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Summary record of the 658th meeting
Held at the Vienna International Centre, Vienna, on Tuesday, 25 May 1999, at 2 p.m.

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

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V.00-50987 (E)

The meeting was called to order at 2.15 p.m.

Election of officers (*continued*)

1. **Mr. Buraimoh** (Nigeria), supported by **Mr. Wallace** (United States of America), nominated Mr. Nur (Sudan) for one of the Vice-Chairman posts.

2. *Mr. Nur (Sudan) was elected Vice-Chairman by acclamation.*

3. **Mr. Abascal Zamora** (Mexico) nominated Mr. Cachapuz de Medeiros (Brazil) for a Vice-Chairman post.

4. *Mr. Cachapuz de Medeiros (Brazil) was elected Vice-Chairman by acclamation.*

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

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

Termination by the contracting authority (legislative recommendations 2 and 3 and paras. 5-23) (*continued*)

5. **Mr. Lee Yong-shik** (Observer for the Republic of Korea), speaking on recommendation 2 (c), said that he agreed with the Japanese representative that an adequate balance was needed between the contracting parties; however, the expression "full compensation" might imply compensation of full market value. For a thirty- or fifty-year project, that would be difficult to establish; and war and other extraordinary events might also prevent a Government from offering full market value. The term "fair compensation" was more flexible and should be maintained.

6. **Mr. Gill** (India) endorsed those views.

7. **Mr. Estrella Faria** (International Trade Law Branch) said that the representative of the United States of America, at the previous meeting, had asked about the relationship between the matters under discussion and legislation. The Secretariat's research indicated that nearly 90 per cent of the jurisdictions with relevant legislation had legislative provisions on termination, often indicating the circumstances in which a project might be terminated.

8. Given the general recourse to termination by contracting authorities in some regions of the world, the Secretariat had been advised to include matters such as the scope, purpose and dangers of termination and the desirability of establishing the conditions under which the right to terminate might be invoked.

9. Recommendation 3 (b) referred to two situations: one where the lenders were given an opportunity to bring about a "cure" through a third party, without replacing the concessionaire, and one where the concessionaire was permanently replaced, in agreement with the contracting authority (a step-in right situation).

10. Several comments had been made on paragraphs 20 and 21, concerning insolvency of the concessionaire. Paragraph 21 merely described the provisions in certain legal systems. Paragraph 20 referred to the possibility of excluding assets from the insolvency proceedings.

11. Regarding the Australian representative's comment on paragraph 14, his understanding was that in some legal systems the concession was awarded by decree and that the project agreement then had to be signed; however, the wording could be clarified.

12. The question of full and fair compensation was related to the sensitive issue of nationalization. There had been much debate in various international forums on the standard for compensation in the event of nationalization or expropriation, and the language used in the guide had to take into account the principles contained, for example, in the relevant General Assembly resolutions. There had been no attempt, however, to go into detail.

13. **The Chairman** suggested that the expression "fair compensation" could be accepted as a reasonable compromise.

14. *It was so agreed.*

Termination by the concessionaire (legislative recommendation 4 and paras. 24-29)

15. **Mr. Wallace** (United States of America) suggested that in the first sentence of paragraph 25 a word such as "substantial" or "material" should be included before "breach", since not all breaches would justify withholding the performance of one's obligations in every legal system.

16. In the first sentence of paragraph 26, the expression "may mitigate" might be misleading if "may" was understood as permissive, depending on the relevant law.

17. **Mr. Zanker** (Australia) noted that subparagraph (a) of recommendation 4 referred to "serious default by the contracting authority". Some examples could be given, as was done in the case of serious default by the concessionaire.

18. **Mr. Lalliot** (France) said that the French and other legal systems allowed for unilateral termination by the contracting authority but not by the concessionaire, who could only ask for termination through a third party, such as the competent court. The text should take that into account.

19. He asked for clarification of the words "serious default by ... other agency of the host Government" in recommendation 4 (a).

20. Paragraph 25, describing the situation in certain legal systems, including the French, should go into more detail. It should be noted that the concessionaire could have recourse to a court. After a court decision the concessionaire had a right to full compensation for prejudice suffered.

21. **Mr. Lee Yong-shik** (Observer for the Republic of Korea), commenting on the remark by the United States representative on paragraph 25, said that it was true that not every type of breach would justify withholding performance of obligations. However, in some jurisdictions a "serious" breach rather than just "material" breach would be needed. He suggested using a general expression such as "certain types of breach".

22. With regard to the last comment of the French representative, he felt that the reference should be to "fair compensation" rather than "full compensation".

23. **Mr. Al-Zaid** (Observer for Kuwait) thought that the reference to termination by mutual consent in recommendation 5 (b) should be expanded.

24. **The Chairman** said that recommendation 5 would be taken up in due course.

25. **Mr. Estrella Faria** (International Trade Law Branch), referring to the comments of the representative of France on paragraph 25, said that the text could be expanded. It was true that the question of the procedure by which the concessionaire could obtain termination was not covered.

26. As to the words "other agency of the host Government" in recommendation 4 (a), the reference was to other agencies that might have undertaken to provide some form of support.

27. **Mr. Mazini** (Observer for Morocco) suggested that the chapeau of recommendation 4 should be reworded to make it clear that such termination would be exceptional.

28. **Mr. Estrella Faria** (International Trade Law Branch) said that recommendation 4 could be amended to that effect and that reference could be made in the notes to the fact that in some legal systems the concessionaire could only request the competent court to terminate the project agreement.

29. **Mr. Wallace** (United States of America) considered that paragraph 24 was already well balanced. To include mention of the court action required in some countries was not necessary. The Commission should be cautious about making changes since the whole point of the guide was to enable countries to receive domestic and foreign investment for infrastructure projects, and investors had certain requirements. They would, he thought, expect to be able to buy their way out of such deals in the circumstances described in subparagraphs (a) and (b). The text was already fully protective of Governments.

30. **Mr. Lalliot** (France) said that it would be only honest to note that the two major types of legal system provided radically different solutions.

31. **Mr. Wiwen-Nilsson** (Sweden) agreed with the principles expressed by the United States representative, but thought that the Secretariat's suggestion was well balanced. The words "under exceptional circumstances" could be added to the recommendation.

32. **Mr. Lalliot** (France) thought that the Secretariat's suggestion could be accepted as a compromise.

33. **Mr. Lee Yong-shik** (Observer for the Republic of Korea) supported the suggested addition to the recommendation. There was little point in debating different legal cultures. The various opinions should be set out in the notes.

34. **Mr. Wallace** (United States of America) said that he could also accept the suggested addition. Perhaps the notes could make it clear that the concessionaire had the right to buy out.

35. **Mr. Estrella Faria** (International Trade Law Branch) said that the Secretariat would try to take account of the suggestions. As far as the drafting of the recommendation was concerned, more flexible language could perhaps be found, to leave open the possibility that termination might require a court decision.

Termination by either party (legislative recommendation 5 and paras. 30 and 31)

36. **Mr. Wallace** (United States of America) said that paragraph 30 of the notes was a little abstract. He wondered what circumstances were envisaged in the first sentence.

37. He asked for clarification of paragraph 31. Would the "mutual consent" referred to be anticipated in the project agreement?

38. **Mr. Lalliot** (France) wondered whether subparagraph (a) of recommendation 5 was not redundant. The point would presumably be covered by recommendations 5 (b) and 4 (b).

39. **Mr. Estrella Faria** (International Trade Law Branch), replying to the question of the representative of the United States on paragraph 31, said that legislative authorization might not be required in all legal systems. In some countries, however, because of rules governing the provision of public services, the contracting authority might lack the power to agree to what would amount to discontinuation of the service. The matter might not need to be provided for in the project agreement.

40. As to the point made by the representative of France, the Secretariat considered that recommendation 5 (a) was different from recommendation 4 (b), since either the contracting authority or the concessionaire could invoke it and it might be of benefit to both.

41. **The Chairman** thought that, with that explanation, recommendation 5 could be left as it was.

Transfer of assets to the contracting authority, transfer of assets to a new concessionaire and financial arrangements upon termination (legislative recommendations 6, 7 and 8 and paras. 33-45)

42. **Mr. Wallace** (United States of America) observed that recommendation 6 did not sufficiently differentiate between the termination contemplated in the contractual arrangement and premature termination. The two situations were treated identically in the recommendations, but they were not the same as far as compensation was concerned.

43. Some redrafting of paragraph 33 of the notes was needed. The discussion on the transfer of project-related assets should also include a reference to assets built by the concessionaire, a point which was in fact acknowledged in paragraph 35 (a). Nor did the discussion seem to cover intangible assets such as accounts receivable or insurance proceeds.

44. Subparagraph (a) of paragraph 35 referred to assets that must be transferred to the contracting authority and said that that category typically included assets owned by the contracting authority. However, there might be other cases in which the contracting authority might wish to have the assets transferred to it.

45. In the penultimate sentence of subparagraph (b), the words "expected to be" could be deleted. In the last sentence, the word "retention" was too narrow. In subparagraph (c), the words "(b) above" should read "(a) or (b) above".

46. In paragraph 36 (b) the last four words ("under the second agreement") should either be removed or made broader.

47. In the last sentence of paragraph 39, the word "negotiating" did not accurately capture what should happen: the contracting authority should propose terms in the documentation and prospective bidders could then ask for clarification or a change. In the fourth line of paragraph 39 (a), the words "immediate loss" were somewhat ambiguous. Regarding the reference in the ninth line of paragraph 39 (b) to difficulties in establishing the value of unfinished works, he suggested that the concept of replacement cost might be mentioned. At the end of that paragraph, the term "amortization" might be replaced by a word like "depreciation".

48. With regard to paragraph 41 (b), he assumed that the parting concessionaire could be the bidder for the project assets mentioned.

49. In connection with the last sentence of paragraph 44, and the reference to compensation not necessarily being "full" compensation, it was not clear whether government guarantees that might have been given would apply.

50. **Mr. Zanker** (Australia) agreed with the United States representative that the text confused the normal end of a project with early termination. Moreover, the various types of contract were not taken into account. The material needed re-ordering.

51. **Mr. Wiwen-Nilsson** (Observer for Sweden) suggested that the problem of the United States representative with the word "amortization" could be solved by transferring the definition in paragraph 39 to the place where the word occurred for the first time in the notes.

52. There was an inconsistency in the treatment of compensation in the legislative recommendations. Recommendation 6 (b) spoke of an option for the contracting authority to purchase certain assets at their “fair market value”, while recommendation 7 spoke of a transfer of assets to a new concessionaire against “adequate compensation”.

53. In subparagraph (b) of recommendation 8, lost profits were included in the definition of compensation due to the concessionaire, but in subparagraph (c) they were not mentioned. In the second sentence of paragraph 45 (b) of the notes, reference was made to compensation for lost profits in such cases. Provision to compensate for lost profits would certainly encourage private investment.

54. In paragraph 36 (b), there seemed to be some confusion between the concept of “financing” and the concept of “expected return”.

55. The last sentence of paragraph 39 (a) gave him cause for concern since in most legal systems damage did indeed include lost profits.

56. He, like the United States representative, was concerned by the sixth sentence of paragraph 39 (b), referring to the difficulties that might be found in establishing the value of unfinished works. The sentence was confusing and irrelevant, and should either be deleted or redrafted.

57. In paragraph 41 (b) the second sentence, suggesting that the Government might envisage less than full financial compensation in the case considered, should also be deleted as it was tantamount to recommending an abuse of power.

58. Turning to the question of how to calculate lost profits, he said that the method of calculation described in the second sentence of paragraph 42, which spoke of calculating lost profits on the basis of the concessionaire’s revenue during previous financial years, was faulty since for a project terminated in the first year of operation there would be no profit at all. The sentence should either be deleted or redrafted. The same applied to the similar statement in the second sentence of paragraph 45 (b).

59. The last sentence of paragraph 45 (a) stated that, in the contract practice of some countries, government agencies did not assume any obligation to compensate for lost profits when a large construction contract was terminated for convenience. That statement was unnecessary and the practice referred to was to be deprecated.

The meeting was suspended at 3.50 p.m. and resumed at 4.15 p.m.

60. **Mr. Lalliot** (France) said that, unlike the Australian representative, he found recommendations 5, 6 and 7, which all dealt with disposal of assets upon termination, to be quite clear.

61. The last part of the penultimate sentence of paragraph 35 (b) of the notes was difficult to understand, at least in the French version. If, in the second sentence of paragraph 36, the words “it may be useful for the law to require the concessionaire to make the assets available to a new concessionaire” meant that all the assets should be made available, that should be spelt out. He asked whether “the required conditions should be reasonable” in the penultimate sentence of paragraph 37 meant that the assets should be returned in such a condition as to allow for normal functioning of the operations. With regard to paragraph 39, the word “amortization” in the last sentence was not the right term.

62. In the first sentence of paragraph 41 (b), “nominal sum” was unclear, at least in the French version, and the word “offered” might be interpreted to mean that the project assets would be given away without charge.

63. In the penultimate sentence and in the last sentence of paragraph 45 (a), and in the first sentence of paragraph 45 (b), reference was made in the French version to “*la partie contractante*”. That should read “*l’autorité contractante*”.

64. **Mr. Wallace** (United States of America) said that the last sentence of paragraph 45 (a), mentioned by the observer for Sweden, was misleading if the implication was that it would apply to long-term concessions as well as short-term construction contracts.

65. He did not entirely agree with the observer for Sweden concerning the second sentence of paragraph 45 (b), since the method of calculation described might be the only one available. Perhaps it could be called “one approach among others” and the reference could be to “the immediately previous financial years”.

66. **Mr. Estrella Faria** (International Trade Law Branch) thanked delegations for their suggestions. However, with regard to the view expressed that the regime for the transfer of assets upon expiry of the project agreement should be different from the regime applying on termination, the Secretariat would appreciate a more concrete indication of what the delegations concerned had in mind.

67. Referring to the comment of the French representative on paragraph 37, he said that the implication of the word "reasonable" was that, depending on the length of the contract, the assets, although they should obviously be in working order, could not be expected to be in the same condition as when they were new.

68. Concerning the word "amortization", he said that the intention was to refer to the time needed to recover initial investment, repay debt and make a reasonable profit. The Secretariat would appreciate any suggestions for a better term.

69. **Mr. Wiwen-Nilsson** (Observer for Sweden) said that the term "amortization" meant recovery of investment. Typically, the investment would be financed through debt and equity. Cash would be generated to repay debt.

Wind-up and transitional measures (legislative recommendation 9 and paras. 46-58)

70. **Mr. Wallace** (United States of America) said that subparagraphs (a) and (b) of recommendation 9 were unclear. Did they refer to transfer of technology and training of personnel after the termination of the agreement or before termination?

71. Turning to the notes, he said that the first sentence of paragraph 46 referred to the transfer of the facility "at the end of the concession period", but one might wish to cover cases of early termination as well.

72. The discussion of the transfer of technology in paragraphs 47 to 51 raised serious questions, touching on so-called "North-South" issues. There needed to be a recognition that many concessionaires would not be prepared to act like charities or foreign aid agencies. More study was needed on the realities of transferring technology in privately financed infrastructure projects. Moreover, much of the discussion on the transfer of technology was not limited to termination but referred to projects as such.

73. With regard to the second sentence of paragraph 47, he noted that not only the contracting authority but also other government agencies would often wish to acquire knowledge of technological processes and their application.

74. It was unclear how the general observation in the second sentence of paragraph 48 that the transfer of technology might occur through the licensing of industrial property applied to privately financed infrastructure projects.

75. The second sentence of paragraph 49 spoke of the possibility for an indication of requirements regarding personnel and their qualifications to be asked for in the request for proposals. It was unclear whether the reference was to requirements during the normal term of the project agreement or at the end. It should be pointed out that the heading of the section under discussion was "Wind-up and transitional measures".

76. The second sentence of paragraph 51 referred to a possible requirement that the supply of all documentation was to be completed by the time fixed for completion of the construction. That was appropriate in the case of a three-year construction project, but would it apply in the case of a thirty-year concession?

77. It might be more appropriate to transfer the reference to spare parts in the first sentence of paragraph 52 to section D.3 (c), entitled "Supplies of spare parts".

78. Paragraphs 53, 55 and 56 raised the question of whether the intention was to cover early termination situations. The discussion on spare parts could perhaps be integrated with the discussion on operation and maintenance.

79. He wondered whether it would not be advisable to include a section E entitled "Post-transfer management contract"; that matter was not yet discussed anywhere in the guide.

80. He also drew attention to some minor drafting points.

81. **Mr. Wiwen-Nilsson** (Observer for Sweden) said, with relation to the references in paragraphs 55 and 56 to spare parts being supplied and possibly manufactured by the concessionaire, and in paragraph 58 to the concessionaire effecting repairs, that the concessionaire would not be in the business of manufacturing spare parts or selling repair services.

82. **Mr. Choukri Sbaï** (Observer for Morocco) suggested that, at the end of subparagraph (a) of the recommendation, the words "during and after the construction period" should be added.

83. In subparagraph (b), he suggested the addition of wording to the effect that it would be desirable for the concessionaire to employ local personnel in the operation and maintenance of the facility.

84. **Mr. Zanker** (Australia) said that a distinction needed to be drawn between what could be asked for at the normal end of a contract and what could be asked for when a concessionaire's contract was terminated early. It was

unrealistic to ask a dismissed concessionaire to provide all the additional information set out in the paragraphs under discussion.

85. **The Chairman** wondered whether the content of paragraphs 46-58 wound not be better placed in chapter IV, on the project agreement.

86. **Mr. Estrella Faria** (International Trade Law Branch) said that in drafting the notes the Secretariat had had in mind not the abnormal but only the ordinary situation in which the parties arranged in the project agreement for the necessary information to be made available to the contracting authority at the end of the project period. It had not wished to invite a discussion on the residual obligations of a concessionaire whose contract was terminated early.

87. **Mr. Mazini** (Observer for Morocco) said that the obligation to transfer technology would be a contractual one. It was not a matter of expecting charity. The necessary licensing should perhaps also be provided for.

88. **Mr. Zanker** (Australia) said it would be helpful to make it clearer that the paragraphs under discussion applied to the normal ending of a project. Some discussion of the situation where a new concessionaire took over at the end of the project would also be useful.

89. **Mr. Lalliot** (France) thought that it would be a good idea to deal with the issues under discussion, which were mainly contractual issues, in another chapter of the guide concerned more specifically with such matters. In any treatment of those issues, both the legitimate interests of the concessionaire and those of the host country must be considered.

90. **Mr. Wallace** (United States of America) supported the comments of the French representative. He also agreed with the observer for Morocco that it would be a matter of contractual obligation, once the parties had agreed on a contract.

General suggestions concerning the drafting of chapter VI

91. **Mr. Lortie** (Observer for Canada) noted that many of the legislative recommendations in chapter VI related to exceptional situations. He suggested that the general principle involved should be set forth at the beginning of such a recommendation, and the exceptions listed after that. For example, recommendation 2 might begin: “The host country may wish to provide that the agreement may not be terminated unilaterally by the contracting authority unless ...”.

The meeting rose at 5.05 p.m.