

TREATY AND CONTRACT IN INVESTMENT ARBITRATION

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“A Subject and a Sovereign are clean different things.”

Charles I, speech on the scaffold, 30 January 1649¹

1. Introduction

No issue in the field of investment arbitration is more fundamental, or more disputed, than the distinction between treaty and contract.² There is a struggle between those who believe BIT claims should be insulated from contractual claims and those who want to relate the two. That struggle has led to a divided jurisprudence and – as often happens when jurists are divided – to a tendency to caricature opposing positions. In these circumstances both time and further reflection are necessary before any consensus can emerge, and the views of one proponent in the debate are no more likely to achieve immediate acceptance than the views of any other. What I will try to do here, however, is to set out the foundations in general international law for the approach I prefer. I am reluctant to attach a label to that approach – which until it was termed “extreme” I fondly regarded as some form of happy medium. But for convenience I will call it the integrationist approach, since it attempts a reconciliation between two propositions both generally agreed but which seem to be in perpetual tension with each other in this field – on the one hand, the proposition that a host State cannot rely on its own law as a justification for failing to comply with its international obligations, including those obligations arising under treaties for the protection of foreign investment; on the other,

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¹ “King Charls his Speech made upon the Scaffold at Whitehall-Gate immediately before his Execution, on Tuesday the 30 of Jan 1648. With a Relation of the manner of his going to Execution.” in *The Trial and Execution of King Charles I: Facsimiles of the contemporary official accounts contained in the Charge of the Commons of England Against Charls Stuart, King Charls His Tryal, King Charls His Speech Made Upon the Scaffold* (reprinted 1966, Scholar Press Limited, Leeds), (6).

² See e.g. Z Douglas, “The Hybrid Foundations of Investment Treaty Arbitration” (2003) 74 BYIL 151; C McLachlan et al, *International Investment Arbitration: Substantive Principles*, (OUP, 2007), 90 (paras 4.33-4.34); 127 (paras 4.149-4.151).

the proposition that an investment is, in the very first place and by definition, a transaction occurring in the host State and governed by its laws.

Now of course there is only one world, however we may divide it conceptually: there is no such *place* as the “international plane”. In the modern period, investment contracts have always coexisted with international law standard for the protection of investments, so this tension is not novel – as students of the old mixed arbitral tribunal decisions will not need reminding. International law resolved that tension in two ways, thereby underpinning the dominant dualist theory about the relation between international and national law. The first was by strictly applying the exhaustion of local remedies rule: national law issues had to be resolved first before the competent national courts.³ The second was by way of the rule that for an international tribunal, national law is a pure question of fact,⁴ a fact for the most part determined by the very resort to local remedies which international law mandated in the field of diplomatic protection. Thus there was a conceptual separation secured by a temporal separation; international law covered the distinct field of interstate claims premised upon the failure to resolve the underlying individual dispute first through national courts and national law.

But in the field of investment arbitration, neither of these rules applies. First, there is no requirement of exhaustion of local remedies prior to commencing investment arbitration – unless, exceptionally, that requirement has been expressly maintained.⁵ (This does not mean that the existence of an adequate local remedy may not be relevant to the merits of a treaty claim – but that is another matter.) Secondly, the standard applicable law clause in BITs – however it may be formulated – mandates and may even require the tribunal to apply the law of the host State alongside international law. Faced with article 42 of the ICSID Convention or some equivalent provision in a BIT, it cannot be argued that the law of the host State is a mere matter of fact. It is true that tribunals have to be informed, by expert evidence or otherwise, of the content of host State law with which they may not be familiar. (Expert evidence of international law is also tendered before such tribunals: whether or not this is desirable, the evidence is not inadmissible.) It is also true that a treaty provision which mandates the application of the law of a State is presumed to do so subject to the international law conflicts rule, that international law prevails over national law in case of inconsistency. But that is a rule of conflict of *laws* – it doesn’t treat national law as a mere matter of fact. And in the large majority of cases where there is no inconsistency between international law and the law of the host State, the two laws have to be applied in parallel.

³ ILC (Dugard, Special Rapporteur), “Draft Articles on Diplomatic Protection with Commentaries” in *Report of the International Law Commission on the Work of its Fifty-eighth Session* (1 May – 9 June; 3 July – 11 August 2006) UN Doc A/61/10. Part 3 of the Draft Articles deals with Local Remedies. Subject to the exceptions in Article 15, Article 14(1) provides that a State may not present an international claim in respect of an injury to a national (or a stateless person or refugee as provided for under Article 8) before the injured person has exhausted all local remedies.

⁴ I Brownlie, *Principles of Public International Law* (6th edn, OUP, 2003), 38- 40.

⁵ C Schreuer, *The ICSID Convention: A Commentary* (CUP, 2001), 388-396; McLaughlan et al, 128 (para. 4.152).

Before I turn to some ways in which this tension has been addressed, two preliminary remarks are called for.

The first concerns the character of the international arbitral function. According to an influential, it may be the dominant, view, it is an illusion to think that there is a right or correct method of resolving such issues as these. Arbitrators are not judges, there is no method of ensuring “correct” decisions, there will be unresolvable disagreements at the general level between arbitrators depending on their own legal traditions and approaches. The requirement that arbitrators give reasons – imposed for example by Articles 48(3) and 52(1)(e) of the ICSID Convention – is a *process* requirement; it is there to ensure that the tribunal does its job and does not decide in an arbitrary manner; it is not intended to enable substantive review of the reasons for deciding the merits of the disputes submitted to arbitration. According to this view, the well-known disagreement in the two *SGS* cases over the umbrella clause⁶ should not be allowed to mask the fact that the two tribunals reached similar functional conclusions, both allowing contract claims to proceed before national level forums (in one case domestic arbitration, in another, national courts) where the parties to the investment contracts had agreed on the exclusive jurisdiction of those forums. On this view it is a mistake to look for a *jurisprudence constante* such as might characterise a unified jurisdiction with a unitary system of law. Rather the search must be for *patterns* of decisions and for an acceptable spectrum of views.

Evidently legal theorists have debated this issue for ages, and it must be added to the lengthening list of points which in the confines of a lecture (if not a lifetime) I am not going to be able to settle. But I must say that I find the current level of dissensus between arbitrators on core questions disturbing; the carpet looks very much as if different people have started from different ends without many common threads – a crazy quilt rather than a Persian rug. At any rate I think we should strive towards a closer agreement on such questions as the effect of the standard umbrella clause or the role of legitimate expectations, rather than rejoicing in a complete system of *laissez faire*.

My second point is more personal. Inevitably a number of the issues I will be discussing arise in pending cases in which I am involved as arbitrator or otherwise. Nothing I say should be taken as indicating any concluded views on the specific issues in these cases.

2. The International Law Framework

I said earlier that I hoped to set out the foundations in general international law for the integrationist approach. Let me do that now. Within the time available I would make five points.

(1) The first is that there is no *a priori* limitation on the scope or content of treaty obligations, even those concerning what would otherwise be internal affairs. There is no

⁶ *SGS Société Générale de Surveillance SA v Islamic Republic of Pakistan* (ICSID Case No. ARB/01/13), Decision on Objections to Jurisdiction, 6 August 2003, 8 *ICSID Reports* 406; *SGS Société Générale de Surveillance SA v Republic of the Philippines* (ICSID Case No. ARB/02/6), Decision on Objections to Jurisdiction, 29 January 2004, 8 *ICSID Reports* 515.

a priori definition of what is or is not international. Nor is there any presumption of the restrictive interpretation of treaties. We find authority for this in *The Wimbledon*, the first contentious case to come before the first permanent international court.⁷ The issue was whether the guarantee of freedom of transit through the Kiel Canal under Art 380 of the Treaty of Versailles of 1919,⁸ a guarantee which extended to ships of “all nations at peace with Germany”, required Germany to allow the transit through the canal of a ship carrying munitions to Poland, then at war with Russia. It was argued that a treaty provision should be restrictively interpreted because otherwise it would amount to an infringement on Germany’s sovereignty. The Court, in a passage echoed many times since...

“decline[d] to see in the conclusion of any Treaty by which a State... undertakes to perform... a particular act an abandonment of its sovereignty. No doubt any convention creating an obligation of this kind places a restriction upon the exercise of the sovereign rights of the State, in the sense that it requires them to be exercised in a certain way. But the right of entering into international engagements is an attribute of State sovereignty.”⁹

Thus an argument from sovereignty was evaded by an appeal to sovereignty: if states could not enter into binding international obligations, they would lack an attribute of statehood.

I should observe that the German argument in that case had considerable weight because it was supported by another basic rule, that the rights of third States are unaffected by treaties to which they are not party. Germany relied on its obligation of neutrality vis-à-vis Russia, not a party to the Treaty of Versailles, in support of a restrictive interpretation of the transit regime for the Kiel Canal under that Treaty – but to no avail. In the investment context, the rights and obligations in question are those of the host State, by definition a party to the treaty. No third State problem arises.

(2) This in turn gives rise to the second general principle, the principle that treaty language is presumed to have its natural and ordinary meaning in its context. This is stated as the general rule in Article 31(1) of the Vienna Convention on the Law of Treaties of 1969. A corollary is the principle of *effet utile*; the words of a substantive treaty provision should be given some rather than no effect – i.e. the normal effect its terms would indicate. A further corollary is that each investment treaty has to be interpreted in its own terms and in its own right. There is no such thing as *the* umbrella clause; rather, there are umbrella clauses. No doubt where these are in identical or nearly identical terms they should be given the same or similar meaning; but where different language is used compared with existing standard formulas, it may be presumed that some difference in meaning was intended.

⁷ PCIJ Ser A No 1 (1923).

⁸ 225 CTS 188.

⁹ PCIJ Ser A No 1 (1923), 25.

The next three principles are drawn from the law of State responsibility. As a general matter the responsibility of States in the field of investment treaty arbitration is a species of State responsibility, i.e. the responsibility of a State party for breach of the substantive international obligations created by the investment treaty. For this purpose it makes no difference whether these obligations are owed to the other State party to the treaty or directly to the investor. The former view was adopted by the NAFTA Tribunal in the *Loewen* case, when it said that:

“233. ...Rights of action under private law arise from personal obligations (albeit they may be owed by or to a State) brought into existence by domestic law and enforceable through domestic tribunals and courts. NAFTA claims have a quite different character, stemming from a corner of public international law in which, by treaty, the power of States under that law to take international measures for the correction of wrongs done to its nationals has been replaced by an ad hoc definition of certain kinds of wrong, coupled with specialist means of compensation. These means are both distinct from and exclusive of the remedies for wrongful acts under private law: see Articles 1121, 1131, 2021 and 2022. It is true that some aspects of the resolution of disputes arising in relation to private international commerce are imported into the NAFTA system via Article 1120.1(c), and that the handling of disputes within that system by professionals experienced in the handling of major international arbitrations has tended in practice to make a NAFTA arbitration look like the more familiar kind of process. But this apparent resemblance is misleading. *The two forms of process, and the rights which they enforce, have nothing in common. There is no warrant for transferring rules derived from private law into a field of international law where claimants are permitted for convenience to enforce what are in origin the rights of Party states.*”¹⁰

That view has been followed and applied by the majority in another NAFTA case, as yet unreported.

This is a fascinating issue – but in the majority of cases it will make no difference to the result. Even if the primary obligation is owed only to the other State party to the BIT and is defeasable on an interstate basis, the responsibility *invoked* by the investor in investor-State arbitration is the responsibility of the State and it is governed, as declaratory of international law, by Part 1 of the ILC Articles on Responsibility of States for Internationally Wrongful Acts.¹¹ In the words of Article 33(2) of the ILC Articles, in investment arbitration the investor, a person or entity other than a State, seeks to

¹⁰ *The Loewen Group Inc. and Raymond L. Loewen v United States of America* (ICSID Case No. ARB(AF)/98/3), Award, 26 June 2003, 7 *ICSID Reports* 442 (emphasis added).

¹¹ Hereafter the ILC Articles. These are appended to GA Res 56/83 of 14 December 2001; they and the ILC’s commentaries are reprinted in J Crawford, *The International Law Commission’s Articles on State Responsibility: Introduction, Text and Commentaries*, (2002, Cambridge, CUP).

vindicate a “right, arising from the international responsibility of a State”, and it does so whether or not the primary obligation is owed to that person or entity.¹²

Within the field of Part I of the ILC Articles, the following propositions are relevant.

(3) For state responsibility to arise, the conduct in question must be attributable to the host State under the rules set out in Articles 4-11 of the ILC Articles. Attribution is a legal operation by which the conduct of a range of domestic law entities is treated as conduct of an international law entity, the State. In some cases, as with Article 4 organs, all the conduct of such organs is attributable to the State, whether or not it is characterized as conduct *iure imperii* or *iure gestionis*. In other cases, as with separate entities exercising elements of governmental authority under Article 5, only certain conduct is so attributable. In principle attribution does not involve any piercing of the corporate veil – although that may be called for in specific cases. Nor does the process of attribution redefine the State in terms of its own internal law: who represents the State domestically may be different from who does so in international law.¹³ I am reliably informed that there is no such entity as Poland in Polish law – by contrast much of 20th century history concerned its existence and identity as a matter of international law. Thus the mere fact that acts of separate entities may be attributable to the State in particular cases does not mean that the contracts of such entities are State contracts.

(4) The fourth proposition, also drawn from the law of State responsibility, concerns breach. In general a finding of a breach of international law does not depend on the characterization of the conduct in question as “governmental”, or as involving the exercise of sovereign authority. There are only two questions: what is the State obliged to do or refrain from doing, and has it complied with that obligation? Unless the primary rule which is the source of the obligation requires it, there is no third question, how to characterize the breach. Still less is there any requirement to prove any particular motive, whether financial or “governmental”. That point is made in the ILC’s commentaries, both on Articles 4 and 12. Thus the ILC said on Article 4:

“It is irrelevant for the purposes of attribution that the conduct of a State organ may be classified as ‘commercial’ or ‘*acta iure gestionis*’. The breach by a State of a contract clearly does not as such entail a breach of international law. Something further is required before international law becomes relevant, e.g. a denial of justice by the courts of the State in proceedings brought by the other contracting party. But the entry into or breach of a contract by a State organ is nonetheless an act of the State for the purposes of article 4, and it may amount to an internationally wrongful act.”¹⁴

The irrelevance of the classification of the acts of State organs as *iure imperii* or *iure*

¹² See ILC Art 33(2) & commentary, para (4), reprinted in Crawford, 207-208.

¹³ Cf *Maritime Delimitation and Territorial Questions between Qatar and Bahrain*, Jurisdiction and Admissibility, Judgment, *ICJ Reports* 1994, 112, paras. 28-29.

¹⁴ See ILC, Commentary to Art 4, para (6), reprinted in Crawford, 96.

gestionis was affirmed by all those members of the Sixth Committee who responded to a specific question on this issue from the Commission.¹⁵

Similarly in its commentary on Article 12, the basic article on breach, the ILC noted that:

“International awards and decisions specifying the conditions for the existence of an internationally wrongful act speak of the breach of an international obligation without placing any restriction on the subject-matter of the obligation breached. Courts and tribunals have consistently affirmed the principle that there is no *a priori* limit to the subject matters on which States may assume international obligations... [T]he breach by a State of an international obligation constitutes an internationally wrongful act, whatever the subject matter or content of the obligation breached, and whatever description may be given to the non-conforming conduct.”¹⁶

To take an example, the refusal at one point by the United Kingdom to proceed with the Concorde project – as required by a bilateral treaty with France¹⁷ – threatened a breach of that treaty, and it was irrelevant whether the British motive was to save money or protect the environment.

(5) The fifth principle is that of independent characterization and is stated in Article 3 of the ILC Articles:

“The characterization of an act of a State as internationally wrongful is governed by international law. Such characterization is not affected by the characterization of the same act as lawful by internal law.”

The relevance of this for our inquiry is explained in the commentary:

“Especially in the fields of injury to aliens and their property and of human rights, the content and application of internal law will often be relevant to the question of international responsibility. In every case it will be seen on analysis that either the provisions of internal law are relevant as facts in applying the applicable international standard, or else that they are actually incorporated in some form, conditionally or unconditionally, into that standard.”¹⁸

To summarise, State responsibility for breach of international law is distinct from the liability of a State for breach of its contracts. But there may be important overlaps: for example, a State may commit by treaty to comply with a contract, in which case its failure to do so is (subject to any circumstance precluding wrongfulness) also a breach of an international obligation. Responsibility for breach of treaty is conceptually distinct

¹⁵ See *Report of the ILC...1998 A/53/10*, para 35.

¹⁶ ILC, Commentary to Art 12, paras (9), (10), reprinted in Crawford, 128-129.

¹⁷ Agreement between the Government of the United Kingdom of Great Britain and Northern Ireland and the Government of the French Republic regarding the development and production of a civil supersonic transport aircraft, 29 November 1962, 453 UNTS 326.

¹⁸ ILC, Commentary to Art 3, para (7), reprinted in Crawford, 89.

from responsibility for breach of contract – but the latter may, depending on the context, entail or imply the former.

These five principles provide the necessary background to what is still the leading case on the contract/treaty distinction, the *Vivendi Annulment* decision. The claimants operated water and sewerage systems in Tucumán, a province of Argentina, pursuant to a contract with the first claimant, a locally-incorporated Vivendi affiliate, and Tucumán. The contract conferred exclusive jurisdiction on Tucumán’s administrative tribunals for “interpretation and application” of the contract.¹⁹

Following numerous disputes, both parties rescinded and claimed the other was in default. The claimants instituted ICSID arbitration on the basis of the 1991 France-Argentina BIT, alleging that its investor rights had been infringed by public health orders, mandatory service obligations and rate regulations. The Tribunal held that the contract did not prevent the investor from proceeding against Argentina under the ICSID Convention on the basis of its alleged violation of the BIT. However, all the claims concerning the action of the Argentine province arose from disputes concerning the performance of the Contract, and the Claimant had agreed to submit those disputes exclusively to the jurisdiction of the Tucumán courts. As it was impossible to separate breaches of the contract by Tucumán from potential violations of the BIT, the Claimant had to first bring proceedings before the administrative courts of Tucumán as provided for by the contract.²⁰

The Tribunal’s award was partially annulled by an *ad hoc* Committee.²¹ The Committee distinguished between determining whether there has been a breach of the BIT which must be considered by reference to international law, and whether the contract has been breached which must be determined by reference to the proper law of the contract (Tucumán law, in the present case):

“As to the relation between breach of contract and breach of treaty... [a] state may breach a treaty without breaching a contract, and vice versa... In accordance with this general principle (which is undoubtedly declaratory of general international law), whether there has been a breach of the BIT and whether there has been a breach of contract are different questions. Each of these claims will be determined by reference to its own proper or applicable law – in the case of the BIT, by international law; in the case of

¹⁹ Article 16.4 of the Concession Contract for Water and Sewage Service in the Province of Tucumán, May 18, 1995 provided as follows:

“For purposes of interpretation and application of this Contract the parties submit themselves to the exclusive jurisdiction of the Contentious Administrative Tribunals of Tucumán.”

²⁰ *Compañía de Aguas del Aconquija SA and Compagnie Générale des Eaux/Vivendi Universal v Argentine Republic* (ICSID Case No. ARB/97/3) Award, 21 November 2000, 5 *ICSID Reports* 299.

²¹ *Compañía de Aguas del Aconquija SA and Compagnie Générale des Eaux/Vivendi Universal v Argentine Republic* (ICSID Case No. ARB/97/3) Decision on Annulment, 3 July 2002, 6 *ICSID Reports* 340.

the [contract], by the proper law of the contract, in other words, the [municipal law].”²²

The Tribunal ought not to have allowed Argentina to rely on the contract’s exclusive jurisdiction clause to avoid the characterisation of its conduct as internationally unlawful under the BIT:

“In a case where the essential basis of a claim brought before an international tribunal is a breach of contract, the tribunal will give effect to any valid choice of forum clause in the contract.”²³

“On the other hand, where ‘the fundamental basis of the claim’ is a treaty laying down an independent standard by which the conduct of the parties is to be judged, the existence of an exclusive jurisdiction clause in a contract between the claimant and the respondent state or one of its subdivisions cannot operate as a bar to the application of the treaty standard. At most, it might be relevant – as municipal law will often be relevant – in assessing whether there has been a breach of the treaty.”²⁴

“It is one thing to exercise contractual jurisdiction...and another to take into account the terms of a contract in determining whether there has been a breach of a distinct standard of international law...”²⁵

“Whether particular conduct involves a breach of a treaty is not determined by asking whether the conduct purportedly involves an exercise of contractual rights.”²⁶

By refusing to interpret the contract, the Tribunal “failed to decide whether or not the conduct in question amounted to a breach of the BIT.”²⁷

“A treaty cause of action is not the same as a contractual cause of action; it requires a clear showing of conduct which is in the circumstances contrary to the relevant treaty standard. The availability of local courts ready and able to resolve specific issues independently may be a relevant circumstance in determining whether there has been a breach of international law... But it is not dispositive, and it does not preclude an international tribunal from considering the merits of the dispute.”²⁸

The Committee held that the tribunal committed a manifest error of jurisdiction if, having upheld its jurisdiction over an admissible treaty claim, it declined to decide that claim.²⁹

²² Ibid., paras 95-96.

²³ Ibid., para 98.

²⁴ Ibid., para 101.

²⁵ Ibid., para 105.

²⁶ Ibid., para 110.

²⁷ Ibid., para 111.

²⁸ Ibid., para 113.

²⁹ Ibid., para 115.

(I note in parenthesis that a second tribunal upheld Vivendi's restated claim, awarding damages of US\$105,000,000.³⁰)

Vivendi Annulment is predicated on the distinction between contractual claims and treaty claims. At some level this is obvious, but nonetheless there is strong disagreement as to the corollaries of this distinction. In the time remaining I will take two fields in which there is arbitral and academic disagreement. These are (1) contractual claims and counter claims; (2) umbrella clauses. Time does not allow an analysis of a third field pertaining to merits issues – legitimate expectations – although similar lessons can be learnt there about the role of contracts in shaping investments and the need to focus on the real rather than an imagined transaction.

3. Contractual Claims and Counterclaims under BITs

If treaties and contracts were “clean different things”, one would expect them to inhabit different worlds. As between sovereigns there could be promises to submit investment disputes to arbitration but those promises would be interstate ones only: they would not sound in contract as against their intended beneficiaries – or at least they would not do so without domestic implementation. It should be noted that BITs are virtually never relied on as part of the internal law of the host State, and they will almost by definition not be part of the law of the seat of the arbitration. Lacking status as internal law, they are relied on exclusively as treaties.

But even in legal systems which give no legal effect to treaties as such, a dualistic construction does not prevail. The established understanding is that an offer to arbitrate is contained in the BIT and is accepted by the investor's notice of arbitration or by such other consent as the treaty may require. At that point, and not before, there is a perfected agreement to arbitrate between a qualified investor and the host State. As the Court of Appeal said in *Republic of Ecuador v Occidental Exploration and Production Co*:

“The treaty involves... a deliberate attempt to ensure for private investors the benefits and protection of consensual arbitration; and this is an aim to which national courts should, in an internationalist spirit and because it has been agreed between states at an international level, aspire to give effect... The present treaty at article VI(3)(a) holds out to investors on a standing basis the right to ‘choose to consent in writing to the submission of the dispute for settlement by binding arbitration’ ... and, at article VI(3)(b), once such consent is given, ‘either party to the dispute may initiate arbitration in accordance with the choice so specified in the consent’. The treaty expressly goes on to provide that the consent of the relevant state ‘hereby’ to the submission of any investment dispute for settlement by binding arbitration... together with the investor's written consent when choosing such arbitration, shall satisfy the requirement for written consent under the ICSID Convention and at article VI(4)(b) for ‘an

³⁰ *Compañía de Aguas del Aconquija SA and Compagnie Générale des Eaux/Vivendi Universal v Argentine Republic* (ICSID Case No. ARB/97/3), Award, 15 August 2007, <<http://ita.law.uvic.ca/>>, para 11.1.

“agreement in writing” for purposes of article II of the [New York] Convention’; and that any arbitration shall be held in a state party to that convention. This purpose can only be fulfilled, in a legal system with a dualist approach to international law like the English, if the operation of the mechanism for consensual arbitration in the treaty does in fact generate an ‘agreement in writing’. The application of the New York Convention depends on such an agreement, and the provisions of the Arbitration Act 1996 (sections 100-104) relating to the enforcement of foreign arbitral awards give effect to this requirement in English law. We would not in the circumstances accept...that the consensual aspect of the arbitration contemplated in article VI of the treaty is a matter of mere form. It must, as it seems to us, have been intended to give rise to a real consensual agreement to arbitrate, even though by a route prescribed in the treaty.

Further ... the agreement to arbitrate which results by following the treaty route is not itself a treaty. It is an agreement between a private investor on the one side and the relevant state on the other.”³¹

Thus the separate agreement to arbitrate an investment claim under a BIT is a contract and not a treaty. If the agreement to arbitrate in *Occidental* had been a treaty, it would have been unenforceable and issues arising under it would have been non-justiciable before an English court, which the Court of Appeal expressly denied. The investor has neither international legal personality nor treaty-making capacity, and it does not acquire either merely by accepting an offer to arbitrate made in a treaty. If the agreement to arbitrate was a treaty, the resulting award would not be enforceable under the New York Convention of 1958, which has no application to international law arbitrations, e.g. between States or other international legal persons.³²

But there is a distinction between a treaty the parties to which are international legal persons and a contract the proper law of which is international law. In the *Occidental* case the Court of Appeal held that the proper law of the agreement to arbitrate is international law.³³ It could not be the law of the seat of the arbitration since the seat will often not be identified at the time the agreement to arbitrate was concluded, and English law cannot abide a floating proper law any more than nature a vacuum. Nor is it likely that the parties could have agreed on the law of the host State as the proper law of the arbitration agreement. That left international law as the only option. It was a credible option since the content of the agreement to arbitrate is determined largely by reference to the BIT, itself undoubtedly governed by international law. Thus the BIT brings forth a binding commitment to arbitrate enforceable through national courts under national law, specifically under the Arbitration Act 1996. In short, a treaty breeds a contract.

³¹ *Republic of Ecuador v Occidental Exploration and Production Co* [2005] EWCA Civ 1116, paras 32-33 (Lord Phillips of Worth Matravers MR, Clarke, Mance LJJ).

³² Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958, 330 UNTS 38, Articles 1, 7.

³³ *Republic of Ecuador v Occidental Exploration and Production Co*, para 33.

That raises in turn the question whether a BIT can provide a basis for straightforward contractual jurisdiction, independently of any umbrella clause. If a treaty can provide a basis for consent to arbitrate treaty claims with the host State, why can it not provide a basis of consent to arbitrate contractual claims? Indeed it has done so: under the Claims Settlement Declaration which is part of the Algiers Accords of 1980, individual claimants brought thousands of contractual claims against Iran,³⁴ and it has been held that the resulting awards of the Iran-US Claims Tribunal are enforceable under the New York Convention.³⁵

Of course, contractual jurisdiction can only be asserted if the terms of the BIT were wide enough to encompass claims under investment contracts. Some BITs are quite clear in excluding that possibility. For example under Articles 1116 and 1117 of the NAFTA, the only claims which may be submitted to arbitration are claims that another NAFTA Party has breached an obligation under specified articles of Chapter 11 itself. Indeed in some cases it has been clear that there were breaches of the investment contract by State organs: that might conceivably be taken into account in applying the minimum standard of treatment in Article 1105(1) on the NAFTA but it would only be relevant incidentally.

By contrast the standard arbitration clauses in BITs make a clear distinction between investment disputes arising between investors and host States, and disputes concerning the interpretation and application of the BIT arising between the States parties to the BIT. The point was made by the *Vivendi Annulment* panel by reference to the France-Argentina BIT, which was in a fairly standard form. Article 8(1) provided that “[a]ny dispute relating to investments made under this Agreement between one Contracting Party and an investor of the other Contracting Party”, if not settled by negotiation, could be referred either to the domestic courts or to international arbitration, the choice between them being final. There was no restrictive definition of “dispute relating to investments”. As the Committee noted:

“Article 8 does not use a narrower formulation, requiring that the investor’s claim allege a breach of the BIT itself. Read literally, the requirements for arbitral jurisdiction in Article 8 do not necessitate that the Claimant allege a breach of the BIT itself: it is sufficient that the dispute relate to an investment made under the BIT. This may be contrasted, for example, with Article 11 of the BIT, which refers to disputes ‘concerning the interpretation or application of this Agreement’.”³⁶

The issue arose in that case not because the claimants called on the Tribunal to award damages under the Concession Contract – they expressly did not – but because the phrase “[a]ny dispute relating to investments” was capable of covering the same dispute, whether it was presented in the form of a claim under the substantive provisions of the

³⁴ D Caron & J Crook (eds), *The Iran-United States Claims Tribunal and the Process of International Claims Resolution: A Study by the Panel on State Responsibility of the American Society of International Law* (Transnational Publishers Inc., New York, 2000), 11-12.

³⁵ *Ministry of Defense of Iran v Gould, Inc*, 887 F.2d 1357 (9th Cir. 1989).

³⁶ *Compañía de Aguas del Aconquija SA and Compagnie Générale des Eaux/Vivendi Universal v Argentine Republic*, Decision on Annulment, 3 July 2002, para 55.

BIT or a claim under the investment contract. Factually there was one dispute not two, whatever causes of action might be invoked. For that reason the Committee was of the view that the claimants, by invoking the jurisdiction of an international tribunal under Article 8, had taken the fork in the road and elected their remedy. In declining to decide the claim under the BIT, the first *Vivendi* Tribunal had deprived the Claimants of a right which the Treaty expressly conferred.³⁷

The implication of all this is that contractual jurisdiction can be invoked under any sufficiently clear generic dispute settlement clause in a BIT, such as Article 8 of the Argentina-France Treaty which was applied in the *Vivendi* case. But this conclusion is subject to a number of qualifications which significantly limit its scope.

The first qualification is that the contractual claim must be characterized at the same time as a claim “relating to investments”. Not every contract entered into by an investor is an investment contract – the classic example is an ordinary contract for the supply of goods and services.

The second qualification is that there can only be contractual jurisdiction under a BIT in respect of an investment contract with the State itself, and not with a separate State entity having its own legal personality, and *a fortiori* with a third party. It is sometimes argued that the question is one of attribution under Chapter 2 of Part I of the ILC’s Articles on State Responsibility, but attribution has nothing to do with it. The issue of attribution arises when it is sought to hold the State responsible for some breach of an international obligation – including one arising under a substantive provision of a BIT. The problem here concerns jurisdiction, not merits; the formation of a secondary agreement to arbitrate, not the breach of a primary obligation concerning the protection of investments. In short, the question is one of interpretation of the jurisdictional offer, not attribution of conduct to the State.

The third qualification concerns the common case where the investment contract with the State contains its own exclusive dispute settlement clause. An investor invoking contractual jurisdiction pursuant to an offer made by the State must itself comply with its contractual arrangements for dispute settlement with that State. The principle *pacta sunt servanda* is not a one-way street. This was the basis for the majority holding in *SGS v Philippines* that a *contractual* claim under a BIT cannot be pursued in breach of an applicable exclusive jurisdiction clause. In *SGS v Philippines* that issue arose under an umbrella clause, a matter to which I will return. But it would arise equally under a generic dispute settlement clause such as Article 8 of the France-Argentina Treaty. Indeed it is arguable that under a generic dispute settlement clause this should be classified as an issue of jurisdiction properly so-called, and not one of admissibility. Whatever answer may be given to the question whether an investor can by contract in advance renounce the right to arbitrate treaty claims, there cannot be any doubt that it can renounce the right to arbitrate contract claims in a treaty forum. An exclusive jurisdiction clause in a contract is surely intended to do just that.

³⁷ Ibid., paras 102-115..

It is worth noting that the drafters of the 2004 US Model BIT sought to achieve essentially this result, though—in the tradition of that instrument—they did so by rather complex drafting. Article 24 of the Model BIT provides, in relevant part:

- “1. In the event that a disputing party considers that an investment dispute cannot be settled by consultation and negotiation:
- (a) the claimant, on its own behalf, may submit to arbitration under this Section a claim
 - (i) that the respondent has breached
 - ...
 - (C) an investment agreement;
 - and
 - (ii) that the claimant has incurred loss or damage by reason of, or arising out of, that breach...”

... provided that a claimant may submit... a claim for breach of an investment agreement only if the subject matter of the claim and the claimed damages directly relate to the covered investment that was established or acquired, or sought to be established or acquired, in reliance on the relevant investment agreement.”³⁸

Article 24 does not deal with the contingency of an exclusive jurisdiction clause in an investment agreement.

There is a second implication of all this, which concerns counterclaims. The core problem with counterclaims in BIT arbitration is that the treaty commitments of the host State towards the investor are unilateral, and anyway the investor is not a party to the BIT. Moreover the agreement to arbitrate, though it incorporates by reference the jurisdictional requirements of the BIT, does not incorporate its substantive provisions nor does it make them applicable bilaterally. In the case of a narrowly drawn counter-claim provision in the applicable arbitration rules, such as Article 19(3) of the UNCITRAL Rules (Article 19(3) of the PCA Rules), it will be argued that no counterclaim is possible because the host State’s counterclaim would not “arise out of the same contract” within the meaning of Article 19(3).

In fact two Tribunals applying the terms of Article 19(3) have held that counterclaims are in principle permissible.

³⁸ 2004 US Model Bilateral Investment Treaty (“Treaty between the Government of the United States of America and the Government of [Country] concerning the encouragement and reciprocal protection of investment”), Office of the United States Trade Representative website <<http://www.ustr.gov/index.html>>.

*Reineccius & others v Bank for International Settlements*³⁹ was not a BIT claim: it arose under the 1930 Convention respecting the Bank for International Settlements and concerned the amount of compensation payable for the recall of the 13.73% of privately held shares in the Bank. The Tribunal held that the Claimants were entitled to compensation for their recalled shares corresponding to a proportionate share of the net asset value of the Bank, discounted by 30%.⁴⁰ It also upheld the counterclaim of the Bank against one of the claimants, awarding the Bank's costs of defending proceedings brought by it in the United States in breach of the agreement to arbitrate.⁴¹ In so far as the breach concerned the agreement to arbitrate, a similar result could be achieved under a BIT – although presumably a claimant which has actually commenced a BIT arbitration will be careful not to pursue competing proceedings before national courts.⁴²

More directly relevant is the second case, *Saluka BV v Czech Republic*,⁴³ a decision of a tribunal presided over by Sir Arthur Watts. In a partial privatisation, Saluka had acquired a substantial minority shareholding in IPB, a Czech state-owned bank: in controversial circumstances IPB became insolvent, was put into administration and sold for a pittance to another bank. Saluka claimed violations of the deprivation of investment (Article 5) and fair and equitable treatment (Article 3) of the Netherlands-Czech Republic BIT. The Czech Republic brought a counterclaim which inter alia alleged breaches of the original share purchase agreement with the privatisation agency, a State organ. The arbitration was conducted under the UNCITRAL Rules.

In its interlocutory decision on the Counterclaim, the Tribunal said:

“Both parties have... accepted that counterclaims might fall within the scope of the Tribunal's jurisdiction under Article 8: the Respondent has done so by virtue of having presented such a counterclaim, and the Claimant has done so by acknowledging that circumstances could be envisaged in which a counterclaim could properly be made, as where a primary claim was presented on the basis of an investment contract and a counterclaim was presented on the basis of that same contract.”⁴⁴

The Tribunal held that

“the jurisdiction conferred upon it by Article 8, particularly when read with Article 19.3, 19.4 and 21.3 of the UNCITRAL Rules, is in principle

³⁹ *Dr Horst Reineccius, First Eagle SoGen Funds, Inc., Mr Pierre Mathieu and la Société de Concours Hippique de la Chââtre v Bank for International Settlements*, Partial Award on the Lawfulness of the Recall of the Privately Held Shares on 8 January 2001 and the Applicable Standards for Valuation of those Shares, 22 November 2002; Final Award on the Claims for Compensation for the Shares Formerly Held by the Claimants, Interest Due Thereon and Costs of the Arbitration and on the Counterclaim of the Bank against First Eagle Sogen Funds, Inc., 19 September 2003, Permanent Court of Arbitration website <www.pca-cpa.org> (hereafter '*Bank for International Settlements*').

⁴⁰ *Bank for International Settlements*, Partial Award, para 202.

⁴¹ *Ibid.*, Final Award, paras 103, 138(1) and (4).

⁴² Cf ICSID Convention, Art 26.

⁴³ *Saluka Investments BV v Czech Republic*, Decision on Jurisdiction over the Czech Republic's Counterclaim, 7 May 2004, para 81.

⁴⁴ *Ibid.*, para 38.

wide enough to encompass counterclaims. The language of Article 8, in referring to ‘All disputes,’ is wide enough to include disputes giving rise to counterclaims, so long, of course, as other relevant requirements are also met. The need for a dispute, if it is to fall within the Tribunal’s jurisdiction, to be ‘between one Contracting Party and an investor of the other Contracting Party’ carries with it no implication that Article 8 applies only to disputes in which it is an investor which initiates claims.”⁴⁵

However jurisdiction in respect of the counterclaim, as for the primary claims, was circumscribed by Article 8 of the Treaty which refers to disputes “concerning an investment”. The counterclaim had to satisfy that requirement to fall within the Tribunal’s jurisdiction.⁴⁶ In addition, “a legitimate counterclaim must have a close connexion with the primary claim to which it is a response.”⁴⁷ The Tribunal cited the ICSID arbitral decision in *Klöckner v Cameroon*, which emphasised the need for the subject-matter of the counterclaim to be intimately connected with the subject matter of the primary claim.⁴⁸ It also cited a number of Iran-US Claims Tribunal decisions to similar effect.⁴⁹

The Tribunal stated that:

“Article 19.3 of the UNCITRAL Rules, Articles 25(1) and 46 of the ICSID Convention and Article II(1) of the Iran-US Claims Settlement Declaration, all reflect essentially the same requirement: the counterclaim must arise out of the ‘same contract’ (UNCITRAL Rules, Article 19.3), or must arise ‘directly out of an investment’ and ‘directly out of the subject-matter of the dispute’ (ICSID, Articles 25(1) and 46), or must arise ‘out of the same contract, transaction or occurrence that constitutes the subject matter of [the primary] claims’ (Article II(1) of the Claims Settlement Declaration). The Tribunal is satisfied that those provisions, as interpreted and applied by the decisions which have been referred to, reflect a general legal principle as to the nature of the close connexion which a counterclaim must have with the primary claim if a tribunal with jurisdiction over the primary claim is to have jurisdiction also over the counterclaim.”⁵⁰

The Tribunal concluded it was without jurisdiction in respect of the Respondent’s counterclaim on the basis that the disputes “which have given rise to the Respondent’s counterclaim are not sufficiently closely connected with the subject-matter of the original

⁴⁵ Ibid. para 39.

⁴⁶ Ibid., para 60.

⁴⁷ Ibid., para 61.

⁴⁸ *Klöckner v Cameroon* (ICSID Case No ARB/81/2) Decision on Annulment, 3 May 1985, 2 *ICSID Reports* 162, 165.

⁴⁹ Eg. *American Bell International, Inc. v The Government of the Islamic Republic of Iran, et al.*; *Westinghouse Electric Corp. v The Islamic Republic of Iran et al.*; *Owens-Corning Fiberglass Corp. v The Government of Iran et al.*; *Morrison-Knudsen Pacific Ltd. v The Ministry of Roads and Transportation et al.*; *Harris International Telecommunications, Inc. v Iran.*

⁵⁰ *Saluka Investments BV v Czech Republic*, Decision on Jurisdiction over the Czech Republic’s Counterclaim, 7 May 2004, para 76.

claim put forward by Saluka to fall within the Tribunal’s jurisdiction under Article 8 of the Treaty.”⁵¹

To summarise, where the host State has a counterclaim arising from the investment contract which falls within the description of a dispute concerning an investment within the terms of the relevant BIT, such a counterclaim may be admissible depending on the actual connection with the primary claim. The term “contract” in Article 19.3 of the UNCITRAL Rules should be interpreted to include the BIT on which the investor’s claim is based, and where there is a generic dispute settlement clause in the BIT claims by the host State under an investment contract to which it is a party, counterclaims under the investment contract may be admissible. *A fortiori* this should be true when the ICSID Arbitration Rules apply: Article 40 refers to “a counter-claim arising directly out of the subject-matter of the dispute”, and as in *Vivendi* a treaty claim and a contract claim, while remaining legally distinct causes of action, may have the same subject-matter. To conclude, contractual claims and counterclaims may be brought under appropriately worded BITs.

This conclusion seems desirable as a matter of policy as well as law. Despite the inherently asymmetrical character of a BIT, BIT tribunals should be able to hear closely connected investment counterclaims arising under the investment contract. Otherwise the maxim *pacta sunt servanda* operates in only one direction.

3. Contractual Claims and the Umbrella Clause

I turn to my second major theme, the so-called “umbrella clause”. In doing so I acknowledge the assistance given by the work of two current doctoral students at Cambridge, Anthony Sinclair and Monique Sasson. In particular Anthony Sinclair has usefully traced the origins of the umbrella clause back to their origins in the aftermath of the *Anglo Iranian Oil Company* case in 1952.⁵² It is not the least of the criticisms to be leveled at the narrow interpretations of the umbrella clause that they disregard this history.

I should start with the standard proviso – deriving from my first general principle. Some umbrella clauses are more equal than others to the interpretative weight put upon them – or to put it in less Orwellian terms, everything depends in their actual language. For example the clause at issue in *Salini Costruttori S.p.A. and Italstrade S.p.A. v. Hashemite Kingdom of Jordan*,⁵³ provided that:

“Each Contracting Party shall create and maintain in its territory a legal framework apt to guarantee to investors the continuity of legal treatment,

⁵¹ *Ibid.*, para 81.

⁵² *Anglo-Iranian Oil Co. case (Jurisdiction)*, ICJ Reports 1952 p 93. See AC Sinclair, “The Origins of the Umbrella Clause in the International Law of Investment Protection” (2004) 20 *Arbitration International* 411.

⁵³ *Salini Costruttori SpA & Italstrade SpA v Hashemite Kingdom of Jordan*, Decision on Jurisdiction, 9 November 2004 (Guillaume, President; Cremades and Sinclair).

including the compliance, in good faith, of all undertakings assumed with regard to each specific investor.”

This was rightly held not to involve any guarantee by the host State with regard to specific transactions.⁵⁴ It was not an umbrella clause at all. Likewise the clause in *SGS v Pakistan* was curiously worded and might have given grounds for a narrower construction.⁵⁵ In what follows I will limit myself to umbrella clauses by which the host State commits itself to comply with obligations it has entered into with regard to investments. For example the 1984 and the 1987 US Model BITs provided that: “Each Party shall observe any obligation it may have entered into with regard to investments.” The 2004 US Model BIT abandoned this formulation, adopting instead the jurisdictional provision with regard to investment agreements to which I have already referred. But similar provisions subsist in the UK, Swiss and German Model BITs. No doubt in consequence, around 40% of BITs contain some version of an umbrella clause.

There is neither the time nor would it be productive to go into the details of the 20 or so cases in which umbrella clauses have been discussed. It is sufficient to identify four schools of thought, if you like, four camps – though some of the dwellers in particular camps may be thought to have a nomadic attitude and to move from camp to camp as the feeling takes them.

The first camp adopts an extremely narrow interpretation of umbrella clauses, holding that they are operative only where it is possible to discern a shared intent of the parties that any breach of contract is a breach of the BIT (*SGS v Pakistan*; *Joy Mining v Egypt*⁵⁶).

The second camp seeks to limit umbrella clauses to breaches of contract committed by the host State in the exercise of sovereign authority (*Pan American Energy v Argentina*; *El Paso Energy v Argentina*).

A third view goes to the other extreme: the effect of umbrella clauses is to internationalise investment contracts, thereby transforming contractual claims into treaty claims directly subject to treaty rules (*Fedax v Venezuela*; *Eureko v Republic of Poland*; *Noble Ventures v Romania*).

Finally there is the view that that an umbrella clause is operative and may form the basis for a substantive treaty claim, but that it does not convert a contractual claim into a treaty claim. On the one hand it provides, or at least may provide, a basis for a treaty claim even if the BIT in question contains no generic claims clause (*SGS v Philippines*, *CMS v Argentina (Annulment)*); on the other hand, the umbrella clause does

⁵⁴ *Ibid.*, paras. 126-7.

⁵⁵ *SGS Société Générale de Surveillance S.A. v Islamic Republic of Pakistan*, Decision on Jurisdiction, 6 August 2003 (Feliciano, President; Faurès and Thomas). Article 11 of the Pakistan-Switzerland BIT provides that: “Either Contracting Party shall constantly guarantee the observance of the commitments it has entered into with respect to the investments of the other Contracting Party”.

⁵⁶ *Joy Mining Machinery Ltd v The Arab Republic of Egypt* (ICSID Case No. ARB/03/11) Award on Jurisdiction, 6 August 2004.

not change the proper law of the contract or its legal incidents, including its provisions for dispute settlement.

In accordance with the general principles articulated above, there are major difficulties with the first three positions. The first effectively deprives the umbrella clause of any content, contrary to the principle of *effet utile* and to the apparent intent of the drafters. The second imposes a characterisation test at the level of breach for which there is no textual warrant and which is capable of producing arbitrary results. One may, for example, take the formulation of the Tribunal in the *CMS* case:

“Purely commercial aspects of a contract might not be protected by the [umbrella clause] in some situations, but the protection is likely to be available when there is significant interference by governments or public agencies with the rights of the investor”.⁵⁷

There are two obvious responses to this. The first is that it does not provide a reliable or even a determinate test for determining whether a tribunal has jurisdiction. Instead it calls for an appreciation of the character of or motive for the breach which in most cases would require a hearing on the merits. The second response is that it would be very odd indeed if a State could defend itself against a claim for repudiation of an investment agreement by arguing that it was acting for commercial reasons!

No doubt there are genuine concerns driving the restrictive view, which is to a significant extent a reaction against the equal and opposite defects of the third view. These need to be addressed.

First there is the problem of scope:

“the ‘commitments’ subject matter of Article 11 may, without imposing excessive violence on the text itself, be commitments of the State itself as a legal person, or of any office, entity or subdivision (local government units) or legal representative thereof whose acts are, under the law on state responsibility, attributable to the State itself”.⁵⁸

But as we have seen, the question of the scope of a commitment to arbitrate made by the State is a matter of interpretation and has nothing to do with attribution. International law does not treat separate entities with their own legal personality as part of the State for all purposes.

Then there is the possibility that an umbrella clause might enable an investor to evade agreed-upon exclusive jurisdiction arrangements in the investment contract, whether these provide for domestic courts or local or international arbitration. Thus the *SGS v Pakistan* Tribunal was not convinced...

“that Article 11 of the BIT has had the effect of entitling a Contracting Party’s investor, like SGS, in the face of a valid forum selection contract

⁵⁷ *CMS v Argentina*, para. 299.

⁵⁸ *SGS v Pakistan*, para. 166.

clause, to ‘elevate’ its claims grounded solely in a contract with another Contracting Party... to claims grounded on the BIT, and accordingly to bring such contract claims to this tribunal for resolution and decision.”⁵⁹

I agree entirely with this concern – but it implies that the obligations of a host State under a general BIT are to be applied without regard to the conduct, including the contractual obligations, of the investor. That is not – and ought not to be – the case, as *SGS v Philippines* showed.

Then there is a concern about flooding ICSID with minor contractual claims, a classic floodgates argument to which standard floodgates responses may be made. BIT arbitration is expensive and even to a successful claimant costs are usually not awarded. The characterisation of a claim as contractual or otherwise is essentially a matter of technique and bears no relation to the frequency or otherwise with which investment disputes arise and are submitted to arbitration.

Fourth and most significant, there is the concern that the umbrella clause leads to a freezing of host State sovereignty, a sort of closet stabilization. And there is reason for the concern. For example the *CMS* Tribunal felt able to say that:

“[t]hese laws and regulations became obligations within the meaning of Article II(2)(c), by virtue of targeting foreign investors and applying specifically to their investments, that gave rise to liability under the umbrella clause”.⁶⁰

But it is a confusion to equate a State law or regulation with an obligation entered into by the State, or to regard an umbrella clause as implicitly freezing the laws of the State as at the date of admission of an investment. The enactment of a law by a State, whether it is specific or general, is not the entry by the State into an obligation distinct from the law itself. No doubt a State is obliged by its own laws, but only for so long as they are in force. In the absence of express stabilization, investors take the risk that the obligations of the host State under its own law may change, and the umbrella clause makes no difference to this basic proposition.

In short, under the integrationist view as applied to standard umbrella clauses the claims are still contractual and they are still governed by their own applicable law. The distinction between treaty and contract is maintained. The purpose of the umbrella clause is to allow enforcement without internationalization and without transforming the character and content of the underlying obligation.

This can be seen from the decision of the *ad hoc* Committee in *CMS v Argentina* (*Annulment*), where the Tribunal’s conclusion on the umbrella clause was annulled. The relevant paragraph of the decision reads as follows:

“95. Moreover there are major difficulties with this broad interpretation of Article II(2)(c).

⁵⁹ Ibid., para. 165.

⁶⁰ Ibid., para. 175.

- (a) In speaking of “any obligations it may have *entered into* with regard to investments”, it seems clear that Article II(2)(c) is concerned with consensual obligations arising independently of the BIT itself (*i.e.* under the law of the host State or possibly under international law). Further they must be specific obligations concerning the investment. They do not cover general requirements imposed by the law of the host State.
- (b) Consensual obligations are not entered into *erga omnes* but with regard to particular persons. Similarly the performance of such obligations or requirements occurs with regard to, and as between, obligor and obligee.
- (c) The effect of the umbrella clause is not to transform the obligation which is relied on into something else; the content of the obligation is unaffected, as is its proper law. If this is so, it would appear that the *parties* to the obligation (*i.e.*, the persons bound by it and entitled to rely on it) are likewise not changed by reason of the umbrella clause.
- (d) The obligation of the State covered by Article II(2)(c) will often be a bilateral obligation, or will be intrinsically linked to obligations of the investment company. Yet a shareholder, though apparently entitled to enforce the company’s rights in its own interest, will not be bound by the company’s obligations, *e.g.* as to dispute settlement.
- (e) If the Tribunal’s implicit interpretation is right, then the mechanism in Article 25(2)(b) of the ICSID Convention is unnecessary wherever there is an umbrella clause.
- (f) There is no discussion in the award of the *travaux* of the BIT on this point, or of the prior understandings of the proponents of the umbrella clause as to its function.”

The decision on this point was annulled for failure to state reasons, leaving open the question whether a broad interpretation of the umbrella clause would have involved a manifest excess of power, even if it had been properly motivated.

For these reasons, the better view is the integrationist one: the umbrella clause is an extra mechanism for the enforcement of claims, but the basis of the transaction remains the same.

4. Conclusions

To conclude, treaties and contracts are different things. But they are not clean different things, in the sense of inhabiting different worlds: between them there is no great gulf fixed. No doubt distinctions between legal systems should be observed – but not at the expense of appropriate connections between them. There is a distinction between treaty

and contract, but they are part of the same one world with many legal systems that international arbitrators have long inhabited.

Applied to international arbitration this insight produces consequences both for jurisdiction and merits. The core point is that a covered investment is a transaction involving a qualified investor and the host State. Contractual or other commitments by each to the other go to define the investment: as *Mihaly v Sri Lanka* held, if there is no intention to enter into legal relations then there is no investment. What a BIT does is to provide an additional layer of protection for the one transaction: the investment is protected by the BIT, but the BIT should not be used as a vehicle to rewrite the investment arrangement. At the level of jurisdiction – and subject always to the caveat that what matters is the actual language of the BIT – there is no reason to interpret a BIT as not covering contractual claims or counterclaims concerning the investment. There may be – as with appropriately-worded umbrella clauses – an international obligation to observe the investment contract, though this does not convert the contract into a treaty or change its applicable law. At the level of the merits it must be borne in mind that the investment contract is itself an allocation of risks and opportunities, and that that allocation is relevant in determining, in particular, whether there has been fair and equitable treatment under the BIT. In particular the doctrine of legitimate expectations should not be used as a substitute for the actual arrangements agreed between the parties, or as a supervening and overriding source of the applicable law.