



#### OPEN ACCESS

SUBMITTED 25 February 2025

ACCEPTED 23 March 2025

PUBLISHED 14 April 2025

VOLUME Vol.07 Issue 04 2025

#### CITATION

Miraziz Khidoyatov. (2025). Methods for Minimizing Legal Risks in The Conclusion of International Investment Agreements. The American Journal of Management and Economics Innovations, 7(04), 35–42. <https://doi.org/10.37547/tajmei/Volume07Issue04-04>

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# Methods for Minimizing Legal Risks in The Conclusion of International Investment Agreements

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**Abstract:** This article examines modern approaches to minimizing legal risks in the negotiation and implementation of international investment agreements, addressing both legal and socio-environmental aspects. Based on an analysis of recent research, key factors contributing to safer and more balanced interactions between investors and host states are identified. Specifically, detailed descriptions of contractual obligations, the introduction of clear sanction and compensation mechanisms, and flexible dispute resolution procedures significantly reduce the likelihood of conflicts. Additionally, the role of proactive contract design is emphasized, which involves a simplified and transparent structure to engage all stakeholders, including local communities. The article also highlights the growing significance of digital trends, from the recognition of virtual assets and cross-border data flows to the adaptation of agreement provisions reflecting the rapidly evolving digital economy. The findings conclude that comprehensive risk management measures not only enhance trust in the international investment environment but also promote more sustainable development while preserving regulatory sovereignty and protecting the key rights and interests of all parties involved. This article is of interest to specialists in international law, legal professionals, economists, government officials, and corporate consultants involved in the development, negotiation, and analysis of investment agreements.

**Keywords:** international investment agreements, legal risks, sanction mechanisms, environmental standards, digital economy, proactive design, dispute resolution,

regulatory sovereignty.

### Introduction:

By nature, international investment agreements seek to balance the expansion of economic cooperation with the protection of public interests. When a state provides legal guarantees to foreign investors, these guarantees must be accompanied by mechanisms that prevent abuse and uphold the principles of sustainable development. As in classical doctrines of international public law, the supremacy of fundamental norms concerning human rights and environmental protection should not be "dissolved" within the framework of transnational transactions. Even the most compelling arguments for diplomatic necessity or economic gain do not justify situations where legal principles are undermined or irreversible risks are created for vulnerable populations.

Current trends indicate that compliance with environmental, social, and other regulatory requirements has become a crucial aspect of any investment transaction, regardless of its scale or industry [11, 12, 13, 14]. At the same time, overly broad privileges for investors, without clearly defined restrictions, undermine trust in the international dispute resolution system. This raises the question: how can legal risk prevention mechanisms be properly structured to ensure fair opportunities for foreign investments without infringing upon the regulatory sovereignty of states? Answering this question requires an in-depth analysis of existing norms and case law, which demonstrate that no "absolute immunities" or overly general guarantees should disregard fundamental principles of responsibility and sustainability.

The aim of this article is to identify and systematize the most effective mechanisms for reducing legal risks in international investment agreements, ensuring a balance between investor interests and state regulatory autonomy.

### Objectives:

1. Analyze existing practices for incorporating environmental, social, and digital provisions into investment agreements.
2. Identify the most effective sanction and compensation mechanisms that encourage responsible investor behavior.
3. Examine the role of joint institutions and proactive contract design in conflict prevention.
4. Determine key factors influencing the successful adaptation of agreements to changing realities (digitalization, ESG standards).

This article explores a modern set of measures for reducing legal risks in the conclusion of international investment agreements. Based on legal studies and economic assessments, it is demonstrated that a responsible agreement is not merely a declaration of investment protection. Instead, it establishes clear cooperation conditions, preventing conflicts at the negotiation stage and ensuring rapid response mechanisms for unforeseen circumstances. This intersection of "economics and law" supports the assertion that a reliable legal framework does not hinder investments but, on the contrary, creates conditions for their safe and sustainable development.

### MATERIALS AND METHODS

This study examines literature addressing the specifics of negotiating and implementing international investment agreements, including issues of environmental and social responsibility, access to justice, and the economic rationale behind legal norms. The work of the Columbia Center on Sustainable Investment and the UN Working Group on Business and Human Rights [1] explores ways to enhance transparency in the investment regime while considering the interests of local communities. The publication by Dotzauer et al. [2] describes the increasing inclusion of sustainability-oriented provisions, whereas Faccio [3] focuses on the reform of investment arbitration and investor accountability mechanisms. The research by Gastinger and Dür [4] analyzes the influence of joint institutional bodies within European Union agreements, while Kaave [5] emphasizes the importance of detailed contract design to ensure sustainable standards in investment financing. Polanco [6] examines the implications of digitalization and its legal consequences, Sykes [7] explores the economic structure and interpretation of obligations, and an analytical Report prepared by the Congressional Research Service (CRS) [8] discusses the dominance of the U.S. dollar in the global system and its associated risks for investment strategies. Vadi [9] reflects on the transformation of international investment law as part of broader international legal norms, while Willemin and colleagues [10] provide an in-depth assessment of the environmental impacts of trade agreements, using the EFTA-Mercosur agreement as an example.

A comparative evaluation of academic publications was conducted to highlight differences in legal regulation and implementation mechanisms of investment agreements. A systematic selection of materials was carried out through an analysis of publicly available legal and economic databases. The objective was to

identify risk mitigation methodologies by incorporating provisions on fair protection of parties and the prevention of environmental and social harm into contractual texts. Critical analysis was used to identify gaps in existing research, particularly regarding digital trends and currency-related factors.

Sources from various disciplines were considered, ranging from socio-legal to economic-legal and environmental perspectives, allowing for a comprehensive understanding of modern tools for minimizing legal risks.

## RESULTS

The findings indicate that many studies on international investment agreements converge on the necessity of legal protection for the interests of all parties while also emphasizing the importance of preserving state regulatory sovereignty [1; 3; 11; 14]. The inclusion of detailed dispute resolution mechanisms, protections for local communities, and environmental safeguards in agreement texts significantly reduces the likelihood of conflicts during investment project implementation [4; 5]. Collectively, studies [1–5] reveal several key trends.

The quality of agreement structuring plays a critical role, particularly in the precise definition of obligations and the scope of regulation [1; 6; 9]. A clear delineation of regulatory parameters—specifying which norms apply to investors, what obligations are imposed on the state, and how these relate to supranational, regional, or sectoral agreements—is essential for reducing legal risks in international investment agreements. Research highlights that vague or ambiguous provisions increase the risk of arbitration disputes and inconsistent interpretations, leading to higher project costs and unforeseen litigation expenses [2; 10].

Proactive and transparent contract mechanisms serve as a crucial risk management tool. A simplified structure and clear language facilitate better cooperation between investors and host states [5]. The more comprehensible the agreement is in terms of obligations, legal remedies, and consequences for non-compliance, the lower the risk of misunderstandings between parties. This approach integrates proactive elements, such as a clearly defined action plan for complying with environmental and social requirements, as well as detailed procedures for engaging local communities in project discussions [1]. Failure to meet these conditions can lead to international claims, significantly increasing project costs due to reputational damage or regulatory enforcement measures.

A combined legal and financial structure, including well-

defined sanction and compensation mechanisms, is of particular importance [3; 6]. For instance, agreements should contain termination procedures in cases where investors fail to meet social or environmental obligations. An alternative approach involves a "floating" system of incentives and penalties, where investors either receive tax benefits for verified ESG compliance or, conversely, face additional financial obligations and even early contract termination in cases of proven harm [3; 5]. Such mechanisms enhance legal certainty and serve as an effective tool for managing adverse outcomes for host countries.

A recent research direction focuses on multilateral bodies and joint committees established under international agreements [4]. These institutions delegate certain powers to the supranational level, reducing the potential for unilateral rule changes. Studies indicate that joint bodies, such as association councils and committees, when operating under a clear framework of representation—including civil society participation—can resolve conflicts at early stages, thereby minimizing the risk of large-scale legal disputes [1; 4]. These entities also play a role in monitoring compliance with obligations, including environmental management, the protection of local community rights, and financial transparency [5; 10].

Recent literature has given significant attention to digital transformation and its impact on international agreements [6]. This includes the legal protection of digital assets and the contractual obligations regarding data storage, cross-border flows of digital assets, and investor identification without physical presence [6]. Since many digital arrangements remain insufficiently regulated, experts emphasize the necessity of adapting "traditional" investment agreements to new realities involving virtual transactions and online services. This adaptation aims to prevent legal loopholes and prolonged disputes over jurisdiction and applicable law.

Researchers [1–4; 6] share a consensus that an effective legal risk reduction strategy should include:

1. Thorough due diligence that evaluates not only the economic feasibility of a project but also its political, legal, and social dimensions.
2. Inclusion of detailed provisions on investor environmental and social responsibility, along with procedural safeguards ensuring transparency in decision-making and access to information for local populations.
3. Establishment of clear and transparent dispute resolution mechanisms within agreements, facilitating the involvement of third parties (such as local communities) and arbitration bodies whose decisions

integrate effectively into national legal systems.

4. Regular monitoring and adaptive revisions. Many agreements remain "fixed" for extended periods, while business conditions evolve, leading to regulatory stagnation risks. The creation of flexible joint bodies and working groups authorized to introduce amendments partially addresses this challenge [4].

5. Consideration of digitalization trends, as investments in virtual assets, data transit, and remote services require distinct mechanisms for investor

qualification and legal protection, including cybersecurity measures, intellectual property rights, and distributed ledger and smart contract regulations [6].

Examining the role of the U.S. dollar within global reserve structures reveals its dominance, which affects not only global financial stability but also the regulatory framework governing international investments (see Figure 1).

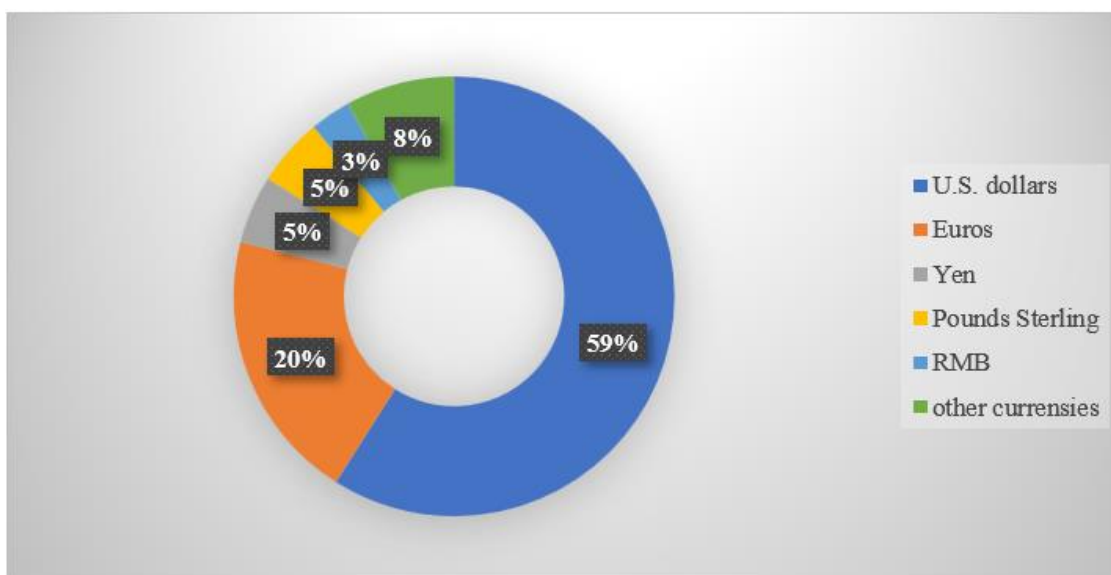


Figure 1 – Central Banks: Currency Composition of Reserves, Q2 2022 [8].

When negotiating investment agreements, states must account for the role of major reserve currencies in managing currency risks, especially when projects or assets are denominated in U.S. dollars. A high share of the dollar in reserves may provide more favorable financing and investment conditions but also creates dependence on U.S. monetary policy. In the context of minimizing legal risks in international investment agreements, it is crucial to establish hedging mechanisms for exchange rate fluctuations, outline

provisions for settlements in national and alternative currencies, and consider potential volatility of key reserve units when drafting dispute resolution clauses.

The table below presents the key factors for reducing legal risks through careful structuring of investment agreements. Special emphasis is placed on transparency and precision in contractual language, the introduction of sanction mechanisms, and the creation of joint bodies to prevent prolonged disputes (Table 1).

Table 1 – Key Directions for Reducing Legal Risks in Investment Agreements (source: compiled by the author based on [1-6]):

Direction	Brief Description
Clear Definition of Obligations	The contract text should include highly detailed formulations of the rights and responsibilities of the parties to prevent misinterpretations and ambiguities [1; 3].
Proactive Contract Mechanisms	A simplified structure and clear language contribute to a better understanding between parties, reducing the likelihood of disputes arising from ambiguous provisions [5; 6].
Sanctions and Compensation	Financial and other sanctions stipulated in the contract for non-compliance, including termination mechanisms, encourage investors to adhere to social and environmental standards [2; 3].
Role of Joint Bodies	Association councils and committees facilitate prompt issue resolution and ensure compliance with contractual norms, including monitoring environmental and social impacts [4].

The following table summarizes effective mechanisms used in international investment agreements to prevent conflicts. The key elements include

comprehensive risk assessment, transparent dispute resolution procedures, and the role of joint bodies that can introduce necessary adjustments in a timely manner (Table 2).

**Table 2 – Practical Mechanisms for Conflict Reduction in Investment Agreements (source: compiled by the author based on [1; 4; 5]):**

Mechanism	Brief Description
Preliminary Research	Comprehensive assessment of political, legal, social, environmental, and financial risks (due diligence) [1].
Clear Dispute Resolution Procedures	Establishing transparent arbitration norms that allow for the participation of third parties (e.g., local communities) ensures a balance of interests [4].
Joint Committees	Regular meetings to monitor agreement implementation and coordinate necessary amendments in response to changing conditions [5].

## DISCUSSION

The conducted analysis has identified several key factors that contribute to reducing legal risks in international investment agreements: clear definition of obligations, flexible sanction mechanisms, proactive contract design, and adaptation to dynamic changes in environmental, social, and digital spheres. First, detailed regulation of investor and host state obligations within the agreement itself helps prevent disputes and simplifies conflict resolution [1], [2]. As noted by Faccio [3] and Gastinger, Dür [4], precise wording of rights and responsibilities, along with a clear

delineation of authority, reduces the risk of misinterpretation by arbitration bodies.

Second, the presence of a well-defined sanction and compensation mechanism incentivizes parties to comply with social and environmental requirements, increasing investor accountability [3], [5]. Growing expectations for "sustainable" business conduct require not only a formal reference to ESG commitments but also the introduction of clear monitoring parameters, as emphasized in the works of Dotzauer et al. [2] and Kaave [5].

The third aspect concerns proactive contract design.



Similar to approaches used in loan agreements for small and medium-sized enterprises [5], investment agreements should incorporate simplified language and visual tools, enabling parties to assess and manage risks without complex legal barriers. This approach establishes a foundation for broader stakeholder engagement, including local communities whose rights may be affected during project implementation [1], [4].

The fourth emerging trend is the necessity to adapt agreements to modern challenges, including digitalization [6]. Policies and legal frameworks regarding virtual assets and cross-border data flows remain unstandardized, increasing the risk of regulatory conflicts. Therefore, states and investors must proactively determine how to regulate virtual transactions and which legal frameworks to use for investor identification in the absence of physical presence [6], [7]. This also includes addressing currency fluctuations, particularly in light of the dominant role of the U.S. dollar [8], which affects financing and settlement conditions.

Finally, joint bodies and committees play a crucial role in promptly clarifying contractual terms, adjusting arbitration procedures, or modifying regulatory requirements when necessary [4], [10]. As research by Willemin et al. [10] demonstrates, the involvement of such institutions is particularly relevant in discussions of environmental risks and their enforcement. At the same time, as emphasized by Sykes [7] and Vadi [9], any coordination mechanisms must not undermine fundamental principles of international law and should remain aligned with requirements for protecting basic rights and freedoms.

Thus, practice indicates that successful legal risk reduction depends not merely on the formal inclusion of protective provisions in agreement texts but on a comprehensive approach that incorporates detailed regulation, well-designed sanction and monitoring mechanisms, active stakeholder involvement, and the ability to adapt to rapidly changing realities.

## CONCLUSION

An analysis of contemporary trends in international investment agreements reveals that a uniform approach to investor protection no longer guarantees a balance of interests for all parties. As investment activities expand and become more complex, states, arbitration institutions, and investors themselves must develop more nuanced legal instruments. The most critical mechanisms ensure compliance with fundamental rights and account for a broad range of risks—environmental, social, and technological. When

contractual provisions prioritize comprehensive transparency and dispute resolution procedures allow for the participation of affected groups and swift modifications, justice is no longer a mere declaration but a practical norm.

Overall, minimizing legal risks in international investment agreements is not a one-time task but an ongoing process in which all parties bear their share of responsibility. If states consistently uphold the necessity of clear environmental and social criteria, if investors demonstrate a commitment to high business standards, and if legal forums effectively protect all participants, the benefits of global investments will be both tangible and long-term. Maintaining a fair balance between rights and obligations fosters trust and, consequently, contributes to building a sustainable legal framework capable of addressing future challenges. In this way, the international legal regime designed to attract investment will not only drive economic growth but also provide meaningful protection for people, communities, and the environment, laying the foundation for genuinely responsible global cooperation.

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