

GUIDE TO LAND CONTRACTS:

FORESTRY PROJECTS



**Columbia Center
on Sustainable Investment**

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ISLP: The International Senior Lawyers Project is a non-profit organization that seeks to foster just and accountable development that is sustainable and supportive of human rights, and that strengthens the rule of law. It strategically mobilizes its unique network of highly skilled and experienced pro bono lawyers to assist, train, and empower civil society and governments around the world in ways that better enable the benefits from development and investment to be shared equitably with legitimate developing country governments and their people.

CCSI: The Columbia Center on Sustainable Investment (CCSI), a joint center of Columbia Law School and the Earth Institute at Columbia University, is the only university-based applied research center and forum dedicated to the study, practice and discussion of sustainable international investment. CCSI's mission is to develop practical approaches for governments, investors, communities and other stakeholders to maximize the benefits of international investment for sustainable development.

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HOW TO USE THIS GUIDE

This Guide was developed to assist non-lawyers in better understanding investment contracts that concern forestry projects, such as those available on OpenLandContracts.org. These “forestry contracts” can be complex, and some provisions may be difficult to understand. This Guide aims to assist the reader in understanding provisions typically found in such contracts. This is not a guide to negotiating contracts, and does not provide model provisions. Rather, this Guide provides explanations for common provisions, as well as a Glossary of certain legal and technical terms used herein. Terms that are included in the Glossary are italicized and bolded the first time they appear in the Guide.

1. INTRODUCTION

1.1 Overview

Forestry is the cultivation, management, and conservation of forested land and the utilization of its resources, including *timber* and other *forest products*, to meet human needs. Large-scale commercial forestry, which occurs throughout the world, involves the intensive harvesting and production of timber, wood, fuel, and/or other forest products from natural or plantation forests for sale in domestic or foreign markets.

Large-scale investments in commercial forestry can generate benefits for *host states*, such as additional revenues or increased employment opportunities for local populations and other citizens. However, if not properly managed, such investments can have significant environmental impacts, including on water quality, soil quality, and biodiversity. Forestry investments can also cause widespread deforestation, imperiling the habitats of animals and plants that live in the forest and contributing to climate change. In addition, such investments can have negative social impacts, including for communities located on and around affected lands. This risk is heightened in states with weak governance¹ or with ambiguous or transitioning land tenure systems.

Governments that host large-scale forestry investments are tasked with balancing their resource development goals and the global demand for forest products with the country’s sustainable development objectives and other important public policy considerations. Such considerations may include allocation of domestic resources, rural development, food security, water management, sustaining the land’s ability to provide *ecosystem services*, and safeguarding the rights of workers as well as local individuals and communities. In some countries, domestic *legal frameworks*—including the constitution, laws, and regulations—may strive to govern the terms of investments in a manner that balances these concerns, while in other countries, legal frameworks may fail to address critical issues such as allocation of risk, social benefit, and/or environmental protection. In either case, an investor’s rights and obligations regarding the use, management, restoration, and preservation of forests may be further elaborated in a forestry contract between the investor and the host government. These contracts delineate the conditions upon which the government authorizes the investor to use land within its *jurisdiction* for purposes of forest management and utilization. These conditions usually include (1) payments by the investor to the government for use of the land and other needed resources, and (2) commitments regarding the investor’s management of the land, its operations, and—in some cases—its interactions with workers and affected communities.

¹ The Organisation for Economic Co-operation and Development (OECD) has labeled as “weak governance zones” those areas that it defines as “investment environments in which governments cannot or will not assume their roles in protecting rights (including property rights), providing basic public services (for example, social programmes, infrastructure development, law enforcement and prudential surveillance) and ensuring that public sector management is efficient and effective.” OECD, “OECD risk awareness tool for multinational enterprises in weak governance zones” (Jun 8, 2006), p. 10, available at: <https://www.oecd.org/daf/inv/corporateresponsibility/36885821.pdf> (last visited Jan 18, 2017).

1.2 Forestry contracts, in brief

Forestry contracts come in many varieties, cover a range of issues, and vary depending on the country context, the investor's objectives, and other factors. This Guide primarily focuses on forest utilization contracts governing large-scale forestry investments and operations in low-income countries. Through these contracts—which may, for example, be structured as timber sale contracts, *concessions*, or land leases—governments typically grant investors rights to extract and utilize *forest resources*. These rights include *tenure rights*, or rights to access, possess and/or control the land, and may also include exploration rights, which allow investors to explore forest potential, and timber harvesting rights, which allow investors to cut and remove timber. For ease of reference, this Guide refers to these contracts as “forestry contracts.”

In addition to the rights described above, forestry contracts typically provide the investor with a range of rights that facilitate its forestry operations. These may include the right to import the equipment and skilled labor needed to fell, cut, and load *logs*; to use existing *infrastructure* on and around the land to carry out the project (for example, irrigation or water supply systems); and to construct any roads—or *rights of way* through adjoining lands—that the investor may require to transport timber to ports or processing centers.

In return for these and other rights, the investor will be required to make payments to the government, which may include license fees, stumpage fees, export taxes, rents, and other fees. Some of these payments will be required under domestic law (for example, taxes). Forestry contracts may also include exemptions to taxes or other payments required by law, depending on what is negotiated between the investor and the government. In addition to payments, the investor will commit to obligations that will define the parameters of its activities. For instance, governments often require investors to manage forests in accordance with specifications mandated by the contract and domestic law, which may be driven by the government's overarching resource development goals. In addition, investors may be bound by certain affirmative obligations, such as obligations to maintain books and records, to source needed products domestically, or to provide certain social benefits to local communities, and by certain negative obligations, such as a prohibition on engaging in any transactions restricted by law.

1.3 The impact of contract negotiation and drafting on forestry investments

Ideally, a country's domestic laws will regulate forestry investments to ensure that various stakeholders realize meaningful benefits, that serious negative environmental and social impacts are avoided, and that those who bear the brunt of an investment's negative impacts are adequately compensated. In practice, however, some governments use forestry contracts, rather than domestic law, to regulate key aspects of such investments. Forestry contracts do not always effectively balance the interests of all affected stakeholders. Governments, for example, often face political pressures and—particularly in low-income states and emerging economies—may be at a disadvantage during contract negotiations because of a lack of access to the high-level legal expertise available to multinational investors. At the same time, investors may lack a nuanced understanding of the domestic political context, local land governance systems, and community dynamics particular to the area, all of which can make it difficult for the parties to negotiate viable deals that are adequately tailored to local conditions. Governments and investors may also limit, or vaguely define, obligations in the contract so as to expedite negotiations or to minimize potentially complex and expensive requirements that may delay operations.

When contract negotiations are imbalanced, or where key matters are not adequately addressed in the contract or by law, problems and disagreements between the parties—or with third party stakeholders, such as affected communities—may arise. These disagreements can lead to interruptions to the investment; for instance, the community may decide to protest the investment and block access to the project site, or the government may withdraw permission for the investor to carry out the investment, whether on a temporary or permanent basis, because of community grievances. Examples of potential problems that can arise from poorly negotiated contracts include:

- The inability of the government and/or affected communities to collect a fair return on the value of the land and the timber and other forest products harvested. This may occur, for example, when contracts permit inaccurate appraisal of the land or the timber market, or provide for broad tax exemptions. The ability of the government and/or host communities to obtain benefits from the investment may be especially undermined where weak governance systems and limited resources restrict the collection of project-related payments and revenue, or where they facilitate bribery and corruption.
- Conflict over indigenous or other affected communities' rights to the land and resources covered by the contract. For instance, when community rights are not clearly recognized by domestic law or addressed in the contract, or when the parameters of the *contract area* are not clear, there may be disagreement as to the nature of the rights and entitlements of the various stakeholders.
- Tension and conflict between investors and communities if the contract does not ensure that economic or social benefits flow to the local level. In countries where government decisions regarding investment are not made transparently or are influenced by corruption, tensions may be exacerbated if communities suspect that deals were negotiated unfairly, unlawfully, and/or to enrich political or business elites at the expense of local populations.
- The parties' non-compliance with the contract, which may be facilitated by inadequate monitoring or enforcement, or by poor drafting of the contract itself. Contract violations may lead to a range of negative outcomes, such as degradation of the soil quality, irreversible environmental damage, loss of biodiversity, deforestation, adverse impacts on the land rights and human rights of local individuals and communities, loss of revenues, and loss or degradation of the traditional lands of local and indigenous communities.

Given these and other challenges, when forestry contracts are used, balanced negotiations and careful drafting are critical.² This is particularly important where domestic law does not comprehensively address the wide range of potential benefits and impacts that forestry investment can produce.

2 KEY PROVISIONS IN FORESTRY CONTRACTS

When reviewing any contract, it is essential to carefully consider the rights granted, and the obligations imposed, by the contract's provisions. It is also important to consider what provisions may have been omitted or only described generally, and the possible consequences of that omission or brevity.³ For instance, a contract that defines the contract area only in terms of size (such as a specified number of hectares of forestland) and approximate location, and not with precise geographic coordinates, may result in confusion and conflict over the exact boundaries of the land that the Investor can use for its forestry operations.

It is also useful to keep in mind the interplay between the contract and the other legal frameworks that govern the investment. In addition to the terms described in the contract, forestry investments are generally subject to domestic law—that is, the constitutional norms, laws, and regulations of the host state. Host states often also have international legal obligations that might affect the governance of

² This Guide provides guidance on understanding forestry contracts negotiated between governments and investors, but does not necessarily endorse the use of such contracts over other alternatives, such as licensing and permitting under domestic regulations. It also does not consider other ways of structuring forestry contracts, for example, tripartite agreements that include third parties, such as affected community members.

³ According to the Food and Agriculture Organization (FAO) of the United Nations (UN), forestry contracts should address six key areas to be comprehensive: (i) the project's technical requirements, including the investor's operational methods and required inputs and outputs; (ii) the investor's obligations to respect the rights of, and provide benefits to, communities in or near the contract area; (iii) control mechanisms for the investor's operations, including procedures permitting the government to monitor compliance with the contract's terms; (iv) legal provisions governing the contract, including clauses dealing with boundaries of the contract area, grants of land tenure rights, dispute resolution, changes in laws, and termination of the contract; (v) risk and financial requirements, which set out the deposit requirements and financial obligations of the parties; and (vi) an interpretation clause, which defines terms used and identifies applicable law governing the contract. FAO et al., "Governance Principles for Concessions and Contracts in Public Forests" (Dec 30, 2003), p. 56-57, available at: <http://www.fao.org/docrep/019/y1398e/y1398e.pdf> (last visited Jan 18, 2017).

forestry investments or provide additional protections to an investor. Given this interplay, where there appears to be a conflict in legal obligations—such as between a contract’s provisions and domestic law—it may be useful to consult with a lawyer to determine which obligations prevail.

The following subsections describe provisions commonly found, and issues commonly addressed, in forestry contracts. These subsections are organized in the general order that certain provisions often appear in contracts; however, the structure and content of contracts vary greatly, and certain types of issues, such as operational or environmental requirements, may arise across a range of provisions throughout a contract. Accordingly, to understand the full scope of any particular contract, it is important to read the contract in its entirety.

2.1 Definitions

A forestry contract may include a definitions section, which typically appears at either the beginning or the end of the document. This section sets out the key terms that will be used throughout the contract and explains what those terms mean. Key terms are often capitalized throughout a contract to signify that the capitalized word is a defined term. Defined terms help the parties achieve uniformity and clarity of meaning throughout the rest of the contract.

2.2 Parties

The *parties* to a contract are the *legal persons* who sign (or *execute*) the contract. By signing the contract, each party agrees to assume certain rights and obligations as described under the contract. In forestry contracts, one party to the contract typically will be the host state (often represented by a government minister or senior civil/public servant) and the other party typically will be the corporation or individual that plans to carry out the forestry investment by planting and/or managing forests, and harvesting timber or other forest products.

This Guide refers to the government party as the ‘Government’ and the corporate (or individual) party as the ‘Investor.’ However, depending on the type of forestry contract, the Government may be referred to as ‘Lessor,’ ‘Authority,’ ‘Grantor,’ or another term in the contract; correspondingly, the Investor may be referred to as the ‘Lessee,’ ‘Holder,’ ‘Licensee,’ ‘Contractor,’ ‘Concessionaire,’ ‘Grantee,’ or another term. Although the titles assigned to the parties in a particular contract may suggest that the contract conveys certain types of rights and obligations (for example, leasehold rights from a Lessor to a Lessee), ultimately rights and obligations are created by the contract’s provisions, and not by the titles used to refer to each party; those titles simply provide a means to refer to the parties in a consistent manner throughout the contract. *See* Section 2.1, *Definitions*.

In some situations, the Investor may enter into the contract, or may conduct the project’s operations, through a *subsidiary* or an *affiliate*. For example, if the law of a particular jurisdiction only permits the host state to lease land to domestic companies, a multinational corporation that wishes to make a forestry investment in that jurisdiction may need to establish a local subsidiary to be the contracting party. A multinational corporation may also decide to make the investment through a local subsidiary due to a range of business considerations, including tax benefits or *liability* concerns. Alternatively, a multinational corporation might enter into the contract itself, while establishing a local subsidiary to operate the project.

Third parties (including affected communities, non-governmental organizations, creditors, and guarantors) may also be involved in negotiations around a forestry investment. Whether or not such legal persons have any *enforceable legal rights* under the related contracts will depend on the specific terms of the contract and the rules applying to contractual rights in the relevant jurisdiction. For example, if the contract has a “*third party beneficiary*” clause that identifies certain third parties as contract beneficiaries (such as persons having an interest in protecting the environment in an area impacted by the contract), those persons may have the ability to sue to enforce the contract’s relevant provisions (such as provisions establishing environmental obligations) against the parties to the contract. Alternatively, a contract may include a “no third party beneficiary” clause that explicitly precludes non-parties from enforcing any provisions of the contract.

2.3 Contract term

The *term*, or duration, of a forestry contract is the amount of time that the contract will be operative. The length of the term may depend on the particular circumstances applicable to the forestry operation, the outcomes sought, and economic considerations. For instance, in some forestry contracts, the Investor is responsible for ensuring that the forest will grow back after exploitation (*regeneration*). Accordingly, the parties may negotiate a term that will provide the Investor sufficient time to generate post-harvest revenues and to apply a portion of those revenues toward regeneration.

The initial term of an agricultural investment contract will typically begin on the contract's *effective date*, which may be the date the contract is signed by all parties (the *signature date*) or the date that the parties meet certain negotiated conditions (the *conditions precedent*). The term will then run for the length of time specified in the agreement, and may end on a specified *termination date*, unless one or more parties to the contract terminate the agreement before the end of the term or before the termination date as permitted by the contract (see Section 2.24, *Termination*). Forestry contracts may also include provisions permitting a renewal or extension of the term—for instance, if the Investor meets certain performance targets; if the parties mutually agree to an extension; or if a *force majeure* event (see Section 2.22, *Force majeure*) occurs and delays operations.

2.4 Contract area

The contract area is the land identified in a forestry contract where the Investor can conduct its operations.⁴ A contract may describe the contract area by specifying the county in which it is located, the amount of hectares it contains, and/or its precise boundaries, which can be described using geographic coordinates or by reference to clear landmarks such as roads and rivers; the contract may also supplement this information with a map that demarcates the area's boundaries. Domestic law may further require that the precise coordinates of the contract area be recorded and made publicly available. Even where not required by law, the parties to the contract may choose to make precise coordinates publicly available to avoid any disputes that may arise due to vague understandings of the contract area's boundaries. The parties may also supplement these coordinates with a map, or a description that is more easily understood by local populations and other stakeholders—for example, a description that describes the contract area by reference to geographic markers, such as trees or rivers.

A forestry contract may also designate certain areas that are to be excluded from the contract area. These may include cultural heritage sites, mountains, reservoirs, land legally owned by residents, or protected areas. Alternatively, a contract may stipulate that a parcel of land is to be surveyed by a certain date to determine if any areas should be excluded from the contract area, such as areas where

For contracts with a term of ten years or more, the FAO recommends including contract provisions that deal with long-term planning and sustainable development and management of forest resources. These could include:

- a long-term *forest management plan* and a long-term timber supply plan (which will ideally cover operations, forest management, and forest renewal for the contract area);
- provisions allowing for flexibility, such as:
 - amendment of the contract due to changed circumstances since the time of signing;
 - modification of the contract to bring it into line with updated resource and environmental standards;
 - modification of the contract area; and
 - variation of the methods by which stumpage fees, area fees, and other *levies* are determined; and
- clauses dealing with forest regeneration, which ideally will be subject to a forest management and environmental management review.

Contracts with shorter terms may be simpler, relying on general requirements for development and management of forest resources under existing domestic law.

See FAO et al., 2003, op. cit., p. 67.

⁴ In some contracts, this may be equivalent to—and referred to as—the “concession area,” the “location,” or under similar terms.

local communities reside. In such cases, the contract may require a legal description of the contract area (with such areas excluded) to be annexed to the contract once the survey is completed.

If the boundaries of the contract area are described in an appendix to the contract or in an additional document—whether on the execution date or at a later time—the contract may indicate where that information may be found (for instance, in the host state’s land registry).

2.5 Rights granted and obligations imposed

A forestry contract will include provisions describing the rights to the forestland and resources that the Government is granting to the Investor. These will include rights that are central to the operation of the contract, such as the tenure rights granted to the Investor in respect of the contract area and the Investor’s rights to undertake the forestry operation. The contract will also typically include rights that are necessary for, but not central to, the operation of the forestry project, such as *easements* (or *rights of way*) across public and/or private lands outside of the contract area to allow transportation to and from the area, and rights to: construct, maintain, and repair the infrastructure necessary for the forestry operation (for example, roads, telephone poles, and security gates);⁵ import supplies and equipment; market, transport, and export forestry products; use specified resources (for example, water, clay, and stones) found in or near the contract area during the forestry operation; and access and use utilities under specified conditions and rates. Details of the timber and other forest products that may be harvested (including their species, size, and location) may also be described in these provisions.

In some cases, persons other than the parties to the forestry contract (for example, indigenous or other local communities, or other Investors with licenses for resource exploration) have pre-existing rights over the contract area. Those rights may be acknowledged or reserved in these provisions. For example, the contract may specify that persons inhabiting the contract area have the right to remain there, or it may grant them the right to continue accessing forest resources that are necessary to maintain their cultures and livelihoods throughout the contract’s term. The contract may also specify under which circumstances the Investor may access land held by individuals or communities within or outside of the contract area—for instance, it may only permit access to such land if a prior mutual agreement is reached between the Investor and the landholders. For a more detailed discussion regarding such agreements, *see* Section 2.14.2, *Access to traditional and livelihood-generating resources; resettlement*.

A “reservations,” “rights withheld,” or similar provision may also specify further restrictions on the Investor’s rights. For example, a reservations provision may prohibit the clearing or harvesting of a particular species or quality of timber, or restrict an Investor’s access to environmentally sensitive or protected areas of forest. The Government may also reserve the right to access, or allow others to access, the contract area for a variety of purposes, including harvesting resources from the contract area, implementing reforestation programs, or building infrastructure. Additionally, the Government may retain the exclusive right to conduct exploration and extract certain non-renewable resources (for example, metals, minerals, oil, or natural gas) located beneath the contract area’s surface, may

The types of land tenure rights granted to the investor are important and can influence the obligations that the investor may be willing to accept. For example, an International Finance Corporation (IFC) report published in 2000 reviewed the implementation of the IFC’s 1991 Forest Strategy and noted that where a forest utilization contract was not fixed to a specified area—for instance, where the investor lacked ownership or contractual control over a clearly delineated part of the forest—the investor generally would not accept responsibility for sustainable management of the forest. In such cases, an investor may also be reluctant to agree to other social and environmental obligations that might otherwise be addressed in a forestry contract.

See International Finance Corporation (IFC), “OEG Review – Implementation of the 1991 Forest Strategy in IFC’s Projects, Operational Evaluation Group” (2000), p. 2, available at: <http://www.ifc.org/wps/wcm/connect/d335ce804a990beebdaff9e0dc67fc6/Forestry.pdf?MOD=AJPERES> (last visited Jan 18, 2017).

⁵ An Investor’s rights and obligations regarding needed infrastructure are further discussed in Section 2.8, *Infrastructure*.

delegate these rights to the Investor, or may retain the right to grant access to third parties for exploration and extraction of such resources.

In addition to conveying rights to access and exploit land and resources (and setting forth limitations on those rights), forestry contracts typically include provisions imposing obligations on the Investor. For instance, a contract may require the Investor to deposit a performance bond with the relevant governmental authority (as further discussed in Section 2.7, *Performance bond*); to avoid unnecessary damage to certain categories of trees; and to implement erosion prevention and control measures in its operations. In addition, the contract may specify who will bear the burden of certain risks that the Investor may face, such as forest fires, storm damage, insects, disease, trespass, poaching, and illegal logging. For example, the contract might note that the government is responsible for fire-fighting efforts, while the Investor is responsible for organizing regular forest patrols.

2.6 Conduct of operations

Forestry contracts often set forth requirements regarding the Investor's conduct of operations, which may address a range of issues, such as: required timber clearing, *felling*, and utilization standards; maintenance of the contract area; planting and replanting requirements; other permitted activities within the concession area; anticipated use of public or private land outside the contract area; appointment of an operator; guidelines for transactions with affiliates; requirements for product sale to local populations; sale prices; and purchasing rights of the Government and/or Investor. Furthermore, a contract may tie those requirements to a supplementary operational plan, or to generally accepted industry standards or standards promulgated by certification schemes, such as the Principles and Criteria established by the Forest Stewardship Council.⁶

These provisions may also require the Investor to meet particular requirements or obtain government approval before the Investor commences with felling trees, processing or transporting trees, harvesting timber, or other ground-disturbing activities. These may include submission of a forest management plan, an annual operational plan, any initial social agreements,⁷ a business plan,⁸ and/or a performance bond. In such situations, the Government might wait to issue the *harvesting certificate* that would allow the investor to commence harvesting until the required documents have been received and approved.

An annual operational plan generally describes activities to be performed in the upcoming year, including logging activities, production, infrastructure construction and maintenance, and requests for use of land exempt from the Investor's use or outside of the contract area. The annual operational plan may also provide a review of the previous year's activities, and may analyze future potential yields of forestry products. The annual operational plan may be included as part of a forest management plan, which addresses longer-term management of the forest and its resources during the contract's term.⁹ For a more detailed discussion of forest management plans, see Section 2.13.1, *Environmental impact assessments and forest management plans*.

2.7 Performance bond

Often, a forestry contract will require that the Investor provide a performance bond or other security deposit to the Government to secure the Investor's performance of its obligations under the contract. If the Investor fails to make a required payment or otherwise meet its contractual obligations, the

⁶ Forest Stewardship Council (FSC), "FSC Principles and Criteria for Forest Stewardship," Version 5 (2015), available at: <https://ic.fsc.org/preview.fsc-principles-and-criteria-for-forest-stewardship-fsc-std-01-001-v5-2-enwebversion-a-4844.pdf> (last visited Jan 18, 2017).

⁷ These are initial agreements executed between the Investor and local communities and/or other stakeholders around social issues. This requirement may also arise in a section dedicated to Investor obligations. For a more detailed discussion regarding such agreements, see Section 2.14.5, *Corporate social responsibility, local development agreements, and community benefit agreements*.

⁸ A business plan will typically demonstrate to the Government that the Investor has technical and financial capacity to manage the contract area sustainably. In cases where the Investor deviates from this business plan, the Investor may be required to report these deviations with justification to the Government.

⁹ FAO, Hans Vellema and Jelle Maas, "A Conceptual Framework for Forest Management Plans" (0579-B4), available at: http://www.fao.org/docrep/ARTICLE/WFC/XII/0579-B4.HTM - P15_83 (last visited Jan 18, 2017).

Government may have the right to deduct an amount equivalent to the missed payment or the amount the government has to expend to address the Investor's failure to perform, such as the cost of required environmental cleanup in circumstances where the Investor fails to meet required pollution controls.¹⁰ Determining the appropriate amount of security that an Investor must provide to the Government therefore requires careful consideration. The financial standing of the Investor, and the risk that the Investor may not be around to complete financially burdensome obligations, such as regeneration, may also be taken into account.

2.8 Infrastructure

Access to ancillary infrastructure can be critical to the viability of any forestry investment. For instance, most forestry investments cannot survive without access to roads, rails, or ports (particularly for export of round logs or timber). Forestry contracts may therefore include provisions that require the Government to provide the Investor with access to infrastructure that is necessary to the Investor's forestry operations. Alternatively, the contract may require the Investor to build needed infrastructure, such as roads for transporting timber, or it may require the Investor to use, and pay for its use of, existing local infrastructure in its operations.

Infrastructure provisions often also address the Investor's rights to construct and install infrastructure, as well as its corresponding obligations to maintain and repair such infrastructure. The contract may require that all infrastructure constructed or installed in relation to the contract comply with domestic *legislation* and avoid any unreasonable risks to the environment or health, safety, and welfare of the public. These provisions may articulate, or note existing, permitting and licensing requirements associated with proposed infrastructure projects, which often mandate prior Government approval over the design, location, size, and potential environmental impacts of proposed infrastructure, and which may establish financing requirements for such projects. Specified approval requirements may apply to infrastructure activities affecting surrounding areas. The contract may also require the Investor to incorporate proposed infrastructure activities in its operational plan, and it may stipulate that the Government not unreasonably deny or delay approval of these activities. In addition, the contract may include ancillary rights for the Investor to exploit secondary resources located in the contract area for the construction of infrastructure.

Additionally, the Government may retain the right to construct or access infrastructure within the contract area under specific circumstances, provided that this does not interfere with the Investor's operations. The contract may also include conditions under which the Government can authorize third party use of infrastructure, or require the Investor to make infrastructure available to local populations during the term of the contract, subject to reasonable and lawful restrictions imposed by the Investor. Finally, infrastructure provisions may establish which party owns the infrastructure, both during the term of the contract and following expiration of the contract. Infrastructure that is built to accommodate a specific forestry project may need to be removed and rehabilitated after contract completion; alternatively, the contract may require that ownership of certain infrastructure, such as roads and power lines, revert to the Government upon expiration of the contract.

2.9 Security

Forestry contracts may include provisions that address security to protect the Investor's forestry operations. If so, the provisions may allow the Investor to hire private security forces, or, alternatively, may require the government to provide adequate security to protect the Investor's contractual right to use the contract area. Additionally, they may define the parameters of security activities and use of force. For instance, they may prohibit private security forces from carrying firearms or other life-threatening weapons, and they may describe the circumstances under which private security forces can apprehend, detain, evict and/or use force against persons in the contract area. The contract may also set out certain measures the Government or Investor must take to prevent

¹⁰ FAO, 2003, op. cit., p. 77–87.

third parties from entering the contract area or to avoid injury to third parties (such as indigenous communities) who have continuing rights to access the contract area.

Security provisions may also set forth training and vetting requirements for private security personnel; Investor reporting requirements and the Government's monitoring rights vis-à-vis the use of such personnel; and requirements for security coordination with local and/or national law enforcement. Finally, contracts may include an affirmative obligation for the parties to adhere to international standards concerning the use of security firms, such as the Voluntary Principles on Security and Human Rights,¹¹ which have been developed by governments, private sector companies, and civil society groups to help companies ensure the safety and security of their operations while maintaining respect for human rights.

2.10 Representations and undertakings

Forestry contracts may include a section (or sections) dedicated to representations, which are statements of fact made by one party on a specific date (often the effective date) to convince the other party to enter into the agreement. In contracts without such a section, representations may still be included elsewhere in the contract. If it is later established that the representation was not true on the date it was made, then the party who made the representation will be in ***breach of contract***, meaning that it has not fulfilled its side of the agreement. If the other party suffers harms as a result of the false representation, it may be able to sue for money ***damages***.¹²

Representations that might be provided in a forestry contract include:

- that the land in the contract area is free of any encumbrances (meaning that there are no competing claims to all or any part of the contract area that would obstruct or prevent the Investor from exercising its rights to the contract area);¹³
- that the Investor is a corporation validly established under the governing laws of the jurisdiction in which it is formed;
- that the Investor has the necessary corporate power and authority to conduct its business and fulfill its obligations under the contract;
- that neither the Government nor the Investor has any litigation or court proceedings pending against it that could significantly affect rights or obligations under the contract;
- that the Investor has the necessary technical capabilities and financial resources to perform its obligations under the contract; and
- that the Investor has no obligations under other contracts, laws and regulations, or court rulings that might conflict with its obligations under the contract.

¹¹ See The Voluntary Principles on Security & Human Rights, "What Are the Voluntary Principles?", available at: <http://www.voluntaryprinciples.org/what-are-the-voluntary-principles/> (last visited Jan 18, 2017). The Voluntary Principles on Security & Human Rights were developed in response to issues in the extractives industry. However, they have since been referred to in various investment contracts governing agricultural investments, and may also be referred to in future forestry contracts.

¹² In the context of forestry contracts, the party granting the interest in the land may not wish to make any representations, and will prefer to grant the interest in the land on an "as is" basis. Conversely, the party obtaining the interest in land will want to have as many reassurances as possible—by way of representations from the other party—so that they are aware of all relevant risks regarding the land. In such cases, one party may pay for land rights only to subsequently learn that the other party did not have the authority to grant such rights (particularly in countries with non-transparent land regimes). To avoid this concern in a forestry contract, an Investor may require the Government to be transparent in its representations about all prior and co-existing claims to the land and resources that are the subject of the contract. Parties may conduct due diligence to confirm that the other party's representations are true prior to executing the contract. For instance, an Investor may consult with local communities to ensure congruity with the State's characterization of land ownership. Doing so may help the Investor avoid future conflicts with local communities or others who have the rights to the land and resources, and, in turn, better safeguard its investment.

¹³ Local communities may disagree with the Government's characterization of the land as free from any claims or encumbrances. This may result in conflict between the communities and the Investor and/or Government, which may impede progress on the forestry project. The importance of community consultation and consent are explored further in Section 2.14.1, *Consultation and "free, prior and informed consent" (FPIC)*.

In addition to representations, this section may include “undertakings” (sometimes called “covenants”)¹⁴ from each party, which are promises one party makes to another about activities that the party will undertake or avoid during the term of the contract. These can be distinguished from representations in that, while representations are statements of fact made as of a specific date (for instance, the execution date), undertakings are forward-looking and relate to future performance, typically during the term of the contract. Standard undertakings may include:

- that (subject to other provisions of the agreement) the Government will not exploit or permit another person to exploit the contract area for commercial purposes;
- that the Government will not grant licenses to any third parties to operate competing businesses within a certain distance of the contract area;
- that the Investor will conduct all of its operations in compliance with all applicable laws and prudent business practice, and
- that the Investor will not knowingly make a false statement or material misrepresentation to the Government regarding any matter relating to the contract.

2.11 Forest levies, taxes, and other payments

The amounts the Investor is required to pay to the Government in exchange for the rights granted and resources exploited under a forestry contract are called “forest levies” (*see text, right*). These may include (or may be referred to as) royalties, stumpage, rent or surface fees/land rental fees, taxes, or other fees. In some cases, the Government may grant the Investor exemptions from these payments; such exemptions may be built into law or established by contract.

Levies are normally charged based on the volume of timber harvested, per area of forest, or a combination of both.

Types of volume-based levies include:

- Stumpage fees: these fees are charged on either a volume or per tree basis. Volume-based stumpage is usually used because timber value can vary based on multiple characteristics (for example, species, quality, and location). Per tree stumpage is rarely used because it does not always reflect the true value of the timber; it might be used, however, where there are difficulties with log measurement or where simplicity of administration is required.
- Forest fees: these fees may be levied based on volumes of processed forest products (such as sawn wood or plywood).
- Export taxes: these are generally levied based on the volume of logs or number of processed forest products exported. In some cases, export taxes are used in place of other forest levies, such as stumpage fees. Export taxes are also sometimes used to encourage domestic processing of forest products.

While forestry contracts typically set out the forest levies imposed on the Investor, they likely do not explain how these amounts were determined. Determining appropriate amounts can be a difficult exercise. Prior to setting them, the FAO recommends that two analyses be undertaken:

- i. an economic analysis which compares the benefits and disadvantages of the proposed use of the forest (from a social utility perspective) and attempts to place a corresponding monetary value on the contract—this analysis often addresses any issues that may arise for local and indigenous communities); and
- ii. a financial analysis, which is concerned with monetary flows from the proposed use of the forest and is used to estimate the commercial value of the contract (from the perspective of an Investor).

See FAO, 2000, *op. cit.*, p. 77–87.

¹⁴ Note that some contracts may use the terms “representations,” “warranties,” “undertakings,” and “covenants” interchangeably. Accordingly, provisions should be reviewed in light of the general principles described here to determine if they are statements of fact as of a given date or forward-looking commitments.

Types of forest area-based levies include:

- Initial license fees: these fees are paid by the Investor when the Government agrees to enter into the contract. Occasionally, they are imposed as a fixed fee; more commonly, the fee will be based on the total contract area.
- Annual area-based fees (or rent): these fees may be used to encourage more efficient or intensive use of the forest.
- Annual allowable cut fees: these fees are based on the allowable annual cut; they are sometimes used as an alternative to annual area-based fees. For example, a Government may impose a fee on a 200,000-hectare timber concession that is equal to one dollar per hectare per year but at the same time require a minimum rotation period of twenty years and demand a sustainable forest management plan. Thus, in any particular year only five percent of the contract area—say, 10,000 hectares—can be harvested, resulting in a maximum fee of \$10,000 for that year. These fees may better reflect the value of the contract and better ensure security of the timber supply because they limit the Investor's ability to extract only the most valuable woods. However, they can be more complex to implement, as the annual allowable cut needs to be calculated beforehand, and controls to ensure compliance must be in place.

In addition to forest levies and fees such as those described above, Investors are often required to pay other taxes (for example, property tax, sales tax, or income tax). Typically, taxation schemes are articulated in domestic legislation, though they may be explicitly referenced in the contract. In some cases, the Government may grant the Investor exemptions from these payments; such exemptions may be built into law or established by the forestry contract.

Finally, forestry contracts may stipulate minimum fees (based on area, volume, or both). Annual fees set without regard to actual use or production may be included to discourage “banking” the concession without using the forestland in a manner that would generate taxable income or other payments.¹⁵

It is worth noting that forest levies, taxes, and other such fees serve a purpose that is distinct from the rationale behind many traditional taxation schemes. While traditional taxes are concerned with revenue maximization, certain levies, taxes, and fees required in forestry contracts represent the price for the right to extract a scarce resource. When these payment schemes are carefully and strategically designed, they can serve to incentivize better long-term management of the forestland, and thus help Governments achieve their desired sustainability outcomes.¹⁶

2.12 Capitalization; Permitted debt

In order to ensure that the Investor has sufficient financial resources to conduct its forestry operations and to fulfill its obligations under the contract and to suppliers, employees, and other creditors, the Government may require the Investor to maintain a certain level of capital, or money value, in the project throughout the contract's term. It may do this by prohibiting the project from exceeding a defined ratio that measures the amount of debt that the project has incurred to fund its operations against its capital or equity value. In a contract, this defined ratio may be a debt-to-capitalization ratio, which is calculated by dividing the project's debt by its total capital (its equity value plus its debt) at a particular time. Alternatively, a contract may include a debt-to-equity ratio, which is determined by comparing the project's total debt to its total equity (its assets minus its liabilities) at a particular time. In either case, this requirement allows the Investor the flexibility it needs to finance the project's operations and to grow its business, while restricting it from incurring aggregate debts that may lead to the project's insolvency.

¹⁵ FAO, 2003, op. cit., p. 90.

¹⁶ The 2000 IFC report reviewing the implementation of the IFC's 1991 Forest Strategy noted that over half of IFC's projects approved between 1991 and 1998 were in State-owned forests, and the stumpage paid in some of the cases studied was lower than the real cost of managing the forests sustainably. See IFC, 2000, op. cit., p. 2. Accordingly, the fee and stumpage schemes established financial disincentives for private concessionaires to adopt the costlier option of sustainable forest management.

If a contract includes this requirement, it typically will require the ratio to be calculated on a periodic basis throughout the contract's term, for instance, every fiscal quarter or fiscal year. The contract may exclude from this calculation certain categories of debt, such as non-interest bearing debt. Debt that is not factored into the ratio may be subject to certain requirements; for instance, the Government may require that any such debt is *subordinated* to any liabilities or obligations that the Investor or the project has to the Government or any claims that the Government has against the Investor or the project. This means that the Government will have a priority right to take ownership of the project's *tangible assets* and *non-tangible assets* to settle such liabilities, obligations, or claims before the holder of the subordinated debt (which may, for example, be a parent entity of the Investor) can seize the project's assets to settle debts and liabilities the Investor owes to them. Furthermore, the contract may prohibit the Investor from taking certain actions during any period in which the project has exceeded the ratio. For instance, it may prohibit the Investor from making any distributions to its equity investors or incurring additional debt for borrowed money during this time.

2.13 Environmental obligations

Forestry operations involve the intensive use of land and natural resources, which can lead to negative—and sometimes devastating—environmental impacts if not managed carefully. Moreover, in some places forestry investments are particularly sensitive given, on the one hand, forests' important role in mitigating climate change (as trees convert carbon dioxide into oxygen, which is then released directly into the atmosphere) and, on the other, the links between deforestation and climate change (as deforestation causes a direct release of greenhouse gases into the atmosphere).¹⁷

In light of these and other factors, domestic laws often mandate a range of environmental protections. In some cases, additional environmental requirements may also be negotiated between the Government and the Investor to further mitigate potential adverse impacts, including any that are specific to the particular investment. Governments interested in proactively mitigating environmental risks may negotiate these obligations into the contract itself or require that a forest management plan be presented before the Government will agree to sign the contract.¹⁸ Some of the principle considerations and associated mitigation obligations that may be required by domestic law or that may appear in contracts and/or forest management plans are discussed below.

2.13.1 Environmental impact assessments and forest management plans

An Environmental Impact Assessment (EIA) is a systematic process undertaken to examine and evaluate the potential environmental impacts of a proposed project or activity. In some situations, this process is extended to include a Social Impact Assessment (SIA), which reviews the project's social impacts (such as relocation, disruption of livelihoods, and impacts on culture). These expanded assessments are commonly known as Environmental and Social Impact Assessments (ESIAs).¹⁹ In many countries, EIAs or ESIs²⁰ are required by domestic law and/or policy to ensure that, prior to approving a project, decision-makers are informed about the potential environmental and/or social impacts and predicted outcomes of a proposed project, as well as measures that may be taken to

¹⁷ “When forests are cleared or burnt, stored carbon is released into the atmosphere, mainly as carbon dioxide. Deforestation accounts for around 18% of all global greenhouse gas emissions due to human activities – this is more than global emissions from transport.” Climate Council, “How does deforestation contribute to climate change?” (Oct 19, 2013), available at: <https://www.climatecouncil.org.au/deforestation/> (last visited Jan 18, 2017).

¹⁸ Agreed mitigation measures may be made public for transparency and monitoring purposes. In addition, they may be shared with affected communities to ensure that those communities have access to accurate, up-to-date, and comprehensive environmental information in order to make informed decisions during consultative processes as discussed in Section 2.14.1, *Consultation and “free, prior and informed consent” (FPIC)*.

¹⁹ Stakeholders may also carry out a Human Rights Impact Assessment (HRIA) to examine the project's potential (or actual) human rights impacts, including on workers and other affected individuals/communities. The human rights and social impacts of forestry projects are addressed in greater detail in Section 2.14, *Social obligations*.

²⁰ Hereafter, this Guide will use the term EIAs, with the understanding that these assessments may also include a social component (that is, may constitute an ESIA).

mitigate potential adverse impacts.²¹ Where not mandated by law, forestry contracts nonetheless may require Investors to conduct this assessment.²²

In addition to requiring an EIA, a forestry contract may require the Investor to develop a Forest Management Plan (FMP) that reflects the risks and related mitigation measures associated with the project.²³ For instance, an FMP might describe the methods the Investor will employ to prevent trespass and illegal logging; monitor and patrol boundaries; undertake surveillance; review security practice effectiveness; train employees and local communities on illegal logging issues; protect fish and wildlife habitat within the contract area; and govern use of forestland for secondary purposes. The FMP may also include maps describing forest resources; information on soil characteristics and productivity, water quality, water management systems, and processing sites; and a projection of the quality and the amount of timber that can be sustainably produced on an annual basis.

To ensure that the Investor takes appropriate mitigation measures as recommended by the EIA or FMP, the contract may require that the FMP be amended periodically to reflect changes to plans for environmental management as the project progresses. Alternatively, the Investor may be required to submit more than one FMP—for example, a one-year plan, a five-year plan, and a plan for the duration of the contract’s term—which they may also be required to update. The contract may also describe monitoring obligations, such as periodic environmental audits, and may require the Investor to incorporate the results of such audits into the FMP.

Some contracts further establish a schedule for delivery of these documents. For instance, the contract may require that these documents be submitted and approved prior to any disturbance of the environment, or that the Investor submit the EIA and/or FMP within a specified timeframe relative to the contract’s effective date. Finally, the contract may stipulate who is qualified to prepare EIA and FMP documents and what constitutes government approval of these documents. Often, EIA and FMP documents must be prepared by a qualified independent environmental consultant and approved by the Government’s environmental protection agency or its equivalent.

2.13.2 Pollution prevention

Pollution is the contamination of air, water, or soil by the discharge of harmful substances, and includes anything that may detrimentally alter the quality of the surrounding environment, affect the safety or health of human beings, or harm wildlife. Pollution prevention is the reduction or elimination of pollution at the source. In the context of forestry, key causes of pollution and other environmental damage include haze resulting from forest fire, leakage of chemicals and petroleum-based products used in processing, and sawdust.

Typically, domestic law will mandate pollution prevention measures, and a forestry contract may simply require that the Investor comply with these legal requirements. Alternatively, the parties may include, in the contract or the FMP, requirements regarding pollution controls and waste

²¹ An FAO study of direct foreign investments in agriculture found a correlation between negative environmental impacts and the failure of investors to perform an adequate environmental impact assessment or implement a proper environmental management plan. World Bank, “The practice of responsible investment in larger-scale agricultural investments: Implications for corporate performance and impact on local communities,” 86175-GLB (Apr 2014), p. 7, available at: http://unctad.org/en/PublicationsLibrary/wb_unctad_2014_en.pdf (last visited Jan 18, 2017).

²² Other contributing stakeholders—including development finance institutions and institutional investors—may also require assessments to be conducted. For example, the International Finance Corporation (IFC) imposes quasi-regulation on prospective clients that are seeking IFC funding for their development projects. Prior to project review and approval by the IFC Board of Directors, an IFC investment team communicates with the client and other project stakeholders, travels to the project site, and analyzes potential social and environmental risks associated with the project to assess whether the project complies with IFC ESIA requirements. IFC Project Cycle, available at: http://www.ifc.org/wps/wcm/connect/corp_ext_content/ifc_external_corporate_site/ifc+projects+database/projects/aips+added+value/project+cycle (last visited Jan 18, 2017).

²³ FMPs may also be voluntarily commissioned, for example, if the Investor needs an FMP to obtain a desired forest certification, such as from the FSC. An Investor may wish to become certified by the FSC in order to gain public and consumer recognition of environmentally responsible business practices. To do so may help lend the Investor “greater credibility with customers and business partners as well as financial institutions and watchdog organizations”—and in so doing, protect the Investor’s brand and reputation and allow it access to highly environmentally sensitive markets. FSC, “Why should I become FSC certified?”, available at: <https://ic.fsc.org/en/solution/become-certified/> (last visited Jan 18, 2017).

management²⁴ practices that are tailored to the forestry activity and relevant ecosystem. These controls and practices may include requirements to provide appropriate training to all persons handling chemicals or disposing of waste; to adhere to all standards for usage established by chemical manufacturers; and to report significant events to authorities, such as chemical or waste spillage.²⁵ Further, the contract may specify conditions under which the Government may suspend relevant permits or licenses—for instance, where a significant risk to life or the environment arises.

Finally, pollution control mechanisms may seek to minimize the risk of forest fire and consequent haze, both of which can have devastating health and livelihood impacts on those living in and near the contract area. Fire and haze pollution can even have significant transboundary impacts, affecting air quality in neighboring States. For these reasons, contracts may specifically address fire prevention and control, identifying which party has the responsibility to address fires and setting a standard of care for preventing, suppressing, and reporting fires within the contract area.

2.13.3 Watercourse protection and water management

In general, the term “watercourse” is used broadly, and can mean any part of a system of surface and groundwater channels and tributaries (and the water they contain), including rivers, lakes, aquifers, glaciers, reservoirs, canals, wetlands, and floodplains. Forests occur naturally in a wide range of ecosystems with diverse watercourses, from estuaries and swamps to wetlands, aquifers, and most commonly, rivers. Forested areas are often in the upper reaches of water catchments and can be an important source of clean water for local communities.

Chemicals and petroleum-based products that may be used in forestry operations can pose serious threats to watercourses by degrading water quality. Additionally, one of the most significant environmental impacts that can arise from forestry operations is the degradation of land and water resulting from the removal of forest cover, which can cause significant erosion and result in the deposit of soils in watercourses. Such effects may harm surrounding ecosystems, and may negatively affect the health of local communities and their ability to sustain their livelihoods. Furthermore, watercourse degradation may eventually lead to reduced forest resource yields, thus jeopardizing the viability of the investment.

As with pollution, domestic law often governs watercourse protection, and forestry contracts may simply require the Investor to comply with such law. However, forestry contracts and/or FMPs may impose additional requirements specific to the investment at hand (for example, restrictions on waste disposal) to ensure that Investors are mitigating potential harms wherever possible.

Domestic law, forestry contracts, and/or FMPs may also include restrictions on water usage and sourcing. This is important, as large-scale forestry operations may involve heavy water usage, and limited water resources can cause competition between industrial operations and local populations. Forestry contracts may therefore contain a provision stating that the Investor may take and use water necessary or useful for its operations, so long as that does not interfere with the rights of third parties or materially deprive villages, tribes, and local people of a reasonable supply of water where such water has customarily been available.

Finally, where operations associated with forestry contracts may affect transboundary watercourses (that is, watercourses traversing one or more international borders), the forestry contract might include an obligation to comply with any watercourse agreements that exist between the neighboring countries or under international law.

2.13.4 Land degradation and regeneration

Land degradation refers to any reduction in the capacity of land to provide ecosystem services. Soil degradation—a particularly serious facet of land degradation—occurs when the health of soil declines, thereby reducing the soil’s capacity to produce forestry or agricultural products and absorb

²⁴ Waste management is the practice of supervising and monitoring waste disposal, which is inextricably linked with the protection of watercourses, land, and air.

²⁵ Smaller, 2014, op. cit., p. 45.

carbon dioxide.²⁶ Land or soil degradation may result in a reduction in forestry yields, an increase in greenhouse gas emissions, and/or loss of biodiversity.

It is often costly, if not impossible, to reclaim already degraded land and restore ecosystem services that are critical to the local society and development.²⁷ To mitigate this risk, forestry contracts or related FMPs may require the Investor to take measures to maintain soil quality and quantity. For instance, they may require the Investor to utilize sustainable felling and skidding²⁸ practices or working methods to prevent erosion in sloping areas. Contracts may also require the Investor to monitor and report on soil health throughout the term of the contract.

Finally, permanent deforestation and loss of native vegetation can have substantial direct and indirect effects on community livelihoods as well as the environment. For these reasons, forestry contracts may set out each party's obligations regarding the condition in which the land should be returned and the standard of regrowth required. Contracts may require the Investor to replant cleared areas, clean up waste, or perform other tasks to restore the environment. In the event that the Investor fails to perform these tasks, the Government may specify that it will assume these responsibilities and charge the Investor for any costs it incurs in the process.

Despite ongoing replanting and other progressive regeneration obligations, there will likely be substantial regeneration necessary towards the end of, or after, a contract's term, at a time when cash flows may be insufficient to fund those obligations. Further, due to the nature of forestry, the effectiveness of any regeneration program will often not be capable of being gauged for several years. Accordingly, some forestry contracts provide for the establishment of a regeneration fund, or require the Investor to provide a bond, an evergreen letter of credit,²⁹ or a similar security instrument to ensure that sufficient funds will be available to finance the regeneration process.

2.14 Social obligations

At a minimum, the Government party to a forestry contract must respect its international legal obligations regarding the human rights of workers and of project-affected communities and individuals, regardless of whether these obligations are explicitly referenced in the contract. Generally speaking, this includes requirements that the Government protects and respects the rights of project-affected communities and individuals. These rights, which are protected under international human rights law, include rights to physical security, liberty, and equal treatment,³⁰ as well as rights to health, housing, food, water, an adequate standard of living, and participation in cultural life,³¹ among other fundamental rights. Governments must also protect these rights, as well as other labor-related rights, for persons employed to work directly or indirectly on the forestry investment.

Investors should respect human rights, and the UN Principles for Responsible Contracts provides guidance on integrating human rights into investment contracts.³² Further guidance on respecting

²⁶ European Commission, L. Montanarella, "Soil at the Interface between Agriculture and Environment" (1999).

²⁷ Soil type, topography, land management and crop types all affect land degradation, making it difficult to measure and very site-specific. Due to difficulties often associated with measuring economic, social, and environmental impacts of land degradation, a number of detailed local and international assessments have been undertaken in recent years. Perhaps the most comprehensive of these, the FAO's Land Degradation Assessment in Drylands (LADA) Project, investigates soil and land degradation in six countries in order to better understand international best practice and provide informed policy advice at global, national, and local level. FAO, "LADA project findings and recommendations: Land degradation assessment in drylands," NR: EP/GLO/502/GEF (Dec 2011), available at: http://www.fao.org/nr/lada/index.php?option=com_docman&task=doc_download&gid=781&lang=en (last visited Jan 18, 2017).

²⁸ The process of transporting timber from a felling site to a landing, road, or other location for transportation out of the forestland.

²⁹ An evergreen letter of credit, also known as an automatic extension letter of credit, is one that extends automatically at the end of its term. Evergreen letters are often used in transactions to secure outstanding obligations of a party.

³⁰ UN General Assembly, *International Covenant on Civil and Political Rights*, UN, Treaty Series, vol. 999 (Dec 16, 1966), p. 171, available at: <http://www.ohchr.org/Documents/ProfessionalInterest/ccpr.pdf> (last visited Jan 18, 2017).

³¹ UN General Assembly, *International Covenant on Economic, Social and Cultural Rights*, UN, Treaty Series, vol. 993 (Dec 16, 1966), p. 3, available at: <http://www.ohchr.org/EN/ProfessionalInterest/Pages/CESCR.aspx> (last visited Jan 18, 2017).

³² UN Office of the High Commissioner for Human Rights, "Principles for Responsible Contracts," HR/PUB/15/1 (2015), available at: <http://www.ohchr.org/Documents/Issues/Business/A.HRC.17.31.Add.3.pdf> (last visited Jan 18, 2017).

human rights is found in the UN Guiding Principles on Business and Human Rights.³³ An Investor may also have agreed to abide by certain international principles, such as those of the UN Global Compact, which focus on the areas of human rights, labor, environment, and anti-corruption.³⁴

Some of these standards may be enshrined in the domestic laws of the host state, and the reach of those laws generally extends beyond the Government, making them potentially applicable to the Investor and the forestry project. Furthermore, in some forestry contracts, the parties may elect to elaborate further on the respective human rights or social obligations of the Government and the Investor. Contracts may address aspects of the forestry project for which binding legal obligations exist under international law—such as resettlement—or aspects for which there is often no binding or clearly articulated legal standard, such as local employment and procurement; they may also cover other investor activities that typically fall under the banner of corporate social responsibility. Some particularly pertinent social obligations that may be addressed in forestry contracts are explored below.

2.14.1 Consultation and “free, prior and informed consent” (FPIC)

Specific consultation practices vary by country. Some countries legally require the Government and/or Investors to consult with, or obtain the consent of, local communities in certain situations, such as when Government or Investor actions threaten to interfere with local lands, livelihoods, and traditional practices. External standards, such as those imposed by certification schemes or by financial institutions, might also require either consultation with, or obtaining the consent of, local communities.

Where the forestland is situated on the lands of indigenous or tribal peoples, the principle of “free, prior and informed consent” (FPIC) applies.³⁵ FPIC entitles a project-affected indigenous or tribal community³⁶ to be consulted with and to provide or withhold their approval before the establishment of any project that stands to directly affect access to their lands, territories, or resources. Any consent obtained must be “free,” occurring without undue pressure or manipulation; it must be obtained sufficiently “prior” to the commencement of the project or public measure; and it should be given after the community is sufficiently “informed” about all aspects of the project.

A forestry contract that adheres fully to FPIC principles would include clear and specific language concerning (1) the scope of consultation, (2) the processes for obtaining community approval, and (3) what happens if the community withholds its consent. In practice, however, contracts that make reference to consultation and consent tend to do so in vague terms. In some cases, there may be a separately negotiated agreement with the community that seeks to clarify the scope of consultation. These agreements between the Investor and the community discussed in Section 2.14.5, *Corporate social responsibility, local development agreements, and community benefit agreements*.

³³ UN General Assembly, John Ruggie, “Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises: Addendum—Principles for responsible contracts: integrating the management of human rights risks into State-investor contract negotiations: guidance for negotiators,” A/HRC/17/31/Add.3, (May 25, 2011), available at: <http://www.ohchr.org/Documents/Issues/Business/A.HRC.17.31.Add.3.pdf> (last visited Jan 18, 2017). See also UN Office of the High Commissioner for Human Rights, “United Nations guiding principles on business and human rights: Implementing the United Nations ‘Protect, Respect, and Remedy’ framework,” HR/PUB/11/04 (2011), p. 13-16 available at: http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf (last visited Jan 18, 2017).

³⁴ UN Global Compact, *The Ten Principles*, available at: <https://www.unglobalcompact.org/what-is-gc/mission/principles> (last visited Jan 18, 2017).

³⁵ The right to FPIC of indigenous and tribal communities is included in, and covered by, a range of international instruments: for example, the right to free and informed consent is explicitly protected in the International Labour Organization’s *No. 169 Indigenous and Tribal Peoples Convention (1989)* (ILO 169), which is binding on ratifying states, as well as in the UN Declaration on the Rights of Indigenous Peoples (2007) (UNDRIP), which, while not technically binding, constitutes soft law and is regarded as bringing together principles from binding sources of international law, such as treaties and customary international law. Another binding instrument, the International Covenant on Civil and Political Rights, has been authoritatively interpreted to protect the right to FPIC in certain contexts as well. International standards, such as the IFC Performance Standards on Environmental and Social Sustainability (2012), also promote FPIC as a requirement in the context of investments.

³⁶ Ensuring FPIC for all local communities, and not just for indigenous peoples, is increasingly viewed as best practice.

2.14.2 Access to traditional and livelihood-generating resources; resettlement

Commercial forestry operations that displace communities involuntarily can have significant adverse effects on those displaced. Displaced communities may lose access to much-needed water reserves, or to the land and resources that form the basis of livelihoods and generate income. Moreover, even short- to medium-term resettlement may be long enough for traditional and cultural practices to be eroded or lost altogether. To protect against these and other harms, such as general infringements on property rights, most jurisdictions have domestic legislation that prohibits land confiscation without due process and/or adequate compensation. As noted above, international law provides additional protection for indigenous and tribal populations, who may have cultural and spiritual connections to the land.³⁷

Historically, large-scale concession agreements and other investment contracts were often negotiated between Governments and Investors with little regard to potential displacement. This was particularly likely in cases where the affected land was communally held, was considered to be “held in trust” for the community by the Government, or was used only during some parts of the year by nomadic or pastoral communities. In recent years, however, there has been growing recognition of the need to protect project-affected communities against forced eviction or resettlement.³⁸ Accordingly, more recent contracts may include a commitment to reduce or minimize displacement and resettlement—for instance, by prohibiting the Investor from conducting operations on land that is legally occupied by local communities. Where resettlement is necessary, these provisions typically identify who will be responsible for effectuating the relocation; they also may require the Investor to negotiate fair compensation for the land directly with the landholders. In such cases, the Investor may receive a tax credit for any expenses incurred in resettling landholders.

Even where forestry projects do not directly lead to displacement, forestry activities can have profound impacts on nearby communities’ access to a range of important traditional and livelihood-generating resources, from firewood, water, and food sources to sacred and historical sites. With that in mind, forestry contracts may offer special protections to affected communities—for instance, requiring that the Investor continue to allow such communities to access such resources and traditional sites.

2.14.3 Local employment and local procurement

Forestry contracts sometimes impose obligations on the Investor to hire employees from local communities or to locally procure goods and services needed for forestry operations.³⁹ In some cases, these obligations are defined via quota requirements—stating, for instance, that a percentage of positions at a given skill level must be filled by locals, or that a percentage of goods and services required by the Investor must be supplied by local businesses. Governments and Investors may opt to include these provisions in contracts to ensure that the forestry project contributes positively to sustainable local development. Furthermore, where the Investor conducts value-adding processes locally rather than exporting raw materials, additional economic benefits may flow to the host state.

³⁷ ILO 169, for example, which is binding upon ratifying states, stipulates in Art. 16(2) that “the peoples concerned shall not be removed from the lands which they occupy” except: (1) where “necessary as an exceptional measure” and (2) with their free and informed consent, or if that cannot be obtained, following procedures established by relevant national law. International Labour Organisation, *Convention concerning Indigenous and Tribal Peoples in Independent Countries (ILO Convention 169)*, 72 ILO Official Bull. 59 (Jun 27, 1989), available at: http://www.ilo.org/dyn/normlex/en/f?p=NORMLEXPUB:12100:0::NO:12100:P12100_ILO_CODE:C169 (last visited Jan 18, 2017).

³⁸ See Inter-Agency, “Handbook on Housing and Property Restitution for Refugees and Displaced Persons: Implementing the “Pinheiro Principles,” (Mar 2007), available at: <http://www.refworld.org/docid/4693432c2.html> (last visited Jan 18, 2017). See also UN Human Rights Council, “Report of the Special Rapporteur on adequate housing as a component of the right to an adequate standard of living, Miloon Kothari,” A/HRC/4/18 (Feb 5, 2007), available at: <http://daccess-dds-ny.un.org/doc/UNDOC/GEN/G07/106/28/PDF/G0710628.pdf?OpenElement> (last visited Jan 18, 2017).

³⁹ Local employment and procurement requirements may risk running afoul of international obligations (for instance, obligations under bilateral investment treaties) not to give preference to domestic businesses over foreign ones.

The meaning of “local,” however, can be a matter of debate, particularly if the contract fails to clearly define the term. For instance, some contracts may reserve local employment and procurement benefits for members of project-affected communities, while others may interpret “local” to include anyone who is a citizen of the host state. In the latter case, the forestry project may draw an even greater number of people from outside the project-affected area than would otherwise be the case, potentially intensifying changes to local economic or social conditions that may prove harmful to the affected community.

Some contracts also require Investors to provide specialized training or technical support to ensure that individuals from local communities or nationals of the host state can benefit from skilled positions.

2.14.4 Worker health and safety

Forestry projects can pose particular risks for workers, such as those arising from the use of dangerous tools or machinery. While health and safety issues are often covered by domestic law, some forestry contracts may seek to provide additional safeguards through provisions dedicated to protecting workers’ health and safety and to otherwise limiting harmful or dangerous labor conditions. For instance, a contract might limit workers’ hours; forbid or limit the use of certain chemicals deemed dangerous to workers’ health; or require that the Investor implement certain safety precautions (for example, the use of masks when spraying chemicals, or the use of blade guards on industrial machinery). Some contracts might also include provisions requiring the Investor to provide regular safety training instructions to its employees. In addition, contracts might include Investor commitments to provide basic medical care to the Investor’s employees and their dependents; to build wells to supply clean and safe drinking water in the contract area; or to construct health facilities and schools for employees and their dependents.

2.14.5 Corporate social responsibility, local development agreements, and community benefit agreements

Some forestry contracts include further social obligations for the Investor. For instance, Investors may commit to providing certain goods or services to affected communities and/or to employees and their descendants, such as health care, education, infrastructure, skills training, or access to food and improved water sources—commitments that might be broadly described simply as “corporate social responsibility” (CSR) or “community development activities.”⁴⁰ Contracts may also include provisions to ensure that such activities are sustainable—for instance, ensuring that schools or health clinics will continue to be staffed and supplied in the Investor’s absence, or ensuring that clean water access points are self-sustaining.

The parameters of such activities may be set forth in the forestry contract itself or in a separately negotiated agreement, or plan, established between the Government and the Investor. These separate arrangements, often referred to as Local Development Agreements (LDAs) or Community Development Plans (CDPs), may or may not be referenced in the forestry contract itself.⁴¹ LDAs/CDPs may be used to outline some or all of the aforementioned community development or CSR activities, and may also be used to establish a Social Development Fund (SDF—also known as a Community Development Fund, or CDF). An SDF might be used to fund some or all of the aforementioned community development activities, and/or to address other community needs as identified by the community itself.

⁴⁰ In addition to being included in the forestry contract, these obligations may also arise from the Investor’s own internal corporate social responsibility (CSR) policy or from negotiations with the affected community.

⁴¹ Although LDAs and CDPs are two of the more commonly used names for these types of agreements/plans, ultimately, the title is at the discretion of the Government and Investor. As such, these agreements/plans may take on a wide variety of names, which cannot be listed exhaustively here.

Alternatively—or sometimes in addition to the LDA—an Investor may elect to enter into a separately negotiated, enforceable side agreement with the affected community itself. Such agreements go by various names, including community benefit agreements (CBAs), community development agreements (CDAs), memoranda of understanding (MOUs), and impact benefit agreements (IBAs).⁴² Like LDAs, CBAs might cover a range of matters, including compensation for lost land, loss of income, and property damage; commitments to train and hire locally; CSR commitments; joint oversight committees; and consultation and grievance mechanisms. In some cases, CBAs may also provide for royalties or other profits to accrue to the community (again, often provided in the form of an SDF).⁴³

Management of LDAs, CBAs, and/or SDFs may be assigned to a committee composed of community leaders, local government officials, and Investor representatives, among other stakeholders.

2.14.6 *Grievance mechanisms*

A grievance mechanism is a routinized process through which an individual or group of people can bring a complaint concerning an investment and seek a corresponding remedy. Grievance mechanisms can be operated by the Government, the Investor, or other entities, such as financiers.

To date, forestry contracts have not commonly included grievance mechanism provisions. When included, such provisions might provide certain rights or obligations regarding the resolution of grievances from local communities (such as allowing the Government to suspend investment activities until problems are resolved), or might require the Investor to set up a site-based grievance process through which it can receive and resolve grievances from local communities or employees.

Best practices dictate that grievance mechanisms are designed and implemented in consultation with the community, and that engaging with such mechanisms should not prevent someone from subsequently seeking judicial or administrative remedies.⁴⁴

2.15 **Monitoring and reporting**

Monitoring the Investor's performance to ensure compliance with its obligations is critical. Forestry contracts and/or domestic law often require an Investor to undergo various levels of periodic monitoring, from internal reviews and self-reporting to compliance evaluations conducted by the Government or an independent third party. For example, a contract may require the Investor to submit to the Government annual operational reports that provide a full account of the number and type of trees felled and the quality of timber that the Investor produced during the relevant reporting period. Reports submitted to the Government may be subject to an independent audit to ensure the objective assessment of the Investor's compliance with the contract's provisions.

Many contracts require an Investor to maintain written books and records to account for the Investor's financial transactions and for matters involving its assets and business during a particular financial reporting period. These records may include financial statements, cash receipts, bank statements, income tax statements, stock ledgers, minute books, and operational plans, among others. The Investor often must maintain these records in a manner that conforms to commonly accepted accounting principles (such as the Generally Accepted Accounting Principles, or GAAP), as well as to the laws of any country that has jurisdiction over the Investor (including the Investor's *home state*—

⁴² In some instances, these agreements between Investors and communities may also be referred to as LDAs; however, for the sake of clarity, in this Guide the term LDA is used only to refer to agreements between Governments and Investors.

⁴³ These revenue-sharing schemes may be tied to, among other features, the project's profits (which may increase the potential revenues to be shared but reduce the predictability or stability of revenue flows to the community) or to total revenue (which may ensure a more steady, but potentially more modest, stream of benefits for the community).

⁴⁴ UN Special Representative of the Secretary-General on the Issue of Human Rights and Transnational Corporations and Other Business Enterprises, "Guiding Principles on Business and Human Rights: Implementing the United Nations 'Protect, Respect and Remedy' Framework," UN Doc. A/HRC/17/31 (Mar 21, 2011), Principle 31(h) and commentary to Principle 29, available at: http://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf (last visited Jan 18, 2017).

where the Investor is legally organized—and the host state—where the forestry operation is situated). A contract might also require the Investor to undergo an annual financial audit to ensure that its books and records are correct and complete.

Further, a forestry contract may grant the Government the right to enter the contract area from time to time to inspect the Investor's activities (including the activities of any sub-contractors); for instance, to inspect the type, quality, and quantity of timber that the Investor is harvesting, processing, and marketing. This enables the Government to ensure that the Investor is complying with its obligations under the contract as well as with all applicable laws and regulations. During such inspections, the Government typically can review the Investor's books and records, including accounting records, production records, and other operational information. The contract may also require the Investor to provide certain information to the Government in a timely manner where this information is of reasonable significance; for instance, business decisions that may have a substantial social or economic impact on the host state.

2.16 Anti-bribery and corruption

As the international regulatory environment for cross-border businesses becomes more complex, anti-bribery and corruption provisions in investment contracts have become increasingly important. Although such provisions are not yet standard in forestry contracts, they may become more common as contracting parties incorporate or adapt model provisions, such as the International Chamber of Commerce Anti-Corruption Clause.⁴⁵ The ICC Anti-Corruption Clause includes, among other things, representations from the parties that they have not engaged in any corrupt activities in connection with the relevant contract, promises from those parties that they will not engage in any such corrupt activities throughout the life of the contract, and provisions establishing measures to be taken if one party discovers that the other has engaged in such prohibited activities.

Regardless of whether an anti-corruption provision is included in the contract, however, contracting parties must still guard against bribery and corruption as required by national and international law—including legislation in the Investor's home state and in the host state.⁴⁶

2.17 Assignment and novation

Assignment and **novation** provisions deal with the transfer of benefits and/or obligations of a contract to a person or entity not party to the original contract.

Assignment is the transfer of the benefits of a contract to a new party, but not the obligations. Novation, on the other hand, essentially puts the new party into the shoes of the party novating (that is, transferring the contract), so that the new party is treated as if it had signed the original contract, thus assuming all of the rights and obligations that the novating party had undertaken. In either case, if an Investor wants to transfer its rights or obligations under a forestry contract to a new party, the contract (or relevant regulations) will likely require it to obtain the Government's consent—typically, in writing—before making any such transfer.

⁴⁵ This clause was published by the International Chamber of Commerce in 2012 to assist companies seeking to embed anti-corruption principles into their contractual agreements. International Chamber of Commerce Commission on Corporate Responsibility and Anti-corruption, and the Commission on Commercial Law and Practice, "ICC anti-corruption clause" (2012), available at: <http://www.iccwbo.org/Advocacy-Codes-and-Rules/Document-centre/2012/ICC-Anti-corruption-Clause/> (last visited Jan 18, 2017).

⁴⁶ In the U.S., legislation requires that companies within its jurisdiction adhere to strict anti-bribery and anti-corruption standards when conducting business abroad. For instance, the U.S. Department of Justice has taken an expansive view of what cases fall under the *Foreign Corrupt Practices Act 1977* (FCPA). The FCPA prohibits U.S. companies from paying (or offering to pay) foreign officials to obtain business, and it further applies these restrictions to foreign entities and citizens who commit such acts while in U.S. territory. Engaging in any such activities is a criminal offense, and penalties for such offenses include severe fines and imprisonment. The UK *Bribery Act 2010* is also extensive in its application. Of most concern for many businesses is Section 7, which states that an entity associated with a person who has offered a bribe may be liable for an unlimited fine if it has not implemented adequate procedures to prevent corruption. The UK Ministry of Justice has stated that it considers contractual anti-corruption standards to be "adequate procedures" within the meaning of Section 7. United Kingdom Ministry of Justice, *The Bribery Act 2010: Guidance about procedures which relevant commercial organisations can put into place to prevent persons associated with them from bribing* (Feb 11, 2012), Section 9, p. 23, available at: <http://www.justice.gov.uk/downloads/legislation/bribery-act-2010-guidance.pdf> (last visited Jan 18, 2017).

Governments typically limit an Investor's ability to transfer its rights and obligations to a new party for a range of reasons. Primary among these reasons are:

- The Investor's access to high value confidential information from the Government during the term of the contract. While the Government may be comfortable disclosing such information to the Investor, it may not want to disclose such information to any entity that may later become party to the contract via an assignment or novation.
- Reliance on the Investor's reputation, financial capability, or industry expertise when entering into the contract. These factors often influence the Government's decision to agree to the project as well as the terms it negotiates into the contract. Accordingly, prior to providing its consent to any assignment or novation, the Government may want to confirm that the proposed new party brings a reputation, financial strength, and industry expertise that are commensurate with the Investor's to ensure the continued viability of the project.

In addition to Government consent rights, assignment and novation provisions may also permit or prohibit certain types of transfers. These often include:

- Whether or not the Investor will be able to sub-contract. Forestry contracts may allow the Investor to sub-contract with third parties during certain phases of the forestry process. If the Investor is allowed to sub-contract, the contract may set parameters for how the Investor does so.
- Whether or not the Investor will be able to assign its rights under the forestry contract—including its rights to access and/or possess the forestland and exploit the forest resources—to a lender as security (or collateral) for a loan. In some situations, the Government may allow the Investor to pledge its interests in some or all of the contract area so that the Investor may obtain financing to carry out the operations contemplated by the forestry contract. Where this is allowed, the forestry contract may include a provision describing the Government's right and remedies if a lender forecloses on the collateral or otherwise exercises remedies in relation to it.

2.18 Change of control

A forestry contract may require the Investor to obtain the Government's consent—typically, in writing—prior to any change in the ownership or management of the Investor. This change in ownership or management is often referred to as a “change of control.” Events that constitute a change of control may include assignments, transfers, or sales of a majority of the stock or economic interests in the Investor (or a parent company); a sale of all or substantially all of the Investor's (or a parent company's) assets; or a change in the majority of the Investor's (or a parent company's) board members. If a change of control occurs without the Government's consent, the contract may allow the Government to terminate the contract.

2.19 Confidentiality and publicity

Confidentiality provisions are designed to ensure that certain types of information shared between the parties to a contract remain confidential and not publicly available. These provisions usually require each party to protect the other party's trade secrets or other information that is conveyed under the understanding that it will not be made readily available to the public. While the confidentiality provision may be broad, it typically excludes certain categories of information, such as information that is already in the public domain or information that must be disclosed by law.

Generally, information covered by a confidentiality provision remains confidential for the life of the contract. In addition, some confidentiality provisions may also survive the termination of the relevant contract, which means that the parties must treat information covered by the provision as confidential even after the contract's term has ended.

Governments, Investors, and local communities may have different views on what constitutes confidential information and when confidentiality provisions should apply. For example, they may disagree on whether the forestry contract itself should be made publicly available.⁴⁷ Relevant guidelines and principles indicate that transparency of these contracts, or of all non-commercially-sensitive provisions included in them, is best practice.⁴⁸

2.20 Stabilization

A *stabilization* provision seeks to shield the Investor from having to comply with or incur the costs of changes in the domestic law.

Some stabilization provisions require the Government to refrain from doing certain things. For example, a provision might prohibit the Government from materially increasing taxes or royalties payable by the Investor under the contract. Other stabilization provisions exempt the Investor and its operations under the contract from compliance with laws or regulations adopted by the Government after the contract was executed, or require that the Investor be compensated for changes in the law affecting its investment.

Stabilization provisions can be grouped into five categories:

1. Intangibility provisions: these provisions prohibit the Government from nationalizing the operations covered by the project or amending the contract without the Investor's consent.
2. Consistency provisions: these provisions may be combined with another type of stabilization provision, and provide that legislation enacted by the Government will only apply to the Investor's operations under the contract if it is consistent with the contract.
3. Freezing provisions: these provisions "freeze" the legislation and regulations affecting the Investor and its operations under the contract to those that existed at the date of the contract. Freezing provisions generally state that legislation and regulations enacted after the commencement of the contract will not apply unless the Investor agrees to be bound by them. Freezing provisions can be either "full freezing provisions," covering all laws concerning the operations under the contract, or "limited freezing provisions," which only freeze some laws (for example, relevant tax laws).
4. Economic equilibrium provisions: these provisions seek to ensure that the Investor is compensated for the costs of complying with any laws or regulations adopted after the contract begins. In contrast to freezing provisions, economic equilibrium provisions do not excuse the Investors from complying with the new laws or regulations. As with freezing provisions, economic equilibrium provisions may be either "full" or "limited." A full economic equilibrium provision protects the Investor against the economic consequences of all changes in legislation and regulations, whereas a limited economic equilibrium provision may only apply to certain laws and regulations, or may only be triggered if compliance costs exceed a certain amount.
5. Hybrid provisions: these provisions contain some elements of freezing provisions and some elements of economic equilibrium provisions and generally require the Government to restore the Investor to the material position it was in before the law changed. This could be through compensation or a special exemption from the law.

⁴⁷ This relates to issues of community access to information and public participation, referenced in Section 2.14.1, *Consultation and "free, prior and informed consent" (FPIC)*. Confidentiality provisions that are narrowly tailored to cover only information that genuinely needs protection for commercial reasons help the Government avoid any conflicting duties it may have with respect to confidentiality (with regards to the Investor) and transparency (with regards to affected communities and the general public). Limiting the scope of confidentiality provisions can also help the Investor avoid accusations of engaging in secret, closed-door deals with Governments, and disclosure of contractual terms that affect local communities may engender more trust within such communities.

⁴⁸ Columbia Center on Sustainable Investment (CCSI), "Recommending Transparency in Land-Based Investment: A Summary of Relevant Guidelines and Principles" (Mar 2016), available at: <http://ccsi.columbia.edu/2016/03/09/recommending-transparency-in-land-based-investment-a-summary-of-relevant-guidelines-and-principles/> (last visited Jan 18, 2017).

Stabilization provisions can be controversial given their potential impact on sustainable development and human rights, particularly when the provision does not create exceptions for changes in law related to labor, human rights, health and safety, the environment, or other social issues. Some stabilization provisions will explicitly carve out such areas, while others are written to only cover limited fiscal issues.

2.21 Dispute resolution

A contract's dispute resolution provisions describe the mechanisms that the parties must use to resolve disputes that may arise under the forestry contract. These provisions may require the parties to employ negotiation, mediation, arbitration (*see text, right*), or court proceedings.

Where parties wish to save costs and time or want to ensure the continuation of the contract, the dispute resolution provisions may require the parties to negotiate before resorting to outside mediation or arbitration. These provisions may also require the use of mediation by an independent experienced third person in order to help the parties identify the issues in dispute, explore the options for resolution, and attempt to reach agreement. Additionally, or alternatively, dispute resolution provisions may specify the use of arbitration where the parties want disputes to be finally resolved by an arbitral tribunal. Often, where this is the case, the contract will identify where the arbitration will be located, which set of arbitration rules will apply,⁴⁹ and how arbitrators will be selected. Finally, if the parties wish to invoke the power of a court to determine the issues and remedies according to law, then dispute resolution provisions will require the parties to resolve disputes through court proceedings; typically, the contract will identify a specific court system (for instance, the courts of the home or host state) where the parties must bring their claims.

2.22 Force majeure

Force majeure provisions are designed to operate on the occurrence of an event outside the parties' control that prevents one or both parties from performing their obligations under the contract.

There are two distinct aspects of force majeure provisions:

- the definition of force majeure events; and
- the operative clause that sets out the effect on the parties' rights and obligations if a force majeure event occurs.

The term "force majeure" does not have a universal definition, and is therefore open to interpretation by the courts of the relevant jurisdiction. For the avoidance of doubt, parties often clearly define in the contract what can constitute a force majeure event. Examples of force majeure events include strikes, war, civil unrest, and extreme weather events. Often force majeure provisions will take into

Arbitrations are often perceived as offering efficient dispute resolution processes and adjudicators with high levels of expertise regarding international investment law and transactions. However, arbitration may involve costs beyond the limited financial capability of the parties, particularly when arbitration proceedings are held outside of the host country.

Additionally, arbitration panels are often unable to adequately address considerations relating to other interested or affected relevant stakeholders (such as impacted affected local communities), and confidentiality rules governing arbitration can severely limit the amount of information those stakeholders receive regarding resolution of the dispute.

In order to mitigate these concerns, contracts may stipulate that arbitration be used by the parties only after they have attempted to resolve their dispute using available domestic dispute resolution processes. Where this is the case, resolution of disputes through domestic systems may result in stronger precedent and jurisprudence governing forestry investments and contract law, as well as more transparent communication of information to all affected parties.

⁴⁹ For example, the International Chamber of Commerce, Rules of Conciliation and Arbitration, or the UN Commission on International Trade Law Arbitration Rules.

account any potentially harmful situations that are more likely to arise in the particular country or region concerned.

If a party's obligations under a forestry contract are rendered impossible to perform or are otherwise significantly affected by a force majeure event, then a party may rely on a force majeure provision as a defense to a claim that it has failed to fulfill its obligations under the contract. The provision may also specify the conditions for extension, suspension, or termination of the contract when a force majeure event occurs. For example, where a local land dispute occurs between an Investor and local communities, authorities may have the right to suspend the contract until the dispute has been resolved.

2.23 Indemnification

An indemnity is a contractual promise by one contracting party to compensate for losses incurred by another party to the contract resulting from claims brought against the latter by a third party. Indemnities commonly cover losses arising from the following situations:

- breach of representation or warranty;
- breach of other contractual obligations;
- violations of law;
- other losses incurred under specified conditions; and
- third party claims under specified conditions (for example, intellectual property infringement claims, product liability claims, or personal injury claims).

Forestry contracts may feature reciprocal indemnities (meaning, indemnities running from each party to the other party) in relation to losses arising out of:

- negligence, carelessness, or willful misconduct by one party (often with the limitation that that negligence, carelessness, or willful misconduct, or the loss itself, must be connected in some way with the forestry project);
- accidents, damage to property, injury, or death suffered by any person occurring in or near the contract area and caused by the party giving the indemnity (or its employees or associated persons); or
- contractual breaches.

Some contracts include survival provisions, which identify certain provisions in the contract that will remain operative after expiration of the contract's term or early termination of the contract. These provisions may pick up indemnification obligations—in such cases, a party that agrees to indemnify the other party for certain claims or liabilities that arise in connection with the contract may be obligated to indemnify the other party for those claims and liabilities that arise after the project has concluded. For forestry investments that involve high environmental risks, this may arise where environmental harms do not manifest until well after the project has come to a close. In such cases, if the Investor has agreed to indemnify the Government for liabilities arising from environmental harms (such as contamination of groundwater or adverse health impacts on communities), the Government may look to the Investor to settle liabilities for as long as the indemnification provision remains operative.

2.24 Termination

Termination provisions allow one or both parties to end the contract prior to expiration of the term if certain events occur. These can include:

- Breach of contract: Typically, if a party fails to comply with the terms of an agreement but the breach is immaterial (that is, it does not prevent the continuation of the entire contract), the other party will not have a right to terminate the contract. Rather, termination usually results from a material breach (a breach that goes to the heart of the contract and negatively affects the outcome of the entire agreement). Even in light of a material breach, a termination

provision might require that the breaching party be given a chance to correct its actions within a set period of time. However, there may be bad acts (or repudiations) that will give rise to an immediate right of termination (for example, breach of confidentiality, breach of anti-corruption legislation, change of control, invasion of protected areas, or materially exceeding allowed levels of consumption). In addition to termination rights, material breaches can give rise to different types of remedies; for instance, the party in breach may have to pay money damages or rectify the breach.

- Frustration of the contract, which may occur when an event outside of the control of either party makes it impossible to fulfill some or all of the contractual obligations (for example, a sustained force majeure event).
- Failure to conduct forestry activities as stipulated by the contract, or to develop a certain percentage of the concession area, within a certain time period. If such performance benchmarks are not met, the Government may have the right to terminate the contract, or restore a portion of the concession, unless the breaching party makes a compensation payment or otherwise remedies the breach.
- Bankruptcy: A contract may allow the Government to terminate the contract if the Investor commences bankruptcy, reorganization, or similar insolvency proceedings, or if any such proceedings are initiated against the Investor by a third party. If such proceedings are brought by a third party, the contract may only allow the Government to terminate if such proceedings have not been dismissed after a specified period of time.

Termination provisions may also provide for termination by agreement between the parties or by the payment of a termination fee by one party to the other. This fee may be on a sliding scale, so terminating early in the term triggers a higher fee than termination closer to expiration of the term. Some termination provisions will set out how parties must give notice of their intention to terminate, or may describe the consequences of termination due to a breach of contract—these consequences may include the availability of restitution or liquidated damages for the non-breaching party. These provisions usually take into account any special laws or regulations around termination that exist in the relevant jurisdiction.

2.25 Disposition of assets

Disposition of assets provisions describe the process by which the Investor will dispose of the project's assets upon termination of the contract. These provisions often distinguish between *movable assets* and *non-movable* assets.

Some contracts provide the Government with the first option to purchase any movable tangible assets (for instance, machinery and tools) that the Investor desires to sell. The contract may also address disposition of non-movable tangible assets upon termination of the contract; these assets often become the property of the Government without charge. In the event of a breach of contract by either party, the value of these non-movable assets may be taken into account when determining any award of damages.

The contract may also stipulate what condition the forestland must be in upon surrendering the land back to the Government, and the specific period of time within which the land must be surrendered following termination of the contract. These stipulations may be specific—for instance, the amount of forest cover required upon the conclusion of the contract term—or subjective—for instance, asserting that the state of the returned land must be “to the satisfaction of the Government.” The contract may also state under which circumstances the Investor will receive compensation for improvements to the land, or under which circumstances the Government or a third party reclaiming the land will receive compensation for damage or restoration purposes.

2.26 Notice

A notice clause states how the parties to a contract will communicate with each other (usually in written form). The notice clause works in conjunction with other provisions of the agreement that specify circumstances under which notice is required (for instance, notice of certain material events,

such as investigations or lawsuits affecting a particular party and/or its operations). Notice clauses may also address what happens when a party changes address or when delivery is refused or rejected. Notice clauses can be very important if relations between parties deteriorate and litigation is contemplated, or when one party needs to serve an important notice (for example, a termination notice) on the other.

2.27 Amendments; Periodic review

Most forestry contracts include an amendment provision, which states whether and under what circumstances the parties may amend the contract. Generally, this provision will state that the contract is the entire agreement between the parties, and that any amendments or modifications are null and void unless made in writing and signed by both parties.

Contracts may also include a provision permitting a periodic review of the contract's terms. A periodic review process provides a systematized means for the Investor and the Government to discuss proposed modifications to a contract and to amend the contract. This process may be triggered after a certain amount of time has passed (for instance, every five years), or due to environmental, social, or economic circumstances that have substantially altered the conditions and assumptions that the parties relied on when they entered into the contract (for instance, a dramatic downturn in relevant commodity prices).

2.28 Governing law

Governing law (or "choice of law") provisions enable the parties to specify the system of law that will apply to determine the rights and obligations of the parties and the interpretation of the contract and its effect if a dispute arises. However, governing law clauses do not indicate how disputes are to be resolved, which is why parties often include a separate dispute resolution clause in the contract.

Governing law provisions do not indicate how disputes are to be resolved, which is why parties often include a separate dispute resolution provision in the contract.

3 GLOSSARY

This Glossary provides basic summaries of certain terms that frequently appear in forestry contracts. However, each forestry contract may have its own set of defined terms, which may be tailored to the relevant forestry project and may differ from the definitions here. For this reason, it is important when reviewing any forestry contract to refer to that contract's definitions section (as further described in Section 2.1, *Definitions*).

Affiliate: A legal person that, with respect to a second legal person, directly or indirectly controls, is controlled by, or is under common control with, that second legal person.

Breach of contract: A failure of a party to a contract to perform its obligations as set forth by the terms of such contract.

Concession: The grant of exclusive privileges by the Government or controlling authority. In the context of forestry contracts, it specifically refers to grant of the rights to enter upon the land and to harvest the trees upon the land in order to make profit.

Condition precedent: An event that must take place before a party to a contract is required to perform its own obligations under the contract.

Contract area: The area of land to which the forestry contract applies.

Damages: Monetary compensation that a court may order one contracting party to pay a second contracting party for loss or injury that the second party (or its property) suffers due to the fault or negligence of the first contracting party.

Easement: The legal right of a legal person to use land not owned by such legal person for a specified purpose.

Ecosystem services: The benefits derived from ecosystems, including but not limited to: provisioning services (food and water), regulating services (climate and disease control), cultural services (spiritual and recreational use), and supporting services (nutrient recycling and crop pollination).

Effective date: The date upon which the contract takes effect. The effective date is frequently specified in the Definitions section of the contract and often refers to the point when all parties have signed the contract or when certain conditions precedent have been met.

Enforceable legal rights: Rights that are recognized by the law and can be enforced by law where necessary. If a legal person holds an enforceable legal right pursuant to the terms of a contract, the party obligated to respect that right pursuant to the contract can be forced or ordered to do so through a legal proceeding.

Execute: To make a document legal, binding, and enforceable by signature.

Felling: The act of cutting down individual trees as part of the logging process.

Forest management plan: A document describing the manner in which commercial forestry will be carried out, and which may specify, for example, optimum harvest rates, means of minimizing environmental impacts, measures to ensure the health and safety of workers, and processes to accommodate interests of local communities.

Forest product: Any material derived from forest resources, including but not limited to flora, fauna, and microorganisms, that may be exploited for social, economic, or other benefits.

Forest resources: Any resources of practical, commercial, social, religious, spiritual, recreational, educational, scientific, subsistence, or other potential use to humans that exists in the forest environment.

Force majeure: An event that produces a fundamentally different situation to that contemplated by the parties when entering the contract, rendering the contractual obligations incapable of being performed. A force majeure clause suspends or removes liability when a force majeure event occurs without the default of either party. For example, war, natural disasters, blockades, and riots are often considered force majeure events, and each party's obligations under the contract may be suspended for the duration of that event.

Governing law: The system of law designated by the parties to apply to the operation of the contract and any disputes arising from it.

Harvesting certificate: Written permission, as issued by a government, which provides permission to harvest timber and/or other forest products.

Home state: The country in which an Investor is primarily based, headquartered, or incorporated (sometimes referred to as the home country).

Host state: The country in which a forestry investment takes place (sometimes referred to as the host country).

Infrastructure: Basic physical and organizational structures and systems (for example, buildings, roads, water, and power supplies) required for the production of goods and services and the distribution of raw material and finished products.

Jurisdiction: The authority to interpret and apply the law, or to govern and legislate, which is granted to a formally constituted legal body, such as a court or political leader. The term jurisdiction is also commonly used to refer to the geographical area over which such authority applies. (*See also* Governing Law.)

Legal framework: A broad system of rules that governs and regulates decision-making, agreements, and laws within a given jurisdiction.

Legal person: A human or non-human entity—such as an individual, corporation, or recognized organization—that is treated as a person for limited legal purposes. Such entities have legal rights and are subject to legal obligations, meaning that they can sue and be sued, own property, and enter into contracts.

Legislation: A body of laws that has been promulgated by a governing body.

Levies: A duty or tax collected by authorities.

Liability: Legal responsibility for the consequences of a parties' act or omission, enforceable by civil remedy or criminal punishment.

Log: The portion of a tree, with or without side limbs and with bark removed, that is otherwise substantially intact and intended for further processing.

Movable assets: An asset that can be moved from one location to another.

Non-movable assets: An asset that cannot be moved from one location to another, or that cannot be moved without destroying or altering it.

Non-tangible asset: An asset that is not physical in nature. Common non-tangible assets include intellectual property (such as patents, trademarks, and copyrights), goodwill, and brand recognition.

Party: A legal person who enters into a binding contract with other legal persons and thus assumes certain benefits and obligations as specified therein.

Regeneration: Actions taken by an Investor to ensure that the forest grows back after exploitation, and that trees are re-established. This process may also be referred to as reforestation.

Right-of-way: The legal right to pass along a specific route through grounds or property belonging to another.

Signature date: The date when a contract is signed by all parties.

Stabilization: A stabilization provision removes or limits the ability of the Government to alter an investor's obligations or entitlements with regards to a particular project by revising relevant legislation after the forestry contract has been signed. A stabilization provision will maintain the legal status quo of the original contract by either exempting the Investor from the changes in law, or providing for compensation of the Investor for any losses resulting from the changes.

Subordinate (to): The act or process of moving something to a lower rank, position, or priority. With respect to claims a creditor may have to a debtor's assets, if those claims are subordinated to another creditor's claims, this means that the other creditor's claims are of a higher priority and will be settled in full before the subordinated claims are settled.

Subsidiary: A company that is owned or controlled by another company.

Tangible asset: An asset that is physical in nature. Common tangible assets include land, buildings, vehicles, machinery, inventory, and cash.

Tenure rights: Rights, whether legally or customarily defined, with respect to land and other natural resources. In the context of forestry investments, tenure rights may, for example, take the form of concessions, leases, licenses, or permits, each of which grant certain temporary rights to access the land and exploit its resources.

Term: The period of time during which a contract is operative.

Termination date: The date when a contract is terminated in accordance with its terms, typically with no action required by any party thereto.

Third party: A person who is not party to a contract or agreement but has involvement and/or may be affected by the outcome.

Timber: Wood that has typically already been processed into logs, beams, or planks for use as building material.