EN

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REVISED ISSUES PAPER

1. This document provides a discussion of issues that the Working Group on International Investment Contracts may wish to consider during its fourth session.

2. The issues considered in this document were identified by the participants in the Subgroups, and the UNIDROIT Secretariat in cooperation with the ICC Institute of World Business Law (ICC-IWBL), considering the outcomes of the previous Working Group sessions. This document does not intend to provide an exhaustive list of issues nor a full legal analysis of each topic. Rather, its purpose is to provide a starting point for the Working Group's deliberations at its fourth session.

3. This document retains a revised version of parts of the Issues Paper from the third session relating to Preliminary Matters (Part I), General Issues Relating to the Contents of the Future Instrument (Part II), and Scope and Structure of the Future Instrument (Part III).

4. Part IV of this document relates to the content of the future instrument, based on the work conducted by the Working Group and the Subgroups so far. This document is accompanied by five Subgroup documents that represent the detailed outcome of the intersessional work and that will be the main object of the deliberations at the fourth session:

- **Report of Subgroup 0** on the Introduction and Chapter 1 of the future instrument;
- **Report of Subgroup 1** on pre-contractual issues, validity, contract formation, and remedies;
- **Report of Subgroup 2** on stabilisation/renegotiation clauses, hardship, and force majeure;
- **Report of Subgroup 3** on addressing policy goals in IICs;
- **Report of Subgroup 4** on choice of law and dispute settlement clauses.

5. In addition, the Working Group has received, on a confidential basis, the responses by Members of the Consultative Committee to a Request for Input that had been developed by the Secretariat and circulated to the Committee in June 2024.

6. Annexe I to this paper provides links to relevant documents to assist the Working Group. Annexe II sets out the draft structure of the instrument (version July 2024).

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I. PRELIMINARY MATTERS

A. Background of the project

1. In 2022, the Secretariat received a proposal from the ICC-IWBL for a joint project on investment contracts for inclusion in UNIDROIT's 2023-2025 Work Programme (UNIDROIT 2022 – C.D. (101) 4 rev., Annexe 3). The proposal aimed to explore how international investment contracts (IICs), *i.e.*, contracts between states, or their controlled entities, and private foreign investors, could be modernised, harmonised and standardised, particularly in light of the UPICC and ICC standards, with a view to address – at the contractual level and therefore mainly from a private law angle – a number of developments in the area of international investment law (IIL) in the last decades, such as the trend to incorporate public policy goals in "international investment agreements" (IIAs), including "bilateral investment treaties" (BITs) and the increasing potential relevance of IICs, also given the need to specify and concretise vague treaty norms and address legal uncertainty deriving from the lack of uniformity in arbitral decisions.

2. On 7 June 2022, the Secretariat, together with the ICC-IWBL, organised a Workshop on Transnational Law and Investment Contracts, during which the then-possible project was discussed with a group of experts in international arbitration and contract law. The Workshop considered developments in IIL and confirmed the need for guidance at the contractual level.

3. At its 101st session (Rome, 8-10 June 2022), the UNIDROIT Governing Council agreed on the importance of the topic and, considering the strong support expressed by Council Members, decided to recommend including the preparation of an instrument on IICs in the 2023-2025 Work Programme as a high-priority project (UNIDROIT 2022 - C.D. (101) 21). The General Assembly, at its 81st session (Rome, 15 December 2022), followed the Governing Council's recommendation and included the project in the new Work Programme of the Institute for the 2023- 2025 triennium (UNIDROIT 2022 – A.G. (81) 9).

4. On 17 February and 12 April 2023, the Secretariat and the ICC-IWCL held two preparatory meetings to discuss, *inter alia*, the composition of the Working Group and to exchange views on the scope, form and content of the future instrument. The Secretariat presented the developments in the preparatory phase for this project to the Governing Council at its 102nd session in May 2023 (UNIDROIT 2023 – C.D. (102) 13). On that occasion, the Governing Council reiterated its strong support for the project and authorised the Secretariat to establish a Working Group on International Investment Contracts and, if deemed convenient, a Consultative Committee composed of experts appointed by States.

B. Format of the future instrument

5. It is anticipated that the Working Group will prepare legal guidance and a set of model clauses in the area of IICs. A functional approach to legal concepts may be most appropriate in order to produce an instrument that would not be jurisdiction specific, but could be applied and reflected in any legal system or culture. The international guidance could enable practitioners to take a common approach to legal issues arising out of IICs.

6. Concerning the form and type of content, it was suggested during the second Working Group session that the instrument take the form of a self-standing set of Principles of International Investment Contracts with commentary and a set of model clauses. The alternative option would be a Legal Guide with model clauses.

7. A Legal Guide is generally less prescriptive than a set of Principles and could accommodate a more extensive consideration of the context of IICs, including more detailed guidance on pre-contractual issues and contract negotiation. On the other hand, a set of Principles with commentary

might be more practical as they could be immediately applied to investment contracts, by total or partial incorporation into contract clauses, by designation as the applicable law or as a tool for interpretation. A set of Principles would maintain a close relationship with the UPICC[1] and place itself among the instruments that complement the UPICC for special categories of contracts, adapting the Principles (as rules of general contract law) to their specificities, while at the same time restating special principles deriving from the practice of relevant economic transactions. Should certain issues benefit from a more detailed discussion, this could be accommodated in the commentary, either in an introductory part or in a separate, accompanying document.

8. The two different options have been already tested in practice. The Working Group may wish to consider, among the existing UNIDROIT instruments, the UNIDROIT/IFAD Legal Guide on Agricultural Land Investment Contracts (ALIC Guide) and the Principles of Reinsurance Contract Law (PRICL).

9. With regard to the development of model clauses, the Working Group may benefit from the long-standing tradition of the ICC in drafting model contracts and clauses. Limiting the focus to the last two decades, the ICC has drafted and published various model contracts. One of the features of ICC model contracts is that they are not drafted to be unilaterally imposed - they can be adapted and fully amended to meet the needs of the situation at hand. The purpose of ICC model contracts is to replace the choice between different national laws, which are often not adapted to the needs of international trade, with a detailed set of contractual provisions. These contractual provisions are not based on any specific national law but incorporate the prevailing practice in international trade as a whole, as well as the principles generally recognised by domestic law.

10. To guide the intersessional work, the Secretariat shared with the Working Group after the second Working Group session a draft template, so that suggestions for the third session would be presented in a form that would be closer to the expected output of the project. The template followed a tripartite structure: (i) Principles, (ii) Commentary, and (iii) Model clauses with short accompanying explanations. To the extent possible, the proposals of the Subgroups for the fourth Working Group session are presented in this format.

Suggestion for the Working Group:

- *The Working Group is invited to confirm the form of the future instrument.*

C. Target audience

11. As consistent with all UNIDROIT instruments, the prospective instrument should be relevant for all jurisdictions, irrespective of legal tradition. It should aim at facilitating the modernisation and standardisation of IICs to the benefit of the contracting parties – States and investors – which would be expected to be the primary addresees of the future instrument.

12. The future instrument would also consider the interests of other categories that may be affected by foreign investments, such as local populations and communities, contractors and sub-contractors, lawyers and consultants, workers, NGOs, academics, research entities or civil society at large. During various sessions of the Working Group, it has been repeatedly stated that it is of paramount importance for the future instrument to address the interests of third parties affected by the investment, particularly local and indigenous communities.

[1] More precisely, a "general to particular" relationship whereby the UPICC express the main principles of general contract law while the self-standing set of principles would not only include UPICC adaptations (*i.e.*, principles clarifying the manner in which the UPICC apply to the specific context of IICs), but also special principles deriving from IICs' practice and addressing IIA/BIT standards.

D. Composition of the Working Group

13. As consistent with UNIDROIT's established working methods, the Working Group is composed of experts selected by UNIDROIT and the ICC-IWBL for their expertise in international investment law and contract law. Members of the Working Group participate in a personal capacity and represent the world's different legal systems and geographic regions. The Working Group is co-chaired by Ms Maria Chiara Malaguti (President of the UNIDROIT Governing Council) and Mr Eduardo Silva Romero (Chair of the ICC-IWBL Council).

14. In addition to the two Co-Chairs, at present, the Working Group on International Investment Contracts is composed of the following experts:

- Mr José Antonio Moreno Rodriguez (*Chair of the Consultative Committee*), Founding Partner, Altra Legal (Paraguay);
- Mr Diego Fernandez Arroyo, Professor, Sciences Po (Argentina/France);
- Mr Lauro Gama, Professor, Pontifical Catholic University of Rio de Janeiro (Brazil);
- Ms Jean Ho, Professor, University of Singapore (Singapore);
- Ms Margie-Lys Jaime, Professor, University of Panama (Panama);
- Ms Ndanga Kamau, Founder, Ndanga Kamau Law (Kenya/the Netherlands);
- Mr Malik Laazouzi, Professor, University of Paris II Panthéon-Assas (France);
- Mr Pierrick Le Goff, Partner, De Gaulle Fleurance & Associés (France);
- Ms Céline Lévesque, Professor, University of Ottawa (Canada);
- Mr Chin Leng Lim, Professor, the Chinese University of Hong Kong (Hong Kong SAR, China);
- Mr Makane Moïse Mbengue, Professor, University of Geneva (Senegal/Switzerland);
- Mr Alexis Mourre, Founding Partner, Mourre Gutiérrez Chessa Arbitration (France);
- Mr Achille Ngwanza, Managing Partner, Jus Africa (Cameroon/France);
- Ms Emilia Onyema, Professor, SOAS University of London (Nigeria/United Kingdom);
- Mr Minn Naing Oo, Managing Director, Allen & Gledhill (Myanmar);
- Mr Aniruddha Rajput, Consultant, Withers LLP (India/United Kingdom);
- Mr August Reinisch, Professor, University of Vienna (Austria);
- Mr Jeremy Sharpe, International Arbitrator (United States);
- Ms Habibatou Touré, Cabinet Habitatou Touré (Senegal);
- Ms Giuditta Cordero-Moss, Professor, University of Oslo (Norway);
- Mr Mohammad Ismail, Judge, Vice-President of the Egyptian Conseil d'Etat (Egypt);
- Ms Meg Kinnear, International Arbitration Specialist (Canada/United States);
- Mr Michèle Potesta, Partner, Lévy Kaufmann-Kohler (Italy/Switzerland);
- Mr Donald Robertson, Partner, Dentons (Australia);
- Mr Stephan Schill, Professor, University of Amsterdam (the Netherlands);
- Mr Christopher Seppälä, Independent Arbitrator (United States/France).[2]

15. In addition, UNIDROIT and the ICC-IWBL have invited a number of intergovernmental organisations and transnational bodies to participate as institutional observers in the Working Group. Participation of these organisations and stakeholders will ensure that different regional perspectives are taken into account in the development and adoption of the instrument. It is also anticipated that the observer organisations will assist in the promotion, dissemination and implementation of the instrument once it has been adopted. To date, the following organisations participate as institutional observers in the Working Group:

[2] The last seven experts participate in the Working Group as individual expert observers. In addition to the list of experts, representatives of the ICC-IWBL for this project include Ms Mélida Hodgson (Vice-Chair) and Ms Cristina Martinetti (Member of the ICC-IWBL Council). Furthermore, Mr Juan Pablo Argentato (Managing Counsel of the ICC International Court of Arbitration) and Mr Andrzej Szumański (UNIDROIT Governing Council Member) take part in the project.

- European Law Institute (ELI);
- International Bar Association's (IBA) International Arbitration Committee;
- International Centre for Settlement of Investment Disputes (ICSID);
- International Institute for Sustainable Development (IISD);
- International Law Association (ILA);
- Roma Tre-UNIDROIT Centre for Transnational Commercial Law and International Arbitration;
- United Nations Conference on Trade and Development (UNCTAD);
- United Nations Commission on International Trade Law (UNCITRAL);
- United States Council for International Business (USCIB) Trade and Investment Committee.

16. Moreover, in light of the very broad interest generated by this project, a Consultative Committee was established to allow for wider participation of experts, ensuring that national and regional sensitivities and realities are considered, and to increase transparency *vis-à-vis* UNIDROIT Member States. The main objective of the Committee is to provide the Working Group with advice, comments and relevant information from a national and/or regional perspective as the work on the future instrument evolves.[3] Following the third Working Group session, the Secretariat developed a first Request for Input from the Consultative Committee. The responses to this request can be found in document Study 50-IIC – W.G. 4 – Doc. 3 (confidential). Furthermore, in August 2024, the Secretariat invited a number of non-Member States with significant investment relations to appoint experts to the Consultative Committee as Observers. This resulted in the appointment of 13 additional experts from eight non-Member States. In total, 35 States are now represented in the Committee.

E. Methodology and timeline

17. The Working Group undertakes its work in an open, inclusive and collaborative manner. As consistent with UNIDROIT's practice, the Working Group has not adopted any formal rules of procedure and seeks to make decisions through consensus.

18. The Working Group meets at least twice a year (for three days at a time). The sessions take place at the seat of UNIDROIT in Rome or at the headquarters of the ICC-IWBL in Paris. Meetings are held in English without translation. Remote participation is possible, although experts are expected to attend in person if circumstances permit.

19. The Working Group benefits from research on ICC arbitral awards conducted by a researcher under the oversight of the ICC-IWBL. Two memoranda prepared by the researcher on (i) the application of the UNIDROIT Principles in ICC awards regarding IICs and (ii) the main disputed clauses in IICs subjected to ICC arbitration were presented to the Working Group on a confidential basis at its first session.

20. Furthermore, research is conducted on publicly available IICs by an informal research task force established within the Roma Tre-UNIDROIT Centre for Transnational Commercial Law and International Arbitration under the supervision of the UNIDROIT Secretariat. The examination of contracts (and, as a next steps, contract-based arbitral awards) is useful to gather examples from practice to create a benchmark against which it will be possible to test the validity of the project's assumptions. The preliminary results of the task force, two memoranda concerning (i) policy goals and (ii) change of circumstances in IICs were presented to the Working Group on a confidential basis at its second session. A third memorandum on choice of law and dispute resolution clauses in IICs was presented at the third Working Group session. Following additional research, updated versions of the three memoranda were presented to the Working Group during a virtual intersessional

[3] The Consultative Committee consists of experts appointed by 27 Member States.

workshop on 3 October 2024. The three memoranda have subsequently been finalised based on the suggestions made by the experts, and will be circulated to the Working group ahead of its fourth session.

21. The preparation of an instrument on IICs is a high-priority project on UNIDROIT's Work Programme for the 2023-2025 triennium and should be completed during this period. The following is a tentative calendar:

(a) Development of an instrument on IICs over at least five in-person sessions of the Working Group between 2023-2025
  (i) First session: 23-25 October 2023 (Rome)
  (ii) Second session: 13-15 March 2024 (Paris)
  (iii) Third session: 3-5 June 2024 (Rome)
  (iv) Fourth session: 25-27 November 2024 (Rome)
  (v) Fifth session: 2-4 April 2025 (Paris)
  (vi) Sixth session: Second half of 2025 (Rome)
(b) Consultations and finalisation in 2025
(c) Adoption by the Governing Council of the complete draft in 2026.

F. Intersessional work

22. At the first Working Group session, in order to facilitate the organisation of the work, the Chairs suggested setting up informal subgroups that would be active during the intersessional period. They would be structured as open-ended, and both experts and observers were to be invited by the Secretariat to express their interest in participating in one or more of them. Five thematic subgroups were set up accordingly.

23. Subgroup 0 is Co-Chaired by Mr Stephan Schill and Mr Diego Fernández Arroyo and was assigned the following subtopics: (i) definitions and conceptualisation of international investment contracts (IICs); (ii) relationship with domestic law and IIAs; and (iii) interaction with the UPICC.

24. Subgroup 1 is Co-Chaired by Ms Giuditta Cordero-Moss and Ms Ndanga Kamau and was assigned the following topics: (i) pre-contractual issues in IICs, formation and validity; (ii) parties, non-signatory parties, and affected stakeholders; (iii) remedies, including compensation and damages; (iv) transfer of rights and obligations; and (v) other UPICC that may need adaptation.

25. Subgroup 2 is Co-Chaired by Ms Margie-Lys Jaime and Mr Pierrick Le Goff and was assigned the following topics: (i) change of circumstances (stabilisation/renegotiation/adaptation, hardship, force majeure); and (ii) other clauses typical of IICs.

26. Subgroup 3 is Co-Chaired by Ms Catherine Kessedjian and Ms Céline Lévesque, and was assigned the following topics: (i) addressing policy goals in IICs; and (ii) other treaty standards to be functionally addressed at the contractual level.

27. Subgroup 4 is Co-Chaired by Mr Michele Potestà and Mr Jeremy Sharpe and was assigned the following topics: (i) choice of law clauses; and (ii) dispute settlement clauses.

First intersessional period (November 2023 – February 2024)

28. Nearly all Working Group members and observers were involved in an intense working schedule established by the Co-Chairs of the Subgroups and supported by the Secretariat. Subgroups 0, 1, 2, and 3 kicked off their work and met virtually, mainly to discuss the organisation of their work and the subtopics assigned to them, and to suggest more precise parameters for each subtopic. Written input was provided by the Subgroup participants to advance the work. The below provides an overview of the meetings held during the first intersessional period:

- SG 0 – First Meeting – 23 February 13:30 – 15:00 (CET)
- SG 1 – First Meeting – 26 January 13:00 – 14:00 (CET)
- SG 1 – Second Meeting – 21 February 13:00 – 14:00 (CET)
- SG 2 – First Meeting – 7 February 13:00 – 14:00 (CET)
- SG 2 – Second Meeting – 29 February 13:00 – 14:00 (CET)
- SG 3 – First Meeting – 2 February 16:00- 17:00 (CET)
- SG 3 – Second Meeting – 20 February 16:00 – 17:00 (CET)

29. The intersessional work conducted by the Subgroups resulted in four comprehensive reports, one for each Subgroup, which were the main object of the deliberations at the second session of the Working Group. A fifth report is expected to be delivered not later than the session of November 2024.

Second intersessional period (April – May 2024)

30. Given the interconnection between the subtopics allocated to Subgroup 0 and the subtopics allocated to other Subgroups, the Co-Chairs of Subgroup 0 decided to continue the work of Subgroup 0 after the third Working Group session.

31. During the second intersessional period, Subgroup 1 focused on two subtopics: (i) pre-contractual issues, and (ii) issues of validity. Following written exchanges, the members of Subgroup 1 finalised their report on these issues, which contains concrete drafting suggestions – including draft principles, commentary, and model clauses – on a significant number of topics.

32. Subgroup 2 met twice (virtually) during the second intersessional period. The first meeting was mainly used to organise the work among Subgroup 2 participants. During the second meeting, the participants discussed draft papers on hardship and force majeure that had been produced by members of the Subgroup. The participants also discussed the 'relational contracts' theory and its potential relevance for this project. Following the meeting, the Secretariat shared an extract from the Note of the UNIDROIT Secretariat on the UPICC and the Covid-19 Health Crisis (2020)[4] for consideration of Subgroup 2.

33. Subgroup 3 met once (virtually) to discuss a draft paper drawn up by the Co-Chairs. The discussions mainly focused on the scope of economic, social and governance (ESG) obligations in IICs and the possible role of the home State in the context of policy goals, even if it was not a contracting party. Following the meeting, the Co-Chairs circulated a second and third draft of the paper to all Subgroup 3 participants for comments.

34. Subgroup 4 held its first virtual meeting end of April 2024. During that meeting, it was agreed to start work on the development of model clauses first, followed by a commentary and underlying principles. The participants agreed that the future instrument should provide different options to contracting parties, both concerning choice of law clauses as well as dispute resolution clauses. Furthermore, statistical information was shared on contracts that had been the subject of contract-based arbitrations at ICSID.

35. The below provides an overview of the meetings held during the second intersessional period:

- SG 2 – Third Meeting – 15 April 14:00 – 15:00 (CEST)
- SG 2 – Fourth Meeting – 13 May 14:00 – 15:00 (CEST)

[4] The Note is available at https://www.unidroit.org/english/news/2020/200721-principles-covid19-note/note-e.pdf.

- SG 3 - Third Meeting – 3 May 15:00 – 16:00 (CEST)
- SG 4 - First Meeting – 30 April 14:00 – 15:00 (CEST)

36. The Reports of Subgroups 1, 2, 3, and 4 were the main object for deliberation by the Working Group at its third session.

Third intersessional period (June – November 2024)

37. During the third intersessional period, the Co-Chairs of all Subgroups were invited by the UNIDROIT Secretariat to attend a virtual meeting on 15 July 2024 to share their views on a revised draft structure of the future instrument (i.e., an update of Annexe II to the Revised Issues Paper for the third Working Group session).

38. Furthermore, the UNIDROIT Secretariat had prepared for the Co-Chairs of Subgroup 0 an outline comprising the elements that had been allocated to Subgroup 0 in the revised draft structure of the future instrument (the "Introduction" and "Chapter 1") for their consideration and to inform the work of Subgroup 0 during the third intersessional period.

39. Subgroup 1, in turn, as agreed at the third Working Group session, exchanged and discussed updated draft texts concerning the subtopics that had been allocated to Subgroup 1, which resulted in the production of the Report of Subgroup 1 for the fourth Working Group session.

40. Subgroup 2 met three times (virtually) during the third intersessional period. In the first meeting, Subgroup 2 addressed the next steps to be pursued, compiled the tasks to be completed and organised the work among its participants. In the second meeting, Subgroup 2 discussed draft papers on stabilisation, hardship and force majeure that had been produced by its members. In the third meeting, Subgroup 2 focused exclusively on addressing issues relating to stabilisation and the material that had been produced by individual participants in this regard. These discussions resulted in the production of the Report of Subgroup 2 for the fourth Working Group session.

41. Subgroup 3 met three times (virtually) during the third intersessional period. In the first meeting, Subgroup 3 mainly discussed the preliminary proposals submitted by its members for a draft Preamble and for a draft corruption provision. In the second meeting, Subgroup 3 focused on discussing pending matters connected to the scope of economic, social and governance (ESG) obligations in IICs. In the third meeting, Subgroup 3 reviewed and commented on a draft sustainability due diligence clause prepared by one of its members and a draft text on policy goals to be included in the introduction of the future instrument. These discussions resulted in the production of the Report of Subgroup 3 for the fourth Working Group session.

42. Lastly, based on the discussions during the third Working Group session, the Subgroup 4 Co-Chairs (Mr Jeremy Sharpe and Mr Michele Potestà), assisted by Mr Johannes Fahner, prepared a draft Report of Subgroup 4 for the fourth Working Group session. The first draft was circulated on 7 October 2024 to the members of Subgroup 4 for feedback by 21 October 2024. The Report of Subgroup 4 was subsequently updated according to the comments received.

43. Moreover, a virtual intersessional workshop was organised by the Secretariat to allow the Task Force on IICs under the Roma Tre-UNIDROIT Centre for Transnational Commercial Law and International Arbitration to present its research on (i) policy goals, (ii) change of circumstances and (iii) choice of law and dispute resolution clauses in publicly available IICs. In addition, a representative of the ICC Institute presented relevant ICC Model Clauses.

44. The below provides an overview of the meetings held during the third intersessional period:

- Co-Chairs' Call – 15 July 2024 10:00 – 11:00 (CEST);

- SG 3 – Fourth Meeting – 16 July 2024 10:00 – 11:00 (CEST);
- SG 2 – Fifth Meeting – 29 July 2024 14:00 – 15:00 (CEST);
- SG 3 – Fifth Meeting – 6 September 2024 11:00 – 12:30 (CEST);
- SG 2 – Sixth Meeting – 10 September 2024 9:00 – 10:00 (CEST);
- Virtual Intersessional Workshop (S50-IIC) – 3 October 2024 8:00 – 10:30 (CEST)
- SG 3 – Sixth Meeting – 4 October 2024 10:00 – 12:00 (CEST);
- SG 2 – Seventh Meeting – 21 October 2024 11:30 – 12:30 (CEST).

45. In addition, during the third intersessional period, Mr Antonio Moreno Rodriguez organised the event *Taller sobre arbitraje y el Estado*, which took place in Paraguay (and remotely, via Zoom) on 14-15 October 2024, where the following topics were discussed: (i) "*investments and change of circumstances: the role of the contractual 'stabilisation' clause*", (ii) "*international investment contracts and policy goals*", (iii) "*applicable law and dispute settlement clauses*" and (iv) "*remedies, with a focus on compensation and damages*". The event was attended by several Latin American members of the Consultative Committee and other renowned experts in the field, as well as the UNIDROIT Secretary-General (in-person), the UNIDROIT President, Deputy Secretary-General, and relevant Legal Officers (virtually). The Secretariat is expected to participate in further events which may contribute to the development and promotion of the project in the next months, starting with the Lillehammer Workshop on International Investment Contracts on 5-6 December 2024 at the Inland Norway University.

46. The Reports of the Subgroups are the main object of deliberation by the Working Group in its fourth session.

G. Relationship with existing international instruments

47. The future instrument is expected to be coordinated with existing instruments and with the ongoing work of several international organisations (IOs) insofar as they may have an impact on IICs, especially as regards the consistency of terminology and language across similar initiatives.

48. Several UNIDROIT instruments play a central role in this project, in particular the UPICC, the PRICL and the ALIC Guide. More generally, the Working Group should take into account the whole set of UNIDROIT instruments where appropriate: for instance, the UNIDROIT/FAO/IFAD Legal Guide on Contract Farming may be relevant for issues such as hardship and force majeure, and the project on Collaborative Legal Structures for Agricultural Enterprises may provide useful guidance on multiparty contracts.

49. Although other IOs have sometimes addressed IICs,[5] their work has mostly targeted public international law instruments (BITs and IIAs). UNCTAD elaborated documents on investment policy options and treaty reform;[6] the OECD regularly publishes studies on IIL standards and has established a forum to discuss investment policies;[7] the WTO manages a number of agreements that have an impact on investments and has launched initiatives on investment facilitation;[8] UNCITRAL

[5] E.g., UNCTAD has issued a publication on contracts between States (or State Entities) and foreign investors: see State Contracts, UNCTAD Series on Issues in International Investment Agreements, Geneva, 2004.

[6] See the 2015 Investment Policy Framework for Sustainable Development, officially launched at the Financing for Development Conference in Addis Ababa, at https://investmentpolicy.unctad.org/investment-policy-framework.

[7] See OECD, Fair and Equitable Treatment Standard in International Investment Law, OECD Working Papers on International Investment, 3, 2004, at https://www.oecd.org/investment/investment-policy/investment-treaties.htm.

[8] See the Agreement on Trade-Related Investment Measures (TRIMs), the General Agreement on Trade in Services (GATS), and the Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPs).

conducts work on Investor-State Dispute Settlement (ISDS) reform,[9] is codifying new standards of conduct for adjudicators in investment disputes in partnership with ICSID,[10] and produced model legislative provisions on "Public-Private Partnership" (PPP), which considered some aspects of PPP agreements that may be relevant to IICs;[11] and the HCCH's expertise on conflicts of law is also essential to this work.[12] To the extent the final instrument will touch upon issues that are covered by existing UNIDROIT instruments or fall within the scope of activity of other IOs, it should be coordinated with their work, and consistency of language and legal concepts should be ensured. Observer organisations in the Working Group are invited to contribute to ensuring such consistency, as well as to identify further studies or initiatives that may be of relevance to this project.

50. Documents elaborated by relevant private sector participants, including model contracts or model clauses elaborated by associations of certain industries, should be considered.[13]

II. GENERAL ISSUES RELATING TO THE CONTENTS OF THE FUTURE INSTRUMENT

51. At its first session, the Working Group recalled the contextual background of the project and agreed with the three "layers of content" of the future instrument: (i) the UPICC as general contract law principles and rules[14], and as adapted to the context of IICs when appropriate; (ii) principles, rules and clauses deriving from current IICs transnational practice; and (iii) possible innovative principles, rules and clauses that may contractually address vague investors' protection standards in IIAs/BITs (with some limitations) and policy goals in recent IIAs.

A. Role of the UPICC and their interaction with the other layers of content

52. Regarding building block (i), it was agreed that the UPICC provide the starting point for this project, while other existing UNIDROIT instruments (especially the ALIC Guide) should also be taken into consideration. The UPICC contain a solid basis of concepts of general contract law that can be imported into IICs practice (e.g., offer and acceptance, consent of the parties). Methodologically, the Working Group would start its analysis by identifying areas for work (pre-contractual and contractual issues, needs for protection and typical breaches, inconsistencies or flaws of the existing protection, emerging policy goals) and look into the UPICC to assess whether any of their principles and rules was suitable for application to that area. If a UPICC Principle was found to be relevant in the context of IICs, the Working Group would examine whether it might apply as it is or might need adaptation to the specificities of IICs.[15] In the latter case, in order to see how and to what extent it should be adapted, the Working Group should take into account how IICs practice (under the second layer of content) articulates that principle or rule in a manner that departs from general contract law as

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[9] See the work of UNCITRAL Working Group III. The reform is five pronged: the establishment of a Multilateral Permanent Investment Court and an Appellate Mechanism, the reform of Procedural Rules, an Investment Mediation and Dispute Prevention policy, the setting of a Multilateral Advisory Centre, and the drafting of Codes of Conduct. More information is available at https://uncitral.un.org/working_groups/3/investor-state.

[10] See the UNCITRAL/ICSID initiative on the drafting of codes for arbitrators and judges.

[11] See the UNCITRAL Model Legislative Provisions on Public-Private Partnerships (2019).

[12] See, e.g., the HCCH Principles on Choice of Law in International Commercial Contracts at https://www.hcch.net/en/instruments/conventions/full-text/?cid=135.

[13] See, e.g., the FIDIC guidance documents on contracts (FIDIC Suite of Contracts or the FIDIC Contracts Guide).

[14] In the context of the UPICC, the term "principles" does not only refer to provisions with a higher degree of generality which incorporate certain value assumptions capable of being projected onto a wider range of more specific provisions (good faith, reliance, cooperation, party autonomy, and the like); the term also includes more specific rules which essentially cover the most important topics of the general law of contract and obligations (*e.g.*, formation, interpretation, validity, performance, non-performance and remedies, assignment, time limitations, conditions, etc.).

[15] It was mentioned that traditional distinctions between public and private law are currently blurring and that differences between the UPICC and IICs needs for protection should not be overestimated.

enshrined in the UPICC. If no UPICC was found to be relevant, the Working Group would look into contract practice, transnational standards, or strive for a better rule.

53. Given the relevance of the UPICC to this Project, the Working Group should consider how and to what extent they are already applied to IICs. In accordance with their Preamble, the UPICC may fulfil different functions.[16] They have been applied by arbitral practice in different ways, most prominently as a means of interpreting and supplementing the applicable domestic law, often to add weight to the tribunal's interpretation of the relevant domestic law, but also as the *lex contractus.*[17] It was advised that the Subgroups examine for each area of work - or each UPICC that is found to be relevant - the existing case-law, and particularly how awards (if available) have applied the UPICC to IICs.

B. Principles, rules and clauses in IICs transnational practice

54. Regarding layer (ii), the Working Group agreed in its first session that it is necessary to consider contract practice to the greatest extent possible, either as a benchmark to adapt the relevant UPICC or to extract the relevant transnational principle or special rule in areas where the UPICC are found not to contain any solution (e.g., stabilisation/renegotiation/adaptation).

55. In order to conduct a correct appraisal of transnational practice, the Working Group should include in the analysis standardised "contract types" and "model clauses" elaborated by governments and industry associations, as well as the principles shaped by arbitral jurisprudence in this area.[18] The ICC model clauses and model contracts will also be taken into consideration.

56. During its first session, the Working Group indicated as areas for work clauses on "pre-contractual responsibility", "change of circumstances",[19] "revenue transfer", "compensation and damages", "choice of law", "dispute resolution", along with "clauses addressing policy goals, including due diligence and affected their parties". "Confidentiality" and issues of interests and currency were also mentioned. The Working Group did not decide whether it would limit its work to key provisions that were characteristic of IICs or rather extend it to a wider range of aspects (joint ventures or associations, issues of insurance, payment, option rights, pre-emption rights, currency fluctuation,

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[16] See the UPICC Preamble (2016 revision), p. 1. The UPICC may apply to a contract if they have been chosen by the contracting parties as the governing law, alone or in combination with the law of the host State, or if the arbitrators consider they are the appropriate rules to govern the contract when the parties have not chosen any law. In addition, they may perform other functions: they may provide a model for negotiators (or legislators) and be incorporated wholly or partly into contract clauses, or be used as criteria and tools for interpretation when they are used to interpret or supplement domestic law or international uniform law instruments, or to help to ascertain their contents. In Joseph Lemire v Ukraine, the tribunal determined that the parties intended their investment contract to be governed by the UPICC since they had incorporated extensive parts of the Principles into their agreement (i.e., a "negative choice" of the UPICC through the exclusion of specific national law). Contracting parties to an IIC may designate as governing law "generally accepted principles of international commercial law", "general principles of law", *lex mercatoria*, of which the UPICC may be seen as a manifestation (see ICC ICA (First Partial Award) case no. 7110 (June 1995); ICC ICA case no. 7375 (5 June 1996); and EUREKO v. Republic of Poland, Ad hoc arbitration, Brussels (19 August 2005)).

[17] In particular, for issues concerning the form of contract, non-performance, good faith and fair dealing, inconsistent behaviour, common intention of the parties, the duty to achieve a specific result versus best efforts, quantification of damages, set-off conditions, hardship, liability exemption clauses, and force majeure. For an overview of the relevant case-law principle by principle, see the UNILEX database.

[18] Arbitral tribunals have identified in their awards a number of general principles of law (or principles common to most legal systems) that have progressively accumulated and that have been found to apply to IICs (good faith, *pacta sunt servanda*, estoppel, reliance, equity and good conscience, justice, unjust enrichment, *non venire contra factum proprium*, *res judicata*, *rebus sic stantibus*, non-discrimination, prohibition of abuse of law, respect of acquired rights, "competence-competence", due process, and the like).

[19] Including "stabilisation" and "adaptation (restoration of the financial equilibrium)", "hardship" and "force majeure".

local procurement, clauses on the minimum amount of investment required over a certain agreed period, and so forth[20]).

57. The Working Group generally agreed to develop generic guidance that would be applicable across sectors, combined with industry-specific guidance. It was noted that model clauses such as those included in the FIDIC standard forms of contract usually provide for a general and a special part. The general clauses might be easier to elaborate, but special clauses can substantially differ depending on the sector. Doubts were expressed during the intersessional period and on the occasion of the virtual intersessional workshop of 3 October 2024 on the possibility to provide uniform principles across different sectors (e.g., energy and construction) and it was suggested to gain more knowledge on the subject matter and assess whether a differentiation of the principles would be required for different type of IICs.

C. Contractual guidance for aspects addressed in IIL treaty standards

58. Regarding layer (iii), the Working Group strongly agreed at its first session that the future instrument should provide guidance on how to address contractually new IIAs/BITs provisions on policy goals in IICs, with a broad scope (e.g., from sustainability to human rights and corporate social responsibility, climate change and the protection of affected populations, such as indigenous peoples). Concerns were generally expressed about the possibility of replicating IIAs/BITs standards of protection, such as FET or the provisions on expropriation, in a contractual setting. Pure replication seemed difficult to achieve and would run the risk of reproducing the flaws of the existing system.[21] Extracting principles from recent treaties should be treated with caution and could be done as long as contractual substitutes existed (e.g., clauses addressing "change of circumstances"). Certain specific standards in IIAs/BITS may be more easily addressed contractually: provisions on transfers of profits and criteria for compensation and calculation of damages were mentioned as examples. It is still discussed whether other IIAs/BITs standards might be functionally contractualised, such as a full protection and security-inspired standard.

59. It could be inferred from the Working Group's reasoning that regulatory stability concerns (including with regard to legitimate expectations, expropriation and regulatory takings) would be covered under functional contractual equivalents, as part of the work of Subgroup 2 on clauses addressing "changes of circumstances". Legitimate expectations concerns might also be covered under arrangements in the pre-contractual phase (Subgroup 1). As a rule, when a contractual functional equivalent to IIAs/BITs standard existed, the Working Group should examine whether a generally accepted transnational principle could be discerned. If not, the Working Group could propose a contractual rule itself.

III. SCOPE AND STRUCTURE OF THE INSTRUMENT

A. Definition of "International investment contracts"

60. The Working Group was invited at its first session to reflect on the notion of "international investment contracts". IICs are commonly described in a general manner as contracts (i) negotiated, concluded and executed between a State (or a State-owned entity, agency or territorial subdivision) and a private foreign investor (or its local subsidiary) that (ii) relate to the establishment and

[20] Other clauses specific to IICs practice of IICs would be: clauses on transfer of technology and know-how, clauses on background and foreground intellectual property; clauses containing reporting requirements for the investor *vis-à-vis* domestic authorities and the right of the State to be informed; clauses providing the State with the right to exert control over operations throughout the duration of the investment, pre-entry screening and right of constant supervision of the operations, including site access and delivery of documents, budget sheets, financial accounts, etc.

[21] In particular, the intimate variability and/or vagueness of the standards, with particular regard to FET and the treatment of indirect expropriation and regulatory takings.

operation of one or more lasting economic activities by the foreign investor in the host State, which are not merely speculative but imply some substantial commitment to its development.[22]

61. IIAs usually do not provide a definition of IICs.[23] Rather, they delimit their scope of application by defining a subjective and an objective element (investor/investment). The ICSID Convention does not define the term "investment". Thus, several conceptual approaches were possible: providing a definition, providing a list of examples or rather describing the "economic significance" of activities and leaving definitional issues to practice and interpretation. On these terms, arbitral tribunals, in the absence of explicit exclusions, have often come to qualify IICs themselves as "covered investments" and thus assets which deserve protection under IIL.

62. With regard to the subjective element, IIAs often refer to an investment as a network of complex interrelated economic activities which may also include contractual relationships between a State - or a governmental agency or entity - and a private, for-profit foreign company.[24] Treaty definitions refer to the importance of investors' nationality as the element that triggers protection and jurisdiction. IIA reform has recently aimed at narrowing the range of protected investors in order to avoid "treaty shopping"[25] and "round-tripping"[26] by including real business activity requirements or denial of benefits clauses.[27]

63. As to the objective element, treaties traditionally include broadly-formulated definitions with a certain prevalence of asset-based definitions referring to direct or indirect control of several kinds of assets or economic activity.[28] More and more exceptions and carve-outs are provided for protected sectors (education, health) and for certain policy areas (taxation). A trend is emerging to limit coverage by expressly excluding short-term, speculative or portfolio investments, sovereign debt obligations and other assets,[29] or imposing certain conditions ("domestic law compliance") or defining certain characteristics of the investment such as the commitment of capital, the expectation of profits and the assumption of risk, or a certain duration or lasting economic relation of the investment.[30]

64. At its first session, the Working Group did not discuss whether the future instrument should provide a normative definition of "international investment contracts", or if it would prefer a list of examples. It was clarified that the scope of the project should include the "background" (or "framework") contract between the State (or a State entity) and the foreign investor, rather than the bundle of connected contracts that regulate the investment. Doubts were raised during the first intersessional period on whether contracts concerning portfolio investments or concluded with (new)

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22 The "international character" of IICs depends on their evident connection with more legal orders: i*nter alia* and in addition to the foreign nationality of the investor, it might be the foreign provenance of the invested capital or know-how, or the choice of law, when it points at international principles and/or at a foreign law, and the deferral of controversies to international arbitration into the dispute settlement clause.

23 Arbitral tribunals have occasionally defined the concept of "investment agreement", often in a narrow way: see Duke Energy v. Ecuador (18 August 2008) and Burlington v. Ecuador (2 June 2010).

24 An investment relationship between a State and a foreign government-controlled entity may also be relevant: see Rumeli Telekom v. Kazakhstan, ICSID Case no. ARB/05/16 (29 July 2008).

25 The channelling of the investment through a "mailbox company" in the territory of a State party to enjoy its protection.

26 The expatriation by domestic investors of investment capital to reinvest in the home country to obtain protection.

27 See policy developments from 2015 onward in UNCTAD World Investment Reports 2015 and 2016, up through World Investment Report 2022, p. 66 *et seq*.

28 Including tangible and intangible property, intellectual property rights, mortgages, liens and pledges, shareholding or participation in a company, claims to money or performance, licences and permits, and the very investment contracts themselves.

29 Other examples of exclusion include claims to money arising from commercial contracts and intellectual property rights not recognised or protected under host State's law.

30 See the EU-Canada Comprehensive Economic and Trade Agreement (CETA) Chapter on investments at art. 8.1, or the Nigeria-Turkey BIT (2011) and, from even earlier, the USA-Chile BIT (2003).

companies incorporated in the host State as part of the implementation of the background contract would fall within the scope of this project.

65. During its second session, the Working Group discussed that it might be preferable not to define the term "international investment contracts" and that, in any case, the notion of "investment" should be subject to the caveat "except as parties otherwise agree" as had been proposed in the Report of Subgroup 0. Furthermore, in addition to Article 25 of the ICSID Convention, it might be useful to consider the Commentary to the Preamble of the UPICC and relevant UNCITRAL instruments.

66. In the third session, the Working Group agreed that including a definition of "international investment contracts" in the future instrument was not necessary, as it could unduly limit its scope of application and render it incompatible with new types of contract that may be created in the future. Furthermore, it was clarified that, in addition to being a major challenge, the search for a definition could be considered all the more expendable if the Working Group decided to primarily develop Model Clauses in the future instrument, since, in this case, the clauses could be included in any type of contract deemed appropriate by the contracting parties.

67. Nevertheless, the Working Group stressed that the future instrument, regardless of a definition of "international investment contracts", should have a clear and defined scope to guide its application. In this regard, some suggested that a possible solution to this issue would be to provide a description of IICs without a specific legal definition and include in the future instrument a non-exhaustive list of categories of contracts (i.e., concession agreements, product sharing agreements, build-operate-transfer agreements, etc.) that would be subject thereto. No final decision was reached by the Working Group concerning this topic.

B. Structure of the instrument

68. The structure and content of the future instrument significantly depend on the format. In case of a set of Principles with comments, the instrument could combine a list of principles that adapt the UPICC to IICs with principles deriving from IICs' practice and/or addressing IIL standards, together with commentary and model clauses. This option would make the instrument more closely resemble a "restatement of principles" concerning a specific sector of contract practice, such as – in UNIDROIT's experience – the PRICL.[31] The PRICL were conceived as a non-binding set of rules that parties can either choose as the law governing their contracts or incorporate into their agreements,[32] including principles whose formulation has been influenced by the UPICC and principles specific to reinsurance contract law. They refer back to the application of the UPICC as principles of general contract law "as they are" in the areas that did not need adaptation.[33]

69. If the option of a Legal Guide is preferred, the Working Group may wish to consider the structure of the ALIC Guide, which aggregates areas of general contract law and thematic areas specific to land investment contracts across seven chapters.[34] While the ALIC Guide drafters carefully

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[31] The PRICL includes five chapters: (i) general part; (ii) duties; (iii) remedies; (iv) aggregation; (v) allocation.

[32] In this respect, the PRICL draw on the example of the Preamble of the UPICC (see Art. 1.1.1).

[33] The PRICL may be considered partly an adaptation of the UPICC as applied to reinsurance contracts and partly a restatement of principles and rules that are specific to reinsurance contracts and have no connection with the UPICC. The comments to the PRICL clearly define the relationship between the PRICL and the UPICC. In particular, they make express reference to the UPICC provisions that influenced the elaboration of the PRICL, as well as to the rules of general contract law contained in the UPICC that are not replicated in the PRICL, but that will govern the contract if the PRICL are chosen as applicable law (Art. 1.1.2). The instrument also contains a base model choice-of-law clause according to which the contract shall be governed by the PRICL, and two base clauses with an addition for gap-filling (PRICL/UPICC and accepted principles of international commercial law; PRICL/UPICC and the national law chosen by the parties).

[34] The ALIC Guide includes seven chapters: (1) legal framework; (2) parties, stakeholders, and contractual arrangements; (3) pre-contractual issues; (4) rights and obligations; (5) contractual relationship with reference

selected relevant areas of interest under general contract law, some of its content and its treatment are specific to ALICs (e.g., land use and tenure rights) and are of less interest for IICs, possibly justifying a different mode of organisation.

70. Based on the discussions during the first and second Working Group session and intersessional deliberations, a preliminary draft structure for the instrument was prepared by the Secretariat on the assumption that the future instrument would take the form of a set of Principles with commentary and model clauses (see Annexe II to the Revised Issues Paper for the third Working Group session).

71. In the third session, the Working Group was invited to reflect on how the future instrument would relate to the UPICC in light of the structure prepared by the Secretariat. It was agreed that the Subgroups should merely refer in the future instrument to the UPICC provisions that were already suitable for IICs *"telle quelle"* without textually reproducing them. To this extent, the Subgroups were required to focus on aspects of the UPICC that called for adaptation or additional clarifications for IICs and on specific guidance, when applicable. Moreover, the Working Group agreed to include in the structure prepared by the Secretariat considerations pertaining to guidance on contract termination, transfer of rights and obligations, and a general principle on cooperation between the parties.

72. For details on the above-mentioned considerations, refer to Annexe II, which was updated by the Secretariat following the third Working Group session.

Question for the Working Group:

- *The Working Group is invited to consider the updated draft structure (Annexe II) when discussing the content of the future instrument.*

IV. CONTENT OF THE INSTRUMENT

73. The topics covered in this section offer an attempt to frame the discussion on the possible content of the future instrument, considering the preliminary draft structure of the instrument.

A. Introduction

Questions for the Working Group:

- *The Working Group is invited to discuss the proposed content of the Introduction to the future instrument (see Outline of Subgroup 0). Should any modifications be made?*

B. General provisions

1. Scope of application, interpretation, usages

Questions for the Working Group:

- *The Working Group is invited to discuss the proposed content of proposed Chapter 1 on General Provisions. Should any modifications be made or additional aspects be covered?[35] Does the Working Group agree with the proposed allocation of work?*

to non-performance and remedies; (6) transfer of rights and obligations under the contract; and (7) grievance mechanisms and dispute resolution.

35 See, for purposes of comparison, Chapter 1 of the UPICC and Chapter 1 of the PRICL.

2. Definitions

74. The practice of IICs relies on specific language and legal concepts that are usually included in a list of definitions at the beginning of the contract, describing their meaning and coverage.

75. While the UPICC already contain definitions for the relevant concepts used therein,[36] a list of definitions in the future instrument specific to IICs may prove useful to establish meanings and provide a clearer context to the prospective users, especially in relatively new areas (e.g., "contractualised" BITs/IIAs standards and other policy goals).[37]

76. It is advised that any definitions be consistent, as far as possible, with the terminology used in other international instruments. Furthermore, at its first session, the Working Group agreed on the importance of a list of definitions to reflect practice and discussed that definitions should be formulated in a manner that allows them to be used in different jurisdictions and industry sectors.

Questions for the Working Group:

- *Which legal concepts should be developed with priority?*
- *Would the Working Group agree to provide Subgroup 0 or a Drafting Committee with a mandate to develop a list of definitions for the fifth Working Group session?*

C. Parties, non-signatory parties and affected stakeholders

77. At its first session, the Working Group strongly supported the inclusion of work addressing the legal nature of the parties to IICs (States and private foreign investors), as well as the different categories of affected stakeholders.[38]

78. It was considered relevant to define, for the purposes of the instrument, the notion of "State party", including its central bodies ("Government", "Ministries") and local subdivisions or territorial entities ("regions", "municipalities"), and "State entities" (State agencies or specialised authorities, "State-owned enterprises"); however, the notion of "investor party" may include foreign companies or locally registered companies but could also be impacted by the relationship between the parent company and a subsidiary in the host country, or by the economic association or affiliation of more enterprises, such as joint ventures or consortia ("multiparty contracts").

79. Possible issues arising from the complex nature of the parties in IICs were considered as areas for work. For example, there would be merit in considering issues of legal representation and special rules that may apply when a State/State agency/State-owned enterprise/territorial entity (e.g., a municipality) signs an IIC. On the investor side, the added complexity was considered that the foreign investor may establish a new company in the host State to execute an IIC, while such company was not a party to the contract.

80. In connection with this topic, the Working Group discussed whether the State concludes an IIC in its sovereign (public) or commercial capacity. Different views were expressed in this regard by the Working Group. Public and private law profiles are tightly interwoven. State contracts might be construed as "private contracts" to which any domestic (or transnational) law might apply depending on party choice, or an "administrative contract" to which special laws on public law contracts in the host State apply. In both cases, the contracts should be controlled against national public policy and

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[36] See, e.g., UPICC Art. 1.11.

[37] The ALIC Guide follows a similar approach when listing categories of parties and stakeholders (such as investor, grantor, local community, traditional authority, legal tenure right holder, etc.).

[38] The Working Group may wish to look at the ALIC Guide, where Chapter 2 contains a description of the type of subjects that are party to land investment contracts, and references to contractual arrangements that might occur between the State and the investor, on one hand, and affected stakeholders, on the other.

domestic mandatory norms in the applicable law. Over time, new types of IICs have taken the stage, such as "concession contracts" and "private-public partnerships" (PPP) that place the parties on an equal footing, with a clear trend to limit clauses providing exorbitant State powers, including as to the termination of contract. A line could be drawn between cases where the State and the foreign investors directly negotiate, as opposed to cases where few margins for negotiations are left ("public tenders"[39]). In the former case, the State could be deemed to act in its contractual capacity, freely negotiating the contents of the contract with the private party, with some specificities depending on the public law nature of its acts; in the latter case, it would act in its public law capacity, concluding an agreement with content mandatorily imposed by the law. Overall, it was considered that when dealing with IICs, i.e. State contracts with an international character, a State is negotiating with the foreign investor on an equal footing with its capacity of private law and therefore IICs should be considered commercial contracts with some specificities depending on the public nature of the State.

81. Subgroup 1 proposed in its Report for the second Working Group session (Subtopic 1) to conduct work on five areas: (1) the State as a multi-faceted actor; (2) identity of parties, rights and obligations; (3) binding non-signatories to an IIC; (4) extending the arbitration agreement; and (5) affected stakeholders. The Report of Subgroup 1 contained questions and issues that Subgroup 1 suggested considering and discussing for each of these areas.

82. During the second Working Group session, it was suggested that, in addition to the UPICC and the ALIC Guide, the Working Group may wish to consider the guidance provided in the UNIDROIT/FAO/IFAD Legal Guide on Contract Farming on these topics. Furthermore, it was generally considered beneficial to conduct further work on the issues raised in the Report of Subgroup 1.

Questions for the Working Group:

- *Should the future instrument provide specific guidance/contain a specific section on the parties to an IIC and other stakeholders (see Chapter 4, which includes a proposed section on third parties), or should any specificities be covered in relevant substantive provisions, e.g., exploring how the identity of the parties might affect their rights and obligations? If the latter approach is followed, which aspects should be covered and where?*
- *In this regard, the Report of Subgroup 1 for the second Working Group session raised issues such as (i) a possible disclosure obligation of an investor's ownership structure, (ii) implications of the involvement of different entities for liability, (iii) attributability of actions to a State, (iv) possible joint venture agreements, (v) rights and obligations of parties in case of a multiparty contract, (vi) implications of nationality in the context of dispute resolution.*
- *Should guidance be provided on the legal capacity to enter into an IIC? If so, what should the guidance entail, and would the Working Group agree to cover this in Chapter 4 (see Annexe II)?*

D. Pre-contractual phase

83. The Working Group agreed at its first session on the importance of providing guidance in the future instrument on pre-contractual issues. Guidance should include classical areas of pre-contractual liability (in particular, the parties' duty to inform), but also issues arising from emerging national and international standards concerning any due diligence required of investors in areas of public interest, including ESG substantive and procedural obligations and the protection of affected third parties ("policy goals"). During the first intersessional period, it was clarified that the Issues

[39] In the area of "public procurement" the State issues a call for tender and provides for strict regulations clearly requiring the bidders to not depart from the provisions included in the call.

Paper covered both areas as interrelated themes for work[40] even if precontractual issues fell within the remit of Subgroup 1 and policy goals under Subgroup 3. Coordination would therefore be needed.

84. The Working Group agreed that, in principle, there were significant divergences between legal cultures as regards the pre-contractual phase. From a common law perspective, pre-contractual issues (and liability) were not part of the contract, i.e., the process that leads the parties to sign the contract is not relevant to define the obligations that each party undertakes; under other legal cultures, the information provided prior to the formalisation of a contract is determinative of the object of contract and therefore a stronger duty to inform can be construed. The manner in which pre-contractual issues are covered would then intertwine with issues of applicable law, as the outcome of any dispute would depend on the forum (a national court or international arbitrators) and on which type of law applies (administrative or private law).

85. At the same time, there was enough consensus that transnational law principles are emerging in IIC practice that depart from domestic laws, especially those which ignore the legal relevance of pre-contractual conducts.[41] In treaty arbitration, international responsibility based on pre-contractual behaviour has been often adjudicated because of the standards existing in that area. In contract-based arbitration, the parallel issue, strictly connected to applicable law, is whether a transnational principle exists that overrides or interacts with domestic law in this area (e.g., the OECD Guidelines for Multinational Corporations or specific industry standards) and that can be relied upon across sectors binding both States and investors. Gaps may exist at the level of domestic law, which may be complemented by reference to a transnational or international standard (such as the obligation to conduct an environmental or social impact assessment concerning the investment). The issue of the *erga omnes* binding character of these standards, often incorporated in international (soft law) documents, or mere intra-corporation relevance, should also be considered.

86. All these issues might be properly approached by guidance that would raise awareness about the most relevant risks in the pre-contractual phase having an impact on the IIC, including the consequences of the law governing the contract, and suggest proper pre-contractual arrangements. Transnational contract practice has shown a significant trend that most pre-contractual issues are being contractualised by way of pre-contractual documents such as letters of intent or warranties and representation clauses. By way of example, a clause might require the investor to accept a statement that it reviewed all the papers of the bidding process and all the relevant laws and regulations of the State in relation to the specific sector. This might be further examined.

87. It was also raised that, especially in long-term contracts, negotiations might occur during the entire lifespan of the contract, and the principles that would be applicable in the pre-contractual phase might also be relevant for negotiations that may take place at a later stage. This might well be the object of a contractual provision concerning principles and procedures that would apply to negotiations.

88. During its second session, the Working Group discussed the Report of Subgroup 1 for the second Working Group session, which proposed that the future instrument covers (i) principles applicable to the pre-contractual phase (considering e.g., article 1.7 of the UPICC on good faith and its interaction with the parties' duty of disclosure, changes of strategy or policy by the private and the public party respectively, and due diligence requirements in the pre-contractual phase), and (ii) the relevance of the pre-contractual phase to determine the scope of contractual obligations (considering e.g., article 2.1.17 of the UPICC on merger clauses). The Working Group generally agreed with this approach. Suggestions were made, *inter alia*, to provide concrete guidance on due

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[40] See Study L-IIC – W.G. 1 – Doc. 2, Part IV. D, 1 to 3.

[41] E.g., the principle that international merchants/investors are deemed to be competent professionals and its principal corollary according to which they shall undertake comprehensive due diligence before investing in a foreign country.

diligence obligations with special regard to their reciprocal allocation on the State and/or the private foreign investor, to consider the specificities of relational contracts and the possible relevance of article 5.1.3 of the UPICC on co-operation between the parties, and the role of warranties and "entire agreement" clauses. It was also discussed that it would be useful to consider clauses in IICs contract practice and pre-contractual documents most commonly used, particularly letters of intent and warranties and representations that the investor fully knows the legislation of the host State.

89. In the third session, Subgroup 1 introduced its Report on pre-contractual issues. The proposal comprised commentary on the existing UPICC provisions and draft Model Clauses on the following five subjects:

(1) a draft Model Clause on "risk for its own assumption": the Model Clause encompassed guidance on pre-contractual due diligence concerning "how", "who" and "if" a determined document and/or data should be requested and/or disclosed by one of the parties;

(2) a draft Model Clause on "party's freedom to evaluate its own interests": the clause aimed at ensuring that throughout the negotiations or possibly the tender process, and until a binding contract was entered into, each party would be entitled to change its negotiation position, including breaking off the negotiations or the tender process, subject to such restrictions as expressly agreed upon by the parties and in the tender documents. The Working Group agreed at its third session that consistency of behaviour and good faith in the approval procedure should be part of the pre-contractual obligations of the State. Nevertheless, some participants suggested that, while Subgroup 1's idea was clear from a commercial law standpoint, it should be considered in the context of investment law, where the State was a party to the contract and public law was to some extent applicable;

(3) a draft Model Clause on "conclusion of contract": several questions were raised on this point by the participants, which concerned, for example, the scope of application of the provision, the multiple meanings of the words chosen depending on the jurisdiction, its possible interpretation as a potestative or illicit condition, and so forth. The Working Group suggested that Subgroup 1 review how the UPICC provisions on public permission requirements applied in the pre-contractual phase;

(4) a draft Model Clause on "mandatory rules": the clause intended to clarify that any specially agreed terms (e.g., tax breaks) would prevail over mandatory rules generally applicable in the host State. The Working Group agreed that this provision encompassed a challenging issue which should be carefully considered. Several questions were raised by the participants regarding, *inter alia*, the legality of the provision, its ramifications, and the legal concepts of "mandatory", "public", and "private" rules;

(5) a draft Model Clause on "entire agreement": the main concern expressed by the Working Group related to the effective need to adapt or supplement the existing UPICC provisions in order to achieve the purpose intended by the draft Model Clause. Subgroup 1 was tasked with addressing this issue.

90. For the fourth session, Subgroup 1 submitted an updated Report on pre-contractual issues considering the comments that were raised by the Working Group in the previous session.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the updated proposals of Subgroup 1.*

E. Validity

1. Suggested form

91. During its first session, the Working Group agreed to elaborate guidance on the form of IICs and provide the necessary adaptation of the "no formal requirement" rule provided in article 1.2 of the UPICC since IICs were usually negotiated and concluded in writing. The Report of Subgroup 1 for the third Working Group session had contained a proposal for a principle requiring that IICs should be drawn up in writing, with flexibility to encompass electronic communications and without prejudice to possible mandatory requirements concerning form in the domestic law of the host State. During the discussions, it was pointed out that in the context of tender processes, the relevant law concerning the written form (including on electronic support) would be the law of the tender (i.e., the law of the host State). This would be a preliminary phase that was governed by procurement law, before the actual choice of applicable law to the IICs. Subgroup 1 underlined that the draft Principle would provide a common ground and complement domestic law when appropriate.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the updated proposal of Subgroup 1, which is now accompanied by a draft Model Clause.*

2. General provisions

92. In the third session, Subgroup 1 illustrated the following proposals for general provisions:

(1) a draft Principle on "validity of mere agreement" - in this regard, some doubts were expressed on the need for such proposal, and it was proposed to consider the specificities of tender processes;

(2) a draft Principle on "initial impossibility".

93. As a general remark, it was recalled during the third session that small adaptations to the UPICC provisions might not be worthwhile. In such case, it might be preferable to refer to the relevant UPICC provision as it was, while providing guidance on how it would apply to IICs.

94. For the fourth session, Subgroup 1 considered the feedback provided by the Working Group in the third session, and complemented the draft Principles with suggested contract language.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the updated proposals of Subgroup 1, which are now accompanied by draft Model Clauses.*

3. Grounds for avoidance

95. As to issues of validity of contract, it was discussed during the first Working Group session that the articles of the UPICC concerning duress, improper influence or gross disparity (and other invalidity grounds) might certainly apply to IICs, but in principle there seemed to be no particular arbitral practice or specific situation to address. Therefore, it was suggested that it might suffice to refer to the UPICC as they were.

96. In its Report for the second Working Group session, Subgroup 1 proposed examining the grounds for avoidance in the UPICC[42] to see whether any adaptations or additional guidance was required. The Report of Subgroup 1 for the third Working Group session contained proposals on: (i)

[42] Reference was made to articles 3.2.5 (fraud), 3.2.6 (threat), and 3.2.7 (gross disparity) of the UPICC.

mistake (*suggesting that the relevant UPICC Principles might not be applicable to IICs*), (ii) fraud, (iii) threat, duress, (iv) gross disparity, (v) third persons, (vi) confirmation, (vii) loss of right to avoid (*suggesting that the relevant UPICC Principle might not be applicable*), (viii) notice of avoidance or request for renegotiation (*suggesting that the relevant UPICC Principle might not be applicable*), (ix) retroactive effect of avoidance, (x) restitution and (xi) damages.

97. In the third session, the following proposals were discussed:

(1) "Mistake": it was suggested that some guidance on the UPICC provisions on mistake could be provided in the Commentary of the future instrument, instead of excluding their application entirely;

(2) "Fraud": during the third session, Subgroup 1 noted that matters relating to fraud might overlap with provisions on representations and warranties, and that there might be differences in its application depending on whether the IIC was individually negotiated or part of a public procurement process. Some discussion took place on the relationship between fraud and corruption, and the attributability of actions to the State (which, it was agreed, would be separately addressed by Subgroup 1);

(3) "Threat, duress": it was suggested to consider (i) that the term "duress" was purposely not used in the UPICC, and that the UPICC terminology should be maintained to the greatest extent possible in the future instrument unless there were specific reasons to deviate from it, and (ii) what the applicable threshold should be;

(4) "Gross disparity": during the third session, Subgroup 1 clarified that the main proposed adaptation to the UPICC provision was to provide for renegotiation rather than avoidance. Different views on the proposal were expressed by the participants, with some suggesting not to include a provision on gross disparity, while others suggested to refer to the UPICC provision as it was;

(5) "Third persons": it was suggested to consider the status of State companies and situations in which a State agency negotiated an IIC but then submitted it to State organs for approval;

(6) "Damages": the Working Group agreed that the work in this area should be coordinated with UNCITRAL's ongoing work on damages, while also considering possible differences in damages for contractual and treaty breaches.

98. For the fourth session, Subgroup 1 submitted an updated Report on grounds for avoidance considering the comments that were raised by the Working Group in the previous session.

Suggestions for the Working Group:

- *The Working Group is invited to discuss the proposals of Subgroup 1.*
- *On mistake, Subgroup 1 proposes to discuss whether it would be proper to formulate a clause to the effect that the host State and the foreign investor had thorough knowledge of the factual assumptions surrounding the transaction and deep knowledge of the applicable laws and regulations, and whether it would be possible to provide a uniform clause considering that representations and warranties varied widely.*
- *On fraud, Subgroup 1 proposes to discuss (i) whether specific provisions should be formulated for (a) fraud by the State, (b) fraud by the investor, (c) "improper influence", and (ii) whether the future instrument should include contractual language covering specific situations in which the investor might be vulnerable to undue/improper influence.*

- *On damages, Subgroup 1 proposes to discuss whether a Model Clause on liquidated damages should be suggested.*

4. Illegality

99. Subgroup 1 proposed in its Report for the second Working Group session to examine the provisions on illegality in the UPICC[43] to see whether any adaptations or additional guidance was required.

100. The question was also raised whether the future instrument should specifically address corruption. During the first Working Group session, it was discussed that work on corruption may prove to be more challenging as the international practice had struggled for decades to elaborate some solution without meaningful results. A hypothesis for work would be to address corruption by contractual means, i.e., taking inspiration from anti-corruption clauses where a contracting party, if the contract turned out to have been obtained through corruption, had a choice between cancellation or damages.

101. In the third session, Subgroup 1 introduced a draft Principle on contracts infringing mandatory rules, which was drawn from UPICC art. 3.3.1 and could allegedly cover, *inter alia*, active or passive corruption. During the ensuing discussion, some participants stressed that the doctrine of illegality was currently under debate, which created doubts regarding the applicable threshold. The Working Group agreed that a separate Principle and Model Clause on anti-corruption should be developed, while the draft Principle on mandatory rules should be reconsidered from the angle of public international law.

102. The Report of Subgroup 1 for the fourth session contains updated proposals on illegality considering the feedback provided by the Working Group in the third session.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the proposals of Subgroup 1.*
- *The Working Group is invited to discuss the proposal of Subgroup 1 concerning anti-corruption together with work of Subgroup 3 in this area.*

F. Rights and obligations of the parties, addressing new IIAs/BITs policy goals through contractual tools

103. The main rights and obligations of the parties in IICs lie at the core of this Project. Although IIL has long focused more on States' obligations, most recent IIAs/BITs have instead been focusing on a more articulated set of rights and obligations between the parties, which increasingly includes investors' obligations. Under the first version of the Issues Paper (see Study L-IIC – W.G. 1 – Doc. 2, Part IV.E.3), the Working Group had been invited to discuss how policy goals contained in treaty law and soft law documents, mainly in the form of "best efforts," could be turned into contractual obligations, with a view to clarify their scope and specify their contents *vis-à-vis* the need of States and investors to gain more certainty about their rights and obligations.

104. The Working Group at its first session generally agreed that policy goals should be addressed contractually with a broad coverage (e.g., from sustainability to human rights and corporate social responsibility, climate change and the protection of third parties and affected populations, with special regard to indigenous peoples). The issue was raised that policy goals were often vague and their interpretation, as the interpretation of human rights concepts, continuously evolved over time,

[43] Reference was made to articles 3.3.1 (contracts infringing mandatory rules) and 3.3.2 (restitution) of the UPICC.

which might make it difficult to capture their contents by the means of contract.[44] Policy goals may also vary depending on the industry sector. The Working Group agreed that these challenges should be addressed by balancing the need for being as specific and concrete as possible with the drafting of model clauses with open textured language and the proposal of a range of options, leaving it to the contracting parties to determine which ones would be relevant to their contract.[45]

105. Work on policy goals could build on article 1.4 of the UPICC on mandatory rules, which included principles of public policy (e.g., human rights, environmental protection), and on the relevant Chapters of the ALIC Guide, which provided examples on how to include policy goals in agricultural land investment contracts,[46] along with the work of organisations that partnered in its drafting,[47] and/or on the concept of "transnational public policy." Regard should also be had to mandatory rules from the jurisdiction in which the (parent) company was located (home State), which would incentivise responsible investments even if the host State was less advanced in prescribing sustainable development norms in its domestic laws. When investors act through local companies or in a joint venture with the host State and domestic law is less advanced, contracts could impose a minimum standard obligation, also on the part of the State, regarding the respect for internationally recognised human rights, or still strive for the highest attainable standard. On the side of investors, respect of international standards may be achieved by imposing (via contract or a code of conduct) liability on the parent company for breaches of ESG obligations by a local company.[48] An area for further work was also how the parent company that signed the framework contract would ensure the respect of the agreed standards on policy goals by subsidiaries implementing the contract or any other outsourcer that is not party to the IIC.

106. The contract may specify the consequences in case the State or the investor does not comply with obligations deriving from policy goals (e.g., relief from certain obligations or the timing thereof). In case of a contractual breach, the remedies for non-performance would be applicable, which include withholding of performance and, as last resort, termination of the contract. Alternative methods for the enforceability of the remedies could be addressed contractually, e.g., dispute resolution mechanisms that would facilitate enforcement. In case of a State's breach of an obligation, the investor could be entitled to suspend performance, but it was raised that this is not always permitted under domestic laws (e.g. public services). These aspects should be examined against the backdrop of domestic laws to see to what extent the development of contractual remedies is possible. The relevance of non-judicial mechanisms such as the OECD National Contact Points (NCP) could also be examined in order either to identify areas of interest and derive indications to draft model clauses or to consider active behavioural change as a an alternative (contractual) remedy. Other tools to be

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[44] For instance, the current UN Sustainable Development Goals (SDGs) were part of the 2030 Agenda for Sustainable Development, but thinking has started about the next generation of goals.

[45] The options should include a general model clause, followed by a set of more specific model clauses that could address specific SDGs or specific standards of the industry. It would be hardly possible to provide equally detailed guidance in all ESG fields since the level of specificity has increased over the years with regard to environmental provisions (EIA, due diligence), while social and governance obligations might be less developed.

[46] See, e.g. Chapter 4.II, lett. B, of the ALIC Guide, e.g. the section on "(E)mployment creation, access to jobs and labour rights", particularly paras 4.70 to 4.82 providing guidance on contractual provisions relating to job creation, targets on employment creations, labour relations, and the like. The ALIC Guide also provides guidance on how local and indigenous communities may be involved in the negotiation of an IIC since the early phase. International standards provide that the investor and the host State may include in their contracts some methods to protect third-party rights, such as consultations, grievance mechanisms or human rights monitoring mechanisms in accordance with existing international business responsibility practices.

[47] The IISD published a list of model clauses designed to integrate principles on responsible business into agricultural contracts.

[48] In this regard, the Annex to the Proposal for a Directive on EU Corporate Sustainability Due Diligence is a benchmark since it contains a comprehensive list of rights and prohibitions enshrined in international human rights agreements that could be imposed on companies: see the Annex to the Proposal of the European Parliament and the Council for an EU Directive on Corporate Sustainability Due Diligence (Brussels, 23.2.2022 COM(2022), 71, final).

examined might be monitoring and grievance mechanisms integrating affected third parties interests and mediation or arbitration rules on business and human rights.

107. It was discussed that the contents of recent IIAs/BITs should be inquired into, including the need for investors to comply with domestic law and regulations (e.g., concerning human rights) and encouraging investors to voluntarily incorporate internationally recognised standards into their business practice and internal policies (e.g., the OECD Guidelines for Multinational Enterprises and the UN Guiding Principles on Business and Human Rights). The legal relationship between these standards and contractual provisions should be clarified and how policy goals related to dispute settlement, i.e., if they had an interpretative function and/or they could lay down rights and obligations, based on a general obligation to comply with the laws and regulations of the host State or on a contractual commitment of the investor to comply with its own code or standard. The risk allocation between a State and a private investor was also relevant in case of breach of an ESG obligation.[49]

108. So far, the Working Group did not discuss other impactful policy trends such as digitalisation policies,[50] including issues such as data protection, cybersecurity, and localisation requirements on IICs,[51] and policies that incentivise SMEs to enter the investment arena.[52] IIAs and BITs currently do not differentiate protection standards between large enterprises and SMEs. However, some IIAs contain specific provisions dedicated to SMEs that underline the need for cooperation between parties to further promote SME development.[53] The Working Group may wish to consider whether to provide specific guidance that would facilitate the access of SMEs to the global market for investments, particularly: (i) joint venture and/or other forms of association-related clauses or contracts as a basis to participate in or be associated with investment operations ("multi-party contracts");[54] (ii) multi-tiered dispute settlement clauses including ADR (conciliation, mediation, good offices), on the model of the CETA, as a means to reduce the costs of investment arbitration.[55] The work of UNICTRAL Working Groups I (Micro- and Medium Size Enterprises) and III (ISDS) should be taken into consideration in this context.

109. Subgroup 3 proposed in its Report for the second Working Group session to conduct work based on two objectives: (i) compliance with host State's public policy, and (ii) conformity with the highest international standards; and to implement these objectives in three areas: (1) pre-contractual documents, (2) the preamble, and (3) the contract itself. The Report also included a work plan proposing to conduct a preliminary mapping of: (1) relevant international standards, (2) policy goals in IIAs and Model IIAs, (3) areas of interest by contractual phase or IIC content, (4) relevance of the UPICC and ALIC Guide, (5) possible other IIA standards to be addressed contractually.

110. During its second session, the Working Group generally agreed with the work plan and discussed how it would be useful to develop clear guidance to help contracting parties understand the scope of their ESG obligations. It was agreed that such guidance should cover the pre-contractual

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[49] For instance, a question might be how to allocate the risk in case the investment site is occupied by third parties as a protest because of the alleged impact of the project on climate change.

[50] See OECD, 2021, p. 38.

[51] *Ibid*.

[52] SMEs usually constitute a large percentage of the businesses in a country and make a most significant contribution to GDP, but they often do not to engage in cross-border investment.

[53] See, e.g., Article 37 Tunisia-Turkey FTA.

[54] UNIDROIT's Project on Collaborative Legal Structures for Agricultural Enterprises is examining the role of "multiparty subjects" as legal tools to improve the aggregation and coordination of agricultural enterprises through the use of contractual networks and the development of corporate governance rules. The Project is considering in particular the option of multiparty contracts as well as legal entities such as cooperatives, corporations, consortia, producer groupings and others (see https://www.unidroit.org/work-in-progress/legal-structure-of-agri-enterprise/).

[55] See the EU-Canada Comprehensive Economic and Trade Agreement (CETA), Art. 8.19, para. 3; Art. 8.23, para. 5; Art. 8.27, para. 9; and Art. 8.39, para. 6.

phase (e.g., due diligence and consultations with local communities), the preamble of an IIC, and provisions in the IIC (e.g., specifying the ESG obligations of parties and consequences in case of non-compliance). The point was raised that consistency should be ensured with the work of other organisations in this area. Furthermore, a level playing field was important; caution was expressed about an approach that would lead foreign investors to be subject to higher standards than local investors. The Working Group also discussed possible guidance on performance in the future instrument (e.g., issues that led to a delay in performance or payment). It was finally considered that any work proposal should balance the need for concrete and specific guidance with the necessity for the instrument to be "future-proof", i.e., not be easily outdated by the continuing evolution of relevant standards, which required a certain degree of generality.

111. In the discussions led by Subgroup 3 for the third Working Group session, key issues highlighted included the need for a sufficiently broad definition of "investor" (emphasising that multinational corporations should be responsible for ESG compliance throughout their value chains, including subcontractors), different approaches across jurisdictions concerning "single" *versus* "double" materiality (with the Working Group suggesting to consider both approaches), and the role of both host and home State laws. Additionally, it was proposed to incorporate the principle of cooperation in good faith in the preamble of IICs, and to consider the role of due diligence in light of relevant international guidance and the EU's Corporate Sustainability Due Diligence (CSDD) Directive. It was also suggested to consider the World Bank's conditions on environmental and social requirements for projects financed by the World Bank.

112. Several participants considered that ESG principles should be included not only in the preamble but also in the main text of IICs to create rights and obligations. Additionally, there was consensus on the long-term nature of IICs and the resulting need for continuous ESG monitoring over the life of the investment. Participants referenced the OECD National Contact Points (NCPs) as a framework to promote transparency and stakeholder engagement in investment projects. However, concerns were raised regarding the voluntary nature of OECD guidelines and the need for more robust mechanisms for enforcing compliance with ESG standards.

113. Regarding the interplay between home State laws and their impact on investor behaviour in host States, the Working Group highlighted the need for an adequate balance, to avoid issues of competition and deterring investments. Participants also raised issues of transparency, stakeholder involvement, and accountability, including the use of informal dispute resolution mechanisms. There was broad consensus on the need for IICs to address ESG compliance in a balanced yet comprehensive manner, ensuring that investors and States shared responsibilities for upholding these standards throughout the life cycle of the investment.

114. Subgroup 3's Report contains proposed text for the Introduction of the future instrument, a draft preamble for IICs (emphasising the importance of a cooperative approach between investors and host States to achieve shared ESG goals, while ensuring flexibility for sector-specific issues), and a draft Sustainability Due Diligence Clause, which requires investors to assess, prevent, mitigate, and monitor the environmental and social risks of investment projects. The Report also highlights the need for anti-corruption clauses based on a wide array of international instruments. The proposals of Subgroup 1 aim at creating a robust and adaptable framework that ensure responsible investment, supporting long-term sustainable development.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the proposals of Subgroup 3.*

G. Principles and clauses addressing "change of circumstances"

115. At its first session, the Working Group discussed at length the function and relevance of stabilisation and readaptation clauses, including clauses that provide for the restoration of economic equilibrium *per se* and their interrelationship with hardship and force majeure clauses. It was discussed that issues behind stabilisation/readaptation were connected to some extent with the notion of hardship: grey areas may exist between the two and therefore the approach to both concepts should be consistent. It was also considered that the consequences of hardship, force majeure, and the breach of stabilisation clauses might be similar to some extent since there was a tendency under general contract law and in IICs practice, especially for long-term contracts, to keep the contract alive in case of supervening events (e.g., by introducing renegotiation as an option even in cases of force majeure). In addition, it may be difficult to discern cases of hardship from cases of force majeure in practice (see Study L-IIC – W.G. 1 – Doc. 2, Part IV.F.1).

116. This prompted the decision that, regardless of their different formal qualifications (rights and obligations, performance/non-performance), Subgroup 2 was to examine stabilisation, hardship and force majeure under the common heading of "change of circumstances."

1. Stabilisation and adaptation/renegotiation clauses

117. In general, during the first Working Group session it was agreed that the future instrument should provide guidance on "stabilisation" clauses. IICs are normally long-term contracts where there is a substantial sunk-in cost and returns on investments are possible only after a certain gestation period. Stabilisation clauses provide a fundamental protection mechanism for investors when States adopt legislative or administrative changes in a manner that affects the terms of the contract or make the functioning and profitability of the contract impossible. On the other hand, it was also noted that the function of "stabilisation" may differ from country to country, that such clauses may provide constraints on States' regulatory powers in the public interest (especially, climate change), that they evolved over time (particularly, into "adaptation" and "renegotiation" clauses), and that stabilisation clauses might not be accepted in certain legal orders, so that other mechanisms may be available to pursue the same goals. During the intersessional work of Subgroup 2, reference was made, for instance, to insurance mechanisms covering legislative change costs and risk diversification through agreements with international lenders.

118. Areas for work identified during the first session included: (i) categorising "legislative changes" and their impact, i.e., modification of industry standards, changes to the fundamental legal framework (e.g., climate change or human rights), with a distinction between those imposed by international obligations and those spurred by States' discretionary policy; (ii) geographical scope of protection (in the host State and in other jurisdictions connected to the investor/investment); (iii) limitations to the material scope of protection (increased cost thresholds to trigger protection, areas of legislation included or excluded, administrative act or practices, case law).

119. During the second Working Group session, it was reiterated that a stabilisation regime would be necessary as a sort of "FET of investment contracts" to ensure certainty to investors in the medium and long run, while being shaped in a manner that would not encroach upon States' sovereignty in any circumstance, mirroring several emerging principles in IIAs/BITs and model agreements, possibly by incorporating a carve-out in a future model clause. A "one size-fits-all" approach would in any case not do justice to the need to consider different needs and legal frameworks in different areas of the globe. Paramount importance was given to specifically define the scope of a possible model stabilisation clause, with different options, identifying with clarity the formal acts that would fall within its field of application (laws, decrees), the notion of "alteration of economic equilibrium" in relation to those acts and particularly how to calculate the effects of the measure, the necessary connection between stabilisation and adaptation/renegotiation, which remedies would follow (if

monetary compensation or continuous renegotiation), and which role and powers would be envisaged for arbitrators in the renegotiation, if any.

120. Subgroup 2 identified in its Report for the third Working Group session three types of stabilisation clauses: (i) "freezing clauses", i.e., classical stabilisation clauses that have a freezing effect on the entire State legal framework, which means that after the date of the agreement States cannot make regulations that affect the investor in any manner; (ii) "fiscal stabilisation clauses", i.e., clauses with similar effect as the freezing clauses but only on fiscal laws which may take different form (exclusion of all taxation also by reimbursement, exclusion of certain taxes of the power to increase taxes, limitation of the power to increase taxes beyond a certain level); and (iii) "economic equilibrium clauses" (or "stabilisation and renegotiation clauses" or simply "renegotiation clauses"), i.e., modern stabilisation clauses entailing that, if there were certain trigger events such as a change to the legal, fiscal or economic framework that results in the alteration of the economic equilibrium of the contract, the parties have to renegotiate in good faith to restore the economic equilibrium (by compensating the investor or any other measures ensuring that the economic equilibrium is sustained). It was recalled that freezing clauses had been subjected to harsh criticism and were out of practice in the oil and gas industry. Fiscal stabilisation clauses were supported by the United Nations Office of the High Commissioner for Human Rights (OHCHR) Principles on Responsible Contracts and the OECD Guiding Principles for Durable Extractive Contracts. The ALIC Guide supported the use of economic equilibrium clauses, while it expressly rejected the use of freezing clauses.

121. The Report of Subgroup 2 for the third Working Group session did not contain one specific proposal on "stabilisation" given the divergent views within the subgroup. It did contain two annexes with proposed approaches on stabilisation (a note on non-automatic and limited fiscal stabilisation and a note on stabilisation in general).

122. During its third session, the Working Group agreed that "freezing clauses" should be disregarded in view of their ability to contractually constrain a State from changing its laws, which was not desirable nor legal in all jurisdictions. Instead, the Working Group favoured a balanced approach and requested Subgroup 2 to provide different options for contracting parties to consider, depending on the circumstances. Subgroup 2 emphasised that the Working Group should agree on a general approach before model contract language could be developed.

123. In its Report for the fourth Working Group session, the Co-Chairs of Subgroup 2 developed general text on stabilisation clauses, accompanied by different proposals submitted by individual Subgroup participants in the Annexes to the Report. Options on stabilisation for consideration by contracting parties included (i) no stabilisation clause (with a proposal for a draft Model Clause specifying that the State was not prevented from amending its law), (ii) an economic equilibrium clause, (iii) a stabilisation and/or renegotiation clause accompanied by a clause that excluded certain measures from its scope (e.g., measures adopted by a State to comply with obligations under international law), (iv) a limited fiscal stabilisation clause. Further options such as insurance and alternative measures were deemed to deserve consideration, too.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the updated proposal of Subgroup 2.*

2. Hardship clauses

124. During the first Working Group session, the participants expanded on the relationship between stabilisation and hardship clauses, exploring the grey areas between the two and in particular to what extent hardship clauses might tackle the typical economic and legislative risks that are covered by stabilisation clauses in IICs. A main difference between stabilisation and hardship

was found in that hardship is caused by a wider set of changes of general application in the dynamics of the market, such as a surge in the price of raw materials, while stabilisation clauses would expressly address changes related to the contract, and particularly legislative changes affecting the contract. In general, hardship would be triggered by external events, i.e., events beyond the control of the contracting parties, while stabilisation clauses concerned changes that were within the control of one of the parties, namely the State. In light of the wording of Article 6.2.2(c) of the UPICC on the "(D)efinition of hardship", which considers "*events beyond the control of the disadvantaged party*", an issue was whether, it was considered that, in theory, a legislative change affecting the costs of an IIC would trigger a hardship clause in favour of the investor. However, due attention was given to the fact that the threshold to trigger a hardship clause is high, since the elements in Article 6.2.2 would need to be met cumulatively.

125. It was finally held that, in principle, in light of the "typicity" of the risk of a State's unilateral change of its legislative framework, an IIC would require including both a stabilisation and a hardship clause to cover all types of risks. The future instrument could provide distinct guidance on both types of clauses, allowing the contracting parties to select those they wished to include. Use of hardship clauses may be implemented by specifying open-ended formulations ("any change" in circumstances) to cover specific risks or by using index clauses (e.g., to address the impact of inflation).

126. It was generally agreed that the future agreement should build on the UPICC principle on hardship, which already contained useful guidance, including on the consequences and remedies. Areas to explore would be: (i) the notion of "economic equilibrium" of the contract; (ii) solutions in case renegotiation failed (e.g., a possible role for the arbitral tribunal to adapt the contract with a view to restoring its equilibrium). While hardship provisions in the UPICC required a fundamental change of the "equilibrium of contract", a more economic approach might be warranted for IICs, so that any factor that might change the equilibrium may give course to renegotiations and/or to (arbitral) adaptation.[56] Time extension, cost protection, contract renegotiation and adaptation were common remedies for hardship and similar clauses, in concurrence with a duty of mitigation of damages.

127. During the second Working Gorup session, it was considered that the trigger event for hardship required to "fundamentally alter the equilibrium" of the contract, setting a high threshold (with cost and value of the performance as relevant benchmarks) that might need adaptation in the context of IICs and particularly a broadening of its scope. The notion of economic equilibrium, which in commercial contracts had to do with the costs of parties' performance, in the context of IICs would rather refer to the project's cash flows. Court procedures might not be appropriate in the context of IICs and a preference was expressed for arbitration. A framework for adaptation should also be provided, possibly taking into account the relevant ICC Model Clause, including parameters to guide adaptation/renegotiation. A doubt remained as to whether any act of the State that changed or influenced the rate of the guarantees elevating the costs of the contract, as something conditioning the market dynamic, would fall under stabilisation or hardship. It was finally considered that such a hypothesis might fall within both and guidance should be provided in this regard for the sake of clarity.

128. The Report of Subgroup 2 for the third Working Group session contains an Annexe relevant to hardship (a note on "relational contract theory") and proposals for a Principle, Commentary, and a Model Clause on hardship presenting different options. As to the Principle, Subgroup 2 proposed to

[56] Guidance as to renegotiation, adaptation and, as a possible ultimate consequence, contract termination, may be taken from the Commentary to Principle IV.6.7 of the TransLex Principles, which refers to the concept of "commercial equivalence" rather than "economic equilibrium" and contains guidelines the contracting parties should consider in a renegotiation process. Innovative guidance as regards renegotiation, and indeed alternative means to settle differences both by private and public bodies such as mediation, third-party facilitation, and conciliation procedures in the context of hardship, may be found in the UNIDROIT/FAO/IFAD Legal Guide on Contract Farming.

conduct work on three sections based on articles 6.2.1-6.2.3 of the UPICC with some adaptations and suggestions for further discussion and changes: (i) contract to be observed (obligation to perform), (ii) definition of hardship (trigger event of the fundamental alteration of equilibrium of contract), (iii) effects of hardship in IICs (renegotiation of the contract, compensation for losses, procedural elements).

129. In the third session, the Working Group raised several topics for discussion regarding the draft Principles on hardship, especially on the requirements and effects, *inter alia*:

(1) the (ir)relevance of the word "temporary" in regard to the nature of the fundamental alteration (draft Principle 2(e)) – it was agreed that, as an implied condition, the reference could be excluded;

(2) the mechanisms and timing for determining the "equilibrium intended by the parties", if at the conclusion of the contract or before the event, especially considering that IICs were usually long-term contracts (draft Principle 3(1)(a) and paragraphs 25-27 of the Commentary);

(3) the allocation of risks between the State and the investor (draft Principle 3(1)(b));

(4) whether a claim for compensation (State and/or investor) should be allowed and, if so, what criteria should be used to calculate the amount due (i.e., "past" losses, "future" losses or both);

(5) the need to include in the Commentary an explanation as to when withholding performance would be allowed (draft Principle 3(5)).

130. For the fourth session, Subgroup 2 submitted an updated Report on hardship clauses considering the considerations that had been raised by the Working Group in the third session.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the updated proposals of Subgroup 2 on hardship.*

3. Force majeure clauses

131. During the first Working Group session it was generally agreed that force majeure is widely recognised across jurisdictions. A force majeure clause was deemed necessary in addition to stabilisation/hardship for cases in which the performance had become impossible. Guidance on a force majeure clause should cover prolonged force majeure events, which could affect the economic equilibrium of the contract, and the timing for triggering termination rights, as well as the notion of *fait du prince*[57] and the link between force majeure and investment treaty arbitration, especially the "necessity" defence.[58] The link could also be examined between "force majeure" and cases where the State was obliged to regulate in the public interest (public health or environmental emergency). An area for work could consist of providing guidance on the possible role of insurance for investors and the question of "uninsurable risk", e.g., when a facility is destroyed by an unforeseeable event

[57] Guidance on force majeure, including on the "*fait du prince*" theory, is available in Chapter 4 of the UNIDROIT/FAO/IFAD Legal Guide on Contract Farming. E.g., as regards the categorisation of relevant events (natural events, governmental acts, internal or external disturbances such as strikes, war, social unrest and market disruptions), the formulation of relevant clauses in relation to risk allocation and the legal consequences (excuse for non-performance, suspension of performance, compensation and indemnity, additional obligations such as notice and mitigation requirements, termination of the contract, right to renegotiate, judicial adaptation).

[58] The necessity defence has been invoked in the context of the financial crisis in Argentina and raises the question of the extent to which it would be possible to contract out of customary international law rules. In principle, if a State is entering into a contract as a commercial legal entity based on domestic law, some of the issues arising from customary international law would not apply.

beyond parties' control before the handover to the State, the question arises who would bear the costs.[59]

132. During the second Working Group session, there was general agreement that article 7.1.7 of the UPICC would be a good starting point, but it might need adaptation in the context of IICs considering its broad scope and the need to preserve the continuity of long-term contracts. A list of events, exhaustive or open-ended, might add clarity. The difference between a temporary and a permanent force majeure event, the latter leading to termination, should be inquired in the context of IICs with a view to ensuring the preservation of the investment relationship once the event dissolved. Several issues were considered: what should be proven to avoid non-performance and thus liability and the payment of damages; how to clearly define a force majeure event, whether of short duration or long duration; how to consider the consequences when the duration of the force majeure event was so long that it would result in a lack of financial equilibrium (e.g., suspension of the cash flow, rising prices in the medium run, etc.); what occurred if there was a failure to give notice on time; and what the consequence of not complying with the notice would be.

133. The Report of Subgroup 2 for the third Working Group session contained two Annexes relevant to force majeure (a note on "relational contract theory" and a note on force majeure) and a proposal for a Principle, Commentary, and a Model Clause, following the tripartite format.

134. In the third session, a participant had raised doubts concerning the need to amend UPICC provisions on hardship and force majeure for IICs. It was suggested that their use in practice had already demonstrated that they were appropriate for IICs in their "original" form. The UNIDROIT Chair requested that Subgroup 2 carefully consider whether adaptations to the UPICC were necessary. In any case, the Working Group raised two topics for consideration regarding the draft Principles on force majeure:

(1) possibly including a specification in the Model Clause to clarify what would happen if the party affected by the force majeure failed to notify the other party;

(2) specifying the conditions in which termination of the IIC was authorised (clarifying that termination was meant to be a last-resort measure).

135. For the fourth session, Subgroup 2 submitted an updated Report on force majeure considering the comments that had been raised by the Working Group in the previous session.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the updated proposal of Subgroup 2 on force majeure.*

H. Compensation and damages

136. At its first session, the Working Group agreed that IIAs/BITs generally left sufficient flexibility for the future instrument to provide specific guidance on remedies, including compensation and damages. IIAs mainly focused on arbitration and monetary damages, with a lack of guidance as to how to salvage the contractual relationship and how a monetary sum should be calculated. There was then a significant opportunity to provide guidance for contracting parties to consider alternative remedies and methods of dispute resolution with a view to preserve the contractual relationship and to examine criteria for the calculation of compensation and damages as a last resort. As to the interaction between remedies, it was discussed that a clear hierarchy of steps or a default option, e.g., favouring renegotiation before turning to compensation and damages, could be established.

[59] In these cases, costs would be normally very high and unlikely to be covered by insurance. Principles could be extracted by arbitral jurisprudence (see, e.g., the arbitral case on the Channel Tunnel between England and France).

137. It was discussed that the following should be explored: (i) limitation of liability clauses (together with a general principle on the prohibition of punitive damages), and (ii) liquidated damages clauses as a means to set boundaries in this area and enhance legal certainty. In this regard, consideration could be given to the principle of proportionality, contractual caps, and the duty to mitigate harm, together with a general principle that the amount of claimed damages should be linked to the timing of the investment to avoid the risk of extraordinary awards of damages. Work on the exclusion and limitation of liability clauses should consider clauses that excluded liability for "consequential loss", an important protection mechanism for investors[60] given that such types of losses could hardly be insured. Guidance on these topics may be found in the UPICC, especially in article 7.4.8 (mitigation of harm), article 7.4.13 (agreed payment for non-performance), and article 5.2.3 (exclusion and limitation clauses), as well as in the ALIC Guide. The UPICC may also provide guidance on issues of interest and currency that have an impact on the calculation of damages.

138. Issues of compensation and damages are closely related to the applicable law.[61] The determination of compensation and damages may depend, indeed, on the legal nature of the contract (e.g., a State contract or commercial contract) and on the approach in a specific jurisdiction. Liquidated damages might be limited to actual loss in certain jurisdictions, while in other jurisdictions the amount was established regardless of the actual loss or whether it had a punitive nature. Therefore, guidance in this area should cover issues of applicable law.

139. In its Report for the fourth Working Group session, Subgroup 1 examined the UPICC provisions on non-performance, right to performance, termination, and damages to see whether any adaptations or additional guidance would be required. The Report contains a draft Commentary for each of these UPICC provisions, as well as suggestions on whether, and if so how, to develop Model Clauses as a next step.

Suggestion for the Working Group:

- *The Working Group is invited to discuss the proposals of Subgroup 1 on remedies, including compensation and damages.*

I. Transfer of rights and obligations under the contract and return of rights

140. So far, the Working Group has not discussed issues of transfers of rights and obligations in detail (assignment of the contract, transfer of rights from an investor to another investor or third parties, return of assets). At the first Working Group session, the argument was raised that the future instrument should not develop guidance on the transfer of rights and obligations under the contract (including the return of rights) since this would be contract-specific and should be left to the contracting parties. An area for work might be how to cover the possible assignment of claims against the State to third parties (e.g., litigation funds) in the future instrument.[62] The question would relate to issues of immunity of State property and would raise aspects of transparency to consider, such as the disclosure of the involvement of a third party. In addition, it was discussed that the assignment of rights might be subject to the consent of the State party. The existing guidance in the ALIC Guide could be useful for the possible development of model clauses on this topic.

141. This subtopic was allocated to Subgroup 1, which did not start work in this area yet.

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60 This type of clauses is often used in IICs concerning construction and infrastructure projects.

61 In an arbitral case, in which a breach of an IIC had amounted to a breach of a BIT and the arbitral tribunal had resorted to general principles of international law to determine the compensation, the award was subsequently annulled because the contract was governed by domestic law and contained a numerical cap on compensation.

62 The topic might be covered to some extent by UNCITRAL, which is undertaking work on third-party funding.

Suggestion for the Working Group:

- *The Working Group is invited to provide a mandate to Subgroup 1 or the Drafting Committee to explore this subtopic and consider whether any adaptations to the UPICC (Chapter 9) would be useful.*

J. Legal framework and applicable law

142. At its first session, the Working Group was invited to discuss the legal framework applicable to IICs, with special regard to issues of choice of law and the question of the possible application of international or transnational law and principles to investment contracts, including the application of the UPICC (as they are or as adapted) and their relation with the application of the law of the host State (see Study L-IIC – W.G. 1 – Doc. 2, Part IV.H.1)

1. The legal relationship between IIAs/BITs, including newly emerging standards on public policy goals, and investment contracts

143. At its first session, the Working Group did not address the legal relationship between IICs and investment treaties (IIAs/BITs) in the wider framework of public international law, if not in the context of the discussion on "contractualising" treaty protection standards. IIAs and BITs are different in nature from the private law of contracts, being public law standards internationally negotiated between States, that private investors may invoke before arbitral tribunals in treaty arbitration. However, depending on their content (as well as the content of the relevant contract) and on their quality and status in the legal system of the host State, IIAs/BITs might be considered as part of the legal framework applicable to IICs, both as "nationalised" international standards and/or as norms which define the normative playing field with which IICs have to comply.

144. Issues of applicable law to IICs and the legal relationship between IIAs/BITs and IICs were discussed in a preliminary manner during the second Working Group session, based on the Report of Subgroup 0 for that session.

Suggestion for the Working Group:

- *The Working Group is invited to provide a mandate to Subgroup 0 or the Drafting Committee to develop concise guidance on the relationship between IICs and IIAs/BITs as part of the Introduction of the future instrument (see Annexe II).*

2. Party autonomy and choice of law: the UPICC (or an adapted version) and other principles of international or transnational law as the law applicable to IICs

145. The Working Group discussed at length aspects of applicable law, reviewing the most relevant issues from different viewpoints. It was agreed that it was often consequential to the investment being located in a certain country that the law of the host State was considered the most closely connected to the investment and thus was often chosen as the law governing the contract. This was also the case when the law of the host State was imposed as the law governing the contract as part of a public tender process, or when it was mandatorily provided as the applicable law in certain sectors (e.g., oil and gas) by the law of the contracting State given their importance for the State's economy.[63]

146. Nevertheless, it was also raised that transnational principles might play an important role in this area and that the room for international and transnational law principles was progressively increasing in contract practice, e.g., in South America. Transnational principles, indeed, may serve as a neutral applicable law *in lieu* of, or in combination with, the law of the host State, thereby

[63] See, e.g., South Africa.

"transnationalising" the contract. The injection of transnational law principles in the law governing IICs, as well as the international arbitration clause, served the purpose of detaching, to some extent, the investment relationship from the law of the host State and added some level of neutrality to the contract, often in the interest of the foreign party. Arbitral tribunals often resorted to international law, sometimes even in cases in which parties had made an express choice for domestic law.[64]

147. A first area to explore was that of freedom of contract and party autonomy, i.e., if the parties were free to choose the law applicable to the contract, including transnational law ("non-State law"), and what would happen if a choice of law was absent or ineffective.[65] Freedom of contract and party autonomy would define the conceptual framework universally accepted for commercial contracts,[66] but IICs might require to abide by the principle of "legality" since the State was subject to the boundaries of its own domestic law and could agree to a certain governing law only if it was allowed to do so by its domestic law. In this case, the administrative law in the domestic law of the host State might apply, depending on national legal constructs concerning IICs and the relationship between domestic law and international law. In any case, even if the parties would be found to enjoy freedom to choose the applicable law, including transnational principles, they could not escape the application of mandatory rules in the host State.

148. A second area of work was to explore the complementarity between national and international law (see e.g., Article 42 of the ICSID Convention),[67] and to consider whether this would be appropriate for IICs. If a stance was taken in this sense, the future instrument – as well as the choice of law clause – should clearly set out the interrelationship between the two.[68] In contrast, if a purely international law-based approach was taken, if any choice was made by the parties or any indicator was in place that pointed at transnational law, the contents of the law of the host State may be deemed by the arbitrators of limited relevance.

149. A third area to explore was to what extent the UPICC and the future instrument could be (i) chosen as applicable law by the parties, (ii) incorporated as terms of the contract, and (iii) used to interpret and supplement the applicable domestic law. It was discussed that the UPICC Model Clauses for the use of the UPICC in international commercial contracts might be useful for the development of model clauses. The future instrument, as a soft law instrument, could provide model clauses with different options regarding the choice of the applicable law. Due regard should be given to the difference between the law applicable to the procedure and the law applicable to the substantive provisions of the contract.

150. During the second Working Group session, it was held that the UPICC as a manifestation of transnational law were not a departure *per se* from domestic law, but were meant to strike a fair balance between domestic and transnational law and elaborate rules fit for the needs of international economic relationships. States often required investors to include host State law compliance clauses in their contracts. Then, a full delocalisation of IICs would not serve the purpose of having in place enforceable contracts. The challenge was to acknowledge party autonomy as an integral element, but also the consequences of a State being party to a contract while being bound by its mandatory laws, also to ensure contract enforceability. IICs required a certain degree of independence from the domestic law to protect the private party against changes in law, discrimination, and unlawful

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64 See the award in the case Texaco Overseas Petroleum Company v. The Government of the Libyan Arab Republic (January 1977).

65 Usually, it would be for arbitrators to choose based on connecting factors and transnational principles.

66 See in, this regard, Article 11 of the HCCH Principles on Choice of Law in International Commercial Contracts.

67 Article 42 of the ICSID Convention reflects a balanced approach towards the role of domestic and international law. ICSID has conducted a study on the application of ICSID rules to contract-based arbitration, which would be published in the near future.

68 Domestic law and international law might be closely related since aspects of international law might be incorporated in the domestic law.

treatment that would be deemed lawful under the host State law; however, the State needed to consider public interests. International and domestic law should be viewed as complementary. More bodies of law may be reconciled for the future interpretation, application and enforcement of the contract.

151. In the third session, the Working Group discussed multiple aspects of choice of law clauses, based on the Report of Subgroup 4 for the third session. Topics for discussion included whether to offer different types of Model Clauses and what the hierarchy should be, if any, between different legal sources (with different views being expressed on *dépeçage*). It was clarified that Model Clauses under this subtopic would govern the contract and should be distinguished from dispute resolution clauses. The Working Group showed strong support for promoting the UPICC as a neutral, supplemental option vis-à-vis domestic law. It was suggested to clearly explain the benefits of applying the UPICC for both investors and host States. The participants also discussed whether or not *renvoi* should be explicitly excluded (i.e., excluding conflict of laws rules from the scope of choice of law clauses). Most participants supported such exclusion, which was common practice and in line with existing frameworks such as the Principles on Choice of Law in International Commercial Contracts of the Hague Conference on Private International Law. Finally, for countries with federal systems, it was recognised that it would be important to specify whether federal or State law applied.

152. For the fourth session, Subgroup 4 submitted an updated Report on choice of law, considering the suggestions that had been made by the Working Group in the third session, accompanied by draft Model Clauses.

153. The Report emphasises that the law governing an IIC served a critical role in guiding interpretation of the contract and filling contractual gaps. Without a designated legal framework, interpretative uncertainty might arise, and even detailed IICs often required supplementary rules. The Report of Subgroup 4 outlines several choice of law options: (i) the future instrument, (ii) the UPICC, (iii) the law of the host State, (iv) the law of a third State.

154. The Report acknowledges that it is common in IIC practice to combine different sources of law. Therefore, it also provides draft Model Clauses that combined domestic law with international law. Drawing from Article 42 of the ICSID Convention, draft Model Clause B.1 would ensure that the application of domestic law was compatible with international treaties, rules of customary international law (e.g., the prohibition of expropriation without compensation), and general principles like good faith. The wording of draft model Clause B.2 was taken from the Model Clauses for the Use of the UPICC and would ensure that gaps in the applicable law were filled through transnational principles or *lex mercatoria* rather than domestic law. The Report recalls the previously-discussed modes of interaction when different sources of law are combined (e.g., *dépecage*, hierarchical prioritisation, complementarity, or using the second source of law as interpretative guidance). An additional manner of interaction would be the use of mandatory law clauses, such as Article 1.4 of the UPICC, to recognise that certain rules – domestic or international – apply regardless of parties' choice of law.

Questions for the Working Group:

- *Do the different proposed Model Clauses provide parties with sufficiently clear and diverse options?*
- *Should additional options be added?*
- *With respect to domestic law, should the Model Clause(s) explicitly include/exclude conflict-of-law rules?*
- *With respect to international law, should the Model Clause(s) specify which rules are considered applicable and/or how the applicable rules can be identified?*

- *Should specific soft-law instruments be included in the Model Clause(s)?*
- *Should a "mandatory rules" clause be included?*

K. Dispute resolution clauses

155. Although arbitration procedures are outside the scope of the Working Group's mandate, this topic should be examined in the context of this project from a purely contractual perspective, i.e., to the limited extent needed to formulate an appropriate dispute resolution clause. The initial Issues Paper proposed drafting a model clause for dispute resolution and exploring the potential inclusion of provisions addressing criticism against ISDS, such as conflicts of interest, transparency, and meeting the present demand for ADR, including fast review of decisions, expert determinations, consultations, good offices and mediation. It was noted that the Working Group might rely on the significant experience of the ICC International Court of Arbitration in the administration of disputes on IICs. The Working Group was also invited to take into consideration the work of other IOs.

156. Subgroup 4 initiated its work on dispute resolution after the second Working Group session. On occasion of the second session, the participants had discussed for the first time the practicability of developing guidance and the possible contents of a dispute resolution model clause for IICs. The IBA Guidelines on Conflicts of Interest in International Arbitration, the UNCITRAL Code of Conduct for Arbitrators in International Investment Dispute Resolution, and the UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration were mentioned as good starting points. In addition, the ICC Note to Parties and Arbitral Tribunals on the Conduct of the Arbitration under the ICC Rules of Arbitration laid out different measures regarding transparency and conflicts of interest. Emerging alternative dispute settlement tools in the infrastructure and construction industry, such as dispute boards (see the FIDIC Forms of Contract, fourth ed., 1987, article 67), and the use of so-called "grievance mechanisms" (e.g., by the World Bank) were also mentioned as a possible benchmark. The issue was raised of preserving the choice for conciliation and mediation in the sequencing of dispute resolution mechanisms by maintaining ADR voluntary. The Working Group also discussed the practicability of model clauses aimed at avoiding parallel proceedings between contract and treaty cases, while acknowledging the concerns about the validity of waiving treaty rights.

157. During the third session, the Chairs of Subgroup 4 emphasised that effective dispute resolution relied on dispute prevention, mitigation, and management. Key aspects discussed included the scope of Model Clauses and coordination of different dispute settlement mechanisms, the avoidance of parallel proceedings, and transparency and conflicts of interest. The Working Group was in favour of incorporating cooling-off periods and ADR options such as mediation, referring to the importance of the United Nations Convention on International Settlement Agreements resulting from Mediation for enforceable mediation outcomes. It was generally considered that mediation should be an optional step prior to arbitration, with possible "mediation windows" at different stages, and that dispute boards, which were commonly used in construction contracts, seemed less appropriate for concession agreements. Furthermore, reference was made to the complexities that might arise in case the investor was a joint venture, and possible solutions to address such challenges were suggested.

158. Discussions also covered third-party participation in dispute settlement (whereby it was recognised that the extent of "contractualisation" in this area depended on the type of third party and the type of proceedings), the avoidance of parallel proceedings, and counterclaims. Support was expressed for referring to the UNCITRAL Code of Conduct for Arbitrators and considering the UNCITRAL Rules on Transparency in Treaty-based Investor Arbitration. Finally, different views were expressed on whether or how to address State immunity, with some participants arguing in favour of clearly addressing this in the future instrument since it was a fundamental issue that had already been addressed in the ICC's Model Clauses.

159. The Report of Subgroup 4 for the fourth Working Group session contains proposals on dispute resolution for IICs, addressing key components to improve fairness, efficiency, and adaptability in resolving disputes. It contains proposals, including draft Model Clauses, on (i) negotiations, (ii) mediation, (iii) arbitration, (iv) counterclaims, (v) conditions and limitations on consent, (vi) notice requirements, (vii) 'fork in the road' and 'no U-turn' provisions, (viii) limitations periods, (ix) sovereign immunity, (x) transparency, (xi) professional codes of conduct, and (xii) non-disputing party submissions.

Questions for the Working Group:

- *What other issues should be addressed in a future instrument?*
- *Should a future instrument offer a Model Clause on domestic litigation?*
- *Should a future instrument address non-signatories or leave that issue to existing arbitral rules?*
- *Should respondents who file counterclaims be required to waive their rights to other dispute resolution mechanisms?*
- *Should a future instrument make clear that the subject matter of the agreement constitutes an investment (for purposes of the ICSID Convention)?*
- *Should a future instrument specify conditions/factors for a tribunal to consider when deciding to accept non-disputing party submissions, or should it rely on existing rules and jurisprudence for such guidance?*

ANNEXE I

ADDITIONAL RESOURCES

UNIDROIT Instruments

UNIDROIT / FAO / IFAD, Legal Guide on Contract Farming (2015)
https://www.unidroit.org/wp-content/uploads/2021/06/Contract-farming-legal-guide.pdf

UNIDROIT, Principles of International Commercial Contracts (2016)
https://www.unidroit.org/wp-content/uploads/2021/06/Unidroit-Principles-2016-English-i.pdf

UNIDROIT, Principles of Reinsurance Contract Law (2019)
https://www.ius.uzh.ch/en/research/pricl.html
UNIDROIT / IFAD, Legal Guide on Agricultural Land Investment Contracts (2021)
https://www.unidroit.org/wp-content/uploads/2021/10/ALICGuidehy.pdf

UNIDROIT / FAO / IFAD project on the Collaborative Legal Structures for Agricultural Enterprises
https://www.unidroit.org/work-in-progress/legal-structure-of-agri-enterprise/

UNCTAD publications

UNCTAD, World Investment Report, Reforming International Investment Governance (2015)
https://unctad.org/system/files/official-document/wir2015_en.pdf

UNCTAD, World Investment Report, International Tax Reform and Sustainable Investment (2022)
https://unctad.org/system/files/official-document/wir2022_en.pdf

UNCTAD-OECD Twenty-eighth Report on G20 Investment Measures (2022)
https://unctad.org/publication/unctad-oecd-report-g20-investment-measures-28th-report

OECD publications

OECD Policy Framework for Investment (2015)
https://www.oecd.org/daf/inv/investment-policy/Policy-Framework-for-Investment-2015-CMIN2015- 5.pdf

OECD, The Future of Investment Treaties: Possible Directions' (2021)
https://www.oecd-ilibrary.org/finance-and-investment/the-future-of-investment-treaties-possible-directions_946c3970-en

UNCITRAL publications

UNCITRAL Model Legislative Provisions on Public-Private Partnerships (2019)
https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/19-11011_mlpppp_e.pdf

Model Clauses

Model Clauses for the Use of the UNIDROIT Principles of International Commercial Contracts (2013)
https://www.unidroit.org/wp-content/uploads/2021/06/UPICC-model-clauses-English-i.pdf

ANNEXE II

DRAFT STRUCTURE OF THE FUTURE INSTRUMENT[69]

Below, a suggested draft structure for the future instrument is set out for consideration. It takes into account the aspects to be covered as discussed in previous Working Group sessions and considering the work of the Subgroups so far. The text included under the Chapter titles in bullet point form is not being proposed in the form of headings, but merely as a prompt for the future content.

Suggestion for the Working Group:

The Working Group is invited to consider the draft structure for the future instrument and propose any additional content that should be included, as well as any rearrangement of content as appropriate.

Issue addressed/goal pursued	Heading	Possible contents	Source/Relevant existing guidance
	Abbreviations *(Secretariat)*	• List of abbreviations used in the instrument	
Reasons for this exercise and (qualification of) specificities of IIC. The need for modernisation of IICs in parallel with IIAs A general framework that could make conditions more homogeneous across countries and type of business/size of activity	**Introduction**	• Background and aim of the instrument (*Subgroup 0*) (from BITs to IICs, including from FET to contractual protections) • Understanding of "IICs", including a non-exhaustive list of examples (*Subgroup 0*) • Relationship with the UPICC and other instruments (clarifying that only IIC-specific rules are set out in the instrument, with "renvoi" to the UPICC as uniform rules of general contract law as in the PRICL)[70] (*Subgroup 0*) • Relationship with IIAs and domestic law (*Subgroup 0*) • Structure of the instrument (*Secretariat*)	

[69] Version July 2024. The future instrument would consist of three main building blocks: (i) an introduction; (ii) thematic chapters containing introductory guidance, principles and commentaries; (iii) an annexe containing model clauses with short explanatory notes. The final document should be concise and provide a contractual framework for protection built around a limited amount of thematic areas.

[70] This section would explain the methodology followed in the preparation of the instrument (i) adapted UPICC, (ii) "renvoi" to non-modified UPICC with, where appropriate, guidance or commentary on the application of some specific UPICC to IICs, and (iii) IICs-specific principles. The guidance or commentary on the application of some specific non-modified UPICC would be placed at the beginning of each thematic chapter, as well as explanation on UPICC that would be deemed inapplicable to IICs. Please note that for each of the subtopics identified in the bullet points in this document the Working Group is expected to verify whether an adaptation of the UPICC is necessary or rather ICCs-specific guidance or commentary is sufficient, without any specific text adaptation of the relevant UPICC.

Principles concerning the instrument itself	**Chapter 1. General provisions concerning the instrument**	[intro] • Scope of application/purpose of the Principles (*Subgroup 4*) • Interpretation (*Subgroup 0*) • External gaps (*Subgroup 4*) • Exclusion or modification by the parties (*Subgroup 4*) • Usages and practices (*Subgroup 0*) • Definitions (*Subgroup 0*)	**Preamble UPICC** (Scope of application) **Art. 1.1.1 PRICL** (Scope of application) **Art. 1.6 UPICC** (Interpretation and supplementation of the Principles) **Art. 1.1.6 PRICL** (Interpretation and internal gaps) **Art. 1.1.2 PRICL** (External gaps) **Art. 1.5 UPICC** (Exclusion or modification by the parties): **Art. 1.1.3 PRICL** (Exclusion or modification of the PRICL) **Art. 1.9 UPICC** (Usages and practices) **Art. 1.1.4 PRICL** (Usages and practices) **Art. 1.11 UPICC** (Definitions) **Art. 1.2.1 PRICL** (Definitions)
General framework for the interpretation and performance of the IIC. **Right to regulate *versus* respect of international standards by investors.**	**Chapter 2. General principles applicable to IICs** (possibly to be reflected in their preamble)	[intro][71] • Freedom of contract • Form of an IIC • Good faith[72] (*Subgroup 1/3*) • Duty of cooperation • Respect for ESG obligations (*Subgroup 3*) • Principle of continuity • Reps & warranties methodology[73]	**Art. 1.1 UPICC** (Freedom of contract) **Art. 1.2 UPICC** (No form required) **Art. 1.7 UPICC** (Good faith and fair dealing) See also **ICC Model Clause on good faith and fair dealing** **Art. 5.1.3 UPICC** (Cooperation between the parties)

[71] If the Working Group considers that there are UPICC that either are deemed inapplicable to IICs or do not deserve modification but merely guidance on how they apply specifically to IICs, this would be included in the "intro", while the rest of the chapter would provide a set of principles, either modified-UPICC or IICs-specific principles.

[72] The Working Group is expected to provide guidance or commentary on how the principle of good faith could be used to provide some level of protection to foreign investors in a functionally similar manner like the FET.

[73] Representations and warranties methodology would help the parties to declare and certify they have complied with certain obligations and thus receive protection.

			Chapter 3 ALIC Guide (ESG, due diligence and affected third parties) **Art. 4.8 UPICC** (Supplying an omitted term) **Art. 5.1.2 UPICC** (Implied obligations) **Art. 2.1.14 UPICC** (Contract with terms deliberately left open)
Good faith and fair dealing in the pre-contractual phase. Non-discrimination. Commercial and ESG Due Diligence obligations, including the allocation of responsibility between the State and the foreign investor in the pre- establishment phase.[74] Transparency. Legitimate expectations caused by negotiations.	**Chapter 3. Pre-contractual phase**	[intro][75] A. Principles applicable to the pre-contractual phase (*Subgroup 1*) • Risk for own assumptions • Freedom to evaluate own interests (change of strategy or policy) • No liability for failure to reach an agreement • Mandatory rules • Pre-contractual aspects concerning policy goals (e.g., ESG due diligence and affected third parties and stakeholders) *(Subgroup 3)* • Reps & warranties methodology[76] B. Relevance of the pre-contractual phase to determine the scope of contractual obligations (*Subgroup 1*) • Entire agreement	**Art. 1.7 UPICC** (Good faith and fair dealing) See also **ICC Model Clause on good faith and fair dealing** **Art. 1.8 UPICC** (inconsistent behaviour) **Art. 2.1.13 UPICC** (conclusion of contract dependent on agreement on specific matters or in a particular form) **Art. 2.1.15 UPICC** (negotiations in bad faith) **Art. 1.4 UPICC** (mandatory rules) **Chapter 3 ALIC Guide** (ESG, due diligence and affected third parties) **Art. 2.1.17 UPICC** (merger clauses) **Art. 4.3 UPICC** (relevant circumstances) **Art. 4.8 UPICC** (supplying an omitted term) **Art. 5.1.2 UPICC** (implied obligations)

[74] This chapter would only cover due diligence obligations in the pre-establishment phase. After the contract has been stipulated, due diligence obligations concerning the entire life-cycle of the investment (monitoring and periodic ESG review) would be included in chapter 6 on rights and obligations.

[75] Given the current discussions within Subgroup 1, please note that several items in the bullet points might not require a modified UPICC principle and then their content might be discussed in the form of guidance on application to IICs in the "intro".

[76] For instance, through representations and warranties an investor may represent that he has conducted proper due diligence in the pre-contractual phase, and then enjoy protection from any cause of harm that cannot be deducted from the due diligence.

State and State-entities. **Privity of contract and third parties.** **Imbalance of powers.** **Specificities for contracts under public bids**	**Chapter 4. Formation, Parties and Authority** *(Subgroup 1)*	[intro] • Legal capacity • Gross disparity • Third parties • Reps & warranties methodology	**Art. 1.1 UPICC** (Freedom of contract) **Art. 3.1.1 UPICC** (Matters not covered) See also **ICC Model clause on Alleging lack of capacity** **Art. 3.2.7 UPICC** (Gross disparity) **Art. 6.2.3 UPICC** (Effects of hardship) **Chapter 2 ALIC Guide** (Parties, stakeholders, and contractual arrangements) and **Chapter 2 Legal Guide on Contract Farming** (Parties, Formation and Form)
Illegality of contracts linked to specific investor's behaviour ('clean hands'). Corruption.	**Chapter 5. Validity** *(Subgroup 1)*	[intro] B. Substantive validity Section 1: General provisions • Validity of mere agreement • Initial impossibility Section 1: Reps & warranties methodology Section 2: Grounds for avoidance[77] • Mistake • Fraud • Threat, duress • Gross disparity • Third persons • Confirmation • Loss of right to avoid • [Notice of avoidance or request for negotiation] • Retroactive effect of avoidance	**Article 3.1.2** (Validity of mere agreement) **Art. 3.1.3 UPICC** (initial impossibility) **Art. 3.2.1 to 3.2.4 UPICC** (Relating to mistake) **Art. 3.2.5 UPICC** (Fraud) See also **ICC Model clause on fraud, wilful misconduct or gross negligence** **Art. 3.2.6 UPICC** (Threat) **Art. 3.2.10 UPICC** (Loss of right to avoid) **Art. 3.2.11 UPICC** (Notice of avoidance) **Art. 3.2.14 UPICC** (Retroactive effect of avoidance) **Art. 3.2.15 UPICC** (Restitution)

[77] Some of the UPICC provisions might be considered to be inapplicable, to IICs. If so, explanations to that end, if deemed useful or necessary, would be included in the intro.

		• Restitution • Damages Section 3: Illegality • Contracts infringing mandatory rules • Corruption (including remedies) • Restitution	**Art. 3.2.16 UPICC** (Damages) **Art. 3.3.1 UPICC** (Contracts infringing mandatory rules) **ICC Anti-Corruption Clause 2012** **Art. 3.3.2 UPICC** (Restitution)
Investor's obligations and its liability for acts of third parties. State's obligation of vigilance and protection. Coercion and harassment by the organs of a host State. Rights of third parties (stakeholders) Arbitrary and discriminatory treatment. Contractual behaviours potentially amounting to expropriation (such as unilateral termination under certain circumstances).	**Chapter 6. Rights and Obligations**	[intro] • State's obligation to monitor and protect, and to provide security *(Subgroup tbc)* • Protection against contractual behaviours by the State tantamount to abuse or expropriation (such as grave non-performance or unilateral termination of an IIC by the State) *(Subgroup tbc)* • State and investor's ESG obligations and commitment to the highest attainable standard (*Subgroup 3*) • State and investor's obligations towards third parties and affected stakeholders (*Subgroup 1 and 3*)	**Chapter 4 ALIC Guide** (Rights and obligations of the parties) **IISD Model Clauses** **Art. 5.2.1 to 5.2.6 UPICC** (Third party rights) **Chapter 2 ALIC Guide** (Parties, stakeholders, and contractual arrangements)
Ensuring a stable and predictable legal framework	**Chapter 7. Change of circumstances** *(Subgroup 2)*	[intro] • "Stabilisation" clauses • Hardship (definition, effect, renegotiation and role of third parties, notice, procedure, compensation, termination) • Force majeure (definition, notice, limitations, termination)	**ICC Model Clause on New or Changes Laws, Standards, Regulations** (ICC Model Turnkey for Major Projects) **Art. 6.2.1 to 6.2.3 UPICC** (Hardship) **Chapter 5 ALIC Guide** (Managing the contractual relationship during implementation: dealing with non-

			performance and remedies) **ICC Hardship Clause 2003** **Art. 7.1.7 UPICC** (Force majeure) **Chapter 4 Legal Guide on Contract Farming** (Excuses for Non-Performance) **ICC Force Majeure Clause 2003 and 2020 + Force Majeure clause in ICC Models**
Consequences of breach of State/investor obligations (against usual contractual remedies). **Principle of full compensation applied to IIC.**	**Chapter 8. Remedies, including compensation and damages** *(Subgroup 1)*	[intro] • Pre-arbitration/litigation options for alleged non-performance (*Subgroup 1 and 4*) • Principle of continuity • Types of remedies for non-performance[78] (*Subgroup 1*) • Remedies for non-compliance with ESG obligations, including towards affected third parties (*Subgroup 3*) • Criteria for calculation of compensation and damages • Limitation of liability and penalty clauses	**Art. 4.8 UPICC** (Supplying an omitted term) **Art. 5.1.2 UPICC** (Implied obligations) **Art. 2.1.14 UPICC** (Contract with terms deliberately left open) **Chapter 7, Section 1 UPICC 7.1.1-7.1.7** (Non-performance in general) **Chapter 7, Section 2 UPICC 7.2.1-7.2.5** (Right to performance) **Chapter 7, Section 2 UPICC 7.3.1-7.3.6** (Termination) **Chapter 7, Section 4 UPICC 7.4.1-7.4.11** (Damages) **Chapter 5 ALIC Guide** (Managing the contractual relationship during implementation: dealing with non-performance and remedies)

[78] Types of remedies include: renegotiation and adaptation, in-kind (e.g., time extension), monetary (compensation/damages/interest), renegotiation and adaptation, suspension of performance, termination. The Working Group is invited to discuss if specific remedies would be covered in each single principle in connection with a specific situation, or rather exclusively in this dedicated chapter, or in both allocating in the latter general principles on non-performance and remedies.

Applicable rules to an IIC as a transnational instrument. **Settlement of disputes in line with current debate on ADR.** **Relationship with 'fork-in-the-road' and other mechanisms to address parallel/sequential proceedings.** **Powers of arbitrators.**	**Chapter 9. Choice of Law and Dispute Settlement** *(Subgroup 4)*	[intro] • Choice of law • Dispute settlement (e.g., different ADR mechanisms, limitation periods, non-signatories) • Avoiding parallel/sequential proceedings • Issues of transparency and conflicts of interest	**Preamble UPICC** **Model Clauses for the Use of the UNIDROIT Principles of International Commercial Contracts 2013** (1.1-1.3, and 2-4) **PRICL art. 1.1.1, Comments 4** (Application by choice of law) **and 6** (Model Clauses for a choice of the PRICL) **Chapter 10 UPICC** (Limitation periods) **Chapter 7 ALIC Guide** on "Grievance mechanisms and dispute resolution" **ICC Arbitration Clauses 2021**