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Thirty-second session

Summary record of the 656th meeting
Held at the Vienna International Centre, Vienna, on Friday, 21 May 1999, at 2 p.m.

Chairman: Mr. Renger ..... (Germany)

Contents

V.00-50975 (E)

The meeting was called to order at 2.05 p.m.

Privately financed infrastructure projects (*continued*) (A/CN.9/458 and Add.1-9)

Chapter V. Infrastructure development and operation (*continued*) (A/CN.9/458/Add.6)

1. **The Chairman** suggested that, in the interests of a structured discussion, the recommendations under the heading "Infrastructure operation" and the accompanying notes in paragraphs 18 to 46 should be subdivided as follows: legislative recommendation 3, with the corresponding notes in paragraphs 18 to 30; recommendation 4, with the corresponding notes in paragraphs 31 to 39; recommendation 5, with the corresponding notes in paragraphs 40 to 43; and recommendation 6, with the corresponding notes in paragraphs 44 to 46.

Legislative recommendation 3 and paragraphs 18-30

2. **Mr. Wallace** (United States of America) said, by way of general comment, that much of the content of the notes corresponding to recommendation 3 dealt with regulatory matters that would not ordinarily be covered in the project agreement.

3. He suggested that the beginning of the third sentence in paragraph 18 should be rephrased to refer not only to countries that had general legislation on concessions, but also to those that planned to have such legislation. The last sentence in paragraph 22 should be reworded to indicate that it would not merely be advisable, but essential, to require that a project agreement should set forth the circumstances under which the concessionaire might be required to carry out extensions in its service facilities and the appropriate methods for financing the cost of any such extension. Although he agreed with the advice given in paragraph 24 to clarify in the project agreement which extraordinary circumstances would justify the suspension or release the concessionaire from its obligations under the project agreement, he asked whether that advice could be accepted in all legal systems.

4. **Mr. Wiwen-Nilsson** (Observer for Sweden) said that, in the last line of paragraph 22, it was not so much a matter of "financing" the cost in question as of covering or bearing the cost. The wording should be amended.

5. The penultimate sentence of paragraph 24, stating that termination typically required the consent of the contracting authority or a judicial decision, could be misinterpreted as expressing advice and should be either deleted or rephrased.

6. **Mr. Lalliot** (France) said that recommendation 3 was particularly important. It was intricately bound up with the essentially public service character of such projects, involving such basic concepts as continuity of service and equality of access.

7. The last sentence of paragraph 19 posed a problem of conflict between statutory and contractual provisions. Under French law, a contractual provision could in no way derogate from a regulatory or legislative provision, which was intrinsically of a higher order, unless the legislative provision specifically stipulated otherwise.

8. Paragraph 22 should begin with the phrase "in some legal systems", since the content of the paragraph was not generally applicable.

9. With reference to paragraph 24, under the French and other legal systems the concessionaire's obligations to ensure the continuous provision of the public service derived from general principles of law or from statutory provisions which could not be superseded by contractual provisions. The contracting public authority's unilateral right to terminate or suspend a contract was a case in point, being exercised under the supervision of a judge on the basis of appropriate compensation for any prejudice suffered by the concessionaire. It was not possible to provide in the project agreement for the extraordinary circumstances that would justify suspending the service or releasing the concessionaire from its obligations. Only a judge could release a concessionaire from those obligations.

10. **Mr. Mazini** (Observer for Morocco) expressed concern that the notes did not adequately reflect the principle of universality of service, which was a broader principle than equality of service since it meant that a public works operator might, for example, have to ensure coverage in underprivileged regions of the country where such operations might not be profitable.

11. With regard to interconnection and access to infrastructure networks, dealt with in paragraphs 27 and 28, he said that the terms on which network operators were required to provide access should be not only fair and non-discriminatory, as stated in paragraph 28, but also objective, as was provided for, *inter alia*, in the relevant World Trade Organization (WTO) guidelines.

12. **Mr. Lalliot** (France) said, with reference to the concern expressed by the observer for Morocco, that the principle of universality was covered in some legal systems under the general principles of equality of access and non-discrimination, the principle of equality obliging the concessionaire, on the basis of fair remuneration, to provide universal access in any part of the territory under its purview. In recent years, European jurisprudence had likewise recognized the validity of the principles of equality, continuity, non-discrimination and universality. In French law, those principles extended to adaptability, requiring the operator to incorporate technological changes during the operation of the concession.

13. **Mr. Estrella Faria** (International Trade Law Branch) agreed that it was necessary to take account of the different legal systems and administrative traditions. The different terminology was perhaps not always reflected in the legislative guide. When the guide spoke of equality of treatment of clients and consumers, that indeed referred to the principle of universality of public services recognized in certain systems.

14. In response to the comment on paragraph 24 by the representative of France that in some legal systems it was not possible for the contract to provide for conditions whereby the service could be suspended, he said that that concern might be met by adding a proviso such as "in legal systems where this is possible" to the wording of the last sentence of that paragraph.

15. **Mr. Mazini** (Observer for Morocco) said that the principle of universality was a general principle that went beyond the principle of equality.

16. **Mr. Wallace** (United States of America) agreed that universality of service was not the same as equality of service. The third sentence of paragraph 22 captured the meaning of the principle of universality where it stated that in some legal systems the concessionaire might be under an obligation to extend its service facilities even if the particular extension was not immediately profitable or even if the concessionaire's territory might eventually include unprofitable areas.

17. **Mr. Choukri Sbaï** (Observer for Morocco) said, with reference to paragraph 24, that an operation might cease to be profitable for reasons that could be ascribed to poor quality of service or errors committed by the concessionaire, and that compensation for loss should therefore be tied to a judicial decision.

18. **Mr. Lalliot** (France) said that the concerns of the observer for Morocco regarding the principle of universality might be met by adding the words "in conformity with the principle of universality of public services" to the second sentence of paragraph 22.

19. **Mr. Zanker** (Australia) said that the fact of the matter, which should be recognized, was that a company that was unable to make a profit would not be able to provide the services, whatever arrangements were put in place.

20. **Mr. Mazini** (Observer for Morocco) said that the representative of France's suggestion would help. However, while the third sentence of paragraph 22 spoke of an obligation to extend service facilities even if the extension was not immediately profitable, the fourth sentence weakened that statement. It would be better simply to say that, if the extension involved unreasonable costs, the authorities should find a way of making up the loss by means, for instance, of tariff subsidies.

21. **Mr. Estrella Faria** (International Trade Law Branch) pointed out that paragraph 37 of draft chapter II, "Project risks and government support" (A/CN.9/458/Add.3), addressed that situation. A similar statement to the one in that paragraph could be included in paragraph 22 of chapter V, or the paragraph could contain a cross-reference to chapter II.

22. **The Chairman** said that, for the sake of brevity, a cross-reference would be preferable.

Legislative recommendation 4 and paragraphs 31-39

23. **Mr. Wallace** (United States of America) said that the first sentence of paragraph 31 was circular and should be redrafted. In paragraph 33, the reference to reviews of tariffs needed further explanation. Paragraph 34 also needed to be clarified: the rate-of-return method would probably work with power supply projects but might not work with roads, for example.

24. With regard to the first sentence of paragraph 38, it was not made clear that the legislator would need to anticipate investors' reactions to the use of one or other of the various tariff adjustment methods.

25. **Mr. Wiwen-Nilsson** (Observer for Sweden) said that recommendation 4 was not quite clear to him. If prices were subject to external control, it would presumably not be the project agreement that would set forth the mechanisms for price adjustment.

26. **Mr. Zanker** (Australia) agreed with the comments of the observer for Sweden and the representative of the United States of America, and said that the discussion in the notes to recommendation 4 was somewhat abstract. The point should be made that, when selecting the method to be used, the regulatory or contracting authority should have regard to the nature of the infrastructure in question. Another matter that did not seem to be dealt with was the component that should be taken into account for maintenance and further investment to ensure that the facility continued to be able to provide the services in question, as well as the margin of profitability.

27. **Mr. Estrella Faria** (International Trade Law Branch) said that regulatory issues were complex and there were many policy options available to host countries. The implementation of recommendation 4, the drafting of which might be deficient, would depend on the type of regulatory structure existing in the country in question. Some countries had statutory rate control mechanisms, and revision could only be effected through a statutory or similar revision procedure; in others the law simply provided for some ministerial body to review the reasonableness of the rate and any rate adjustment was left to the project agreement.

28. He agreed with the representative of the United States that some appropriate wording might be added to paragraph 33 in the interests of clarification. The discussion in the notes was indeed rather compressed.

29. **Mr. Zanker** (Australia) thought that the text could be elaborated in the light of the comments made.

30. **Mr. Wiwen-Nilsson** (Observer for Sweden) said that there were obviously different situations in different countries, but the wording of recommendation 4 would need to be amended so that it was not contradictory.

31. **The Chairman** said that the Secretariat would make the necessary adjustments to the wording.

Legislative recommendation 5 and paragraphs 40-43

32. **Mr. Wallace** (United States of America) pointed out with reference to recommendation 5 (b) that the monitoring of the concessionaire's performance might be carried out by the regulatory body, rather than the contracting authority, depending on the legal system of the country.

33. **Mr. Lalliot** (France) proposed a linguistic change in the French version.

Legislative recommendation 6 and paragraphs 44-46

34. **Mr. Lee Yong-shik** (Observer for the Republic of Korea) said that the meaning of the recommendation might be clearer if the phrase "subject to the approval of the contracting authority" were moved to the end of the sentence.

35. **Mr. Zanker** (Australia) said that one point worthy of mention was that the rules governing the use of the facility might need to be scrutinized to ensure that they were in conformity with government policy. In the case of a railway facility, for example, there might be rules contrary to a policy of access where there were a number of different operators running the facility.

36. **Mr. Phua Wee Chuan** (Singapore) said that, under the system prevailing in Singapore, the power to issue rules rested with the legislature. The third sentence of paragraph 45, which said that the concessionaire might be authorized to issue rules governing the use of the facility by the public, should be reworded to make it clear that the rules in question were not statutory in nature.

37. **Mr. Wallace** (United States of America) said that, although he agreed that a delicate balance had to be struck between constitutional or legislative authority and delegated authority, the notion of what was "inherently governmental", as referred to in the last sentence of paragraph 44, was constantly changing. In the last sentence of paragraph 45, the word "discretionary" seemed unsatisfactory; presumably the meaning was that the right should not be exercised arbitrarily. It was unclear from the penultimate sentence of paragraph 46 whether what was meant was that legislative authorization might be required on a case-by-case basis or that a general law might be needed to provide that authorization.

38. **Mr. Mazini** (Observer for Morocco) said, with reference to paragraph 45, that a distinction should be drawn, in the matter of regulatory powers, between the power to issue general rules governing operation, which was the responsibility of the State or an administrative regulatory authority designated by the legislator, and the special technical rules or conditions governing the use of the facility by the public, which the operator was free to issue, unless otherwise stipulated by statute. The third sentence of paragraph 45 should be revised to make it clear that the concessionaire would not be free to derogate from the general rules governing a public service. He agreed that the word "discretionary" in the final sentence was inappropriate. The prior condition should be that the terms should be fair, non-discriminatory and objective.

39. **Mr. Lalliot** (France) endorsed the comments by the observer for Morocco. There was a difference between technical matters concerning operation, which were covered by the contract specifications, and the powers of regulation deriving from legislative or supra-legislative sources, from which there could be no derogation. Paragraph 45 should be reworded accordingly.

40. With regard to the fourth sentence of paragraph 46, the reference to "legislative authority" was not very satisfactorily worded, at least in the French version.

41. **Mr. Zanker** (Australia) said that it had emerged from the discussion that the complex and delicate issue of where the authority lay for issuing rules or regulations should be approached with caution. A possible solution might be to give practical illustrations. Quoting the example of a railways operation, he said that, where the facility had been entirely privately owned and developed, the owner or operator should have the right to establish the terms of use by others, most appropriately by way of contract. He agreed that what was "inherently governmental" might change over time.

42. **Mr. Choukri Sbaï** (Observer for Morocco) suggested that, in the third sentence of paragraph 45, the words "the concessionaire may be authorized to issue rules governing the use of the facility" should be replaced by "the concessionaire may be authorized to regulate the use of the facility".

43. **Mr. Estrella Faria** (International Trade Law Branch), acknowledging that the Secretariat had not foreseen all the sensitive theoretical implications of the recommendation, said that what it had had in mind were simple technical rules governing the use of the facility by the general public. The reference to the concessionaire's authority to issue rules was not intended to imply a transfer to the concessionaire of statutory or inherently governmental powers. Another facet of the issue was that of the liability of the service provider vis-à-vis its customers and the extent to which that liability might be limited by unilateral rules issued by the public service provider that touched upon the very sensitive matter of consumer protection, upon which the Secretariat had considered it wise not to dwell, but he acknowledged that the entire section needed careful redrafting to take account of the concerns expressed.

44. **Mr. Mazini** (Observer for Morocco) said that it needed to be specified that the concessionaire was not free to issue technical rules that were contrary to legislative rules or principles governing operation. Moroccan experience in the field of telecommunications showed that there might be even technical rules that were prejudicial to the continuity, equality, accessibility and universality of public services.

Guarantees of performance and insurance (legislative recommendation 7 and paras. 47-58)

45. **Mr. Wallace** (United States of America) said that it should be made clear in the notes that performance bonds and other kinds of performance guarantees should be provided for in the request for proposals. He asked whether performance bonds were to be required throughout the contract period if a concession was granted in perpetuity. He appreciated that such concessions were rare but believed that they would become more common in the future. The difference between contract bonds and performance bonds, referred to in paragraph 48, was unclear to him in the present context.

46. He thought that, if the concessionaire was allowed to fix the sum payable under the guarantee or stand-by letter of credit as a small percentage of the project cost, as suggested at the end of paragraph 52, a statement to that effect would need to be included in the request for proposals. In the eighth sentence of paragraph 56, he wondered whether "latent defects" was not meant, rather than "late defects". In the final sentence of that paragraph, "waived" should perhaps be replaced by "dispensed with".

47. **Mr. Lalliot** (France) said that there was as yet no legislative provision for performance guarantees in France, but that the subject was on the agenda of forthcoming debates on the reform of the government contracts code. With reference to the penultimate sentence in paragraph 49, he asked whether arbitral proceedings were the only context in which the contractor's liability needed to be proved.

48. **Mr. Zanker** (Australia) agreed that "late" in paragraph 56 should read "latent".

49. **Mr. Estrella Faria** (International Trade Law Branch) confirmed that "latent" was the correct word.

50. The penultimate sentence in paragraph 49 would be revised to refer to dispute settlement procedures rather than specifically to arbitral proceedings.

51. In response to the questions asked by the representative of the United States, he said that a performance bond was a type of guarantee whereby the guarantor undertook to procure the completion of the works if the original contractor failed to do so, instead of

simply paying a sum of money as would be the case in other types of guarantee. As to guarantees in perpetuity, he understood that the insurance industry already had difficulties in providing performance guarantees over the extended period of time typical of such projects and that it would therefore be even more difficult to provide guarantees in perpetuity.

52. **Mr. Kaerle** (Observer for the Pan-American Surety Association) confirmed the explanations provided by the representative of the Secretariat. The insurance and particularly the re-insurance industry had great difficulty in accepting terms covering a concessionaire or consortium over a period of twenty or thirty years. Some solutions were suggested in paragraph 59, but the problem was not yet resolved.

53. **Mr. Wallace** (United States of America) said that his question concerned contract bonds, as distinct from performance bonds.

54. **Mr. Estrella Faria** (International Trade Law Branch) said that the performance bond fell into the category of non-monetary performance guarantees. He understood that a contract bond was a form of accessory guarantee; accessory guarantees differed from on-demand guarantees, including stand-by letters of credit, in that the latter were payable on the basis of the bearer's statement that there had been a breach of contract, whereas that would normally have to be demonstrated in the case of accessory guarantees.

55. **Mr. Kaerle** (Pan-American Surety Association) noted that, according to the first sentence of paragraph 54, the terms of an accessory guarantee usually required the beneficiary to prove the failure of the contractor to perform and the extent of the loss suffered by the beneficiary. He would suggest that there should be a reference to the rules of the International Chamber of Commerce allowing the beneficiary to call an accessory guarantee once an independent third party, to be named by all parties involved, had issued a certificate of non-performance or failure of the concessionaire and determined the extent of the loss suffered by the beneficiary.

56. **The Chairman** said that those observations would be taken into account, although such matters would be further discussed at a later stage.

Changes in conditions (legislative recommendation 8 and paras. 59-68)

57. **Mr. Wallace** (United States of America) said that, despite the cross-reference, after the mention of an indexation clause in paragraph 59, to paragraphs 33 to 37, the word "index" appeared only once in those paragraphs. Nor had he been able to find a previous reference to fuel supply agreements.

58. With regard to the second sentence in paragraph 65, it should not be for the concessionaire to negotiate mechanisms affording protection against the adverse impact of extraordinary and unforeseen events; such mechanisms should be included in the request for proposals. In the same sentence, "had they been taken into account" should read "had the events been taken into account". He wondered whether the mechanism would not in many cases be a provision for adjustment of tariffs of the kind discussed earlier.

59. The last line of paragraph 68 should be redrafted to distinguish more clearly the two different points: firstly, the desirability of having a ceiling for the cumulative amount of periodic revisions of the project agreement and, secondly, the appropriate amount.

Exemption provisions (legislative recommendation 9 and paras. 69-79)

60. **Mr. Wallace** (United States of America) said that the wording of paragraph 71 was confusing in that the penultimate sentence jumped to a different point, unrelated to the difficulty of listing all possible events of the *force majeure* type. The words "the concessionaire" were missing before "cannot" in the final clause of paragraph 72. He asked what was meant by the "special procedure" referred to in the last sentence of paragraph 73.

61. **Mr. Estrella Faria** (International Trade Law Branch) said that the wording at the end of paragraph 73 could be clarified. The idea was that either it might either be provided that the occurrence in question would produce automatic legal effects or the issue might be referred to a dispute settlement body, for example, which would first have to establish whether the occurrence should really be considered as constituting an exempting impediment.

62. **Mr. Lalliot** (France) said that he, too, had been surprised by the term "special procedure" in the sentence referred to. In view of the importance of the subject matter, the paragraph needed further clarification. The idea was presumably to allow the parties to define what they

understood by an "exempting circumstance". The meaning of the reference in the first sentence to giving the parties "the necessary freedom to find suitable arrangements" was unclear.

63. **Mr. Estrella Faria** (International Trade Law Branch) said that the formulation was deliberately vague to take account of the fact that in some legal systems there might be limits on the powers of the parties to provide either for exempting circumstances or for their consequences, whereas in other legal systems the parties would have more freedom in that regard. In order to meet the concerns of the representative of France, a reference to possible limits on the powers of the parties under the law applicable in the country might be added. With regard to the second sentence, in some legal systems an exempting circumstance produced immediate legal effects, whereas in others, if the parties opted for a special procedure, the effects might be produced from the date of the decision taken pursuant to such a procedure. He agreed that the sentence should be clarified.

64. **Mr. Lalliot** (France) said that a clear distinction should be made between exemption from liability and exemption from the obligation to perform. In French law, the contractor could be exempt from liability but could be required to continue to execute the project, if that was materially possible, even if it was no longer profitable, subject to the right to receive compensation subsequently.

Events of default and remedies (legislative recommendations 10 and 11 and paras. 80-91)

65. **Mr. Wallace** (United States of America) said, with reference to recommendation 11, that the term "serious failure" might not be clear to readers outside an UNCITRAL context.

66. In the fourth sentence of paragraph 81 of the notes, "review of the contracting authority by" should perhaps read "review by the contracting authority and by". In the last sentence of paragraph 84, the text should state that it was important to "limit" rather than to "reserve" the contracting authority's right to intervene to certain cases. The previous sentence interrupted the pattern of thought expressed in the paragraph and should be relocated.

67. In the second sentence of paragraph 86, "prompted" could perhaps be replaced by "caused" or "required". In the first sentence of paragraph 87, the word "nonetheless" could be inserted before "might". With regard to the first sentence of paragraph 91, wording could perhaps be added to that sentence to take into account a possible need to allow corresponding adjustments to the obligations in the project agreement.

68. **Mr. Mazini** (Observer for Morocco), recalling his reservations about the assignment of concessions, observed that paragraphs 87 to 90 seemed to imply that the lenders had a right of pre-emption. He had some misgivings about the reference in paragraph 90 to a need for the contracting authority to follow the same procedures as applied to the selection of the original concessionaire in the selection of a new concessionaire when that became necessary.

69. **Mr. Lalliot** (France) said that the second sentence of paragraph 81 needed further clarification since in some legal systems the right of review, for example, was a legislative prerogative. The distinction drawn between essential and secondary or ancillary obligations in the penultimate sentence of paragraph 81 was somewhat puzzling in the context of penalties, and should be further explained.

70. He asked what was meant by the term "apparently irremediable" in the last sentence of paragraph 88 and the expression "an implied step-in right" in the last sentence of paragraph 89.

71. Like the representative of Morocco, he had reservations concerning the assignment of concessions. Paragraph 90 did not adequately bring out the differences between the various legal systems, under some of which legislative authorization would be needed on so fundamental an issue.

72. **Mr. Zanker** (Australia) said that a point had been raised regarding the reference to "serious failure" in recommendation 11. The last sentence of paragraph 88, which referred to the contracting authority's right to intervene in the event of a specific, temporary and urgent failure of the service, probably threw light on what was meant by "serious failure". He cited the recent example of a total breakdown in the gas supply in one area of his country to illustrate what was no doubt meant. There was a need for consistency in the terminology used.

73. **Mr. Estrella Faria** (International Trade Law Branch) said that the question of step-in rights, with one concessionaire replacing another by joint agreement between the contracting authority and the lender, reflected increasingly common practice in major international infrastructure projects, although he conceded that there were difficulties in reconciling that practice with principles such as the non-transferability of a concession or the

personal nature of a delegation of a public service. The legislative guide therefore described the practice, while noting possible difficulties, especially in countries with a system based on Roman law. The first sentence of paragraph 90 mentioned the point, perhaps in compressed form. In some Latin American countries, clauses had been introduced in recent legislation explicitly authorizing a transfer of a concession under such circumstances. The last sentence of paragraph 89 referred to the possibility that existed in some countries of obtaining a security interest over the entirety of the concessionaire's rights and interests. That system was described in detail in chapter IV of the guide. With regard to "apparently irremediable" failure, the implication of the last sentence of paragraph 88 was that the step-in possibility for the lender was an extreme case that would be applied only where it was unavoidable. The sentence in paragraph 81 referring to secondary or ancillary obligations indeed contributed little to the paragraph and could be deleted.

74. The term "serious failure" was used to cover different terms used in national laws and had been used in other texts produced by the Commission. It referred to a situation that amounted to an apparently irremediable disruption of service and did not imply breach of contract.

75. **Mr. Choukri Sbaï** (Observer for Morocco) expressed reservations about the practice referred to in paragraph 91. A distinction should be drawn between the original agreement entered into between the contracting authority and the concessionaire, which was subject to certain rules such as transparency, objectiveness and competitiveness, and the agreement entered into between the lender and the concessionaire, also subject to certain criteria and based on guarantees to be given to the lenders. The designation of a new concessionaire by the lender could lead to arbitrary decisions. The wording of the paragraph should make it quite clear that the contracting authority might object to the designation of a new concessionaire.

76. **Mr. Estrella Faria** (International Trade Law Branch) pointed out that paragraph 91 provided for the possibility of refusal on the part of the contracting authority. The Arabic version was perhaps unclear, and would be reviewed.

77. **Mr. Choukri Sbaï** (Observer for Morocco) said that the contracting authority should propose the new concessionaire to the lender and not the other way round.

78. **The Chairman** said that it was in the interests of both the lender and the contracting authority to ensure continuity in the project, and the interests of both sides should be accommodated.

79. **Mr. Kashiwagi** (Japan) said he was in favour of retaining paragraph 91 as it stood, since it reflected recent practice.

80. **Mr. Wallace** (United States of America) suggested that the concerns of the observer for Morocco might be met by adding wording such as "by mutual agreement" where the paragraph spoke of a proposed substitute.

Chapter VI. End of project term, extension and termination (A/CN.9/458/Add.7)

81. **Mr. Estrella Faria** (International Trade Law Branch), introducing the chapter, said that it was an entirely new chapter, dealing not with the duration of the project agreement but with what happened after the agreement had reached the end of its term, and covered the extension of the agreement, its termination and the consequences of termination.

The meeting rose at 4.55 p.m.