guiding Principles for Durable Extractive Contracts and the OHCHR (Office of the United Nations High Commissioner for Human Rights) Principles for Responsible Contracts provide important benchmarks for assessing the appropriateness and scope of stabilisation clauses in IICs. Parties are encouraged to have regard to these instruments when negotiating and drafting stabilisation and renegotiation clauses.

383. Section B provides policy suggestions and alternatives due to the sensitivities and controversies surrounding stabilisation clauses. Therefore, the first principle in Section B, Principle 23(1), sets out that the parties are free to choose to include a stabilisation and renegotiation clause if deemed appropriate, but they should do so with full knowledge of its consequences. This principle is a policy suggestion to guide contract drafters. The second principle in Section B, Principle 23(2), provides three alternatives. First is the economic equilibrium clause, provided in paragraph (1) of Principle 23(2)**,** which is the most prevalent in practice and considered to provide a balance between the demands of stability of the contract and the freedom of States to undertake regulatory changes. Second is a fiscal stabilisation clause contained in paragraph (2) of Principle 23(2)**,** whereby a State may make a promise to freeze the tax framework as applicable to the investor for the entire duration of the IIC or any other period so agreed. Third, hybrid clauses represent a combination of economic equilibrium clauses and fiscal stabilisation clauses. Parties are free to agree to a combination as they deem appropriate based on the nature of the transaction and the sector of operation.

384. Given that IICs are long-term contracts, it is possible that over the course of the term of the contract, a hardship situation may arise. When that happens, it would generally be in the interest of both the State entity and the investor to try to ensure that the contract carries on. Termination of the contract could deprive the public of an essential or important service or stop the production of a commodity from

which the State derives substantial revenue. For the investor, the substantial investments it had put into the project may be lost upon termination. Renegotiation of the contract then provides a viable option to remedy the economic imbalance brought about by the hardship situation.

385. Articles 6.2.1 to 6.2.3 of the UPICC deal with hardship, and they are also relevant to IICs. The principle of continuity and renegotiation embodied in Article 6.2.3 is particularly pertinent to IICs given the long-term nature of IICs and the substantial investments involved. As Articles 6.2.1 to 6.2.3 of the UPICC apply to IICs, separate principles on hardship are not provided in this Instrument. The commentary explains the application of these UPICC provisions to IICs.

386. The ICC Model Clause on hardship is proposed for parties to consider, with options provided for parties to choose as appropriate depending on the circumstances of their project.

387. Force majeure clauses have become widely accepted and commonly used in commercial contracts and cross-border trade and investment contracts. IICs are no exception. Force majeure is addressed in Article 7.1.7 of the UPICC. It would apply equally to IICs. As IICs are typically long-term, high-value contracts, there is an incentive on the part of the host State as well as the investor to try to keep the contract alive when a force majeure event occurs. Renegotiation after a force majeure event may therefore be a more viable option than termination. Thus, building on Article 7.1.7, an additional principle, Principle 24, is included in this Instrument, taking into account particular aspects of IICs such as the long-term nature of the contract and the fact that a project once built or installed is not easily dismantled or moved. Principle 24 clarifies that Article 7.1.7 of the UPICC does not limit the right of parties to renegotiate the contract as a consequence of a force majeure event. Principle 24 makes it clear that the parties may choose to renegotiate rather than terminate the contract. The ICC Model Clauses on force majeure are recommended for consideration by parties for use in IICs.

388. There are several distinguishing factors between stabilisation clauses, hardship and force majeure although they all address changes of circumstances. The nature of the change of circumstance that can form the basis to invoke them is different. In the case of stabilisation clauses, it is the changes to the regulatory framework by the host State. Hardship clauses cover situations where the performance of the contract becomes onerous. For force majeure, it is an occurrence of a serious nature beyond the control of the parties that makes performance impossible. Also, in the case of stabilisation clauses, it will be the action of the host State that will trigger stabilisation clauses, while the events leading to the invocation of hardship and force majeure will often be beyond the control of the host State. Therefore, the situation for them to come into operation, the procedure once the situation occurs, and the outcomes all differ from one provision to another. In commercial contracts, change of law is deemed to be force majeure or hardship because it is beyond the control of both parties, but in IICs this is not the case because one party is the State.

389. The practical consequence of this distinction for the allocation of loss is significant. In a hardship situation, the loss is shared because the cause is beyond the control of both parties, whereas under a stabilisation clause the alteration of the economic equilibrium is attributable exclusively to State conduct. It follows that under hardship, compensation (if awarded) would typically be allocated between the parties in proportion to the circumstances, whereas under a stabilisation clause, the full cost should in principle be borne by the State, the action of which triggered the disruption. This difference in attributability has further implications for the remedial framework. Under hardship, Article 6.2.3 of the UPICC contemplates judicial or arbitral adaptation of the contract terms to restore its equilibrium, whereby the adjudicator may redistribute the burden of the changed circumstances equitably between both parties, taking into account the distribution of risks agreed upon in the contract. Under a stabilisation clause, by contrast, the remedial logic is restitutionary rather than distributive: the objective is to restore the investor to the economic position it would have occupied but for the State's regulatory intervention. This may take the form of a

fiscal adjustment, a tariff recalculation, an extension of the concession period, or direct monetary compensation, depending on the type of stabilisation mechanism chosen by the parties (see Principle 23(2)). A further distinction concerns the burden of proof. In a hardship claim, the party invoking hardship must demonstrate that the change of circumstances was unforeseeable, beyond its control, and that the risk of the change was not assumed by it (Article 6.2.2 of the UPICC). In a stabilisation claim, the investor need only show that a covered regulatory change has occurred and that it has materially affected the economic equilibrium of the contract or, in the case of fiscal stabilisation, that a change in the applicable fiscal regime has taken place. The causal link between State action and contractual disruption is inherent in the nature of the clause itself.

390. The threshold for the application of each is also different. For stabilisation and renegotiation clauses, based on the type of stabilisation clause chosen by the parties, the threshold for its invocation will differ. In case of economic equilibrium clauses under paragraph (1) of Principle 23(2), the effect on the investment has to reach a substantial degree. However, in case of fiscal stabilisation clauses, under paragraph (2) of Principle 23(2), any alteration to the fiscal laws applicable to the investor and covered by the clause would be sufficient. In the case of hardship clauses, the performance shall become "onerous" and the threshold to decide what is onerous is contained in Article 6.2.2 of the UPICC, which applies "as is" to IICs covered by this Instrument. The threshold for invocation of force majeure, as contained in Article 7.1.7 of the UPICC – which applies to IICs covered by this Instrument – is high.

391. In relation to change of circumstances, renegotiations to alter the IIC will follow the invocation of economic equilibrium clauses under paragraph (1) of Principle 23(2), hardship and force majeure. However, the procedure and outcome of renegotiations envisaged in each of these provisions is different due to the differences in the reasons for their invocation and their consequences. The presence of renegotiation in each of those provisions shall not be understood to have the same meaning nor entail the same degree of renegotiation. The procedure for renegotiation and the potential outcome will differ in each situation.

## B. Stabilisation and Renegotiation Clauses

### Principle 23(1)

**General provision**

**If appropriate and with full knowledge of the consequences, the parties may agree to include a stabilisation and renegotiation clause in the IIC.**

**Commentary**

*A. If appropriate*

392. The term "if appropriate" is used to indicate that a stabilisation and renegotiation clause is not to be automatically included, and it is at the discretion of the parties to decide whether to add a stabilisation clause after sufficient negotiations.[34]

393. Additionally, "if appropriate" is used to indicate situations where a stabilisation and renegotiation clause may not be included in the IIC or that it would not have effect because the State may not be a party to the IIC. This includes situations where the contract is between the investor and an entity on the State

[34] See ALIC Guide, para. 4.139.

side that is not a State or cannot bind the State. Accordingly, only if one of the parties is a State or capable to bind the State can a stabilisation clause be included in the IIC.

394. Considering the peculiarities of IICs, stability of the contractual relations is important. Equally there is a need to balance that with the regulatory freedom of States. The practice of IICs seeks to maintain that balance through stabilisation and renegotiation clauses. In the following Principle 23(2), three alternatives are provided. First, the economic equilibrium clause encourages stabilisation of the contract and provides for renegotiation in case of regulatory changes, whereas a fiscal stabilisation clause stabilises the fiscal regime. A hybrid stabilisation clause will be a combination of the first two, hence they all are collectively referred to as "stabilisation and renegotiation clauses".

*B. With full knowledge of the consequences*

395. The negotiating parties, especially the State, shall enter into a stabilisation and renegotiation clause with full knowledge of the consequences of such a clause. The term "full knowledge of consequences" is used to cover the knowledge of the four competing considerations, *inter alia*, in relation to the need and effects of stabilisation and renegotiation clauses that shall be kept in mind.

396. First, depending on their formulation, stabilisation and renegotiation clauses may constrain the sovereign right of the State to regulate in the public interest, especially the protection of human rights, labour standards, environmental protection, climate change and other related measures.

397. Second, the threat of non-commercial risks affecting the IIC, directly or indirectly, cannot be denied. These risks are aggravated due to the long-term nature and the time taken to receive the returns on the investment.

398. Third, lenders of projects under an IIC may demand some assurance of stability of the contract to receive timely loan repayment, thus requiring the investors to negotiate a stabilisation and renegotiation clause.

399. Fourth, unlike investment treaties or national legislation protecting investors, which contain protection *in rem* (available to all investors without the State knowing the identity of specific investors), IICs and the stabilisation and renegotiation clauses therein operate *in personam* (the State is aware of the identity of the investor).

**Principle 23(2)**

**Types of Stabilisation and Renegotiation Clauses**

**The parties are free to choose from one of the following stabilisation and renegotiation clauses:**

**(1) Economic equilibrium clause: If a measure adopted by the State after the coming into force of the IIC substantially reduces, either in the short term or in the long term, the economic return expected at the time of entering into the IIC or any other time agreed by the parties, the investor may request renegotiation to achieve the economic equilibrium by adhering to the following procedure:**

**(a) The request for renegotiation shall be made without undue delay and shall indicate the grounds on which it is based;**

**(b) The parties shall renegotiate in good faith to achieve the economic equilibrium of the international investment contract; and**

**(c) The request for renegotiation does not in itself entitle the parties to withhold performance.**

**(d) If one of the parties fails to fulfil the conditions contained in sub-paragraphs (a) through (c), the other party can resort to the dispute resolution procedure agreed in the IIC.**

**(2) Fiscal stabilisation clause: The State cannot reduce or remove the tax, customs or other fiscal incentives given to the investor for the period of the IIC or any other period so agreed by the parties; and the changes made to the tax, customs or other fiscal laws that substantially reduce the economic returns under the IIC shall not apply to the investor for the period of the contract or any other period so agreed by the parties. If the State acts contrary to the commitments made in this paragraph:**

**(a) The investor must inform and provide full details to the State of the reduction in the economic returns under the IIC; and**

**(b) The State shall compensate the investor through monetary compensation or enter into negotiations without undue delay to provide other comparable alternatives as compensation to be mutually agreed.**

**(c) If one of the parties fails to fulfil the conditions contained in sub-paragraphs (a) and (b), the other party can resort to the dispute resolution procedure agreed in the IIC.**

**(3) Hybrid stabilisation and renegotiation clause: The parties can choose a stabilisation and renegotiation clause which is a combination of the types of stabilisation clauses specified in paragraphs (1) and (2).**

**Commentary**

400. Broadly speaking, three principal types of stabilisation clauses exist in contract practice: freezing clauses, economic equilibrium clauses, and limited stabilisation such as fiscal stabilisation clauses. Other types of stabilisation clauses, such as intangibility clauses (*les clauses d'intangibilité*) or allocation of burden clauses, that shift the burden entirely on the State, have the same effect as freezing clauses. The effect of freezing clauses is that the investor is excluded from the application of any changes to the regulatory framework of the State. Freezing clauses are seen to severely constrain the regulatory freedom of States both generally and specifically for addressing human rights, labour standards, environment protection, climate change and other related measures. Moreover, they do not reflect the dominant contemporary practice.[35] Therefore, freezing clauses are not provided for in this Instrument. Instead, other types of stabilisation and renegotiation clauses, namely economic equilibrium clauses, fiscal stabilisation clauses and hybrid clauses, are suggested.

401. The economic equilibrium clause in paragraph (1) can be entered into by a State or any other entity on the side of the State. But the fiscal stabilisation clause will require that the party is a State and not any

[35] See ALIC Guide, paras 4.137-4.138.

other entity on the side of the State. Any other entity except the State will not be competent to make such a promise, unless the State is made a party to the IIC or a State entity party to the contract is an organ of the State or under State control depending on the applicable law and has assumed the stabilisation commitment (see Principle 12 on Legal capacity). In case of hybrid clauses, since there would be elements of fiscal stabilisation, a State will have to be a party to the IIC. The meaning of the expression "The parties" in the chapeau has to be understood accordingly. When the party to an IIC is not a State but rather a State entity, the parties should seek a contractual commitment by which the State entity shall endeavour to facilitate discussions and make efforts to persuade the State to ensure the stabilised fiscal treatment.

*A. Economic equilibrium clause*

402. The economic equilibrium clause balances the need for States to undertake regulatory measures in the public interest and the right of the investor to rely on a stable framework and receive reasonable economic returns on its investment.

403. The term "a measure adopted by the State" is a general formulation used to cover a wide range of measures that may be adopted by various organs of the State that may affect the economic equilibrium of the IIC. The term "a measure adopted by the State" covers legislation, constitutional changes and amendments, executive or administrative orders or decisions, and judicial decisions. An investor can seek renegotiation only if "a measure adopted by the State" is adopted after the coming into force of the IIC. An investor cannot seek protection under the economic equilibrium clause if it had the knowledge of an impending measure before the coming into force of the IIC.

404. In order to seek renegotiation under the economic equilibrium clause, the measure adopted by the State shall substantially reduce the economic return expected by the investor at the time of entering into the IIC. Minor or negligible effects are not sufficient to seek renegotiation. The assessment of substantiality of the effect has to be done based on the economic size of the investment and the losses caused. The time frame to assess the reduction in the economic return is broad, as reflected in the phrase "either in the short term or in the long term". An investor may seek renegotiation if it concludes, based on sufficient material, that the substantial reduction of the economic returns may be suffered in a shorter period of time or over a longer period of time.

405. Additionally, it is sufficient to establish substantial reduction in the economic return either in the short term or in the long term due to a measure adopted by the State. It is immaterial if the substantial reduction in the economic return is caused indirectly. Such situations would be covered by hardship and *force majeure* clauses.

406. The substantial reduction in economic returns is to be based on the assessment of the returns made at the time of entering into the IIC or any time agreed by the parties. In practice, mostly parties agree to the benchmark of the time of entering into the IIC, but there are examples in practice of choosing other benchmarks such as before the measure was taken or a general economic balance without a reference to any benchmark.

407. Once all the conditions of paragraph (1) of Principle 23(2) are satisfied, the investor can seek renegotiation to achieve the economic equilibrium by following the procedure in sub-paragraphs (a) to (c).

408. The investor shall make a request for renegotiation without undue delay, and the grounds based on which renegotiation is sought shall be clearly indicated in the request. The necessary evidence forming the basis of the renegotiation shall be shared with the State along with the request. Upon receipt of the request, both parties shall renegotiate in good faith to achieve the economic equilibrium of the IIC. The

parties may provide in the IIC whether they wish to restore the economic equilibrium existing at the time of entering into the contract or a reasonable economic equilibrium. In the absence of such a reference, it should be a reasonable economic equilibrium. The renegotiation could lead the parties to agree on changes to the terms of contract to restore the economic equilibrium or other comparable measures that would restore the investor's expected return, such as, but not limited to, entering into another contract at a lower price for other products or services. During the process of renegotiation, the parties shall continue to perform their obligations, and they are not entitled to withhold the performance of the IIC.

409. If one of the parties fails to fulfil the conditions contained in sub-paragraphs (a) to (c), the other party can resort to the dispute resolution procedure identified in the contract. The remedies in Chapter 7 would normally be available, including compensation. The parties are free to specify the possible consequences of failed renegotiation in their contract. For instance, the parties may agree to grant authority to an arbitral tribunal (or defer to an expert determination or dispute board procedure) to decide how the contract should be adapted and performed going forward.

**Model Clause**

1. If after the coming into force of this Contract, new measures are introduced or existing measures are amended by the State which substantially reduce the economic return as expected by the Investor [*at the time of coming into force of this Contract or any other time agreed by the parties*], the Parties shall meet and consult with each other and shall make the necessary changes to this Contract or take other mutually agreed actions to achieve the economic equilibrium [*as existing at the time of coming into force of this Contract/that is reasonable*]. The term "measure" under this Contract shall be understood as including laws and regulations [*including constitutional laws and amendments*], executive or administrative orders or decisions, and judicial decisions.

2. If the situation specified in paragraph 1 occurs, the following procedure shall be followed:

   (a) The Investor shall write to the State, without undue delay, requesting negotiations with the grounds for the request.

   (b) The Parties shall meet [*without undue delay/with 60 days' notice received by the State*] to renegotiate to achieve economic equilibrium [*as existing at the time of coming into force of this Contract/that is reasonable*].

   (c) The Parties must negotiate in good faith to achieve economic equilibrium [*as existing at the time of coming into force of this Contract/that is reasonable*] within a period of [*60 days/90 days/other*] from the commencement of negotiations.

   (d) The request for renegotiation does not in itself entitle the Parties to withhold performance.

*B. Fiscal stabilisation clause*

410. The fiscal stabilisation clause is a limited freezing clause since the freezing effect is limited to the fiscal laws and the duration agreed to by the parties. The fiscal stabilisation clause contained in paragraph (2) of Principle 23(2) restricts the power of the State to reduce or remove the tax, customs or other fiscal incentives (including by introducing new taxes or increasing the existing ones) given to the investor for the period of the contract or any other period so agreed by the parties. The promise by the State to the investor to this effect shall be clearly specified in the IIC. The parties may agree to decide whether the fiscal stabilisation clause will apply during the entire period of the IIC or only a limited duration.

411. If the State acts contrary to these provisions, if stipulated in an IIC, it shall compensate the investor through monetary compensation or other comparable alternatives as compensation to be mutually agreed by the parties. The negotiations for mutual agreement under paragraph (2) sub-paragraph (b) are limited to the comparable alternatives as compensation and not to the amount of compensation. The investor must inform and provide full details to the State of the reduction in the economic returns under the IIC. The State shall enter into negotiations without undue delay to provide compensation or other comparable alternatives as compensation. The parties shall negotiate the compensation or other comparable alternatives as compensation in good faith. These negotiations would be limited to the alternative forms of compensation. If one of the parties fails to fulfil the conditions contained in sub-paragraphs (a) and (b) of paragraph (3), the other party can resort to the dispute resolution procedure identified in the contract.

**Model Clause**

1. The State shall maintain the stability of income tax, customs, property tax and other fiscal laws applicable to the Investor on the date of coming into force of this Contract for [*entire duration of the Contract/for ten years from the coming into force of the Contract*].

2. If the State fails to comply with paragraph 1, it shall compensate the Investor through monetary compensation or other comparable alternatives as compensation to be negotiated in good faith and mutually agreed by the Parties. The mutual agreement is limited to the comparable alternatives as compensation and not to the amount of compensation.

3. The Investor must inform and provide full details to the State of the reduction in the economic returns under the Contract.

4. The State shall provide monetary compensation or enter into negotiations without undue delay to provide other comparable alternatives as compensation. [*Monetary compensation or other comparable alternatives shall be provided within a period of […] from the notice received by the State*.]

*C. Hybrid clauses*

412. Normally, a hybrid stabilisation clause would be a combination of more than one type of stabilisation and renegotiation clause. Since freezing clauses are not recommended in these Principles, a hybrid clause for the purpose of these Principles is limited to the combination of a fiscal stabilisation clause and an economic equilibrium clause.

**Model Clause**

1. The State shall maintain the stability of income tax, customs, property tax and other fiscal laws applicable to the Investor on the date of coming into force of this Contract for [*entire duration of the Contract/for ten years from the coming into force of the Contract*].

2. If the State fails to comply with paragraph 1, the Parties shall meet and consult with each other and shall make the necessary changes to this Contract to achieve economic equilibrium [*as existing at the time of coming into force of this Contract/that is reasonable*].

**Principle 23(3)**

**Exclusion of certain measures**

**Economic equilibrium and fiscal stabilisation clauses (or a combination thereof) as referred to in Principle 23 shall not apply to measures adopted in good faith, in a non-discriminatory manner, and in the public interest by the State, necessary to comply with the obligations to protect human rights, public health, the environment, climate change, or labour standards.**

**Commentary**

413. Principle 23(3) is a carve-out provision which excludes certain types of measures adopted by the State from the operation of the stabilisation and renegotiation clause. The measure must satisfy certain conditions (good faith, non-discriminatory, public interest) in order to be a legitimate exercise of sovereign authority aimed at achieving certain objectives (protection of human rights, public health, the environment, climate change, or labour standards). The two sets of conditions are essential and aim to maintain regulatory freedom at an optimum level because if it were too broad it would defeat the purpose of stabilisation and renegotiation clauses.

*A. Good faith, non-discriminatory, public interest*

414. A measure may be excluded from the operation of the stabilisation and renegotiation clause only if the measure satisfies the conditions of being adopted in good faith, non-discriminatory, and in the public interest. The measures shall be adopted in good faith that is exercised genuinely for the purpose of achieving the public interest set out to be achieved. The State has discretion to choose the appropriateness of the measure, as long as the background and the material supporting the adoption of the measure show that the measure was adopted to achieve the purpose. The measure shall be non-discriminatory, that is, it shall not discriminate between similarly-placed investors. The investors may be domestic or foreign, including from third States. Lastly, the measure must be made in pursuit of the public interest. States enjoy discretion to decide the public interest they wish to protect, as long as the choice is made in good faith.

*B. Obligations necessary to protect human rights, public health, the environment, climate change, and labour standards*

415. In addition to the measure being adopted in good faith, non-discriminatory, and in the public interest, the measure shall be based on an obligation on the State arising out of [either domestic or] international law in relation to one or more of the following areas: protection of human rights, public health, the environment, climate change, or labour standards.

*C. Parties' freedom to articulate the scope of the carve-out provision*

416. If the requirements of Principle 23(3) are met, the investor does not have renegotiation or compensation rights. This is the deliberate consequence of the carve-out advocated in this Instrument. However, the parties remain free to articulate the scope of the carve-out provision. For instance, they may decide to specify the measures that are included in the carve-out (*e.g.*, referring to specific legislation), or to provide exceptions to the carve-out. Parties may also decide to provide a renegotiation right for all or specific measures or in certain circumstances (*e.g.*, if the adopted measures came as a surprise rather than as part of planned legislative policy on which the investor had the opportunity to express its views).

417. In this context, parties should be aware that fiscal stabilisation clauses may interact with internationally agreed tax reform instruments, such as the OECD/G20 Inclusive Framework on Base Erosion and Profit Shifting (BEPS), including the Pillar Two global minimum tax. Fiscal stabilisation clauses risk

constraining the State's ability to implement internationally recognised tax reform instruments. The parties are therefore encouraged to consider, when drafting the scope of the carve-out provision, whether measures adopted to implement such internationally agreed fiscal reform instruments should be expressly included within the carve-out or otherwise addressed in the stabilisation framework.

**Model Clause**

The [*clauses/chapter containing the stabilisation and renegotiation clause*] shall not apply to measures adopted in good faith, non-discriminatory, and in the public interest by the State to comply with obligations to protect human rights, public health, the environment, climate change, or labour standards.

## C. Dealing with unforeseen events: hardship and force majeure

418. Force majeure and hardship are frequently invoked in international trade in case of the occurrence of unforeseen events which make performance impossible or impracticable (*force majeure*) or which substantially upset the economic balance of the contract (hardship). In the first case, the aim of the party successfully invoking force majeure is to be relieved from performance, while in the second case, the aim of the party subject to hardship is to be entitled to renegotiate the contract and in certain cases to obtain its adaptation to the changed circumstances.

419. Most national legislators provide rules dealing with force majeure, less dealing with hardship; the principles developed in domestic law such as frustration (English law), impossibility of performance (civil law systems) or impracticability (American law) may imply substantial differences. It may thus happen that the same circumstances exempt a party from responsibility (or grant the adaptation of the contract) in one legal system and not in another.

420. Therefore, it is common practice in international contracts to include clauses on force majeure and hardship to derogate from domestic rules or to fill the gap of the law. The purpose of the ICC Force Majeure and Hardship Clauses is precisely to provide parties with balanced and effective standard clauses to be included in international contracts or to be used as a basis for drafting tailor-made clauses.

421. The ICC Force Majeure Clause and the Hardship Clause 2020 proposed below are an updated version of the previous clauses[36] that consider recent developments in trade and introduce a number of improvements dictated by the experiences encountered in the intervening years. ICC introduced both a long form Force Majeure Clause, which can be incorporated by reference, and a short form.

### 1. Hardship

**Commentary**

422. Hardship is addressed in Articles 6.2.1 to 6.2.3 of the UPICC. As IICs are by nature long-term contracts, situations of hardship may occur, and the provisions of the UPICC on hardship are therefore relevant. Generally, there will be a desire of both parties to maintain the performance of the contract, which means that renegotiation should be the main effect of hardship, again as is the case in the UPICC.

[36] The ICC Force Majeure Clause 2003 and the ICC Hardship Clause 2003. See also The ICC Force Majeure Clause 2003 and the ICC Hardship Clause 2003 in International Commercial Contracts - Institute Dossier XVII, 2018.

423. On the side of the State party, continuity of the performance of the contract is typically beneficial because of the general interest served by its implementation. Stopping the performance of the contract could mean interrupting an important or essential service offered to the public, or stopping production from which the State derives a significant part of its revenue. The investor will also typically have an interest in continuing the contract given the financial investments it made. Therefore, the principle of continuity of performance of contracts has an impact on how hardship applies to an IIC.

424. The event triggering hardship must be beyond the control of the parties. In the IIC context, one party of the contract is the State or a State entity. If a measure imputable to the State causes a fundamental alteration of the economic equilibrium of contract and a causality link is proved, this would be covered by a stabilisation clause, where provided, rather than by hardship. Hardship might also apply, absent a different type of risk allocation, where a State entity or a territorial subdivision of the State is the contracting party and the situation of hardship depended on acts of the central State.

425. Once a situation of hardship has been established, this should lead the parties to renegotiate the contract to remedy the major imbalance in performance that the hardship event causes. Although nothing is said in Article 6.2.3 of the UPICC to that effect, both the request for renegotiation by the disadvantaged party and the conduct of both parties during the renegotiation process shall be subject to the general principle of good faith, as indicated in the associated model clause.

*A. No unilateral termination*

426. State parties might, under their national law, be entitled to terminate the contract unilaterally in the event of non-performance by the counterparty. A similar right of unilateral termination by the public party might exist in the event of hardship in some national laws. Nevertheless, depending on the applicable law, this right of unilateral termination could give way in the event of a clause to the contrary.

427. While not all national laws may allow a public entity to waive its contractual power to terminate unilaterally on the grounds of the needs of general interest – a right that may not even exist in some jurisdictions – it is recommended not to grant the State entity a unilateral termination power in the event of hardship. By denying both parties the right of unilateral termination, as a matter of principle, they will be placed on an equal footing.

428. Where the applicable law allows for unilateral termination, under specific circumstances, this possibility should take precedence, as continuity of performance is not always beneficial for either the host State or the investor. Indeed, it might be appropriate to allow either party to terminate the contract where, due to situation of crisis or resource constraints, continued performance would become unduly burdensome, thereby ensuring a balanced approach that protects both parties.

*B. Renegotiation*

429. Renegotiation is an important tool to ensure the continued performance of the contract. The focus of the negotiation may differ depending on whether it aims to restore the equilibrium on the day the contract was entered into, or the equilibrium on the day before the cause of hardship (if the contract has been performed over a fairly long period, other mechanisms of variation may have come into play). It is important to distinguish between the equilibrium intended by the parties under the contract and the equilibrium on the day of the contract's formation *stricto sensu*. Only the first should matter, even if the operation of different mechanisms of variation may lead to the necessity to assess the equilibrium on the day immediately before the date of the cause of the hardship.

430. The question may arise as to how the "equilibrium intended by the parties" would be determined, considering that IICs are long-term contracts and that the contract might have changed since its conclusion. First, it is necessary to determine the date on which the economic equilibrium is to be assessed to in turn determine whether it has undergone a fundamental change. This may depend on whether the parties themselves have altered the economic equilibrium between the conclusion of the contract and the moment preceding the event causing the hardship. The aim of the renegotiation could be to restore the economic equilibrium that existed at the time immediately prior to the occurrence of the hardship. Second, a more fundamental point might be that the parties themselves might be best placed to determine the economic equilibrium of their contract.

*C. Adaptation*

431. Article 6.2.3(4)(b) of the UPICC allows a court (which includes an arbitral tribunal according to Article 1.11 of the UPICC) to adapt or terminate the contract in the event of hardship, to restore its economic equilibrium. However, it might be challenging for third parties (judges or arbitrators) to understand the technical, financial, and commercial issues in connection with an IIC and to assess those in light of the parties' interests. In the case of IICs, it may therefore be considered to limit the effects of hardship to renegotiation.

432. The ICC Hardship Clause 2003 recognised, in case of failure of renegotiation, only the right of the party invoking hardship to terminate the contract, without including the option to request adaptation by the competent judge or arbitrator. This restrictive position was strongly supported at the time by many businesspeople who feared that this option might leave space for possible abuses, arguing that a third party would never be able to decide a new balance of obligations on behalf of the parties.

433. This concern is still shared by a great part of the business world. However, it must be recognised, at the same time, that there are situations (particularly in the context of long-term contracts) where adaptation, after the failure of renegotiation, is the only way to overcome critical situations which cannot be resolved otherwise. Moreover, the right to request adaptation of the contract will often be a strong incentive for the other party to agree on a compromise solution. The Hardship Clause 2020 provides the option to choose between the solutions of contract termination and contract adaptation.

*D. Compensation*

434. Some domestic law allows for compensation for the losses resulting from hardship.[37] The importance of the contract for the State party needs to be emphasised here. Due to the imperative of business continuity and public service, the State party might be prepared to compensate for the financial consequences of the hardship to ensure that the contract be fulfilled as it should be. The State party will be aware that if the contract is terminated, it will have to find another contractor, with no guarantee of lower costs to perform the contract. Compensation will also be in the interest of the investor, especially in cases where a substantial upfront investment was made long before any profit was realised.

435. In the IIC context, the possibility of compensation may be integrated into the renegotiation process – *i.e.*, the parties may agree to the payment of compensation as part of their renegotiations. Compensation may also be included in an IIC as an independent and express remedy. For instance, the parties could decide to include compensation as a fallback option to renegotiation in order to avoid that prolonged or

[37] A principle of compensation follows *e.g.*, from French case law. Compensation may seem to shift the risk of hardship to the other party. This was the intention of the "*théorie de l'imprévision*" in France. The assumption was that a State would prefer the continued performance of an IIC given the general interest served by it, and would, in return, accept the shift in burden that comes with a compensation mechanism.

inconclusive renegotiations risk leaving the disadvantaged party without an effective remedy. The parties could specify that such compensation would only be due where the hardship event was beyond the control of both parties and renegotiation failed to restore equilibrium within a specified timeframe. Parties might choose several solutions, such as leaving it to adjudicators to decide on the amount of compensation or providing for automatic compensation (*i.e.*, a pre-agreed compensation fallback clause). They could also limit compensation as an express remedy to certain hardship events, such as terrorism or third-State acts.

436. While a court in the host State could decide on a solution (including compensation) based on the pursuit of the general interest as it exists in its legal system, an arbitral tribunal cannot be readily expected to substitute its own understanding of the public interest for that adopted by the public entity of that State. Consequently, the award of compensation by an arbitral tribunal may not be on the same terms as by the court of the host State.

437. Including compensation as an express remedy might have the benefit of enabling the court or arbitral tribunal to consider hardship without altering the contract. This is why, under French law, for example, compensation for hardship is awarded on an extra-contractual basis. However, reliance on such a mechanism may prove problematic outside the legal framework of a given State. Consequently, while this possibility of seeking compensation for the consequences of hardship does not amount to a guarantee or insurance policy for the benefit of the investor, but rather results from a given legal system's understanding of the general interest in the performance of contracts often connected with the provision of essential public services, such an approach may appear less readily transposable in proceedings before a judicial authority outside that State.

*E. Withholding performance*

438. As indicated in the commentary to Article 6.2.3(2) of the UPICC, suspension of performance can only be justified in extraordinary circumstances, or in exceptional circumstances creating an "unreasonable burden" as explained in the commentary to UPICC Article 7.2.2(b). The parties are advised to clarify in their IIC the extent to, and conditions under, which suspension of performance would be possible, considering the principle of continuity. There may also be situations of crisis (*e.g.,* war or economic collapse) in which resource or capacity constraints may affect how continuity is ensured in practice.

*F. Termination by mutual agreement*

439. Termination of the contract by mutual agreement is at the heart of party autonomy and should therefore be possible in the event of hardship. As mentioned above, Article 6.2.3(4)(b) of the UPICC also allows a court or arbitral tribunal to adapt or terminate the contract in the event of hardship. The ICC Model Clause on Hardship provides for three possibilities (termination by a party, termination or adaptation by the judge, termination by the judge) but does not envisage, for example, the granting of specific compensation for hardship accompanying termination. The parties to an IIC are advised to clarify in their contract the solution(s) that suit(s) them best.

**Model Clauses**

**Option 1: ICC Hardship Clause 2020**

1. A party to a contract is bound to perform its contractual duties even if events have rendered performance more onerous than could reasonably have been anticipated at the time of the conclusion of the contract.

2. Notwithstanding paragraph 1 of this Clause, where a party to a contract proves that:

a) the continued performance of its contractual duties has become excessively onerous due to an event beyond its reasonable control [and that of the State] which it could not reasonably have been expected to have taken into account at the time of the conclusion of the contract; and that

b) it could not reasonably have avoided or overcome the event or its consequences, the parties are bound, within a reasonable time of the invocation of this Clause, to negotiate alternative contractual terms which reasonably allow to overcome the consequences of the event.

*[N.B.: Options to be chosen by the parties when entering the contract]*

**Option 3A** - Party to terminate

Where paragraph 2 of this Clause applies, but where the parties have been unable to agree alternative contractual terms as provided in that paragraph, the party invoking this Clause is entitled to terminate the contract but cannot request adaptation by the judge or arbitrator without the agreement of the other party.

or

**Option 3B** - Judge to adapt or terminate

Where paragraph 2 of this Clause applies, but where the parties have been unable to agree alternative contractual terms as provided for in that paragraph, either party is entitled to request the judge or arbitrator to adapt the contract with a view to restoring its equilibrium, or to terminate the contract, as appropriate.

or

**Option 3C** - Judge to terminate

Where paragraph 2 of this Clause applies, but where the parties have been unable to agree alternative contractual terms as provided in that paragraph, either party is entitled to request the judge or arbitrator to declare the termination of the contract.

***

**Option 2: Alternative Model Clause on Hardship**

1. A case of hardship exists when, either because the cost of a Party's performance has increased, or because the value of the performance received by a Party has decreased, the occurrence of events fundamentally alters the equilibrium of the present Contract, and

(a) the events or their consequences occur or become known to the disadvantaged Party after the conclusion of the present Contract;

(b) the events or their consequences could not reasonably have been considered by the disadvantaged Party at the time of entering into the present Contract;

(c) the events are beyond the control of the disadvantaged Party and of the State; and

(d) the risk of the events has not been assumed by the disadvantaged Party within the framework of this Contract.

2. In the event of hardship, each Party shall nevertheless be bound to perform its obligations subject to the following provisions.

3. In the event of hardship, the disadvantaged Party is entitled to request renegotiation of the Contract. The request shall be made in writing within [*XX*] days after the occurrence of the event of

hardship or its consequences or after the requesting Party has knowledge of the event or its consequences. The request shall state the reasons on which it is based and shall contain a proposal for the solution of the consequences of the hardship on the equilibrium of the Contract.

4. The disadvantaged Party shall not be entitled to withhold performance as a result of the request for renegotiation.

5. The Parties shall meet within [*XX*] days of receipt of the request and shall have discussions in good faith with a view to renegotiate the Contract.

6. The renegotiation should aim to:

**OPTION 6.A**: restore the economic equilibrium that existed at the time immediately prior to the occurrence of the hardship.

**OPTION 6.B**: mutually acceptable termination of the contract or other suitable solutions

7. Failure to reach agreement shall not entitle the disadvantaged Party to withhold performance, nor shall it in itself permit unilateral termination of the Contract by either Party.

8. Upon failure to reach agreement within [*XX*] days after receipt of the request for renegotiation, either Party may refer the matter to [*include reference to applicable dispute resolution forum*].

9. If the [*court/arbitral tribunal*] finds hardship it may, as appropriate:

**OPTION 9.A**: terminate the Contract at a time and on terms to be determined.

**OPTION 9.B**:

(i) adapt the Contract so as to restore its equilibrium [**OPTION 6.A** or **OPTION 6.B**], or

(ii) terminate the Contract at a time and on terms to be determined.

**OPTION 9.C:**

(i) adapt the Contract so as to restore its equilibrium [*OPTION 6.A or OPTION 6.B*], but only if both Parties agree to the possibility of applying to the [*court/arbitral tribunal*] for this adaptation, or

(ii) terminate the Contract at a time and on terms to be determined.

Commentary to the ICC Hardship Clause 2020

440. The ICC Hardship Clause 2020 engages the parties to negotiate alternative contractual terms and suggests three remedial options in case of failure of renegotiation, to be chosen by the parties when they enter the contract: (i) termination by the party, (ii) adaptation and termination of the contract by the judge or the arbitrator, or (iii) termination of the contract by the judge or the arbitrator. These three alternative solutions are contained in paragraph 3 of the clause, as 3A, 3B and 3C.

441. In light of the recommendations set forth in the commentary (see Subsection A on unilateral termination), the suggested option 3A (Party to terminate) should be carefully considered by the parties.

442. Furthermore, parties shall check whether adaptation by the judge or the arbitrator, as provided in option 3B (Judge to adapt or terminate), is admitted according to the applicable law.

443. In option 3B, the judge or arbitrator may decide which of the two alternatives, adaptation or termination, is more appropriate, in particular where no adaptation is reasonably possible. Under this provision, the judge or arbitrator receives the power to change the contract terms in order to restore the

original balance of obligations, or, where this does not appear possible or appropriate, to declare its termination. In order to facilitate the determination of the possible terms of this adaptation, the judge or arbitrator may invite the parties to submit proposals of modification they would deem appropriate, which can be taken as a starting point for the adaptation.

Commentary to the Alternative Model Clause

444. As is the case with the suggested force majeure clause, the hardship clause starts with setting out the criteria to benefit from hardship protection.

445. An important clarification in the clause is the principle whereby, if a hardship situation has arisen, it does not automatically entitle the affected party to suspend or terminate the performance of the contract, including during the renegotiation phase. The rationale here is to avoid business disruption and maintain the continuity of public service while the parties endeavour to find a solution to the hardship impact.

446. In terms of renegotiation goals, the clause suggests various options depending on how the parties envisage a restoration of the economic equilibrium.

447. The same approach of options applies to the remedies that the parties may wish a court or arbitral tribunal to apply, depending on whether they wish to allow the court or arbitral tribunal to merely decide on the contract's termination, or whether they want to give the court or arbitral tribunal more flexibility in applying remedies to overcome the hardship situation.

## 2. Force majeure

**Principle 24**

**(1) Nothing in Article 7.1.7 of the UPICC limits the right of the parties to re-negotiate the contract as necessary as a result of force majeure.**

**(2) If a dispute arises as to whether a right to suspend performance or terminate the contract as a result of force majeure was properly exercised, the parties may stipulate a dispute resolution mechanism, such as dispute boards.**

**Relevant UPICC provision**

Article 7.1.7 (Force majeure) of the UPICC

**Commentary**

448. The notion of force majeure is now widely accepted and used in international trade and cross-border contracts. Article 7.1.7 of the UPICC sets out the principle that, when a force majeure event occurs, the defaulting party is excused for the non-performance.

449. In principle, the impossibility of performing the contractual obligations distinguishes force majeure from hardship, where the contract performance has become more onerous but not impossible. However, literature has more and more often stressed how difficult it is to clearly distinguish *ex ante* cases of force majeure from hardship, thus suggesting a limited use of the notion of "impossibility".

450. In general, a force majeure clause would excuse non-performance by a party where (a) an impediment to performance has occurred after the conclusion of the contract; (b) the impediment was

beyond the party's control; (c) the party could not reasonably have taken the impediment into account at the time of the conclusion of the contract; and (d) the impediment makes it impossible for the party to perform the contract.[38]

451. The following factors should be recognised as being particularly relevant in applying the concept of force majeure to IICs:

(a) The amount of resources invested may be substantial;

(b) Return on investment may be deferred;

(c) Projects may not be easily dismantled or removed, *e.g.*, infrastructure projects; and

(d) Contracts may be long-term.

452. This means that a force majeure event should not, as far as possible, lead to a termination of the contract. Parties should be encouraged, in their interests, to try to keep the contract "alive".

453. Termination, if at all, should be authorised only in the event of a prolonged force majeure situation, since a prolonged status means that (i) the equilibrium of the contract becomes severely impacted and (ii) resumption of performance at a later stage becomes more doubtful, thereby reducing the rationale for contract renegotiation.

454. On the other hand, force majeure should also not lead to a contract being disrupted without good reason, and parties not being able to avail themselves of the remedy of termination. It should be a genuinely disruptive event that makes performance impossible. To that end, Principle 24 provides that nothing in Article 7.1.7 of the UPICC limits the right of the parties to renegotiate the contract as necessary and that where disagreement on the proper exercise of a suspension or termination of the contract for force majeure arises, dispute resolution mechanisms (*e.g.*, dispute boards), may be useful while the contract carries on.

455. Force majeure clauses typically also cover sovereign or governmental acts. In commercial contracts between private parties, it is logical that such acts may qualify as force majeure events because they are beyond the control of both parties. In the IIC context, however, one of the contracting parties is a State or State-related entity. Under Article 7.1.7 of the UPICC, force majeure requires that the impediment is beyond the control of the party invoking it to excuse its non-performance. Accordingly, a State should not ordinarily be entitled to invoke force majeure in relation to events or measures failing within its sphere of control. But still, force majeure clauses in IICs should be carefully drafted so as to avoid situations in which the State could trigger or rely upon its own sovereign acts in order to suspend or terminate the contract. Therefore, it may be considered to limit the possibility of termination for force majeure events that fall within the control of the host State and/or exclude such events from the scope of force majeure if the contract provides the investor with other adequate protection (*e.g.*, through a stabilisation clause or the ordinary measures provided for in Chapter 7 for cases of non-performance by the host State).

456. Standard force majeure rules typically excuse performance but do not provide a right to compensation. As a result, investors may remain exposed to irreversible capital losses arising, for instance, from armed conflicts, insurrections, civil strife, or other catastrophic events. In line with IICs practice, the parties could consider agreeing *ex ante* on risk-sharing mechanisms, such as partial compensation schemes, insurance-trigger mechanisms, or revenue-balancing arrangements, particularly in relation to high-impact force majeure events that are not attributable to either party and which may not be fully

[38] UPICC Article 7.1.7; ALIC 5.1.7.

insurable. Such clauses may help preserve the financial viability of long-term investment projects despite catastrophic events, while promoting fairness and preventing prolonged force majeure from disproportionally burdening one party (*e.g.*, the State retaining revenues while operations are suspended).

**Model Clause**

**ICC Force Majeure Clause Short Form - 2020 (with modification)**[39]

1. "Force Majeure" means the occurrence of an event or circumstance that prevents or impedes a Party from performing one or more of its contractual obligations under the contract, if and to the extent that that Party proves:

(a) that such impediment is beyond its reasonable control; and

(b) that it could not reasonably have been foreseen at the time of the conclusion of the Contract; and

(c) that the effects of the impediment could not reasonably have been avoided or overcome by the affected Party.

2. In the absence of proof to the contrary, the following events affecting a Party shall be presumed to fulfil conditions (a) and (b) under paragraph 1 of this Clause:

(a) war (whether declared or not), hostilities, invasion, act of foreign enemies, extensive military mobilisation;

(b) civil war, riot, rebellion and revolution, military or usurped power, insurrection, act of terrorism, sabotage or piracy;

(c) currency or trade restrictions, embargoes, sanctions;

(d) act of authority whether lawful or unlawful, compliance with any law or governmental order, expropriation, seizure of works, requisition, nationalisation;

(e) plague, pandemic, epidemic, natural disaster or extreme natural event;

(f) explosion, fire, destruction of equipment, prolonged break-down of transport, telecommunication, information system or energy;

(g) general labour disturbance such as boycott, strike and lock-out, go-slow, occupation of factories and premises.

3. A Party successfully invoking this Clause is relieved from its duty to perform its obligations under the Contract and from any liability in damages or from any other contractual remedy for breach of contract, from the time at which the impediment causes inability to perform, provided that the written notice thereof is given without delay. If such notice thereof is not given without delay, the relief is effective from the time at which notice thereof reaches the other Party. Where the effect of the impediment or event invoked is temporary, the above consequences shall apply only as long as the impediment invoked impedes performance by the affected Party. Where the duration of the impediment invoked has the effect of substantially depriving the contracting Parties of what they were reasonably entitled to expect under the Contract, either Party has the right to terminate the contract by notification within a reasonable period to the other Party. Unless otherwise agreed, the Parties

[39] Slight amendments have been made to adapt the Model Clause to the context of IICs; for the original language, see "ICC Force Majeure and Hardship Clauses", March 2020, available at: https://iccwbo.org/wpcontent/uploads/sites/3/2020/03/icc-forcemajeure-hardship-clauses-march2020.pdf.

expressly agree that the Contract may be terminated by either Party if the duration of the impediment exceeds 12 months.

**ICC Force Majeure Clause Long Form – 2020 (with modifications)**

1. **Definition**. "Force Majeure" means the occurrence of an event or circumstance ("Force Majeure Event") that prevents or impedes a party from performing one or more of its contractual obligations under the contract, if and to the extent that the party affected by the impediment ("the Affected Party") proves:

a) that such impediment is beyond its reasonable control; and

b) that it could not reasonably have been foreseen at the time of the conclusion of the contract; and

c) that the effects of the impediment could not reasonably have been avoided or overcome by the Affected Party.

2. **Non-performance by third parties**. Where a contracting party fails to perform one or more of its contractual obligations because of default by a third party whom it has engaged to perform the whole or part of the contract, the contracting party may invoke Force Majeure only to the extent that the requirements under paragraph 1 of this Clause are established both for the contracting party and for the third party.

3. **Presumed Force Majeure Events**. In the absence of proof to the contrary, the following events affecting a party shall be presumed to fulfil conditions (a) and (b) under paragraph 1 of this Clause, and the Affected Party only needs to prove that condition (c) of paragraph 1 is satisfied:

a) war (whether declared or not), hostilities, invasion, act of foreign enemies, extensive military mobilisation;

b) civil war, riot, rebellion and revolution, insurrection, act of terrorism, sabotage or piracy;

c) currency or trade restrictions, embargoes, or sanctions;

d) plague, pandemic, epidemic, natural disaster or extreme natural event;

e) explosion, fire, destruction of equipment, prolonged break-down of transport, telecommunication, information system or energy;

f) general labour disturbance such as boycott, strike and lock-out, go-slow, occupation of factories and premises.

4. **Notification**. The Affected Party shall give notice of the event in writing without delay to the other party.

5. **Consequences of Force Majeure**. A party successfully invoking this Clause is relieved from its duty to perform its obligations under the Contract and from any liability in damages or from any other contractual remedy for breach of contract, from the time at which the impediment causes inability to perform, provided that the notice thereof is given without delay. If notice thereof is not given without delay, the relief is effective from the time at which notice thereof reaches the other party. The other party may suspend the performance of its obligations, if applicable, from the date of the notice.

6. **Temporary impediment**. Where the effect of the impediment or event invoked is temporary, the consequences set out under paragraph 5 above shall apply only as long as the impediment invoked prevents performance by the Affected Party of its contractual obligations. The Affected Party must notify the other party as soon as the impediment ceases to impede performance of its contractual obligations.

7. **Duty to mitigate**. The Affected Party is under an obligation to take all reasonable measures to limit the effect of the event invoked upon performance of the contract.

8. **Contract termination**. Where the duration of the impediment invoked has the effect of substantially depriving the contracting parties of what they were reasonably entitled to expect under the contract, either party has the right to terminate the contract by notification within a reasonable period to the other party. Unless otherwise agreed, the parties expressly agree that the contract may be terminated by either party if the duration of the impediment exceeds [12 months].

9. **Unjust enrichment**. Where paragraph 8 above applies and where either contracting party has, by reason of anything done by another contracting party in the performance of the contract, derived a benefit before the termination of the contract, the party deriving such a benefit shall pay to the other party a sum of money equivalent to the value of such benefit.

Commentary to the ICC Force Majeure Clause 2020

457. The ICC Force Majeure Clause (Long Form) can be included in the contract or incorporated by reference by stating "The ICC Force Majeure Clause (Long Form) is incorporated in the present contract". Parties may also use the Clause as the basis for drafting a "tailor-made" clause, which takes into account their specific needs. Should the parties prefer a shorter clause, they can include in their contract the "Short Form" of the ICC Force Majeure Clause.

458. The Long Form, especially the comments included in the original,[40] may give guidance on issues in which the Short Form is silent. The main consequence of successfully invoking force majeure is that the affected party is relieved from its duty to perform and from responsibility or damages from the date of occurrence of the event (provided that the other party has been notified in a timely manner) and, in case of a temporary impediment, until the impediment ceases to prevent the performance.

459. As regards the question of what constitutes force majeure, the ICC Force Majeure Clause intends to achieve a compromise between the general requirements of force majeure, which need to be met in all cases, and the indication of events presumed to be beyond the control of the parties and not foreseeable at the time of the conclusion of the contract. For that purpose, the ICC Force Majeure Clause provides a general definition (paragraph 1) and a list of force majeure events that are presumed to qualify for force majeure (paragraph 3). Parties are invited to check the list and verify if some events should be deleted from or added to it.[41]

460. The general definition of force majeure requires three conditions, all of which must be fulfilled in order to relieve a party of its duties. However, as regards the two first conditions, (a) and (b), they are presumed to be fulfilled in case of listed events, while the third one must be proved in any case by the affected party.

461. The conditions are worded in such a way as to provide a threshold lower than impossibility in order to relieve a party from its duties, by introducing the criterion of reasonableness.

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[40] Slight amendments have been made to adapt the Model Clause to the context of IICs; for the original language, see "ICC Force Majeure and Hardship Clauses", March 2020, available at: https://iccwbo.org/wpcontent/uploads/sites/3/2020/03/icc-forcemajeure-hardship-clauses-march2020.pdf.

[41] For instance, the parties may wish to consider whether to exclude events that are within the scope of control of the State, as discussed in paragraph 455 of this Chapter (e.g., currency or trade restrictions, embargoes, sanctions; act of authority whether lawful or unlawful, compliance with any law or governmental order, expropriation, seizure of works, requisition, nationalisation).

462. Thus, for instance, when it would in theory be possible to ship by plane a large quantity of iron when shipment by sea (as agreed in the contract) is prevented, the force majeure defence will nevertheless apply if the affected party can prove that shipment by air is not a reasonable way to overcome the impediment.

463. The parties may of course modify the clause by making it more restrictive (*e.g.*, by cancelling the reference to reasonableness) or more flexible (*e.g.*, by excluding the unforeseeability requirement). However, they are advised, when changing the balance of the force majeure conditions, to always keep in mind that the clause can benefit both parties.

464. Paragraph 2 of the clause deals with a specific issue, *i.e.*, the case of force majeure invoked because of non-performance by third parties (subcontractors). This provision states, in conformity with Article 79(2) of the Vienna Convention on the International Sale of Goods (CISG) of 1980, that the affected party may invoke force majeure only if the requirements of force majeure are established both for that party and the third party. In other words, the affected party must prove that the third party was subject to force majeure as well.

465. It should be noted that this provision refers to "third parties engaged to perform one or more contractual obligations" of the affected party, *i.e.*, subcontractors, and does not extend to those who supply products or services to the affected party. Non-performance by simple suppliers will normally not amount to force majeure.

466. Paragraph 5 of the clause states: *"A party successfully invoking this Clause is relieved from its duty to perform its obligations under the Contract and from any liability in damages or from any other contractual remedy for breach of contract …"* Consequently, the affected party is not responsible for damages, penalties, etc. due to impediments falling under the definition of force majeure. It is important to stress that the force majeure event relieves a party from the duty to perform its obligations but does not entitle the party to claim for the extra costs sustained or damages suffered as a consequence of the force majeure event, except if the parties have agreed otherwise (see the explanations on possible ex-ante risk sharing mechanisms above).

467. In the IIC context, certain force majeure events may be caused by the action, behaviour, or conduct of the State. In such cases, the State should not be entitled to claim force majeure and termination, while the investor may address the consequences of State action under the stabilisation principle, if applicable, or by claiming the ordinary remedies available under Chapter 7 (termination and compensation) for events of default.

468. As provided in the second part of paragraph 5, the effects of the force majeure occur "[...] from the time at which the impediment causes inability to perform, provided that the notice thereof is given without delay". The obligation to notify of the force majeure event in a timely manner, as reiterated in paragraph 4 (Notification), is an essential feature of the force majeure clause. If notice of the event has not been given in a timely manner, relief will only be effective when the notice reaches the other party. Thus, for instance, if an event causing delay in performance is not notified in a timely manner, the affected party will benefit from its effects (relief from performance and possible penalty) only from the date on which the other party has been informed. This is an important means for preventing a party from invoking the existence of an alleged force majeure event only when the other party claims non-performance of its obligations.

469. Paragraph 6 provides to this effect: (i) that the consequences of force majeure shall apply "[...] only as long as the impediment invoked prevents performance by the Affected Party of its contractual

obligations", and (ii) that "[...] the Affected Party must notify the other party as soon as the impediment ceases to impede performance of its contractual obligations."

470. Furthermore, paragraph 8 provides that, when the duration of the force majeure goes on for too long and consequently has the effect of depriving the contracting parties of what they were reasonably entitled to expect under the contract, either party has the right to terminate the contract by notification to the other party within a reasonable time. The clause expressly provides a maximum period of 120 days, which applies unless otherwise agreed by the parties. For IICs, this time period was extended to 12 months.

# CHAPTER 7. REMEDIES, INCLUDING COMPENSATION AND DAMAGES

## A. Introduction

471. Because investment contracts typically involve the public interest and are long-term in nature, parties to an IIC are expected to perform their obligations and maintain their contractual relationship as agreed. Accordingly, parties to an IIC have a duty to cooperate more closely with each other towards compliance of their respective contractual obligations than if they were in a purely commercial context. Article 5.1.3 of the UPICC provides guidance as to how the duty of cooperation, particularly in the context of long-term and complex contracts, must be understood.

472. This Chapter addresses remedies for non-performance (or breach) of obligations arising out of IICs. Such remedies shall be primarily determined on the basis of the terms and conditions contracted for by the parties. The law governing the IIC may limit the parties' freedom to regulate the remedy regime applicable to their investment contract.

473. The Principles contained in this Chapter and the relevant UPICC provisions referred to below provide guidance to parties and adjudicators as to the remedies applicable in case of non-performance of obligations arising from an IIC.

474. The most common remedy in investment disputes is monetary compensation, also known as damages. However, given the public interest concerns typically associated with IICs, the remedy of monetary compensation should be considered a last resort ("a fallback remedy") when other less onerous remedies are available and accepted by the parties.

475. As a remedy for breach, monetary compensation flows from principles firmly rooted in contract law, such as the right to damages and full compensation (Articles 7.4.1 and 7.4.2 of the UPICC, respectively). Questions regarding the certainty of harm (Article 7.4.3), causation, foreseeability (Article 7.4.4), mitigation (Article 7.4.8), and contributory fault (Article 7.4.7) are central to the calculation of damages and may reduce the amount due to the aggrieved party. In this regard, the UPICC provide an appropriate framework to address the controversial issue of a fair and proportionate calculation of damages for non-performance of contractual obligations in IICs.

476. The complexity of investment relationships often makes the counterfactual scenario highly speculative, especially in early-stage projects or high-risk industries. For this reason, a liquidated damages clause that predetermines a specific amount of money one party must pay the other in the event of breach of the IIC provides certainty and avoids the difficulty of proving actual damages. This type of clause – referred to as an "agreed payment for non-performance" under Article 7.4.13 of the UPICC – is especially relevant in the context of IICs, where the exact loss from a breach is frequently hard to calculate (see Section F.4 in this Chapter).

477. Beyond damages, the UPICC lists a number of other remedies that may be considered by the parties or the adjudicator in case of non-performance of an IIC. These remedies include but are not limited to: withholding performance (Article 7.1.3), which may serve as an incentive to perform the contract (see Section B.1); specific performance (Article 7.2.2), which reinforces the binding character of the contract but is subject to certain qualifications; and restitution (Articles 7.3.6 and 7.3.7), which is primarily used in case of contract termination to restore the *status quo ante* (*i.e.,* the position of the parties as it existed prior to the conclusion of the contract). Parties to an IIC are encouraged to specifically regulate the restitution and transfer of infrastructure and equipment as a consequence of contract termination, relinquishment of explored areas, and completion of contract performance.

478. As the UPICC offer a comprehensive framework for addressing contractual non-performance in a manner sensitive to contractual justice and international standards, several UPICC provisions relating to non-performance, right to performance, termination, and damages may be integrated into or applied to IICs. The synergy between the UPICC and State-investor relations is especially evident in long-term contracts, which are vulnerable to economic and political disruptions.

479. The provisions contained in Chapter 7 of the UPICC on non-performance form the basis of the guidance in this Chapter. Where a UPICC provision applies *telle quelle,* it is not repeated here. Where appropriate, additional commentary is provided on the application of UPICC provisions in the context of IICs. Moreover, a number of new principles specific to IICs, reflecting their particular characteristics, are proposed.

## B. Types of remedies for non-performance

### 1. Withholding Performance

**Relevant UPICC provision**

Article 7.1.3 (Withholding performance) of the UPICC

**Commentary**

480. Article 7.1.3 of the UPICC allows a contracting party to withhold performance until the other party has performed. While this provision may be appropriate in the investment context, its application should consider the specific characteristics of IICs.

481. Parties to an IIC usually undertake multiple obligations, some of which may be performed simultaneously, while others may be performed consecutively. The remedy of withholding performance provided for in Article 7.1.3(1) of the UPICC only applies where the parties are to perform simultaneously, while Article 7.1.3(2) applies to situations in which the parties are to perform consecutively. Since IICs are typically long-term contracts involving different obligations to be performed at different times, the parties may wish to consider whether the right to withhold performance should be limited to situations in which there is a sequence of timing that justifies compelling the non-performing party to perform at a specific time.

482. Furthermore, IICs often involve the provision of essential public services, such as water supply, waste management, essential power supply, and communication networks, which cannot be disrupted without profound and multifaceted negative effects on the population in general. This is why some jurisdictions do not authorise the investor to activate the *"exceptio non adimpleti contractus".* Thus, parties must be aware of, and accordingly address in their IICs, the fact that, in certain situations, withholding performance might not be desirable or even legally possible.

483. As withholding performance is not a mandatory principle under the UPICC, parties are free to adapt it to the particular circumstances of their project. While parties may agree to integrate into their IIC the UPICC principle of withholding performance, they must nonetheless also abide by the principle of continuity and the duty to ensure the provision of essential public services. With regard to other types of investments (*e.g.,* certain construction contracts), parties may wish to exclude withholding performance to ensure that the project be finalised within the agreed timeframe.

**Illustration**

In the context of a 30-year concession for electricity distribution in a densely populated region, for the third consecutive year State A fails to comply with its obligation to review the rates paid by consumers, which leads to a serious economic disequilibrium of the contract.

While investor A has a right to seek a review of the rates paid by consumers, it cannot withhold performance (*i.e.*, reduce or suspend the distribution of electricity) while State A has not tendered its performance under the IIC.

In the present case, investor A must abide by the principle of continuity and the duty to ensure the provision of essential public services even where the contract has become economically or financially unbalanced.

484. Non-application of the right to withhold performance does not prevent the investor from pursuing other remedies for non-performance of the IIC by the State.

**Model Clauses**

Where appropriate, contract language may stipulate that performance can only be withheld in exceptional circumstances or cannot be withheld at all.

**Option 1:**

**Withholding Performance (fundamental non-performance)**

In the event of non-performance by a Party amounting to a fundamental breach, both Parties agree that the innocent Party may withhold performance until the other Party cures the breach and tenders its performance.

**Option 2:**

**Continuing Performance**

Each Party acknowledges and accepts that continuity of public services is a fundamental principle of this Contract. In the event of non-performance by a Party, both Parties hereby waive any right to withhold performance and agree to continue their respective performance under this Contract to the extent feasible in light of the other Party's non-performance.

### 2. Cure by non-performing party

**Relevant UPICC provision**

Article 7.1.4 (Cure by non-performing party) of the UPICC

**Commentary**

485. This UPICC provision sets out a pro-contract regime that allows a non-performing party to cure its non-performance. The non-performing party must give notice of cure, which the aggrieved party is obliged to accept. It also contains conditions for cure by the non-performing party and the consequences of invoking the right to cure.

486. As IICs are usually long-term projects, cure by the non-performing party may be relevant to ensure continuity of services and contract preservation. Under certain contracts, the investor must give prompt notice of cure to the State in order to avoid the latter's exercise of step-in rights.

487. One of the conditions of a right to cure is that it be carried out promptly. However, the types of obligations found in IICs are such that prompt cure of non-performance may not always be possible. Many of these obligations require the performance of complex activities over several months and years. So, non-performance (or partial non-performance) may only be detected after many months, and, in turn, may only be cured after several more months or years. Hence, parties to an IIC are encouraged to establish a procedure to cure non-performance that is adapted to the particular circumstances of their project.

**Model Clause**

The language adopted by the parties to an IIC may distinguish which obligations are not covered by the right to cure non-performance.

| |
|---|
| Cure by non-performing Party (Article 7.1.4 of the UPICC) does not apply to [*list the provisions in the contract*]. |

### 3. Additional period for performance

**Relevant UPICC provision**

Article 7.1.5 (Additional period for performance) of the UPICC

**Commentary**

488. In contractual relationships, there may be good reasons why an aggrieved party may grant additional time to a non-performing party to perform its obligations – so too in IICs. This UPICC provision sets out the regime by which an aggrieved party may grant additional time to the non-performing party – in contrast to the previous provision, where the non-performing party initiates the additional time by giving notice to cure non-performance.

489. While this provision allows the aggrieved party to withhold performance of its own reciprocal obligations (if not excluded by agreement or by the otherwise applicable law) and seek damages incurred during the additional time, the aggrieved party is prevented from terminating the contract during the extension. If the non-performing party does not perform during the additional time, then the aggrieved party may terminate the contract. If the delay in performance was not yet fundamental when the additional time was granted, Article 7.1.5(3) of the UPICC specifies that termination is only permitted at the end of the period of extension if that extension was of reasonable length. In the context of IICs, the non-performed obligation must be fundamental for the aggrieved party to resort to termination (see Section D below). The determination of breach of a fundamental obligation will depend on contract interpretation and the facts of each case.

490. IICs often contain provisions that foresee that performance might be delayed. Usually, these provisions require the non-performing party to ask the other party for an extension of time. More time is usually available at the discretion of the aggrieved party. However, it is not the usual practice that the aggrieved party initiates the extension of time.

491. When drafting an IIC, parties should consider contract language that sets out the circumstances under which additional time may be granted by the aggrieved party, and any situations in which additional time may not be granted (*e.g.*, in cases of repeated or wilful breach). It may also be appropriate to specify how additional time may be granted depending on the type of obligation, *e.g.*, payment obligations (sign-up bonuses, royalties, taxes, etc.), other obligations (*e.g.*, construction milestones, provision of services, mineral production, power generation, etc.).

492. To avoid prolonged non-compliance, including in cases of environmental harm, parties may wish to set clear limits on cure periods or even impose immediate cure. For instance, the contract could establish the additional period of time in advance, depending on the type of breach, or it could indicate that any extension be of a reasonable length, considering the nature of the contract and the type of non-performance to be cured. The contracting parties may also wish to specify the consequences of non-performance in the additional period.

## C. Right to Performance

### 1. Performance of monetary obligation

**Relevant UPICC provision**

Article 7.2.1 (Performance of monetary obligation) of the UPICC

**Commentary**

493. This UPICC provision reflects the generally accepted principle that payment of money due under a contractual obligation can always be demanded and, where the demand is not met, can be enforced through legal action (arbitral tribunal, court). The effect of the provision is that a party may demand payment or ask an adjudicator (arbitrator, judge) to compel the other party to pay the money it owes.

494. In the context of IICs, money may be owed by the investor to the State for sign-up bonuses, royalties, share of profits, etc. Money may also be owed by the State to the investor for tax rebates, VAT refunds, or compensation for infrastructure costs in the context of a public-private partnership. Hence, it might be useful that the IIC contain declarations and assurances by the parties to the effect that appropriate approvals for the transfer of money will be given. Payments and transfers are dealt with more specifically in Chapter 5, Section C.3 of this Instrument.

495. Whether performance of a monetary obligation is due or not depends on factors such as time of performance, place of payment, method of payment, and proper currency. It may also be contingent on the certainty of the required amount and the fact that it is due for payment.

496. At the drafting stage of the IIC, due consideration must be given by the parties to particular circumstances that may characterise force majeure or hardship, such as the effects of international sanctions on the enforcement of monetary obligations arising from an IIC. Hardship and force majeure are dealt with more specifically in Chapter 6, Section B, of this Instrument.

497. Parties to an IIC should consider situations where the obligee, usually the investor, sells its right to payment of a monetary sum from the State (the obligor) to a third party. The purpose of such assignment of monetary rights may be to finance the investor's ordinary activities (*e.g.,* by way of factoring or securitisation of receivables) or the investor's claim against the obligor.

498. Chapter 9, Section 1 of the UPICC deals with assignment of rights. Several of its provisions may be useful to regulate the assignment of monetary rights in the context of an IIC, such as those that address the definition of an assignment (Article 9.1.1), the possibility of a partial assignment and of future rights (Articles 9.1.4 and 9.1.5, respectively), the fact that the mere agreement between assignor and assignee is sufficient to transfer the monetary rights of the former (Article 9.1.7), and the fact that, until the obligor receives a notice of the assignment from either the assignor or assignee, it is discharged by paying the assignor.

**Illustration**

In the context of a 25-year public-private partnership (PPP) for healthcare infrastructure and services, State A undertakes to pay for all infrastructure costs (maintenance and utilities costs), while service costs are to be borne by healthcare patients.

Investor B is the private operator who undertakes to build, develop and maintain the facilities, the costs of which (both capital and operational expenditures) are to be periodically reimbursed by State A.

The PPP contract does not prevent B from assigning to a third party its right to payment of monetary sums from State A. Thus, in order to finance its activities, investor B may assign its monetary rights to company C by way of securitisation of receivables.

**Model Clause**

**Assignment of monetary rights:** A Party's right to the payment, either actual or future, of a monetary sum under this Contract may be assigned to a third party. The other Party must be given prompt notice of assignment made by the Party entitled to payment.

499. In the context of IICs, parties should also consider two other situations concerning the assignment of rights and/or obligations, namely: (i) the assignment of the IIC as a whole; and (ii) the assignment of claims (usually against the State party).

500. The investor cannot assign the contract as a whole to a third party without previous and express consent of the State party. Articles 9.3.1 to 9.3.7 of the UPICC provide guidance to parties in this matter. Furthermore, parties to an IIC are encouraged to specifically regulate situations which qualify as intra-group assignment (*i.e.*, assignment of the contract to an affiliate entity) and whether those situations require the previous and express consent of the other party.

501. In the investment context, even where the State party consents in advance to the assignment of the IIC in some circumstances, including intra-group assignments, parties are advised to submit the effectiveness of such assignment to a reasonableness test. The reasonableness test consists of assessing the fairness and appropriateness of the assignment of the contract in the circumstances, considering what a reasonable person would expect.

502. Should one of the parties to an IIC assign monetary rights in spite of a non-assignment clause, the conflicting interests of the obligor and the assignee must be weighed. The approach followed in the UPICC (Article 9.1.9) is that the assignee must be protected – meaning that the assignment of a monetary right is effective despite a non-assignment clause (while the assignor may be liable to the obligor for breach of contract). In the investment context, where non-assignment clauses are commonly used and serve legitimate purposes, the application of Article 9.1.9(1) of the UPICC should be adjusted for IICs.

Accordingly, in the context of IICs, non-assignment clauses should be given full effect, including for monetary rights, subject to a reasonableness standard. The parties should distinguish between the assignment of individual claims (which may be permissible in certain circumstances, such as project finance or third-party funding) and the assignment of the contract as a whole (which requires prior consent). This adjustment is without prejudice to the legitimate interests of lenders and project financiers, who may require the assignment of receivables as security, but it ensures that the State party's interest in controlling the identity of its contractual counterpart is adequately protected.

**Illustration**

In the context of a 25-year public-private partnership (PPP) for healthcare infrastructure and services, State A has expressed its previous consent to the assignment of the PPP contract by the original investor (B) to an affiliate company in the future, except where such assignment is deemed unreasonable.

After five years of poor operational records, investor B gives notice to State A that the PPP contract will be assigned to a newly-created affiliate company, with no financial and credit history, and no experience in the healthcare market. State A rightly opposes such assignment, unreasonable under the circumstances.

**Model Clause**

**Assignment of the contract:** No Party shall assign this Agreement or any part hereof without the prior written consent of the other Party. Subject to the foregoing, this Agreement shall be binding upon and inure to the benefit of the Parties and their respective permitted successors.

**Option 1:** Such consent shall not be unreasonably conditioned, withheld or delayed.

**Option 2:** Such consent may be granted or withheld at the State's discretion, including on public-interest grounds.

**Assignment to affiliate:** The Investor shall be entitled to assign to an affiliate its rights and obligations under this Agreement without the prior written consent of the State party, except where such assignment is deemed unreasonable. For purposes of this clause, an "affiliate" shall mean an entity controlled by, controlling or under common control with the Party, but only so long as such control exists.

503. Finally, situations in which the investor may wish to assign a claim it has against the State party to a third party will be addressed in Chapter 8 of this Instrument.

### 2. Performance of non-monetary obligation

**Relevant UPICC provision**

Article 7.2.2 (Performance of non-monetary obligation) of the UPICC

**Commentary**

504. Article 7.2.2 of the UPICC provides for specific performance of non-monetary obligations; it allows each party, as a rule, to require performance by the other party of non-monetary obligations assumed by that party. This general rule contains several exceptions, namely: a) when performance is impossible in law or in fact; b) when performance is unreasonably burdensome or expensive; c) when the party entitled

to performance may reasonably obtain performance from another source; d) when performance is of an exclusively personal character; or e) when the party entitled to performance does not require performance within a reasonable time after it has, or ought to have, become aware of the non-performance.

505. Specific performance is a familiar, and often preferred, remedy in civil-law jurisdictions. It is less so in common-law jurisdictions, where it is generally regarded as an exceptional remedy. Where specific performance is unavailable or inadequate, the obligee may resort to other available remedies, in particular a claim for damages.

506. In contemporary IIC practice, parties rarely seek specific performance, preferring instead to claim damages for breach. Even when specific performance is requested, it is typically sought only in the alternative. This preference reflects considerations that go beyond the exceptions listed in Article 7.2.2 (a)-(e) of the UPICC. They may include, for example, concerns that a court or arbitral tribunal may not be able to compel a State to perform or that specific performance interferes with the sovereign acts of States. Specific performance may include acts such as reinstating a licence or giving access to an area or region. In the context of IICs, an order of specific performance is not in any way meant to affect the State's power to regulate. Stabilisation clauses and their impact on IICs are dealt with more specifically in Chapter 6, Section B, of this Instrument.

507. However, there are some contractual arrangements where specific performance is likely to be sought, particularly against the investor. This is especially true in public utility contracts (*e.g.,* water, sewage, and electricity services), where the continuity and adequacy of the service are matters of public interest. If the concessionaire fails to perform, or performs inadequately, an adjudicator may order specific performance to ensure compliance with the contractual obligations undertaken.

508. Parties to an IIC may stipulate that specific performance cannot be requested against the State party so that, in case of non-performance by the State, the aggrieved party must claim damages instead or request renegotiation of the contract terms and conditions (*e.g.,* extension of the concession term).

**Illustration**

In the context of a 30-year highway concession contract, investor A fails to expand the road system by the time-limit set out in the programme of works approved by State B.

In accordance with the IIC concluded by the Parties, State B decides to exercise its right to compel A to specifically perform its obligations under the contract.

To that end, State B starts arbitration proceedings against A and requests the arbitral tribunal to order A to specifically perform the road expansion, along with payment of recurring penalties (*astreintes*) and damages.

In defence, A argues that State B's request should be dismissed, since in the case at hand performance or, where relevant, enforcement is unreasonably burdensome or expensive, given that State B has not removed illegal occupants from the areas to be used for expansion of the road system as agreed in the contract.

**Illustration**

In the context of a 30-year highway concession contract, State B fails to remove illegal occupants from the areas to be used for expansion of the road system by the time-limit set out in the programme of works approved by the parties.

As the IIC concluded by the Parties does not permit investor A to request specific performance of non-monetary obligations undertaken by State B, investor A must, as an alternative, (i) claim damages or (ii) request renegotiation of the contract terms and obligations.

### 3. Penalty imposed by a court or arbitral tribunal

**Principle 25**

**The parties to an IIC may agree whether a penalty payment consisting of a coercive monetary measure may be sought from a court or arbitral tribunal to encourage compliance with orders of performance issued by that forum. Any such agreement between the parties operates only to the extent permitted by applicable law and the relevant procedural rules.**

**Relevant UPICC provision**

Article 7.2.4 (Judicial penalty) of the UPICC

**Commentary**

509. A penalty payment as referred to here is an indirect enforcement measure whereby a sum of money is ordered by a judge or arbitrator to compel a party to perform an order issued by the court or arbitral tribunal. Such order issued by the court or arbitral tribunal usually refers to the performance (or non-performance) of a contract term or condition by a party. Parties can agree to such a penalty payment in their IIC unless this is prohibited by the applicable law. This Principle, adjusted to the investment context, is based on Article 7.2.4 of the UPICC, which aims at ensuring a party's compliance with an order for performance given by a court or arbitral tribunal by imposing on that party a monetary penalty for non-compliance.

510. The monetary penalty ordered by a court (or arbitral tribunal) for compliance with its own order, referred to in this Principle, is owed to the party requesting the order to the court or arbitral tribunal. It is to be distinguished from a contractual penalty clause and a liquidated damages clause or an agreed payment for non-performance (Article 7.4.13 UPICC, see Section F.4 below). While the former aims at ensuring a party's compliance with a court order for performance of the contract, the latter facilitates the recovery of damages for breach of contract or operates as a deterrent against non-performance.

511. In the context of IICs, this kind of penalty is uncommon, thus rarely sought or imposed. Differently from the UPICC provision, this Principle regulates the applicability of such coercive monetary measures with a focus on the parties' agreement and the limitations arising from the applicable laws and regulations.

512. While parties to an IIC are free to cover this matter in their contract, they must be aware that one of the contracting parties is a State or State entity, which may give rise to issues of non-enforceability.

513. The court's power to impose a penalty on the party who does not comply with an order for performance issued by that court cannot usually be changed by agreement of the parties. Parties to an IIC can nonetheless agree contractually whether to seek such penalties before a court.

514. Furthermore, parties to an IIC may agree to grant (or to exclude from) an arbitral tribunal the power to impose penalties on a party for the same purposes. Whether such agreement is enforceable will depend on the laws applicable to the dispute, the *lex arbitri,* the applicable arbitration rules, and the court's powers to enforce such order.

515. While penalties are a discretionary tool for courts and arbitral tribunals, they may serve as an incentive for performance, without affecting the aggrieved party's claim for damages.

**Model Clause**

**Option 1:** In case of non-performance, the aggrieved Party may resort to all remedies available under the applicable law, including penalties for non-compliance with an order for performance made by the applicable dispute resolution forum.

**Option 2:** The parties agree not to seek penalties for non-compliance with an order for performance issued by the applicable dispute resolution forum.

## D. Termination

### 1. Right to terminate the contract

**Relevant UPICC provision**

Article 7.3.1 (Right to terminate the contract) of the UPICC

**Commentary**

516. Termination of contracts is an important issue for parties to IICs. Many IIC disputes arise after one or more parties terminate(s) a contract. It is not unusual for a party to ask the tribunal to determine that the termination was unlawful and that the aggrieved party is entitled to damages.

517. The grounds for termination of an IIC may not always be clear, and the contractual procedures governing termination may not always be followed by the parties. For example, there have been instances in which a new government has come to power and terminated existing IICs on policy grounds (*e.g.*, because they were considered contrary to the national interest), without complying with the termination provisions contained in those contracts.

518. Article 7.3.1 of the UPICC (right to terminate the contract) applies both where the non-performing party is liable for the non-performance and where the non-performance is excused. At its core, the provision provides that a party may terminate the contract if the other party's failure to perform amounts to a fundamental non-performance.

519. Article 7.3.1 further identifies factors to be considered in determining whether a non-performance is fundamental. These include whether (a) the non-performance substantially deprives the aggrieved party of what it was entitled to expect under the contract, unless the other party neither foresaw nor could have reasonably foreseen that result; (b) strict compliance with the obligation that has not been performed is of essence under the contract; (c) the non-performance is intentional or reckless; (d) the non-performance gives the aggrieved party reason to believe that it cannot rely on the other party's future performance; and (e) termination would cause the non-performing party a disproportionate loss in light of the preparation or performance already undertaken.

520. In addition, in cases of delay, the aggrieved party may terminate the contract if the other party fails to perform before the expiration of an additional period granted for performance.

521. As IICs are often long-term agreements that serve important public interests, the principles of continuity and preservation of the contractual relationship may warrant greater protection than in ordinary commercial contracts. Accordingly, the termination of an IIC may be subject to more stringent requirements, such as extended notice periods and more elaborate procedural safeguards, than those applicable to ordinary commercial agreements. This does not preclude the State's right to terminate an IIC unilaterally for reasons of public interest (subject to compensation of the investor) where such right is recognised under the applicable domestic law.

522. Parties to an IIC are encouraged to identify and agree upon specific circumstances (events of default) that may give rise to termination. These may include policy-related grounds, termination without cause, or other events that the parties consider particularly relevant to the project and its context. Because such grounds are specifically negotiated, they are generally well suited to the particular characteristics of the investment relationship. For example, the parties may provide for termination in the event of a breach of declarations and assurances (*e.g.*, a representation by the investor that it complies with all applicable laws), as well as in cases of fraud or corruption. Other grounds for termination commonly found in IICs include the failure to maintain required guarantees, insurance coverage, or performance security; the unauthorised transfer or assignment of contractual rights; and changes in ownership or control without prior approval of the investor's identity and capabilities.

523. As discussed in greater detail below, parties to an IIC are also encouraged to regulate the restitution, upon termination, of whatever either party has supplied under the contract, provided that such party concurrently restore whatever it has received. Articles 7.3.6 and 7.3.7 of the UPICC provide useful guidance in this respect, distinguishing between contracts to be performed at one time and long-term contracts.

**Model Clause**

1. The provisions for termination contained in this article are in addition to the rights of termination provided to the Parties elsewhere in the Contract and the applicable law.

**Termination for Investor Default**

1.1 Subject to applicable laws and save as otherwise provided in this Contract, in the event that any of the defaults specified below shall have occurred, and the Investor fails to cure the default within a Cure Period of [*XX days*], the Investor shall be deemed to be in default of this Contract (the "Investor Default"), unless the default has occurred solely as a result of any non-performance of this Contract by the State or due to Force Majeure. The defaults referred to herein shall include:

(a) …

(b) …

(c) …

1.2. Without prejudice to any other rights or remedies that the State may have under this Contract against the Investor upon occurrence of an Investor Default, the State shall be entitled to terminate this Contract by issuing a Termination Letter to the Investor, and the Termination shall be effective from the date of such Termination Letter, provided that before issuing the Termination Letter, the State shall by a Termination Notice inform the Investor of its intention to issue such Termination Letter and grant 15 (fifteen) days to the Investor to make a representation, and may after the expiry of such

15 (fifteen) days, whether or not it is in receipt of such representation, issue the Termination Letter, subject to the provisions of Clause 1.1 above.

**2 Termination for State Default**

2.1. In the event that any of the defaults specified below shall have occurred, and the State fails to cure such default within a Cure Period of [*90 (ninety) days or such period as has been expressly provided in this Contract*], the State shall be deemed to be in default of this Contract (the "State Default") unless the default has occurred as a result of any breach of this Contract by the Investor or due to Force Majeure. The defaults referred to herein shall include

(a) …

(b) …

(c) …

2.2. Without prejudice to any other right or remedy which the Investor may have under this Contract, upon occurrence of a State Default, the Investor shall, subject to the provisions of the Substitution Agreement, be entitled to terminate this Contract by issuing a Termination Letter to the State; provided that before issuing the Termination Letter, the Investor shall by a Termination Notice inform the State of its intention to issue the Termination Letter and grant 30 (thirty) days to the State to make a representation, and may after the expiry of such 30 (thirty) days, whether or not it is in receipt of such representation, issue the Termination Letter.

Commentary to the Model Clause

524. The Model Clause on termination is structured around a dual-default mechanism that distinguishes between Investor Default and State Default. This dual architecture reflects the contractual logic of this Instrument, which recognises that both parties assume obligations under the IIC and that both must have access to effective remedies in the event of the other party's non-performance. The clause is designed to be adapted by the parties to the specific circumstances of their project, and the lists of defaults under clauses 1.1 and 2.1 are intentionally left open for the parties to negotiate and complete.

525. With respect to Investor Default (clause 1), the Model Clause provides that the State party may terminate the contract where the investor has failed to cure a specified default within a defined cure period. The cure period mechanism is essential: it reflects the principle that termination of an IIC should be a last resort, and that the defaulting party should be given a reasonable opportunity to remedy its non-performance before the contract is brought to an end. The clause also excludes from the definition of Investor Default any failure that is solely attributable to a non-performance by the State party or to force majeure, thereby ensuring that the investor is not penalised for circumstances beyond its control or caused by the other party's own conduct.

526. With respect to State Default (clause 2), a parallel structure is adopted, but with certain differences that reflect the distinct position of the State party. Notably, the cure period for State Default is set at 90 days (or such longer period as the contract may provide), which is longer than the cure period typically applicable to Investor Default. This longer period recognises the institutional and procedural constraints that may affect the State's ability to remedy a default promptly, including the need for inter-agency coordination, budgetary approvals, or legislative action. The clause also provides that the investor's right to terminate is subject to the provisions of any Substitution Agreement, reflecting the common practice in project finance transactions of allowing lenders to step in and cure defaults before termination takes effect.

527. Both clauses incorporate a procedural safeguard in the form of a two-step termination process: first, a Termination Notice informing the other party of the intention to terminate; and second, the issuance of a Termination Letter, which takes effect only after the expiry of a further period during which the defaulting party may make representations. This graduated process serves several purposes: it ensures due process, provides a final opportunity for the defaulting party to present its case, and introduces a cooling-off period that may facilitate a negotiated resolution short of termination. The notice periods specified in the clause (15 days for Investor Default and 30 days for State Default) are indicative and may be adjusted by the parties to reflect the complexity of the project and the nature of the obligations involved.

528. The Model Clause should be read in conjunction with the provisions on restitution upon termination (see Section D.3 of this Chapter), which address the consequences of termination for the parties' respective positions, including the return of assets, the settlement of outstanding payment obligations, and the transfer of the project to the State party or to a successor investor. Parties are also encouraged to specify in their IIC the consequences of termination for third parties, including lenders, subcontractors, and local communities that may be affected by the cessation of project operations. The interaction between the termination clause and the dispute resolution provisions of the contract (see Chapter 8) should also be carefully considered: it is advisable that any dispute concerning the validity or consequences of a termination notice be submitted to the dispute resolution mechanism agreed in the IIC, including any interim or provisional measures that may be necessary to preserve the *status quo* pending resolution of the dispute.

**Illustration**

A 30-year concession for a hydroelectric power plant is awarded by State A to Company B under a build-operate-transfer model. The power plant is in full operation and generating electricity when a severe drought hits Country A for over 10 months.

State A blames Company B for the electricity shortage that ensues and decides to terminate the concession agreement before its original term.

The court or arbitral tribunal will assess whether the concession was rightfully terminated or not in light of the specific circumstances set out in the contract for termination plus, if the case may be, the fact that non-performance of the agreement by Company B amounted to a fundamental non-performance.

### 2. Notice of termination

**Relevant UPICC provision**

Article 7.3.2(1) (Notice of termination) of the UPICC

**Commentary**

529. This UPICC provision sets the requirement for notice to terminate a contract. In essence, the right of a party to terminate a contract is exercised by notice to the other party. The provision also states that if performance has been offered late or otherwise does not conform to the contract, the aggrieved party will lose its right to terminate the contract unless it gives notice to the other party within a reasonable time after it has or ought to have become aware of the offer or of the non-conforming performance.

530. In the context of investment contracts, the notice to terminate should be in writing.

531. Parties to an IIC may wish to exclude paragraph (2) of the aforementioned UPICC provision from their agreement, which reads as follows: "If performance has been offered late or otherwise does not conform to the contract the aggrieved party will lose its right to terminate the contract unless it gives notice to the other party within a reasonable time after it has or ought to have become aware of the offer or of the nonconforming performance". This UPICC provision deals with situations arising more frequently in commercial transactions where non-performance equates to goods not arriving or services not being rendered. In the context of IICs, however, non-performance may not always be easy to detect; thus, the circumstances that lead to the loss of the right to terminate must be clearly expressed and regulated in the parties' agreement.

532. For certainty and predictability, the contract may include language on (i) the formal requirement for termination of a contract, *e.g.*, a written notice of termination, and (ii) the circumstances under which a party may lose its right to terminate the IIC.

533. This contract language should be drafted together with the contract language in the previous sub-section D.1 so that it is clear (i) when a party may terminate a contract – including early termination, (ii) what the formal requirements for termination are, and (iii) under which circumstances a party may lose its right to terminate the contract.

### 3. Restitution concerning long-term contracts

**Relevant UPICC provision**

Article 7.3.7 (Restitution with respect to long-term contracts) of the UPICC

**Commentary**

534. This UPICC provision states that, for long-term contracts, restitution in the case of termination is only available for the future, provided that the contract is divisible. In the case of contracts to be performed at one time, Article 7.3.6 of the UPICC applies to investment contracts without any further explanation or adjustment.

535. In the context of long-term IICs, when restitution is to be made, parties are to rely on Article 7.3.6(2) to (4) of the UPICC, which provide that (i) if restitution in kind is not possible or appropriate, an allowance has to be made in money whenever reasonable, (ii) the recipient of the performance does not have to make an allowance in money if the impossibility to make restitution in kind is attributable to the other party, and (iii) compensation may be claimed for expenses reasonably required to preserve or maintain the performance received.

536. The obligations undertaken by the parties in IICs frequently involve long-term investment in infrastructure, natural resource development, and similar projects, rather than a simple exchange of goods or services. Accordingly, it is advisable for the IIC to address expressly the terms and conditions governing restitution in the event of termination.

537. Certain projects, such as those involving oil and gas or mineral exploration, require substantial upfront investments by the investor, which are typically recovered only after many years of operation. If the IIC is terminated after significant investments have been made during the initial stages of the project but before any revenue has been generated, restitution on an *ex nunc* basis may give rise to difficult issues. Accordingly, the parties may wish to regulate expressly the consequences of termination, including by agreeing on mechanisms that allow the recovery of costs incurred prior to termination.

538. Where restitution in value is available, the parties may wish to specify the basis for its calculation. The contract may accordingly provide for restitution (whether in kind or in value) and set out the conditions under which restitution may be awarded, as well as the criteria for its quantification.

## E. Remedies for non-compliance with sustainability obligations, including towards affected third parties

**Principle 26**

**(1) Parties to an IIC shall cooperate with each other and relevant third parties with the purpose of providing early remedy to a party's non-performance of sustainability obligations under the law and their IIC.**

***Notification and direct negotiations***

**(2) If a party fails to comply in any material respect with its sustainability obligations, the other party shall give the former written notice to cease and remedy the failure.**

**(3) Once notice is received from the non-complying party, the parties shall meet without delay to conduct direct negotiations and adopt effective remedies to be implemented collaboratively and based on an agreed timeline. The management plan should provide procedures and timeframes to regulate non-performance of sustainability obligations and failure to implement the remedial measures envisaged in the plan.**

**(4) The direct negotiations could be facilitated by a Joint Sustainability Committee, where established.**

***Dispute resolution mechanism***

**(5) If disagreement persists, the parties may resort to the dispute resolution mechanisms as provided for in the IIC.**

***Remedies***

**(6) In case of non-performance by a party with its sustainability obligations, and the procedures in paragraphs (2) to (4) do not remedy the situation, the other party shall be entitled to exercise the regular contractual remedies in this Instrument and any other remedies mutually agreed by the parties.**

**(7) The remedies in this Instrument, and any other remedies specified by parties in their IIC, shall not limit or preclude the possibility for any third party affected by the non-performance of sustainability obligations to bring direct claims and liability compensation actions against the non-performing party.**

**Commentary**

539. In the context of IICs, parties have a duty to cooperate towards compliance with sustainability obligations arising from either the law or their contractual relationship. When a party fails to comply with its sustainability obligations under the IIC, the principle of cooperation requires that a structured, multi-step process to remedy such failure be adopted, rather than resorting directly to other remedies available under the contract or the law.

540. To that end, parties may draw on the monitoring mechanism provided in Chapter 5, Section D.3 to prevent or manage non-compliance with sustainability obligations and address possible disagreements between them. These may include (i) providing procedures and timeframes to remedy non-compliance through direct consultation in the management plan following the initial sustainability due diligence, and (ii) if established, the Joint Sustainability Committee provided under Chapter 5, Section D.3, could be charged with managing the direct consultations between the parties and the ensuing procedures in accordance with the management plan. Disagreements between the parties, especially if a Joint Sustainability Committee is not established, may be brought before one-stop-shops or ombudspersons for foreign investments established by the State.

541. The ample spectrum of regular contractual remedies (see the rest of this Chapter) should also be available in the event of non-performance of sustainability obligations. This includes, for instance, the right to seek specific performance (including the right to request the applicability of a penalty until the failure is remedied) and the right to withhold performance. The parties may also agree to hire a third party, at the cost of the defaulting party, to remedy the breach or include more project-specific regulatory remedies in their contract, such as step-in rights for the State, withdrawal of permits, or loss of entitlement to agreed incentives for the investor.

542. A hierarchy of steps is essential considering the specificity of non-compliance with sustainability obligations and the primary interest in early cure of failures to comply. Considering the severity of the remedies, it is envisaged that they will apply only (i) in the event of a material breach and (ii) if the defaulting party fails to remedy its breach within a reasonable cure period. Only as a final resort, and where non-compliance with sustainability obligations amounts to a fundamental non-performance of the IIC, should termination of the contract and damages be considered.

543. Remedies available in the event of non-performance of sustainability obligations are not meant to be in lieu of remedies available under the applicable law. In other words, an exclusive remedy concept whereby a party would be limited by the remedies expressly specified in the IIC is not envisaged.

544. It is expected that the choice of remedy and the extent to which several remedies may be applied cumulatively will, at all times, be subject to other guiding principles of the IIC, such as fairness, good faith and cooperation, or the duty to avoid abuse of rights.

545. It may very well be the case that, if a party is in breach of its sustainability obligations, this may cause harm to third parties. It is therefore important to make the parties aware that, regardless of the remedies specified in the IIC, the non-performing party may be exposed to legal actions brought by third parties.

**Model Clause**

1. If a Party fails to comply in any material respect with its sustainability obligations under this Contract or the applicable law, the other Party shall give the non-complying Party written notice specifying the nature of the failure and requesting that it cease and remedy the failure within [*60/90*] days from receipt of such notice (the "Cure Period").

2. If the failure is not remedied within the Cure Period, or if the Parties disagree as to whether a failure has occurred or has been adequately remedied, either Party may refer the matter to [*the Joint Sustainability Committee, if established/direct negotiations between senior representatives of the Parties/one-stop-shop/ombudsperson, where applicable*]. The Parties shall negotiate in good faith for a period of [*30/60*] days with the objective of agreeing on corrective measures.

3. If the Parties fail to resolve the matter through direct negotiations within the period specified above, either Party may refer the dispute to [*expert proceedings/mediation/a dispute board*] in accordance with [*cross-reference to Chapter 8, Section C*]. The costs of such proceedings shall be shared equally unless the third-party neutral determines otherwise.

4. The remedies available to a Party in the event of a material and continuing failure to comply with sustainability obligations include, in the following order of preference: (a) specific performance of the sustainability obligation, including the imposition of agreed payment for non-performance until the failure is remedied; (b) the right to engage a qualified third party to carry out the required measures at the cost of the non-complying Party; (c) step-in rights allowing the aggrieved Party to take over performance of the relevant obligation; and (d) only as a last resort and where the non-compliance amounts to a fundamental non-performance of this Contract, termination in accordance with [*cross-reference to termination clause pursuant to Chapter 7, Section D*].

5. Nothing in this Clause shall limit or preclude the right of any third party affected by the non-performance of sustainability obligations to bring direct claims and liability compensation actions against the non-performing Party under the applicable law.

Commentary to the Model Clause

546. This Model Clause operationalises the structured, multi-step remedial process described in the commentary to Principle 26. It translates the principle of cooperation and graduated remedies into contractual language that the parties may adopt or adapt. Paragraph 1 establishes the first step: upon a material failure to comply with sustainability obligations, the aggrieved party must give written notice specifying the nature of the failure and granting a cure period of 60 or 90 days. This cure period mechanism reflects the principle that early cure of sustainability failures is in the interest of both contracting parties and of affected third parties. Paragraph 2 provides for a second step: if the failure is not remedied within the cure period, the matter may be referred to direct negotiations — either through the Joint Sustainability Committee (if established under Chapter 5, Section D.3) or between senior representatives, or bringing the case before a one-stop-shop or ombudsperson, where established. This collaborative step reflects the Instrument's preference for dialogue over adversarial proceedings. Paragraph 3 introduces a third step: referral to an amicable, third-party mechanism such as expert proceedings, mediation, or a dispute board (see Chapter 8, Section C.2). Paragraph 4 sets out the hierarchy of remedies available in the event of material and continuing non-compliance: specific performance (including agreed payment for non-performance), third-party engagement at the defaulting Party's cost, step-in rights, and — only as a last resort where non-compliance amounts to fundamental non-performance — termination. This graduated hierarchy ensures that the contractual relationship and the investment project are preserved to the greatest extent possible. Paragraph 5 preserves the rights of affected third parties to bring direct claims under the applicable law, recognising that sustainability breaches may cause harm beyond the contractual relationship.

## F. Compensation and damages

### 1. Full compensation

**Relevant UPICC provision**

Article 7.4.2 (Full compensation) of the UPICC

**Commentary**

547. It is important to clarify at the outset that compensation and damages under this Instrument are contractual in nature and grounded in the UPICC. Unlike treaty-based investment arbitration, where compensation standards are drawn from public international law, the present Instrument provides a framework rooted in contractual principles of non-performance. The parties' rights to compensation arise from the contract and are governed by the contractual remedies set out in this Chapter, as supplemented by the UPICC. This distinction is fundamental: practitioners and adjudicators should not automatically import public international law standards — and the associated debate on damages and full compensation in the investment-treaty context — into contract law. The discussion of valuation methodologies in the commentary below is intended as illustrative guidance that parties may choose to adopt in their contract, not as a default standard imposed by this Instrument.

548. Parties to an IIC are encouraged to specifically make provisions concerning compensation (*e.g.,* in the event of expropriation) and damages (*e.g.*, in case of non-performance) in their contracts. In line with the principle of full compensation set out in Article 7.4.2 of the UPICC, the essence is to restore the aggrieved party as closely as monetarily possible to the position in which it would have been had the wrong or expropriatory act not been done.

549. The UPICC contain a normative framework that aims at achieving proportionality in calculating damages and ensuring that they do not assume a punitive character. While the aggrieved party is entitled to full compensation, which includes loss suffered by the aggrieved party and loss of profits (sometimes called consequential loss), full compensation is subsequently qualified by other UPICC provisions, such as those requiring (i) certainty of harm, (ii) foreseeability of harm, (iii) reduction of damages when harm is due in part to the aggrieved party, and (iv) mitigation of harm. Damages should not enrich the aggrieved party and should have regard to any changes in the harm, including its expression in monetary terms, which may occur between the time of non-performance and that of the judgment or award.

550. Article 7.4.2 of the UPICC on full compensation also allows compensation for non-pecuniary harm, such as physical suffering or emotional distress (sometimes referred to as moral damages). Such compensation may take the form of monetary damages, although a court or arbitral tribunal may also grant other forms of redress (*e.g.,* the publication of a notice). Although the availability and scope of moral damages remain debated in some jurisdictions, parties in international arbitration may often agree to apply the UPICC provision on non-pecuniary harm, subject to applicable public policy limitations at the seat or place of enforcement. The requirement that the harm be established with reasonable certainty, as well as the other conditions for entitlement to damages, must also be satisfied in cases of non-pecuniary harm.

551. In practice, full compensation is the standard of compensation observed in disputes arising out of IICs. However, while the compensation for loss suffered is uncontroversial, the award of loss of profits is riddled with controversy. The concerns here are that claims for loss of profits may be speculative, excessive, lead to double recovery, and so forth.

552. Parties to IICs can and should clearly allocate risks and demarcate the amount of damages that may be claimed in the event of non-performance or expropriation. Recognising that such damages, though real, may be difficult or even impossible to prove, parties are encouraged to agree on one or more liquidated damages clauses – referred to as "agreed payment for non-performance" under Article 7.4.13 of the UPICC. By virtue of this type of clause, the parties agree on a fixed sum or a set formula to calculate the amount of money a party will owe the other if it breaches the IIC or commits an expropriatory act, so that the aggrieved party is compensated for its losses (see subsection 4 below for additional guidance).

553. In addition, the parties to an IIC may wish to consider several aspects relating to the calculation of damages in the absence of a liquidated damages clause, such as the applicable valuation methodology and the approach to punitive damages.

554. In the event of expropriation, compensation in investment arbitration will generally be deemed "adequate" or "appropriate" when it is based on the "fair market value" of the expropriated assets, determined as of the date immediately preceding the moment when the expropriation became known to the public, together with interest accruing until payment. This valuation date is intended to prevent the pending expropriation from significantly reducing the market value of the investment.[42] However, significant divergences remain regarding the appropriate method for determining fair market value. Arbitral practice has developed methodologies for that purpose. One of the most frequently used is the "discount cash flow" (DCF) method, which seeks to determine the price that a hypothetical willing buyer would pay for the investment. The DCF method projects the future cash flows that the investment is expected to generate and discounts them to present value by taking into account the time value of money and relevant risk factors, including macroeconomic conditions and political risks. It is therefore a forward-looking methodology. Other valuation methods include the "market comparables method", where reliable comparable transactions or companies exist, and the "stock market-based valuation method", which relies on the share price of the investing company where it is publicly traded. These methodologies have generally been applied by arbitral tribunals where the expropriated investment constitutes an established going concern with a proven record of profitability. By contrast, where the investment is in its early stages, has not yet generated revenue, or is unlikely to generate future income, tribunals have often considered it appropriate to apply alternative valuation methods. These include valuation based on "liquidation value" (*i.e.,* the amount that could be realised through the sale of the remaining in a liquidation scenario), "asset-based valuation methods" (including net asset value, replacement value, and book value), and the assessment of "sunk costs" or "invested capital", which seeks to reimburse actual investment expenditures. These approaches are commonly described as backward-looking valuation methodologies.

555. This Instrument, and the UPICC incorporated therein, provide a principled framework that may assist adjudicators in determining fair and proportionate compensation for expropriatory acts, as well as assessing damages. Relevant guidance may be found, *inter alia,* in the UPICC provisions on certainty of harm (Article 7.4.3), causation and foreseeability (Article 7.4.4), contributory fault (Article 7.4.7), and mitigation of harm (Article 7.4.8).

556. Given the significant differences among industries and investment projects, it would generally be inappropriate to prescribe uniform rules on the methodology for compensating expropriatory acts or calculating damages in IICs. An industry-specific approach to the assessment of compensation or damages is therefore preferable to the adoption of a single, generally applicable methodology. To promote certainty and predictability, parties are encouraged to address expressly in their IICs the methodology for calculating compensation for expropriatory acts, including, where appropriate, a preferred valuation methodology or establishing a hierarchy of methods suited to the particular investment. In doing so, the parties may take

[42] See also World Bank Guidelines on the Treatment of Foreign Direct Investment, Guideline IV(3).

into account factors such as the timing of the expropriation and the stage of development of the investment at which it occurs, issues of causation, probabilistic valuation, and adjustments reflecting relevant public-interest considerations.

**Model Clauses**

**Option 1**

1. The Parties agree that any monetary damages payable under this Contract shall:

(a) not exceed the harm suffered by the aggrieved Party, as valued on the date of the breach;

(b) in the case of expropriation, be an amount equivalent to the fair market value of the expropriated investment immediately prior to the expropriation date. Fair market value may be determined using appropriate valuation methods, including going concern value, asset-based valuation (including declared tax value of tangible property), and other criteria reasonably appropriate in the circumstances. The expropriation damages award shall not reflect any change in value occurring because the intended expropriation had become known earlier. The amount awarded shall include interest at a commercially reasonable rate applicable to the relevant currency from the date of expropriation until the date of payment;

(c) relate only to harm caused by the non-performance and resulting therefrom;

(d) be established with a reasonable degree of certainty and shall not include harm that is speculative or hypothetical; and

(e) be freely transferable.

2. In determining any monetary damages under this Contract, the arbitral tribunal shall consider only the submissions of the disputing Parties, and, as applicable:

(a) any contribution to the harm by the aggrieved Party, whether intentional or negligent;

(b) any failure by the aggrieved Party to mitigate the harm;

(c) any prior compensation or damages already received for the same loss; and/or

(d) restitution of property, or the repeal or modification of the measure giving rise to the non-performance.

3. The Parties agree that, in cases other than expropriation, the arbitral tribunal may award monetary damages for loss of future profits only to the extent that such damages meet the requirements under paragraph 1. Any such determination shall be made on a case-by-case basis and shall take into consideration, *inter alia*, whether the investment has been operated for a sufficient period of time to establish a performance record of profitability.

4. The arbitral tribunal may award pre-award and post-award interest at a commercially reasonable rate, compounded annually.

5. The arbitral tribunal shall not award punitive damages.

**Option 2**

1. Where non-performance of this Contract has caused economic damages to the Investor and such damages are to be compensated, the compensation shall follow the principle of full compensation. In all cases, the damages must be proven, effective, and a consequence of the non-performance.

2. Compensation shall be equivalent to the reduction in the fair market value of the Investment resulting from the non-performance of this Contract. Fair market value shall be determined using various valuation methods, including, to the extent possible: (i) information on recent market transactions involving comparable assets; and (ii) business and/or management representations relating to the value of the Investment. The valuation date shall be the date immediately prior to the occurrence of the breach. The fair market value shall be calculated in a freely convertible currency, at the prevailing market exchange rate for that currency applicable at the valuation date.

3. In no event shall damages include punitive, exemplary, or penal damages, nor shall a party recover damages for speculative or insufficiently proven loss of profit. Any compensation shall be reduced to the extent that the harm resulted from the aggrieved party's own act or omission, including any failure to take reasonable steps to mitigate the harm.

4. Compensation shall include simple interest accruing from the valuation date until the payment date. The interest rate shall correspond to the rate of sovereign debt of the host State, at the corresponding term.

5. Compensation shall be paid promptly, be effectively realisable, and be freely transferable, to the account designated by the Investor. Payment may be made in any freely convertible currency accepted by the Investor. In no case shall taxes imposed by countries other than the host State be included in the compensation.

6. The calculation of the compensation shall take into account any compensation already paid by the other Contracting Party for the same cause.

Commentary to the Model Clauses

557. The Model Clauses on full compensation offer two alternative approaches. Option 1 is designed as a comprehensive, self-contained damages clause that addresses both general breach and expropriation. Paragraph 1 establishes the overarching principle that damages shall not exceed the harm suffered, and provides specific guidance on the calculation of compensation in the case of expropriation, including the use of fair market value methodologies (going concern value, asset-based valuation, and other appropriate criteria). It further requires that damages relate to harm caused by the non-performance, be established with a reasonable degree of certainty, and be freely transferable. Paragraph 2 directs the arbitral tribunal to consider contributory fault, failure to mitigate, prior compensation, and restitution. Paragraph 3 addresses the particularly contentious issue of loss of future profits, limiting their award to cases meeting the requirements of paragraph 1 and requiring a case-by-case assessment. Paragraph 4 allows for the award of interest at a commercially reasonable rate. Paragraph 5 prohibits punitive damages, in line with the UPICC's rejection of punitive remedies.

558. Option 2 adopts a different approach, framed around the principle of full compensation in Article 7.4.2 of the UPICC. It focuses on the reduction in fair market value of the investment as the primary measure of compensation and provides for the use of multiple valuation methods, including recent market transactions and business representations. Option 2 also expressly excludes punitive or exemplary damages, lost profits that are speculative, and harm attributable to the aggrieved party's own conduct or failure to mitigate.

559. Both Options are intended as contractual frameworks that parties may adapt to their specific circumstances; they are not default standards imposed by this Instrument. As stated in the commentary above, the discussion of valuation methodologies is illustrative guidance that parties may choose to adopt, and practitioners should not import public international law standards on compensation into contract law.

The parties should select the Option that best fits the nature and stage of their investment project, taking into account the applicable industry sector, the degree of risk borne by each party, and the enforceability of damages awards in the relevant jurisdictions.

### 2. Interest for failure to pay money

**Relevant UPICC provision**

Article 7.4.9 (Interest for failure to pay money) of the UPICC

**Commentary**

560. Interest is an element of full compensation. It is an important topic for IICs, not only because it is frequently overlooked by parties, but also because it can have huge implications for the amount of a damages claim. For example, the rate of interest awarded and whether simple or compound interest is awarded, and the period for which interest is awarded, may lead to a claim for interest being almost the same amount as, or even more than, the damages award.

561. As other topics in the context of investment contracts, the award of interest should be a tool to promote foreign direct investment and offer sufficient protection to investors. Different alternatives for interest regulation may be available to parties, depending on the approach they deem appropriate to their specific project. One should note that the domestic law of the host State, including its mandatory provisions, is often chosen as the governing law of the IIC, and tends to play a central role in contract-based investment disputes, different from treaty-based disputes. This means that specific domestic rules on interest may apply (*e.g.*, some jurisdictions provide restrictions on compound interest or rules preventing interest from exceeding the principal). If the law of the host State is not chosen as the law applicable to the IIC, domestic interest rules may still apply if they are mandatory rules that are applicable in accordance with the relevant rules of private international law (Article 1.4 of the UPICC).

562. Parties to an IIC are therefore encouraged to agree on clear contractual provisions on interest.

**Model Clauses**

**Option 1**

**Interest in the case of expropriation**:

Compensation due to the Investor in the case of expropriation shall include interest at a commercially reasonable rate for the freely convertible currency in which compensation is determined, from the date of the expropriation until the date of payment.

**Interest in the case of restitution of property and/or monetary damages**:

If a tribunal makes a final award against the respondent Party, in respect of its finding of liability, the tribunal may award, separately or in combination, only:

(a) monetary damages and any applicable interest; and

(b) restitution of property, in which case the award shall provide that the respondent Party may pay monetary damages and any applicable interest in lieu of restitution.

**Final award:**

The tribunal may award pre-award and post-award interest at a reasonable rate of return compounded annually.

**Option 2**

The compensation will include simple interest from the valuation date to the payment date. The interest rate will correspond to the rate of the sovereign debt of the country receiving the Investment, at the corresponding term.

### 3. Currency in which to assess damages

**Relevant UPICC provision**

Article 7.4.12 (Currency in which to assess damages) of the UPICC

**Commentary**

563. This UPICC provision stipulates that damages are to be assessed in the currency of the obligation or the currency in which the harm was suffered, whichever is more appropriate in the circumstances. Article 7.4.12 of the UPIC does not address the currency in which damages are to be paid; this is covered by Article 6.1.9 of the UPICC.

564. In the context of IICs, damages may be assessed either a freely convertible currency or in another currency, typically the host State's currency. Where the host State currency is non-convertible or subject to high (and increasing) inflation, parties commonly denominate obligations in freely convertible currency to mitigate exchange-rate and convertibility risks, even though local disbursements may occur in local currency. Article 7.4.12 of the UPICC leaves it to the aggrieved party to choose in which currency damages should be assessed, provided that the principle of full compensation is respected. However, parties are encouraged to stipulate in their IIC in which currency damages should be assessed and paid (see also the Model Clauses on full compensation and interest in case of expropriation in Sections F.1 and F.2 above).

**Option 1**

Any damages awarded under this Contract shall be assessed in a freely convertible currency. Unless otherwise demonstrated by the aggrieved Party to be more appropriate in the circumstances, such currency shall be [*insert currency*].

**Option 2**

Any damages awarded under this Contract may be assessed in the currency in which the harm was suffered, including the currency of the host State. However, where such currency is not freely convertible, damages shall be converted into [*insert currency*] at the prevailing market exchange rate on the date determined by the tribunal as appropriate to achieve full compensation pursuant to the UPICC.

### 4. Agreed payment for non-performance

**Relevant UPICC provision**

Article 7.4.13 (Agreed payment for non-performance) of the UPICC

**Commentary**

565. In certain contracts, it may be difficult, costly, or even impossible to prove the actual loss resulting from a non-performance. For example, in a road or bridge project, quantifying the loss suffered by the State or public entity as a result of delay may be particularly difficult. Likewise, where a delay in the supply of machinery prevents a factory from commencing production, the resulting loss may be difficult to ascertain with precision. In such cases, the parties may agree in advance on a specified sum payable upon non-performance as a reasonable estimate of the loss likely to result from breach.

566. Article 7.4.13 of the UPICC covers agreements to pay a specified sum in the case of non-performance. It is intentionally broad.

567. Unless the parties expressly provide otherwise, a valid, agreed-upon payment clause stipulating a specified amount of liquidated damages payable upon non-performance of the IIC will generally evidence the parties' intention that no additional claim for general damages may be made in respect of the same breach.

568. Such clauses are not only sector-specific but also contract-specific. They should reflect both the practical realities of project implementation – including third-party dependencies, funding delays, evolving administrative approvals, and site- or terrain-specific challenges – and the allocation of risks agreed upon by the parties in the particular project. As part of their overall risk allocation strategy, the parties to an IIC may also wish to include a limitation of liability clause in their agreement.

569. In the context of IICs, agreements to pay a specified sum in the case of non-performance are commonly found in construction contracts, where they often operate alongside delay damages provisions. They may also be found in concession agreements and other infrastructure projects involving the provision of public services.

570. In some jurisdictions, a contractual clause providing for an agreed payment upon non-performance may be subject to judicial or arbitral review where the stipulated amount is disproportionate to the harm resulting from the non-performance. Likewise, under the UPICC, an agreed payment for non-performance may be reduced to a reasonable amount if it is grossly excessive in relation to the harm resulting from the non-performance and to the other relevant circumstances, including the nature of the contract.

571. Liquidated damages clauses may be particularly appropriate in sectors where delay is likely to cause substantial harm that is difficult to quantify with precision. A typical example is an IIC involving the construction of infrastructure – such as roads, dams, airports, ports, railway, or metro systems – where the parties may agree in advance on the amount payable in the event of delay.

**Model Clause**

**Liquidated Damages for Delay**

If the Investor fails to achieve Completion by the Scheduled Completion Date, as such date may be extended in accordance with this Contract, for reasons other than (a) an act or omission of the State Party or (b) an event of force majeure, the Investor shall pay delay liquidated damages to the State Party at the rate of [*insert amount or % of the Contract Price*] per day for each day of delay from the Scheduled Completion Date until the earlier of:

(i) the date on which Completion is achieved; or

(ii) the date of termination of this Contract in accordance with its terms.

The aggregate liability of the Investor for delay liquidated damages under this Clause shall not exceed [*insert cap amount or % of the Contract Price*].

The Parties acknowledge and agree that:

(a) the actual loss likely to be suffered by the State Party in the event of delay would be difficult to determine precisely at the time of contracting;

(b) the liquidated damages provided for in this Clause represent a genuine pre-estimate of the loss likely to be suffered by the State Party as a result of such delay; and

(c) the amounts payable under this Clause are intended to constitute an agreed payment for non-performance within the meaning of Article 7.4.13 of the UPICC.

Payment of delay liquidated damages shall be the sole and exclusive monetary remedy of the State Party for the Investor's failure to achieve Completion by the Scheduled Completion Date, except in cases of fraud, wilful misconduct, or gross negligence by the Investor.

For the avoidance of doubt, nothing in this Clause shall:

(a) relieve the Investor from its obligation to complete the Project, unless this Contract has been terminated in accordance with its terms;

(b) prejudice the State Party's right to terminate this Contract in accordance with its terms; or

(c) limit remedies available in respect of breaches other than delay in achieving Completion.

The State Party may deduct or set off any liquidated damages due under this Clause against amounts otherwise payable to the Investor under this Contract, subject to applicable law.

**Liquidated damages for failure to meet performance standards**

If a Party fails to meet any performance standard expressly identified in this Contract as giving rise to liquidated damages, and such failure is not caused by (a) an act or omission of the other Party; or (b) an event of force majeure, the non-complying Party shall pay liquidated damages of [*insert amount or %*] for each occurrence of non-compliance.

The aggregate liability of a Party for liquidated damages under this Clause shall not exceed [*insert cap amount or % of the Contract Price*].

The Parties acknowledge and agree that:

(a) the actual loss likely to arise from failure to meet the relevant performance standards would be difficult to determine precisely at the time of contracting;

(b) the liquidated damages provided for in this Clause represent a genuine pre-estimate of the loss likely to be suffered as a result of such non-compliance; and

(c) the amounts payable under this Clause are intended to constitute an agreed payment for non-performance within the meaning of Article 7.4.13 of the UPICC.

The liquidated damages payable under this Clause shall be the sole and exclusive monetary remedy for the specific failure to meet the applicable performance standard, except in cases of fraud, wilful misconduct, or gross negligence.

* * *

**Liquidated damages for non-compliance with regulatory requirements**

If a Party fails to comply with any applicable regulatory requirements specified in this Contract, liquidated damages of [*amount*] per violation will be assessed, with a total maximum liability of [*amount*] per year during the term of the Contract. The Parties agree that this amount reflects a reasonable estimate of the loss caused by such failure.

This Clause does not apply to failure of the Investor to comply with regulatory measures adopted by the State after the coming into force of this Contract as referred to in [*cross-refer to stabilisation and renegotiation clause*].

* * *

**Liquidated damages for failure to meet quality standards**

If a Party fails to meet the quality standards specified in this Contract, liquidated damages of [amount] will be paid for each instance of non-compliance, with a total maximum liability of [*amount*] per year during the term of the Contract. The Parties agree that this amount reflects a reasonable estimate of the loss caused by such failure.

* * *

**Liquidated damages in case an IIC is declared void for mistake, fraud or gross disparity**

If this Contract is declared void for mistake, fraud, threat, or gross disparity, the Party who knew or ought to have known of the ground for avoidance shall pay liquidated damages to the other Party in the amount of [*amount*].

### G. Limitation and exclusion of liability

**Relevant UPICC provision**

Article 7.1.6 (Exemption clauses) of the UPICC

**Commentary**

572. Limitation and exclusion of liability clauses, also referred to as "exemption clauses", are contract terms that exclude or limit a party's liability in the event of non-performance or defective performance. In the terminology of the UPICC, exemption clauses encompass both limitation-of-liability and exclusion-of-liability clauses. Such clauses derogate from the legal regime otherwise applicable to breach of contract and constitute an important mechanism for the contractual allocation of risk.

573. Because the most common remedy for non-performance is an award of damages, limitation and exclusion clauses usually concern the parties' liability for monetary compensation. Parties to complex commercial and investment contracts often seek to avoid exposure to indeterminate or disproportionate economic loss and therefore regulate liability *ex ante* during contract negotiations. Such clauses enhance predictability, facilitate the pricing and allocation of risk, and may reduce the legal uncertainty associated with divergent domestic legal regimes. In this sense, limitation and exclusion clauses operate as a cost-efficient mechanism for mitigating contractual risk, including in IICs.

574. Limitation-of-liability clauses may take a variety of forms. The parties may stipulate that liability is to be limited to a fixed amount, a ceiling or a cap, a percentage of the contract value, or the retention of a deposit. They may also limit liability to particular categories of loss (*e.g.*, direct damages only), or to particular forms of misconduct (*e.g.*, ordinary negligence, as opposed to gross negligence or intentional misconduct). In addition, the parties may exclude liability for damages altogether through an exemption clause.

575. A clause providing that a party who fails to perform must pay a specified sum to the aggrieved party in the event of non-performance (an "agreed payment", "agreed sum" or "liquidated damages" clause, see Section F.4 above) may likewise have the effect of limiting liability where the agreed amount is lower than the damages that would otherwise be recoverable. Unlike agreed-payment clauses, however, exemption clauses are not primarily intended to induce performance. Rather, they are stipulated principally for the benefit of the obligor and serve to allocate, limit, or contain contractual risk.

576. In accordance with the principle of freedom of contract, limitation and exclusion clauses are generally valid and enforceable, including in the context of international investment projects. Their validity, interpretation, and enforceability are nevertheless subject to mandatory rules of law (including public policy) and constrained by the overarching principles of good faith and fair dealing, as well as reasonableness. In many jurisdictions, certain categories of liability – such as liability arising from fraud, wilful misconduct, gross negligence, or personal injury – cannot be excluded or limited by agreement.

577. Article 7.1.6 of the UPICC is addressed to adjudicators, whether judges or arbitrators. It gives effect to the principle of fairness by providing that an exemption clause may not be relied upon if it would be grossly unfair to do so. In such circumstances, the clause is denied effect notwithstanding the parties' agreement that the non-performing party should be exempt from liability or that its liability should be limited to a specified amount. The adjudicator's role is limited to determining whether the clause may be invoked; Article 7.1.6 does not confer any power to revise or modify its terms.

578. Consistent with the principle of freedom of contract, exemption clauses are, in principle, valid and enforceable even in the context of international investment projects. However, as reflected in Article 7.1.6 of the UPICC, such clauses should not be relied upon where doing so would be grossly unfair, having regard to the purpose of the contract and, in particular, to what the aggrieved party could legitimately have expected from its performance.

579. In the context of IICs, limitation and exclusion clauses should be interpreted in light of the contract as a whole and the need to ensure a fair allocation of risk between the parties. Such clauses should reflect a negotiated balance of rights and obligations, and risk appropriate to the particular investment project.

580. Certain exemption clauses may be regarded as incompatible with the nature or purpose of particular contractual obligations. This may be the case, for example, where an exemption clause purports to exclude liability for the non-performance of sustainability obligations that are fundamental to the investment project. Given the increasing importance of sustainability commitments in international investment projects, an adjudicator may conclude that exempting a party from liability for the breach of such obligations would be incompatible with the purpose of the contract or grossly unfair in the circumstances. This may apply, depending on the terms of the IIC, to obligations relating to clean energy investments, climate-related innovation, responsible supply chain conduct, carbon-pricing mechanisms, or sustainability reporting requirements.

581. Under certain circumstances, a clause exempting the State from liability for losses caused to the investor under an exploration or extraction investment contract may be considered grossly unfair. This may be particularly so where the investor assumes substantial exploration risk, including the possibility that no commercially exploitable natural resources will be discovered. Factors that may support a finding of gross unfairness include significant information asymmetry between the parties, a manifestly one-sided allocation of risk, or the absence of meaningful negotiation regarding the exemption clause.

**Model Clauses**

**Exclusion of Liability**

Neither Party shall be liable to the other Party for any indirect, incidental, or consequential loss or damage which may be suffered by the other Party in connection with the Contract, including loss of profits, nor for punitive, exemplary, or penal damages *[,except as otherwise expressly provided in this Contract or other than under [include relevant clauses, e.g., on delay damages and payment after termination:*

*(a) […];*

*(b) […];*

*(c) […].]*

* * *

**Limitation of Liability:**

Subject to Clause [*cross-refer to clause "No exemption from liability"*], the liability of either Party for any claims, damages, or losses arising out of or relating to this Contract, whether based on contract, tort, strict liability, or otherwise, shall not exceed [*insert amount / % of the Contract Price / the total amount of the Contract Price*].

The Parties agree that this limitation of liability constitutes an essential element of the agreed allocation of contractual risk and has been taken into account in determining the economic terms of this Contract.

* * *

**Liability of Government of XYZ**

It is expressly understood and agreed between [*the Investor*] and [*SOE*] that [*SOE*] is entering into this Contract solely on its own behalf and not on behalf of any other person or entity. In particular, it is expressly understood and agreed that the [*Government*] is not a party to this Contract and has no liabilities, obligations or rights hereunder. It is expressly understood and agreed that [*SOE*] is an independent legal entity with power and authority to enter into contracts solely on its own behalf under the applicable laws of [*State*] and general principles of contract law. The Investor expressly agrees, acknowledges and understands that [*SOE*] is not an agent, representative or delegate of the [*Government*]. It is further understood and agreed that the [*Government*] is not and shall not be liable for any acts, omissions, commissions, breaches or other wrongs arising out of the Contract. Accordingly, the Investor hereby expressly waives, releases and foregoes any and all actions or claims, including cross claims, impleader claims or counter claims against the [*Government*] arising out of this Contract and covenants not to sue the [*Government*] as to any manner, claim, cause of action or thing whatsoever arising of or under this Contract.

* * *

**No exemption from liability**

Nothing in this Contract excludes or limits liability for either Party's fraud, wilful misconduct or gross negligence.[43]

Nothing in this Contract excludes or limits liability for either Party's non-performance of its sustainability obligations under this Contract.

[43] See the ICC Model Turnkey Contract for Major Projects.

Commentary to the Model Clauses

582. The Model Clauses on exemption from liability establish two non-derogable minimum standards. The first clause provides that neither Party may exclude or limit its liability for fraud, wilful misconduct, or gross negligence. This reflects a widely accepted principle in both domestic and international contract law: parties should not be permitted to shield themselves from the consequences of their most serious forms of misconduct, as such a result would be contrary to the fundamental requirements of good faith and fair dealing (see Article 1.7 of the UPICC and Principle 15 of this Instrument). The second clause extends this protection to sustainability obligations by providing that neither Party may exclude or limit its liability for non-performance of sustainability commitments undertaken under the contract. This provision reflects the policy choice embodied in this Instrument that sustainability obligations occupy a central role in contemporary international investment relationships and should therefore not be deprived of practical effect through exemption or limitation-of-liability clauses (see paragraph 580 above). The two clauses operate cumulatively and are intended to establish minimum standards of accountability that the parties may not contractually derogate from. They should be read together with the remedies for non-compliance with sustainability obligations set out in Section E of this Chapter.

## H. No double recovery

**Principle 27**

**None of the parties shall recover compensation more than once for an injury suffered due to non-performance of the IIC.**

**Commentary**

583. In addition to the dispute resolution mechanism provided for in the IIC, the parties may have access to other fora, such as national courts or tribunals constituted under investment treaties. Such parallel proceedings – which should generally be avoided in the context of IICs (see Principle 32) – may be based on different causes of action, since they arise under distinct legal instruments and may involve allegations of non-performance of contractual, national, or international obligations. Nevertheless, neither party should recover compensation more than once for the same injury arising out of breaches of the IIC. The pursuit of multiple proceedings does not entitle a party to multiple recoveries for the same loss. Any compensation awarded in one forum should therefore be taken into account in subsequent proceedings to avoid double recovery. Obtaining compensation for an injury that has already been fully compensated would result in unjust enrichment and is therefore generally precluded in most legal systems.

**Model Clause**

1. Neither Party shall recover compensation more than once for the same injury arising out of or in connection with this Contract, regardless of whether such compensation is sought through contractual, judicial, treaty-based, or any other proceedings.

2. If a Party has obtained compensation for an injury through proceedings other than those provided for in this Contract, the amount so obtained shall be deducted from any compensation that may be awarded under this Contract for the same injury. The [*insert applicable dispute resolution forum*] shall take into account all forms of reparation already received, including amounts paid under insurance policies, settlement agreements, or awards rendered by other fora.

3. Each Party shall promptly disclose to the other Party and to any dispute resolution mechanism applicable under this Contract the existence and outcome of any proceedings (whether pending or concluded) in which it has sought or obtained compensation for the same or substantially similar injury. Failure to make such disclosure shall constitute a breach of the duty of good faith [*under Principle 15*].

Commentary to the Model Clause

584. This Model Clause operationalises the principle of no double recovery set out in Principle 27 by translating it into enforceable contractual language. Paragraph 1 establishes the overarching prohibition: neither party shall recover compensation more than once for the same injury, regardless of the forum in which compensation is sought — whether contractual, judicial, treaty-based, or otherwise. This reflects the general principle, recognised in most legal systems, that double recovery constitutes unjust enrichment. Paragraph 2 provides a practical deduction mechanism: if a party has already obtained compensation through other proceedings, the amount so obtained shall be deducted from any award under the contract. This ensures that the court or arbitral tribunal takes a holistic view of all forms of reparation already received, including insurance payments, settlement amounts, or awards from other fora. Paragraph 3 imposes a disclosure obligation, requiring each party to inform the other and any tribunal of the existence and outcome of any parallel or concluded proceedings in which compensation for the same or substantially similar injury has been sought or obtained. Failure to disclose constitutes a non-performance of the duty of good faith under Principle 15. This transparency requirement is essential to the effective operation of the no-double-recovery principle, as it provides the tribunal with the information necessary to avoid duplicative awards and to apply the deduction mechanism in paragraph 2.

# CHAPTER 8. CHOICE OF LAW AND DISPUTE SETTLEMENT

## A. Introduction

585. This Chapter is divided into two main sections. Section B deals with the choice of the law applicable to an IIC, while Section C concerns the means for the settlement of disputes arising out of an IIC.

586. As regards Section B, Principle 28 reaffirms the central role of party autonomy in the choice of the law applicable to an IIC. The Commentary clarifies, however, that party autonomy is not without limits and identifies the areas in which the parties may face restrictions, with particular regard to the choice of non-State rules of law, such as this Instrument. Where such restrictions exist, it also provides guidance on how parties may nevertheless give effect to the choice of non-State rules, for example by submitting the contract to arbitration or by incorporating non-State rules as contractual terms. The Commentary encourages parties to choose the applicable law to their IIC in advance, in order to ensure certainty as to their respective legal positions. To this end, two model clauses are offered for applying this instrument to an IIC, as primary governing law or to interpret and supplement a chosen domestic law (typically that of the host State). These model clauses have been inspired by the Model Clauses for the Use of the UPICC.[44]

587. In Section C, for the same reason of certainty and clarity, the parties are encouraged to agree in advance on the process to be followed in case a dispute arises. Recognising that IICs often adopt a multi-tiered dispute resolution structure, it offers Principles and model clauses on a range of options. In particular, Principle 29 and Principle 30 encourage the parties to prioritise, respectively, direct negotiations and third-party amicable dispute settlement mechanisms — such as mediation and conciliation, expert proceedings, and dispute boards — in order to seek to settle disagreements amicably instead of resorting directly to adjudicative dispute settlement proceedings. It provides different types of model clauses to assist parties in selecting the mechanisms most suitable for their contract (including a multi-tiered clause). Where amicable mechanisms do not lead to a solution, Principle 31 invites the parties to choose an appropriate adjudicatory forum for the settlement of their disputes. It proposes an arbitration clause, while also including a clause referring disputes to a domestic court.

588. Principle 32 encourages the parties to avoid parallel or duplicative adjudicatory proceedings, and offers model clauses containing different forms of waivers of treaty arbitration and judicial proceedings. The Chapter also addresses issues of transparency and conflicts of interest in international arbitration, encouraging the parties to consider these aspects by reference to relevant instruments developed by arbitral institutions and international organisations. Principle 33 reaffirms the right of the parties to raise counterclaims in relation to the obligations of the other party connected with the IIC, which is an important advantage compared to treaty-based investment arbitration.

## B. Choice of law

**Principle 28**

**Scope of party autonomy**

**An IIC is governed by the rules of law chosen by the parties.**

**Commentary**

[44] See Model Clauses for the Use of the UNIDROIT Principles of International Commercial Contracts, available at https://www.unidroit.org/instruments/commercial-contracts/upicc-model-clauses/.

589. The rules of law applicable to an IIC regulate the formation of the contract, rights, obligations, remedies, and other legal consequences of the contract, including the interpretation of the provisions of the IIC. The terms of an IIC ordinarily will not suffice to settle all questions that may arise in connection with an investment project. The applicable law can serve to fill gaps in the IIC.

590. Party autonomy as to the choice of law applicable to IICs is generally accepted. It refers to the freedom of parties to select, through an agreement, the rules of law to govern their contractual relationships. However, that autonomy is not without limitations, and the extent of such autonomy is subject to the applicable mandatory rules (see Article 1.4 of the UPICC and Principle 8 above). Limitations to party autonomy may concern various aspects of parties' choices, such as the aspects of the contract that can be governed by the chosen rules of law, formality requirements for making such choices, and limitations imposed by public policy. Whether and to what extent parties can choose non-State rules of law, such as the present Instrument, to govern their contract depends on the circumstances. In arbitration, parties enjoy substantial freedom to choose non-State rules of law applicable to the merits of their dispute. In a judicial setting, most national law does not allow parties to choose non-State rules of law to govern the contract, although there is a growing recognition of this possibility. Nevertheless, even in States that do not give effect to the choice of non-State rules of law by the parties, such non-State rules of law may still be applied indirectly by way of incorporation by reference, namely, as terms of the contract.[45]

591. It is advisable that parties to an IIC agree on the applicable law in advance, and clearly stipulate it in the contract. In the absence of a choice of law, the parties will face uncertainty as to how the terms of the IIC should or will be interpreted. IICs typically designate the law of the host State as the applicable rules of law, either exclusively or in conjunction with other rules. To assist contracting parties, model clauses are suggested below, focusing on the choice for (i) the Principles in this Instrument, which include the UPICC (see also Principle 2(1)) and (ii) a particular domestic law, with a role for the Principles in this Instrument, which include the UPICC, in the interpretation and supplementation of the chosen domestic law (see also Principle 2(5)). These options are not exhaustive and other options include the domestic law of the host State or the law of a third State, both either alone or in combination with other sources of law. When choosing a domestic law, parties should bear in mind that, in the case of a multi-unit State (*e.g.,* the United States of America, Canada, Australia, etc.), they should specify the particular jurisdiction to which they intend to refer. If multiple sources of law are combined, it is advisable to clarify their relationship.[46]

592. If the parties have not chosen any rules of law applicable to the IIC, the applicable law will be determined pursuant to the applicable conflict-of-laws rules, which may vary in accordance with the method of dispute resolution chosen by the parties.

**Model Clause A**



[45] See UNCITRAL, HCCH and UNIDROIT Legal Guide to Uniform Instruments in the Area of International Commercial Contracts, with a Focus on Sales (2021), Chapter II. As follows from Principle 2(1), the parties to an IIC may incorporate the Principles in this Instrument as terms of contract (even if they choose to have their IIC governed by another law). They may incorporate the Principles in their entirety or they may incorporate individual provisions or selected parts only. Insofar as a given rule of this Instrument has been incorporated as a term of the IIC, the contractual relationship between the parties will be governed by that rule. However, as a term of the contract, the rule can bind the parties only to the extent that it does not violate the mandatory provisions of the law governing the contract; in other words, those rules from which the parties to a contract may not derogate by way of agreement.

[46] For instance, in case of a hierarchical relationship, the choice-of-law clause could refer to "[source X] subject to [source Y]" or list the difference sources of law in order of precedence. In case of a complementary relationship, reference could be made to "[source X] and, with respect to issues not covered by [source X], by [source Y]". If one source is meant to interpret another source, reference could be made to "[source X], interpreted and supplemented by [source Y]. It is also possible to subject different parts of an IIC to different sources of law (*dépeçage*). However, this may further complicate the legal framework applicable to an investment project.

This Contract shall be governed by the UNIDROIT–ICC Principles of International Investment Contracts.

Commentary to the Model Clause

593. Model Clause A may be used by parties wishing to choose the Principles in this Instrument as the rules of law governing their contract. As explained in the Introduction and as follows from Principle 1, this Instrument refers to and incorporates the UPICC for issues of general contract law not addressed herein. Therefore, choosing this Instrument as the governing law of an IIC implies a concomitant choice of the UPICC.

594. Choosing the Principles in this Instrument, which incorporate the UPICC, as the governing law of an IIC is in the interest of both contracting parties. By combining a set of rules specifically adapted to the needs of IICs with a neutral and widely accepted transnational set of general contract rules, such as the UPICC, parties introduce a standard of interpretation that is predictable, balanced, and internationally oriented as per Article 1.6.1 of the UPICC.

595. The Principles in this Instrument, which include the UPICC, can only apply as governing law to issues that are within their scope. Issues that are within the scope of the UPICC but are not expressly settled by them may be settled, as far as possible, in accordance with the basic ideas underlying the UPICC (see Article 1.6.2 of the UPICC). Issues *outside* the scope of this Instrument and the UPICC will need to be governed by other legal sources. Such issues will be determined in accordance with the law designated by the applicable conflict-of-laws rules.[47]

596. In situations where the parties wish to designate a domestic law (of the host State or otherwise), they may wish to combine the choice of this Instrument with such law by adding the phrase "and, with respect to issues not covered by the Principles, by the law of [State X]".

597. As mentioned above, party autonomy is not absolute. Application of this Instrument as governing rules of law to an IIC does not restrict the application of mandatory rules, whether of national, international or supranational origin (see Article 1.4 of the UPICC).[48] Therefore, the Principles in this Instrument and in the UPICC can only be the primary source of law in relation to non-mandatory rules.

598. This model clause may also be used by contracting parties, with appropriate adaptations, when a dispute has arisen. Depending on the applicable rules of procedure, this may be done in a separate agreement, before or after the commencement of arbitral or judicial proceedings.

599. In the context of international investment arbitration, parties are generally permitted to choose soft-law instruments such as this Instrument and the UPICC as the "rules of law" on which the arbitrators are to base their decisions.[49] These Principles will then apply subject only to the application of "overriding"



[47] See the HCCH Principles on Choice of Law in International Commercial Contract (2015) (HCCH Principles 2015).

[48] See also Principle 8, which clarifies that, in the context of IICs, Article 1.4 of the UPICC is not intended to restrict the application of specific arrangements duly approved in accordance with the applicable law.

[49] See *e.g.,* Article 22(1) of the ICC Arbitration Rules (2026), Article 42(1) of the ICSID Convention (2022), Article 35(1) of the UNCITRAL Arbitration Rules (2021). In those instruments, "rules of law" is used to describe rules that do not emanate from State sources.

mandatory rules.[50] Domestic courts, on the other hand, are bound by the rules of private international law of the forum. Some States allow the application of non-State rules of law, while others do not.[51]

**Model Clause B**

> This Contract shall be governed by the law of [*State X*], interpreted and supplemented by the UNIDROIT–ICC Principles of International Investment Contracts.

Commentary to the Model Clause

600. In existing IIC practice, different sources of law, *e.g.*, domestic law and international law, are commonly combined. This practice reflects the transnational character of IICs.

601. Model Clause B may be used by parties wishing to choose a particular domestic law as the law governing their contract (in IICs, typically the law of the host State) while also wishing that law to be interpreted and supplemented by the Principles in this Instrument (which include the provisions of the UPICC). This approach enables a harmonised interpretation of domestic law. Adding an interpretative role to the Principles in this Instrument may serve the interests of both parties by providing a neutral benchmark against which to assess rights and obligations. By referring to this Instrument to interpret and supplement the applicable domestic law, parties can achieve greater predictability and thereby reduce transactional and litigation costs. It can also increase the attractiveness of an investment project to banks and other financiers, thereby enhancing the project's bankability.

602. Choosing to assign a supplementary role to this Instrument – alongside a particular domestic law – can also support the achievement of sustainable investment, as it encourages parties to an IIC to pursue the investment in accordance with the highest international standards related to sustainability (see Principle 6 on sustainable investment, Principle 11 on sustainability due diligence, and Chapter 5, Section D on sustainability obligations).

603. Generally, the choice of a particular domestic law does not include the private international law rules of the chosen law, unless the parties expressly provide otherwise.[52] This confirms the parties' intentions and avoids the possibility that the private international law rules of the chosen domestic law result in the application of the law of the forum State or the law of a third State (*renvoi*). This means that a choice-of-law clause that refers to a particular domestic law is generally interpreted as referring solely to the substantive law of that State. The chosen law will typically apply to contractual issues. Issues where the parties cannot choose the applicable law because party autonomy is restricted will be subject to the law designated by the applicable conflict-of-laws rules.

604. As explained in the commentary to Model Clause A, this model clause may also be used by contracting parties, with appropriate adaptations, when a dispute has arisen.



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[50] See Article 11 of the HCCH Principles on how courts and arbitral tribunals may or must apply overriding mandatory rules and public policy (*ordre public*). See also UNCITRAL, HCCH and UNIDROIT, Legal Guide to Uniform Instruments in the Area of International Commercial Contracts, with a Focus on Sales (2021), Chapter III.C "Mandatory rules and public policy".

[51] The HCCH Principles (2015) endorse the possibility for parties to choose non-State legal norms as the applicable law to a contract. See Article 3 and par. 3.6 of the commentary thereto, which expressly refers to the UPICC.

[52] See Article 8 of the HCCH Principles (2015).

## C. Dispute settlement

605. To ensure clarity and avoid uncertainty in the event of a dispute, parties to an IIC should agree in advance on a dispute resolution process and expressly set it out in the contract. IICs often adopt a multi-tiered dispute resolution structure, which typically begins with amicable efforts before escalating to adjudicatory mechanisms. Parties may consider direct negotiations (see Principle 29), as well as forms of amicable dispute settlement that involve a third party, including mediation, conciliation, expert proceedings, and dispute boards (see Principle 30). While the parties must try to settle their dispute amicably, either party may pursue binding dispute resolution if such efforts fail to resolve the dispute.

606. The dispute resolution clause in an IIC may thus refer to multiple means of settlement. The model clauses provided in this Instrument are intentionally flexible. They do not impose a mandatory, sequential process, whereby failure of one step is a legal precondition to move to the next. If the parties prefer a mandatory step-by-step approach, however, they should clearly define the sequence of steps, the rules and the timeframes applicable to each stage. In the latter case, it is suggested that the parties also clarify whether failing to effectively engage in amicable settlement would give rise to issues of admissibility if arbitration is initiated.

### 1. Negotiations

**Principle 29**

> **Parties should endeavour to resolve disputes arising out of or in connection with the IIC amicably through direct negotiations. A party's written request for negotiations should include sufficient information about the dispute to facilitate good-faith discussions and promote settlement.**

**Commentary**

607. It is advisable for parties to include in their IIC a dispute settlement clause that prioritises amicable resolution as the first step in addressing any disputes arising out of or in connection with the contract. The objective of amicable dispute settlement is to reach a mutually acceptable solution through cooperation and dialogue, rather than immediately resort to judicial or arbitral proceedings.

608. IICs increasingly include provisions requiring parties to attempt to settle disputes amicably through direct negotiations. These negotiations, which typically involve senior representatives from both sides, are a flexible and often effective means of resolving disputes. Negotiations may help contracting parties avoid the time and expense of judicial or arbitral proceedings and minimise friction in the parties' investment relationship. Even when negotiations do not result in a settlement, they may help the parties clarify or narrow the issues, facilitating a more efficient resolution in possible subsequent proceedings.

609. It is advisable to specify in the contract that negotiations commence upon written request by one of the parties. The obligation to try to resolve disputes through direct negotiations implies an obligation to provide sufficient information about the dispute to enable meaningful dialogue.

610. The parties should retain the flexibility to pursue amicable dispute resolution at any stage, including after the initiation of judicial or arbitral proceedings.

**Model Clause**

The Parties shall use best efforts to settle through direct negotiations any dispute or controversy arising out of or in connection with this Contract.

Either Party may propose negotiations by written notice. Such notice shall include sufficient information about the dispute or controversy to facilitate good-faith discussions and promote settlement.

## 2. Mediation/Concilitation and other third-party amicable dispute settlement mechanisms

**Principle 30**

**Parties may at any time submit to mediation, conciliation, or other third-party amicable dispute settlement mechanism any dispute arising out of or in connection with the IIC, without prejudice to the legal position or rights of any party.**

**Commentary**

611. Mediation and conciliation are valuable, although underutilised, means to resolve international investment disputes. The aim of mediation and conciliation is to reach an amicable settlement of the dispute with the assistance of a neutral third party. Differences between these two processes may exist depending on the applicable law and procedural framework.[53]

612. The growing interest in investor-State mediation is reflected in several instruments developed in recent years, a steady rise in provisions referencing mediation and conciliation in international investment agreements, and numerous publicly known investor-State mediation cases.

613. The United Nations Convention on International Settlement Agreements Resulting from Mediation (Singapore Convention) marks another important development. By providing a uniform and efficient framework for the recognition and enforcement of international settlement agreements resulting from mediation, the Singapore Convention could facilitate the development of mediation, including investor-State mediation.

614. Contracting parties to an IIC are encouraged to include mediation and/or conciliation in their dispute resolution clause. The choice between institutional and *ad hoc* mediation depends on the parties' needs for structure, support, cost-efficiency, and flexibility.[54] The parties should specify the chosen type of process, with explicit reference to the applicable rules.[55] Furthermore, they are encouraged to stipulate the language



[53] Internationally, the terms "mediation" and "conciliation" are used to describe processes that sometimes are substantively the same and sometimes are similar but have some differences. Where there are substantive differences, there is no uniform understanding of what those differences are. See ICC Mediation Guidance Notes (2014), footnote 2. For instance, the ICC and UNCITRAL interpret mediation broadly as encompassing conciliation, while ICSID distinguishes between both proceedings.

[54] Referring disputes to mediation institutions may help the parties with identifying mediators with the appropriate experience, appointing mediators when the parties cannot agree or managing other financial and logistical aspects of mediations.

[55] *E.g.*, the ICC Mediation Rules (2014), ICSID Mediation Rules (2022) and ICSID Conciliation Rules (2022), IBA Rules for Investor-State Mediation (2012), UNCITRAL Mediation Rules (2021). See also the UNCITRAL Guidelines on Mediation for International Investment Disputes (2024), which include Model Provisions.

and place of the proceedings. Some arbitration institutions have established specialised centres providing mediation services.[56]

615. In line with the flexible approach followed in this Section, a generic model clause on mediation and conciliation as non-mandatory means of dispute settlement is provided below. Option 1 refers only to mediation (and/or conciliation), whereas Option 2 combines different amicable dispute settlement options, including negotiation (if this approach is followed, the model clause would replace the model clause accompanying Principle 29).[57]

616. As mentioned above (see commentary to Principle 29), the parties should retain the flexibility to pursue amicable dispute resolution at any stage, including after the initiation of judicial or arbitral proceedings or after an award. Access to mediation during arbitration can be facilitated by "mediation windows", *i.e.*, pre-agreed periods during the course of a dispute during which the parties pause or delay other proceedings (such as arbitration) in order to attempt mediation.[58]

**Model Clauses on mediation and/or conciliation**

**Option 1:**

The Parties may at any time, without prejudice to any other proceedings, submit to mediation [*or conciliation*] any dispute or controversy arising out of or in connection with this Contract in accordance with [*include reference to agreed rules*].

The language of the mediation shall be [*include language*] and the mediation shall take place in [*include location*].

**Option 2:**

The Parties agree to seek to resolve any dispute or controversy arising out of or in connection with this Contract amicably through discussions or negotiations, which may include the use of non-binding, third-party procedures such as mediation or conciliation.

Either Party may propose negotiations, mediation, or conciliation by written notice. Such notice shall include sufficient information about the dispute or controversy to facilitate good-faith discussions and promote settlement.

The language of the mediation [*or conciliation*] shall be [*include language*] and the mediation [*or conciliation*] shall take place in [*include location*].



[56] *E.g.*, the ICC International Centre for Amicable Dispute Resolution (ADR) administers mediation proceedings under the ICC Mediation Rules.

[57] Institutions have developed tailored model clauses, which may be considered by the parties. See, *e.g.*, the ICC Model Clauses on Mediation, which offer four alternative model mediation clauses to parties wishing to have recourse to ICC mediation or other settlement procedures under the ICC Mediation Rules (including model clauses permitting parallel or subsequent arbitration).

[58] See, *e.g.*, ICC Commission on Arbitration and ADR, Report on Facilitating Settlement in International Arbitration (2023) and Guide on Effective Conflict Management (2023).

617. If parties prefer including mediation or conciliation as a mandatory step in a multi-tiered dispute resolution clause, it is advisable to specify the timeframe applicable to the mediation stage. A generic model clause on mediation in a multi-tiered setting is provided below.[59]

**Model Clause on mediation in a multi-tiered setting**

In the event of a dispute or controversy arising out of or in connection with this Contract, the Parties shall refer to mediation [*/or conciliation*] in accordance with [*include reference to agreed rules*]. The language of the mediation [*or conciliation*] shall be [*include language*] and the mediation shall take place in [*include location*].

If any dispute, controversy, or claim arising out of or in connection with this Contract, or the breach, termination or invalidity thereof, does not settle within [*XX* days] of the [*notice of dispute/default notice*], either Party may submit such dispute, controversy, or claim to arbitration [in accordance with the rules of [*include reference to the applicable arbitration rules*] or pursuant to *[include legal basis for the arbitration]*].

Unless the Parties agree otherwise:

i. [*The place of arbitration shall be […]* ]
ii. The number of arbitrators shall be […].
iii. The language of the arbitration shall be […].
iv. The law governing the arbitration agreement shall be […].

618. The parties to an IIC may also consider expert proceedings and dispute boards as means of third-party amicable dispute settlement. While mediation and conciliation aim to facilitate agreement between the parties, expert proceedings typically focus on providing a decision or assessment about a specific technical, financial, or other specialised issue, based on expertise in a particular field. Referring one or more issues in dispute to experts allows the parties to obtain either a non-binding expert evaluation, which may serve as a basis for settlement negotiations, or a binding expert determination, where the parties agree to be contractually bound by the expert's findings. The parties are advised to agree in advance on the types of issues that may or should be submitted to expert proceedings, and to make this explicit in their IIC (*e.g.*, by referring to specific contract clauses). Furthermore, it is advisable to clarify whether the findings of the expert will be binding for the parties and whether they will be final or may be subject to further review.

619. Given the common recognition that one of the most pressing issues in the investment context is that of damages, the parties are encouraged to address in their dispute resolution clause whether the dispute resolution forum may appoint independent experts to assist in the quantification of damages.

[59] Institutions have developed tailored model clauses on mediation in a multi-tiered setting, which may be considered by the parties. See *e.g.*, the ICC Model Clauses on Mediation, Clauses C and Clause D. Under Clause C, the parties are obliged to refer a dispute to mediation but do not need to conclude the mediation proceedings, or wait for an agreed period of time, before commencing arbitration. Under Clause D, the parties are obliged to refer a dispute to mediation and shall not commence arbitration until an agreed period of time has lapsed following the request for mediation (the model clause suggests 45 days, but the parties may agree on another period).

620. The ICC International Centre for Amicable Dispute Resolution (ADR) offers various services relating to experts, including in disputes involving States and State entities.[60] It may propose or appoint one or more experts on an *ad hoc* basis[61] or administer the entire expert proceedings[62]. The ICC has developed several options for model clauses on ICC expert proceedings.[63] Generic model clauses on expert proceedings are provided below.

**Model Clauses on expert proceedings**

**Option 1:**

The Parties may at any time, without prejudice to any other proceedings, submit to expert proceedings any dispute or controversy arising out of or in connection with *[this Contract/clause X of this Contract]/[X] issues]* in accordance with [*include reference to agreed rules*].

**Option 2:**

The Parties agree to seek to resolve any dispute or controversy arising out of or in connection with *[this Contract/clause X of this Contract]/[X] issues]* through expert proceedings in accordance with [*include reference to agreed rules*].

[*The Parties agree that the findings of the expert shall be contractually binding upon them*.]

**Option 3:**

**Model Clause on expert proceedings in a multi-tiered setting**

In the event of a dispute or controversy arising out of or in connection with *[this Contract / clause X of this Contract]/[X] issues]*, the Parties shall refer, first, to expert proceedings in accordance with [*include reference to agreed rules*].

If the dispute or controversy has not been resolved through expert proceedings, either Party may submit such dispute or controversy to arbitration [*in accordance with the rules of* [*include reference to the applicable arbitration rules*] or pursuant to *[include legal basis for the arbitration]*].

Unless the Parties agree otherwise:

i. [*The place of arbitration shall be […]* ]

ii. The number of arbitrators shall be […].

iii. The language of the arbitration shall be […].

iv. The law governing the arbitration agreement shall be […].

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[60] The ICC International Centre for ADR is one of the most prominent institutions offering experts services, but several other institutions also offer expert determination rules and may assist in the appointment of experts (*e.g.*, the Royal Institution of Chartered Surveyors, the Centre for Effective Dispute Resolution, some domestic and regional arbitration institutions).

[61] See the ICC Rules for the Proposal of Experts and Neutrals (2015) and the ICC Rules for the Appointment of Experts and Neutrals (2015).

[62] See the ICC Rules for the Administration of Expert Proceedings (2015).

[63] See the ICC's Suggested clause providing for ICC as appointing authority for expert proceedings, Clause A on optional administered expert proceedings, Clause B on obligation to submit dispute to non-binding administered expert proceedings, Clause C on Obligation to submit dispute to contractually binding administered expert proceedings, and Clause D on Obligation to submit dispute to non-binding administered expert proceedings, followed by arbitration if required.

621. Dispute boards are neutral panels that may issue non-binding recommendations or binding decisions, depending on the type of board. They are most commonly used in the context of construction and infrastructure projects, where a standing board is typically established at the start of the project and follows its progress, helping parties to avoid or overcome disagreements as they arise.[64]

622. While dispute boards have traditionally been associated with construction and infrastructure projects, their utility extends to other types of IICs, including resource extraction contracts, public utility concessions, and large-scale service concessions. In these contexts, a standing panel familiar with the project's technical, financial, and operational dimensions can resolve disputes efficiently and help preserve the contractual relationship.

623. Under the 2015 ICC Dispute Board Rules, and upon parties' request, the ICC International Centre for ADR may appoint Dispute Board members, decide on challenges filed against them, review their decisions, and fix their fees. The parties may choose from among three types of dispute boards: (i) a Dispute Review Board, which issues recommendations that are not immediately binding but which become binding if no party objects within 30 days; (ii) a Dispute Adjudication Board, which issues decisions that are binding upon notification to the parties; or (iii) A Combined Dispute Board, which generally issues recommendations but may, in specific circumstances, issue binding decisions. The ICC has developed several options for model clauses on ICC dispute boards.[65] In line with the approach followed in this Chapter, a generic model clause on dispute boards is provided below.

**Model Clause on dispute boards**

The Parties agree to establish a Dispute Board (DB) in accordance with [*include reference to agreed rules*].

The DB shall comprise [*one/three/X*] qualified member(s), who shall be appointed within [*XX*] days of the commencement of the Project. If the Parties fail to agree on the appointment within that period, either Party may request the appointing authority identified in [*include cross-reference to the relevant part of the Contract or the agreed rules*] to make the appointment.

In the event of a dispute or controversy arising out of or in connection with this Contract, the Parties shall refer it, first, to the DB for a decision [*OR: a recommendation*]. The DB shall issue its decision [*OR: recommendation*] within [*XX*] days after receiving the referral.

If any Party is dissatisfied with the DB's decision [*OR: recommendation*], it shall send a written notice to the other Party and the DB within [*XX*] days after receiving the decision [*OR: recommendation*]. If no such notice is given within that period, the decision shall become final. [*OR: If no such notice is given within that period, the recommendation shall become final and binding*.] If notice of dissatisfaction is given, the Parties shall attempt to resolve the dispute amicably.

If the DB does not issue its decision [*OR: recommendation*] within the time limit provided in [*include reference to agreed rules*] or if a Party's dissatisfaction with the DB's decision [OR: recommendation] has not been resolved amicably within [*XX*] days of the notice of dissatisfaction, the dispute or controversy shall be finally settled by arbitration [*in accordance with the rules of [include reference to the agreed arbitration rules] or pursuant to [include legal basis for the arbitration]*].

64 For instance, dispute boards are built into FIDIC contracts.

65 See here the ICC Model Clauses on (i) ICC Dispute Review Board followed by ICC arbitration if required, (ii) ICC Dispute Adjudication Board followed by ICC arbitration if required, and (iii) ICC Combined Dispute Board followed by ICC arbitration if required.

If any Party fails to comply with the DB's decision [*OR: recommendation*], when required to do so pursuant to [*include reference to agreed rules*], the other Party may refer such failure to arbitration. The Party that has failed to comply with the DB's decision [*OR: recommendation*] shall not raise any issue as to the merits of the decision [*OR: recommendation*] as a defence to its failure to comply without delay with the decision [*OR: recommendation*].

Unless the Parties agree otherwise:

i. [*The place of arbitration shall be […]* ]

ii. The number of arbitrators shall be […].

iii. The language of the arbitration shall be […].

iv. The law governing the arbitration agreement shall be […].

### 3. Dispute resolution forum

**Principle 31**

**Parties may choose an appropriate forum for resolving disputes arising out of or in connection with the IIC.**

**Commentary**

624. The parties to an IIC should agree in their contract on the binding dispute resolution mechanism to be used if amicable settlement fails. While some States may prefer to finally resolve disputes in their domestic courts (and may require that investors exhaust local remedies or pursue domestic remedies for a certain period), investors often consider a neutral third-party dispute resolution mechanism of paramount importance. They typically prefer international arbitration precisely because it affords the parties a neutral, fair, specialised, and effective mechanism with a globally enforceable regime for settling international investment disputes, including those arising under IICs.

625. The parties may choose between institutional and *ad hoc* arbitration, depending on their needs for structure, administrative support, cost-efficiency, and procedural flexibility.[66] The UNCITRAL Arbitration Rules[67] are widely used in *ad hoc* investor-State arbitration, both in treaty-based and contract-based disputes. Various international and regional arbitration institutions are experienced in administering disputes between States and investors concerning IICs, and the choice of parties may vary according to the specific features of an institution, its history, and its regional scope.

626. Among them, the ICC International Court of Arbitration ("ICC Court"), created in 1923, has long-standing experience in administering disputes involving commercial parties, States and State-owned entities. ICC arbitration adds value in IICs, particularly in the light of the significant number of arbitration cases administered by the ICC Court globally and the high number of States and State-owned entities participating in ICC arbitrations annually. As a response to the growing number of cases involving States and State-owned entities, ICC has issued specific guidance on how ICC arbitration is adaptable to the

[66] Institutional and *ad hoc* arbitration offer distinct advantages, and the appropriate choice depends on the nature of the dispute, the parties' preferences, and the context of their relationship. Institutional arbitration provides structure, administrative support, and procedural safeguards, which may be particularly valuable in complex or contentious disputes. *Ad hoc* arbitration offers greater flexibility and party autonomy, which can be well suited to situations where the parties are experienced, cooperative, or seeking a more tailored approach. Ultimately, the decision should reflect the parties' needs, resources, and the level of formality they consider appropriate for resolving potential disputes.

[67] UNCITRAL Arbitration Rules (2021). The rules can also be used in administered arbitrations.

particularities of such disputes.[68] ICC arbitration is conducted under the ICC Arbitration Rules and includes the scrutiny of draft awards by the ICC Court as an important and attractive feature of ICC arbitration, which generally improves their quality and enhances the enforceability of the award, and has no equivalent in other institutional rules. ICC arbitral awards are enforceable globally under the New York Convention.[69]

627. ICSID was established as part of the World Bank Group in 1966 under the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention), which has been ratified by 158 Contracting States as of 2025. The ICSID Convention is a unique, self-contained, de-localised legal framework, with rules specifically designed for investor-State disputes and a robust enforcement mechanism. Once rendered, an ICSID arbitration award is final and binding and can be enforced in any ICSID Contracting State as if it were a final judgment from that State's courts. The ICSID Convention provides a set of post-award remedies, including annulment, interpretation, and revision.

628. Any arbitration clause in an IIC should clearly reflect the parties' consent to arbitration and designate the applicable arbitration rules[70] or legal basis for the arbitration[71]. Furthermore, the clause should specify the number of arbitrators (typically one or three), the language of the proceedings, and the governing law. The seat of arbitration may also need to be designated.[72]

629. Generic model arbitration clauses are provided below. Option 1 refers only to arbitration, whereas Option 2 considers that amicable dispute settlement options may be pursued within a pre-agreed time period first. Several institutions have developed tailored model clauses, which may also be considered by the parties.[73]

630. For smaller or less complex cases, the parties to an IIC may wish to consider expedited arbitration, designed to resolve disputes quickly and efficiently with simplified procedures, typically involving a sole arbitrator and shorter timelines. Expedited arbitration options and rules are offered by several institutions.[74]

**Model Clauses on arbitration**

> **Option 1:** All disputes arising out of or in connection with this Contract shall be finally settled by arbitration [in accordance with the rules of [*include reference to the agreed arbitration rules*] or pursuant to *[include legal basis for the arbitration]*][75].



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68 See ICC Commission on Arbitration and ADR, Report on States, State entities and ICC Arbitration (2012).

69 The ICC recommends the following model clause: *All disputes arising out of or in connection with the present Agreement shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce by one or more arbitrators appointed in accordance with the said Rules.* Parties are free to adapt the clause to their particular circumstances.

70 *E.g.*, the ICC Arbitration Rules (2026), UNCITRAL Arbitration Rules (2021).

71 *E.g.*, for arbitration to be conducted under the ICSID Convention, explicit reference should be made to that Convention.

72 This is not necessary for arbitration conducted under the ICSID Convention.

73 See *e.g.*, the Standard ICC Arbitration Clause, ICSID Model Clauses, UNCITRAL Model arbitration clause for contracts.

74 See *e.g.*, Article 32 and Appendix V of the ICC Arbitration Rules, Chapter XII of the ICSID Arbitration Rules and Article 1(5) and the Appendix of the UNCITRAL Arbitration Rules. Under the ICC Arbitration Rules, an expedited procedure applies automatically to lower-value cases, unless the parties expressly opt out. Conversely, the parties may also agree to apply the expedited procedure to higher-value disputes by opting in. The threshold for automatic application is disputes not exceeding USD 4 million for arbitration agreements concluded on or after 1 June 2026.

75 For the formulation "in accordance with the rules of" reference can be made, *e.g.*, to the ICC Arbitration Rules or UNCITRAL Arbitration Rules. The alternative formulation should be used if parties wish to submit a dispute to ICSID Arbitration (*i.e.*, "pursuant to the ICSID Convention").

**Option 2:** If any dispute, controversy, or claim arising out of or in connection with this Contract, or the breach, termination or invalidity thereof, does not settle within [*XX* days] of the [*notice of dispute/default notice*], either Party may submit such dispute, controversy, or claim to arbitration [in accordance with the rules of [*include reference to the applicable arbitration rules*] or pursuant to *[include legal basis for the arbitration]*].

Unless the Parties agree otherwise:

i. [*The place of arbitration shall be […]* ]

ii. The number of arbitrators shall be […].

iii. The language of the arbitration shall be […].

iv. The law governing the arbitration agreement shall be […].

631. If the parties do not wish to refer their disputes to arbitration, they may also agree to refer the dispute to national courts by agreeing on one of the following clauses.

**Model Clauses on judicial proceedings**

**Option 1:** All disputes arising out of or in connection with this Contract shall be submitted to the courts of [*State*].

**Option 2:** Any dispute, controversy, or claim arising out of or in connection with this Contract, or the breach, termination or invalidity thereof, not settled within [*XX* days] of the [*notice of dispute/default notice*], shall be resolved in the courts of [*State*].

### 4. Avoiding parallel/sequential proceedings

**Principle 32**

**Parties should endeavour to avoid parallel or duplicative adjudicative dispute resolution proceedings.**

**Commentary**

632. Parallel proceedings are increasingly common in international investment disputes. Issues may arise when an investor has different means of asserting claims against a State (such as through a treaty and an IIC), or when related investors (such as a company and its shareholders) have different means of asserting claims against a State. Parallel proceedings may increase costs, decrease predictability, and lead to multiple and potentially conflicting awards or decisions.

633. The practice of international investment agreements may be relevant to IICs. These include fork-in-the-road provisions, by which a claimant must make an irrevocable choice to pursue either domestic-court litigation or arbitration.

634. To maximise legal clarity and avoid forum shopping, the parties to an IIC should ideally have recourse only to the dispute settlement mechanism specifically designated in the contract. The parties may seek to achieve this result by (i) clearly designating the chosen adjudicative forum in their contract (see Principle 31) and (ii) explicitly referring to that as the sole and exclusive means of adjudicative dispute settlement and waiving their rights to have recourse to any other dispute settlement forum (Principle 32).

635. A first type of waiver is a waiver of treaty-based investment arbitration. This is a waiver by the investor, since only the investor is able to commence investor-State treaty arbitration. Whether this type of waiver is enforceable depends on the circumstances. A relevant consideration in this context concerns the relationship between IICs and umbrella clauses in international investment agreements. An umbrella clause typically extends treaty protections to breaches of contractual or other commitments made by the host State in relation to a covered investment. Difficulties arise when the underlying contract contains an exclusive choice-of-forum clause and/or a waiver of the parties' right to pursue dispute resolution in an alternative forum. Arbitral tribunals disagree on the effect of such contractual provisions. A party can waive claims for any breach alleged under the agreement or any claim the "fundamental basis" of which is contractual.[76]

636. A second type of waiver is a waiver by both parties to initiate formal dispute resolution proceedings – whether judicial or arbitral – under rules or in a forum other than the one designated in the IIC. If the IIC contains a clear arbitration clause, parties can object to the initiation of proceedings elsewhere (*e.g.*, before a domestic court). However, it may be useful to explicitly state in the contract that the Parties waive recourse to any other dispute settlement mechanism than the one chosen in the contract. Caveats may apply depending on the specific context (*e.g.*, mandatory jurisdiction of local courts in some States or for specific issues).

637. A waiver of other dispute resolution proceedings does not necessarily bind third parties unless they are also party to the contract. In case of multiple proceedings involving different parties (*e.g.*, shareholders or affiliates of the investor) against the same host State concerning the same investment, an option could be to seek the consolidation of proceedings if allowed by the relevant arbitration rules. To enable consolidation, it is important to include the same arbitration clause in all contracts that govern an investment project (see also Principle 5 on interdependent contracts).

**Model Clause**

**Option 1: Investor's waiver of Treaty Proceedings**

The investor shall submit with its request for or notice of arbitration a written and non-conditional waiver of any right [*for itself or its shareholders*] to initiate other adjudicatory dispute resolution proceedings, with respect to:

(a) Any breach alleged under this Contract, or

(b) Any claim the fundamental basis of which is contractual.

**Option 2: Mutual waiver of Treaty Proceedings**

The Parties hereby waive their rights to initiate a proceeding and file claims under any applicable investment treaty regarding matters arising out of or in connection with this Contract.

**Option 3: Exclusive Dispute Resolution Forum and Waiver of Other Proceedings**

[76] See, *e.g.*, *Compañía de Aguas del Aconquija S.A. et al. v. Argentine Republic*, ICSID Case No. ARB/97/3, Decision on Annulment, para 101 (3 July 2002) ("[W]here 'the fundamental basis of the claim' is a treaty laying down an independent standard by which the conduct of the parties is to be judged, the existence of an exclusive jurisdiction clause in a contract between the claimant and the respondent state or one of its subdivisions cannot operate as a bar to the application of the treaty standard.") (citing *Woodruff* case, American-Venezuelan Mixed Commission, *Reports of International Arbitral Awards*, vol. IX, 213, 223).

The Parties agree that any dispute arising out of or in connection with this Contract shall be exclusively finally settled through adjudicative proceedings [*include reference to arbitration forum and rules*], as provided in this Contract.

Each Party irrevocably waives any right to (i) initiate or participate in any proceedings before the courts of any jurisdiction, except for proceedings seeking to enforce, recognise, or challenge an arbitral award rendered under this Contract; (ii) initiate or participate in any arbitration proceedings other than the one provided for in this Contract, whether under any other arbitration rules or institutional framework. This waiver shall not apply to proceedings concerning matters that fall outside the jurisdiction of the arbitral tribunal designated under this Contract.

To the extent permitted by applicable law and the relevant investment treaties, the Investor irrevocably waives any right to initiate or participate in adjudicative dispute settlement proceedings against the host State (including its agencies and subdivisions) under any bilateral or multilateral investment treaty in relation to disputes arising out of or in connection with this Contract. The Investor confirms that it makes this waiver with full knowledge of its rights under applicable investment treaties, and that it voluntarily relinquishes such rights to the fullest extent permitted by law. The Investor undertakes not to circumvent this waiver, directly or indirectly, through corporate restructuring, assignment, or proceedings through shareholders, affiliates, or third parties based on substantially the same facts or claims.

Commentary to the Model Clause

638. The Model Clause offers three progressively comprehensive options for managing the risk of parallel proceedings. Option 1 provides for an investor's waiver of treaty proceedings, requiring the investor to submit, together with its request for arbitration under the contract, a written and unconditional waiver of its right to initiate adjudicatory proceedings under any investment treaty. This is the narrowest option: it applies only to the investor (since only the investor can initiate treaty-based arbitration) and only to claims that are contractual in nature or that allege a breach of the contract. Option 2 provides for a mutual waiver: both Parties waive their rights to initiate proceedings and file claims under any applicable investment treaty regarding matters arising out of or in connection with the contract. This broader option reflects the principle that, if the parties have agreed on a comprehensive dispute resolution mechanism in the IIC, recourse to other fora should be foreclosed for both sides. Option 3 is the most comprehensive: it designates the contractual dispute resolution mechanism as the exclusive forum for all disputes and includes a detailed waiver of both judicial proceedings (except for enforcement or challenge of awards) and treaty-based arbitration. Option 3 also includes an anti-circumvention undertaking by the investor, preventing the use of corporate restructuring, assignment, or proceedings through related parties to circumvent the waiver. The enforceability of these waivers may vary depending on the applicable law and the relevant investment treaties; parties are encouraged to seek legal advice on the effectiveness of their chosen option in the specific legal context of their investment.

### 5. Issues of transparency and conflicts of interest

639. In recent years, States and other stakeholders have undertaken steps to increase transparency in international investment arbitration to take account of the public interest involved in such arbitrations, including through the adoption or amendment of treaties and rules of procedure.

640. Many States and other stakeholders, however, continue to value confidentiality in international investment arbitration.

641. During contract negotiations, parties may wish to consult the procedural rules applicable to their chosen arbitration forum in order to determine whether to include a clause on transparency or confidentiality of arbitration awards in their contract.[77] Parties may agree to the application of the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration (2014).[78]

**Model Clause**

**Option 1:** The Parties agree to make available to the public any award or decision with redactions of confidential or protected information.

[**Option 2:** The Parties agree that no award or decision made in the arbitration shall be published.]

**Option 3:** The UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration (2014) shall apply to arbitrations conducted under this Contract.

642. States and other stakeholders have undertaken steps in recent years to address conflicts of interest in international investment arbitration. Arbitration institutions may have specific rules or practices to ensure the independence and impartiality of arbitrators and address potential conflicts of interest that would apply or that the parties may be willing to refer to.[79]

643. In 2023, UNCITRAL adopted a Code of Conduct for Arbitrators in International Investment Dispute Resolution, which the UN General Assembly subsequently endorsed. The Code of Conduct for Arbitrators in International Investment Dispute Resolution may govern disputes brought under international investment contracts, as well as under investment treaties and foreign investment laws.[80]

644. Other soft-law guidance may govern other aspects of international arbitrations, including those brought under IICs. For instance, the IBA Guidelines on Conflict of Interest in International Arbitration (2024) are frequently referred to in arbitration proceedings.[81]

### 6. Counterclaims

**Principle 33**

**The parties to a dispute arising out of an IIC have a right to bring counterclaims in relation to the obligations of the other party in connection with the IIC.**

**Commentary**

645. An IIC stipulates rights and obligations for both the investor and the counterparty on the State side. Therefore, both parties to an IIC have a right to initiate dispute resolution proceedings and bring a claim against the other party for disputes arising out of or in connection with the contract, and the party

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77 See, *e.g.*, the ICC Note to Parties and Arbitral Tribunals on the Conduct of the Arbitration under the ICC Rules of Arbitration (2026), Part IV (Transparency); Chapter X of the ICSID Arbitration Rules.

78 See UNCITRAL, Rules on Transparency in Treaty-based Investor-State Arbitration (2014).

79 See *e.g.*, the ICC Note to Parties and Arbitral Tribunals on the Conduct of the Arbitration under the ICC Rules of Arbitration (2026), Part III.A.

80 UNCITRAL, Code of Conduct for Arbitrators in International Investment Dispute Resolution, Arts. 1 and 2.

81 IBA Rules on Conflicts of Interest in International Arbitration (2024), Introduction, para. 5 ("The Guidelines apply to all international arbitration….").

responding to the claim has the right to bring counterclaims. The contract provides the source of consent of both parties to the tribunal's jurisdiction and the scope of disputes it can hear.

646. This is a difference compared to treaty-based investment arbitration, where the investor unilaterally submits a claim under the applicable treaty and the State's ability to file a counterclaim depends on the treaty and the tribunal's rules and interpretation.

647. Arbitration rules may vary in how they address the scope and admissibility of counterclaims. For instance, Article 6 of the ICC Arbitration Rules does not restrict counterclaims to those arising out of the subject-matter of the dispute. In contrast, Article 46 of the ICSID Convention allows "counter claims arising directly out of the subject-matter of the dispute".

648. In contract-based investment arbitration, the scope of the claims by the responding party extends to all aspects relating to the IIC (it is not limited to the original claim). The objective is that all aspects of the dispute shall be resolved at one forum and avoid parallel/sequential proceedings.

649. In this context, the symmetrical architecture of this Instrument means that, in contract-based arbitration, the State, apart from commencing a direct claim, may bring counterclaims for breach of the investor's sustainability obligations under Chapter 5, including obligations relating to environmental protection, labour standards, human rights due diligence, local content, and community development. The availability of such counterclaims reinforces the balanced and reciprocal nature of the contractual relationship established by this Instrument.

**Model Clause**

1. Each Party has the right to bring counterclaims in any proceedings initiated under this Contract. The scope of permissible counterclaims extends to all obligations arising out of or in connection with this Contract, including obligations relating to investment protection, sustainability, payments and transfers, cooperation and assistance, and any other matter governed by this Contract.

2. [Without limiting the generality of paragraph 1, the State Party may bring counterclaims for non-performance of the Investor's sustainability obligations under [cross-reference to Chapter 5, Section D], including obligations relating to environmental protection, labour standards, human rights due diligence, local content, and community development.]

3. The tribunal shall have jurisdiction to hear and determine all claims and counterclaims of the Parties arising out of or in connection with this Contract in a single proceeding, with the objective that the entirety of the dispute be resolved in one forum.

Commentary to the Model Clause

650. This Model Clause gives contractual expression to the right of both parties to bring counterclaims, as articulated in Principle 33. Paragraph 1 establishes broad counterclaim jurisdiction, extending to all obligations arising out of or in connection with the contract. This ensures that the scope of counterclaims is not artificially limited to the subject matter of the original claim, reflecting the comprehensive and reciprocal nature of the contractual relationship in an IIC. Paragraph 2 specifically addresses the State party's right to bring counterclaims for breach of the investor's sustainability obligations, including environmental protection, labour standards, human rights due diligence, local content, and community development. This provision reinforces the symmetrical architecture of this Instrument: just as the investor

has contractual remedies for non-performance by the State, the State has contractual remedies – including counterclaims – for non-performance of the investor's sustainability commitments. This is a significant advantage over treaty-based investment arbitration, where the availability and scope of State counterclaims are often contested. Paragraph 3 reinforces the objective that the entirety of the dispute be resolved in a single proceeding, consistent with the Instrument's broader policy of avoiding parallel or sequential proceedings (see Principle 32).