Indonesian Journal of International Law

Volume 20
Number 4 *Trade & Investment*

Article 1

August 2023

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Indonesian Journal of International Law (2023), Vol. 20 No. 4, pp. 649 - 670
http://doi.org/10.17304/ijil.vol20.4.2

THE INVESTORS-STATE CONTRACT MAKING CASE FOR RENEGOTIATION OF THE ORIGINAL CONTRACT

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Abstract

Most Investor-State projects involve significant capital investment, while recognizing the existence of acute risk factors. After making such investments, investors expect fiscal, regulatory, and political conditions to remain stable or favorable throughout the project's duration. However, due to the long-term nature of agreements, there have historically been significant disputes over differences in expectations versus reality. States may rapidly evolve their economies and interests, sometimes pushing for new deals seen as fairer to investors with changing circumstances. Stabilization clauses have traditionally been used by investors to protect their interests, but over time, such measures have weakened as they are perceived as a threat to the State's sovereignty. As an alternative, renegotiation is being considered as a more mutually inclusive process. This article explores the significance of renegotiation, its evolution, and the issues that need addressing for it to be an acceptable solution for all stakeholders.

Keywords: *ISDS, renegotiation, stabilization clauses*

Received : 6 August 2022 | Revised : 11 December 2022 | Accepted : 11 March 2023

I. INTRODUCTION

Several common characteristics of contract relating to the Energy sector[1] are complexity, capital intensiveness, and a long duration.[2] Given the long-term nature of such agreements, the parties involved have been noted to encounter changes in the political, economic, and social spheres, often leading to disputes over the original drafted contract. This became more evident in the past 2-3 years following the impact of the COVID-19 pandemic and a sharp decline in the prices of oil, with countries tending towards low-carbon alternatives.

[1] From the perspective of this paper, 'Energy sector' here encompasses companies in the oil & gas and petrochemical sectors.
[2] Peter D. Cameron, *International Energy Investment Law: The Pursuit of Stability*, First Edition (Oxford: Oxford University Press, 2010), 74.

Since the subject of such contract are 'resources' of the State, the agreements are mostly entered into with the State-owned entities or companies that have separate legal personalities. These contracts may surpass the realm of national laws when international law is identified as applicable and creates a complex web, which results in several significant legal questions.

The most important category is represented by concession agreements, production-sharing contract, service contract, or other types of contractual relations in the petroleum exploration and production fields. The foreign investors in natural resources traditionally expect economic, political, and regulatory stability from the host State at the time of investment. However, the duration of contract prevents the State from continuing with the same policies owing to changes in circumstances that affect contract. The mechanism of stabilization clauses traditionally used by the investors to negate the potential risk of alterations to the regime or policies has garnered mixed success and is often criticized for being against the interest of the host State.[3] Renegotiation appears as an alternative approach to such situations by examining contract's mutability and facilitating organic changes. This enables adaptation to changes and maintains the continuity of contract by re-establishing the equilibrium. Unlike stabilization clauses, renegotiation provides the State with an adequate opportunity to follow legitimate policies by allowing the investors to achieve their objectives from contract.

The debate surrounding stabilization and renegotiation clauses is now more significant than ever, owing to the sweeping changes that policies focusing on climate change mitigation will bring. The Paris Agreement on Climate Change mitigation is a primary example of the multi-structural changes that the countries will be obligated to make in their policies, which inevitably will alter predetermined circumstances. Therefore, this research focused on the need for parties to adopt renegotiation clauses in their Energy Sector contract. The *first scenario* examined stabilization clauses, their evolution, and analyses to determine the existence of a more subdued form of such clauses. It also highlighted the gradual tilt towards renegotiating rather than freezing contract. The *second scenario*

[3] John Ruggie, "Stabilization Clauses and Human Rights," International Finance Corporation (World Bank Group), 2008, available at http://www.ifc.org/ifcext/media.nsf/Content/Stabilization_Clauses_Human_Rights.

assessed the need for recognizing renegotiation as an alternative in situations where the State' policies make changes to contract beyond wealth maximization. The *third scenario* evaluated situations where no renegotiation clauses are expressly provided for in contract. *The fourth scenario* analysed the possibility of the co-existence or contradiction of renegotiation and stabilization clauses. The *fifth scenario* discussed the issues with renegotiation that need further addressing in order for the process to become a more acceptable solution in the future.

II. STABILIZATION CLAUSES

Stabilization clauses have been defined as "explicit or specific commitments designed by the host State to shield the foreign investors from political risk and, in particular, subsequent adverse legislative or regulatory change in the host State."[4]

Some have described stabilization clauses as the 'investors biased' mechanism, where the protection is either against unilateral modifications or the deprivation of the rights of the investors.[5] Traditionally, stabilization clauses have been identified as providing bankability to investment agreements and helping maintain the economic equilibrium through the use of its freezing effect[6]. This role was best highlighted in *Charanne BV v Spain,*[7] where the State were not restricted from enacting any laws or regulations, providing they were fair, equitable, and non-discriminatory unless they had a stabilization clauses in place.

However, such traditional outlooks towards stabilization clauses have changed. This has led to adjustments from the classic freezing clauses or clauses stricto sensu. In this type of clause, the provisions of a national legal system chosen to govern a contract on a specified date

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[4] James Crawford, *Brownlie's Principles of Public International Law* (Oxford: Oxford University Press, 2019), 606.

[5] Cameron, *International Energy Investment Law*, 86.

[6] International Finance Cooperation, Sta*bilization Clauses and Human Rights*, World Bank (2008), available at <http://www.ifc.org/wps/wcm/connect/9feb5b00488555eab8c4fa6a6515bb18/Stabilization%2BPaper.pdf? MOD=AJPERES>

[7] *Charanne BV and Construction Investments S.A.R.L v Kingdom of Spain*, SCC Case no 062/2012.

remain 'constant in its application' without being affected by any future alterations to the national law.[88] The adjustments have been towards a more system of more equilibrated or rebalanced benefit clauses. In these clauses, the effects of changes are managed by negotiating for amendments to contract in order to maintain a balance of benefits for both parties involved.[99]

Another criticism of stabilization clauses concerns their relevance. Substantive protection mechanisms, such as a guarantee of 'Fair and Equitable Treatment' (FET), 'Prohibition on expropriation without compensation,' whether directly or indirectly, and 'Prohibition of discrimination,' are considered much more convenient for the investors. The consent of the most State to international arbitration for claims presented by the foreign investors also results in misgivings about the applicability and relevance of stabilization clauses. However, the treaty protection claims are often subjected to interpretation by tribunals, which leads to a wide range of differing views. Experiences have further shown that having a stabilization clauses negotiated in contract strengthens the investors' argument while approaching a tribunal through a treaty. This was highlighted in *Total vs. Argentina,*[10] where the expectations of the investors would have been considered 'undoubtedly legitimate,' supposing they were based on stabilization clauses. This highlights the importance of such clauses, particularly while establishing stability and damage expectations.[11]

Interestingly, the restrictive nature of the classical stabilization clauses has slowly led to its demise and prompted the preference for the economic equilibrium model, which aims to maintain the equilibrium between the parties at the time of contract by offsetting the adverse policies. Despite such changes and adaptations, there are remnant inherent issues with such clauses. Many scholars have argued that such measures have been ineffective in preventing the State from adopting

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88 *Amoco International Finance Corporation v. The Government of the Islamic Republic of Iran & Ors*, (1987) 15 Iran-US Claims Tribunal 189.

99 Muthucumaraswamy Sornarajah, *International Commercial Arbitration: The Problem of State Contracts* (New York: Longman, 1990), 59, 75.

10 *Total S.A. v Argentine Republic* (ICSID Case No. Arb/04/01).

11 Peter D. Cameron, "Stabilization Clauses: Do They Have a Future?" *BCDR International Arbitration Review* 7, no. 1 (2020): 112.

nationalization policies through the use of permanent sovereignty over resources.[12] According to some others, the effectiveness of these clauses is limited to helping the investors secure an exit with better financial terms. Another affected area is the length of contract in the energy sector, which exceeds the life of any particular government and affects the stability of the regime.[13] For example, a change in tax consideration[14] or a tectonic shift in economic policies[15] are among the many reasons that have often contributed to the rise in the Investors-State disputes.

Contrastingly, the *Aminoil Award*[16] illustrated the limitations of contractual obligations in restricting the acts of the State done in a sovereign capacity. Experience also suggests that such clauses rarely deter the State from taking measures for national interest even when expropriation may occur. The reasons for the ineffectiveness of stabilization clauses become evident from the State's perspective. Since such clauses attempt to limit the Sovereign powers of the State over its natural resources, its *jus cogens* rights add to the uncertainty and consistent tilting of balances.

A. EVOLUTION OF STABILIZATION CLAUSES

Stabilization and renegotiation are traditionally considered contradictory to each other, primarily due to the existing tensions of stability and flexibility respectively sought by each system. However, the change in the language of stabilization clauses from the classic freezing clauses to economic procedures has highlighted the failure of

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[12] Nelia Daniel Dias, "Stability in International Contracts for Hydrocarbons Exploration and Some of the Associated General Principles of Law: From Myth to Reality," *Oil, Gas, and Energy Law* 8, no. 4 (2010), available at www.ogel.org/article.asp?key=3053.

[13] Mario Mansour and Charole Nakhle, "Fiscal Stabilization in Oil and Gas Contracts," *The Oxford Institute for Energy Studies*, (2016), available at https://www.oxfordenergy.org/wpcms/wp-content/uploads/2016/02/Fiscal-Stabilization-in-Oil-and-Gas-Contracts-SP-37.pdf

[14] Danish Mehboob, "Vodafone v. India," ITR Global Tax Review, 5 February 2021, accessed 5 February 2022, https://www.internationaltaxreview.com/article/2a6a800txc7nnn27smio0/itr-global-tax-50-2020-21-vodafone-v-india.

[15] Ana M. Lopez-Rodriguez and Pilar Navarro, "Investment Arbitration and EU Law in the Aftermath of Renewable Energy Cuts in Spain," *European Energy & Environmental Law Review* 25, no. 1 (2016): 5.

[16] Kuwait v. The American Independent Oil Company (AMINOIL), 21 ILM 976.

the restrictive approach. The economic equilibrium clauses facilitate the negotiation of amendments to contract in an effort to reinstate the balance of the original contract.[17] A variant is the 'allocation of burden clauses,' which focuses on indemnifying the loss or damage suffered by the investors due to the actions of the State in order to establish the original contract equilibrium.

The modern approach seeks to maintain a balance of interests between the investors and the State and attempts to be equally beneficial to both, a significant diversion from the original approach. Furthermore, parties in the hybrid clauses are obliged to negotiate in good faith to establish the original balance whenever the status quo is disturbed by government actions.[18] The features of such clauses can be identified as containing the following:

i. Defining the change of circumstances that will trigger renegotiation. This can be defined in general or specific economic terms.
ii. Indicating the effect of change on contract
iii. Outlining the objective and procedure of renegotiation
iv. Providing a solution if renegotiation fails.19

These changes have not necessarily created uniformity in the type of stabilization clauses applied currently, as a significantly large number of the State still offer freezing obligations as security to the investors. However, the investors have started to realize that such clauses can be purely to attract investments with no guarantee of commitment. The termination of contract in most situations also ends up benefitting none of the parties involved and majorly results in long-standing legal disputes, which significantly increase costs. Therefore, economic balancing mechanisms like renegotiation, which give both parties a better chance to negotiate in new circumstances are gaining more recognition than unilateral protections.

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[17] Cameron, *International Energy Investment Law*, 87.
[18] *Ibid.*, 75.
[19] *Ibid.*,103.

III. ANALYSING THE PREFERENCE FOR RENEGOTIATION

The Arbitral Tribunal in the *Aminoil* case defined renegotiation as a mechanism through which "a new equilibrium is re-established for a contract in place of the original equilibrium that was lost as a result of a change in circumstances." It also highlighted that a change in the circumstances or nature of contract can lead to a need for renegotiation. A general change over the decades in the energy industry has been the evolving role of the State. This encompasses a greater administrative influence over the way investors are expected to handle natural resources, thereby necessitating a renegotiation of the original contract. This is also because of the changing dynamics of the State's bargaining power during the initiation of the original contract, which was much weaker before the influx of investments.[20]

One of the key advantages of a renegotiation clauses is the flexibility offered to the parties. Unlike the rigidity of stabilization clauses which strive to nullify the effects of an action undertaken by the State, renegotiation offers flexibility for parties to re-assess terms and arrive at an equitable solution.

This flexibility is also helpful when acts of the State are not limited to wealth maximization, such as in situations driven by other factors, including socioeconomic reforms. The most relevant example involves changes to the policies of the many State due to their commitment to reaching net-zero carbon emissions. Renegotiation would offer a strong case for continuing contractual relationship after any rearrangement of contract terms that were affected by changes in circumstances.

This is a view contrary to the idea of unilateral termination of contract by the State and the associated compensation, which is driven by the principles of efficient breach. Under such principles, the parties are given an incentive to uphold contract unless inefficient.[21]

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[20] John Y. Gotanda, "Renegotiation and Adaptation Clauses in International Investment Contracts, (Revisited)", *Vanderbilt Journal of Transnational Law* 36 (2003): 1463.

[21] Barry E. Adler, "Efficient Breach Theory Through the Looking Glass," *New York University Law Review* 83, no. 6 (2008): 1684. See also Eric A. Posner and Alan Sykes, *Economic Foundations of International Law* (London: Harvard University Press, 2013), 103.

A. THE ECONOMIC EFFICIENCY ARGUMENT

Two different standards of compensation are generally followed in International practice. They are The Hull principle, which requires compensation to be 'prompt, adequate, and effective,' and the Appropriate Compensation standard, where the compensation is analysed on case-by-case basis.[22] In *Lithgow v. United Kingdom*,[23] the European Court of Human Rights contested that the State acts of nationalization were still unrecognized as a part of its sovereign right and the idea of compensation is so inextricably associated, meaning the State was in the best position to assess the compensation payable to the investors. Therefore, the court highlighted its inability to interfere with the process of compensation in the absence of reasonable grounds. Such ideas in favour of appropriate compensation have also been echoed in other judgments.[24]

The Hull principle is generally more accepted in investment arbitration[25] with several tribunals holding that 'appropriate compensation' can also mean full compensation and examining the aspects of lost profits while determining compensation. Under the 'efficient breach theory,' the termination of a contract is based on the prism of achieving greater economic efficiency than contract can provide. This applies the Pareto efficiency principle, where 'a rule is seen as efficient if no person is made worse off by it, and at least one-party benefits.'[26] This approach gives a damage or compensation-oriented approach to the breach of a contract rather than providing any encouragement to continue with the same. It finds relevance in long-term contract by enabling the State to act opportunistically, as there would original be an obligation to compensate the investors, which would also include the lost future profits. Therefore, the State would

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[22] Sangwani Patrick Ng'ambi, "Efficient and Flexible: The Case for Renegotiation Clauses in Concession Agreements," *Zambia Law Journal* 45, no.1 (2014): 3.
[23] *Lithgow v. United Kingdom*, (1986) 8 EHRR.
[24] *Williams & Humbert v. W & T Trademark*, (1986) AC 368.
[25] Andreas F. Lowenfeld, *International Economic Law*, Second Edition (Oxford: Oxford University Press, 2008) 564. See also Campbell McLachlan, Laurence Shore and Matthew Weiniger, *International Investment Arbitration Substantive Principles*, First Edition (Oxford: Oxford University Press, 2010), 317.
[26] *Ibid*.

ideally only make an efficient termination of a contract when a profit is made after indemnifying the investors for the expropriated loss.[27]

The premature termination of energy-related contract is supposed to negatively affect the State, as the extensive duration of investments means *lucrum cessans* should be paid to the investors, and the nature of the business signifies a protracted period would be needed to recover the cost, thereby forcefully binding the State to contract. However, this approach is limited to the idea of wealth maximization and ignores the fact that the role of the State cannot be restricted to economic efficiency. The State's actions can equally be driven by public purposes or policies, such as the nationalization of Lena Goldfields by the Soviet government after shifting its policies towards capitalism.[28] Regardless of the purpose of the policies undertaken, renegotiation clauses can help the State increase flexibility since compensation, including the provision of future profits, must occur.[29][29]

The advantage of renegotiation clauses is their ability to avoid the stage of termination by allowing contracting parties to reassess conditions before reaching any conclusion. Therefore, these clauses are flexible as well as *Pareto efficient* because they ensure the investors and the State make profits. The inherent flexibility of renegotiation clauses allows the State to pursue legitimate public purposes.[30] This preference for flexibility and an intent to renegotiate is apparent from the upsurge in the trend towards 'new terms' as a more economically efficient model than creating a 'new dispute.' Such upsurges within countries are visible in areas relating to (a) transitioning away from fossil fuels; (b) market

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[27] Lopez-Rodriguez and Navarro, "Investment Arbitration and EU Law," 8. See also Brandon Marsh, "Preventing the Inevitable: The Benefits of Contractual Risk Engineering in Light of Venezuela's Recent Oil Field Nationalization," *Stanford Journal of Law, Business and Finance* 13, no. 2 (2008): 453.

[28] V. Vedeer, "The Lena Goldfields Arbitration: The Historical Roots of the Three Ideas," *International and Comparative Law Quarterly* 47, no. 4 (1998): 755, doi: 10.1017/S0020589300062527.

[29] [29] Abdullah Al Faruque, "Renegotiation and Adaptation of Petroleum Contracts: The Quest for Equilibrium

[and] Stability," *Journal of World Investment and Trade* 9, no. 2 (2008): 122, doi:10.1163/221190008X00124.

[30] Ng'ambi, "Efficient and Flexible," 6.

disruptions created by COVID–19 on the demand and supply sides; (c) capital constraints created by wars and geographic imbalances.

One of the best examples of the utilization of renegotiation was in the Production Share Agreement (PSA) concerning Kashagan in Kazakhstan. This case pertained to the 'cost recovery' for the investors to whom a large slice of the production, called 'Cost Oil,' was allotted in order to recover their initial costs, including the infrastructure and human resources. Although this simply appeared as a textbook procedure followed in the many PSA, the allocation of percentage in Kashagan was so low that only a total of 2 percent of the oil manufactured for the first decade of production would have been received. According to the original contract, the investors was entitled to 80 percent of the 'Cost Oil' off the top, while 90 percent of the remaining production, called 'Profit Oil,' was allocated to the investors and 10 percent to the State. However, contract contained complicated trigger clauses and timelines from which the State eventually benefitted until the investors/ contractors was allocated almost 98 percent of the total production, inclusive of the cost oil and profit oil.[31] In this case, renegotiation played a significant role in changing the PSA to a more balanced position, as a subsidiary of the national oil company was allowed to double its stake, new priority shares were allotted to the Government off the top, and a new schedule and cost control mechanism was introduced to the benefit of all parties involved. This emphasizes the economic efficiency of renegotiation clauses and exemplifies a situation where the parties can use such mechanisms to reassess and negotiate from positions which would otherwise have led to termination and consequent disputes.

IV. RENEGOTIATION WITHOUT A CLAUSE

The absence of an express provision for renegotiation has resulted in two conflicting opinions on its applicability. The first group argues that there is no obligation to renegotiate in the absence of a specific agreement. The other claims that regardless of the presence

[31] George Kahale, "The Uproar Surrounding Petroleum Contract Renegotiations," Oxford Energy Forum, August 2010, available at https://www.oxfordenergy.org/ publications/issue-82-august-2010-2/.

of a renegotiation clauses, its provision is implicit in the long-term contractual arrangement and should be inferred.

A. IMPLIED DUTY

The advocates for an implied duty rely on the principle of *rebus sic stantibus* and attempt to impose an obligation to renegotiate. However, this principle has been applied in limited situations primarily to avoid misuse as well as owing to its diverging interpretations in common law and civil law jurisdictions. A shadow of this principle can be found under the Vienna Convention on Treaties[32] and was considered in the *Gabcikovo- Nagymaros Project*[33] case by the International Court of Justice. The court took a cautious approach, limiting the use of the principle to exceptional situations involving an unforeseen fundamental change of circumstances that relates to the root of the original treaty. Ultimately, the parties were left to renegotiate among themselves based on good faith.[34] Professor Sornarajah, who advocated for the same, spoke lengthily of the factors preceding an implied duty. According to the professor, various sources create substantial arguments for the existence of an implied obligation to renegotiate, including codes of conduct, such as the 'Draft Code of Conduct on Transnational Corporations,' as well as arbitral awards, principles of fairness and justice, *clausula rebus sic stantibus,* and the Algerian Declaration. [35]

However, agreeing with all the arguments proposed by Professor Sornarajah as the reason for renegotiation is difficult. This particularly concerns controversial arguments on renegotiation in disputes like *SPP vs Egypt*,[32] where alternate arrangements would have been difficult to reach due to the substance of the agreement. Regardless, implied obligations could be inferred by making regular use of the evidence about trade practices to add certainty to otherwise vague or open-ended contract terms. By becoming a common practice within the trade or

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[32] Vienna Convention on the Law of Treaties, opened for signature 23 May 1969, 1155 UNTS 331 (entered into force 27 January 1980), art. 62 (1).

[33] *Gabcikovo-Nagumaros Project, Hungary vs Slovakia*, 1997 ICJ 3.

[34] Andreas F. Lowenfeld*, International Economic Law*, Second Edition (Oxford: Oxford University Press, 2008) 564. See also McLachlan, Shore and Weiniger, *International Investment Arbitration*, 317.

[35] Sornarajah, *International Commercial Arbitration*, 433.

industry, a reasonable effort can be made at ensuring renegotiation is an implied term in an agreement, subject to the duty of good faith. This implied duty would be guided more by the unwritten rules of expediency and bargaining power than the procedural law governing contract.[36]

B. COST-BENEFIT COMMITMENT

The other school of thought, which argues against any implied obligation, identified other factors that convince the parties to renegotiate. JW Salacuse stressed that, unlike the original contract, the parties involved in an 'extra-contract' renegotiation have had their expectations shattered and are bound by a legal economic relationship, which prevents their unilateral withdrawal. Therefore, the parties will conduct a cost-benefit analysis of renegotiation and pursue a legal remedy where the net benefit inclines towards renegotiation. Moreover, the impact of such actions with respect to other existing contract and business relationships is one of the factors that determine renegotiation. This concern for a potential ripple effect stems from the idea that the parties, mostly the State, do not want such an action to provide a gateway for the other contracting parties to renegotiate their original contract.[37]

In situations where renegotiation fail and even with an implied duty, there would be no liability on the parties. This is because no national or international law has laid down any duty on the parties to reach an agreement, even with a renegotiation clauses present in contract. Providing the parties conduct the process in good faith and observe their obligations during renegotiation process, there would be no underlying consequences in the event of a failed renegotiation. This view was expressed by the PCIJ and ICJ in the *Railway Traffic between Lithuania and Poland*[38] and the *North Sea Continental Shelf*[39] case, respectively. In these case, the views of the courts underlined the absence of any obligation on the parties to agree as long as the exercise was not treated

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[36] Howard Hunter, "Commentary on 'The Renegotiation of Contracts'" *Journal of Contract Law* 13, no. 3 (1998): 206.

[37] Jeswald W. Salacuse, *The Three Laws of International Investment-National, Contractual and International Frameworks for Foreign Capital*, First Edition (Oxford: Oxford University Press 2013), 274.

[38] *Railway Traffic between Lithuania and Poland*, P.C.I J., Series A/B, No. 42, at 116.

[39] *North Sea Continental Shelf, Germany v. Denmark,* (1968) ICJ Rep.9, para. 85.

as a mere formality and the parties strived to arrive at a solution in good faith. The tribunal in the *Aminoil award* also stated that 'an obligation to negotiate is not an obligation to agree'[40].

In addition, the UNIDROIT Principles of International Commercial Contract provided for a framework within which renegotiation can occur (under Article 6) and permitted a third-party adaptation of contract in the event of 'hardships' in case where renegotiation fails.[41]

Force Majeure and *Hardship Clauses* also aim to reduce damages that affect the parties involved in a contract with changed circumstances by circumventing the strict rules of frustration in national systems, thereby allowing the parties to either adjust or terminate their contract unilaterally.[42] However, the trend in modern energy contract is to follow the former position and focus on overcoming force majeure situations for contract to continue and survive any threatening obstacles.[43] This focus on survival rather than termination makes the role of force majeure clauses particularly significant when there is no renegotiation clauses.[44] In fact, force majeure clauses are given a broad formulation that includes events discussed in hardship clauses. These wide interpretations allow renegotiation to be triggered without a clauses, even in force majeure or hardship situations.

V. STABILIZATION AND RENEGOTIATION CLAUSES: IS CO-EXISTENCE POSSIBLE?

As highlighted above, an express feature of the broadly worded modern stabilization clauses is the inclusion of 'renegotiation of contract'. However, this tilt brings back the old debate concerning the

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[40] *The Government of Kuwait v. Aminoil,* 24 ILM 976 (1982).

[41] Gotanda, "Renegotiation and Adaptation Clauses," 1469. Abimanyu Kadarisman, "Disclosure of Third-Party Funding Arrangements and The Existence of Third-Party Funders in International Investment Arbitration," Indonesian *Journal of International Law* 17, no. 1 (2019): 95.

[42] Sornarajah, *International Commercial Arbitration*, 438.

[43] Al Faruque, "Renegotiation and Adaptation," 127.

[44] Hubert Konarski, "Force Majeure and Hardship Clauses in International Contractual Practice," *International Business Law Journal* 4, no. 1 (2003): 407.

objective of each clauses. Professor Sornarajah expressed renegotiation as the antithesis of stabilization, leading to a more significant question concerning the prudence to club the ideas of stability and flexibility within one hybrid clauses.

The evolution of the stabilization clauses has expressed the theoretical possibility of the co-existence of both clauses in a contract. Case for such co-existence is made based on the difference in objective. Stabilization clauses aim to protect the sanctity of contract with the private investors by recognizing that the State's administrative and legislative function will not modify contractual terms to the investors' detriment. However, renegotiation clauses investigate the interest of the party whose position became more onerous owing to the change in the economic equilibrium of contract. This indicates that the end goal of both clauses is interest protection for all parties involved.[45]

Contrary to the anti-thesis view, scholars have advocated for the presence of stabilization clauses as leverage for renegotiation. Since stabilization clauses effectively strengthen the private parties' position in contractual bargain, the choice of a dispute over contractual renegotiation to arbitration works as an incentive for the State to compromise. Such clauses have been considered a strict yardstick in international arbitration with the corresponding counterpart of legal consequences for a breach of contract. In case of expropriation, the tribunal would scrutinize the stabilization clauses to determine the legality of the action.[46] Scholars also argue that the investors might be unwilling to conclude long-term contract without stabilization clauses. This has led advocates for the co-existence to call for a more subdued stabilization clauses that will be clubbed with the arbitration clauses[47]. This suggestion is based on the understanding that a well-worded

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[45] Klaus Peter Berger, "Renegotiation and Adaptation of International Investment Contracts: The Role of Contract Drafters and Arbitrators," *Vanderbilt Journal of Transnational Law* 36, no.4 (2003): 1347.

[46] Wolfgang Peter, Jean-Quentin de Kuyper, and Bénédict de Candolle, *Arbitration and Renegotiation of International Investment Agreements*, Second edition (Dordrecht: Martinus Nijhoff Publisher, 1995), 131.

[47] Leo J. Bouchez, "The Prospects for International Arbitration: Disputes Between States and Private Enterprises," *Journal of International Arbitration* 8, no. 1 (1991): 81, doi: 10.54648/joia1991005.

renegotiation clauses could also address stability issues. Stability can be achieved by restricting the subject matter, time, and conditions that cause renegotiation. Therefore, the idea is to have a renegotiation clauses that is similar to stabilization clauses, where the point of distinction emerges from the limitations of substantive matters and time.[48] An example is the *Ghana-Valco* renegotiation, where the stabilization clauses were subjected to renegotiation after Ghana renounced the stabilization of its laws.[49] This foreshadows the argument that there can be a two-prong approach by making renegotiation clauses broad enough to include aspects of stability or introducing a subdued stabilization clauses that increases the effectiveness of renegotiation.

Moreover, the characteristics highlighted by Bernadini in modern stabilization clauses include the idea of renegotiation. This means the modern practical approach with regards to such clauses and the earlier jurisprudence on their co-existence seems contradictory.[50] However, the ultimate aim of either approach is to treat the parties equally and enable their acceptance of the validity of these procedures. Providing success is achieved, the subdued form of one clauses under the other should not call for much criticism, though the legal implications might be significantly different when considered from their individual existences.

VI. RENEGOTIATION: ISSUES THAT NEED TO BE ADDRESSED

Renegotiation is no panacea, as certain inherent problems need addressing. Firstly, **the Good Faith Problem** – the first concern, as discussed earlier, is that much stress is put on the 'good faith' exercised by the parties an agreement after renegotiation is not reached. There is no accepted universal definition of 'good faith,' which creates further problems in ascertaining the obligations of the parties during renegotiation.

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[48] Peter, De Kuyper, and de Candolle, *Arbitration and Renegotiation*, 220.
[49] *Ibid*
[50] Bouchez, "The Prospects for International Arbitration," 82.

Secondly, **assessment of imbalance and limit of renegotiation** – there may be issues with restoring contract to the original equilibrium when unclear clauses result in open-ended ambits. The criteria for assessing imbalance and the extent of renegotiation of the terms should be clarified in the clause, as there may be debates in certain situations. An example is case requiring compensation, where the need for full payment or the consideration of public policy factors underlying the State Contract while deciding the amount of compensation may be deliberated.[51][52]

Thirdly, **failed renegotiation** – the third potential problem surrounding renegotiation is focused on situations where the process fails. Although jurists have argued with evidence about the existence of a duty to renegotiate, international and national laws do not explicitly identify any duty for the parties to reach any agreement. There is a lack of clarity regarding the existence of a 'dispute' between the parties supposing an agreement was not attained. An important distinction is necessary because, in the absence of an existing dispute, an arbitral tribunal would have no jurisdiction or may even be accused of exceeding its authority. This issue rolls back to the idea there is no breach of contract during renegotiation and no real dispute since the parties are not obliged to reach an agreement.[52] This is critical because the uncertainty over the tribunal's jurisdiction may also create problems during the enforcement stages.

Fourthly, **trigger event** – this fourth concern arises from the practical viability of the events that trigger renegotiation. Having renegotiation clauses in place of stabilization allows the host State to take certain measures, even though a change in circumstances may occur.[53] The subsequent question that arises concerns the presence of a threshold on limits to the aspect of 'change of circumstances' and the inclusion of the actions directly within the control of the host State under trigger events when not necessarily connected to 'reasonable' public policy. Although the likes of Salacuse[54] limited the definition of change

[51] [52] *Ibid*

[52] Gotanda, "Renegotiation and Adaptation Clauses," 1469.

[53] Berger, "Renegotiation and Adaptation," 1348.

[54] Salacuse, *The Three Laws of International Investment-National*, 387.

in circumstances to events outside the control of the parties, several scholars[5556] have pushed to include the actions within the control of the State. Although the investors would have the opportunity to restructure and may not encounter problems, this approach may lead to excessive renegotiation, particularly in deciding the changes that are 'necessary' and 'reasonable.'

The fifth is a more generic concern, **uncertainty and instability**, where renegotiation are criticized for bringing uncertainty and instability to contract, and characteristics exceed the requirements of investment necessities. The coexistence of stabilization and renegotiation clauses may create an unfavourable situation for the State. Although stabilization clauses might effectively push the State for renegotiation, the structuring of the investment by the investors could increase the returns to offset the risk created by the environment at the behest of the State.[56]

Sixth, **cluttered idea of consent'** – there have been concerns with forced renegotiation in certain circumstances. According to jurists, such as Muchlinski, coercive actions used by the host State put the investors under duress and amount to expropriation. However, the absence of 'absolute rule' to guide the tribunals complicates the process of determining that the consent was voluntary.[57] Muchlinski also indicated that the limitations may justify expropriation by the State in case other than threats of physical injury or property.[58] The impact of these limitations on renegotiation have been highlighted in case like *Aminoil*[59], where the argument for duress was not accepted by the tribunal and *Desert Line*[60], and critics argued against the probability of

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[55] [56] Peter, De Kuyper, and de Candolle, *Arbitration and Renegotiation*, 219.

[56] Salacuse, *The Three Laws of International Investment-National*, 387.

[57] Jean Ho, *State Responsibility for Breaches of Investment Contracts*, First Edition (Cambridge: Cambridge University Press, 2018), 168. See also Peter T. Muchlinski, *Multinational Enterprises and the Law*, Third Edition (Oxford: Oxford University Press, 2021), 500-501.

[58] Muchlinski, *Multinational Enterprises and the Law*. See also Detlev F. Vagts, "Coercion and Foreign Investment Rearrangements," *American journal of International Law* 72, no. 1 (1987): 24, doi:10.2307/219970.

[59] *The Government of Kuwait v. Aminoil*, 24 ILM 976 (1982).

[60] *Desert Line Projects LLC v. The Republic of Yemen*, ICSID Case No. ARB/05/17.

claimants' success, supposing their argument had been based solely on expropriation claims.[61]

VII. CONCLUSION

The principle of *pact sunt servanda* is the widely accepted norm, though the change of circumstances in exceptional case may necessitate contract to be adapted accordingly by the parties. In such situations involving changes to contract, narrowly worded stabilization clauses have been found to be inefficient because of their dependence on the law applicable to contract. Therefore, a renegotiation clauses can act as a solution in these situations by bringing flexibility and stability to contract. Renegotiation helps the State obtain an equal opportunity to receive a fair deal while pursuing their legitimate interest by recognizing that their actions are not restricted to wealth maximization. For the investors, renegotiation reduce the risk of unilateral termination of contract and offer both parties an opportunity to re-assess terms to avoid confrontation. The evolution of the language of Stabilization clauses highlights the significance of renegotiation. A tilt towards renegotiation clauses has been observed, restricting the use of stabilization clauses as leverage for renegotiation. Although the possibility of renegotiation being invoked by the State is more likely, they may also be useful to the investors in many circumstances. This increasing acceptability necessitates the inclusion of a renegotiation clauses in contract with clarity on four accounts, all of which were recognised in this paper as potential grey areas. The argument was based on the mechanism of incorporating special consideration in determining the triggering point of such clauses and clearly defining the procedure to be followed as well as the maximum threshold to which contract can be changed during renegotiation. The scope of the clauses and the procedure the parties must follow in case of unsuccessful renegotiation should also be defined to further increase the acceptability of these clauses. However, many of these issues are significantly related to the interpretation of such clauses in international and national laws through their forums. This necessitates

[61] Salacuse, *The Three Laws of International Investment-National*, 389.

legal literature and jurisprudence to develop and fill the grey areas with clarity and certainty.

The importance of contract-based protection clauses is not lost on any of the parties involved. The need for time demands that the stabilization clauses must converse with the idea of renegotiation to provide flexibility to reassess potential areas of sensitivity. This is not the first time that the energy sector faces sweeping changes. However, the recent recognition of nations concerning the reduction of CO_2 emission, the benefits of greener alternatives, and impending geopolitical changes through wars, global health, or economic crisis will transform policies, which will directly or indirectly affect the Energy sector. Regardless of the other alternatives available, flexible stabilization or renegotiation clauses have adapted much better, particularly in the Energy sector, than the expectations of critics, and are likely to remain a significant option for parties to protect their commercial needs.

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