Environmental, Social and Economic Development Provisions in Investment Contracts

A Resource for Government Lawyers in the Commonwealth

Motoko Aizawa and Howard Mann

The Commonwealth

Environmental, Social and Economic Development Provisions in Investment Contracts

A Resource for Government Lawyers in the Commonwealth

Motoko Aizawa and Howard Mann

The Commonwealth

Commonwealth Secretariat
Marlborough House
Pall Mall
London SW1Y 5HX
United Kingdom

Published by the Commonwealth Secretariat
Typeset by Nova Techset Private Ltd, Bengaluru & Chennai, India
Printed by APS Group

Copies of this publication may be obtained from:

Publications Section
Commonwealth Secretariat
Marlborough House
Pall Mall
London SW1Y 5HX
United Kingdom
Tel: +44 (0)20 7747 6500
Email: publications@commonwealth.int
Web: https://books.thecommonwealth.org/

A catalogue record for this publication is available from the British Library.

ISBN (paperback): 978-1-84929-196-5
ISBN (e-book): 978-1-84859-988-8

Preface

This resource document ("Resource") is intended to help government drafters and reviewers of foreign investment projects and related contracts. It specifically focuses on fairness and balance in investment relationships with respect to environmental, social, and economic development matters in order to maximise the sustainable development benefits and minimise the costs to government and citizens. Setting up an investment project for success for the duration of a contract is a complex undertaking that takes time, energy and proper resources. Of the myriad issues that investment contracts must address, a failure to adequately provide for the environmental, social and economic development consequences of an investment will, inevitably, lead to a contract that is suboptimal for the government. All too often, it ends in financial loss, which is ultimately shouldered by the people in the host state. The role of lawyers in this process will, for the reasons discussed, be of ever-increasing importance.

Negotiating good contracts requires an understanding of how to establish and implement good negotiating practices. The need for sound preparations that engage the government departments responsible for the key issues being raised cannot be stressed enough. The important role of the lawyer in this process will be underscored throughout this Resource. Governments that lack capacity and experience should seek support, and use the opportunity to ensure government officials learn from outside specialists. Negotiating a contract is a business process, not a policy-making process: a contract will not be reopened whenever there is a change in government, at least not without a high risk of triggering disputes. Understanding the provisions being negotiated and consequences thereof is absolutely essential.

The issues addressed in this Resource are one basket of issues in a contract setting. Numerous additional issues must be considered, including properly defining the project scope and location, the financial terms, the timelines and deliverables at different stages of the project, certain fiscal elements, and the warranties of each party. Historically, too much emphasis has been placed on the beginning of the relationship (signing a contract) and how to maintain that status quo, but not enough on how to manage the evolution of the relationship over its full, often decades-long, lifespan. Changes in the relationship, such as amendments, assignments, stepping-in and winding-down, all of which seem impossibly far in the future, are likely to occur. Properly structured dispute management and dispute settlement processes are also critical.

While recognising the importance of all of these issues, this Resource focuses exclusively on the environmental, social and economic development dimensions of investment, which time and again have proved to be a blind spot in so many failed investment projects. To help lawyers anticipate and address this blind spot, this Resource sets out practical, principle-based guidance on the procedural and substantive rights and obligations involved in environmental, social, and economic development matters (Chapter 4), followed by guidance related to general, legal or procedural provisions that apply to the entire contract (Chapter 5). Many of these general provisions are understood as legal 'boilerplate' and yet they can have a surprising impact on the sustainable development of the host country, its people and the environment. A summary of all guidance appears in the Annex.

We hope that governments and drafters and reviewers of investment contracts can use this Resource to maximize the sustainable development impacts of investment projects, not least those implemented to help governments recover and build back better following the ravages of the coronavirus pandemic.

Acknowledgements

The authors would like to thank Foley Hoag LLP for generously sharing their collection of investment laws and regulations, model documents, and investment contracts in the infrastructure sectors.

Drafts of the text were reviewed by Matthew Moorhead, Naadira Ogeer and Alache Fisho of the Commonwealth Secretariat. We are very grateful for their inputs. Mr Moorhead shepherded the project from conception to completion for the Commonwealth Secretariat, and we are grateful for his attention to detail, his guidance and his support throughout.

Contents

List of Figures and Boxes

Abbreviations and Acronyms

ADR	alternative dispute resolution
BIT	bilateral investment treaty
CCSI	Columbia Center on Sustainable Investment
CDA	community development agreement
CSR	corporate social responsibility
EHS	environmental, health and safety
ESIA	environmental and social impact assessment
ESMP	environmental and social management plan
FPIC	free, prior and informed consent
ICC	International Chamber of Commerce
ICSID	International Centre for the Settlement of Investment Disputes
IFC	International Finance Corporation
IIA	international investment agreement
ILO	International Labour Organization
ISDS	investor–state dispute settlement
KPI	key performance indicator
MDB	Multilateral Development Bank
MMDA	Model Mine Development Agreement
NGO	non-governmental organisation
PPP	Public-Private Partnership
SDGs	Sustainable Development Goals
UNDRIP	United Nations Declaration on the Rights of Indigenous Peoples
UNGPs	UN Guiding Principles on Business and Human Rights

About the Authors

Motoko Aizawa is President of the Observatory for Sustainable Infrastructure, a research organisation that aims to bridge the sustainability gap of mega-infrastructure development, investment and finance through data collection and policy research. Motoko spent more than two decades at the World Bank Group in various capacities, including as Sustainability Advisor to the World Bank's Sustainable Development Network. She is the principal author of the original IFC Performance Standards; she also supported the creation and implementation of the Equator Principles. Motoko began her career as a business lawyer, specialising in due diligence in mergers and acquisitions, and project financing of infrastructure projects at IFC's Legal Department. After she left the World Bank, she served as Managing Director USA of the Institute for Human Rights in Business between 2014 and 2016. She currently serves as the Chair of the District of Columbia's Commission on Human Rights.

Howard Mann has been specialising in international law and sustainable development for almost 30 years. He began his career with the Government of Canada as an international environmental treaty negotiator. In 1999, he began working with the International Institute for Sustainable Development, where he established the Investment and Sustainable Development programme. He has advised dozens of governments on international and domestic law relating to foreign investment, as well as on dispute settlement processes and arbitrations. This includes investment contracts and investment treaties. He is widely published in these areas. Howard is also serving as an arbitrator in an international investment arbitration. See www.howardmann.ca for more information.

Chapter 1

Background and Rationale

Chapter 1
Background and Rationale

There is growing recognition that sound investment contracts between foreign investors and host states can play an important role in helping countries meet the Sustainable Development Goals (SDGs), and ensure that valuable benefits accrue for society and the environment. At the same time, many current investment relationships are understood to lack fairness and balance. While economic and financial considerations can go a long way in righting this relationship, a more comprehensive treatment of environmental, social and economic development aspects in investment contracts is also necessary to help the contracting parties achieve a relationship that minimises harm and maximises benefits to the host state, people and the environment.

Unfortunately, for government practitioners who wish to draft investment contracts to support sustainable development in a fair and balanced investment relationship, adequate reference sources are scarce, and what is available tends to focus on traditional contract approaches and not on how the investment can maximise its sustainability benefits by fully integrating these issues into the contract development process.[1] Similarly, despite a vast literature on international investment treaties and sustainable development,[2] there is a surprising vacuum in the academic literature on investment contracts and sustainable development.

There is a surprising vacuum in academic literature on investment contracts and sustainable development.

This Resource is intended to help government drafters and reviewers of investment contracts achieve the requisite fairness and balance in investment relationships with respect to environmental, social and economic development matters. In so doing, it will also highlight issues concerning the relationship between domestic law and investment contracts, and the need for these two legal elements governing investments to be developed in a symbiotic way.

1.1 How this Resource came about

This Resource was informed by several interrelated elements. The results of a 2019 questionnaire issued to Commonwealth Attorney-General departments by the Commonwealth Secretariat,

Box 1.1 Model Mine Development Agreement (MMDA)

The MMDA produced by the International Bar Association in 2011 is probably the only model contract developed from the starting point of demonstrating a holistic approach to sustainable development. As such, its table of contents provides a useful guide to a complete outline of a contract in the mining sector but is also relevant to other sectors. The MMDA was developed through a multi-stakeholder process, and many of its provisions remain state of the art to this day.

Source: International Bar Association (2011), *Model Mine Development Agreement*, available at: http://www.mmdaproject.org/

and the outcome document of a subsequent consultation meeting in Johannesburg in June 2019 captured the challenges that government lawyers face in drafting and negotiating investment contracts, and provided valuable insights into the necessary focus of this Resource.

The specific guidance proposed in this Resource was also informed by available literature, including guides and materials from international organisations and development banks and other relevant general or sector-specific standards and practices. In addition, an extensive review of clauses from publicly available contracts in the extractive (oil, gas and mining), agriculture, and infrastructure sectors was undertaken. Key sources here included publicly disclosed infrastructure contracts and model contracts by certain jurisdictions identified by the law firm of Foley Hoag LLP, as well as those in the large contracts databases maintained by the Natural Resource Governance Institute (NRGI) and the Columbia Center on Sustainable Investment (CCSI). This research is discussed in more depth in Chapter 2.

Finally, the Resource was supplemented by the authors' combined decades of practical experience and perspectives gained from negotiating and drafting investment contracts, model agreements and laws, International Investment Agreements (IIAs), and international standards on sustainable development used in investment activities.

1.2 The scope of the Resource

The Resource focuses on investment contracts between host states and investors. Known also as investor–state contracts, they are, for many governments, a common tool for establishing and managing foreign investments into their countries. These contracts are not international investment agreements or investment treaties that are concluded between two or more states, but contracts directly between the investor and the host state government. This reflects the very different nature of these instruments, and the critical need of governments for support in the contracting process.

The Resource focuses on the environmental, social and economic development dimensions of an investment contract. These three dimensions of sustainable development should be a part of every investment contract. The approach taken here is to suggest ways to fully incorporate these dimensions into contracts, rather than to treat them as piecemeal add-ons to traditionally designed contracts that often considered these issues to be outside their scope. Maximising the value of investments for sustainable development requires clear formulations of the social, economic and environmental obligations of each party to the contract that are designed to achieve this end.

The environmental, social and economic sustainability dimensions are one group of issues in any contract. This resource is limited to these issues. Moreover, in the context of 'economic' issues, we address only those related to the economic contributions of the investment project to the local and national economy in terms of 'spinoffs': labour, upstream and downstream supply chain relationships, skills and know-how transfers and so on, that stimulate local economic activity and social development. In other words, we focus on the direct economic impacts of the project in the local community and region of the investment. What we do not include here are issues relating to overall business and economic structures of the investment, such as financing, taxation or general risk allocation. The financial and fiscal issues between the government and investor, which we acknowledge are often central to the economic sustainability of a business for the investor, are not included here.

The Resource is intended to be most relevant for investments in large-scale and long-term projects, such as infrastructure, natural resource extraction (oil and gas, mining, forestry), and agricultural projects.[3] While this is the target, it is anticipated that the Resource will be relevant for smaller projects as well.

The Resource does not propose a model contract – instead it suggests practical guidance for drafters, informed by existing good practice and lessons learned. Each contract will differ based on the precise investment proposed, the country, the legal system, the scope of domestic law in relation to the project, and other factors. It is thus hoped that principle-based guidance will be more useful across these differences than specific language that might apply in more limited circumstances.

As this Resource is broadly based and not sector-specific, it will be important for government users to ensure they have access to sector-specific expertise in negotiating any given investment contract. It is essential for government negotiators to be able to match the level of expertise of the investor who is proposing the project, and this can only be done on a sector-by-sector basis.

1.3 Key audiences

The key audiences for this Resource are government contract negotiators and their negotiating teams.

Ensuring that legal advice informs the goals of a government in a negotiation, and in the actual negotiation itself, emerged as a significant issue during the Commonwealth Secretariat consultations with member governments in 2019. This Resource takes the position that lawyers for the government should be involved in the development of negotiating positions as early as possible in the process. Unfortunately, this is often not the case. In many instances, lawyers are not involved in the development of negotiating positions, the initial drafting of the contract, and often even the contract negotiations with the investor. This leads to poor drafting, the creation of conflicts between domestic law and contracts, or other difficulties that cause a lack of clarity in the operating environment of the investment. Lawyers can identify such issues when they arise and help avoid them. They can also understand provisions that might create excessive liabilities for governments, or create other imbalances in the contract, including building an understanding of what issues should be addressed through the applicable domestic law and what should be in the contract (see the discussion in Chapter 3). These and other reasons suggest strongly that government lawyers should be part of the negotiating team at all times.[4]

At times, governments may need outside legal expertise, which is not a sign of internal failure but a good investment in their capacity. The fact is that few governments have the level of expertise needed to negotiate contracts across a full range of sectors and issues. Bringing in the needed expertise is therefore an investment in the long-term future and maximising the benefits of the potential investment. Nonetheless, government lawyers provide a backstop and expertise that is essential for fully understanding the contract, the responsibilities and liabilities governments are assuming, and how the contract fits with other applicable law. Getting these issues right from the beginning of a contract is critical.

The audience for this Resource extends beyond government lawyers to all government officials working on developing government negotiating positions and those who participate in government negotiating teams. It is vitally important that government officials who participate in the contract process have an understanding of what is legitimately possible for governments to seek in that negotiation. Of course, not every contract will include every element set out below: some may not be relevant to a given context and others may be fully reflected in domestic law and need not be in a contract. But understanding the scope of what governments can expect as their legitimate right in return for an investor's benefits of its investment is crucial. This Resource is based on the view that the host state has the legitimate right to expect good outcomes on environmental, social and economic development issues in relation to an investment.

It is vital that government officials who participate in the contract process have an understanding of what is legitimately possible for governments to seek in negotiation.

In many cases, government officials, and especially Ministers, see achieving a contract as an end point in itself. Ministers may be satisfied to have achieved a contract, often knowing there will be another Minister in that position if something goes awry down the road. But this distorts the reality that a contract is the starting point of a relationship between the government, investor and local community, not an end point. The contract must, therefore, set the stage properly for the project to meet the goals of all stakeholders over the longer period of time. The lawyer's role in making this happen can be invaluable.

Notes

1 See, for example: World Bank Group (2019), Guidance on PPP Contractual Provisions, available at: https://ppp.worldbank.org/public-private-partnership/sites/ppp.worldbank.org/files/documents/Guidance_on_PPP_Contractual_Provisions_EN_2019_edition.pdf; UNCITRAL (2019), UNCITRAL Model Legislative Provisions on Public-Private Partnerships,

available at: https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/19-11011_en.pdf; and UNCITRAL (2020), *UNCITRAL* Legislative Guide on Public-Private Partnerships, available at: https://uncitral.un.org/en/lgppp; but also note more integrated discussions, for example in International Bar Association (2011), *Model Mine Development* Agreement, available at: http://www.mmdaproject.org/; UN OHCHR (2015), A Turn to Responsible Contracting: Harnessing Human Rights to Transform Investment, available at: https://e15initiative.org/wp-content/uploads/2015/09/E15-Investment-OHCHR-Final.pdf; and Brauch, Martin (2017), Contracts for Sustainable Infrastructure: Ensuring the economic, social and environmental co-benefits of infrastructure investment projects, IISD, available at: https://www.iisd.org/sites/default/files/publications/contracts-sustainable-infrastructure.pdf

2 See for example, Commonwealth Secretariat (2013), Integrating Sustainable Development into International Investment Agreements: A Guide for Developing Country Negotiators; and Mann, Howard, Aaron Cosbey, Konrad von Moltke and Luke Eric Peterson (2005), *IISD Model International Agreement on Investment for Sustainable Development*, IISD, available at: https://www.iisd.org/publications/iisd-model-international-agreement-investment-sustainable-development-negotiators

3 Agriculture can also be understood as an extractive sector, extracting water as its principal resource. However, for present purposes, we have stayed with more commonly used categorisations here. See Smaller, Carin and Mann, Howard (2009), *A Thirst for Distant Lands: Foreign investment in agricultural land and water,* IISD, available at: https://www.iisd.org/publications/thirst-distant-lands-foreign-investment-agricultural-land-and-water

4 In the context specifically of the mining sector, this is explained in some detail in Mann, Howard (2015), *IISD Handbook on Mining Contract Negotiations for Developing Countries Volume 1: Preparing for Success*, IISD, available at: https://www.iisd.org/publications/iisd-handbook-mining-contract-negotiations-developing-countries-volume-1-preparing

Chapter 2

Lessons Learned from Contracts and Models

Chapter 2
Lessons Learned from Contracts and Models

In order to understand the current state of practice of drafting sustainable development focused clauses in investment contracts, and to draw lessons and recommendations for this Resource, this project analysed investment contracts in various sectors. The overall lesson that can be drawn from this exercise is that investment contracts from developing countries do show many good practice examples. However, they are usually drafted to address just some but not all the environmental, social and economic development dimensions. Another major observation is that there is a significant variance in practice between sectors.

Altogether, about 120 contracts and a few national model contracts for certain project activities were identified and analysed. Contracts were obtained from two contract databases: one managed by NRGI and dedicated to the extractives sector (oil, gas, mining, etc.),[1] and the other managed by CCSI and dedicated to contracts for land, agriculture and forestry (agribusiness) projects.[2] In addition, the law firm of Foley Hoag LLP provided access to its collection of publicly available infrastructure project contracts, infrastructure policy documents, bidding document templates, and model contracts for certain infrastructure projects, all from developing countries. These contracts reflected projects (or expected projects) from 29 countries, many of which are common law jurisdictions.

To identify the relevant contractual clauses efficiently, the project developed a set of key words to search contracts for clauses that addressed environmental, social and economic development issues: 'climate change', 'human rights', 'disputes resolution', 'change in law' and 'stabilisation'. These key words were applied to the collection of contracts and model contracts provided by Foley Hoag. In the case of the CCSI and NRGI databases, they are set up to be searchable by specific criteria provided in a drop-down menu of the database; as a result, the appropriate criteria that corresponded to the key words described above were used to search clauses. The search selected only contracts in the English language, signed between 2010 and 2018. Using these criteria, 60 contracts out of 2,286 contracts in the NRGI extractives contracts database and 50 contracts out of 866 agribusiness contracts in the CCSI agribusiness database were identified as contracts containing one or more clauses relevant for this Resource.

Most contracts attempted to address at least one aspect of sustainability issues perceived to be material, frequently of an environmental nature.

The notable findings from the analysis are as follows:

- **Contracts from emerging market countries show many good practice examples**. Most contracts attempted to address at least one aspect of sustainability issues perceived to be material, frequently of an environmental nature, such as compliance with national environmental laws and permits, and an obligation to conduct an environmental impact assessment under national law. A handful of these clauses were detailed and well crafted to create meaningful and enforceable obligations. Some contracts in relation to agricultural or forestry projects stood out for containing detailed provisions that protect project workers and their families and communities. A fair number of contracts overall contained obligations of some kind to procure local labour and materials.
- **Unique features in relation to environmental, social and economic development issues exist**, in some cases driven by national priorities or sectoral practice. As an example, the model contract for Sao Paolo's Metrorail project[3] is notable for the detailed mention of the project's social protection and societal obligations, reflecting the country's priorities and social system. These include payment of taxes, social security and other employment benefits, compliance with labour, health and safety, workers' compensation insurance laws, and the law providing for priority service for vulnerable groups of people. It also includes the establishment of ombudsman services for rail users, and requires a performance bond for environmental, civil, tax and labour liabilities incurred.

  Some projects commit to adherence to certification standards for particular commodities, such as the Forest Stewardship Council's certification standard for sustainably sourced wood, and the Roundtable on Responsible Palm Oil's certification standard

Box 2.1 Example of positive economic and social development text

Some positive economic and social development text is found in the contract between Heng Yue (Cambodia) International Company Limited, Concession (Cambodia 2011):

'Heng Yue (Cambodia) International Company must ensure that people living in the investment zone benefit from the project, including the use of infrastructure, roads, schools, health centers and the creation of job opportunities linked to the project, which shall include the integration of household farmers' production.'

Source: Heng Yue (Cambodia) International Company Limited, Concession (Cambodia 2011). NRGI, the World Bank, and CCSI: ResourceContracts.org

for sustainable palm oil. These clauses reflect the forestry and agribusiness sectors' public commitment to seek to obtain certifications under the respective commodity standards.

Several other unique or innovative features on environmental, social and economic development issues are noteworthy. One hydroelectric model contract required a minimum flow commitment in order to ensure that sufficient water is released downstream of the dam at all times. Another metro project, from India, explicitly required accommodations for persons with disabilities. Some even contained very progressive obligations, such as mandating improved living standards for resettled people (rather than a status quo), a right for those resettled to purchase equity in the project company, and electrification and free energy for communities (hydropower,[4] or positive project benefits for the adjacent communities (agribusiness – see Box 2.1).

- Generally speaking, **extractives and agribusiness contracts do a better job than infrastructure contracts** when it comes to sustainable development provisions. The drafting of the former tends to be more comprehensive and refers to wide-ranging issues that concern stakeholders, such as community development and funding obligations for it, grievance mechanisms, project monitoring, and so on, and have more sophisticated approaches to them, such as a separate contractual arrangement for community development to ensure that commitments to communities that are not part of the investment contract are memorialised and honoured. Of the 60 extractives contracts selected from the NRGI extractives database, 19 had separate community development agreements, in addition to obligations in the investment contracts to promote local employment and procurement of materials. Of the 50 agricultural contracts selected from the CCSI agribusiness database, 34 had 'social contracts'. In contrast, only one of the infrastructure contracts reviewed for this project referred to a separate community development agreement.

No contract appears to have addressed all potentially relevant environmental, social and economic development issues.

Notwithstanding these notable examples, no signed contract appears to have managed to address all the potentially relevant environmental, social and economic development issues. The existence of environmental clauses was no indication that social clauses also existed. Some of the provisions mentioned above appeared in isolation. And some requirements appeared too cursory to be meaningful in implementation. For example, many contracts required the project to carry out a process of environmental and social impact assessment (ESIA) but fell short on the subsequent steps. The contract must specify what flows from the ESIA in the correct sequence, and it must specify processes to help meet all the relevant requirements specified in each stage. (Concrete guidance on this point can be found in Chapter 4.) This patchy state of practice underscores the urgent need for contracts to integrate all three dimensions of sustainable development in an even and systematic manner.

- **References to climate change and human rights are conspicuously absent**. On climate change, one model contract in the hydropower sector states that the carbon credits generated from the project will split evenly between the contracting authority and the private operator. But mention of climate risk assessment, mitigation and adaptation measures, issues related to the use of technology in the future, insurance, and disputes related to climate events is altogether absent from contracts in all sectors, with the exception of one oil and gas contract, from the United States, which expressly tackles climate mitigation issues, as discussed in detail in Section 4.5.

On human rights, the contracts do not explicitly include the words 'human rights', though they obviously address environmental, social and economic development issues, all of which support human rights. As mentioned above, the two metro rail project documents mention accommodations for disabilities, and one of them explicitly prohibits advertisements that refer to 'any kind of injury, discrimination or prejudice of any order, including prejudices against race, color, creed, gender, sexuality, social or a xenophobic nature'. This statement is supportive of a number of human rights. Nonetheless, it was surprising that extractive and agribusiness contracts do not require at the least the private operator to respect human rights, abide by the UN Guiding Principles on Business and Human Rights (UNGPs),[5] or to carry out human rights due diligence, since it is almost standard practice these days for companies in these sectors to have corporate policies on human rights. The absence of meaningful obligations related to human rights and climate change is likely due to a lack of familiarity with risks that these issues can pose to the project, people and the environment, and how to turn these issues into legal obligations that can be enforced.

- **The approach taken to stabilising laws and disputes resolution varied widely** among the contracts reviewed. With respect to stabilisation, some demonstrated good practice, such as excluding environmental, labour, health and safety and similar laws from the scope of stabilised laws, while others used traditional language exempting projects from having to comply with new laws. Similarly, dispute resolution clauses ranged from national courts to in-country arbitration using national arbitration rules to arbitration in foreign venues using the United Nations Commission on International Trade Law (UNCITRAL) Rules of Arbitration or other rules. This indicates that the usage of change-in-law clauses is in a state of flux and that government lawyers need to be well aware of the general direction in which the public policy discourse on this topic is moving when drafting or negotiating such a clause.

- Finally, there is conspicuous disparity between sectors when it comes to transparency of contracts. **Investment contracts for infrastructure projects are not readily accessible**. There is no centralised database[6] that is comparable to those created and managed by NRGI and CCSI and there has been no concerted NGO advocacy for transparency of infrastructure project contracts, unlike the massive transparency drive that pressured the extractive industries in the 1990s, and the later campaign against land grabs that influenced agribusiness contracts. As a result, contracts for infrastructure are not systematically made public.[7] To some extent they become publicly available through different channels, including through national open government, e-government or transparency initiatives, multilateral development banks that finance projects, and international arbitration, but availability is haphazard at best. Even in the extractives sector, where contract transparency is much more accepted as best practice, not all contracts are publicly available.

All in all, the reviewed contracts give assurance that investment contracts for projects in emerging economies are evolving to support some aspects of sustainable development. This trend, seen also in the context of countries steadily improving their laws in order to protect the environment and people, consistent with their international obligations, and in support of the SDGs, is encouraging. The key now is to systematise this good practice and to ensure that all environmental, social and economic dimensions of sustainability are consistently captured in contracts for better project outcomes.

Notes

1 NRGI, the World Bank, and CCSI, https://www.resourcecontracts.org/

2 CCSI, *An Online Repository of Open Land Contracts*, available at: https://www.openlandcontracts.org/

3 Brazil, STM PROCEDURE No. 000770/2015 – CONCESSION OF LINES 5 LILAC AND 17 GOLD Draft of the CONCESSION AGREEMENT No. /2017.

4 Government of Nepal, Model Project Development Agreement (for Hydropower Projects with installed capacity less than 500MW), available at: https://moewri.gov.np/storage/listies/May2020/proposed-draft-pda.pdf)

5 UN (2011), *Guiding Principles on Business and Human Rights: Implementing the United Nations "Protect, Respect and Remedy" Framework*, available at: https://www.ohchr.org/documents/publications/guidingprinciplesbusinesshr_en.pdf

6 An ongoing initiative of the Open Contracting Partnership is focusing on infrastructure transparency that is more data-driven than documents-driven, and making some country data platforms available, e.g., in Honduras. See: Fenz, Bernadine (2019), The #OC4IDS: A new standard for infrastructure transparency, Open Contracting Partnership, available at: https://www.open-contracting.org/2019/04/17/the-oc4ids-a-new-standard-for-infrastructure-transparency/

7 This point can be illustrated by the sector-specific disclosure requirements in the Sustainability Policy of the International Finance Corporation (IFC), the private sector arm of the World Bank Group. While it mandates the disclosure of principal contracts with governments in the case of extractive industry projects, it only 'encourages' the disclosure of 'information relating to household tariffs and tariff adjustment mechanisms, service standards, investment obligations, the form and extent of any ongoing government support' in the case of projects involving the final delivery of essential services to the general public under monopoly conditions (paras 50 & 53). However, there are notable exceptions to the non-disclosure practice. Nigeria's Infrastructure Concession Regulatory Commission has made it a government policy to disclose all of its PPP contracts, in an effort to promote transparency of projects, which in turn is expected to attract additional investors. See Box 5.3.

Chapter 3

The Laws Governing Foreign Investments: Getting the Relationships Right

Chapter 3
The Laws Governing Foreign Investments: Getting the Relationships Right

For any foreign investment, there are potentially three 'sources' of law that may apply to the investor and its investment in the host state.[1] This chapter looks briefly at the appropriate relationships between these three different sources of law:

- domestic law, including elements such as tax law, labour law, zoning law, environmental law, and consumer protection laws;
- contracts between an investor and the national government of the host state (or subnational governments in some jurisdictions); and
- investment treaties concluded between the host state where the investment is located and the home state of the investor, when such a treaty applies.

Whether the contracts between an investor and the host government are a true 'source' of law or spring from national law as the source of law is a theoretical question somewhat beyond the necessary scope of this Resource. For our purposes we note that such contracts, which are the main subject of this Resource, possess important qualities which can have major impacts on their functioning inside or outside the national legal system of the host state. These key qualities include a status as 'international contracts' that often also attracts international law as a source of law; frequent use of international arbitration for disputes; and in many cases the inclusion of provisions designed to displace and replace normally applicable law with the negotiated provisions in the contract. In some cases, the contracts are enacted into legislation by national legislatures, or pre-defined as being of a special legal status that allows them to include provisions contrary to the normally applicable law. In many instances, the contracts are not even governed by the national law of the host state but by another national law imposed by the investor as part of the negotiations (often English or French law). All of these issues make contracts between foreign investors and host governments different from normal domestic-only contracts, and potentially elevate the role of the contract under international law. Investment contracts involving developing countries tend to have more of the characteristics described in this paragraph.

For present purposes, it is sufficient to note that these contracts can contain some of, and in some cases most of, the critical obligations and rights of the governments and investors who negotiate them. Hence, understanding how they fit in the relationship as a part of the law governing the investment is crucial to determining, in the context of a specific negotiation, the role they should play in relation to a planned investment.

In the most positive situation, the legal provisions regulating any investment should come primarily from the applicable domestic law. This is certainly the prevailing situation in developed countries, but is less the case in developing countries that turn more often to extensive contracts. Where the domestic law of the host state is fully developed and applied, this will significantly reduce the scope for negotiations in a contract. Where the domestic law provides the bulk of the legal regime, the contracts will provide the specific details for implementing and applying the law to the individual project.

When lawyers are fully engaged in the contracting process, they can ensure the proper relationship between domestic law and the contract is maintained.

Reliance on domestic law will ease the burden on governments during any negotiation, make the rights and obligations of investors more consistent and transparent, ease burdens on enforcement of the applicable law, reduce opportunities for corruption to play a role in the establishment or conduct of the investment, and generally promote a business and legal environment that respects all aspects of domestic law. When lawyers are fully engaged in the contracting process from the beginning, they can ensure the proper relationship between the domestic law and the contract is maintained, and that the contract remains fully consistent with domestic law instead of seeking to displace it.

Generally, governments should be aware of the extent to which contracts between governments and foreign investors displace or replace the law generally applicable to other investors and create a specific legal regime for each particular investor, and be clear about the extent to which contracts will be allowed to deviate from the generally applicable law. In our view, in a perfect world, it is indeed arguable that investment contracts of the type that create bespoke legal regimes for individual investments would stop being used completely and be replaced with regulatory structures that are supplemented only to the extent needed by the terms of the business deal and related specifics of each project. This would still require negotiation of these specific applications, but it would end the practice of bespoke legal regimes for every investment.

In a well-structured domestic legal regime, applicable investment treaties will apply only to protect investors from egregious government acts with significant impacts on the investment. They will not fill in additional law, as the main law will come from the applicable domestic law, supplemented by the contract or permit. As noted by the Commonwealth Secretariat[2] among others, investment treaties will contain generalised provisions such as a requirement of fair and equitable treatment of investors or non-discrimination between investors. The treaties usually add a layer of dispute settlement as well. IIAs are often tilted in favour of investor rights and rarely incorporate significant investor obligations. As a result, they can constrain future policy space and risk creating regulatory chill for governments that seek to improve their regulatory regimes. There have also been instances where international investment treaties raise potential barriers to the application of other international law obligations by governments, such as in relation to the environment (see, e.g., the discussion on climate change below) or Indigenous People's rights, and others. To ensure these barriers do not arise, it is important for governments to reflect their international obligations as much as possible in their domestic legal regime.

Figure 3.1 The relationship between sources of law, right way and wrong way

What is important to note is that the impact of investment treaties on regulating how specific investments perform in relation to environmental, social and economic development obligations will at best be minimal when the domestic law regime is well developed. For legal regimes where the domestic law is not well developed, we often see the inverse pyramid (see Figure 3.1).

In these circumstances, investors and governments attempt to buttress the absence of domestic legal provisions with the contents of the contract. Indeed, in many instances, investors will seek to use the contract to displace the local law with a new, bespoke legal regime just applying to that investment. This can include taxation, employment, land acquisition, environmental issues, and other areas of law. Such negotiations will inevitably lead to unbalanced contracts, especially when government negotiating teams are not as skilled or experienced as the company lawyers and negotiators.

In this situation, investment treaties can lead to even more imbalance due to the restriction on policy space many treaties bring with them. In particular, it often becomes especially hard to put in place new laws of general application that will apply to the investment when a contract has been used to displace the domestic law in whole or in part. And the additional layer of dispute settlement that the treaties enable enhances the risks governments face in seeking to improve their domestic law. Indeed, in the event of a dispute, the treaty in this inverse relationship will work to reinforce the imbalance in rights and obligations that often comes with the contract developed in this context due to the imbalance in the treaty with its investor rights and absence of obligations.

Including provisions that are contrary to domestic law degrades domestic law and creates a business and legal environment that risks a lack of respect for it.

In summary, the inverse pyramid creates several risks to the role of domestic law in managing any FDI project. The practice of including provisions that are contrary to domestic law degrades domestic law and creates a business and legal environment that risks a lack of respect for domestic law, and hence respect for the rule of law. IIAs can also contribute to such an environment of less respect for domestic law. And yet domestic law should be the most important source of law for managing foreign as well as domestic investment. As for the rights of the population at large, there is no source of law other than domestic law that would protect them. There is no short-term fix for this problem, but one thing governments can do is to work to prevent domestic law from being hollowed out in contracts. This Resource supports the role of government lawyers in reflecting domestic law in contracts.

These issues are discussed further in Section 5.4 on Applicable Law.

Notes

1 A full discussion of this can be found in Selacuse, Jeswald (2013), *The Three Laws of International Investment,* Oxford University Press.

2 Commonwealth Secretariat (2013), *Integrating Sustainable Development into International Investment Agreements: A Guide for Developing Country Negotiators.*

Chapter 4

Guidance on Drafting Environmental, Social and Economic Sustainability Provisions in Investment Contracts

Chapter 4
Guidance on Drafting Environmental, Social and Economic Sustainability Provisions in Investment Contracts

Many public officials and government lawyers tasked with investment decisions and contracts rank environmental and social risks at or close to the top of the list of project risks and opportunities they grapple with. Many fear internal criticisms and a public outcry if mistakes are made, yet they feel they lack the knowledge and experience to address these issues appropriately. Considering the technical nature of the substantive issues, the perceived intricacies of procedural requirements, and a lack of clear boundaries of responsibilities inside government and between the contracting authority and the private operator, their apprehension is understandable. At the same time, some are also frustrated that investment contracts are not being put to use more purposefully to create a common purpose and modality for investment projects to facilitate the sustainable development of the host country and people. Chapters 4 and 5 respond to these concerns and desires to address risks and opportunities appropriately in contracts through practical and concrete pointers. Sections 4.1–4.7 explain the procedural and substantive rights and obligations involved in environmental, social, and economic development clauses, whereas Sections 5.1–5.6 continue with guidance related to general, legal and procedural provisions that apply to the entire contract, making it fair and balanced.

Investment contracts are not being put to use to allow projects to facilitate the sustainable development of the host country.

This part of the Resource aims first and foremost to serve the needs of practitioners involved in investment contract drafting, negotiation or review. It aims to unpack the seemingly vague concept of sustainable development in the context of investment projects and to demonstrate how to create concrete legal obligations – for both doing no harm and doing good – that support and enhance sustainable development. In doing so, the guidance focuses on issues commonly faced by investment projects regardless of the sector, and should benefit all practitioners who work with investment contracts (of course, illustrations and concrete clauses are derived from sector-specific contracts). In addition to the practitioners, the guidance will also benefit government officials involved in developing negotiation positions, legislators involved in enacting legislation that promote and regulate large-scale projects, and those involved in negotiating IIAs, since the guidance tends to expose areas that would work best when appropriately regulated and reinforced through national law and international agreements.

Chapter 4 envisages the government lawyer working with other officials to develop government negotiating positions, and then getting ready to draft or review a draft of an investment contract. If the project has gone through a procurement process with a draft contract as part of the requirements for bidders, once the winning bidder is announced the detailed contract negotiation would begin. Or, in some cases, the lawyer may be asked to review a draft contract submitted by the project proponent.[1]

The starting point of contractual negotiation should be a credible document that provides sufficient guidance on the environmental, social and economic development aspects of projects.

If at all possible, the starting point of contractual negotiation should be a credible document that provides sufficient guidance on environmental, social and economic development aspects of projects, such as an industry model agreement, provided the model has incorporated a sustainable development approach;[2] model agreements suggested by the host government for certain sector or activity can also serve this purpose. If the negotiation must be based on the draft submitted by the proponent, the government lawyer should review such model contracts and good practice examples of signed contracts for reference, in addition to this Resource. Numerous extractive contracts and some in the infrastructure sector are publicly available, as mentioned above. Finally, pro bono legal assistance and legal clinics associated with universities and non-profit organisations may be able to offer hands-on help for large-scale or complex projects, especially in countries with less developed national law.[3]

4.1 Sustainable development objectives in a contract

The contracting parties should include in the investment project's objective – whether it is to build a metro rail system or start a palm oil plantation – their intent to enter into a fair and balanced relationship with rights and responsibilities that contributes to the sustainable development of the host country and its people. The statement should also affirm the parties' intention to avoid or minimise harm to the environment and people, especially those who are vulnerable or marginalised, respect human rights, and maximise the environmental,[4] social and economic benefits of the project.

The parties could point to any number of international and national documents and initiatives that best support their vision of sustainable development. They could mention the SDGs, or the host country national sustainable development plan, if one exists. A contract can also identify relevant international agreements that the project intends to be guided by, such as the Paris Climate Agreement, the Convention on Biological Diversity, or the International Labour Organization (ILO) Convention 169 on Indigenous and Tribal Peoples Convention.

This statement of objectives can be inserted into several places in the contract, including the preamble section, if it exists, or the definition section that defines the project. It may also precede as a chapeau to a cluster of environmental, social and economic development requirements. Alternatively, it could be a free-standing 'Objectives' clause that states the overarching sustainable development purposes of the project. Wherever it appears, the parties should expressly agree that the contract should be read in light of this statement.

Such a statement sets the tone of the contract and the contractual relationship, and could serve as a valuable touchstone between the parties throughout their decades-long relationship. The statement will be valuable when the project is faced with a novel issue not contemplated in the contract, particularly disputes related to environmental, social or economic development aspects of the project. This is all the more relevant when a dispute involves the rights of local communities who have no standing in the contractual relationship. The point about the rights of communities is discussed further in this chapter and Chapter 5.

Guidance I: Stating the sustainable development objectives of a contract

✓ The contract should state clearly, in the preamble or an 'Objectives' clause, that the project seeks to support the sustainable development objectives of the host country, and specifically the environmental, social and economic development of the nation and host community.

- ✓ The contract should specifically itemise the critical international agreements or standards and sustainable development goals it will seek to support.
- ✓ The contract should include a statement that makes clear the contract should be interpreted and applied in a manner that best ensures the intent of the objectives are met.

Sample Text: Sustainable Development Objectives

MMDA, Preamble:

[...] Whereas, the objective of this Agreement is to develop the Minerals in a manner to promote long term stability in the conditions of mining investment and contribute to the sustainable development of the State and its communities through a process in which the production and use of non-renewable natural resources takes place in an equitable framework; and

Whereas, the Parties to this Agreement believe that the Project can be developed, economically operated, and closed while protecting the natural environment of the State and the productivity of its ecosystems, and while managing adverse environmental impacts to eliminate, minimize, or mitigate them to acceptable levels, and compensating for any remaining impacts; [...]

4.2 Due diligence on environmental, social and economic obligations

The quality of environmental, social and economic development clauses in contracts depends greatly on the quality of due diligence.

Due diligence is a key activity by which a project's environmental, social and economic risks and opportunities will be identified and managed (environmental, social, economic and governance considerations in due diligence are often aggregated and called 'non-financial' due diligence to differentiate from financial due diligence). The quality of environmental, social and economic development clauses in contracts will depend greatly on the quality of such due diligence. The project lawyer should inquire about the nature and quality of such non-financial due diligence conducted so far, whether by the contracting authority or the private partner, and attempt to correct any gaps through contractual provisions, to the extent feasible. When initiating the review of the nature and quality of non-financial due diligence, the lawyer (and other government officials) should be aware that the environmental, social and economic responsibilities of and opportunities in investment projects will likely arise from several sources, which are:

- national laws and regulations;
- international standards derived from international agreements or international organisations;
- generally accepted industry standards;
- environmental and social impact assessment (ESIA) processes and other assessments, such as climate change impact assessment, health impact assessment, human rights impact assessment, gender assessment, and related assessments (see References for more on ESIAs and other related instruments);
- environmental permits or licences; and
- inputs from consultations with affected communities and other stakeholders with an interest in the project.

The role of the ESIA in due diligence

The ESIA is an instrument that is a critical part of the upfront due diligence process for both the investor and the government. It identifies potential positive and negative environmental and social impacts of a proposed project, and suggests specific measures to avoid, minimise or manage the negative impacts and to enhance the positive ones in an environmental and social management plan (ESMP). The ESIA process should involve iterative consultations with affected communities and other stakeholders, and in some cases should enable affected stakeholders to guide and inform the process in a participatory format, especially in projects with significant local development components or involving indigenous peoples. The ESIA process informs decisions and guides the critical points, targets and specific responsibilities to include in the contract. The scope of the ESIA should be consistent with the proposed project's potential impacts and risks.[5]

This guidance refers to the process of ESIA, which combines environmental impact assessment with social impact assessment in an integrated way, so that the two disciplines can inform each other, eliminate duplications, and explore efficiencies and synergies. It is possible to have two free-standing processes, one for the environment and another for the social side, but this approach is generally considered to be suboptimal. The ESIA could be supplemented with free-standing assessments for specialised topics, such as climate change, human rights, biodiversity, gender, and so on, as appropriate for the project. If these assessment processes are ongoing or will occur at a later date, the contract should specify them, identify the responsible party to conduct them, set out the government approval process clearly, and require implementation of the findings and recommendations. (The ESIA could also benefit from other studies, possibly carried out ahead of the ESIA, such as strategic impact assessment, sectoral assessment, regional assessment, and cumulative impacts assessment (see References), but these may be the responsibility of other agencies and not the contracting authority.)

Some projects use experts or expert panels to determine the quality of the ESIA or supplemental assessments, or monitor management activities and results on the ground. This may be a useful mechanism when such assessments do not require the approval of any government agency, or when they are very technical in nature and the government lacks capacity for review, provided that the experts are appropriately qualified in the relevant environmental and social areas and act independently of the project.

Each contracting party has an active responsibility to take part in due diligence. During project preparation and as part of feasibility studies, the contracting authority should either initiate or actively monitor the ESIA process initiated by the project proponent, so that the environmental and social risks and opportunities can be specifically identified and inform the content of the ESMP. Responsibility and monitoring for the public consultation process related to the ESIA should also be clearly set out. The private operator should be responsible for setting up the more detailed project management programme that will give effect to the ESMP. The private operator's responsibility to implement the ESMP and the management programme should be clearly documented in the contract. If this is not done, the contracting authority could bear the consequences and the knock-on costs of such impact, which could be significant depending on the sector and circumstances.

Because of the special expertise involved in the ESIA process, it takes place apart from other corporate activities, yet it is crucially important that the ESIA findings and recommendations are integrated into other business processes, including architectural, engineering, financial, human resources, legal (and vice versa). For instance, the cost of implementing the ESMP must be estimated and included within the project budget; failure to do so can result in poor implementation, contractual disputes, or project interruption. Such budget should be adjusted from time to time to take into account periodic technology upgrade.

The result of the ESIA should be a set of specific ESMPs that are then incorporated into the contract to give effect to the project-specific application of the domestic legal requirements, other normative standards, and the due diligence process. This is addressed in Section 4.3.

A critical aspect to be addressed in the due diligence process is the correct sequencing of the process that should follow the ESIA, and the translation of the results of the process into legal obligations. A failure to provide clarity on this sequencing has resulted in multiple international arbitrations. The next part of this guidance explains the relevance of this process.

Sequencing of assessments, approvals, and licences and permits

A typical sequence of environmental and social assessments, approvals, and licences and permits contemplated under many national laws is shown in Figure 4.1.

The sequence of events is explained below:

1. A **feasibility study** explores the practicality of a proposed project, and delineates the project in sufficient detail. This process will generate a project description, which will be the basis for a number of processes, including an ESIA process and the environmental permitting process (see item 4). The feasibility study would benefit from other parallel upstream processes, such as disaster and climate change risks studies, alternatives analyses, as well as cumulative, regional, sectoral, or strategic environmental assessments, which are particularly

Figure 4.1 Flow of environmental and social assessments, approvals, and licences and permits

important in large projects, transboundary projects, projects proposed in sensitive locations, and in the case of investment programmes with multiple projects under consideration.

2. An **ESIA** will establish the 'baseline' environmental and social conditions prevailing at the time of the assessment, identify all potential negative and positive environmental and social impacts of a project, and suggest how negative impacts can be avoided or mitigated and positive impacts enhanced through an **ESMP**. Consultation with affected communities and other relevant stakeholders helps verify the impacts predicted by the assessment process and identify additional impacts. This process may be carried out by the consultants hired by the project proponent (the contracting authority or the private operator). Regardless of who takes the responsibility, the assessment at this stage, if it takes place at all, may be a high-level document, and the ESMP may lack sufficient detail.
3. If the ESIA and ESMP provide sufficient level of detail, they can be submitted for **approval** by the responsible government ministry or agency (ideally the ministry

Box 4.1 Public procurement and ESIAs

Public-private partnership projects in the infrastructure sector typically go through a competitive public procurement process to select the private operator of the project. In these cases, the findings of the ESIA, including the ESMP (assuming the government has already commissioned it) must be handed over to the procurement process so that the bidders can propose and price out the environmental, social and local development components of the project. Bidders should be required to specify their qualifications with respect to the implementation of the ESMP.

When this 'handover' is done well, the winning bidder will have a clear understanding of its responsibilities in regard to the environmental, social and economic development requirements, which can be reflected in the investment contract in detail. When this step is missed, the value of the ESIA and ESMP is entirely lost; furthermore, the onus of carrying out a new ESIA is often placed on the winning bidder.

The procurement process should be structured as sustainable procurement that prefers bids that demonstrate the bidders' capacity for addressing the environmental, social and economic conditions of the project. Women- and minority-owned businesses should be given preference where appropriate.

of environment, but in some jurisdictions this would be the ministry in charge of the sector, such as the ministry of mines for mining projects).

4. The approval of the ESIA should precede or coincide with the issuance of an **environmental permit or licence**. The permit or licence will be based on the project description, should include key requirements from the ESMP, and may attach additional conditions to the project. In addition, and depending on the jurisdiction, other related permits for specific sectors, such as fishing, forestry, or exploitation of ocean resources, may be necessary. It is only when all requisite permits and licences are issued that a project should be considered as receiving final approval and thus when construction activities can start.
5. It is usually left to the private operator to translate the results of the ESIA and the ESMP into engineering and operational **management systems and programmes**. (If a full ESIA has not been conducted prior to the selection of the private operator, and the expectation is that it is the responsibility of the operator to carry it out, it must do so before it can even translate the results of the ESIA and ESMP into management programmes. This is clearly a practice that is out of proper sequence, but is frequently observed.) The private operator will propose detailed management programmes that are tailored to the technical specifications of the project, consistent with items 2 and 4 above, and will apply the programmes through an appropriate management system, setting aside sufficient human and financial resources for implementation of the management programmes. Some detailed programmes and plans, such as mine closure plans, mandated by law in certain jurisdictions for the mining sector, can only be set up once project details are settled. If this is the case, these programmes and plans should be mandated in the contract.
6. The project should be constructed, operated, monitored, reported, and wound down in accordance with the ESIA, ESMP, the environmental licence, and the management programmes (including the closure plan mentioned in point 5 above).

This sequencing of events broadly applies to most countries, though obviously there are variations. In some countries, there may be additional steps, such as a pre-feasibility study phase, and more complex rules relating to the process of ESIA, while others may rely on contracts to set out all requirements.

In many jurisdictions, the sequencing outlined above occurs smoothly with all steps intact, whereas in others the process may be less clearly structured. In a rush to expedite projects, environmental permits may be issued prematurely without, or in anticipation of, an appropriate ESIA. The permits or contract may specify that an assessment must be completed at a later date, but the follow-up process may be neglected. Permits may be issued by line ministries in charge of specific sectors, without a meaningful review and comment by the environmental agency. Worse, permits may be issued on payment of bribes in order to expedite the approval process. Considering these possible scenarios, the lawyer must be generally familiar with the legal requirements and the sequence of events for ESIAs and environmental permitting under their national law, and be clear about the point at which the contract is being signed in relation to the process described above. This is critical for ensuring clear obligations on the investor.

The lawyer must be familiar with the legal requirements and sequence of events for ESIAs and environmental permitting under national law.

If the contract is signed after stage 5 above, with all the steps occurring in the correct sequence, the contract should provide for the private operator to commit to constructing and operating the project in compliance with the ESMP and the environmental and related permits. These documents could be attached to the contract, or if too numerous or lengthy, referred to in an annex. Whether the project should also be made to comply with the rest of the ESIA will be a case-by-case determination. Generally, its main purpose is to predict potential impacts, both negative and positive, of a proposed project based on agreed project description, and is not intended to be a compliance document on its own; instead, it forms the basis for the ESMP.

Whether the project should comply with the environmental and social management system and programmes will also depend on the content of the programme. In some cases, it may not make sense for the project to have to comply with detailed engineering and operational specifications, which may be extremely detailed and technical and may have to adjust flexibly to the situation on the ground. On the other hand, it will be of comfort to the contracting authority to be able to insist that the management system and programme be followed carefully. On balance, if the management system and programmes have a good change management process written into them, it will be worthwhile to specify that the investor comply with them.

If the contract is being signed before stage 5, or if the assessments and approvals are out of sequence or missed, then the contract should provide that: (i) no construction activities should commence until such time as the appropriate ESIA and ESMP have been carried out, they are approved by the responsible ministry or agency, the environmental licence and other requisite licences have been issued, and the private operator has established appropriate environmental and social management system and programmes, consistent with the ESIA and ESMP and the terms of the environmental licence; and (ii) the private operator should commit legally to operating the project consistent with the ESMP and the environmental and social management system and programmes, as noted in the paragraph above.

Operational-phase 'due diligence'

The due diligence process for environmental, social and economic sustainability should be carried out at an early stage of an investment-making process, leading to the ESIA and ESMP, among other things. Although due diligence is typically associated with the project's preparation phase, it has also become the expectation that it should be periodic and ongoing, since changes will occur as projects develop. While the ESIA and ESMP originate at a certain point in time, project circumstances are dynamic and require constant adjustments. It is thus important that the ESMP and the management system and programmes be updated continuously as issues arise or new activities are proposed. The private operator should rely on a change management process in its management systems to adjust its ESMP to meet any changed circumstances in a flexible manner, and establish corrective action plans as needed to address poor performance.

Although due diligence is typically associated with the project's preparation phase, it should be periodic and ongoing.

If a material change to the project description is necessary during construction or implementation, such as unplanned resettlement becoming necessary later in the construction timeline, the project should carry out a supplemental ESIA, consult stakeholders on the proposed change, seek any amendments to permits as necessary, and update the management programme. The contracting authority must approve such a supplemental ESIA. Because these changes are by definition material, the contract should anticipate such changed circumstances and provide for the supplemental ESIA process and related approvals, which may include a default approval by the environmental ministry or other responsible agency, subject to a valid reason to object to the change. Corrective action plans should be reviewed by experts, approved by the contracting authority, and made public, and should not lower the standards set out in the initial plans.

Other types of supplemental assessments may become necessary. For example, a changed country context during the operational phase, such as conflict, or labour or general unrest, or new legislation being proposed by the government may necessitate the process of human rights due diligence by either or both contracting parties. This topic is discussed further in Section 4.6.

As a follow-up to due diligence and contractual obligations, each of the contracting parties should also discharge its respective responsibility to monitor the project's environmental and social performance, and stay in close communication with the other party during all phases of the project. The contracting parties should agree on key performance indicators (KPIs) on environmental and social issues specific to the project, and actively use such indicators to report on the project's ongoing sustainability performance (see Section 5.3).

Guidance II: Conducting environmental and social due diligence in the pre-contract and operational phases

- ✓ Ascertain the extent of due diligence carried out in the pre-contract phase and identify gaps, if any, making sure that the due diligence process is not being curtailed by a rush to contracting.
- ✓ Pay particular attention to the process of the ESIA so that the approval and permitting events that should follow the ESIA are in the correct sequence.
- ✓ Require compliance with ESMP and the environmental and related permits at a minimum as contractual obligations; if there are gaps in documents or incorrect sequencing of assessments, approvals and permits, remedy them before the execution of the contract, and if this is not possible, provide for the appropriate sequencing and corrective measures in the contract.
- ✓ Ensure ESMP implementation cost is part of the total project cost to avoid project shortfall, and adjust the budget periodically for technology upgrades and other changing needs.

- ✓ Provide specifically for the responsibility of the contracting authority to approve changed project descriptions or plans that alter the underlying obligations in any material way, and guard against any deviations that lower standards.
- ✓ Provide for ongoing operational phase reviews of the ESMP implementation plan and the need for adjustments to be made to it over the life of the project.

4.3 Manage negative and positive environmental and social impacts

Investment projects should impact the environment and people positively, but all too often the negative impacts outweigh the positives and thus require special attention in investment contracts. When asked to name the main environmental and social obligations of investment projects, most lawyers will likely respond that they consist of compliance with national environmental and labour laws, and a requirement for an ESIA. Some may also mention compliance with certain international standards (such as the safeguard policies or performance standards of a multilateral development bank (MDB), or the Equator Principles – see below). But these requirements are incomplete and don't create meaningful substantive and procedural obligations that are necessary for the project's negative environmental and social impacts to be avoided, minimised, mitigated, or compensated for effectively (in this exact order – this is known as the 'mitigation hierarchy').

Several tools can help inform the project of the risks and potential impacts of their planned activities, most notably the MDBs' environmental and social safeguard policies or performance standards.

Several tools can help inform the project of the risks and potential negative (and positive) impacts from their planned activities, most notably the MDBs' environmental and social safeguard policies or performance standards. They help the lenders anticipate these impacts in projects they finance, and identify the mitigation requirements to impose on the borrowers. Examples include the International Finance Corporation's (IFC) Performance Standards,[6] which are also the basis of the Equator Principles,[7] used by 105 international banks engaged in project finance; furthermore, the Standards are shared with the OECD export credit agencies under their Common Approaches to Environmental and Social Due Diligence,[8] and the European Development Finance Institutions.[9] Some policies of the regional development banks reflect regional considerations (for example, in-depth provisions concerning indigenous peoples in the environmental and social framework of the Inter-American

Development Bank[10]). Industries also frequently make use of the World Bank Group's Environmental, Health and Safety Guidelines (EHS Guidelines) as a technical reference containing general and industry-specific examples of good international industry practice. These standards and guidelines are frequently used as reference points in the process of ESIA, in addition to national law references. The following summary broadly follows IFC's Performance Standards, unless otherwise noted. This summary of issues is not meant to be comprehensive, but illustrative. Each sector will raise its own specific issues, as will the technology, geography and other issues relevant to a specific project. However, the impacts identified below are common across multiple sectors and projects and so serve to illustrate the key issues and approaches.

Environmental impacts

The environmental impacts are better known in comparison to the social impacts (see below) and can range from brown (pollution and resource efficiency) to green (biodiversity) issues, and, depending on the project location and sector, blue (impacts on the ocean and its biodiversity and other resources). The common **pollution** and **resource efficiency** issues that should be considered for specific obligations, where implicated, are:

- emission of pollutants to the air, water, and soil
- generation of hazardous and non-hazardous wastes
- use, transportation and disposal of hazardous materials and pesticides
- use of resources and inputs, such as water and energy
- supply chain issues associated with construction materials (sand, concrete, timber, steel, etc.)
- emissions of greenhouse gases.

Release of pollutants and use of resources must be minimised through the use of best available technology and good operational practices, as well as good hazardous substances management techniques. Greenhouse gas emissions should be estimated, mitigated, tracked and reported publicly. Projects should abide by international agreements as well as the applicable national law on these issues. The detailed management protocol should be managed through the

ESMP and the project's management programme. (See IFC Performance Standard 3.)

The key impacts to **biodiversity** include:

- loss of biodiversity through destruction of habitats and other project activities
- damage to ecosystems, including ecosystem services on which humans and other living things rely
- management practices for the sustainable management of living natural resources.

Biodiversity (both terrestrial and marine living resources) and ecosystem services (nature's services for human wellbeing) must be protected through avoidance of disturbance of critical areas, minimisation of habitat destruction, and habitat restoration. Biodiversity assessment and management plans are frequently used to manage impacts on biodiversity due to the technical nature of the subject matter. This process may require significant lead time because baseline information collection could require one or more reproductive or annual cycles in order to describe the baseline and inform the mitigation measures adequately. Mitigation and management measures vary significantly depending on the type of habitats (from already converted land to critical or legally protected areas) and the ecosystem services involved, and may include habitat restoration or reclamation, set-asides within the project area, the establishment of biodiversity corridors, and various management techniques. Since biodiversity and ecosystem services must be assessed at a landscape level (going well beyond the project boundaries), collaboration is usually required with local, national and international stakeholders and conservation experts. In certain cases, biodiversity loss at the project site could potentially be offset by biodiversity protection elsewhere (using the 'like-for-like or better' principle), though this is extremely challenging to achieve in practice, both in terms of techniques and management of relationships with third parties. (See IFC Performance Standard 6.)

Social impacts

These negative environmental impacts affect not only the environment but also people's health, wellbeing and livelihoods. But social impacts of projects go well beyond the environmental impacts described above and affect many stakeholder groups differently depending on their vulnerability. Within project-affected people are certain subgroups, such as workers, persons displaced due to project activities, indigenous peoples, women, children, older persons and persons with disabilities, all of whom will feel differentiated impacts from projects due to their identity or condition.

Negative impacts on the **health, safety and security of local communities** can be:

- environmental health issues
- resilience and safety issues associated with the project's infrastructure and assets, especially during disasters and emergencies, and project and community disaster preparedness
- use and disposal of hazardous materials
- damage to ecosystems services relied on by the communities
- emergency situations
- security of people when projects deploy security personnel to safeguard project assets and personnel.

Several instruments are available to evaluate these impacts, such as ESIAs, health assessment, climate risk or disaster risk assessment, and security risk assessment. Established management techniques for mitigation by specific sectors may be available in the EHS Guidelines. Impacts may be exacerbated in a situation of conflict, especially with respect to the project's use of armed security personnel, and should be monitored carefully. Other community impacts could include induced in-migration (see below) and gender-based violence generally associated with projects, and especially during the construction period.

The specific impacts on **workers** include:

- poor labour practices, especially failure to follow ILO's Fundamental Principles and Rights at Work (freedom of association, the right to collective bargaining, the elimination of forced or compulsory labour, and abolition of child labour, and the elimination of discrimination in respect of employment and occupation)

- other poor practices relating to working conditions and terms of employment
- impacts associated with retrenchment (collective dismissals)
- poor labour practices involving vulnerable workers (in addition to the use of child and forced labour/modern slavery), such as migrant workers, workers engaged by third parties, and those in the project's supply chain
- health and safety in the workplace.

Considering the globally connected supply chains, it is important to assess labour practices not only through the lens of national law but also through the relevant international standards, especially those established by the ILO (and reflected in many of the safeguard policies and performance standards mentioned above). The ESIA process, or a free-standing labour assessment, and in the case of existing enterprises, a labour audit, are used to assess labour practices. Depending on the legal status of the worker – whether engaged directly by the project, contracted through third parties, or engaged in the project's supply chain – the leverage and techniques of the project to influence the labour practices will vary, but poor practices with any of these types of workers are likely to be associated with the project and can cause reputational damage and even legal liability issues. (See IFC Performance Standard 2.) Contract provisions can address these issues, reinforce relevant domestic legal provisions and improve the domestic law standards through higher levels of obligations where needed.

Resettlement can involve physical displacement (loss of housing) or economic displacement (loss of income-producing assets and livelihoods) and a multitude of potential human rights violations. Adverse consequences of resettlement are numerous, complex and significant, and require detailed attention and vigilance over an extended period of time. They can be divided into:

- risks to persons being resettled, such as loss of shelter and household property, income-producing land and assets, access to jobs, social services, and communities, and livelihoods, potentially leading to lower living standards and poverty, and
- risks to communities that receive resettled people.

Since resettlement carried out under national law could entail the risk of compulsory acquisition for private use of land rather than for public purposes, risk of low (or no) compensation (based on depressed assessed value of the lost property), and forced eviction, it is advisable to plan resettlement under international standards.

Risks associated with resettlement in rural areas are different from those in urban resettlement, though lack of land to ensure land-for-land resettlement is a prevalent issue. In both situations, risks can stretch over years, and possibly beyond the life of the project, especially when livelihood restoration is required. As a result, resettlement should be avoided or minimised where possible and especially for high-risk groups, such as indigenous peoples.

Resettlement planning normally involves many years and multiple steps, including household surveys, compensation negotiation (in some cases involving the national eminent domain or compulsory acquisition process), compensation payment or settlement of replacement property, physical relocation, and resettlement or livelihood restoration monitoring. Typically, these steps are recorded in resettlement action plans. The assistance of competent resettlement specialists is required, often in collaboration with the ministry of housing or other authorities. (See IFC Performance Standard 5.)

Contract provisions should establish clearly who is operationally and financially liable for establishing and implementing resettlement plans. Governments often undertake to carry out land acquisition and resettlement. If the private operator is offered cleared land for the project, it should ascertain that land acquisition and resettlement have been carried out appropriately. If the private operator is tasked to acquire land and resettle people, the government should carefully monitor the process. In particular, safeguarding the rights of the local communities and individuals is a basic obligation of the government in this process that should not be contracted out to the private operator. This creates an important balance for negotiators to address in the contract.

Over 300 million indigenous people live around the world, often in resource-rich areas. These areas can become subject to development, triggering negative impacts on the territories and culture of indigenous peoples, including:

- loss of land, resources, livelihoods, ways of living, cultural heritage, and unique knowledge and practice, and
- high risks associated with relocation of indigenous peoples from lands subject to traditional ownership or under customary use.

As a result of their unique circumstances, international instruments (ILO Convention 169 and the UN Declaration on the Rights of the Indigenous Peoples) guarantee the process of free, prior, and informed consent (FPIC) of indigenous peoples with respect to measures that affect them, such as impacts on their ancestral land and the resources on it. A few countries have reflected the FPIC requirement in national law. However, today, businesses are obligated to respect the FPIC rules as part of customary international law, or through the application of safeguard policies (such as IFC's Performance Standards or the Inter-American Development Bank's policies) when the rights of indigenous peoples are at risk. Many projects, especially natural resource and hydroelectric projects, have been derailed and/or ended in international arbitration when governments have belatedly recognised the need to address and protect their rights after a contract was signed or a permit was issued, but no consent of the indigenous peoples was obtained.

International instruments guarantee the process of the free, prior, and informed consent of indigenous peoples with respect to measures that affect them.

In addition to protecting basic rights, the principle of project benefits enhancement and sharing that applies to all project-affected people and communities is particularly pertinent in the context of development taking place in the territories of indigenous peoples. This means community development planning for the affected communities should regard indigenous peoples as partners in development, and should be carried out with their active participation, and with ample lead time and expert advice. Implementation should be accompanied by close monitoring. Typically, these issues are addressed in a free-standing indigenous peoples development plan, though in cases where affected communities of indigenous people exist near non-indigenous communities that are also project-affected, care should be taken to ensure equity[11] among all involved communities. (See IFC Performance Standard 7.) In the case of communities of indigenous peoples who are in self-isolation, projects must avoid them (as provided in the policy of the Inter-American Development Bank).

Cultural heritage encompasses both tangible (or physical) forms and intangible forms (cultural knowledge, innovations, and practices of communities embodying traditional lifestyles). Both forms can be subjected to adverse project impacts, such as destruction, degradation or desecration, or other forms of abuse, such as commercial exploitation in the case of intangible culture. Although in-situ preservation of tangible forms of culture is the best, other mitigation measures may be possible, including removal and preservation, which should be decided in consultation with the affected local communities and, depending on the situation, experts and national antiquities or similar authorities. See IFC Performance Standard 8.

In addition to all the impacts mentioned above, which are direct impacts, projects could also generate **indirect or induced impacts**. Within a project life cycle, the construction phase normally generates the most adverse impacts, including induced impacts. For example, job prospects at the project site could attract a temporary rush of job seekers, who may contribute to the boom-town effects of construction to the communities surrounding the project, with prostitution, gender-based violence, diseases, and competition for scarce local resources. As these acts may not be well regulated by national law, projects must avoid the negative impacts or minimise, mitigate or compensate for them, often in collaboration with local law enforcement.

Transboundary impacts, such as impacts on rivers that cross national boundaries, pollution that spreads to neighbouring nations, potential transmissions of epidemics or pandemics, and impacts from facilities that the project relies on but does not control (e.g. dedicated transmission lines associated with a power plant) should also be considered in the ESIA process as appropriate.

In some sectors, projects may promise infrastructure and social services to local communities as part of mitigation or compensation for negative environmental or social impacts. These programmes are also offered as a way to promote local economic and social development (see Section 4.4). But they are also frequently added on as part of the private operator's corporate social responsibility or charity programme, or as a way to earn and maintain the project's social licence to operate. Projects may offer to share their soft or hard infrastructure with the local population, such as health clinics for staff, access roads for construction, or railway system for transporting commodities to the nearest port. Or, they may agree to build new facilities and installations, such as schools and libraries, wells, irrigation systems, off-grid electrical stations, and so on. It is important to be clear what is being proposed in order to specifically mitigate or compensate for negative impacts identified in the ESIA process. When this is the case, specific compliance, monitoring and reporting obligations should apply.

Finally, **gender issues** cut across all the issues discussed above. Some MDBs specifically require the process of gender assessment in order to identify and address project impacts that are differentiated on the basis of gender. Under certain circumstances, the risk of gender-based violence must be considered and appropriately addressed.[12] Social obligations with respect to women and girls, including health, education and economic development can be very controversial in some areas, but require ongoing care by companies and governments.

Enhancing positive impacts

ESIAs and ESMPs in theory are intended to address both negative and positive impacts of projects; yet, in practice they tend to concentrate on the former, and frequently miss opportunities to offer insights into how potential positive impacts can be realised and enhanced so as to contribute to the host country's sustainable development. On the environmental side, project activities could potentially offer opportunities for restoration of land, soil and water sources and improvement of air quality, and conservation and restoration of biodiversity and ecosystem services, among others. These positive environmental impacts can help projects manage negative impacts and, in some cases may even offset the negatives (for example, biodiversity offsets). Realising positive environmental impacts will invariably also lead to direct or indirect positive impacts on people.

Negative impacts on certain people cannot be offset by positive impacts on others. Corporate social responsibility programmes cannot be used as a mitigation measure for harmful impacts on people.

On the social side, projects can potentially offer opportunities to remedy past inequities and exclusion and enhance greater social equity and the inclusion of many. Resettlement programmes, while presenting great risks, can also offer great potentials for improving resettled people's livelihoods, living standards and wellbeing, if well executed. Socially positive outcomes can also enforce positive environmental outcomes, as in generation of green jobs. Good analysis of positive impacts is valuable for local economic and social development planning purposes. However, it should be noted that negative impacts on certain people cannot be offset by positive impacts on others. Corporate social responsibility programmes cannot be used as a mitigation measure for harmful impacts on people.

The due diligence process should ensure that these opportunities have been adequately explored, including the opportunities that can be revealed through the process of ESIA. Specific project commitments to boost positive project impacts should be documented in the contracts.

Guidance III: Strong environmental and social obligations to manage negative and positive impacts

- ✓ Strong environmental and social obligations go beyond the requirement for compliance with law or international standards, or the obligation to carry out an ESIA. The obligations should be based on precise understanding of potential negative and positive impacts.
- ✓ Review the ESIA to understand the potential negative impacts of the project and the ESMP for the proposed management measures. Ascertain what specific plans are required to manage the negative impacts.
- ✓ In addition to the ESMP, the contract should explicitly require the implementation of the specific mitigation measures or plans, or third-party agreements.
- ✓ Although not tailored for the specific purpose of identifying economic impacts of projects, ESIAs can also provide valuable information for the purpose of local economic and social development planning.
- ✓ Social obligations should be identifiable and verifiable. They should be developed with the community involved, for their benefit.

Sample Text: ESIA Requirements

Model Exploration and Production Sharing Contract [hydrocarbons] Republic of Cyprus (2012) [environmental provisions excerpted from several sections]

[Note that the following illustrates how to obligate the private operator to conduct ESIAs at various key milestones during the project for approval by the relevant government agency. It does not include other relevant environmental provisions discussed in the Resource.]

'Proposals relating to production procedures shall ensure environmental protection conforming to best practices in the petroleum industry and comply with the relevant regulations.

The licensees will conduct a preliminary environmental impact assessment study prior to the initiation of any exploration work and a full environmental impact assessment study prior to the initiation of any exploitation work, both of which

Sample Text: ESIA Requirements (*Continued*)

will comply with the provisions of the strategic environmental assessment of the hydrocarbon licensing program of the Republic of Cyprus and with the relevant opinion of the environmental authority, as well as with the relevant provisions of the Directive 85/337/EEC.

If the company declares that a discovery is a commercial discovery, the company shall submit to the government for approval within 4 months of such declaration: a full environmental impact study prepared in accordance with the applicable environmental legislation, covering the proposed development and any related facilities or infrastructure inside or outside of the contract area, which shall be subject to prior approval in accordance with the applicable environmental legislation.

The licensees will conduct a full environmental impact assessment study prior to the initiation of any exploitation work, which will comply with the provisions of the strategic environmental assessment of the hydrocarbon licensing program of the Republic of Cyprus and with the relevant opinion of the environmental authority, as well as with the relevant provisions of the Directive 85/337/EEC.'

MMDA, Article 2.4.2 Environmental Assessment and Environmental Management Plan (NB: Art. 2.4.3 includes similar provisions for Social Impact Assessment and Action Plans)

[NOTE: The objective of the Environmental Management Plan is to prevent any unnecessary and undue degradation of the environment by the Project; to protect public health and safety, particularly for communities in the Mining Area; to preserve water quantity and quality; to ensure that impacts within the Mining Area are contained in that area; to stabilize the site physically and chemically at the end of mining operations to prevent offsite impacts; and to ensure that the Mining Area may be safely and beneficially used by future generations.]

a. The Company shall have an Environmental Assessment prepared based on sound engineering and economic principles, and having regard to Good Industry Practice including IFC Performance Standard 1, establishing a baseline of environmental conditions existing at the Effective Date, and assessing the Project-related environmental effects and impacts.

b. The Company shall have an Environmental Management Plan prepared (which if prepared by the Company is verified by an independent environmental consulting firm recognised as having expertise in the international mining industry), based on the Environmental Assessment and sound engineering and economic principles, and having regard to Good Industry Practice including IFC Performance Standard 1. The Environmental Management Plan shall upon request by the State, be made publicly available in a language and in a form that is accessible to affected communities in the Project Area, and shall be placed in the document files identified in Section 30.1 of this Agreement. The Environmental Management Plan shall be and updated prior to any major change to the mine plan. The Environmental Management Plan shall include [elements as the Parties may agree, such as the following]:

   i. Measures that the Company intends to use to mitigate adverse consequences of further of the Project as described in the Feasibility Study;

Sample Text: ESIA Requirements (*Continued*)

ii. Plans for the management, remediation, rehabilitation and control of all environmental aspects of the Project, excluding all historic environmental matters that are not assumed by the Company, including

A. A plan to avoid, minimise, mitigate, rehabilitate and offset, where appropriate, impacts on biological diversity within the Mining Area;

B. A plan for preventing, minimising or mitigating adverse environmental impacts to rivers and other potable water and ensuring that such pollution does not cause unnecessary harm or destruction to human or animal life or fresh water fish or vegetation;

C. Opportunities for the improved management and conservation of natural resources in the Project Area;

D. A plan to avoid or minimize greenhouse gas air emissions (as defined by the IPCC) from the Project taking into account economically and commercially feasible technology;

E. A plan to effectively manage soil resources to allow future use of the surface land consistent with the proposed post mining land use;

iii. A description of the actions to be taken during any periods of temporary closure or cessation of operations and for the closure activities to be performed should closure be required prior to the completion of the planned mine life;

iv. A plan for concurrent reclamation to the extent practicable;

v. A plan to restore all mined areas to a final landform that is safe, stable, and suitable for the proposed post mining land use.

vi. A plan regarding the intended post mining land use in the Project Area;

c. The Company shall comply with the environmental laws of the State in force at any time during period of this Agreement [including any provincial and local laws], including laws relating to protection of water quality, air quality, quality of land, the preservation of living natural resources, the protection of biodiversity, and the disposal of hazardous and non-hazardous wastes. Subject to Section 33.2.2, a material failure to comply with environmental laws, the terms of environmental licenses or Environmental Management Plan, as the same may be amended from time to time, constitutes a breach of this Agreement. (Emphasis added)

MMDA, Article 10.2: Applicability of IFC Performance Standards and Equator Principles

Where Applicable Law and regulations on environmental and social impact assessment and management, and pollution prevention are less stringent than the IFC Performance Standards, the Company shall undertake its activities in a manner consistent with the IFC Performance Standards. To remove any doubt, the Company and the State recognise that the IFC Performance Standards outline processes to be followed enabling site-specific environmental compliance limits to be developed, where required.

4.4 Maximise opportunities for local economic and social development

Investment projects are usually justified on the basis of expected national and local economic growth. The many direct and indirect project benefits that can help propel economic growth, especially during the construction period, and to a lesser extent during operations, are of major value and interest to communities and local governments near the project site. Although direct job opportunities with the project company and its foreign contractors will be finite, depending on the scale and nature of the project, local businesses that supply goods and services to the project can generate new local employment. Projects can also create opportunities for training and skills and knowledge transfer, and help nurture careers, entrepreneurship and leadership, both within and outside the project.

It is frequently assumed that economic benefits should accrue automatically to local communities by virtue of the project, and that the larger the project the larger the benefits. However, studies show time and time again that larger projects consistently experience cost overruns and shortfalls of benefits.[13] Unless the national and local governments and the project proponent purposefully set their sights on maximising local economic development in the early stages of the project development, and articulate the economic development objectives in a strategic manner through appropriate planning and consultation with stakeholders, the risk of economic benefits falling short for local communities will be real and can be significant. Well-meaning but unilateral charitable donations or community development programmes based on the private operator's existing corporate social responsibility (CSR) programmes may not meet the needs, expectations and ambitions of communities. Resentment and discontent can spread quickly when hoped-for project benefits fail to materialise, and can provoke unrest, protests, project stoppages and even violence.

Unless the national and local governments and project proponent aim to maximise local economic development, the risk of economic benefits falling short for local communities can be significant.

It should go without saying that projects can generate tax revenues that can fund future social programmes by local governments. However, it is important to ensure clarity on allocations of tax revenues between different levels of government, because this is almost always not automatic. Tax payments to the central government may never be shared with the local governments, and jobs may easily bypass local communities and go to those outside the communities, or even outside the host country. To address this problem, some domestic law sets out a specific sharing ratio for taxes collected in order to ensure that local communities share in the increase in tax revenues a project generates. Such an arrangement can also be specified in a contract. Negotiators may wish to address this issue as well.

It is not the traditional role of the investment contract to right the omission of national, sectoral or project-level planning and stakeholder consultation early in the project phases, but it can prompt the contracting parties to take a hard look at the project and its potential to promote local economic development, propose an approach or a plan, and help ensure its systematic implementation. While planning is generally the responsibility of the government, the project can be designed to align with the official plan(s), and the contract then becomes one means for supporting this process. Successful local development plans seek to maximise the value of local skills and resources for the duration of the project and beyond, and both within and outside the project boundaries, based on active input from the local government, business and community members. Needless to say, companies making community investments should not become a substitute for local government, but should work with local government on these issues.

The lawyer should not rely on a simple contractual statement that the private operator will give preference to local labour, goods and services, as was the case with most of the contracts reviewed for this project. Instead, the detailed modalities, targets, budgets and timelines for local employment and project procurement of goods and services should be provided in specific provisions, in an annex to the investment contract, or if too lengthy, in a separate community development plan, or even a free-standing community development agreement. Regardless of the mechanics, the contract should specify that implementation is a legal obligation of the private operator. Section 5.1 elaborates on how to create legal obligations enforceable by communities. Targets and indicators could provide the basis for the project's periodic reporting on local economic participation and development (see Section 5.3). In many cases, national laws may set minimum levels or targets for these issues, which must be maintained or exceeded within any contract.

The detailed modalities, targets, budgets and timelines for local employment and project procurement of goods and services should be provided in specific provisions.

Although it is usually not the job of the lawyer to draft local economic development plans, it may be useful to consult handbooks on community development[14] and, critically, engage with the appropriate government ministries or agencies. The following pointers may provide a quick orientation on the topic. Even though not all of them are legal in nature, they could help improve the plans and the chances of local development.

- The private operator should give preference to the project procurement of local goods and services for the project, provided that the conditions of price, quality, delivery time and terms of payment are similar to those from non-national sources. This qualification is necessary to ensure that the project benefits from competitive goods and services.
- Some international trade or investment agreements may include limitations on preferential purchasing requirements. However, these requirements are now very common in the extractives sector and infrastructure procurement and can also be applied in other sectors.[15]
- Projects should offer training programmes designed to enable local participation in projects through a range of positions and skill levels. As a matter of priority, local businesses should be offered training on how to bid for project contracts, and manage operational, financial, accounting, and other management challenges. Targets for percentages of local purchasing of goods and services should rise over time, to take into account the benefits of mutual experience and capacity-building.
- In many instances, companies will have very large procurement packages. These should be unbundled as much as possible in order to maximise opportunities for local procurement. Working with local communities, companies can identify possible 'low-hanging fruit' that can be enhanced through appropriate unbundling.
- Employment of local personnel from communities around the project and from the host state should be factored into the contract or a related agreement.

Employment in higher-skill positions and management positions should be anticipated to grow over time, and targets should reflect this over time. It is essential also for human resource departments to establish longer-term career planning for employees, not simply to focus on short-term job placements. This is known to improve job retention for both the employees and employers.

- The private operator should treat its workforce based on the principle of non-discrimination, equal opportunity and fairness, and apply this principle to women and men, minorities and non-minorities, and so on. At the same time, we note that it is now widely accepted that measures or assistance to remedy past discrimination, and to promote the hiring of local community members and nationals of the host state for this purpose, will not be deemed as discrimination so long as they are consistent with national law and policy.[16]
- Projects should be aware of the business case for paying attention to gender issues at the workplace,[17] and should support women's participation in project activities on an equal footing with men. In addition, projects can create opportunities to support women's entrepreneurship and leadership generally. Activities that promote women in the workplace should be carried out in consultation with women. In countries where women's civic and economic participation is not culturally acceptable, gender experts should be engaged to solicit the views of women in a culturally appropriate manner.
- Provisions addressing all of the above must also reflect on the impacts of new technology across many sectors. Governments can no longer assume previous levels of employment and local purchasing for new projects, given the impacts of new technologies. In some sectors, employment is expected to drop 75 per cent or more in the next few years.[18] Expectations must therefore be realistic and not create a recipe for failure.

Guidance IV: Local economic and social development

- ✓ Go beyond a general requirement to prefer local inputs, employment and other economic development measures by providing details and timelines that will improve the chances of implementation.
- ✓ Minimum requirements in domestic laws should be adhered to or exceeded.
- ✓ Ensure that the project plans its contributions to local economic and social development strategically and systematically. Large-scale

procurement requirements should be unbundled to allow greater access to local businesses.

- ✓ Ensure consultation with the local government, businesses and community members to develop the plans, and work with community groups to ensure implementation.
- ✓ Companies must work with the local government, not to replace it.
- ✓ Create a legal obligation on the part of the company to implement community development commitments and plans where these are separate from the actual contract.

Sample Text: Employment and Training / Local Content

Maryland Oil Palm Plantation Concession Agreement (Liberia 2012)
[local employment, training and procurement provisions]

'Section 13

EMPLOYMENT AND TRAINING

13.1 Employment. Investor's Employment practices shall conform to Law. In no case shall Investor hire non-Liberian nationals for unskilled labor positions. Investor shall give preference for employment at all levels of financial, accounting, technical, administrative, supervisory and senior management positions and other skilled positions to qualified Liberian nationals as and when they become available, it being the objective of the Parties that the operations and activities of Investor under this Agreement should be conducted and managed primarily by Liberian nationals as soon as is practicable. Subject to availability of qualified and capable applicants who meet the reasonable requirements of Investor, Investor shall cause Liberian nationals to hold at least fifty percent (50%) of the ten most senior management positions within five (5) years of the Effective Date, and at least seventy-five percent (75%) of such positions within ten (10) years of the Effective Date. As of the Effective Date, the ten (10) most senior positions are the President and Managing Director, the General Manager, the Comptroller, the Operations Manager, the Plant Manager, the Technical Services Manager, the Agricultural Operations Manager, the Research and New Development Manager, the Personnel/Human Resource Manager and the Chief Accountant. The list of the ten (10) most senior positions may be amended from time to time by agreement of the Parties. Appointment of a Liberian national to a particular position shall not, however, preclude subsequent employment of a non-Liberian in such position as long as, subject to availability, the overall percentage of Liberian nationals employed in senior positions is otherwise met. In the event Investor is unable to meet the targets set forth above, upon the request of Government, Investor must demonstrate that it used all reasonable efforts to fill such positions with Liberian nationals but was unable to do so.

13.2 Training. In furtherance of the objective stated in Section 13.1, Investor shall provide for the training of Liberian nationals in order to qualify them for the positions described in Section 13.1 and as required by Investor's operations under this Agreement. Investor shall also provide on-the-job training, vocational training, and undertake whatever other measures are necessary and reasonable to achieve the objectives stated in Section 13.1 (including, subject to operational needs and economic conditions, scholarships for qualified Liberian employees to

Sample Text: Employment and Training / Local Content (*Continued*)

pursue relevant advanced studies abroad). Investor shall prepare (and revise when necessary) detailed plans and programs for its on-the-job training programs, including time tables and schedules, as part of its reporting requirements under Section 21 hereof. Specifically, Investor shall make available to all of its employees, and to members of the surrounding communities, desirable vocational training and adult literacy programs. In addition to the foregoing, Investor shall also invest not less than US$20,000, which amount shall be subject to inflationary adjustments, calculated in the same manner as Section 19.11 of this Agreement or as otherwise provided for in applicable Law, in internal vocational training programs. Investor has affirmed that, as a part of its support for education in Liberia, it shall provide annual scholarships for Liberian nationals or other educational support for Liberian nationals originating from the Developed Area. Specifically, Investor shall provide US$40,000 per year, which amount shall be subject to inflationary adjustments in, calculated in the same manner as Section 19.11 of this agreement or as otherwise provided for in applicable Law, for scholarships and financial support for students at the WVS Tubman University or other similar institution of higher learning designated by mutual consent with the Government. Investor agrees to implement a policy of technology transfer, which shall include a transfer of operational techniques and modern management techniques. Investor shall provide on the job training necessary for employees to undertake their work competently and shall also provide them with opportunities to learn new techniques which will allow such employees to progress into positions requiring more complex and demanding skills.

Section 14

USE OF LIBERIAN PRODUCTS AND SERVICES

Investor shall, when purchaseing goods and services related to Investor Activities, give preference to the maximum extent possible to goods produced in Liberia by Liberian nationals, and services provided by Liberian nationals resident in Liberia, or entities incorpoerated or formed in Liberia where Liberian nationals resident in Liberia are entitled to receive sixty percent (60%) of more of all profits from such entities, provided that such goods and services are equal to or better than comparable goods and services obtainable from other Persons taking into account price, quality, safety standards, service, quantity, delivery, schedules, availability and other terms. Investor shall make reasonable efforts to structure its procurement of goods and services so as to maximize the possibility of Liberian nationals providing such goods and serviceds. In addition, Investor agrees to include in each contract or work order with any Investor Party a provision requiring it to adhere to the requirements of this Section 14, and to require its sub-contracts to do so, with respect to any activities undertaken in Liberia by such Persons (and their sub-contractors), on behalf of Investor. Subject to the foregoing, Investor may freely contract with any Person.'

MMDA Art. 22: Local Community Development

22.1 Community Development Agreement

Within thirty (30) Days after the Effective Date of this Agreement, the Company shall enter into Consultation and negotiations with the objective of concluding one or more community development agreements as described in this Section or agreements with communities impacted by the Project, to promote sustainable development and enhance the general welfare and quality of life of inhabitants, as well as to recognize and respect the rights, customs, traditions and religion of the affected persons (each, a "Community Development Agreement"). It is the objective of each of the Parties hereto that the Mining Operations shall be carried out in a manner that is consistent with the continuing economic and social viability of centers of population that have formed and which may form as a result of such operations during the term of this Agreement. Upon request of the State at any time the Company shall consult with the State and with the community mutually to establish plans and programs for the implementation

Sample Text: Employment and Training / Local Content (*Continued*)

of this objective and thereafter the Company shall cooperate with the State with regards to its effort concerning the realization of such plans and programs. Each Community Development Agreement shall be subject to Applicable Law, and shall;

a. Address both how local communities can take advantage of the development opportunities presented by the Project, and how the Project's adverse impacts can be mitigated;
b. Serve as the agreement that specifies how the Company's obligation to spend funds for local development shall be met;
c. Address environmental, social, and economic conditions during mining and after mine closure, and the eventual transition from a mining economy to a post-mining economy in the Project Area as may be agreed upon among the Parties to such Community Development Agreement; and
d. Be based on the objectives listed in Annex B.

22.2 Relationship of This Agreement to Community Development Agreement

[Where an inconsistency occurs between a provision in the Community Development Agreement and the terms or conditions of this Agreement, the provision in the Community Development Agreement shall prevail unless this Agreement specifically states that the provision in this Agreement shall prevail.] [A final written and reasoned decision of a duly constituted court or arbitral panel declaring a material breach of the Community Development Agreement by the Company, shall constitute a breach of this Agreement.] [A breach of the Community Development Agreement shall be governed by the terms thereof.] [See comments for discussion of issue.]

22.3 Local Business Development Plan

The Company resolves to cooperate with the State in carrying out the State's responsibilities by developing a local business development program to promote economic development and growth in the area of communities impacted by the Project. Such a program would be modified from time to time to fit the existing circumstances related to the particular operating phase (development, construction and operation) in the life of the Project.

The program would be based on the objectives listed in Annex C.

MMDA Art. 24: Employment and Training of Local Citizens

24.1 Minimum Employment Levels

In selecting employees to carry out its Mining Operations under this Agreement the Company shall give preference to qualified and competent the State executives, officers, engineers, consultants, technicians and skilled and semi-skilled labour.

24.2 Investment in Skills of Local Work Force

The Company shall develop and implement an annual training plan with the objectives to:

a. Organize training of its employees to upgrade employees' skills and provide further practical experience;
b. Train employees in line with the Company's short and mid-term human resource plans; and
c. Upgrade selected employees' qualifications by enrolling them in studies inside or outside the State on a contractual basis to further upgrade their professional qualifications.

24.3 Labour Training and Capacity Enhancement

Sample Text: Employment and Training / Local Content (*Continued*)

The Company shall develop and implement a comprehensive training program for the State personnel in the State and in other countries, if necessary, and carry out such program for training and education in order to meet the requirement for various classifications of skilled and semi-skilled full time employment for the Project.

24.4 Management Training and Capacity Enhancement

The Company shall develop and implement training for the State personnel in the State and in other countries, if necessary, in order to qualify them for technical, administrative and managerial positions, with the objectives to:

a. Establishing and operating a vocational and training institute to provide vocational, technical and advanced training programs in the community;
b. Furnishing on-the-job counterpart training, not only in the State but to the extent reasonably feasible in the offices of the Company in the State, in order that the beneficiaries may receive training in the overseas aspects of the Company's shipping, marketing and accounting functions;
c. Providing scholarships for inhabitants of affected communities to pursue studies, including advanced studies in the State or abroad; and
d. Enhancing such training and educational opportunities as already exist in the vicinity of the local community.

4.5 Anticipate and manage climate change risks

Climate change affects every major investment project, everywhere in the world. It is imperative that the climate-related risks be factored into the design, construction, operation and emergency plans for any large-scale project. Although climate change is a dynamic risk that will affect projects lasting two decades or more, the contracting parties must use the investment contract, which is traditionally an inflexible instrument, to agree to climate risk management at the outset of the project.

The understanding of how the contract should address incremental climate risks on an ongoing basis and extreme weather events through *force majeure* provisions is still evolving. Issues of foreseeability are changing rapidly. Even if a climate change event cannot be predicted for one specific location, events are increasing rapidly in frequency and severity, making climate change a foreseeable risk in broader terms. The contract allows the parties to allocate the risks of a climate event impacting the business between the parties, beginning with the inclusion of climate resilient construction and operating plans in the contract with the appropriate cost allocations.

As technical capacity is one of the attributes often being sought when attracting foreign investors, it is reasonable for governments to expect this capacity to extend to climate change resilience and mitigation issues. Due diligence and risk allocation provisions should reflect this expectation and allocate the risk to the private sector partner. This will also ensure maximum effort by the investor to address rather than minimise climate change risks.

In addition, failing to address climate risks in the design, construction and operation of large-scale projects risks impacting local and, in some cases, more distant communities if an event happens and a facility is largely or fully destroyed or services largely or fully stopped. The potential impacts on third parties can be significant, and cannot be contracted out of by the contracting parties. A failure to address the issues of climate change resilience in the design and operation of an investment thus exposes the contracting parties to the risk of multiple levels of liability arising from project designs and construction. The only way to address this potential liability is to incorporate it into the contract.

It is vitally important for the contracting parties to be able to work together in a flexible manner to resolve future difficulties that will inevitably arise from climate events. It is equally imperative that governments not be hampered from putting in place climate-related policies and regulations that may limit or even preclude generating or using carbon-based energy sources or their infrastructure in the future. Given the critical nature and breadth of climate change issues, and to dispel the common perception that climate change risks should be borne entirely by the host state, this Resource includes a specific section on it.

It is vitally important for contracting parties to work together in a flexible manner to resolve future difficulties that will inevitably arise from climate events.

If climate assessment is not part of the original ESIA, a separate risk assessment should be carried out as appropriate. The contract should then memorialise the key elements needed for this purpose. This could be in terms of engineering standards, new construction materials or standards, operations and maintenance protocols, afforestation, agricultural practices, environmental health measures, future technology upgrades, a disaster response plan, or other terms that ensure clear responsibilities in this area. It is also important that the risk assessment focus on risks to people from project-induced incidents that could be exacerbated due to changing climate conditions, such as flooding, landslides, forest fires, and water shortages.

Resilience-building adaptations to infrastructure are not expensive if incorporated early in the project lifecycle, with research demonstrating average incremental costs of 1 and 2 per cent for infrastructure projects.

Resilience-building adaptations to infrastructure are not expensive if incorporated early in the project lifecycle, with research demonstrating average incremental costs of 1 and 2 per cent for infrastructure projects.[19] By the contract negotiation stage, it would be late to introduce climate risk management into the design of a project, but it would be better to do so even at this stage than have the far greater costs of retrofitting a few years after the project is constructed because the risks have grown. Hence, climate risk mitigation and adaptation should be addressed in the project design and development stages, and should be integrated into the operations phase, with the contract setting out the agreed standards and liabilities for any impacts of a climate-related event. There are multiple risk assessment, cost-benefit analysis and climate modelling tools available to do so today, and it is the shared obligation of governments and investors to make sure these are used appropriately. The failure to do so will result in significant potential liabilities for the project and the government, so it is always appropriate for lawyers to raise this issue and ensure it is addressed, even if it is being done for the first time at the contracting stage. Lawyers should be well equipped to explain the increasing liability that a failure to do so entails.

In addition, the climate-related provisions of a contract should include emergency preparedness planning, taking into account the latest climate modelling data available for the project site. The private operator should work with the local communities to ensure that the planning can be implemented. Where practicable, the contract could specify a requirement to upgrade technology as new technologies become available. The contract should specify how and when such an upgrade should occur and who will pay for it. As upgrading technology is generally part of operational costs, it should be attributable to the project, subject to appropriate tax treatment for operational or capital expenses.[20]

As noted above, the private sector party should have the expertise to address these issues in their project design and development. In some instances, such as infrastructure projects where the government provides project specifications for the private party to build and/or operate, the private sector partner may not have been part of the project design work. In such

Box 4.2 Example of corporate liability for climate change

In June 2020, Pacific Gas and Electric (PG&E), the large California electricity supplier, pleaded guilty to 85 legal infractions in relation to the so-called Camp Fire wildfires of 2018. The proximate cause was faulty transmission lines and equipment that ignited during the peak period of extended drought due to climate change. PG&E had not made required investments in new technologies to address the risks from the increasing impacts of climate change. PG&E was fined almost US$4 million. But the major costs to them come from a requirement to establish a US$13.5 billion trust for victims of the fire.

Source: 'PG&E pleads guilty to 85 counts in 2018 Camp Fire', Eliott C. McLaughlin and Stella Chan, CNN, updated 16 June 2020.

cases, the private operator should be required to undertake a climate risk assessment and provide recommendations on how to mitigate or eliminate identified risks. This will ensure that the operator is informed and liable for ensuring that its work does not create risks for others due to climate-related events.

Climate change events are no longer unforeseeable, and should not be treated as 'Acts of God' in contracts.

Climate change events, such as increasing temperatures, intense rainfall and droughts, are no longer unforeseeable, and should thus not be treated as 'Acts of God' in contracts. Rather, the responsibility to address these climate events should be set out in the contract and in emergency response plans. The contract should also specify the type of insurance that the project will purchase to cover climate events, if available. Availability of insurance products for climate events continues to improve as the industry gains experience and innovates. These steps will avoid later arguments as to whether climate change impacts are *force majeure* or not, arguments which are subject to increasing doubts that *force majeure* would be a defence to claims between contract parties or claims for damages by third parties.[21] Contract provisions here can be understood as akin to *force majeure* provisions, but with specific allocations of responsibilities and liabilities that obviate the need to actually argue the point.

Governments need to maintain the right to adopt new laws and regulations that reduce the reliance on fossil fuels and other greenhouse gases in energy and other sectors.

The second type of issue to note is the need for governments to maintain the right to adopt new laws and regulations that reduce the reliance on fossil fuels and other greenhouse gases in energy and other sectors. That governments will have to increase regulations towards this end is well understood today. Domestic regulation can introduce clarity into existing investment policy and legal frameworks to enable contracting parties to proceed with confidence about their respective climate responsibilities.

Box 4.3 Preserving the government's right to regulate climate change and Sample Text

The following provisions are from a permit allowing the acquisition of a local major gas utility in Maryland and Washington DC by a Canadian company, AltaGas. Ensuring the right to regulate was a key issue for the government of Maryland. The company did not dispute the right to regulate for climate change purposes, but rejected issuing a waiver of its arbitration rights under the investment chapter of the North American Free Trade Agreement (NAFTA), the applicable investment treaty. Instead, the company acknowledged in writing the right of the government to regulate future levels of use of natural gas, and acknowledged that the government made no promises and raised no expectations to the contrary. This was important in that it negated any possible substantive claim under NAFTA if the government reduces or even eliminates the use of natural gas in the jurisdiction. The key provisions read:*

> *20. Notwithstanding any other provisions of these conditions, AltaGas, Washington Gas, and WGL recognize that the State of Maryland and the Government of the United States retain the full right to enact bona fide laws and regulations in relation to the production and distribution of natural gas and other carbon-based energy sources. Nothing in these conditions or the Commission's orders restrict or alter these rights or creates or implies any limitation on the State of Maryland or its agencies, or on the Government of the United States and its agencies, with respect to future measures in this regard. This includes measures to address climate change and other public interest issues such as air quality.*
>
> *21. AltaGas, Washington Gas, and WGL expressly acknowledge that the Commission, by approving the Merger, is not creating any special expectations to induce AltaGas, as an entity covered by North American Free Trade Agreement ('NAFTA'), to close the Merger.*

Procedurally, a merger permit is a negotiated process in Maryland, and this was no exception. The text of this provision was subject to several rounds of negotiation, with AltaGas represented by one the leading NAFTA experts in the United States. The result above is the first known instance where a fossil fuel company has expressly acknowledged the right of a government to, effectively, regulate it to the point of being out of business. It is perfectly applicable in either a permit or contract negotiation.

Sources: Order 88631 In the Matter of the merger of AltaGas Inc and WGL Holding Ltd., April 4, 2018, Public Service Commission of Maryland, Case 9449.

* Conditions 20-21 of the Order are found at p. A-11.

But many contracts in the past have limited this right of governments and some investment treaties have been read to limit government policy-making scope in this area.[22] Thus, it has become increasingly important for governments to protect the space to act in this area.

The first step in doing so is to ensure that the contract does not include a provision stabilising non-fiscal laws applying to the project. This issue is examined in more detail in Section 5.5. Existing good practice goes beyond exempting changes in law to address climate change from stabilisation clauses. The example above (Box 4.3) describes a contractual provision from an oil and gas sector acquisition in the State of Maryland in the United States that actually affirms the right of the government to regulate limitations in the sector and precludes claims under investment treaties.[23]

Guidance V: Climate change provisions in contracts

- ✓ Go beyond the environmental provisions in the contract and address climate change risks explicitly, including climate event resilience, climate mitigation, and the right of governments to regulate in this area.
- ✓ Ensure that the project has carried out a climate risk assessment prior to finalising the contract.
- ✓ Ensure design and operational standards are appropriate to address climate-related weather events that can impact the investment, based on available scientific data and best industry practices.
- ✓ Ensure the design and operational standards are consistent with anticipated future reductions of greenhouse gas emissions, and new technologies can be implemented.
- ✓ Ensure that in any risk allocation provisions the project company is liable for the consequences of any foreseeable climate-related weather event, and that appropriate insurance is obtained where possible.

4.6 Project must respect human rights

What does it mean for investment projects to respect human rights? This question was considered in detail in the UN Guiding Principles on Business and Human Rights (UNGPs), issued in 2011, and the accompanying Principles for Responsible Contracts.[24] The former establishes a 'protect-respect-remedy' approach to addressing human rights risks arising from business activities. This means a state has a duty to *protect* human rights,[25] business has a corporate responsibility to *respect* human rights,[26] and both must ensure access to effective *remedy* for adverse human rights impacts from business activities. The UNGPs inform all sectors and all business enterprises, whether owned publicly or privately. At the core of the UNGPs is the responsibility to carry out human rights due diligence, which involves the identification and assessment of the nature of the

At the core of the UNGPs is the responsibility to carry out human rights due diligence.

actual and potential adverse human rights impacts with which a business enterprise may be involved. This process of inquiry should take place when proposing new activities, such as making an investment, and when changes or new issues arise.

The Principles for Responsible Contracts offer 10 pointers to help integrate the management of human rights risks into various phases of state-investor contracts, from contract preparation, negotiation, guidance for specific clauses such as on stabilisation, monitoring and compliance, to transparency. Although these Principles were written for a general audience and not directed to the legal community, they provide helpful explanation for anyone on how human rights risks from investment contracts – from risks to labour rights to stabilisation of environmental and social laws to investor-state dispute settlement mechanisms, to name a few – can be addressed. Principle 2 suggests that the responsibilities for preventing and mitigating human rights risks associated with the project and its activities should be clarified and agreed before the contract is finalised. And the methodology for identifying the risks is human rights due diligence.

Human rights due diligence need not be distinct from other types of assessments, such as environmental and social assessments, as long as it appropriately identifies human rights risks against the minimum set of human rights instruments identified in the UNGPs,[27] and targets especially those who

Box 4.4 Principles for Responsible Contracts

1. Preparation and planning
2. Managing potential adverse human rights impact
3. Project operating standards
4. Stabilization clauses
5. 'Additional goods or service provision'
6. Physical security for the project
7. Community engagement
8. Project monitoring and compliance
9. Grievance mechanisms for harm to third parties
10. Transparency / Disclosure of contract terms

Source: UN OHCHR (2015), *Principles for Responsible Contracts: Integrating The Management Of Human Rights Risks Into State-Investor Contract Negotiations: Guidance For Negotiators.*

are worse off, such as those who are vulnerable, marginalised or poor. For the most part, ESIAs will adequately identify project-specific human rights issues, because ultimately social and environmental issues are also human rights issues.[28] But it is also the case that human rights due diligence is qualitatively different from ESIAs. Issues regarding the host country context and the behaviour of national or municipal governments, the judiciary, police, army, political parties and interest groups (which are likely understood as public governance or law and order issues rather than environmental or social issues) tend not to be covered in ESIAs.[29] While this type of information may be generated as part of an initial country screening by the private operator, it may not be recognised and processed as information pertaining to human rights. ESIAs also do not include 'know your client' (KYC) due diligence, which can expose environmental and social issues, as noted above, and even human rights issues. As one example, a KYC team at one MDB discovered that a project proponent had close ties with a person wanted by the International Criminal Court for genocide crimes in a target host country. ESIAs would not have exposed such an issue, whereas human rights due diligence could have done so.

A KYC team at one MDB discovered that a project proponent had close ties with a person wanted by the International Criminal Court for genocide crimes in a target host country. Human rights due diligence could have exposed this issue.

As a matter of practice, the process of human rights due diligence requires an expertise in human rights law and the output of the due diligence is often separate from the ESIA document. Companies often task lawyers to carry out human rights due diligence in order to assure attorney-client privilege on the output. This makes it virtually impossible for outsiders to understand the exact nature of human rights issues identified in the process.

Another difference between the assessment and the human rights disciplines is that negative human rights impacts cannot be offset by positive impacts, unlike biodiversity loss in one place, which can sometimes be offset by gains elsewhere. Furthermore, the materiality lens used in financial due diligence is not appropriate in the case of human rights due diligence, which concerns rights of individuals as well as groups, communities and peoples. As a result, human rights due diligence is qualitatively different and cannot always be presumed to be covered by the ESIA process alone.

Investment contracts should clearly obligate both contracting parties to conduct human rights due diligence when risks to people can be anticipated.

Taking these considerations into account, investment contracts should clearly obligate both contracting parties to conduct human rights due diligence when risks to people can be

Box 4.5 Supreme Court of Canada judgment: International human rights law applies directly to companies

On 28 February 2020, the Supreme Court of Canada issued a ground-breaking ruling in the case of *Nevsun Resources Ltd. v Gize Yebeyo Araya, Kesete Tekle Fshazion and Mihretab Yemane Tekle*. The court held that Canadian mining companies operating abroad have direct obligations under international human rights law relating to torture, forced labour and cruel and inhumane treatment in particular. The Court ruled that these laws can be enforced against the company in Canada, including for actions by subsidiaries of the company outside Canada. The court ruling is important for stating two key points:

1. An alleged breach of international human rights law can be the basis for a claim for legal damages directly against a company; and
2. Such a claim can be made in Canada's domestic courts for the acts of a subsidiary company abroad, thus reducing the barriers to uphold jurisdiction for holding a company liable for its acts abroad.

Notably, the Court stated:

> *The rapid emergence of human rights signified a revolutionary shift in international law to a human-centric conception of global order. The result of these developments is that international law now works not only to maintain peace between states, but to protect the lives of individuals, their liberty, their health, and their education. The context in which international human rights norms must be interpreted and applied today is one in which such norms are routinely applied to private actors.*

The majority of the court based its decision on the nature of the alleged breaches, stating these were of the highest level of customary international law (torture, forced labour, cruel and inhumane treatment). It remains to be seen whether the court will make the same conclusion in the future for other breaches, such as those related to environmental law, right to water, local community rights including indigenous peoples' rights, etc.

Source: *Nevsun Resources Limited v Araya*, 2020 SCC 5, available at: https://decisions.scc-csc.ca/scc-csc/scc-csc/en/18169/1/document.do

anticipated. Prior to signing the contract, each party should ensure that the provisions in the contract do not create adverse human rights impacts (for the state, this means that nothing in the contract should conflict with its international human rights obligations). Ongoing due diligence should be carried out before taking major business decisions, when business circumstances change, when certain national contexts change, when new issues arise, etc. There may be more urgency for such due diligence depending on the prevailing host country condition or the proposed project location or activities, sector, etc. The contract could make these 'triggers' for the due diligence specific. And the obligation should bind both parties. Although the private operator is likely to benefit most from human rights due diligence, any proposed regulatory or procedural change, including proposed change in tariffs in certain projects, by the contracting authority may also trigger such due diligence.

Depending on the sector and the human rights risks posed by the project, compliance with international human rights and humanitarian laws should be signalled as a legal obligation, regardless of whether the international instruments expressly bind states and not business enterprises, with appropriate recourse for different breaches. Indeed, one major value of the contracting process here is to erase any doubt on this question by transforming the international law standards directly into contractual obligations (in the event that these standards are not reflected in national law). Some projects already reference ILO 169 and the United Nations Declaration on the Rights of Indigenous Peoples (UNDRIP) when they impact indigenous peoples. Public-private partnership projects in the water, health and education sectors could reference the explicit human rights standards set out in the International Covenant on Economic, Social and Cultural Rights. When the project must engage public or private security personnel, who may be armed to protect project assets and personnel, it would be appropriate to mention the United Nation's Code of Conduct for Law Enforcement Officials and the UN Basic Principles on the Use of Force and Firearms by Law Enforcement Officials.[30] And even though project scenarios involving gross violations of human rights[31] are not commonplace, projects located in conflict situations and other exceptional circumstances may need to make specific undertakings to refrain from gross human rights violations.

The exact nature of business responsibility with respect to international human rights law continues to be examined and efforts are being made to clarify the shift of business responsibility from a voluntary one to mandatory.

The exact nature of business responsibility with respect to international human rights law continues to be examined and efforts are being made to clarify the shift of business responsibility from a voluntary one to mandatory. The above-noted Supreme Court of Canada case is a useful illustration of this shift in action. Transforming international human rights standards into contractual obligations is another example. Lawyers should also be aware that an intergovernmental working group organised by the UN Human Rights Council is working on a new treaty that would create a 'legally binding instrument to regulate, in international human rights law, the activities of transnational corporations and other business enterprises'.[32] Case law is also evolving in this area. As seen above, one very recent Canadian case makes companies directly responsible for human rights violations under certain international human rights laws, in particular torture, forced labour, and cruel and inhumane treatment practised by a mining company.

Finally, guidance on human rights would not be complete without recognising the fact that environmental and human rights defenders, labour union leaders and leaders of indigenous communities around the world remain subjected to intimidation, criminalisation, violence and even murder for voicing their opinions against investment projects and defending their land and resources. As such, lawyers should take care to ensure that the investment contract requires the contracting parties to refrain from retaliations against defenders and put in place measures to protect the rights and freedoms of these defenders, including protecting them from violence by third parties.

The UNGPs, as noted, include a 'remedy' component. This issue is addressed in Section 4.7 under stakeholder issues.

Guidance VI: Incorporating human rights obligations into contracts

- ✓ Prior to the execution of the investment contract, carry out human rights due diligence so that the host state can ensure that nothing in the contract contradicts the state's international human rights obligations.
- ✓ Check that the ESIA for the project adequately covers key human rights issues; if it does not, and human rights risks can be expected, obligate the contracting parties to carry out human rights due diligence with respect to the expected activities of the project.
- ✓ Obligate contract parties to carry out human rights due diligence throughout the duration of the contract, specifying the circumstances when it is required.
- ✓ Add specific references to international human rights and humanitarian law or other international standards depending on project circumstances.

Sample Text: Human Rights

MMDA, Art. 10.3: Parties' Commitment to Protecting Human Rights

a. The Parties each commit themselves to the protection and promotion of the human rights of all individuals affected by the Project, as those rights are articulated in the United Nations' 1948 Universal Declaration of Human Rights, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social, and Cultural Rights, and Applicable Law.

b. In all dealings between Company security departments and the police, military, or other security organs of the State, the Parties pledge themselves to comply with Applicable Law and to respect the guidance set forth in the Voluntary Principles on Security and Human Rights.
c. The Company shall ensure that its operational policies reflect the responsibility to respect human rights and that the policies have the objectives of preventing, mitigating and remediating any potential or actual negative human rights impacts from Mining Operations.
d. A process to procure an independent assessment of the potential for human rights impacts from the presence and activities of the Project, and how the Company's policies, procedures, and practices affect the human rights of the population in the area of the Project, such process will be guided by the tenets of transparency, independence, and inclusivity, as defined by international standards.

4.7 Engage with stakeholders and address their concerns

The contract parties should view stakeholder engagement as a fundamental aspect of creating common expectations for the project among all stakeholders, and mitigating risks for themselves, for the project, and for the individuals, communities and other stakeholders affected by the project.[33] Stakeholder engagement is enabled through stakeholder identification, multiple avenues of communication and periodic reporting, two-way dialogues and responding to feedback, addressing grievances through an appropriate mechanism, and communications regarding emergencies that pose risks to the public. A commitment to transparency and disclosure underpins successful stakeholder engagement.

Environmental assessment laws usually require stakeholder consultation as part of the ESIA process, but engagement should not stop there. It should be carried out throughout the life of the project.

Stakeholder identification and engagement[34] should occur at the outset of the project (e.g. during early stage project consultations or the ESIA process). Environmental assessment laws usually require stakeholder consultation as part of the ESIA process, but engagement should not stop there. It should be carried out throughout the life of the project, on a regular and iterative basis, and whenever new activities or significant changes are proposed, or a new issue or risk arises. The contracting parties should engage with the respective stakeholders proactively for early identification of issues and adequate resolution, before issues turn into disputes. Engagement should be based on prior disclosure of an appropriate and sufficient level of information, including in the local language, to enable stakeholders to participate actively.

Since stakeholder engagement is a recurrent activity throughout the project, a sufficient budget should be estimated and set aside for the implementation of the stakeholder engagement plan. Projects should anticipate transportation costs for remote stakeholders, meals and stipends for those who forego their daily wages, venue and translation costs, and in some cases fees for experts who can help design consultation meetings when women, LGBTQ persons, indigenous peoples and others are unable or unwilling to participate in public meetings. It is also helpful for the private operator to employ community liaison staff, who can be the 'face' of the project and a regular point of contact with communities.

When indigenous peoples are involved, the engagement process will require careful attention. The existence of 300 million indigenous people around the world, often in resource-rich areas, means project encounters with and encroachment on their land occurs not infrequently. Since in-depth guidance on the topic of engagement with indigenous peoples is available, this Resource does not discuss the dos and don'ts of engagement with indigenous peoples.[35] This section will only point out that indigenous peoples' free, prior and informed consent (FPIC) must be sought and obtained on key project issues that concern them, in accordance with the requirements under UNDRIP, ILO Convention 169, and in some cases national law. This FPIC process likely will require a longer lead time and an iterative and culturally sensitive approach. The lawyer should be vigilant when this is likely to be an issue.

This consent issue is especially difficult for lawyers where there is debate over whether there are indigenous peoples in a given area. Many states deny the presence of indigenous peoples within their borders. At the same time, investors have independent responsibilities to apply the FPIC standard and respect other rights of indigenous peoples. Given that the social licence to operate for many projects will depend on how they have addressed this issue, purely legalistic debates will not solve this problem in these instances. Thus, structuring how engagement takes place may become an important role for the lawyers to ensure any gaps are bridged in a constructive way.

When asked, government agencies often say stakeholder engagement is a responsibility of the private operator. In fact, it is a responsibility of the project, and as a result specific tasks should be shared between the contracting parties. The contracting authority's representative(s) should always be present at public consultation events organised by the project, and on specific topics within its domain, such as regulations, tariffs, or law and order, to name a few, it may be appropriate for the contracting authority to initiate public meetings. The respective engagement responsibilities of the contracting parties should be recorded in the contract. This can be in the form of a structured ongoing stakeholder engagement plan, which could be mandated in the contract.

As noted above, the UNGPs include a component on remedying breaches of human rights. The private operator and the contracting authority should both consider ways to facilitate access to effective grievance mechanisms that meet the requirements of Principles 28 through 31 of the UNGPs. For the private operator, it would be appropriate to establish a non-judicial operational-level grievance mechanism.[36] When a project is providing infrastructure or other public services, the contracting authority could consider ways to enable consumers and members of the public to provide project feedback. These can be a national ombuds function or other quasi-regulatory complaints or feedback mechanisms. The investment contract should explicitly provide for these mechanisms, so that grievances of all relevant stakeholder groups are captured and considered. The volume and nature of complaints received and the project follow-up actions should be accounted for (without attribution) in the project's regular reporting.

As part of the project's emergency preparedness and response system, the private operator should collaborate with local governments and affected communities to prepare them for emergencies, and actively communicate appropriate response activities, resources and responsibilities on an ongoing basis. Such engagement is crucial when the relevant local governments have little or no capacity to respond to emergency situations. The contract should also make clear that, when an emergency situation is anticipated or ongoing, the contracting parties must co-ordinate in order to ensure proactive, clear and precise communications to the affected communities, and to carry out the respective emergency response measures.

Guidance VII: Identifying and engaging with stakeholders

- ✓ The project should: have a systematic approach to stakeholder identification and engagement; set out a plan and budget; and make implementation a contractual obligation.
- ✓ Ensure that both contracting parties have responsibilities for ongoing stakeholder identification and engagement.
- ✓ Pay particular attention to engagement with indigenous peoples and their right to free, prior, and informed consent.
- ✓ Establish grievance mechanisms and ombuds systems and other measures to receive grievances of the affected stakeholders.
- ✓ Be specific about the need for open and precise communication regarding and during project emergencies.

Notes

1 Accepting a contract prepared by the investor as a starting point of negotiations is guaranteed to set the government negotiators up to respond to what the investor wants as opposed to setting forth its own goals and interests forcefully. This may create an imbalance that is reflected in the final result. If the government does not have a model or template of its own, it is better to start with a term sheet of negotiable items rather than a draft produced by the investor.

2 Such as the MMDA.

3 Organisations that offer such services include the Commonwealth Secretariat, the German CONNEX initiative, IISD, CCSI, and the International Senior Lawyers Project. Numerous other city and national bar associations and non-profit organisations also offer services.

4 Some question the notion of maximising environmental benefits. In our view this comes from moving past notions of doing no or minimal harm to understanding how ecosystem services and uses can be enhanced by careful stewardship of the environment and by utilising environmental restoration processes as much as possible when generating environmental plans. These processes can help enhance the environmental benefits of a project.

5 See: IFC Performance Standard 1 on the requirements of ESIAs. Other MDBs also have specific requirements on the assessment processes. In addition, some have a free-standing standard on community engagement, whereas IFC Performance Standard 1 incorporates community engagement requirements alongside those for ESIAs.

6 Available at: https://www.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_Site/Sustainability-At-IFC/Policies-Standards/Performance-Standards. Also see the detailed Guidance Notes that correspond to the Performance Standards.

7 See Equator Principles website, https://equator-principles.com/

8 OECD (2020), *Recommendation of the Council on Common Approaches for Officially Supported Export Credit and Environmental and Social Due Diligence*, available at: https://legalinstruments.oecd.org/public/doc/280/280.en.pdf

9 See: *EDFI Policy*, available at: https://www.edfi.eu/policy/

10 IADB (2006), *Operational Policy on Indigenous Peoples and Strategy for Indigenous Development*, available at: http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=2032081

11 Equity here does not mean identical. Indigenous peoples have special rights under international law for cultural and other protections that may lead to very specific results. The point, however, is that these rights should not be addressed at the expense of addressing the impacts on non-indigenous communities.

12 See, for example, World Bank (2018), *Good Practice Note Addressing Gender Based Violence in Investment Project Financing involving Major Civil Works*, available at: http://documents1.worldbank.org/curated/en/399881538336159607/Environment-and-Social-Framework-ESF-Good-Practice-Note-on-Gender-based-Violence-English.pdf

13 Flyvbjerg, Bent (2011), *Over Budget, Over Time, Over and Over Again: Managing Major Projects*, in Peter W G Morris, Jeffrey K Pinto, and Jonas Söderlund (eds), *The Oxford Handbook of Project Management*, Oxford: Oxford University Press, pp. 321–344, 2013, DOI: 10.1093/oxfordhb/9780199563142.003.0014

14 See, for example: IFC (2010), *Strategic Community Investment: A Good Practice Handbook for Companies Doing Business in Emerging Markets*, available at: https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/publications/publications_handbook_communityinvestment__wci__1319576907570

15 An early analysis of this is seen in Cosbey, Aaron and Howard Mann (2014), Bilateral Investment Treaties, Mining and National Champions: Making it Work, IISD, available at: https://www.iisd.org/sites/default/files/publications/bilateral_investment_treaties_mining_national_uneca.pdf

16 See IFC Performance Standard 2, para 17.

17 See, for example: IFC, *Investing in Women: New Evidence for the Business Case*, available at: https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/gender+at+ifc/priorities/entrepreneurship/investing+in+women_new+evidence+for+the+business+case

18 Cosbey et al. (2016), *Mining a Mirage? Reassessing the shared-value paradigm in light of the technological advances in the mining sector*, IISD, available at: https://www.iisd.org/sites/default/files/publications/mining-a-mirage.pdf; Ramdoo, Isabelle (2019), New Tech, New Deal: Technology Impacts Review, Intergovernmental Forum on Mining and Sustainable Development, available at: https://www.iisd.org/publications/new-tech-new-deal-technology-impacts-review

19 World Bank (2018), *Emerging Trends in Mainstreaming Climate Resilience in Large Scale, Multi-sector Infrastructure PPPs*, available at: https://library.pppknowledgelab.org/PPIAF/documents/2874/download

20 This is consistent with Principle VII of the 2020 OECD Guiding Principles on Durable Extractive Contracts, available at http://www.oecd.org/dev/Guiding-Principles-Durable-Extractive-Contracts-2020.pdf, discussed in more detail in section 5.5.

21 See, for example, Knoll, Jocelyn L and Shannon L Bjorklund (2014), 'Force Majeure and Climate Change: What is the New Normal?', *Journal of the American College of Construction Lawyers*, Vol. 8 No. 1, available at: https://www.dorsey.com/-/media/files/newsresources/publications/2017/force-majeure-and-climate-change-what-is-the-new-normal.pdf?la=en

22 The Energy Charter Treaty (ECT) is one such treaty that investors have frequently turned to in order to block government climate change measures. This treaty has led to decisions that have supported both states

and investors on exactly the same facts, highlighting the deep levels of risk states assume with the ECT. This is important as the ECT Secretariat is actively pursuing membership from developing countries, despite the fact the European Commission and other agencies have expressed the need for deep changes to the treaty text. See Bernasconi, Nathalie (2018), 'How the Energy Charter Treaty Could Have Costly Consequences for Governments and Climate Action' (blog), IISD, available at: https://www.iisd.org/articles/how-energy-charter-treaty-could-have-costly-consequences-governments-and-climate-action

23 The provisions are discussed in more detail in Mann, Howard (2019), 'Reducing IIA Risks to Climate Change Rules Using Permits' (blog), IISD, available at: https://www.iisd.org/articles/foreign-investment-climate-change-rules. For full disclosure, Howard Mann advised the Maryland Attorney General's office on this merger and the negotiation of these clauses to protect the government's right to regulate for climate change purposes.

24 UN OHCHR (2015), Principles For Responsible Contracts: Integrating The Management Of Human Rights Risks Into State–Investor Contract Negotiations: Guidance For Negotiators, available at: https://www.ohchr.org/Documents/Publications/Principles_ResponsibleContracts_HR_PUB_15_1_EN.pdf; also see: UN OHCHR (2015), A Turn to Responsible Contracting: Harnessing Human Rights to Transform Investment, available at: https://e15initiative.org/wp-content/uploads/2015/09/E15-Investment-OHCHR-Final.pdf

25 Although this duty to protect is mentioned explicitly in the context of business and human rights, states also have the additional responsibility to respect and fulfil human rights under international law.

26 Under the UNGPs, human rights are understood, at a minimum, as those expressed in the International Bill of Human Rights (the Universal Declaration of Human Rights, the International Covenant on Economic, Social and Cultural Rights, and the International Covenant on Civil and Political Rights and its two Optional Protocols) and the principles concerning fundamental rights set out in the ILO's Declaration on Fundamental Principles and Rights at Work. The commentary on Principle 12 of the UNGPs goes on to state that, 'Depending on circumstances, business enterprises may need to consider additional standards. For instance, enterprises should respect the human rights of individuals belonging to specific groups or populations that require particular attention, where they may have adverse human rights impacts on them. In this connection, United Nations instruments have elaborated further on the rights of indigenous peoples; women; national or ethnic, religious and linguistic minorities; children; persons with disabilities; and migrant workers and their families. Moreover, in situations of armed conflict enterprises should respect the standards of international humanitarian law.' The responsibility to respect these human rights is a responsibility that exists over and above compliance with national laws and regulations protecting human rights (UNGPs, Principles 11 and 12).

27 UNGPs Principles 11, 12 and 18.

28 UN OHCHR and Heinrich Böll Stiftung (2018), *The Other Infrastructure Gap: Sustainability. Human Rights and Environmental Perspectives*, available at: *https://www.ohchr.org/documents/Publications/TheOtherInfrastructureGap_FullLength.pdf*

29 See: IFC (2012), 'The International Bill of Rights and IFC Sustainability Framework', available at: https://www.ifc.org/wps/wcm/connect/

topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/publications/ibhr_ifc_sustainability_framework

30 It is also appropriate to mention the Voluntary Standards on Security and Human Rights (available at: https://www.voluntaryprinciples.org/), a multi-stakeholder initiative with government, business and NGO members committed to addressing the use of security personnel in business in a human rights compatible manner.

31 UN General Assembly in its Declaration of the High-level Meeting of the General Assembly on the Rule of Law at the National and International Levels defines gross violations of human rights as genocide, war crimes and crimes against humanity, or for violations of international humanitarian law and gross violations of human rights law (para 22). United Nations A/RES/67/1 (2012).

32 Available at: https://www.ohchr.org/Documents/HRBodies/HRCouncil/WGTransCorp/Session6/OEIGWG_Chair-Rapporteur_second_revised_draft_LBI_on_TNCs_and_OBEs_with_respect_to_Human_Rights.pdf

33 Principles for Responsible Contracts, Principle 7, Community Engagement.

34 For a complete guide to stakeholder engagement see, for example: Inter-American Development Bank (2013), *Guidelines on Consultation and Stakeholder Engagement in IDB Projects*, available at: https://publications.iadb.org/publications/english/document/Guidelines-on-Consultation-and-Stakeholder-Engagement-in-IDB-Projects.pdf; IFC (2007), *Stakeholder Engagement: A Good Practice Handbook for Companies Doing Business in Emerging Markets*, available at: https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/publications/publications_handbook_stakeholderengagement__wci__1319577185063; and OECD (2017), *Due Diligence Guidance for Meaningful Stakeholder Engagement in the Extractive Sector*, available at: https://www.oecd.org/publications/oecd-due-diligence-guidance-for-meaningful-stakeholder-engagement-in-the-extractive-sector-9789264252462-en.htm

35 Several resources are available to guide FPIC implementation; for example, see: FAO FPIC Tool Kit, available at: http://www.fao.org/indigenous-peoples/our-pillars/fpic/en/

36 See: The Office of the Compliance Advisor/Ombudsman (2007), *A Guide to Designing and Implementing Grievance Mechanisms for Development Projects*, IFC, available at: http://www.cao-ombudsman.org/howwework/advisor/documents/implemgrieveng.pdf

Chapter 5

Related General Guidance for Contracts

Chapter 5
Related General Guidance for Contracts

Previous chapters have addressed some of the specific issues around procedural and substantive rights and obligations in relation to environmental, social and economic clauses in investment contracts. But for them to be effective there must also be a range of surrounding processes and obligations that apply not just to these issues but to the contract as a whole. It is to this set of issues that we turn now.

5.1 Ensure third-party rights are protected

The sudden burst of on-site activities during the feasibility study and ESIA stages can signal to local communities the possible magnitude of the development impacts to come from the proposed project, both positive and negative. From this stage on, the project proponent will have to manage the concerns and expectations of the local officials and communities, while moving the project activities forward. Engagement with local communities will help reveal their needs and wants, and the project proponent will be making commitments to address them. Promises will also be made informally in casual encounters with community members (such as a pledge to keep dust and noise down during construction or to pay compensation for domestic animals being run over). The proponent will have to be extremely vigilant in capturing all these commitments, large and small. In some cases, commitment registries are used to memorialise commitments made and to display them transparently for all to see. In most cases, they are enshrined in the ESMP or other plans or agreements. Regardless of the methods used, it is key that communities trust the project to capture and honour commitments.

The investment contract is one of the better places to enshrine commitments, so that the contracting authority can monitor and enforce them in the case of failure to implement.

Commitments can be memorialised on paper, but this will not give people the legal right of enforcement, unless conscious efforts are made to create such right. Commitment registries and benefit plans, if publicly disclosed, can create a moral obligation for the project and possible enforcement by public sentiment, but not necessarily a legal obligation. If the project is receiving financing from one or more multilateral development banks (MDBs), implementation of the plans required to mitigate negative impacts under the MDBs' environmental and social safeguard policies or standards will be covenanted by the borrower (the project proponent) in the loan agreement. This will be a legally enforceable obligation, enforceable by the MDBs. Yet even these long-term lenders will stay with the project for only a few years, whereas the project life will likely extend to up to three decades. The investment contract is one of the better places to enshrine commitments, so that the contracting authority can monitor and enforce them in the case of failure to implement. Another way to create legal leverage is to turn the commitments into an agreement with local communities, or another third party.

In the case of large-scale or complex commitments, especially those designed as mitigation to negative impacts, such as large-scale resettlement, community economic development programmes, indigenous people's development plans, or biodiversity offsets, a free-standing plan is desirable to ensure proper documentation, implementation and follow-up. The plans should be referenced in the contract. This way, at least the contracting authority is in a position to require that the private operator implement the plans. Even in these cases, communities do not have a direct right of enforcement, unless the contract specifically names them as third-party beneficiaries. Hence, a third-party beneficiary clause in favour of the beneficiaries of various mitigation plans in an investment contract is one way of ensuring a contractual right and leverage of affected persons. Another intermediate measure would be to state that material non-compliance with mitigation plans should attract the same sanctions as material non-compliance with the contract provisions themselves (also see Section 4.4).

A direct agreement between the project and the local authority and/or one or more representatives of the affected community will be a superior instrument for ensuring legal enforceability. Community development agreements (CDAs) are frequently used in the extractives sector to assure the affected communities of local economic and social development, including the funding obligation. This is often done as a mitigation measure to community-wide impacts from projects; it is also a way to share the project's wealth with communities and to maintain the project's social licence to operate. Close to 40 jurisdictions mandate community development in mining laws (though not necessarily CDAs), many of which are Commonwealth jurisdictions.[1] CDAs are particularly prevalent when indigenous peoples' land, rights or interests may be implicated in the project. Ample examples of CDAs exist and can be searched in ResourceContracts.org's database. Some agreements are structured as a tripartite agreement between the project, local government, and the affected communities, in order to ensure enforceability and protection of all parties' rights and interests. There are no technical reasons why similar arrangements cannot be used in other sectors to ensure that communities are able to enforce community development and other commitments that run to them.

Formal agreements are also used in the case of complex mitigation arrangements that require an active role for a third party. For instance, a biodiversity offset and management plan may require a non-governmental organisation (NGO) as an offset manager, whose terms of engagement would be best captured in an agreement between the project and the NGO, rather than a reference in the investment contract. In rare cases, communities can be offered an opportunity to purchase equity in the project company.

Box 5.1 Ensuring community ownership through purchase of equity in the project company

The Model Project Development Agreement for the Government of Nepal for hydroelectricity projects of less than 500MW contemplates the possibility of project-affected people purchasing equity in the project company:

[Section 15.5] 'All Project Affected People required to be resettled and rehabilitated as a result of the Project, including all persons residing permanently in the district of the Project Area at the date on which the construction activities for the Project commence, may, by written notice to the Company and/or the GON [the Government of Nepal] in the period from the Effective Date to two years beyond COD [commercial operation date], exercise an option to purchase up to a .... equity share in the Company at face value. On receipt of such notice, the Company shall make arrangements to sell the requested equity share in the Project to such people in consultation with the GON.'

Such an arrangement will obviously have to be finalised via a direct contractual agreement between the project company and the purchaser of the shares.

Source: Model Project Development Agreement (for Hydropower Projects with installed capacity less than 500MW) (Nepal).

A material failure to implement the agreements, or persistent failure to correct breaches of agreements should be designated as a breach of the investment contract and should attract the same sanctions as material non-compliance with the contract provisions themselves. However, it is generally the case that affected stakeholders would prefer breaches of commitments to be rectified amicably and flexibly rather than to pursue judicial or arbitral remedies.

Guidance VIII: Respecting third-party rights

- ✓ The social, environmental and economic rights and benefits for local communities should be enforceable by the local communities, and not only by the contracting authority.
- ✓ Community development agreements and other third-party agreements are the best vehicle for creating direct legal right of enforcement by communities or other affected third parties.
- ✓ When plans are used and mentioned as mandatory in the contract, the contract could name the third parties as third-party beneficiaries under the contract.
- ✓ A material failure to implement the plans or agreements, or persistent failure to correct breaches of plans or agreements should be designated as a breach of the investment contract and should attract the same sanctions as material non-compliance with the contract provisions themselves.

5.2 Transparency of contracts[2]

Transparency, as a governance and human rights concept, is a prerequisite for accountability of both the contracting authority and the private operator, as well as a means to eradicate corruption.

Transparency underpins sustainable development in multiple ways. Prior disclosure of project information greatly aids the quality of participation of project-affected people in consultation, which in turn can contribute to improved project design and outcomes. Disclosure of project information allows local communities to understand the nature and scope of project commitments, which in turn enables them to participate in project monitoring and enforce obligations that affect them. Transparency, as a governance and human rights concept, is a prerequisite for accountability of both the contracting authority and the private operator. And transparency is a means to eradicate corruption throughout the project life cycle, including in bidding and construction stages. Beyond these project-level benefits are broader benefits. Some governments have reasoned that transparency of investment can enhance their reputation and stimulate additional investment.

In the extractives sector, transparency of projects and contracts has been a recognised industry best practice for two decades, and many contracts are publicly available in well-organised databases, as already mentioned above. However, not all governments and investors follow this best practice. To support this or similar best practice, and to encourage the infrastructure and other sectors to follow suit, this Resource advocates for transparency commitments to be embedded in the investment contract, and for the lawyer to advocate for transparency throughout the project life cycle.

An investment contract should not constrain the contracting parties to keep the terms of the parties' agreement confidential; instead, it should set out the principle of presumption in favour of disclosure, and allow the parties to freely disseminate key project information, such as the ownership structure of the project company, the financial structure of the project (especially the financial incentives offered by the government), the project contract, and the full monitoring information, such as the performance reporting by the private operator, and any reports generated by the project company for submission to the regulator (whether the contracting authority or another agency). If necessary, the parties should agree at the outset what may constitute proprietary business information or sensitive information that would not be subject to the presumption in favour of disclosure; however, they should be aware that much of this information may already be in the public domain. This is often the case with commercial information that is disclosed to industry press for promotional purposes. In some countries, the entire contract is part of parliamentary record and accessible by anyone who seeks it. Amendments and modifications to the contract should also be disclosed.

Box 5.2 Ghana's Petroleum Register

In 2018, Ghana launched its new petroleum register, which discloses a wide range of information on the companies extracting the country's oil, including the actual contracts. It joins 29 countries that are members of the Extractive Industries Transparency Initiative (EITI) which have published at least some oil, gas and mining contracts.

Source: EITI (2018), 'The Journey to Contract Disclosure in Ghana' (blog), available at: https://eiti.org/blog/journey-to-contract-disclosure-in-ghana

Box 5.3 Nigeria's transparency initiative: PPP contracts disclosure web portal

Within the first 100 days of the administration of President Buhari, Nigeria pledged to promote transparency in all ministries and departments, and as part of such commitment, launched the Infrastructure Concession Regulatory Commission (ICRC) PPP Contracts Disclosure Web Portal in September 2017. The rationale for the Portal is to expose consistent project processing procedures from the project start in order to signal efficiency in its ability to process investments, to explain the important features of service standards and the PPP contract, and to demonstrate good project performance, while repelling corruption. This in turn is expected to attract additional foreign capital and expertise to bridge the infrastructure gap in Nigeria.

ICRC requires contract parties to disclose the following items on its portal:

- Financial structure of the SPV (special purpose vehicle)
- Redacted PPP contract
- Renegotiations and renegotiated contract
- Performance information

Source: ICRC (2017), 'PPP Contract Disclosure Portal: Key to Improvement of Infrastructure Deficit in Nigeria?', available at: https://www.lexology.com/library/detail.aspx?g=eda7a188-1cc6-45ac-93d4-71c3e9cb3005

Also see: World Bank (2016), *A Framework for Disclosure in Public-Private Partnership Projects*, available at: https://www.worldbank.org/en/topic/publicprivatepartnerships/brief/a-framework-for-disclosure-in-public-private-partnership-projects

Lawyers can play a valuable role in a project team, beyond providing mechanical legal advice. Clients look up to lawyers as a voice of reason and moral authority and expect to receive legal and even business or non-legal advice based on the lawyer's knowledge and direct experience. In this vein, lawyers can also be an advocate for transparency within governments, and push for disclosure portals and other disclosure mechanisms to make it easier for the public to access project information and contracts. The World Bank's Framework for Disclosure in PPPs (see Box 5.3) provides a blueprint for how this can be done in the context of PPPs for infrastructure projects, but the principles and approaches are equally relevant in other investment sectors and structures.

Guidance IX: Transparency of contracts

- ✓ Each contracting party should be free to disclose the investment contract when concluded.
- ✓ If the contract contains truly sensitive or proprietary information, it can be redacted. It is important to note that redactions lead to questions as to what is withheld and why.
- ✓ An online, publicly accessible database can be used as an access point for public contracts.
- ✓ After material modification or amendment, the contract should be disclosed again.

Sample Text: Transparency

World Bank Guidance on PPP Contractual Provisions (2019) Section 10.3

[Note: These provisions were excerpted from the World Bank's Guidance on PPP Contractual Provisions. Although they are intended for PPP contracts, they will work well with contracts in other sectors. The authors of this Resource both provided extensive comments on the draft Guidance in an effort to improve its content from a sustainability perspective. While the overall quality of the Guidance is uneven, the provisions excerpted here have improved from the previous versions and represent a good reference point for lawyers. The drafting tips that appear in bubbles in the Guidance were deleted as they are technical and refer to other sections of the Guide.]

'Public Relations and Publicity

1. The Private Partner shall not by its directors, officers, employees or agents, and shall procure that its Sub-contractors shall not, communicate with representatives of the press, television, radio or other communications media on any matter concerning the PPP Contract without the prior written approval of the Contracting Authority.
2. The Private Partner may not represent the views of the Contracting Authority on any matter, or use the name of the Contracting Authority in any written material provided to third parties, without the prior written consent of the Contracting Authority.

Publication of the PPP Contract in the public domain

3. The Parties agree that the provisions of this PPP Contract [and insert any other relevant documents defined as the Project Agreements] shall, subject to Clause (7) below, not be treated as Confidential Information and may be disclosed without restriction and the Private Partner acknowledges that the Contracting Authority, subject to Clause (7) below, is entitled to:
    a. publish this PPP Contract [and some of the Project Agreements] on a website; and
    b. publish (on the internet or otherwise) a summary of the PPP Contract [and the Project Agreements and any associated transaction document] which shall include

Sample Text: Transparency (*Continued*)

i. the terms and conditions of the PPP Contract [and the Project Agreements and any associated transaction document] and
ii. any document or information arising out of or connected to the PPP Contract [and the Project Agreements and any associated transaction document], including performance of the PPP Contract [and the Project Agreements and any associated transaction document].

4. The Parties agree that Base Case Equity IRR information shall not be treated as Confidential Information and the Private Partner acknowledges that the Contracting Authority intends to publish such information on a website.
5. The Parties agree that information in respect of any direct or indirect change in ownership which has actually taken place shall not be treated as Confidential Information.

Confidentiality

6. For purposes of this PPP Contract, 'Confidential Information' means:
   a. information (however it is conveyed or on whatever media it is stored) the disclosure of which would, or would be likely to, prejudice the commercial interests of any person, trade secrets, commercially sensitive intellectual property rights and know-how of either Party, including all personal data and sensitive personal data; and
   b. the sub-set of Confidential Information listed in Column 1 of Part I –Commercially Sensitive Contractual Provisions and Column 1 of Part II – Commercially Sensitive Material of Schedule [insert reference to the Commercially Sensitive Information Schedule] in each case for the period specified in Column 2 of Parts I and II of such Schedule ("Commercially Sensitive Information").
7. Clause (3) above shall not apply to Confidential Information which shall, subject to Clause (9) below, be kept confidential for the periods specified in Schedule [insert reference to the Commercially Sensitive Information Schedule].
8. The Parties shall keep confidential all Confidential Information received by one Party from the other Party relating to this PPP Contract [and any Project Agreements] or the PPP Project and shall use all reasonable endeavors to prevent their employees and agents from making any disclosure to any person of any such Confidential Information.
9. Clauses (7) and (8) above shall not apply to:
   a. any disclosure of information that is reasonably required by any person engaged in the performance of their obligations under the PPP Contract for the performance of those obligations;
   b. any matter which a Party can demonstrate is already, or becomes, generally available and in the public domain otherwise than as a result of a breach of this Clause [Confidentiality];
   c. any disclosure to enable a determination to be made under Clause [insert reference to Dispute Resolution clause] or in connection with a dispute between the Private Partner and any of its sub-contractors;

Sample Text: Transparency (*Continued*)

d. any disclosure which is required pursuant to [insert reference to legislation containing public disclosure obligations] as well as any other statutory, legal (including any order of a court of competent jurisdiction) or Parliamentary obligation placed upon the Party making the disclosure or the rules of any stock exchange or governmental or regulatory authority concerned;

e. any disclosure of information which is already lawfully in the possession of the receiving Party, prior to its disclosure by the disclosing Party;

f. any provision of information to:

   i. the Parties' own professional advisers or insurance advisers; and/or

   ii. the Lenders or the Lenders' professional advisers or insurance advisers or, where it is proposed that a person should or may provide funds (whether directly or indirectly and whether by loan, equity participation or otherwise) to the Private Partner to enable it to carry out its obligations under the PPP Contract, or may wish to acquire shares in the Private Partner in accordance with the provisions of this PPP Contract to that person or their respective professional advisers but only to the extent reasonably necessary to enable a decision to be taken on the proposal; and/or

   iii. international or bilateral financial institutions involved in the PPP Project as Lenders, political risk insurers or guarantors; and/or

   iv. any rating agency which may be engaged to provide a rating or rating assessment in relation to any Senior Debt;

g. any disclosure by the Contracting Authority of information relating to the design, construction, operation and maintenance of the PPP Project and such other information as may be reasonably required for the purpose of conducting a due diligence exercise, to any proposed new private partner, its advisers and Lenders, should the Contracting Authority decide to re-tender the PPP Contract or undertake any market testing;

h. any registration or recording of the required permits and property registration required;

i. any disclosure of information by the Contracting Authority to any other relevant authority or their respective advisers or to any person engaged in providing services to the Contracting Authority for any purpose related to or ancillary to the PPP Contract; or

j. any disclosure for the purpose of:

   i. the examination and certification of the Contracting Authority's or the Private Partner's accounts;

   ii. any examination pursuant to [insert reference to any auditing obligations for public contracts] of the economy, efficiency and effectiveness with which the Contracting Authority has used its resources;

   iii. complying with a proper request from either Party's insurance adviser, or insurer on placing or renewing any insurance policies; or

Sample Text: Transparency (*Continued*)

iv. (without prejudice to the generality of Clause (d) above) compliance with [insert reference to any laws requiring disclosure (e.g. environmental laws)]].

10. When disclosure is permitted under Clause (9) above, other than Clauses (9)(b), (d), (e), (h) and (j), the Party providing the information shall ensure that the recipient of the information shall be subject to the same obligation of confidentiality as that contained in this PPP Contract. [The Private Partner shall expressly inform any person to whom it discloses any information under this Clause [Confidentiality] of the confidentiality restrictions set out in this Clause [Confidentiality] and shall procure its compliance with the terms of this Clause [Confidentiality] as if it were Party to this PPP Contract and the Private Partner shall be responsible for any breach by any such person of the provisions of this Clause [Confidentiality].]
11. Where the Private Partner, in carrying out its obligations under the PPP Contract, is provided with information relating to [end users], the Private Partner shall not disclose or make use of any such information otherwise than for the purpose for which it was provided, unless the Private Partner has obtained the prior written consent of that [end user] and has obtained the prior written consent of the Contracting Authority.
12. On or before the expiry date, the Private Partner shall ensure that all documents or computer records in its possession, custody or control, which contain information relating to [end users] including any documents in the possession, custody or control of a Sub-contractor, are delivered up to the Contracting Authority.
13. The provisions of this Clause [Confidentiality] are without prejudice to the application of [insert any relevant law governing official secrets or national security information].'

MMDA, Preamble and Article 30.1

[...]

Whereas, the Parties recognize that this Agreement is of fundamental public importance and that it is and by its nature ought to be freely and publicly available on request to any person requesting it;

[...]

Art. 30: This Contract is a Public Document

30.1 This Contract a Public Document

a. This Agreement and the Documents required to be submitted under Section 2.4, by any past and present Parties is a public document, and shall be open to free inspection by members of the public at the appropriate State office and at the files designated in the following subsection (e), and at the Company's office in the State during normal office hours.
b. There shall be a presumption that any information regarding this Agreement, or the activities taken under this Agreement is public, other than Confidential Information.
c. All reports and submissions by the Company to the State, and all responses by the State, are freely available on request to the State

Sample Text: Transparency (*Continued*)

or the Company, provided that Confidential Information may be redacted prior to disclosure.

d. The Company shall maintain document files to facilitate public access to this Agreement and the Documents, and informed participation in all Consultation required by this Agreement. These files shall contain this Agreement, the Documents, all adopted updates and amendments thereto, and information on payments and reporting under Section 30.0 of this Agreement. These files shall be maintained at the following locations and shall be open to all members of the public during normal business hours:

e. On payment of a reasonable fee prescribed by the State, any member of the Public shall be entitled to obtain a copy of this Agreement from the appropriate State office or at the Company's offices listed above.

5.3 From enforcement to compliance promotion: Monitor and report on project performance and material events

Where investment contracts are part of the investment-making process, their execution is a crucial milestone in a project life cycle. Without the contract, no financing can flow and no construction can begin. (Of course, signing a contract in and of itself is not a guarantee for financing or construction, since other conditions precedent may still have to be met.) As a result, much effort and resources are expended to enable the contracting parties to reach this milestone. Until this point in the project life cycle, project monitoring and reporting seem distant activities that hardly merit any attention. Consequently, contracts often fail to specify the scope of these obligations in detail, and contracting parties frequently neglect this important aspect during project implementation.

Concluding a contract marks the beginning point of what is intended to be a long-term relationship between the investor, the government, and in many cases the local communities. This view allows one to better understand the need for the contract to set out the processes and institutions needed to manage the contract over, potentially, several decades. It is in this context that this section should be viewed.

Concluding a contract marks the beginning point of what is intended to be a long-term relationship between the investor, the government, and in many cases the local communities.

It is also important to understand that the traditional concept of enforcement of the legal obligations of the project company, whether derived from national law or the contract, is being challenged. The old view of large government departments whose function it is to inspect sites, monitor compliance, issue orders where compliance is poor or non-existent, and take legal measures against the company in court when needed has become largely dysfunctional or is non-existent today. This is not just a developing country issue, but applies equally to developed countries. Governments, often facing demands for lower taxes and smaller government, have simply stopped funding these enforcement activities. Investors understand that the impact of this is to significantly reduce the chances of being caught in violation of their obligations, and that any risks of fines being imposed is small.[3] Yet compliance remains a critical issue, and especially for the local communities that may be most immediately and seriously impacted by non-compliance with the sustainability-related obligations.

Investors and governments must understand that the concept of a social licence to operate is an ongoing concept. It does not automatically remain in effect throughout the life of the project but must be maintained with a sense of deliberateness every year of operation of the project.

The core of a compliance promotion model is routine, usually annual, reporting and monitoring obligations.

Fortunately, these challenges have a common solution that shifts the traditional enforcement model to a community-based compliance promotion model. It seeks to shift the project company from evaluating the risk of being caught not complying to an understanding that its social licence to operate is dependent on demonstrating its compliance with agreed social, economic and environmental obligations. The core of a compliance promotion model is routine, usually annual, reporting and monitoring obligations.

Monitoring and reporting obligations are activated once the project operator enters into the construction phase, gathers sufficient data on key performance indicators and parameters, and reports on its performance using an appropriate reporting format that is accessible to the national and local stakeholders. Monitoring and reporting inform the private operator and the contracting authority of project performance, and can help improve poor performance through corrective actions. Because of its importance, some contracts stipulate that monitoring data should be verified by a third party on an annual basis.[4] Project reports can inform other host government agencies, such as those in charge of the environment or labour matters, that can make appropriate protective interventions as necessary.

The private operator should inform the project's contractors and subcontractors of the project's obligations with respect to environmental, social and economic sustainability, and be legally required to pass on the appropriate requirements to them in order to ensure these entities comply with them.

Project reports also inform stakeholders, including the affected communities. In fact, community members need not be passive recipients of project data; they can play a proactive role by participating in project monitoring activities, and even in the enforcement of contractual provisions that affect them. Without monitoring and reporting, the project will not know about its performance and has nothing to tell its stakeholders.

Meaningful monitoring is facilitated first by contractual transparency, as discussed above. Stakeholders need to be clear about the scope of the project and the respective obligations of the contracting parties.

The contract should establish KPIs for the project's environmental, social and economic development performance, as discussed in the sections on the substantive obligations in these areas. The indicators should reflect issues of importance to the project and the stakeholders. Obviously the KPIs will differ significantly from project to project and sector to sector. For instance, in the case of infrastructure projects, indicators regarding service quality, regularity of service, physical accessibility, affordability, acceptability and safety considerations would be meaningful to consumers of these services, other stakeholder groups, members of the public generally, the

Box 5.4 Community employment in the Far North in Canada

Remote environments are among the hardest places to manage employment issues in large-scale investments. In one mine on Canada's northern territories where indigenous peoples predominate, the investors had promised a designated number of jobs for local employment. But the company found that while it could still scramble and meet the targets, the turnover rate of employees was almost 75 per cent every year, making it hard to have a consistent workforce and to stay on target. Neither the employees nor the company were achieving their goals. The company engaged the community to find out why the turnover rate was so high. The community elders found this was because the employees tended to have lower wages and less rewarding jobs and, most importantly, no career paths. When the company adopted stronger measures to promote career paths instead of just a job, retention rates reversed, with less than 25 per cent turnover every year. The monitoring process here led to stronger compliance with the targets and better results for all stakeholders.

contracting authority, and other government agencies. Data on these KPIs should be collected regularly, and should be disaggregated by stakeholder groups whenever possible to ensure that priority is given to those who are worst off, and that targeted interventions (whether by the contracting authority or another agency of the host government) can be directed to these people as necessary. Similarly, the key targets set out in the contract for social projects, employment opportunities, gender equality, local purchasing, etc., can be measured and reported against, showing progress or lack of progress in achieving the contractual obligations in these areas.

The private operator and the contracting authority both have obligations to report on the project performance, including appropriate corrective actions taken in the case of incidents and issues, at least annually. The private operator should be responsible for issuing the project's sustainability reports.

Many companies are wary of ongoing public reporting obligations. In some cases, this is due to the perception that any failure to fulfil an obligation can be seen as a breach of the ongoing contract, which should not be shared with those outside the project. Thus, it is important to understand the role of KPIs in relation to compliance in order to achieve positive results. In practical terms, this means highlighting the KPIs as targets, not as absolute compliance issues. This allows a failure to meet the targets to be treated as part of the long-term engagement with the community to achieve

Box 5.5 Financial mechanisms to ensure corrective action

The private operator should set up one or more financial mechanisms to ensure adequate funds are available for contingencies, corrective actions, or project closure to avoid shortfalls and failure to remedy harm created by the project. This should be a general provisioning that is separate from specific budgets to be set up for implementation of one or more of the plans described in this Guidance. By way of example, projects can purchase **insurance policies** and **performance bonds** for certain specified events, including extreme weather events. In addition, **escrow accounts, sinking funds or contingency funds** can be established for specific events, and **indemnity** can be used in the case of damage caused to the environment or people. Financial provisioning is particularly important at the end of the project, which could face significant site rehabilitation obligations and economic obligations to the local community, and yet be short on funds and human resources to address them; as a result, some jurisdictions require **closure plans and financing** for their implementation, especially in the mining sector.

and exceed the obligations. It is only when there is an ongoing failure to remedy the poor performance, and a failure to show good faith efforts to correct non-compliance, that issues will rise to the level of a material breach of the contract allowing enforcement action or even termination of the contract. Some projects use various financial measures (see Box 5.5) to ensure that funds are available in the event of performance failures and contingencies to pay for corrective action.

Projects have many types of sustainability reporting formats to choose from, depending on many factors, from internal strategy and sector-wide preferences, to regulatory requirements. The contracting authority may have regulatory reporting obligations to the central government or may take it upon itself to provide its own assessment of project performance under applicable law. These reports should be publicly available on the project website and an appropriate site of the government. The contracting parties are also jointly responsible for timely provision of information to stakeholders on material events and incidents that pose a risk to them or otherwise may concern them.

Guidance X: Options for compliance promotion

- ✓ The contract should anticipate the project's monitoring and reporting needs and allocate the responsibilities appropriately between the contracting parties.
- ✓ Community members should be enabled to participate in project monitoring.
- ✓ The private operator should inform the project's contractors and subcontractors of the project's obligations with respect to environmental, social and economic sustainability, and be legally required to pass on the appropriate requirements down to them in order to ensure these entities comply with them.
- ✓ Targets should be well defined and measurable but should be treated as goals to be achieved collaboratively rather than black and white compliance issues. This allows all parties to learn as the project unfolds. At the same time, a persistent failure to achieve the goals, or to make best efforts to achieve them, should be elevated to an issue of material compliance with the project company's obligations.
- ✓ Regular disclosure of the project's monitoring information will enable affected communities to act as de facto enforcers of specific obligations owed to them.

5.4 Applicable law

It is important for the applicable law clause to clarify first that the domestic law of the host state is the overall applicable law.

Chapter 3 addressed the relationship between different sources of law that might apply to foreign investments: domestic law, investment contracts and international investment treaties. It looked at the 'right' and 'wrong' form of relationships. In contract terms, one aspect of these issues will play out in what is usually referred to as an 'applicable law' clause. An applicable law clause sets out what the governing law of the project and the contract is and, often, what law will apply in the event of a dispute that goes to court or an arbitration tribunal.

In this context, it is important for the applicable law clause to clarify first that the domestic law of the host state is the overall applicable law. This may seem obvious, but it is only in recent practice that this has been fully recognised. Until the last decade or so, it was common for contracts to identify the law of New York, England, France or other former colonial powers or commercial or financial centres as the law governing the contract and project. The thinking on this was that these bodies of law were better developed to deal with commercial disputes and stayed more consistent than the laws in developing countries, leading to more predictable legal environments. This approach is no longer seen as appropriate. Governments should ensure that the applicable law is defined as the law of the host state, since all aspects of the project's activities will be effectively subject to the laws of the host state.

A second issue is what source of law prevails in the event of conflict: the applicable law or the contract. In our view, the law should prevail and the contract should be required to be consistent with the applicable local law. As discussed in Chapter 3, the contract should be used to implement the applicable law in the specific circumstances of the project at hand, not displace that law. Governments should strive to have as much of the legal regime applying to investments in the domestic law as possible to have the most transparent and consistent application of the law, avoid unnecessary negotiations with each large-scale investor, minimise the opportunities for corruption and imbalances in results, and promote an environment that respects domestic law.

A third issue is often the role of international law in these contracts. In some instances, international law is defined as part of the applicable law, often as a supplement to the domestic law. This is often also seen in applicable law clauses that provide for a specific application of international law to investment contracts between governments and foreign investors. This can be acceptable, as long as international law is a supplement to and does not displace the host state law as the primary applicable law.

These details are consequential and lawyers should ensure they are correct in order to preserve the appropriate relationship between the domestic law, the contract and international law.

Guidance XI: Applicable law

- ✓ The domestic law of the host state should be defined as the applicable law governing the contract and the project.
- ✓ Contracts should comply with the applicable domestic law, and not contain provisions in breach of the laws. Contracts should be negotiated to implement the domestic law applicable to an investment, not replace it.
- ✓ Governments should strive to have as much of the legal regime applying to investments in the domestic law as possible to have the most transparent and consistent application of the law, avoid unnecessary negotiations with each large investor, and minimise the opportunities for corruption and imbalances in results.
- ✓ Contracts should, where necessary, particularise the application of the domestic law to a specific project, providing sufficient detail to ensure it is clear and enforceable in terms of the obligations on the investor and government parties.

Sample Text: Applicable Law

MMDA, Article 35

This Agreement shall be governed by and construed in accordance with the laws of the State, including international treaties and bilateral investment treaties to which the State is a party (collectively, "Applicable Law").

World Bank Guidance on PPP Contract Clauses, 2019, sample drafting 11: Governing Law

(1) This PPP Contract and any non-contractual obligations arising out of or in connection with it are governed by and shall be construed in accordance with the laws of [country].*

* The governing law selected in a PPP Contract determines the legal system whereby the rights and obligations under the PPP Contract will be determined. Typically, the national law of the Contracting Authority will be the applicable law. (NB: this note accompanies the above text and is included here for clarity of the intended outcome.)

5.5 Avoid stabilisation of non-fiscal laws

For many years, developing country governments were advised that in order to attract large investments they had to make multiple concessions to investors on tax or other incentives and on stabilising the law applicable to the investment. The former point is beyond the scope of this Resource, though we note with some urgency the more recent work of the IMF and OECD and others indicating that tax incentives are generally not a good means of attracting and maintaining investments.[5]

A stabilisation clause (sometimes also referred to as a change in law clause)[6] in investment contracts sets out how changes in law after the execution of the contract will affect the rights and obligations of the parties. Traditionally, stabilisation clauses precluded the application of new laws for the duration of the contract, thus freezing the law applying to the investment as of the day the contract is signed. Alternatively, the clause would allow the new laws to apply, but require the government to compensate the company for any costs of complying. These clauses became known as economic equilibrium clauses and provided economic guarantees to the project company.

Foreign investors and their lawyers, governments are told, will insist on one form or another of these clauses, and argue that the contract will not be bankable without it, especially in countries that are deemed to have an unstable legal environment. Naturally, domestic investors have long been critical of the practice because they are bound by national law as it evolves. More recently, its use has been criticised by civil society organisations and experts for chilling the right and obligation of the host state to protect the environment and people in accordance with its own vision of sustainable development, or pursuant to commitments to reflect obligations under international law in domestic law.[7]

The issue of stabilisation is divided into two parts. The first is fiscal stabilisation, dealing with taxes and other government revenues from a project. This is again beyond the scope of this Resource.[8] The second part is often referred to as non-fiscal stabilisation, and notionally includes any law or regulation that is not fiscal in nature. This would include all of the environmental, social and economic development issues addressed in this Resource. This Resource seeks to address non-fiscal stabilisation.

The prevalence of stabilisation in investment contracts was analysed in some detail by the IFC in a report prepared for Prof. John Ruggie in his capacity as special representative of the UN Secretary General on Business and Human Rights during the preparation of the UNGPs.[9] This report found that the highest percentage of contracts deploying non-fiscal stabilisation clauses was in sub-Saharan Africa, with somewhat lower levels in other developing country regions. The most extreme type of stabilisation clauses (e.g., complete freezing of national law for the duration of the investment contract, some of them extending for 99 years) were prevalent in the mining sector in Africa.[10] The research found virtually no non-fiscal stabilisation clauses applying in the OECD countries. The study also found that these clauses could have significant impacts on the ability of developing countries to meet their international human rights obligations, as they prevented governments from developing new human rights laws that applied to major economic actors in their countries.

Professor Ruggie, in Addendum 3 to his report on the UNGPs: *Principles For Responsible Contracts: Integrating The Management Of Human Rights Risks Into State–Investor Contract Negotiations: Guidance For Negotiators*,[11] concluded that:

> *Contractual stabilization clauses, if used, should be carefully drafted so that any protections for investors against future changes in law do not interfere with the State's bona fide efforts to implement laws, regulations or policies in a non-discriminatory manner in order to meet its human rights obligations. (Principle 4)*

This report also suggested that the private operator factor into its project and financial planning the potential implications of the evolution of the host state's national law.

While this appears on the surface to be a fairly narrow limitation on the use of non-fiscal stabilisation clauses, in practice this is not the case. This is because Ruggie's conception of human rights includes economic and social development rights as well as environmental rights that had begun to solidify as human rights, such as the human right to clean water, while his work was in progress. Thus, a good deal of what is addressed in this Resource is, in principle, covered by the Responsible Contracting[12] framework for business and human rights.

The contracts reviewed for this Resource, which dated from 2010 to 2018, indicate that the practice of stabilisation is in a state of flux. Of the extractive contracts, over 60 per cent of the oil, gas and mining contracts have stabilisation clauses, whereas just under 25 per cent of the agribusiness contracts stabilised new laws. Almost all the infrastructure contracts reviewed contained one kind of stabilisation clause or another. While many contained the traditional, broad stabilisation clauses, several excepted environmental, labour, and health and safety laws from the scope of change in law.

Given the ongoing controversy and flux in drafting, it was not a surprise that the OECD took up the issue again in the context of preparing its Guiding Principles on Durable Extractive Contracts, from 2016–2019. Principle VII of this document now states:

> *Durable extractive contracts are consistent with applicable laws, applicable international and regional treaties, and anticipate that host governments may introduce bona fide, non-arbitrary, and non-discriminatory changes in law and applicable regulations, covering non-fiscal regulatory areas to pursue legitimate public interest objectives. The costs attributable to compliance with such changes in law and regulations, and wholly, necessarily and exclusively related to project specific operations, should be treated as any other project costs for purposes of tax deductibility, and cost recovery in production sharing contracts.*

Within the decade after Prof. Ruggie tied his position on non-fiscal stabilisation to not interfering with the attainment of human rights, the OECD went beyond this to delegitimise the use of non-fiscal stabilisation provisions in extractive contracts.

Thus, within the decade after Prof. Ruggie tied his position on non-fiscal stabilisation to not interfering with the attainment of human rights, the OECD went beyond this to, for all practical purposes, delegitimise the use of non-fiscal stabilisation provisions in extractive contracts. While the OECD text is focused on the extractives sector, as many experts had previously identified the extractives sector as the one most exposed to risks from changes in law due to the high cost of initiating projects and the lengthy return period in many cases, there is no compelling reason why the principle should be limited to that sector. It stands to reason that the same principle should apply to other sectors similarly exposed. In practice, this should include all sectors for which this Resource is relevant, including agribusiness and infrastructure.

In the unusual situation where a change in law results in the inability of an investor to perform its obligations or makes the project financially unsustainable, the contracting authority and the private operator should agree to engage in good faith discussions which might eventually lead the parties to agree to renegotiate the terms of the contract.[13]

Guidance XII: Non-fiscal stabilisation

- ✓ Governments should not agree to accept clauses stabilising the non-fiscal laws applying to an investment.
- ✓ If, despite this clear guidance, governments choose to agree to a stabilisation clause, they should ensure that, consistent with Principle VII of the OECD Guiding Principles on Durable Extractive Contracts, non-fiscal laws such as environmental, labour, health and safety, disclosure and other related laws that aim to protect people and the environment should be excluded from any stabilisation provisions (sometimes also called change of law provisions).
- ✓ Governments should acknowledge that the costs to companies of meeting changes in law should be treated as tax deductible expenses of the company in keeping with other operational expenses.
- ✓ Companies should anticipate changes in national law as an ongoing process and budget to comply with changes in the normal course of affairs.

Sample Text: Stabilization or Change in Law

[*Note: We do not include this as a model to adopt, as explained in §5.5. However, this text does show the complexity that can result from negotiation complex stabilization clauses, and the many risks that can be incurred in this complexity.*]

Model Concession Agreement for Hydro less than 500MW (Nepal)

'Change in Law' means the:

A. adoption, promulgation, bringing into effect, repeal, amendment, reinterpretation, change in application, change in interpretation or modification after the date hereof of any Laws of Nepal, by any GON Agency, or by a competent court of Nepal;
B. imposition of any material condition not required as of the date hereof in connection with the issuance, renewal or modification of any Government Approval, by any GON Agency;
C. change or modification of the Generation Licence by any GON Agency (other than as requested in response to a petition therefor by the Company agreeable to the GON); or
D. the imposition of other obligations imposing a cost on the Company, which in case of any of the above, establishes either a material increase in cost, material reduction in revenue, or material delay

Sample Text: Stabilization or Change in Law (*Continued*)

in schedule as a consequence of any requirement for the design, construction, financing, ownership, operation or maintenance of the Hydro Property that is materially more restrictive than the most restrictive requirements (i) in effect as of the date hereof, (ii) specified in any applications, or other documents filed in connection with such applications, for any specified Government Approval, or (iii) agreed to by the Company in this Agreement, but excluding a Change in Tax.

The term 'Change in Law' shall not include any imposition, adoption, promulgation, bringing into effect, repeal, amendment, reinterpretation, change in application, change in interpretation or modification (a) implemented to address and rectify any Company Event of Default or any action or inaction on the part of the Company which is inconsistent with this Agreement, or (b) relating to the areas of human rights, labour, environment, and health and safety matters.

'Change in Tax' [...]

17. CHANGE IN LAW

17.1 Change in Law – Remedies

17.1.1 If there is a Change in Law or Change in Tax (other than a Change in Law or Change in Tax leading to termination pursuant to Section 18 during the period from the Agreement Date to the date falling twenty (20) Years after COD, the Company shall provide the GON with fully evidenced written notice of the nature and anticipated effect of the material increase in cost, material reduction in revenue, or material delay in schedule, as the case may be, which has arisen as a result of the Change in Law or Change in Tax. Provided that any change in Royalty and income tax shall in no case constitute Change in Law and Change in Tax.

17.1.2 The written notice shall be accompanied by the certificate of the auditor of the Company setting out full confirmation of the accuracy of the statements prepared by the Company and submitted to the GON.

17.1.3 If GON accepts the effect of the Change in Law or Change in Tax as set out in the written notice provided by the Company, the time limits and deadlines for the performance by the Company of its obligations under this Agreement which are affected by such Change in Law or Change in Tax shall be extended for as long as the Company is delayed in complying with its obligations in this Agreement because of the occurrence of such Change in Law or Change in Tax or the effects of such Change in Law or Change in Tax.

17.1.4 If GON accepts the effect of the Change in Law or Change in Tax as set out in the written notice provided by the Company, the Company shall first fund any such material increase in costs incurred or material reduction in revenue through:

A. the proceeds which the Company is entitled to claim from the Export Offtaker under the Export Power Purchase Agreement; and

B. the proceeds of any insurance policies which have been taken out by the Company, including the proceeds from the insurance policies required by Section 15.14.

17.1.5 In the event that the Company is unable to fully recover such material increase in costs incurred or material reduction in revenue through the methods specified in Section 17.1.4, provided that the Company has fully exercised all its

Sample Text: Stabilization or Change in Law (*Continued*)

rights to claim such costs or loss of revenue under the Export Power Purchase Agreement and the applicable insurance policies, the GON shall compensate the Company for such material increase in costs incurred or material reduction in revenue which remain outstanding by means of one, or a combination of, the following (determined at the sole discretion of the GON):

A. reducing the Energy Royalty payable by the Company to the GON under Section15.22; and/or
B. reducing the Capacity Royalty payable by the Company to the GON under Section 15.22; and/or
C. reallocating all, or a proportion of, the electrical energy which is to be provided to the GON by the Company free of charge under the Domestic Free Power Purchase Agreement and Section15.15.

The Company shall sell any additional electrical energy reallocated by the GON under Section 17.1.5(C) into the market on arm's length commercial terms and at a price which is not less than that being paid under the Export Power Purchase Agreement.

17.1.6 In the event that the Company is unable to fully recover such material increase in costs incurred or material reduction in revenue through the methods specified in Section 17.1.5, provided that the Company has satisfied its obligations under Section 17.1.5 to mitigate the effects of such Change in Law or Change in Tax, GON shall reimburse the Company for any remaining material increase in costs incurred or material reduction in revenue which it is entitled to recover under this Section 17.1 within sixty(60) Days after presentation to it by the Company of an invoice and full supporting documentation with respect thereto.

17.1.7 The Company shall not be entitled to make a claim under Sections 17.1.4, 17.1.5 and

17.1.6 until such point as the total material increase in costs incurred or material reduction in revenue as a result of Changes in Law and/or Changes in Tax have reached an aggregate amount of [GON to insert amount based on value of Project cost and commercial agreement with the Company].

17.1.8 The time to be extended and the amount to be compensated as a result of the Change in Law or Change in Tax as specified in Sections 17.1.3, 17.1.5 and 17.1.6 shall be determined by the Compensation Committee of Independent Experts as referred to in Section 16.5.4. If either Party does not accept decision of the Compensation Committee of Independent Experts, such matter may referred to an arbitration in accordance with Section 21.

17.1.9 If the GON does not accept the effect of the Change in Law or Change in Tax as set out in the written notice provided by the Company under this Section 17.1, the matter shall be referred to an arbitration for resolution in accordance with Section 21.1. The arbitral tribunal shall make its determination with respect to the effect of the Change in Law or Change in Tax, as the case may be, within thirty (30) Days of such referral.

17.1.10 If the arbitral tribunal determines that the effect of the Change in Law or Change in Tax is not as set out in the written notice provided by the Company under this Section 17.1, the time limits and deadlines and/or the costs payable by the GON shall not be revised.

Sample Text: Stabilization or Change in Law (*Continued*)

17.1.11 If the arbitral tribunal concludes that the effect of the Change in Law or Change in Tax is as set out in the written notice provided by the Company under this Section 17.1, the arbitral tribunal shall determine the extension to the time limits and deadlines for the performance by the Company of its obligations under this Agreement and/or the level of costs reimbursable by the GON to the Company.

17.1.12 If the level of costs fixed by the arbitral tribunal is more than [GON to insert amount based on specifics of each project], or the revised timetable fixed by the arbitral tribunal provides for a movement to the timetable set out in the Agreement of more than [GON to insert time period based on specifics of each project], the GON may elect to terminate this Agreement in which case the provisions of Section 18 shall apply.

17.2 Change in Law in favour of the Company

In case of increased revenues due to the Change in Law or Change in Tax, the Company shall reimburse to the GON the amount as determined by the Compensation Committee of Independent Experts.'

5.6 Dispute avoidance and dispute settlement

Disputes are an inevitable part of any relationship and a contractual relationship for investment is no exception. As noted previously, the completion of a contract is the beginning of a long-term relationship, not an end point in itself. Thus, to manage the ups and downs of the relationship, a series of dispute settlement provisions is needed to promote de-escalation of disputes rather than immediate escalation to courts or arbitral tribunals. This section explores these steps. To give this context, it begins with a discussion of why immediate recourse to international arbitration, a preferred option of international investors, is not the preferred approach here. It then sets out several sequential tools short of litigation, options for domestic litigation, and finally international arbitration. This section seeks to provide an avenue forward through the complexity and expectations that allows governments to identify their best options for promoting strong long-term relationships, while at the same time ensuring effective dispute settlement when needed.

Turning to a discussion of international arbitration first is important for context. In international investment relationships, investor-state dispute settlement (ISDS) has taken on a life of its own.[14] This has created multiple risks for governments, especially in developing countries. These risks include chilling the host state's right and duty to regulate, and imposing costly, lengthy and non-transparent arbitration proceedings, often in foreign countries, which can result in high arbitral awards against the host state.[15] Indeed, several ISDS cases have seen awards over US$2 billion.[16] At least one known investment contract-based arbitration, against Nigeria, recently crossed the US$2 billion level in a tax case.[17]

ISDS cases have in fact been triggered in relation to international investments by disputes related to environmental, social or economic sustainability, such as new legislation on these matters,[18] projects being denied for failing ESIA processes,[19] the protection of environmental and cultural rights of indigenous peoples,[20] the protection of local waters and waterways,[21] and cultural property issues.[22] Arbitral awards against host states can be rendered by commercial arbitrators who remain blind to public policy, sustainability, and broader international law considerations, giving rise to billions of dollars of awards against states, big enough to affect national budgets. This in turn can significantly diminish the ability of national governments to pay for social programmes, such as health and education services. Some predict that the global coronavirus pandemic will unleash a new wave of ISDS cases that will disable developing countries for years to come.[23]

Consequently, it is absolutely worthwhile not only from a legal point of view but also from a sustainable development and human rights perspective[24] to avoid ISDS and to seek amicable resolution of disputes, especially those involving sustainability, whenever possible. This is especially important because the interests of communities and other affected stakeholders will not be formally represented in arbitral and legal proceedings to settle disputes, even those that concern them.

It is worthwhile not only from a legal point of view but also from a sustainable development and human rights perspective to avoid ISDS and to seek amicable resolution of disputes whenever possible.

The experience to date with ISDS through arbitration is primarily through arbitrations under investment treaties, regional integration agreements that include investment chapters, international arbitration provisions in national laws, and of course provisions in investment contracts. Often this layering of rights results in guaranteed access to international arbitration, many times in two or more arbitral proceedings being initiated, and all of this side-stepping national judicial process altogether. Even as IIAs undergo various reforms of the types currently being discussed at UNCITRAL,[25] investment contracts can easily create an ironclad right of the investor to international arbitration of their choice. When asked to explain such provisions, investors and their counsel will insist that international arbitration in Western venues that applies familiar arbitration rules, frequently those of the International Chamber of Commerce (ICC), is a sine qua non of international investment.[26] As this is patently not the case, lawyers should be aware that host states have several possible options.

These options include, in sequence and in order of preference for developing country governments:

- Alternative dispute settlement through mediation or the use of other non-litigation processes;
- Recourse to expert assessors for technical issues;
- Recourse to domestic courts;

Box 5.6 *Force majeure* and COVID-19

Force majeure clauses have become much discussed due to the COVID-19 pandemic. *Force majeure* clauses should allocate the contracting parties' responsibilities fairly in the event of a *force majeure* event, but also seek to provide clarity on what constitutes a *force majeure* event. Not all environmental, social and economic sustainability risks should be borne by the state. For example, labour disputes, strikes and lockdowns on the project premises are definitely not *force majeure* events, and even those that escalate into national events should not be a *force majeure* event if it originated with the project. Similarly, as discussed in Section 4.5, many extreme weather events from climate change are increasingly foreseeable, which means these events should be excluded from *force majeure* provisions and responsibilities to prevent damage from such events should be clearly allocated by the contract. In the case of *force majeure* affecting the Contracting Authority, it should not have to compensate private operators for lost revenue and costs due to events classified as *force majeure* events, as this is inconsistent with the basic principles underlying the concept of *force majeure*. Additional detailed guidance will undoubtedly be needed in the near future in terms of the impacts of COVID-19 on *force majeure* provisions, such as the treatment of 'pandemic' events, as well as government actions, such as lockdowns, that impact the cash flow and profits of private operators.

When a *force majeure* is triggered, the responsibilities of both parties in relation to the steps to be taken afterward should be clear. *Force majeure*, it should be noted, does not trigger the automatic termination of the contract, but puts in place obligations to discuss the impacts of the event over time, determine mitigating measures that can be taken, and only as a last resort termination of the contract. In other words, it triggers requirements to save the contractual relationship and project prior to allowing for termination.

- Nationally based arbitration or regionally based arbitration;
- International arbitration after exhaustion of national court remedies; and finally
- International arbitration as a first recourse of right.

Before turning to these individual elements, it is worth noting that, in addition to a well-designed provision on dispute resolution, investment contracts should strive to allocate responsibilities clearly and fairly, with a view to avoiding escalation of disputes and ISDS. This is important not only for disputes between the contracting parties, but also for disputes between the private operator and the communities involving the protection of the environment and the rights of affected people. These disputes can potentially escalate into disputes between the contracting parties. In fact, this entire Resource is designed to steer contracting parties toward clear allocation of responsibilities related to sustainable development issues to avoid disputes between them, and with the affected communities.

In order to minimise the risks of disputes escalating, the contracting parties should pay attention to the following practice pointers on preventing and mitigating disputes:

- As a matter of contract provision and contract management, the contracting parties should agree to notify each other of relevant events and incidents, share pertinent information, and consult with each other frequently for early identification of problems before they escalate. This is especially the case with the implementation of the various plans mentioned in this Resource – the closer the parties are in touch and better they co-ordinate with each other, the more likely it is that the parties will reach an outcome that is better for them and for the affected communities.
- For sustainability-related disputes, the contracting parties can learn from decades of experience by the alternative dispute resolution (ADR) community that tackles environmental and social conflicts around the world. Many contracts build in an ADR process, such as mediation, as a required step before the parties proceed to formal arbitration or legal proceedings.

- The parties can also consider the use of an expert or a panel of experts to resolve technical disputes. One advantage with this technique is that the parties need not educate arbitrators or judges about technical issues with which they have no familiarity. But if the issues are more than technical or complex and also involve members of affected communities, for instance, then the contracting parties should either ensure that the panel of experts includes at least one expert who is competent to address community issues, or defer the matter to a different mechanism.
- A grievance mechanism is a non-judicial or operational-level mechanism suited to addressing project-level complaints from people in the local communities or otherwise impacted by the project. It can also be used in the context of workplace complaints. It enables the project to gauge people's response to the project, and to prevent grievances from escalating into community unrest, protests against the project, and violence. Large-scale conflicts involving communities should be treated with care and may merit an involvement of independent and neutral facilitators.[27] Even conflicts that appear small to the company should be treated with care as the issues may often be much bigger for the individuals involved.
- The project can also consent to submit to the jurisdiction of a local judicial forum designed to enable claims and disputes involving natural citizens of the host state for resolution.[28]

If disputes cannot be settled by the above remedies, the government should seek to have disputes resolved in the national courts. This is the usual option in developed countries, and should be the starting point in all countries. A simple provision that disputes arising from this contract shall be resolved by the national courts of the host state is all that is needed.

That being said, it is a reality that in some cases the foreign investor will insist on other recourses. Some options are available to address this short of international arbitration as a first recourse:

- A provision that allows the parties to agree to arbitration in the event a dispute arises can signal a willingness to have arbitration if needed, but not commit the state to it immediately. In other words, this would be a provision to consider arbitration with the other party if needed.
- Arbitration under national arbitration rules in the host state or a neighbouring state with similar legal culture can meet the need of an investor for arbitration while remaining more familiar in legal culture and geography to the host state. The availability of high-quality national arbitration facilities is an important element for this option to work. It should be noted that even if regional or international arbitration is adopted, this can be under the national arbitration law (or alternative dispute resolution law) of the host state, thus maintaining critical legal linkages to the national law of the host state.
- Many areas of the global South have strong regional arbitration institutes and processes. In francophone Western and Central Africa, the leading arbitral institution is the Common Court of Justice and Arbitration based in Abidjan, Côte d'Ivoire, which was established by the Organization for the Harmonization of Business Law in Africa (also known as 'OHADA', its French acronym). Egypt has the Cairo Regional Centre for International Commercial Arbitration. In the Commonwealth, Mauritius has a strong centre affiliated with the London Court of International Arbitration and Singapore is well known for its International Arbitration Centre. All have good reputations for independence and are viable and reasonable options.
- International arbitration in these forums or in more traditional places such as London, Paris, Washington or New York can be permitted, but only after local court remedies have been exhausted and the dispute not resolved. This notion of exhaustion of local remedies was common in international law until three or four decades ago, when direct access to ISDS began to grow.

- Finally, direct recourse to international arbitration at the World Bank's International Centre for the Settlement of Investment Disputes (ICSID), under UNCITRAL's arbitration rules, in Stockholm, London or The Hague can be considered. If this occurs, the recourse permitted and the applicable arbitration rules should be clearly designated.

If international or even national arbitration is engaged, the government lawyers should be aware of several issues that need to be addressed in establishing a process they wish to have.[29] Five critical issues here are:

- **Clear identification of the applicable law:** This has been addressed in Section 5.4 in general terms. It is important to clearly designate the national law and the contract as the primary applicable law, and international law as only a supplementary source. The government should not agree to a process that downgrades the national law as the primary source of applicable law.
- **Transparency:** Almost all commercial arbitrations are conducted in a confidential setting. Arbitrations involving governments are split between being more public under IIAs dispute settlement and usually private under investment contracts. Given the value of transparency in international investment discussed in Section 5.2, we recommend that governments strongly consider applying the transparency provisions of UNCITRAL Rules on Transparency in Treaty-based Investor-State Arbitration, 2014, to the contract-based arbitration. These Rules, while developed for treaty-based arbitration, are fully applicable to contract-based arbitration. They can be incorporated into the arbitration provisions of the contract and will then be binding and effectively supplement any other arbitration rules identified in the contract. Governments are strongly encouraged to move in the direction of full transparency in this regard.
- **Third-party funders:** International arbitration against government is now a big business. As such, it has attracted financial investors whose business

is investing in claims against governments. These so-called third-party funders, which include hedge funds, pay the costs of the arbitration process, the lawyers and usually an adverse costs award in exchange for a percentage of the award the company wins if it does so. The practice is also known as champerty. It is important for governments to know if the case is being run by third-party funders or if it is fully in the hands of the investor, in order to prevent conflicts of interest for the arbitrators, counsel and for overall transparency in the process. Governments will have to insist on a clause requiring a full declaration of the presence, identity and role of third-party funders if they agree to arbitration.

- **Waivers of sovereign immunity:** States have what is known as sovereign immunity under international law. This means they cannot be sued by private parties for their sovereign acts. For arbitration to work, the government must waive this immunity from suit. An agreement to arbitrate constitutes such a waiver in practice. However, there is a second immunity for sovereign states relating to enforcement of an award against the state. This immunity prevents sovereign state property used for statecraft purposes from being seized to enforce an award. This can include embassies, central bank offices, military equipment, and closer to home even parliament buildings and other government buildings. Investors will always seek a written waiver of this immunity from enforcement in an arbitration clause. Our recommendation is simple: say no. This should simply not be agreed to by the government.

- **Waiver of other recourse:** Finally, there is the issue of the ability of investors to have multiple recourses. This should be addressed in the contract by expressly allowing the investor (including its owned investment) one recourse only. To do this, there should be what is known as a fork in the road clause for choosing local courts or arbitration. Once a path is chosen, the other is no longer available. But the risk of multiple recourse goes beyond that. Arbitrations are often commenced under domestic law provisions, contracts and applicable investment treaties. What is important to note here is that in such a scenario, the company only has to win once to win. The government, however, has to win every time not to lose. This unfair system can be stopped by insisting on an express waiver of any other arbitration rights in the contract, expressly including any arbitrations under applicable international investment treaties or chapters of regional economic agreements. Such waivers must also be clear that it is any arbitration relating to the underlying measure of the government impacting the investor that is being waived. Preventing several options for arbitration being cumulated is critical for the success of an arbitration process for governments.

The above presents a complex chain of issues. The notion that arbitration clauses can be as simple as saying the two parties consent to arbitration under a designated set of rules and leave it at that is outdated.[30] The above issues reflect a number of lessons learned by governments and practitioners from previous experiences.

Guidance XIII: Dispute avoidance and dispute settlement

- ✓ Dispute settlement provisions should be comprehensive and clear and ensure a step-by-step approach to resolving disputes.
- ✓ The tools with the lowest risk of escalating disputes should be tried first, including mediation, expert reports, and other ADR options.
- ✓ National courts remain the first choice for formal dispute settlement. This should be the default position of governments.
- ✓ Only if this cannot be achieved should arbitration be considered, beginning with arbitrations in national settings, then regional and finally as a last resort international.
- ✓ Arbitrations should be transparent and open. Third-party funders, if permitted, should be made known at the beginning of the arbitration.
- ✓ Arbitration provisions are growing in complexity to ensure against misuse and multiple proceedings. These issues have to be taken seriously and addressed in writing in the contract to protect governments from such practices.

Sample Text: Dispute Avoidance and Dispute Settlement

MMDA Art. 27: Rights of Citizens of the State

27.1 Company Grievance Mechanism

a. The Company shall, at its own expense, promptly respond to communities' concerns related to the Mining Project as outlined in paragraph 23 of IFC Performance Standard 1.

b. Where not established under a community development agreement, the Company will establish a grievance mechanism to receive and facilitate resolution of the affected communities' concerns and grievances about the Company's environmental and social performance. The grievance mechanism should be proportionate to the risks and adverse impacts of the Project. The grievance mechanism should be established in Consultation with the communities who are anticipated to use it, through an understandable and transparent process that is culturally appropriate and readily accessible to all segments of the affected communities, at no cost to the affected communities and without retribution. The mechanism should not impede access to judicial or administrative remedies. The Company shall inform the affected communities about the mechanism in the course of its community engagement process.

27.2 Forum for Claims and Disputes Involving Natural Citizens of the State

A natural citizen of the State who has a claim or dispute regarding the Project may submit such claim or dispute for resolution under Applicable Law, or under an applicable customary law dispute resolution mechanism recognized under Applicable Law. The Company consents to the jurisdiction of local institutions for these purposes.

MMDA Art. 30.1(c)

(c) All reports and submissions by the Company to the State, and all responses by the State, are freely available on request to the State or the Company, provided that Confidential Information may be redacted prior to disclosure.

MMDA Art. 36.1: Periodic Review

36.1 Modification and Review

This Agreement shall upon written request of a Party, be subject to periodic review once every five (5) years after the Effective Date for the purpose of good faith discussions to consider any proposed modification(s) to this Agreement as may be necessary or desirable in the light of any substantial changes in circumstances that may have occurred during the previous five (5) years, or experience gained in that period. The Parties agree always to be open to discussing any matter which may help maximize the positive development benefits of the Project, or minimize its undesirable impacts. Nothing herein shall preclude a Party from requesting the other Party to initiate discussions regarding any provision herein, provided that this Agreement shall remain in effect during the period during which the parties are conducting such discussions.

Notes

1 CCSI (2017), *Requirements for Community Development in Mining Laws*, available at: http://ccsi.columbia.edu/files/2014/09/Mining-Community-Development-Requirements-Summary-Table-CCSI-2017_February.pdf; also see: Loutit, Jennifer, Jacqueline Mandelbaum and Sam Szoke-Burke (2016), *Emerging Practices in Community Development Agreements,* CCSI, available at: http://ccsi.columbia.edu/files/2016/02/Emerging-practices-in-CDAs-Feb-2016-sml.pdf

2 There is a close relationship between transparency and anti-corruption measures. The Commonwealth Secretariat has recently published the 'Commonwealth Anti-Corruption Benchmarks'. These are good practice 'benchmarks' covering 25 areas. They have been developed in consultation with member countries for about two years. The Benchmark 'package' has four parts: an Introduction (explaining the purpose and scope of the Benchmarks), Principles (short statements of principle for each of the 25 Benchmarks), the Benchmarks themselves (setting out the standards and actions required to meet the Benchmark), and Guidance (explaining the choices in the Benchmarks, and the connections to existing international standards and practice).

3 The current model can be described as a 'Catch Me if You Can' model: Government investigators rarely go to facilities to monitor compliance; if they do they have to find the violation, which may well be hidden on any given day; if they find it, officials in capitals have to approve enforcement action; political decision-makers may then oppose enforcement actions; if actions go ahead, new investigations will happen and investigators can often be bribed; and if all else fails, the fines are usually low enough to simply be the cost of doing business. So the attitude is: 'even if you can catch me, I don't really care'. This section offers an alternative approach to this model of enforcement.

4 This is standard practice among MDBs when they finance high-risk (or 'Category A') projects.

5 IMF, OECD, UN and World Bank (2015), Options for Low Income Countries' Effective and Efficient Use of Tax Incentives for Investment. *A report to the G-20 Development Working Group by the IMF, OECD, UN And World Bank*, available at: http://www.oecd.org/tax/tax-global/options-for-low-income-countries-effective-and-efficient-use-of-tax-incentives-for-investment.pdf

6 For a quick primer on stabilisation clauses, see Thomson Reuters Practical Law, 'Glossary: Stabilization Clause', available at https://uk.practicallaw.thomsonreuters.com/1-501-6477?transitionType=Default&contextData=(sc.Default)&firstPage=true

7 Amnesty International (2006), *Human Rights, Trade and Investment Matters,* p. 31, available at: https://www.amnestyusa.org/files/pdfs/hrtradeinvestmentmatters.pdf

8 For further information see: OECD (2019), OECD Guiding Principles on Durable Extractive Contracts, Principle VIII and accompanying explanatory text. Available at: http://www.oecd.org/dev/Guiding-Principles-Durable-Extractive-Contracts-2020.pdf

9 IFC (2009), *Stabilization Clauses and Human Rights. A research project conducted for IFC and the United Nations Special Representative of the Secretary-General on Business and Human Rights*, available at: https://www.ifc.org/wps/wcm/connect/0883d81a-e00a-4551-b2b9-46641e5a9bba/Stabilization%2BPaper.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-0883d81a-e00a-4551-b2b9-46641e5a9bba-jqeww2e. Motoko Aizawa designed and managed this research project for the IFC.

10 Ibid.
11 UN OHCHR (2015), available at: https://www.ohchr.org/Documents/Publications/Principles_ResponsibleContracts_HR_PUB_15_1_EN.pdf
12 Ibid.
13 As set out in Principle VII of the OECD Guiding Principles on Durable Extractive Contracts.
14 The latest ISDS trend can be easily accessed from UNCTAD's Investment Dispute Settlement Navigator, accessible at https://investmentpolicy.unctad.org/investment-dispute-settlement. This section will only take note of the fact that as of the end of 2019, over 1,000 known investment treaty-based ISDS cases existed, of which 343 cases are pending. Of the concluded cases, 36 per cent have been decided in favour of the state, and 29 per cent in favour of the investor.
15 For example, see: Mattli, Walter and Dietz, Thomas (eds) (2018), *International Arbitration and Global Governance*, Oxford University Press; and CCSI (2018), *Rethinking International Investment Governance*, available at: http://ccsi.columbia.edu/files/2018/09/Rethinking-Investment-Governance-September-2018.pdf
16 The top 10 amounts for arbitral awards as of June 2020 are set out by UNCTAD (UNCTAD Investment Policy Hub, 'Investment Settlement Dispute Navigator', available at: https://investmentpolicy.unctad.org/investment-dispute-settlement). They include one at US$40 billion, and the remaining top nine between US$8.6 billion and US$1.1 billion against Russia, Venezuela and Ecuador, among other states.
17 Esso Exploration and Production Nigeria Ltd. (now owned by Exxon) and Shell Nigeria Exploration and Production Company Ltd. in 2009. The case is reported at IAReporter (2019), 'Analysis: $2.7 Billion Award By Fortier and Brower Surfaces …', available at: https://www.iareporter.com/articles/analysis-2-7-billion-award-by-fortier-and-brower-surfaces-as-a-result-of-nigerian-efforts-to-block-enforcement-ruling-in-favor-of-shell-and-exxon--entities-touched-on-constitutional-questions-as-we/.
18 For example, South Africa's Black Economic Empowerment legislation was challenged in *Piero Foresti, Laura de Carli and others v Republic of South Africa* (ICSID Case No. ARB(AF)/07/1). This challenge lasted several years and was ultimately withdrawn by the company when permits it was seeking were granted.
19 For example, the successful claim against Canada after a permit was denied for a quarry, *Clayton and Bilcon of Delaware Inc. v Government of Canada* (PCA Case No. 2009-04).
20 For example, *Glamis Gold Ltd. v United States of America*; and recently in Colombia, a number of arbitrations have followed a decision not to allow mining in a highly sensitive watershed that also has special relationships with indigenous peoples.
21 For example, Canada is facing an ongoing challenge to a law banning fracking for gas under the St Lawrence River in Quebec, *Lone Pine Resources Inc. v Canada* (ICSID Case No. UNCT/15/2)
22 For example, *Parkerings v Lithuania* concerned the World Heritage status of part of Vilnius, and the type of construction allowed in the protected area.
23 Law firms have started to issue client advisories and run webinars, using headlines such as 'The Coming Wave Of COVID-19 Arbitration - Looking Ahead' (by Alston Bird). Whether these law firm postings are a warning of a surge in ISDS cases or a promotion of such a surge is in the eye of the reader. Clearly concerned about the potential consequences of increased ISDS cases, CCSI has issued a call for ISDS moratorium;

see CCSI (2020), 'Call for ISDS Moratorium During Covid-19 Crisis and Response', available at: http://ccsi.columbia.edu/2020/05/05/isds-moratorium-during-covid-19/, whereas IISD has urged governments to protect against ISDS claims in the midst of COVID-19 (see IISD (2020), 'Protecting Against Investor-state claims amidst COVID-19: a call to action for governments', available at: Https://Www.Iisd.Org/Sites/Default/Files/Publications/Investor-State-Claims-Covid-19.Pdf). CSOs are also running campaigns against ISDS; for example, Both Ends, a Dutch CSO, through an 'open letter to governments', is asking them to 'take immediate action to ensure that the duty of governments to regulate in the public interest is safeguarded and put beyond the scope of ISDS claims'.

24 UN OHCHR and Heinrich Böll Stiftung (2018), *The Other Infrastructure Gap: Sustainability. Human Rights and Environmental Perspectives.*

25 The official UNCITRAL reform website is at https://uncitral.un.org/en/working_groups/3/investor-state. Multiple elements of the reform process are reviewed here by IISD (https://www.iisd.org/projects/uncitral-and-reform-investment-dispute-settlement).

26 World Bank (2019), Guidance for PPP Contractual Provisions, p. 198: "In Developed Markets, the Contracting Authority will generally opt for domestic courts. The selection of an established arbitral institution and of institutional procedural rules is of particular importance in many developing countries, where PPP Projects are unlikely to be bankable if recourse to acceptable arbitration arrangements or offshore courts with established PPP expertise is not agreed." Available at: https://ppp.worldbank.org/public-private-partnership/sites/ppp.worldbank.org/files/documents/Guidance_on_PPP_Contractual_Provisions_EN_2019_edition.pdf

27 For example, see: The Compliance Advisor Ombudsman, *Building Consensus: History and Lessons from the Mesa de Diálogo y Consenso.* CAO-Cajamarca, Peru. Monographs 1 through 3.

28 MMDA, Section 27.2.

29 A recent report by the Commonwealth Secretariat supports addressing a number of key issues in international arbitration. See: *Study of International Commercial Arbitration in the Commonwealth*, forthcoming. A key finding of the study, based on interviews with lawyers, arbitrators, chambers of commerce, and others, was that there is a strong desire to retain arbitration in-country, and to develop local arbitration centres and local arbitration practitioners.

30 In the context of infrastructure, see, for example, World Bank (2019), Ch. 11; and in mining, see Fry, Jason and Louis-Alexis Bret (2019), The Guide to Mining Arbitration*s*, available at: https://globalarbitrationreview.com/edition/1001343/the-guide-to-mining-arbitrations-first-edition

Annex: Summary of Guidance

Annex: Summary of Guidance

Guidance I: Stating the sustainable development objectives of a contract

- ✓ The contract should state clearly, in the preamble or an 'Objectives' clause, that the project seeks to support the sustainable development objectives of the host country, and specifically the environmental, social and economic development of the nation and host community.
- ✓ The contract should specifically itemise the critical international agreements or standards and sustainable development goals it will seek to support.
- ✓ The contract should include a statement that makes clear the contract should be interpreted and applied in a manner that best ensures the intent of the objectives are met.

Guidance II: Conducting environmental and social due diligence in the pre-contract and operational phases

- ✓ Ascertain the extent of due diligence carried out in the pre-contract phase and identify gaps, if any, making sure that the due diligence process is not being curtailed by a rush to contracting.
- ✓ Pay particular attention to the process of the ESIA so that the approval and permitting events that should follow the ESIA are in the correct sequence.
- ✓ Require compliance with ESMP and the environmental and related permits at a minimum as contractual obligations; if there are gaps in documents or incorrect sequencing of assessments, approvals and permits, remedy them before the execution of the contract, and if this is not possible, provide for the appropriate sequencing and corrective measures in the contract.
- ✓ Ensure ESMP implementation cost is part of the total project cost to avoid project shortfall, and adjust the

budget periodically for technology upgrades and other changing needs.

- ✓ Provide specifically for the responsibility of the contracting authority to approve changed project descriptions or plans that alter the underlying obligations in any material way, and guard against any deviations that lower standards.
- ✓ Provide for ongoing operational phase reviews of the ESMP implementation plan and the need for adjustments to be made to it over the life of the project.

Guidance III: Strong environmental and social obligations to manage the positive and negative impacts

- ✓ Strong environmental and social obligations go beyond the requirement for compliance with law or international standards, or the obligation to carry out an ESIA. The obligations should be based on precise understanding of potential negative and positive impacts.
- ✓ Review the ESIA to understand the potential negative impacts of the project and the ESMP for the proposed management measures. Ascertain what specific plans are required to manage the negative impacts.
- ✓ In addition to the ESMP, the contract should explicitly require the implementation of the specific mitigation measures or plans, or third-party agreements.
- ✓ Although not tailored for the specific purpose of identifying economic impacts of projects, ESIAs can also provide valuable information for the purpose of local economic and social development planning.
- ✓ Social obligations should be identifiable and verifiable. They should be developed with the community involved, for their benefit.

Guidance IV: Local economic and social development

- ✓ Go beyond a general requirement to prefer local inputs, employment and other economic development measures by providing details and timelines that will improve the chances of implementation.

- ✓ Minimum requirements in domestic laws should be adhered to or exceeded.
- ✓ Ensure that the project plans its contributions to local economic and social development strategically and systematically. Large-scale procurement requirements should be unbundled to allow greater access to local businesses.
- ✓ Ensure consultation with the local government, businesses and community members to develop the plans, and work with community groups to ensure implementation.
- ✓ Companies must work with the local government, not to replace it.
- ✓ Create a legal obligation on the part of the company to implement community development commitments and plans where these are separate from the actual contract.

Guidance V: Climate change provisions in contracts

- ✓ Go beyond the environmental provisions in the contract and address climate change risks explicitly, including climate event resilience, climate mitigation, and the right of governments to regulate in this area.
- ✓ Ensure that the project has carried out a climate risk assessment prior to finalising the contract.
- ✓ Ensure design and operational standards are appropriate to address climate-related weather events that can impact the investment, based on available scientific data and best industry practices.
- ✓ Ensure the design and operational standards are consistent with anticipated future reductions of greenhouse gas emissions, and new technologies can be implemented.
- ✓ Ensure that in any risk allocation provisions the project company is liable for the consequences of any foreseeable climate-related weather event, and that appropriate insurance is obtained where possible.
- ✓ Ensure the ongoing ability of the government to regulate for climate change purposes, and protect against the threat of arbitration by the company under any applicable investment treaty.

Guidance VI: Incorporating human rights obligations into contracts

- ✓ Prior to the execution of the investment contract, carry out human rights due diligence so that the host state can ensure that nothing in the contract contradicts the state's international human rights obligations.
- ✓ Check that the ESIA for the project adequately covers key human rights issues; if it does not, and human rights risks can be expected, obligate the contracting parties to carry out human rights due diligence with respect to the expected activities of the project.
- ✓ Obligate contract parties to carry out human rights due diligence throughout the duration of the contract, specifying the circumstances when it is required.
- ✓ Add specific references to international human rights and humanitarian law or other international standards depending on project circumstances.

Guidance VII: Identifying and engaging with stakeholders

- ✓ The project should: have a systematic approach to stakeholder identification and engagement; set out a plan and budget; and make implementation a contractual obligation.
- ✓ Ensure that both contracting parties have responsibilities for ongoing stakeholder identification and engagement.
- ✓ Pay particular attention to engagement with Indigenous Peoples and their right to free, prior, and informed consent.
- ✓ Establish grievance mechanisms and ombuds systems and other measures to receive grievances of the affected stakeholders.
- ✓ Be specific about the need for open and precise communication regarding and during project emergencies.

Guidance VIII: Respecting third-party rights

- ✓ The social, environmental and economic rights and benefits for local communities should be enforceable by the local communities, and not only by the contracting authority.

- ✓ Community development agreements and other third-party agreements are the best vehicle for creating direct legal right of enforcement by communities or other affected third parties.
- ✓ When plans are used and mentioned as mandatory in the contract, the contract could name the third parties as third-party beneficiaries under the contract.
- ✓ A material failure to implement the plans or agreements, or persistent failure to correct breaches of plans or agreements should be designated as a breach of the investment contract, and should attract the same sanctions as material non-compliance with the contract provisions themselves.

Guidance IX: Transparency of contracts

- ✓ Each contracting party should be free to disclose the investment contract when concluded.
- ✓ If the contract contains truly sensitive or proprietary information, it can be redacted. It is important to note that redactions lead to questions as to what is withheld and why.
- ✓ An online, publicly accessible database can be used as an access point for public contracts.
- ✓ After material modification or amendment, the contract should be disclosed again.

Guidance X: Options for compliance promotion

- ✓ The contract should anticipate the project's monitoring and reporting needs and allocate the responsibilities appropriately between the contracting parties.
- ✓ Community members should be enabled to participate in project monitoring.
- ✓ The private operator should inform the project's contractors and subcontractors of the project's obligations with respect to environmental, social and economic sustainability, and be legally required to pass on the appropriate requirements down to them in order to ensure these entities comply with them.

- ✓ Targets should be well defined and measurable, but should be treated as goals to be achieved collaboratively rather than black and white compliance issues. This allows all parties to learn as the project unfolds. At the same time, a persistent failure to achieve the goals, or to make best efforts to achieve them, should be elevated to an issue of material compliance with the project company's obligations.
- ✓ Regular disclosure of the project's monitoring information will enable affected communities to act as de facto enforcers of specific obligations owed to them.

Guidance XI: Applicable law

- ✓ The domestic law of the host state should be defined as the applicable law governing the contract and the project.
- ✓ Contracts should comply with the applicable domestic law, and not contain provisions in breach of the laws. Contracts should be negotiated to implement the domestic law applicable to an investment, not replace it.
- ✓ Governments should strive to have as much of the legal regime applying to investments in the domestic law as possible to have the most transparent and consistent application of the law, avoid unnecessary negotiations with each large investor, and minimise the opportunities for corruption and imbalances in results.
- ✓ Contracts should, where necessary, particularise the application of the domestic law to a specific project, providing sufficient detail to ensure it is clear and enforceable in terms of the obligations on the investor and government parties.

Guidance XII: Non-fiscal stabilisation

- ✓ Governments should not agree to accept clauses stabilising the non-fiscal laws applying to an investment.
- ✓ If, despite this clear guidance, governments choose to agree to a stabilisation clause, they should ensure that, consistent with Principle VII, non-fiscal laws such as environmental, labour, health and safety, disclosure

and other related laws that aim to protect people and the environment should be excluded from any stabilisation provisions (sometimes also called change of law provisions).

- ✓ Governments should acknowledge that the costs to companies of meeting changes in law should be treated as tax deductible expenses of the company in keeping with other operational expenses.
- ✓ Companies should anticipate changes in national law as an ongoing process and budget to comply with changes in the normal course of affairs.

Guidance XIII: Dispute avoidance and dispute settlement

- ✓ Dispute settlement provisions should be comprehensive and clear and ensure a step-by-step approach to resolving disputes.
- ✓ The tools with the lowest risk of escalating disputes should be tried first, including mediation, expert reports, and other ADR options.
- ✓ National courts remain the first choice for formal dispute settlement. This should be the default position of governments.
- ✓ Only if this cannot be achieved should arbitration be considered, beginning with arbitrations in national settings, then regional and finally as a last resort international.
- ✓ Arbitrations should be transparent and open. Third-party funders, if permitted, should be made known at the beginning of the arbitration.
- ✓ Arbitration provisions are growing in complexity to ensure against misuse and multiple proceedings. These issues have to be taken seriously and addressed in writing in the contract to protect governments from such practices.

Suggested Reading

Suggested Reading

General Guidance on Environmental Impact Assessment, Cumulative Impact Assessment, Strategic Impact Assessment, etc.

Canadian Environmental Assessment Agency (2018), *Assessing Cumulative Environmental Effects under the Canadian Environmental Assessment Act, 2012.* Version 2, available at: https://www.canada.ca/en/impact-assessment-agency/services/policy-guidance/assessing-cumulative-environmental-effects-ceaa2012.html

Ehrlich, A and W A Ross (2015), 'The significance spectrum and EIA significance determinations', *Impact Assessment and Project Appraisal*, Vol. 33 No. 2, 87–97, available at: https://www.tandfonline.com/doi/full/10.1080/14615517.2014.981023?src=recsys

Impact Assessment Agency of Canada (2019), *Reference Guide: Addressing Cumulative Environmental Effects*, available at: https://www.canada.ca/en/impact-assessment-agency/services/policy-guidance/reference-guide-addressing-cumulative-environmental-effects.html

International Institute for Sustainable Development. Environmental Impact Assessment Online Learning Platform. https://www.iisd.org/learning/eia/eia-7-steps/

International Institute for Sustainable Development (2016), *Environmental Impact Assessment Training Manual*, available at: https://www.iisd.org/learning/eia/wp-content/uploads/2016/06/EIA-Manual.pdf

Morgan, R (2012), *Environmental Impact Assessment: The State of the Art*. Impact Assessment and Project Appraisal Vol. 30 No. 1, 5–14, available at: https://www.tandfonline.com/doi/full/10.1080/14615517.2012.661557?scroll=top&needAccess=true

Noble, B (2015), *Introduction to Environmental Impact Assessment: A Guide to Principles and Practice*, 2nd edn, available at: https://www.researchgate.net/publication/273439630_Introduction_to_Environmental_Impact_Assessment_A_Guide_to_Principles_and_Practice_3rd_Edition

Morrison-Saunders, A (2018), *Advanced Introduction to Environmental Impact Assessment*, available at: https://www.e-elgar.com/shop/usd/advanced-introduction-to-environmental-impact-assessment-9781785369711.html

United Nations Economic Commission for Europe (2017), *Convention on Environmental Impact Assessment in a Transboundary Context (Espoo Convention)*, available at: https://www.unece.org/fileadmin/DAM/env/eia/documents/legaltexts/Espoo_Convention_authentic_ENG.pdf

General Guidance on Social Impact Assessment

International Finance Corporation (2009), *Projects and People, A Handbook for Addressing Project-Induced In-Migration*. World Bank Group, Washington DC, available at: https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/publications/publications_handbook_inmigration

Mackenzie Valley Environmental Impact Review Board (2007), *Socio-Economic Impact Assessment Guidelines*, available at: http://reviewboard.ca/process_information/guidance_documentation/guidelines

Queensland Government. Department of State Development, Manufacturing, Infrastructure and Planning (2018), *Social Impact Assessment Guideline*, available at: https://www.statedevelopment.qld.gov.au/__data/assets/pdf_file/0017/17405/social-impact-assessment-guideline.pdf

Smyth, E and F Vanclay (2017), 'The Social Framework for Projects: A Conceptual but Practical Model to Assist in Assessing, Planning and Managing the Social Impact of Projects', *Impact Assessment and Project Appraisal*, Vol. 35 No. 1, 65–80.

Vanclay, F (2002), 'Conceptualizing social impacts', *Environmental Impact Assessment Review*, Vol. 22, 183–211.

Vanclay, F (2003), 'International Principles for SIA', *Impact Assessment and Project Appraisal*, Vol. 21 No. 1, 5–11, available at https://www.iaia.org/uploads/pdf/IAIA-SIA-International-Principles.pdf

Vanclay, F and A M Esteves (2011), *New Directions in Social Impact Assessment, Conceptual and Methodological Advances*. Edward Elgar Publishing Inc., Massachusetts.

Vanclay, F, A Esteves, I Aucamp and D Franks (2015), *Social Impact Assessment: Guidance for assessing and managing the social impacts of projects*. International Association for Impact Assessment, available at: https://www.iaia.org/uploads/pdf/SIA_Guidance_Document_IAIA.pdf

Impact Assessment for the Resource Sectors

Esteves, A M (2008), 'Evaluating community investments in the mining sector using multi-criteria decision analysis to integrate SIA with business planning', *Environmental Impact Assessment Review*, Vol. 28 No. 4–5, 338–348.

Franks, D, C Fidler, D Brereton, F Vanclay and P Clark (2009), *Leading Practice Strategies for Addressing the Social Impacts of Resource Developments*. Centre for Social Responsibility in Mining, Sustainable Minerals Institute, The University of Queensland, available at: https://www.csrm.uq.edu.au/publications/leading-practice-strategies-for-addressing-the-social-impacts-of-resource-developments

International Finance Corporation (2010), *International Lessons of Experience and Best Practice in Participatory Monitoring in Extractive Industry Projects*, available at: https://www.commdev.org/publications/international-lessons-of-experience-and-best-practice-in-participatory-monitoring-in-extractive-industry-projects-guidance-note-on-designing-participatory-monitoring-programs/

IPIECA (2015), *Community grievance mechanisms in the oil and gas industry. A manual for implementing operational-level grievance mechanisms and designing corporate frameworks*, available at: http://www.ipieca.org/resources/good-practice/community-grievance-mechanisms-in-the-oil-and-gas-industry/

Mancini, L and S Sala (2018), 'Social impact assessment in the mining sector: Review and comparison of indicator frameworks', *Resources Policy*, Vol. 57, 98–111.

Office of the Compliance Advisor Ombudsman (2016), *Grievance Mechanism Toolkit. A practical guide for implementing grievance mechanisms in different sectors*, available at: https://www.cao-grm.org/

State of New South Wales. Department of Planning and Environment (2017), *Social Impact Assessment Guideline. For State significant mining, petroleum production and extractive industry development*, available at: https://www.planning.nsw.gov.au/~/media/Files/DPE/Guidelines/social-impact-assessment-guideline-2017-09.ashx

Witt, K, V Vivoda, J Everingham and N Bainton (2018), *A framework for social impact assessment of shale gas development in the Northern Territory*. Centre for Social Responsibility in Mining, Sustainable Minerals Institute, The University of Queensland, available at: https://frackinginquiry.nt.gov.au/inquiry-reports?a=476740

World Business Council on Sustainable Development (2016), *Guidelines for Environmental and Social Impact Assessment.* Cement Sustainability Initiative, available at: http://docs.wbcsd.org/2016/08/Guidelines_for_Environmental_Social_Impact_Assessment.pdf

Climate Change Impact Assessment

Sabin Center for Climate Change Law (2020), 'EIA Guidelines for Assessing the Impact of Climate Change on a Project'. Columbia Law School / Columbia University Earth Institute. [A comprehensive online reference guide for guidelines by US federal, state and local jurisdictions, foreign jurisdictions, and international and non-governmental organisations], available at: https://climate.law.columbia.edu/content/eia-guidelines-assessing-impact-climate-change-project

Health Impact Assessment

Asian Development Bank (2018), *Health Impact Assessment: A Good Practice Sourcebook*, available at: https://www.adb.org/documents/health-impact-assessment-sourcebook

International Council on Mining & Metals (2010), *Good Practice Guidance on Health Impact Assessment*, available at: https://www.icmm.com/en-gb/guidance/health/guidance-hia

International Finance Corporation (2009), *Introduction to Health Impact Assessment*, available at: https://www.ifc.org/wps/wcm/connect/e7f68206-7227-4882-81ad-904cd6387bb7/HealthImpact.pdf?MOD=AJPERES&CACHEID=ROOTWORKSPACE-e7f68206-7227-4882-81ad-904cd6387bb7-jqeABQN

IPIECA and International Association of Oil and Gas Producers (IOGP) (2016), *Health Impact Assessment. A guide for the oil and gas industry*, available at: http://www.ipieca.org/resources/good-practice/health-impact-assessment-a-guide-for-the-oil-and-gas-industry/

Quigley, R, L den Broeder, P Furu, A Bond, B Cave and R Bos (2006), 'Health Impact Assessment International Best Practice Principles', International Association for Impact Assessment Special Publication Series No. 5, Fargo, USA, available at: https://www.iaia.org/uploads/pdf/SP5_3.pdf

World Health Organization (1999), *Health impact assessment: main concepts and suggested approach European Centre for Health Policy.* WHO Regional Office for Europe, Copenhagen.

Human Rights Impact Assessment

Danish Institute for Human Rights (2016), 'Human Rights Impact Assessment. Guidance and Toolbox', available at: https://www.humanrights.dk/business/tools/human-rights-impact-assessment-guidance-and-toolbox

Goldcorp (2011), *Human Rights Assessment of Goldcorp's Marlin Mine*, On Common Ground, available at: http://q4dev.s11.clientfiles.s3-website-us-west-2.amazonaws.com/653477107/files/doc_downloads/portfolio_docs/marlin/OCG_HRA_Marlin_Mine_May_17_linked.pdf

International Council on Mining & Metals (2009), *Human Rights in the Mining & metals Industry, Overview, Management Approach and Issues*, available at: https://www.icmm.com/en-gb/publications/mining-and-communities/human-rights-in-the-mining-and-metals-industry---overview-management-approach-and-issues

International Council on Mining & Metals (2009), *Human Rights in the Mining & metals Industry. Handling and Resolving Local Level Concerns & Grievances*, available at: https://www.icmm.com/en-gb/publications/mining-and-communities/handling-and-resolving-local-level-concerns-and-grievances

IPIECA (2013), *Integrating Human Rights into Environmental, Social and Health Impact Assessments. A practical guide for the oil and gas industry*, available at: http://www.ipieca.org/news/integrating-human-rights-into-environmental-social-and-health-impact-assessments/

United Nations Office of the High Commissioner for Human Rights (2012), *The Corporate Responsibility to Respect Human Rights. An Interpretive Guide*, available at: https://www.ohchr.org/documents/publications/hr.pub.12.2_en.pdf

United Nations Office of the High Commissioner for Human Rights (2014), *Women's Rights are Human Right*, available at: https://www.ohchr.org/_layouts/15/WopiFrame.aspx?sourcedoc=/Documents/Events/WHRD/WomenRightsAreHR.pdf&action=default&DefaultItemOpen=1

Cultural Heritage and Impact Assessment

Partal, A and K Dunphy (2016), 'Cultural impact assessment: a systematic literature review of current methods and practice around the world', *IAPA*, Vol. 34 No. 1, 1–13.

Indigenous Peoples and Impact Assessment

Gibson, G and C O'Faircheallaigh (2015), *IBA Community Toolkit. Negotiation and Implementation of Impact Benefit Agreements.* Commissioned by The Gordon Foundation, available at: http://gordonfoundation.ca/resource/iba-community-toolkit/

Gwich'in Council International (2018), *Impact Assessment in the Arctic: Emerging Practices of Indigenous-led Review*, available at: https://gwichincouncil.com/sites/default/files/Firelight%20Gwich%27in%20Indigenous%20led%20review_FINAL_web_0.pdf

International Council on Mining & Metals (2010), *Good Practice Guidance, Indigenous Peoples and Mining*, 2nd edn, available at: https://www.icmm.com/en-gb/publications/mining-and-communities/indigenous-peoples-and-mining-good-practice-guide

Gender and Impact Assessment

Canadian Research Institute for the Advancement of Women (2018), *Strengthening Impact Assessment for Indigenous Women*, available at: http://fnn.criaw-icref.ca/images/userfiles/files/Strengthening%20impact%20assessments%20for%20Indigenous%20women.pdf

Canadian Research Institute for the Advancement of Women (n.d.), *Gender-based analysis meets environmental assessment: Aligning policy mechanisms* *to address the resource development in Canada's North*, available at: http://fnn.criaw-icref.ca/images/userfiles/files/GBAMeetsEnviroAssessPP.pdf

Hill, C, C Madden and N Collins (2017), *A Guide to Gender Impact Assessment for The Extractive Industries*, Australian Aid, Carlton, Australia, available at: https://www.oxfam.org.au/wp-content/uploads/2017/04/2017-PA-001-Gender-impact-assessments-in-mining-report_FA_WEB.pdf

Oxfam Australia (2013), *Balancing the Scales. Using Gender Impact Assessment in Hydropower Development*, available at: https://cgspace.cgiar.org/handle/10568/34805

World Bank (2009), *Mainstreaming Gender into Extractive Industries Projects. Guidance Note for Task Team Leaders*, available at: https://openknowledge.worldbank.org/handle/10986/18235

Disability

World Bank (2018), *Good Practice Note. Environment & Social Framework for IPF Operations. Non-Discrimination and Disability*, available at: http://pubdocs.worldbank.org/en/573841530208492785/ESF-GPN-Disability-June-2018.pdf

Financial Institution Standards and Guidelines

European Bank for Reconstruction and Development (2019), *Environmental and Social Policy*, available at: https://www.ebrd.com/news/publications/policies/environmental-and-social-policy-esp.html

Equator Principles Association (2020), The Equator Principles (EP4), available at: https://equator-principles.com/wp-content/uploads/2020/05/The-Equator-Principles-July-2020-v2.pdf

Inter-American Development Bank (2020), *Environmental and Social Policy Framework*, available at: http://idbdocs.iadb.org/wsdocs/getdocument.aspx?docnum=EZSHARE-2131049523-16

International Finance Corporation (2012), available at: 'IFC Sustainability Framework', [Policy on Environmental and Social Sustainability and Performance Standards.] https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/sustainability-at-ifc/policies-standards/sustainability+framework

World Bank (2017), 'Environmental and Social Framework', available at http://documents.worldbank.org/curated/en/383011492423734099/The-World-Bank-environmental-and-social-framework

The Commonwealth

It is increasingly recognised that sound investment contracts between foreign investors and host states can play an important role in helping countries to meet the Sustainable Development Goals (SDGs). At the same time, many current investment relationships lack fairness and balance.

This book helps government drafters and reviewers of investment contracts to achieve fairness and balance in investment relationships with respect to environmental, social and economic development matters. As well as providing detailed guidance on drafting sustainability provisions in investment contracts, it highlights issues concerning the relationship between domestic law and investment contracts, and the need for these two legal elements to be developed in a symbiotic way.

ISBN 978-1-84929-196-5
9 781849 291965